

# A Securities Law Framework for Blockchain Tokens

To estimate how likely a particular blockchain token is to be a security under US federal law

[Refer to: full legal analysis](#)

## Instructions

**Step 1: Copy to a new google sheet (File > Make a copy) or download as .xls**

Step 2: Review each characteristic and determine whether or not it applies to the token

Step 3: Select Y or N for each characteristic from the drop down menu

Step 4: Review results at the bottom of this page

## Element 1: Investment of Money

Is there an investment of money?

Characteristic	Points	Explanation
There is no crowdsale. New tokens are given away for free, or are earned through mining	0	Tokens which are not sold for value do not involve an investment of money.  For example, if all tokens are distributed for free, or are only produced through mining, then there is no sale for value.
Tokens are sold for value (crowdsale)	100	Tokens which are sold in a crowdsale, at any time, regardless of whether sold for fiat or digital currency (or anything else of value) involve an investment of money

## Element 2: Common Enterprise

What is the timing of the sale?

Characteristic	Points	Explanation
Pre-deployment	70	A sale of tokens before any code has been deployed on a blockchain is more likely to result in a common enterprise where the profits arise from the efforts of others. This is because the buyers are completely dependent on the actions of the developers, and the buyers cannot actually participate in the network until a later time.
The protocol is operational on a test network	60	If there is a functioning network there is less likely there is to be a common enterprise where the profits arise from the efforts of others. The closer the sale is to launch of the network, the less likely there is to be a common enterprise.

Live network is operational	<b>50</b>	If the token is sold once there is an operational network using the token, or sold immediately before the network goes live, it is again less likely to result in a common enterprise
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#### What do token holders have to do in order to get economic benefits from the network?

Characteristic	Points	Explanation
All token holders will always receive the same returns	<b>25</b>	If returns are paid to all token holders equally (or in proportion to their token holdings) regardless of any action on the part of the token holder, then their interests are more likely aligned in a common enterprise
There is a possibility of varying returns between token holders, based on their participation or use of the network	<b>-20</b>	If token holders' returns depend on their own efforts, and can vary depending on the amount of effort they each put in, then there is less likely to be a common enterprise

### Element 3: Expectation of Profit

#### What function does the token have?

Characteristic	Points	Explanation
Ownership or equity interest in a legal entity, including a general partnership	<b>100</b>	<p>Tokens which give, or purport to give, traditional equity, debt or other investor rights are almost certainly securities.</p> <p><b><i>If one or more of these characteristics apply, the token is almost certainly a security, notwithstanding the results of the other elements</i></b></p>
Entitlement to a share of profits and/or losses, or assets and/or liabilities	<b>100</b>	
Gives holder status as a creditor or lender	<b>100</b>	
A claim in bankruptcy as equity interest holder or creditor	<b>100</b>	
A right to repayment of purchase price and/or payment of interest	<b>100</b>	

No function other than mere existence	<b>100</b>	A token which does not have any real function, or is used in a network with no real function, is very likely to be bought with an expectation of profit from the efforts of others, because no real use or participation by token holders is possible.  Voting rights alone do not constitute real functionality.
Specific functionality that is only available to token holders	<b>0</b>	A token which has a specific function that is only available to token holders is more likely to be purchased in order to access that function and less likely to be purchased with an expectation of profit.

#### Does the holder rely on manual, off-blockchain action to realize the benefit of the token?

Characteristic	Points	Explanation
Manual action is required outside of the network (e.g. off-blockchain) in order for the holder to get the benefit of the token	<b>80</b>	A token whose value depends on someone taking specific manual action outside of the network means that the token is not functional in and of itself. Instead, the token relies on a level of trust in a third party taking action off-blockchain. This sort of token is more likely to be bought for speculation - i.e. the expectation of profits.
All functionality is inherent in the token and occurs programmatically	<b>0</b>	A token which is built with all the necessary technical permissions means that the token holder does not rely on manual actions of any third party. This means that the buyers are more likely to purchase the token for use rather than with the expectation of profit from the efforts of others.

#### What is the timing of the sale?

Characteristic	Points	Explanation
Pre-deployment	<b>20</b>	A sale of tokens before any code has been deployed on a blockchain is more likely to result in buyers purchasing for speculative reasons with the expectation of profit, rather than practical use cases.
The protocol is operational on a test network	<b>10</b>	If the sale occurs after code has been deployed and tested, the token is closer to being able to be used
Live network is operational	<b>0</b>	If the token is sold once there is an operational network using the token, or immediately before the network goes live, it is more likely to be purchased with the intention of use rather than profit.

### Can the token holders exercise real and significant control via voting?

Characteristic	Points	Explanation
Token holders as a whole are able to control the development team's access to funds	<b>-20</b>	If the collective approval of token holders is required in order for the development team to access the funds raised in the crowdsale, then any value realized by the token holders is more closely tied to their own decisions, and less reliant on the efforts of others.
Token holders as a whole are able to vote on significant decisions for the protocol	<b>-10</b>	If the collective approval of token holders is required in order to make significant changes to the protocol, then any value realized by the token holders is more closely tied to their own decisions, and less reliant on the efforts of others.

