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Legal update

Delaware provides legal clarification for blockchain maintenance of corporate records – the view from Canada

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Interest in blockchain, the technology driving the virtual currency Bitcoin, has grown dramatically over the last few years as it has the potential to transform many business processes, making these processes more efficient, transparent and secure while reducing human error, costs and administrative delays.

A blockchain is a digital record of transactions between parties on a network. The parties participate collectively in maintaining and validating transactions via a computerized consensus protocol. While many stock exchanges have begun to experiment with blockchain technology as a way to register and trade shares, Delaware's General Corporation Law has recently been amended to provide statutory authority for Delaware corporations to use blockchain, a type of distributed ledger technology or "DLT," for creating and maintaining corporate records, including the corporation's securities register. These legislative changes could eventually "pave the way for the entire life cycle of a share – the issuance, custodianship, trading, shareholder communication and redemption – to be enacted on a blockchain."[1]

As the home of more than 50% of all publicly traded corporations in the United States, including more than 50% of the Fortune 500, Delaware aims to have the "most advanced and flexible business formation statute in the nation"[2] and is taking the lead in providing the optimal legal environment, through its Delaware Blockchain Initiative, to ensure that companies incorporated in Delaware can fully benefit from blockchain technology. In doing so, Delaware sets an important precedent and might influence other jurisdictions such as Canada to follow suit.

Delaware corporate law

Delaware corporate law now specifically recognizes blockchain maintenance of corporate records by allowing such records to be kept on one or more electronic networks or databases provided certain conditions are met, including (1) that the records so kept be converted into clearly legible paper form within a reasonable time and, (2) with respect to securities registers, that such registers be used, among other things, to prepare the list of shareholders or record share transfers.[3] There is no more mention of "officers" in charge of the securities register or records "maintained" by the corporation. Instead, Delaware law now refers to records "administered by or on behalf of the corporation" to ensure blockchain technology can be used for these purposes instead of relying on a corporate officer. These amendments mean private corporations incorporated in Delaware can now track share issuances and transfers using blockchain.

Canadian corporate law

The *Canada Business Corporations Act* (CBCA) specifically requires that a central securities register be maintained by the corporation at its registered office or at any other place in Canada designated by the directors.[4] It allows registers to be entered or recorded by any system of mechanical or electronic data processing or any other information storage device that is capable of reproducing any required information in intelligible written form within a reasonable time.[5] Provincial corporate laws[6] and financial institutions legislation[7] include similar provisions.

Some are of the view that the CBCA should be amended to specifically allow the use of blockchain technology for record-keeping purposes. They argue that the need for a central securities register to be maintained by the corporation at a single location is incompatible with how this technology works. With blockchain, records of share issuances and transfers are kept simultaneously in multiple locations by different users. Participating computers use an automated process to validate the record to be included in the next "block." The information is recorded in a block once this consensus is reached. The full set of blocks forms the blockchain. Each computer participating in the blockchain network maintains a copy of the complete ledger, which is updated in real time as new blocks are created and validated.

Others argue that the CBCA does not prohibit the use of blockchain as long as the full records may be reproduced in intelligible written form within a reasonable time and made available at the corporation's registered office or at any other location in Canada designated by the directors. Although not maintained by the corporation in a single location, these records could form the central securities register.

Why it matters

Blockchain technology facilitates simultaneous record-keeping and validation by providing a secure, transparent and immutable audit trail without the need for any intermediaries. In other words, this technology could eventually enable public corporations to take back control of their own record-keeping as the network itself becomes the intermediary, ensuring the traceability and security of transactions while considerably reducing manual processing and paperwork. Costs would be reduced as there would be no need for a central intermediary or custodians.

A blockchain-based capital markets system could provide greater accuracy and efficiency for settling trades, having the potential to reduce settlement times to minutes, instead of the usual two or three days. Listing shares on a public blockchain would provide greater transparency as all interested parties could view changes to a corporation's share ownership practically as they happen. This of course could be seen as a disadvantage for some investors such as activists wishing to conceal their trades. There is some debate over whether public "permissionless" blockchains or private "permissioned" blockchains would be more desirable in capital markets and ultimately, a range of options offering various degrees of investor anonymity might be proposed.

Using blockchain in corporate record-keeping and in capital markets more generally would have important corporate governance implications. For instance, blockchain technology could enable corporations to streamline proxy voting and provide shareholders with end-to-end confirmation as to how their shares have been voted. Some corporate actions such as dividend payments and stock splits would also be automated.

Further insight from Norton Rose Fulbright on the legal and regulatory implications of blockchain technology can be found here.

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Footnotes

1 Noelle Acheson, Equity Markets on a Blockchain: Delaware's Potential Impact, CoinDesk, July 10, 2017, online: https://www.coindesk.com/equity-markets-blockchain-delawares-potential-impact/.

2 State of Delaware's website: http://www.corp.delaware.gov/aboutagency.shtml.

3 See amendments to Section 224 of Delaware's General Corporation Law, online: http://legis.delaware.gov/BillDetail?LegislationId=2573.

4 Section 50(3) of the CBCA.

5 Section 22(1) of the CBCA.

6 See, for instance, sections 140(1)(d) and 141(1) of the *Business Corporations Act* (Ontario) and sections 31(4) and 35 of the *Business Corporations Act* (Québec).

7 See, for example, section 239 of the *Bank Act* (Canada).

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