UNDERSTANDING DIGITAL TOKENS

Legal Landscapes Governing Digital Tokens in Canada

Prepared by the Token Alliance – an industry initiative of the Chamber of Digital Commerce

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**CHAMBER OF DIGITAL COMMERCE**

The Chamber of Digital Commerce is the world’s largest trade association representing the blockchain industry. Our mission is to promote the acceptance and use of digital assets and blockchain technology. Through education, advocacy, and working closely with policymakers, regulatory agencies, and industry, our goal is to develop a pro-growth legal environment that fosters innovation, jobs, and investment.

**TOKEN ALLIANCE**

The Token Alliance is an industry-led initiative of the Chamber of Digital Commerce, developed to be a key resource for the emerging industry surrounding the generation and distribution of tokens using blockchain technology. Comprised of more than 400 industry participants, the Alliance includes blockchain and token and legal experts, technologists, economists, former regulators, and practitioners from around the globe. The Token Alliance develops community-driven guidelines for the responsible development of tokens.

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### CHAMBER OF DIGITAL COMMERCE INDUSTRY INITIATIVES & WORKING GROUPS

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I. ACKNOWLEDGEMENTS

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II. PART 1: REGULATORY OVERVIEW OF DIGITAL TOKEN MARKETS

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I. INTRODUCTION

Digital token units, often referred to as “coins” or “tokens”, issued as part of an ICO or initial token offering ("ITO") - terms for digital token distributions that have been used by Canadian Securities Administrators - can represent many different things, including a portion of an asset, whether tangible or intangible; services or units of services; or an ownership interest in a business. Whether Canadian securities laws apply to ICOs and ITOs will likely depend on the use to which the coin or token may be put and what rights it represents.

There may be a distinction between tokens that fall within the ambit of securities regulation and those that fall outside of it. Proponents of this view conceive of at least two distinct types of tokens. The concept of a “utility token” involves a token or coin that represents services or units of services, for example, using tokens to play a game at an arcade. On the other hand, a “securities token” entitles the holder of the token or coin to certain rights in the business' assets, revenues or profits. Since a securities token functions similar to a typical security such as a share, Canadian securities laws are likely to apply.

While reference is made throughout this discussion to “securities tokens,” it is important to note that any distinction between utility tokens and securities tokens has not been explicitly accepted by Canadian securities regulatory authorities. On August 24, 2017, Canadian Securities Administrators (“CSA”) staff, with the exception of Saskatchewan, published Staff Notice 46-307 – Cryptocurrency Offerings1 (“CSAN

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46-307”), in response to requests from fintech businesses for guidance on the applicability of Canadian securities laws to “cryptocurrency offerings,” “cryptocurrency exchanges,” and “cryptocurrency-focused investment funds.” CSAN 46-307 articulated a general view that “in many instances” digital tokens associated with ICOs/ITOs are securities.

On June 11, 2018, the CSA published Staff Notice 46-308 Securities Law Implications for Offerings of Tokens (“CSAN 46-308”), which provides additional guidance on the applicability of securities law to offerings of blockchain-based tokens or coins.

The discussion that follows outlines certain of the Canadian securities law considerations that may apply to the distribution or trading of a digital token that qualifies as a “security” within the meaning of Canadian securities laws.

II. THE CANADIAN LEGAL FRAMEWORK

Securities legislation in Canada is principally governed by Canada’s ten provincial and three territorial governments with the view of balancing investor protection against efficient capital markets. While each province and territory has its own securities legislation, some coordination among jurisdictions is achieved through the CSA as an umbrella organization. While the following discussion will focus mainly on the securities laws of the Province of Ontario, the rules in many areas of securities regulation have been standardized among the provinces and territories and cooperative systems have been established among the regulators through the CSA.

A. THE DEFINITION OF “SECURITY” AND ITS APPLICATION TO DIGITAL TOKENS

The provincial securities Acts have expansive statutory definitions of “security.” The statutory definitions of “security” include as one category, an “investment contract”, which is the category Canadian courts and securities regulators generally use to assess whether a new type of transaction involves a security.

