The Investment Lawyer
Covering Legal and Regulatory Issues of Asset Management
VOL. 25, NO. 3 • MARCH 2018

Initial Coin Offerings: Recent Regulatory and Litigation Developments

By Jennifer J. Carlson and Anne M. Selin

A company is considering issuing a customized coin or token to raise money for an application it is building. It feels confident it can capitalize on the growing rise in such innovative funding methods and avoid onerous regulatory regimes in the process. However, the company should proceed very cautiously, lest it raise the ire of regulators here and abroad, as well as investors who may feel defrauded or wronged if the investment is unsuccessful.

This article examines recent enforcement actions and the increasing attention on fundraising methods that use coins or tokens—that is, Initial Coin Offerings (ICOs)—by regulators in the United States, including the Securities and Exchange Commission (SEC), as well as in certain other jurisdictions throughout the world. Ambiguities and dynamic change abound in this area so it is imperative that companies keep abreast of the latest developments. Although a company can still engage in a successful (and fair and lawful) ICO in many jurisdictions, it is important to make sure it seeks out and receives informed advice from counsel in order to manage any potential risks.

The Rise of ICOs

Virtual currency, most notably Bitcoin,[1] has been gaining increasing attention including for its largely volatile (and debatable) valuation.[2] Some fear that this is a "bubble that could burst."[3] However, companies are increasingly capitalizing on its benefits. That being said, one of the purported benefits of virtual currency, the lack of central bank involvement, is also a significant concern, leading many to believe that it may be used by criminals and other bad actors "who look to avoid detection by skirting standard payments systems."[4]

In lockstep with the rise of virtual currency has been the rise of the ICO. The term "ICO" was originally coined to refer to an initial offering of a cryptocurrency. However, the term has come to refer also—and, perhaps, primarily—to a method for raising money by selling tokens that (like Bitcoin and most other cryptocurrencies) operate on decentralized ledger systems, but (unlike Bitcoin and many other cryptocurrencies) generally represent some sort of rights with respect to the issuer.[5] The focus of this article is on the latter types of ICOs.

This method of fundraising has been compared to "crowdfunding" as the ICOs typically "offer buyers of digital tokens the right to use them at some future date to buy a product or service the company will develop."[6] Or, as recently explained by the SEC, "promoters of ICOs may tell purchasers that the capital raised from the sales will be used to fund development of a digital platform, software, or other projects and that the virtual tokens or coins may be used to access the platform, use the software, or otherwise participate in the project."[7] In 2017, companies and other organizations raised more than $3 billion from investors through coin offerings.[8]

However, the rise of ICOs—many of which have been done outside securities regulatory regimes—has been met with some fierce criticism. Some have likened this way of raising money as a "Wild West" situation given that "law and order has not kept pace with the sprawl of society into uncharted territories."[9] As expressed by Joseph Grundfest, who was a commissioner at the SEC in the 1980s and is currently a professor at Stanford University, "I.C.O's represent the most pervasive, open and notorious violation of the federal securities laws since the Code of Hammurabi."[10] Grundfest predicted a rise of enforcement actions and hoped for a "sweep of 50 I.C.O.s."[11]

Recent SEC Enforcement Actions and Lawsuits in the United States

Recap of the SEC's DAO Report

On July 25, 2017, the Securities and Exchange Commission (SEC)'s Division of Enforcement issued its first report evaluating the legal classification of tokens in the context of a virtual organization known as "The DAO" (standing for Decentralized Autonomous Organization), which aimed to sell tokens to investors through an ICO. These tokens were also promoted by a German firm called Slock.it.[12] Although the SEC did not pursue an enforcement action, it did find that the tokens qualified as securities under the United States securities laws (the Securities Act of 1933, as amended (the Securities Act), and the Securities Exchange Act of 1934, as amended (the Exchange Act)).[13] In classifying the token as a security, the SEC applied its longstanding and "flexible" definition of a security from the *Howey* case[14] and reiterated that a security includes an investment contract which "is an investment of money in a common enterprise with a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others."[15] As part of its application of the *Howey* test, the SEC noted that Slock.it and its co-founders actively oversaw The DAO and provided significant managerial efforts including managing vulnerabilities in The DAO's code. Ultimately, the SEC urged companies to examine carefully whether ICO tokens would meet the definition of a security: "The Commission stressed that those who offer and sell securities in the US are required to comply with federal securities laws, regardless of whether those securities are purchased with virtual currencies or distributed with blockchain technology."[16] To be clear, the SEC did not say that *all* ICOs involved securities but rather only that they may involve securities in certain instances and that it was incumbent on companies to take a hard look at whether a token was in fact a security.

