

## PUBLICATION

### Kik and the U.S. Securities and Exchange Commission

Matthew T. Burgoyne

September 24, 2019

With Kik in the news recently, Matthew Burgoyne shares his insights on their response to the complaint made by the U.S. Securities and Exchange Commission ("SEC") filed against Kik several months ago.

The SEC complaint against Kik is not surprising. Most people understand why securities regulators are curious about cryptocurrency and token sales. Cryptographic tokens are new and novel, and the law on investment contracts in the U.S. has been around for decades. The courts in both the U.S. and Canada have had the opportunity to weigh in on a multitude of investment schemes with many different characteristics and unique features. The issue is the application of the law and with the exception of some unique circumstances, most Initial Coin Offerings conducted in the last few years have probably involved the distribution of securities under existing Canadian (and probably U.S.) law.

Essentially, the allegation made by the SEC was that Kin tokens were investment contracts, and therefore securities under U.S. law. Specifically, Kik users invested money to purchase Kin, participating in a common enterprise (with Kik and with each other) with an expectation of profits for users and Kik, derived mostly from the future efforts of Kik to build the Kin ecosystem and drive demand for Kin. An important allegation is that Kik undertook its ICO without first achieving a decentralized economy for its token Kin and without making available a bona fide good or service which users could purchase with the tokens. Indeed, the same allegation could be made against many other ICO issuers (including many Canadian projects which came across my desk in 2017 and 2018).

Most of Kik's response is dedicated to the argument that '*investment contract*' is unconstitutionally vague and violates the Due Process Clause of the United States Constitution (which requires that laws be sufficiently clear enough for ordinary people to understand and to know what standards apply). One of the responses from Kik is that at the time of the token sale, Kik did not have 'adequate/advance notice' of whether its token sale would constitute an 'investment contract'. I'm not so sure how strong that argument is, given my comments above on the long-standing existing law and interpretation of investment contracts.

Kik contends that contradictory public statements from the SEC make the application of the 'Howey test' to cryptographic tokens unclear. There is some truth to this, and ultimately this case may proceed to court (Kik has requested a jury trial), and if it does, the industry may get some sought after clarity after all on the application of securities law to token offerings.

In Canada, the Ontario Securities Commission previously took the position that the Kin tokens were securities, so Kik barred Canadians from purchasing Kin in the ICO. The regulators in Canada have been clear on their position as it relates to ICOs/token sales and Kik would not likely have an argument that there is a lack of clarity or contradictory positions being taken by provincial securities commissions, which is an important part of Kik's defence in the U.S.