The leading case in Canadian jurisprudence on the meaning of investment contracts is Pacific Coast Coin Exchange v. Ontario Securities Commission (“Pacific Coast”), which was expressly cited as the relevant case law in CSAN 46-307. The Supreme Court of Canada in Pacific Coast considered and adopted certain United States jurisprudence on the meaning of investment contracts, and in particular, the common law test set out in SEC v. W.J. Howey Co., 328 U.S. 293 (1946) and other United States cases.

4 Canadian Securities Administrators, online: https://www.securities-administrators.ca/.
The application of this Canadian case law to so-called “utility” tokens has not been further elaborated upon directly by the Canadian courts.

In its application to “cryptocurrency offerings,” the CSA has stated that it will conduct an evaluation of whether a “cryptocurrency” – a term that it leaves undefined – qualifies as a “security” on a case-by-case basis and that substance will be considered over form. In CSAN 46-307, the CSA noted that the appropriate interpretive test was the four-prong test: does the ICO/ITO involve (1) an investment of money, (2) in a common enterprise, (3) with the expectation of profit, (4) to come significantly from the efforts of others. The CSA further stated in CSAN 46-307 that the case law requires an assessment of the economic realities of a transaction and a purposive interpretation, keeping in mind the objective of investor protection.7

The CSA did not provide any clear guidance in CSAN 46-307 on the characteristics that would indicate that “securities may not be involved.” Generally, however, it can be concluded that a token that entitles the holder to share in the business profits of the entity distributing the token will likely be considered a security.

In CSAN 46-308, the CSA emphasized that one should assess not only the technical characteristics of the token itself, but the economic realities of the offering as a whole, with a focus on substance over form. With respect to utility tokens, CSAN 46-308 noted that, “the fact that a token has a utility is not, on its own, determinative as to whether an offering involves the distribution of a security.”

CSAN 46-308 provided additional guidance on how the CSA staff have viewed certain examples, based on situations seen to date. The anonymized examples focused on various elements of the Howey test.

In CSAN 46-308, the CSA staff expressed the view that if management “clearly and uniformly promotes the token in a manner that, taken as a whole, promotes only its utility and not its investment value, the implication that purchasers have an expectation of profit may be reduced.”

If tokens are not fungible or interchangeable and each token has unique characteristics, and any future market value of the token is primarily based on market forces, the value of the token may be based on its unique characteristics, and not on the efforts of others. There may not be a common enterprise.

If tokens have a fixed value on the platform that does not automatically increase over time, or change based on non-commercial factors, this may reduce the purchaser’s expectation of profit.

If the token’s software, platform or services are not yet available or are still in development, the CSA said this could indicate that the purchaser is not purchasing the tokens for their immediate utility, but because of an expectation of profit. “Although some purchasers may be purchasing the token for

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7 Canadian Securities Administrators, supra note 83.
the utility function, many purchasers may be purchasing the token in order to sell it on a cryptoasset trading platform or otherwise in the secondary market.” This is particularly true where the existence of secondary trading is critical to the success of the offering of tokens or is featured prominently in the marketing of the offering. This could also indicate the existence of a common enterprise because management’s efforts are still needed to develop or deliver the software, online platform or application or goods and services.

B. CSA SANDBOX APPROVALS

The CSA established a regulatory sandbox\(^8\) in February 2017 (the “CSA Sandbox”), a program whereby issuers seeking to offer innovative products, services and applications, such as digital tokens, are invited by the CSA to discuss their business model and applicable securities laws, and possible exemptive relief, directly with the applicable securities regulators on a coordinated and flexible basis. As CSA Sandbox approvals are intended to allow the issuers to operate in a test environment, the approvals are time-limited, so far to one or two years.

To date, only two limited exemptions relating to digital tokens have been granted through the CSA Sandbox process.