Initial Guidance and Investor Alerts from the SEC

Also on July 25, 2017, the SEC issued an Investor Bulletin related to ICOs.[17] It noted that ICOs "may provide fair and lawful investment opportunities" but that they could also be used "improperly to entice investors with the promise of high returns in a new investment space."[18] Later, on August 28, 2017, the SEC's Office of Investor Education and Advocacy Issued an Investor Alert related to public companies making "ICO-related claims."[19] In that Alert, the SEC noted again that while ICOs "may provide fair and lawful investment opportunities" they were also susceptible to wrongdoing. Among other items, investors were cautioned to look for "warning signs of possible ICO-related fraud" such as a "[c]ompany that has common stock trading claims that its ICO is "SEC-compliant" without explaining how the offering is in compliance with the securities laws; or [c]ompany that has common stock trading also purports to raise capital through an ICO or take on ICO-related business described in vague or nonsensical terms or using undefined technical or legal jargon."[20]

Creation of the SEC's Cyber Unit, Additional Guidance and Recent Enforcement Actions

Further reflecting its dedication to the scrutiny of ICOs, on September 25, 2017, the SEC announced

the creation of a new Cyber Unit that would target "cyber-related misconduct."[21] The SEC's press release for the new unit specifically called out a focus on "violations involving distributed ledger technology and initial coin offerings" as well as more traditional cyberthreats like hacking, misconduct perpetrated through using the dark web and threats to trading platforms.[22]

On September 29, 2017, the SEC charged a businessman (Maksim Zaslavskiy) and two companies with defrauding investors related to an ICO involving a token called REcoin, which investors were told was the first ever "cryptocurrency" backed by real estate.[23] Zaslavskiy allegedly told investors that he had a team of lawyers, professionals, brokers, and accountants that would invest REcoin's ICO proceeds in real estate. In reality, according to the SEC, no such operations existed and Zaslavskiy never hired or even consulted any professionals. The SEC sought and obtained an emergency court order freezing the assets of Zaslavskiy and his companies.

The SEC also issued a statement, on November 1, 2017, related to potentially unlawful promotions of ICOs by celebrities and warned that "any celebrity or other individual who promotes a virtual token or coin that is a security must disclose the nature, scope, and amount of compensation received in exchange for the promotion. A failure to disclose this information is a violation of the anti-touting provisions of the federal securities laws."[24]

On November 8, 2017, SEC Chairman Jay Clayton made remarks addressing ICOs and noted that "investors often do not appreciate that ICO insiders and management have access to immediate liquidity, as do larger investors, who may purchase tokens at favorable prices" and that "[t]rading of tokens on these platforms is susceptible to price manipulation and other fraudulent trading practices."[25] He reiterated that the SEC had "warned that instruments, such as 'tokens,' offered and sold in ICOs may be securities, and those who offer and sell securities in the United States must comply with the federal securities law."[26]

Later, at the end of November, Chairman Clayton made even stronger statements indicating that the SEC was going to move into more enforcement action related to ICOs. In particular, he stated at a symposium at which he was the keynote speaker: "I think that now we have given the market a sufficient warning *where we can move from level-setting the field to enforcing it.* … Where we see fraud and where we see people engaging in offerings that are not registered, we are going to pursue them because these types of things have a destabilizing effect on the market."[27] To the issue of what constituted a "security" in an ICO, he bluntly stated: "I have seen none of them [ICOs] that don't have the hallmarks of securities."[28]

