

ARTICLE SERIES

**INITIAL OFFERINGS;
EXAMINING THE LEGALITY OF RAISING
CRYPTOCURRENCY TOKENS**



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INTRODUCTION

Since its advent in 2008, cryptocurrency has been widely accepted internationally, as a viable means of investment. This is notwithstanding its volatility, as the world appears to be highly interested in the sale and purchase of digital assets. For example, bitcoin currently has about 14million in circulation. [1] Save for its volatile nature, and the period where its price drops, investors in the cryptocurrency space are often guaranteed of juicy returns. Interestingly, in mid-2021, bitcoin hit an all-time high of USD66,000 (Sixty-Six Thousand Dollars). In the same year, the formal launch of the first Bitcoin exchange-traded fund yielded investments to the tune of USD550m (Five Hundred and Fifty Million Dollars) on its first day[2]. This clearly shows that cryptocurrency is here to stay.

While the buzz about cryptocurrency is still rife and transactions involving the sale and purchase of cryptocurrency remains popular, it must be noted that there are certain ways entrepreneurs, companies or project owners can launch or issue a new cryptocurrency product or service to the public, and in turn, raise capital. Cryptocurrency can be issued through an Initial Coin Offering (ICO), Initial Dex Offering (IDO), and Initial Exchange Offering (IEO).

The succeeding paragraph of this article examines these cryptocurrency offering options, their relevance, advantages, and drawbacks.

INITIAL COIN OFFERING

ICO is a type of fund raising in cryptocurrency. Similar to initial public offering (IPO) which raises capital for a new company in its first listing in the stock market, ICO is a way in which cryptocurrency is issued to the public or in the market for the first time, usually at a discounted price in order to raise capital[3].

It is one of the most popular methods of crowdfunding in the cryptocurrency space[4] and it is used to launch or offer a new cryptocurrency product or service e.g., a new token, in the cryptocurrency market[5]. Some of the merits and drawbacks of ICOs are highlighted below.

[1]PWC "Money is no object: Understanding the evolving cryptocurrency market" (<https://www.pwc.com/us/en/industries/financial-services/library/cryptocurrency-evolution.html>)

[2] Rakesh Sharma "First Bitcoin ETF begins Trading" (<https://www.investopedia.com/first-bitcoin-etf-begins-trading-5206196>)

[3] Bholdus "what are ICO, IEO and IDO?" (<https://bholdus.com/blog/article/what-are-ico-ieo-and-ido>)

[4] It must, however, be noted that a private ICO which does not seek public investment is also possible.

[5] Ibid.

ADVANTAGES OF AN ICO

- 1.The cost of launching an ICO is quite low. Hence, it is preferable for rookie investors with small investment in the cryptocurrency market.
- 2.There is currently the absence of or little government regulation of ICOs, which suggests that anyone can launch one, provided they have the right technology in place.
- 3.Starting and establishing an ICO project is easy. What companies with ICO projects need to do is to issue a Whitepaper, a website of related products, and a team that will execute the project's techniques.
- 4.Tokens can be easily sold globally.
- 5.ICOs can be utilized to enjoy newly developed services.
- 6.It eliminates the need for middlemen in the sale of tokens or coins, between buyers and sellers.
- 7.The tendency of more liquidity in a short period of time is very high.
- 8.Investors have total control over their money/investments[6].

DRAWBACKS OF AN ICO

- 1.ICOs are generally regarded as risky (even under the best of circumstances) and they have a high potential for scams. The system can be easily exploited by scammers[7].
- 2.Where the ICO project fails, the token sought to be issued loses its value and becomes worthless.
- 3.Regulated mechanisms for ICOs are not fully available. However, in countries like Nigeria, they are now subject to regulation. Notwithstanding, this regulation appears to be quite tedious as platforms through which ICOs are carried out are now required to register with the Nigerian Securities and Exchange Commission where the digital assets sought to be issued can be classified as "securities"[8].
- 4.Given their susceptibility to bad actors/scammers, then can be easily used by malicious companies to cause uneven ICOs.
- 5.For long-term investments, ICOs may not be a good choice[9].

6] Ibid.

[7] Benjamin Sherry "what is an ICO: An ICO Brings New Cryptocurrencies to Market but is Risky" (<https://www.investopedia.com/news/what-ico/>)

[8] On the 13th of May 2022, the Nigerian Securities and Exchange Commission, issued the New Rules on Issuance, Offering Platforms and Custody of Digital Assets. The New Rules require platforms carrying out digital asset offering (including ICOs) to register with the SEC where the digital asset sought to be offered are regarded as "Securities". This is after the issuer has carried out an initial assessment filing with the SEC to determine whether the digital assets sought to be offered are securities.