The first limited exemption was for Montreal-based Impak Finance Inc. (“Impak”), which received exemptive relief on August 16, 2017 from the Québec Autorité des marchés financiers (“AMF”) and seven other Canadian jurisdictions from the dealer registration requirement and the prospectus requirement in respect of the resale of Impak Coins (“MPK”).\(^9\) The initial distribution of MPK was made in accordance with the standard terms of an already existing statutory offering memorandum prospectus exemption. This allowed Impak to carry out the ICO. The issuance of MPK, a new digital currency based on the Waves blockchain platform, was proposed in order to fund the development of Impak’s online social network dedicated to the impact economy. The MPK network did not exist at the time of the ICO. MPK were not delivered to purchasers upon closing of the offering, rather, only once Impak launches its digital wallet sometime in the future.

### DIGITAL TOKEN PRODUCTS RECEIVING EXEMPTIVE RELIEF IN THE CSA REGULATORY SANDBOX

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<td>IMPAK</td>
<td>Issue MPK tokens to fund the development of Impak’s online social network, impak.eco.</td>
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<tr>
<td>TOKEN FUNDER</td>
<td>Offer FNDR Tokens on the Ethereum blockchain to investors to fund the creation of Token Funder’s smart token asset management platform, intended to facilitate third-party issuers raising capital through the offering of blockchain-based securities.</td>
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The Impak exemption order had a number of significant conditions. Impak was required to conduct both know-your-client and suitability reviews for each MPK purchaser. In this context KYC means more than simply identity verification, and includes knowing clients’ overall investment experience and objectives, in order to assess investment suitability for the client. Impak was permitted to accomplish this through an online interactive questionnaire. There was no prospectus relief granted for any resale by a holder of MPK, except for a transfer by a participant to a social impact merchant. MPK cannot be listed and traded on any exchange unless it is done in accordance with Canadian securities laws and first approved by the AMF. The exchange rate for MPK to the Canadian dollar is established by an MPK governance body, and MPK may be redeemed for Canadian dollars at that rate, although Impak does not guarantee the purchase or conversion of MPK to participants. The exemption expires 24 months from the date of the decision.

The second limited exemption was for Toronto-based Token Funder Inc. (“Token Funder”), which received exemptive relief on October 17, 2017 from the Ontario Securities Commission (“OSC”) and other Canadian securities regulators from the dealer registration requirement to allow it to sell its own digital tokens, called FNDR Tokens, to the public.\(^\text{10}\) The initial distribution of FNDR Tokens would be made in accordance with the standard terms of an already existing statutory offering memorandum prospectus exemption. Token Funder was seeking to offer FNDR Tokens on the Ethereum blockchain to investors in order to fund the creation of its smart token asset management platform, intended to facilitate third-party issuers raising capital through the offering of blockchain-based securities. FNDR Tokens were designed to share in distributions from Token Funder arising from the operation of the platform, in the discretion of the Board of Directors of Token Funder and will have certain voting rights on the entities entitled to use the platform. FNDR Tokens cannot be listed and traded on any exchange unless done in accordance with Canadian securities laws and first approved by the OSC. The exemption will expire 12 months from the date of the decision.

Unlike the FNDR Tokens, MPK was unusual in that it was generally not freely transferable by its terms, but was redeemable at a non-guaranteed rate to be established. Given that the Impak network was still a work in progress, the MPK tokens had no utility at the time of the ICO and were treated by the issuer and the AMF as being investment contracts. The FNDR Tokens are more clearly securities tokens due to their distribution entitlements. From these two narrow examples, few clear factors on the broader application of the law around investment contracts to tokens can be elucidated.

C. FACTORS RELATING TO THE CONSIDERATION OF WHETHER A TOKEN IS A SECURITY

While the following factors are relevant to the analysis of whether a token does or does not qualify as a “security,” it is not clear whether the securities regulatory authorities in Canada will consider any particular factor or set of factors as determinative:

What is the token’s use or purpose?