True to his words, on December 4, 2017, the SEC announced it had halted a "fast-moving" ICO fraud that had raised up to $15 million by falsely promising to investors a "13-fold profit in less than a month."[29] That case—which also marked the first case filed by the new Cyber Unit—involved a "recidivist" securities law violator named Dominic Lacroix, who had previously been banned from dealing in securities, and his company PlexCorps, which had marketed and sold securities called PlexCoin to investors in the United States and elsewhere. The SEC's complaint charges Lacroix, PlexCorps and another business partner with violating the anti-fraud provisions, and Lacroix and PlexCorps with violating the registration provision of the US federal securities laws. The complaint seeks permanent injunctions and disgorgement plus interest and penalties. On December 14, 2017, a judge in the Eastern District of New York granted the SEC's request for a preliminary injunction to freeze the assets pending trial and noted that the SEC was likely to demonstrate that the entity defendant had violated the Securities Act and Exchange Act and explicitly ruled (without any fulsome explanation) that the "'PlexCoin Tokens' were "investment contracts subject to the Securities Act and Exchange Act."[30]

The SEC's crackdown on ICOs further expanded when it took action against an ICO *without* making

any fraud claims.[31] On December 11, 2017, the SEC halted a San Francisco company's (Munchee Inc., or Munchee) $15 million ICO because Munchee offered and sold tokens to the public without registering the offering under the Securities Act. Munchee Inc. operates an iPhone app that reviews restaurants, and its ICO, which had raised $60,000 from 40 investors before it was shut down by the SEC, offered investors coins (called MUN) in exchange for Bitcoin or Ethereum. As noted above, the SEC order made no allegations of fraud. Ultimately, the company halted the offer, refunded investors and did not pay a penalty to end the investigation.[32]

Notably, and also on December 11, Chairman Clayton issued a "Statement on Cryptocurrencies and Initial Coin Offerings" that included the following warning that the SEC was closely scrutinizing ICOs: "[f]ollowing the issuance of the 21(a) [DAO] Report, certain market professionals have attempted to highlight utility characteristics of their proposed initial coin offerings in an effort to claim that their proposed tokens or coins are not securities. Many of these assertions appear to elevate form over substance."[33] At a December speech for the American Institute of CPAs, Chairman Clayton told the audience that more enforcement actions would follow if coin sponsors continue to ignore securities laws: "We have a pretty good body of law," Clayton told the audience. "But lawyers need to do a better job of explaining when a bit of code becomes a security."[34] On January 4, 2018, Chairman Clayton stated (along with Commissioners Kara M. Stein and Michael S. Piwowar): "Unfortunately, it is clear that many promoters of ICOs and others participating in the cryptocurrency-related investment markets are not following these laws," and "[t]he SEC and state securities regulators are pursuing violations."[35]

More recently, Chairman Clayton said that "market professionals, especially gatekeepers, need to act responsibly and hold themselves to high standards. To be blunt, from what I have seen recently, particularly in the initial coin offering … space, they can do better."[36] He has also stated that "if people don't change their ways we're going to be bringing more cases."[37]

Indeed, on January 30, 2018, the SEC announced that it had obtained a court order to halt another ICO that allegedly raised $600 million in just two months by selling unregistered investments in the "AriseCoin" cryptocurrency.[38] The SEC's complaint centers on misrepresentations by the company and its principals, who allegedly falsely claimed that it purchased an FDIC-insured bank and omitted to disclose the criminal background of key executives.[39] Steven Peikin, Co-Director of the SEC's Enforcement Division, further stated related to the action against AriseCoin that: "This is the first time the Commission has sought the appointment of a receiver in connection with an ICO fraud. We will use all of our tools and remedies to protect investors from those who engage in fraudulent conduct in the emerging digital securities marketplace."[40]

Although we have not yet seen Professor Grundfest's hope for a "sweep of 50 I.C.O.s,"[41] the above recent enforcement actions may just be the tip of the iceberg as the Cyber Unit of the SEC continues to train its sights on ICOs. Moreover, the scrutiny by the SEC is not limited to those companies that offer tokens that may be securities but also extends to so-called intermediaries such as exchanges and brokers who facilitate crypto-currency transactions. In his December 11 Statement noted above, Chairman Clayton also stated that: "In addition to requiring platforms that are engaging in the activities of an exchange to either register as national securities exchanges or seek an exemption from registration, the Commission will continue to seek clarity for investors on how tokens are listed on these exchanges and the standards for listing; how tokens are valued; and what protections are in place for market integrity and investor protection."[42]

