

SEC Cautions on Use of Distributed Ledger/Blockchain Technology to Raise Capital

September 26, 2017

In July, the SEC issued a report addressing the applicability of U.S. federal securities laws to the offer and sale of securities by "virtual corporations or capital raising entities that use distributed ledger or blockchain technology to facilitate capital raising and/or investment." The report stemmed from an SEC investigation into whether The DAO, an unincorporated organization, its promoters, and certain intermediaries may have violated federal securities laws in connection with an "initial coin offering" of blockchain-based digital tokens known as "DAO Tokens." The report describes The DAO as one example of a Decentralized Autonomous Organization ("DAO"), "a term used to describe a 'virtual' organization embodied in computer code and executed on a distributed ledger or blockchain." In 2016, DAO Tokens were offered in exchange for Ether, a virtual currency, raising the equivalent of \$150 million, to be used to fund certain projects on an ongoing basis. DAO Token holders stood to profit from these projects as a return on their investment. In addition, they could monetize their tokens by reselling them on a number of web-based platforms. Based on its investigation, the SEC determined that DAO Tokens are securities and strongly cautioned "those who would use a [DOA entity], or other distributed ledger or blockchain-enabled means for capital raising, to take appropriate steps to ensure compliance with the U.S. federal securities laws." In addition, the SEC warned that "any entity or person engaging in the activities of [a securities] exchange must register as a national securities exchange or operate pursuant to an exemption from such registration." And, although the report did not analyze whether The DAO was an "investment company," the SEC cautioned that "[t]hose who would use virtual organizations should consider their obligations under the Investment Company Act." Whether a particular transaction involves the offer and sale of a security depends on the facts and circumstances. While acknowledging this, the SEC emphasized that the federal securities laws apply "regardless whether the issuing entity is a traditional company or a [DAO], regardless whether those securities are purchased using U.S. dollars or virtual currencies, and regardless whether they are distributed in certificated form or through distributed ledger technology." In the case of The DAO, the SEC decided against pursuing an enforcement action in

favor of cautioning market participants generally regarding its views on the use of virtual organizations and other distributed ledger or blockchain-enabled means for raising capital. Those who fail to heed the SEC's guidance are unlikely to be as fortunate.

Authored By



Edmund J. Zaharewicz

Related Practices

[Blockchain and Digital Currency](#)
[Financial Services Regulatory](#)

Related Industries

[Life, Annuity, and Retirement Solutions](#)
[Securities & Investment Companies](#)

©2024 Carlton Fields, P.A. Carlton Fields practices law in California through Carlton Fields, LLP. Carlton Fields publications should not be construed as legal advice on any specific facts or circumstances. The contents are intended for general information and educational purposes only, and should not be relied on as if it were advice about a particular fact situation. The distribution of this publication is not intended to create, and receipt of it does not constitute, an attorney-client relationship with Carlton Fields. This publication may not be quoted or referred to in any other publication or proceeding without the prior written consent of the firm, to be given or withheld at our discretion. To request reprint permission for any of our publications, please use our Contact Us form via the link below. The views set forth herein are the personal views of the author and do not necessarily reflect those of the firm. This site may contain hypertext links to information created and maintained by other entities. Carlton Fields does not control or guarantee the accuracy or completeness of this outside information, nor is the inclusion of a link to be intended as an endorsement of those outside sites.