Does the token represent access to a business’ platform, or does it represent an ownership stake in a business that could increase or decrease in value depending on the success of the business?

At the intended time of sale of the token, does the relevant platform still need to be developed or is there an existing, functioning ecosystem in which the token can be utilized?

Will the purchaser receive the token upon payment of the full price?

Is the token’s market value reflective of the general attractiveness of the business?

Is the token transferable, and is the anticipated value derived from future market demand?

Does the token expire after a certain period of time of not being in use?

Is the purchaser’s purpose for purchasing the token personal use or consumption, rather than merely investment purposes?

III. CONSIDERATIONS REGARDING “ICOS” OF A “SECURITY”

A. ISSUING A SECURITIES TOKEN

1. PROSPECTUS REQUIREMENT OR EXEMPTION

If the purchaser of a securities token is located in a Canadian jurisdiction, Canadian securities laws must be considered regardless of the location of the issuer of the token. Canada’s prospectus requirement creates a closed-system whereby any distribution of a security, even if made by a private company, must either be qualified by a prospectus or must qualify for a prescribed prospectus exemption.

To date, there has been no prospectus filed and approved to undertake an ICO in Canada. Upon filing and receiving a receipt for a final prospectus, the issuer would become a “reporting issuer” in Canada. A reporting issuer is subject to all of the continuous and timely disclosure requirements of Canadian securities laws, which are extensive and include the requirement to prepare and disseminate quarterly and audited annual financial statements.

As an alternative to a public prospectus, one of the most commonly used prospectus exemptions is the “accredited investor” exemption.11 This exempts an issuer or selling security holder from the prospectus requirement when distributing securities to certain institutional investors or wealthy individuals (for example an individual whose financial assets before taxes but net of liabilities of over $1 million, or whose net income exceeds $200,000 in each of...
the two most recent calendar years). Individual accredited investors below certain financial thresholds are required to receive and sign a prescribed risk acknowledgment form.

Token Funder and Impak each relied on the “offering memorandum” prospectus exemption in respect of the initial distribution of their securities tokens. While the details vary by Canadian jurisdiction, the offering memorandum exemption allows an issuer to distribute its securities to purchasers who are not accredited investors or eligible investors (which are investors who meet a slightly less stringent financial test than the accredited investor test), so long as the issuer provides purchasers with a prescribed form of offering memorandum (which is similar to a prospectus), the issuer obtains a signed risk acknowledgment form from the purchaser and the purchaser’s acquisition cost does not exceed a prescribed maximum amount. While the prescribed maximum amount in many jurisdictions is ordinarily $10,000 for non-eligible investors, the OSC and the AMF in their exemptive relief decisions in respect of Token Funder and Impak, imposed lower $2,500 investment limits for investors who did not qualify as accredited investors or eligible investors.

2. MARKETING RESTRICTIONS

“Trading” of securities includes any act, advertisement, solicitation, conduct or negotiation directly or indirectly in furtherance of a distribution of securities, and thus triggers the prospectus requirement.

If the accredited investor exemption is to be relied upon, before a marketing document, such as a term sheet or offering memorandum, is provided to potential investors, their eligibility for the accredited investor exemption must already have been assessed. In the case of reliance on the offering memorandum exemption, an offering memorandum in the prescribed form and in many cases, a risk acknowledgment form, must be obtained from the purchaser prior to signing the agreement to purchase the security.

In order to meet these requirements, issuers have used a “walled garden” approach whereby potential investors may access the electronic marketing materials on the issuer’s website only once their compliance with the applicable exemption has been verified.

