Decoding The Legal Grey Zones Around Cryptocurrencies

January 28, 2019

The growth in cryptoassets is causing seismic shifts — and driving opportunity — in the global financial sector. But will a challenging regulatory framework force homegrown innovators to leave Canada?

Cryptocurrency and Blockchain 101

Cryptocurrency is a secure form of digital money that has been anonymized through the use of cryptography. Any associated transaction and purchase information appears in uncrackable code. Bitcoin was the first cryptocurrency.

Blockchain is a digital ledger that records cryptocurrency transactions.

"Disruptive" can be an overused word these days: It seems like every new innovation is heralded as a game-changer — even when it isn't. But the invention of Bitcoin and its foundational blockchain technology has been called revolutionary for very good reason.

Cryptocurrencies, blockchain and the automated financial transactions they enable, are transforming supply-chain management practices, contracting, payment and banking services and real estate transactions. New uses for the technology are being developed every day.

Moving from Fringe to Mainstream

Early on, cryptocurrencies were the niche domain of tech insiders. They preferred this peer-to-peer, electronic money system over fiat currencies for two main reasons:

- It removed central banking authorities from the creation and control of cash, and
- It drastically reduced service costs by eliminating middlemen.

But if cryptocurrencies got their start on the fringes of the financial ecosystem, they are now moving solidly to the mainstream.

A number of Canada's big financial institutions are looking at the rise of cryptocurrencies and how it has impacted their operations. In response, they are testing blockchain technologies and seeking ways to help their clients transact in cryptocurrencies. Experts believe it is just a matter of time before one of them makes a major move into the cryptocurrency arena.

> **Even the Bank of Canada is investigating the possibility of creating its own digital currency.**

Cryptocurrency developers themselves are beginning to recognize the benefits of having a presence in a more mainstream market, which could boost the credibility of their products. In fact, there is a growing number of developers that see and understand the need for more robust regulations in this space. A regulated environment, they argue, would help remove some of the stigma that has been associated with cryptoassets since their inception.

Can Regulations Keep Up?

However, authorities in Canada and around the world are struggling to regulate cryptocurrencies as new and more innovative blockchain applications emerge. Why the hold up? For one thing, blockchain is a form of technology, and as a rule, laws don't regulate technology, just certain uses.

Then there's the fundamental question of whether cryptocurrencies should be defined as securities. Canadian regulators have yet to take a firm position on that issue, and this is making it difficult for industry players looking to establish cryptocurrency exchanges. The uncertainty has some local developers considering foreign bases of operation.

A Look to the Future

Regulators will catch up — they have no choice. And as they do, we'll see more and more sophisticated investors moving into this field, including:

- Funds that are vying to offer cryptoasset-backed investment opportunities at both the institutional and retail levels
- Businesses that want to set up exchange platforms for cryptocurrency trading
- Entrepreneurs who are interested in launching initial coin offerings or creating storage and custodial enterprises for digital assets

We are currently advising a wide variety of start-ups and established companies that are exploring ways to enter this new and exciting space. To help ensure their success, we and other corporate law firms should be working with securities commissions and other regulators to pre-emptively identify and address public policy concerns.

One thing is for certain, these technologies are not going away, and they will continue to disrupt business and finance in profound and unexpected ways. The sooner a solid regulatory framework is in place, the easier it will be for Canadian companies to take advantage of all the opportunities at hand.

By

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