**Note: Voting rights must be in addition to functionality. A token with voting rights alone**

### How is the token sale marketed?

Characteristic	Points	Explanation
Marketed as an 'Initial Coin Offering' or similar	<b>50</b>	It is not possible to prevent some buyers from buying a token purely for speculation. However, marketing the token as an investment leads buyers to believe they can profit from holding or trading the token, rather than from using the token in the network.  Using terms like 'Initial Coin Offering' or 'ICO', and investment-related language like 'returns' and 'profits' encourages buyers to buy a token for speculation, rather than use.
Marketed as a Token Sale	<b>0</b>	Marketed as a sale of tokens which give the right to access and use the network
There is no economic return possible from using the network	<b>-100</b>	If there is genuinely no economic return possible for the token holders, then there is unlikely to be a common enterprise. This will be rare.

## Results

### Guide

Total Points	How likely is the element to be satisfied?
0 or less	Very unlikely
1 - 33	Unlikely

34 - 66	Equally likely and unlikely
67 - 99	Likely
100 or more	Very likely

A token will only be a security if it satisfies all three elements. The higher the point score, the more likely it is to be a security.

— [Howey Test: A Guide to the SEC's New Test for Determining Whether a Digital Currency or Token is a Security](#)

## Important notes

*Please remember that this methodology produces nothing more than an estimate. The Overall Score is not a guarantee.*

*The Howey test has not yet been directly applied by the courts to any digital currency or block involve any points-based calculation. The points system is intended as a guide - to highlight the*

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Examples	Y or N
There was never any token sale for Bitcoin. The only way to acquire new bitcoin is via mining.	N
A token which is randomly distributed for free	
A token which is sold for bitcoin in a crowdsale.	Y
A token which is sold for ether in a crowdsale.	

Total for Element 1 100

Examples	Y or N
A developer has an idea for a new protocol, writes a white paper and does a crowdsale.	Y
A developer has an idea for a new protocol, writes a white paper and deploys a working test network before doing a crowdsale.	N

The crowdsale is done at the same time the network is launched.	N
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Examples	Y or N
'HodlToken' holders are automatically paid an amount of ETH each week, based on fees generated by other users of the network	N
'FoldToken' does not pay any return, and there is no way to earn more tokens within the network (but they can be bought, sold or traded)	
'CloudToken' holders can earn more tokens by providing data storage on the network, or can spend tokens to access data storage. Holders who do not provide data storage do not earn any more tokens.	N

**Total for Element 2** 70

Examples	Y or N
A developer releases and sells 100 'BakerShares' tokens. Each token entitles the holder to 1 share in Baker, Inc.	N
A developer releases and sells 100 'BakerProfit' tokens. Each token entitles the holder to 1% of the profits of Baker, Inc. for the next year.	N
A developer releases and sells 100 'BakerDebt' tokens. Each token entitles the holder to principal and interest repayments based on the initial token sale price.	N
	N
	N

A developer releases and sells 100,000 'SocialCoin' tokens to fund the development of a new Social Network. However, SocialCoin is not required to access the network and has no real function after the sale.	N
'CloudToken' is the only way to access and use a decentralized file storage network.	Y

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Examples	Y or N
A developer releases and sells 'FreightCoin', which will allow the holder to pay FreightCoin to access capacity on a new real-world freight network. The network relies on legal contractual relationships and manual actions. (This alone does not make FreightCoin a security)	N
Holders of 'SongVoteToken' can sign transactions on the network as votes for their favorite new songs and earn rewards for doing so.	Y

Examples	
Examples	Y or N
A developer has an idea for a new protocol, writes a white paper and does a crowdsale.	Y
A developer has an idea for a new protocol, writes a white paper and develops a working test network before doing a crowdsale.	N
The live network is launched before the crowdsale.	N



Examples	Y or N
<p>A development team sells 100,000 Tokens for a total of 100,000 ETH.</p> <p>50,000 ETH will be released from the token contract to the development team immediately, but the remainder is only released once milestones are met, which requires approval of a majority of the token holders each time. If the milestones are never met, the remaining ETH will be returned to the token holders.</p>	N
Changes to the protocol require a vote by token holders.	N

and no other real functionality is very likely to satisfy element 3

Examples	Y or N
'ProfitCoin' includes potential of 'high ROI' and 'investor profits' in its marketing material.	N
	Y
Backers contribute to a cause and receive a 'thank you' token which has no economic value.	N

Your results	
Total for Element 1	100
Total for Element 2	70

Total for Element 3	20
Overall Risk Score	20

score for each element, the more likely the element is to be

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*Overall Risk Score and the categories of likelihood are a guide only.*

*chain token. The Howey test as applied by the courts does not  
re characteristics of a token which are relevant to the securities*

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