3. EXEMPT DISTRIBUTION REPORTING

Certain prospectus exemptions, including the accredited investor and offering memorandum exemptions, require the filing of exempt distribution reports (and in some cases offering memoranda) with the CSA within ten days after the distribution. The names of any agents or underwriters that assist with an offering of securities tokens and their fees must also be

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13 Section 2.9 of National Instrument 45-106 — Prospectus Exemptions.
14 See, e.g., the definition of “trade” under section 1(1) of the Ontario Securities Act R.S.O. 1990, c. S.5.
15 See, e.g., Form 45-106F1 Report of Exempt Distribution (Form 45-106F1).
recorded on the reports. As these exempt distribution reports require detailed information about purchasers, issuers of securities tokens must ensure their purchase procedures have the capability of capturing and recording information in respect of each purchase of securities, including the name, address and telephone number of each investor in Canada, their particular sub-category of accredited investor, if applicable, as well as the price and number of securities purchased by each investor. Issuers based in the Canadian provinces of Alberta, British Columbia or Québec have additional reporting obligations, even for distributions made outside Canada.

4. RESALE RESTRICTIONS

Securities tokens purchased in reliance upon a prospectus exemption are subject to restrictions on resale pursuant to National Instrument 45-102 – Resale of Securities (“NI 45-102”). NI 45-102 generally prohibits resale of a security purchased under the accredited investor exemption unless either (i) the issuer of the security has been a reporting issuer in a jurisdiction of Canada for the four months preceding the trade, or (ii) the resale is made under another prospectus exemption, such as the accredited investor exemption, which would entail continued resale restrictions, or the security is of a foreign issuer and is resold outside Canada under certain conditions.16 Unless the issuer of a securities token becomes a reporting issuer in Canada, the resale restrictions continue indefinitely and do not expire, so the tokens would never become freely tradeable in Canada.

B. TRADING OR ADVISING IN SECURITIES TOKENS

Persons in the business of trading or advising in securities, or holding themselves out as being in the business of trading or advising in securities, must register as dealers or advisers with the relevant CSA regulator and meet the requirements set out in National Instrument 31-103 – Registration Requirements, Exemptions and Ongoing Registrant Obligations.17 The determination of whether one is, or holds oneself out to be, in the business of trading or advising in securities is a factual determination commonly referred to as the “business trigger” for registration.

Startup issuers that are raising capital to advance their operating business plans would typically not be considered to be in the business of trading in securities unless they engage an employee with primary responsibility and/or compensation for capital raising activities. However, it is notable that both Token Funder18 and Impak19 sought and received temporary exemptions from the dealer registration requirement upon conditions, including: conducting investment know-your-client and suitability reviews of purchasers, not providing investment advice to purchasers, and establishing

18 Ontario Securities Commission, supra note 92.
19 Ontario Securities Commission, supra note 91.
policies and procedures that establish a system of controls and supervision sufficient to manage the risks of the business.

On September 6, 2017, Canada’s first “Cryptocurrency Fund,” a term used by the CSA to refer to an investment fund that invests solely in specified digital tokens, was established. The British Columbia Securities Commission (“BCSC”) and the OSC granted to First Block Capital Inc. (“First Block”) the first registration in Canada to an investment fund manager (“IFM”) and exempt market dealer (“EMD”) solely dedicated to digital token investments, in order to operate a bitcoin investment fund.20 First Block’s registration was granted subject to a number of tight restrictions and requirements, including:21

» Prior approval must be granted by the BCSC for any new Cryptocurrency Fund established by First Block;

» A specific custodian (Xapo) was prescribed and changes to a Cryptocurrency Fund’s custodian or to the entity principally responsible for the execution of trades for such fund will also be subject to prior approval;

» First Block must require its custodians and brokers to maintain compliance systems that provide reasonable assurance of compliance with regulatory requirements, and to manage business risks in accordance with prudent business practices;

» Independent auditor reports reviewing the sufficiency of the Cryptocurrency Fund’s custodian’s security practices as well as regulatory compliance documents received by First Block from its custodians and brokers must be provided to the BCSC;

» Annual audited financial statements must be available to security holders for each Cryptocurrency Fund, and net asset value reports must be available on a monthly or more frequent basis for each Cryptocurrency Fund; and

» Prior to making a trade in a digital token, First Block must make its own determination of a current and reasonable fair price for the digital token.