Private Class Action Lawsuits

ICOs are also now appearing front and center in lawsuits brought by purchasers of tokens, most notably multiple lawsuits centering around

the blockchain Tezos ICO, which raised $232 million in July 2017[43] for a startup called Dynamic Ledger Solutions, Inc. (DLS). The purchasers of Tezos tokens (Tezzies) purchased the tokens with US dollars, Bitcoin, or Ethereum. A Swiss-based foundation—the Tezos Foundation—was created to collect the ICO proceeds.

Multiple lawsuits were filed as putative class actions against DLS, its founders (Arthur and Kathleen Breitman) and other parties premised on the notion that Tezzies are securities and alleging various causes of action including violations of the federal securities laws, as well as California's Corporate Securities Law of 1968 and California's Unfair Competition Law (Section 17200 of the California Business and Professional Code). On November 13, 2017, a class action lawsuit was filed in federal court in Florida against DLS, the Breitmans, and Tezos Foundation.[44] Moreover, four cases have been filed before the Northern District of California and the Honorable Richard Seeborg, involving the Tezos ICO.[45] Plaintiffs allege, among other things, that the defendants attempted to skirt US securities laws by basing the Tezos Foundation in Switzerland as well as characterizing the funds raised as "donations" rather than investments. Not surprisingly, at least one of the class action complaints features on its first page Professor Grundfest's quote that "I.C.O.s represent the most pervasive, open and notorious violation of the federal securities laws since the Code of Hammurabi."[46]

In one of the four California-based cases (the *MacDonald* case), the plaintiffs sought an emergency injunction to freeze defendants from spending, converting, or dissipating the cryptocurrency assets acquired through the Tezos ICO, which the court denied on December 20, 2017. The court held there was insufficient evidence that the ICO funds, which were being held by the Swiss foundation, were being mismanaged or dissipated pending the lawsuit and, thus, the plaintiff could not show the necessary "irreparable harm" for the provisional remedy.[47] In another one of these cases (*Okuso*), a preliminary injunction hearing was set for January 11, 2018 but was later withdrawn.[48]

Similar ICO lawsuits have been filed in federal court in Florida against Centra Tech, Inc. (whose tokens were promoted by Floyd Mayweather and which may have prompted the SEC's anti-touting statement discussed above) and in federal court in Washington against Giga Watt Inc., a proposed Bitcoin mining host. Lawsuits have also been filed against cryptocurrency exchanges such as Coinbase (*see* below regarding the lawsuit against Coinbase related to an IRS summons), Kraken and the now-defunct Cryptsy.[49] On January 30, 2018, another class action lawsuit was filed by an investor (who is represented by the same plaintiffs' counsel who sued Centra Tech in Florida) in the Northern District of California in connection with an ICO dubbed the "Paragon ICO" that raised at least $70 million in digital cryptocurrencies and that was focused on the marijuana industry.[50]

Most of these lawsuits are still in the early stages (indeed, no class has yet been certified in the *Tezos* cases) but it is clear that entities issuing tokens should consider the potential civil liabilities (be it for securities violations or common law fraud), in addition to regulatory scrutiny. Courts will have increasing input into determining the legal nature of cryptocurrency tokens (for example, whether the particular tokens qualify as securities) and the liabilities and responsibilities for entities and persons that engage in ICOs.

State Securities Authorities, CFTC, and Other Regulators

In addition to the SEC, state securities authorities and the US Commodity Futures Trading Commission (CFTC) are also beginning to regulate ICOs. For example, Texas became the first state to issue administrative orders against cryptocurrency companies. The Texas securities commissioner entered two separate cease-and-desist orders against cryptocurrency companies for unregistered offerings of securities.[51] And on January 4, 2018, the North

America Securities Administrators Association (NASAA), the 50-state association of securities regulatory authorities, reported on its cryptocurrency survey of state regulators and warned of the perils of investing in ICOs and related investment products.[52]