[9]The Scientific World "Advantages and Disadvantages of Initial Coin Offering" (<https://www.scientificworldinfo.com/2021/07/advantages-and-disadvantages-of-ico.html>)

INITIAL EXCHANGE OFFERING

IEO is a form of token issuance that allows companies or project owners to raise capital for the first time by selling their tokens on a centralized exchange (e.g., Binance, Okex).

In an IEO, tokens are directly issued on the centralized exchange to investors. This method of issuing token has become popular because the centralized exchange platforms often carry out due diligence on the offering. This is to protect their customers and their own reputation. Hence, making IEOs a less risky way of investing in cryptocurrency than ICOs[10].

However, it is imperative to note that cryptocurrency entrepreneurs or project owners that intend to offer their products and services through a centralized exchange platform must pay a listing fee along with a percentage of the number of tokens sold. Upon making the payment of the said listing fee, the tokens of these companies will be listed on the exchange, immediately after the IEO ends[11].

[10] Mark Anson "Initial Exchange Offerings: The Next Evolution in Cryptocurrencies" (<https://bit.ly/32nxxOP>)

[11] Ibid.

[12] Ibid.

ADVANTAGES OF IEO

- 1.All cryptocurrency exchanges are KYC/AML verified. This guarantees a certain level of safety for investors.
- 2.IEOs put the reputation and good name of the centralised exchange behind the token offering; thereby providing a level of integrity, fairness and safety[12].
- 3.Here, investors personally/directly participate in the exchange.
- 4.The exchange platforms can protect investors from fraudulent activities, and this is due to the level of regulation involved.
- 5.Investors are allowed to buy the issued tokens directly into their accounts, as against transferring their funds into a smart contract.

ADVANTAGES OF IEO

- 1.IEOs are not free, as their funding costs are usually very high and an IEO system is difficult to set up.
- 2.Liquidity is very low compared to ICOs.
- 3.While investors can directly participate in the exchange, they have little control over the operations of the exchange.

INITIAL DEX OFFERING

An IDO occurs when a company or project owners decides to launch their token for the first time, on a Decentralised Exchange (such as DAO Pad, GameFI, bscpad), in order to raise funds. An IDO is a variation of an IEO. The difference here is that while an IEO is executed on a centralized platform, an IDO is executed on a decentralized platform.

One of the main advantages of IDOs is that they give investors the opportunity to invest in a project that might usually be closed off to only private banks or venture capital firms[13]. Also, an IDO can be organised by the issuer of a cryptocurrency product or service, independent of any unit, organisation or individual[14].

ADVANTAGES OF IDO

- 1.IDOs allows tokens to be openly traded almost immediately and it guarantees better liquidity that allows for lower price fluctuations.
2. There is no need for anybody's authorization.
- 3.IDOs allow almost everyone to invest. This makes the project more appealing not just to the VCs, but to individual investors.
- 4.It entails lower costs and simple solutions.
- 5.IDOs allow tokens to be listed immediately. Hence, investors can trade their investment with minimal lockup period.
- 6.It is easierto launch compared to ICO and IEO.

DISADVANTAGES OF IDO

- 1.IDOs are highly susceptible to liquidity scams. This is particularly because of the absence of a control mechanism.
- 2.Because of consistent price movements i.e., unstable pricing, traders take unfair advantage of the moving price.
- 3.IDOs give less control to the project owners, which can result in any of the following issues:
 - a.Inability to identify purchasers of the tokens being sold, and the quantify purchased.
 - b.The Price of tokens may start moving after the very first swap.
 - c.Top investors can purchase stacks of tokens of a project which gives them damaging powers over the token project.

[13] Tikarr "Looking For The Next 10X? Why You Should Consider Investing in An Initial Dex Offering (IDO)" (<https://bit.ly/3t085xd>)

[14] IDO can be performed directly from the project's development team on the blockchain platform through transactions from the project's product, the issuer.

CONCLUSION.

As of 12 May 2022, the world's cryptocurrency market was worth more than \$1,204,000,000,000 (One Trillion, Two Hundred and Four Billion Dollars)[15]. This is an indicator of the growth of the cryptocurrency market.

These statistics clearly underscore the fact that the cryptocurrency market is evolving and playing host to new participants and investors, every day. These market participants on their part must do well to ensure that there is little, or no risk involved in the avenue through which they offer these cryptocurrency products (tokens) and services and consequently raise funds.

Investors at their own end, must not only understand how these modes of offering (ICO, IEO and IDO) impact on their cryptocurrency investments, they must also be prudent enough to utilize the appropriate mode of investing.

[15]Raynor De Best "Weekly Market Cap of All Cryptocurrencies Combined up until May 2022"
(<https://www.statista.com/statistics/730876/cryptocurrency-maket-value/>)



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