Subsequently, the Alberta Securities Commission (“ASC”), OSC and AMF imposed similar restrictions on the registrations of Ross Smith Asset Management ULC (“RSAM”),22 3iQ Corp.,23 and Majestic Asset Management LLC (“Majestic”),24 respectively, each of which notified the relevant regulator

21 First Block Capital Inc. (5 September 2017), online: https://www.securities-administrators.ca/uploadedFiles/Industry_Resources/DE_First%20Block.pdf.
that it intended to establish, manage and distribute securities of a fund that will invest solely in “cryptocurrencies,” which, for the purposes of the decision documents, the ASC, OSC, and AMF (as applicable) defined to mean bitcoin, ether, Litecoin (in the case of the 3iQ Corp. decision document) and “anything commonly considered a cryptocurrency, digital or virtual currency, or digital or virtual token.” The decision documents note that an investment fund that invests solely in one or more specified “cryptocurrencies” is a novel business model in Canada and, as such, additional reporting is required in order to monitor developments in the area.

It was significant at the time that First Block was not also required to register as a portfolio manager in order to manage investment activity for the initial bitcoin trust, as this implied that the underlying bitcoin was not considered by the BCSC and OSC to be a security. However, RSAM, 3iQ Corp., Majestic and Rivemont Investments Inc., investment portfolio manager of the fund created by Majestic, are all also registered as portfolio managers, implying that the issue is not yet settled.

On December 5, 2017, the OSC issued a notice to all registered firms (dealers, advisers or investment fund managers) saying that any firms that plan to establish, manage, advise and/or trade in securities of investment funds with portfolios of “[b]itcoin and/or other cryptocurrencies, cryptocurrency assets and coins and token offerings” are required to report changes in their business activities “to include cryptocurrency products and/or services” by completing and filing a prescribed form of notice of change of registration information. The OSC said that following reviews of the information provided, the OSC may impose terms and conditions on the firm’s registration to ensure adequate investor protection.

C. CREATING A MARKET FOR SECURITIES TOKENS

As part of CSAN 46-307, the CSA signaled its concern that platforms facilitating trades in coins, tokens or cryptocurrencies that qualify as securities may also be subject to Canadian securities law requirements involving recognition or exemption from recognition as an exchange or as a quotation and trade reporting system. At this point in time, no entity has obtained the recognition required, nor an exemption from such recognition requirement, in order to allow Canadians to participate in on-exchange trading of tokens that are securities.

The definition of “marketplace” in the Ontario Securities Act and other relevant rules is broad and includes an exchange, a quotation and trade reporting system, or any person or company that constitutes, maintains or provides a market or facility for bringing together orders for securities from

25 3iQ Corp., supra note 105.
27 Id.
28 Canadian Securities Administrators, supra note 83.
multiple buyers and sellers using established, non-discretionary methods under which orders interact with each other and the buyers and sellers entering into the orders agree to the terms of a trade.29

A person or company is considered to bring together orders for securities if it (a) displays, or otherwise represents to marketplace participants, trading interests entered on the system; or (b) receives orders centrally for processing and execution. Merely routing orders to marketplace or a dealer for execution is not considered to be providing a market or facilities for bringing together buyers and sellers of securities.30

Marketplaces will generally be found to be exchanges if the marketplace provides a listing function, provides a guarantee of a two-sided market for a security on a continuous or reasonably continuous basis, sets requirements governing the conduct of marketplace participants or disciplines marketplace participants, for example by levying fines or taking enforcement action.31 A marketplace that does not meet these exchange indicia and is not a quotation and trade reporting system may be characterized as an “alternative trading system” (“ATS”). An ATS proposing to carry on business in Canada is required to become registered as an investment dealer and provide detailed specified information to the CSA.