In a 2015 enforcement action, the CFTC expressed the view that Bitcoin and other virtual currencies that are traded in interstate commerce are commodities subject to its anti-fraud and anti-manipulation authority.[53] More recently, the CFTC issued an educational document in which it expresses the admittedly untested view that it has jurisdiction to regulate derivative contracts referencing virtual currencies and margined, leveraged, or financed virtual currency trading, which could be read to include ICOs.[54] In subsequently reported remarks, CFTC Commissioner Quintenz attempted to clarify the CFTC's position by explaining that ICOs "may start their life as a security from a capital-raising perspective but then at some point—maybe possibly quickly or even immediately—turn into a commodity."[55] He explained that the tipping point from a security to a commodity may be when the value of the virtual currency, which he alternatively referred to as a virtual commodity, is no longer based primarily on the efforts of others, but rather is based on its own intrinsic value.[56]

Separately, the CFTC did not stop the Chicago Mercantile Exchange and Chicago Board of Options Exchange from launching Bitcoin futures, and trading opened for these "new derivatives" in December 2017; however, the agency warned customers that speculation in Bitcoin is a "high-risk transaction."[57] The CFTC also held a public meeting in January 2018 to address the self-certification process used by the exchanges to launch the Bitcoin futures products.[58]

Although beyond the purview of this article, it is worth noting that the Financial Industry Regulatory Authority (FINRA) has prioritized its review of broker-dealer involvement in effecting transactions in digital assets and ICOs to ensure FINRA member firms' compliance with federal securities laws and FINRA rules.[59] In addition, the IRS has stated that cryptocurrency must be treated as property for tax purposes and recently won a ruling (on November 30, 2017) by a federal judge in San Francisco who held that Coinbase, an exchange for Bitcoin and Ethereum, needs to surrender certain user date for 2013-2015 to the IRS in response to the IRS' summons.[60]

Certain International Developments

Companies considering an ICO are, of course, not limited to formation and the sale of digital assets in the United States. International companies planning to raise money through an ICO, however, are not necessarily free from regulation under United States law. As we have seen, some entities involved in an ICO may be located in a foreign jurisdiction, such as the Tezos Foundation based in Switzerland, but still subject to the long arm of US federal securities laws if they offer tokens or coins that could be purchased by US persons.

Given the global nature of ICOs and as companies and investors explore ICOs in other jurisdictions, it is important to be aware of how non US jurisdictions are approaching and regulating ICOs. As noted below, the approaches vary widely from extreme (for example, outright banning of ICOs in China and South Korea) to more nuanced and case-by-case approaches similar to the United States. It is also important to recognize that this space is continuously, and often rapidly, evolving. With that caveat, below is a general summary of some varying approaches by different countries.[61]

South Korea and China: Outlawing ICOs

On September 4, 2017, China banned ICOs outright.[62] A joint statement from the People's Bank of China and other government departments advised that individuals and organizations that have completed ICO fundraisings should make arrangements to return funds.[63] Some have argued that the ban is a "temporary measure," but that remains to be seen.[64] China was the first to enact such a ban with South Korea following suit.

In the case of South Korea, financial regulators banned all forms of cryptocurrency-based money raising activities based on concerns about the lack of control and monitoring of ICOs.[65] The Financial Services Commission stated that "stern penalties" would be issued on financial institutions and parties involved in issuing ICOs "without elaborating further on the details of those penalties."[66] More recently, in January 2018, South Korea's justice minister stated that the ministry is preparing a bill *to ban cryptocurrency trading* through its exchanges.[67]

Europe

While known for its comparatively intense regulation, the European Union so far appears relatively receptive to ICOs describing them as an "innovative way of raising money from the public, using coins or tokens."[68] According to one study, startups in Europe raised more capital through ICOs in the last three years than in any other region in the world.[69] However, similar to the investor alerts issued by the SEC noted above, the European Securities and Markets Authority (ESMA) has issued several statements on ICOs after observing the "rapid growth in ICOs globally and in Europe."[70] One statement relates to detailing the risks of ICOs for investors (including warning investors about the high risk of "so-called ICOs" which include the "total loss of your investment" and noting that some ICOs may operate "outside the regulated space" and may be used for fraudulent or illicit activities).

