September 19, 2022

Attack of the Crypto Acronyms! ICOs, STOs, IEOs, IDOs – What Is What?

An alphabet soup of acronyms has proliferated in the crypto world for the past few years in the context of sales of cryptocurrency and other digital assets. ICOs, STOs, IEOs, IDOs and so on are some of the acronyms that we will briefly explore in this article.

In the 2010s, growing fatigue and disillusionment with traditional financing sources such as venture capital, private equity and traditional stock markets inspired companies that offered technology services and goods to raise funds for their projects and businesses using so-called crowdfunding campaigns. Crowdfunding is a way to raise funds for a specific cause or project by asking a large number of people to donate money, usually in small amounts. Typically, crowdfunding is done online, often through social networks. As crowdfunding projects grew in size and became more sophisticated, crowdfunding campaigns soon began to leverage the then-upcoming blockchain technology, giving rise to fundraising in exchange for offers of cryptocurrency or other digital assets. Enter initial coin offerings, or ICOs.

ICOs pioneered, and soon became a popular mode for, projects to raise funds from the public in exchange for cryptocurrency, typically in the form of utility tokens. Utility tokens are a form of digital cryptocurrency that is issued in order to fund development of a project of the issuer, with the expectation that such tokens ultimately may be used to purchase the goods or service offered by the issuer. Since the utility token sales were unregulated, an inherent flaw in ICOs was the opportunity for scams and fake projects, as there was the possibility projects never would materialize. Moreover, because the smart contracts associated with digital tokens were managed by the issuers themselves, the issuers were not accountable, directly, for the failure of projects, causing investors to incur losses of their investments.

To address the inherent flaw of ICOs, the security token offering, or STO, was born. An STO is similar to an ICO, where an investor exchanges money for coins or tokens. Unlike ICOs, however, STOs distribute fungible tokens that are linked to an underlying security or investment asset such as stocks, bonds, real estate investment trusts or other funds with attached monetary value. Exchanges that offer security token trading need to fully comply with regulations, including extensive investigations into token listings, disclosures of data, and investor vetting and onboarding procedures. The investors, however, invest with peace of mind, knowing that the issuers are bound by investor protection laws. While STOs come with the boon of offering protection to investors, they also come with the bane of such requirements being time-consuming and often expensive for the bootstrapped issuers.

The diminishing popularity of ICOs and STOs paved the way for initial exchange offerings, or IEOs. IEOs are similar to ICOs, except the tokens are launched on a centralized exchange and come with the promise that the investor will not be scammed. IEOs are available exclusively to the exchange's users, although some IEOs may be in several exchanges. The exchanges conduct rigorous vetting of the crypto projects before listing the token and managing the token offering and smart contracts, which adds credibility to the project and the offering and builds trust among the crypto investor community. IEOs are not without drawbacks, however. The centralized nature of the exchanges makes them prone to theft and cyber scams.

The popularity of IEOs was short-lived, thanks to the advent of decentralized exchanges (DEXs) offering initial DEX offerings, or IDOs. DEXs, which do not hold investor funds, are not susceptible to security breaches, as the investors access tokens through their secure wallets. This autonomy, coupled with the elimination of fees to intermediaries–aka centralized exchanges and regulators—and the ability for investors to immediately access and trade the tokens unless a vesting schedule was predetermined, rendered IDOs a better avenue to launch tokens and raise funds without the complications of centralized exchanges. Moreover, because the community of investors—rather than the exchange, the project or a central authority—makes decisions related to the project, there is more accountability to and control in the hands of the investors.

IDOs also are not free of challenges, however. Unlike with ICOs and IEOs, which have waiting periods, the tokens offered in an IDO are immediately available to the investor for trading. This may lead to "pump and dump" scenarios, where initial investors purchase large numbers of tokens, cause a hike in the price and then sell the immediately available tokens at huge profits, resulting in a price drop.

The fast-evolving demands of the crypto community ensure constant evolution of the modes of crypto offerings and trading, which leaves the issuer or the investor—depending on who you are—weighing what is best suited for each of you. Since each form of offering has its own pros and cons, no one size fits all. Day Pitney's Technology Transactions team is well positioned to help investors and issuers evaluate their options.

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