IV. ANTI-MONEY LAUNDERING

In 2014, the federal government proposed amendments to the Proceeds of Crime (Money Laundering) and Terrorist Financing Act (“PC Act”)32 that, once in force, will require entities engaged in the business of “dealing in virtual currencies” to register as money services businesses with the Financial Transactions and Reports Analysis Centre (“FINTRAC”). In June 2018 the Department of Finance published proposed regulations defining what “virtual currency” means. In that regard virtual currency is defined as (a) a digital currency that is not fiat currency and that can be readily exchanged for funds or for another virtual currency that can be readily exchanged for funds; or (b) information that enables a person or entity to have access to a digital currency referred to in paragraph (a). The proposed regulations would limit AML/ATF obligations to virtual currencies that are exchangeable, also known as convertible. This would include both centralized virtual currencies which are administered by a single authority and decentralized virtual currencies such as bitcoin, where authority is distributed across a network. The definition of virtual currency also includes information that provides access to the use of virtual currency, such as a private key in a cryptographic key pairing. There is a comment period in respect to the proposed regulations until September 7, 2018, and accordingly the final language will not be finalized until after that time. The proposed amendments to the PC Act have already received Royal Assent but the in-force date is not known.

Once the proposed amendments are in force, entities that must register as money services business will need to report certain transactions to FINTRAC, verify the identities of customers and maintain records with respect to transactions beyond a financial threshold and implement an anti-money laundering and counter-terrorist financing compliance regime. These requirements will apply to entities that have a place of business in Canada as well as entities that do not, provided they direct their services to persons or entities in Canada. As they are drafted, the proposed amendments will not apply to entities or individuals that simply use, and do not otherwise deal in, digital tokens.

Until the proposed amendments are in force, platforms that trade digital tokens that are not securities are not directly addressed in the PC Act. Such an entity may remit, transmit, or deal in digital tokens that are not securities and because these tokens are not a recognized national currency of a foreign country and are not considered “funds” within the meaning of the PC Act, such activities alone do not yet bring the entity within the scope of acting as a money services business under the PC Act.

However, entities dealing in digital tokens that are not securities do not operate in a legislative vacuum across Canada. If an entity operates an automated teller machine or trading platform for digital tokens in Québec, the AMF has taken the position that such entities are money services businesses for the purposes of Québec legislation and must be licensed as such.33

V. COMMODITIES AND DERIVATIVES

Although the Bank of Canada has said that “digital currencies” are currently treated as commodities,34 this has not been formally accepted or adopted by the CSA or other regulators. Some OSC staff have publicly complained that the Bank of Canada has not come out with a position as to whether bitcoin, ether, or any other coin is currency.35

In Canada, contracts for the sale of commodities, other than exchange-traded commodity futures contracts, could still qualify as investment contracts and thus be “securities” regulated by the provincial and territorial securities laws.

The CSA noted in CSAN 46-307 that digital tokens may also constitute derivatives and be subject to the derivatives laws adopted by the Canadian securities regulatory authorities;36 however, the application of commodity trading laws and derivatives laws to digital tokens in Canada remains to be determined.

36 Canadian Securities Administrators, supra note 83.
VI. ENFORCEMENT PROCEEDINGS

Recent events suggest that caution must be exercised when considering the launch of, or the investment in, digital token distributions.

On July 20, 2017, the AMF obtained prohibition orders against various parties in connection with soliciting investments in PlexCoin, a digital token. The PlexCoin “purported” ICO proceeded regardless in August. On December 8, 2017, the Québec Superior Court sentenced the individual behind PlexCoin to jail and fines for contempt of the court orders. On December 1, 2017, the United States Securities and Exchange Commission filed charges against the parties behind PlexCoin, describing the individual as “a recidivist Quebec securities law violator” and the ICO as a “full-fledged cyber scam.”

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UNDERSTANDING DIGITAL TOKENS

Legal Landscapes Governing Digital Tokens in Canada