In another statement, the ESMA describes the rules applicable to firms involved in ICOs: "[W]here the coins or tokens qualify as financial instruments it is likely that the firms involved in ICOs conduct regulated investment activities, such as placing, dealing in or advising on financial instruments or managing or marketing collective investment schemes" and "may be involved in offering transferable securities to the public."[71] In those situations, EU rules would apply, such as the Prospectus Directive (requiring publication of a prospectus before the offering is made within an EU Member State), the Markets in Financial Instruments Directive (or MiFID), and the Fourth Anti-Money Laundering Directive.[72] In relation to the Anti-Money Laundering Directive, the European Parliament and the council reached an agreement in December 2017 that the Directive will be amended with a view to virtual currencies and focused on "measures to better counter the financing of terrorism and to ensure increased transparency of financial transactions."[73]

Germany—a prominent Member State of the EU—has also issued warnings to consumers about the risks of ICOs. For example, on November 15, 2017, Germany's Federal Financial Authority (BAFin) released such a warning to investors and also expressed the opinion that tokens qualify as financial instruments and, accordingly, persons dealing with tokens are required to obtain a license from the BaFin pursuant to section 32 of the German Banking Act (Kreditwesengesetz).[74]

Hong Kong

In Hong Kong, the Securities and Futures Commission (SFC) stated that "depending on the facts and circumstances of an ICO, digital tokens that are offered or sold may be 'securities' as defined in the Securities and Futures Ordinance (SFO), and subject to the securities laws of Hong Kong."[75] In particular, examples of situations where tokens could be regarded as securities include the following:

- "Token holders may be given shareholders' rights, such as the right to receive dividends and the right to participate in the distribution of the corporation's surplus assets upon winding up."
- "An issuer may repay token holders the principal of their investment on a fixed date or upon redemption, with interest paid to token holders."
- "Token proceeds are managed collectively by the ICO scheme operator to invest in projects with an aim to enable token holders to participate in a share of the returns provided by the project."[76]

In cases when an ICO involves an offer to the Hong Kong public "to acquire '*securities*' or

participate in a [collective investment scheme], registration or authorization requirements under the law may be triggered unless an exemption applies." Moreover, "parties engaging in the secondary trading of such tokens (for example, on cryptocurrency exchanges) may also be subject to the SFC's licensing and conduct requirements" and "[c]ertain requirements relating to automated trading services and recognized exchange companies may be applicable to the business activities of cryptocurrency exchanges."[77]

Of note, on February 9, 2018, the SFC announced it had sent warnings to seven cryptocurrency exchanges in Hong Kong or with connections to Hong Kong as well as to seven ICO issuers, and the SFC pledged to continue "to closely monitor ICOs."[78]

However, apart from those digital tokens falling within the definition of "securities" under the SFO, "Hong Kong does not have any targeted regulatory measures on virtual commodities in respect of their safety or soundness, as well as the trading platforms or operators of such commodities," which are subject to existing laws of Hong Kong against money laundering, terrorist financing, fraud and cyber-crimes.[79]

Russia

On December 28, 2017, the Russian Ministry of Finance submitted a bill that would limit the amount that can be raised through an ICO to 1 billion rubles [~ USD$17.4 million] and limit the amount that each unqualified investor will be able to invest in an ICO to 50,000 rubles [~$900].[80] In a more recent draft of the bill, the amount of investment was still limited to 50,000 rubles.[81] "Moreover, the Finance Ministry wants to allow only for the trading of cryptocurrencies on licensed exchanges of digital financial assets, or through existing trading platforms that have stock exchange licenses."[82]

Conclusion

Issuers of digital assets, tokens, coins or forms of virtual currency hoping to capitalize on the wave of ICOs should proceed with caution and seek advice of experienced counsel relating to the applicability of securities and other laws in the United States as well as other jurisdictions, including advice that takes into account where and how the tokens or coins are being marketed. Experienced counsel can also assist with precise disclosure that will help satisfy obligations under the federal securities laws. If the token is deemed to be a security, then the ICO must be registered with the SEC under the Securities Act or an applicable exemption from the registration requirements must be available. Depending on the reach of the ICO, other countries' laws and regulations may also apply and local counsel may need to be consulted. ICOs provide an innovative way to raise money and are allowed in most jurisdictions, provided they comply with the many (and dynamically changing) legal regimes.

Ms. Carlson is a partner, and **Ms. Selin** is an associate, in the Palo Alto, CA office of Mayer Brown LLP. The authors would like to thank Holger Schelling, counsel in the Frankfurt, Germany office, David Beam, a partner in the Washington, DC office, Jeckle Chiu, a partner in the Hong Kong office of Mayer Brown JSM, Nina Flax, a partner in the Palo Alto, CA office, and Matthew Bisanz and Kevin Healy, associates in the Washington, DC office, for their assistance in preparing this article.

This article summarizes recent regulatory and litigation developments as of February 9, 2018.

NOTES

1 While Bitcoin became a household name in 2017, other virtual currencies are also on the rise. For instance, XRP is a digital currency offered by the San Francisco startup Ripple, and it has recently soared in valuation and is "quickly becoming the second-largest crypto-asset behind bitcoin and adding 42 percent in the first days of 2018." Paul Vigna, "Ripple Steals Bitcoin's Thunder, Surges 1,184% in a Month,"

Wall Street Journal, Jan. 5, 2018, available at *https://www.wsj.com/articles/ripple-steals-bitcoins-thunder-surges-1-184-in-a-month-1515167147#comments_sector* .

[2] The value of Bitcoin continues to be debated, and Bitcoin's price has been notoriously volatile. It appears that even a panel of prestigious North American economic experts cannot agree on at least a fundamental value of Bitcoin, with Nobel laureate Robert Shiller of Yale arguing that "[t]he results of a serious attempt to assess the value of Bitcoin can only be ambiguous." Jeff Cockrell, "What's the Fundamental Value of a Bitcoin," Chicago Booth Review, (Dec. 21, 2017) available at *http://review.chicagobooth.edu/economics/2017/article/what-s-fundamental-value-bitcoin.*

[3] *See, e.g.*, John Ruwitch, Jemima Kelly, "China Hits Booming Cryptocurrency Market with Coin Fundraising Ban," Reuters, Sept. 4, 2017, available at *https://www.reuters.com/article/us-china-finance-digital/china-hits-booming-cryptocurrency-market-with-coin-fundraising-ban-idUSKCN1BF0R7* (noting concern with "bubble" given "a rapid ascent in the value of cryptocurrencies)."

[4] Steven Russolillo, Sharon Shi, Crystal Tai, and Andrew Peaple, "Bitcoin: The Rise of the Regulators," *Wall Street Journal*, (Jan. 4, 2018) available at *https://www.wsj.com/articles/bitcoin-the-rise-of-the-regulators-1515065459?mod=cx_picks&cx_navSource=cx_picks&cx_tag=video&cx_artPos=6#cxrecs_s.*

[5] A detailed description of initial coin offerings was provided in the November edition of the *Investment Lawyer*, which also examined how the Investment Company Act of 1940 might apply to certain ICOs and discussed the SEC's DAO Report and the SEC's reasoning for finding that certain tokens qualified as securities. Joel S. Telpner and Thomas M. Ahmadifar, "ICOs, the DAO, and the Investment Company Act of 1940," *The Investment Lawyer* (Nov. 2017) available at *http://www.sandw.com/assets/htmldocuments/ICOs%20The%20DAO%20and%20the%20Investment%20Company%20Act.pdf.*

[6] Dave Michaels, "App Maker Halts $15 Million Initial Coin Offering After SEC Investigation," *Wall Street Journal* (Dec. 11, 2017) available at *https://www.wsj.com/articles/app-maker-halts-15-million-initial-coin-offering-after-sec-investigation-1513012449.*

[7] Investor Bulletin, SEC, Initial Coin Offerings (July 25, 2017) available at *https://www.sec.gov/oiea/investor-alerts-and-bulletins/ib_coinofferings.*

[8] Nathaniel Popper, "Initial Coin Offerings Horrify a Former S.E.C. Regulator," *N.Y. Times*, (Nov. 26, 2017) available at *https://www.nytimes.com/2017/11/26/business/initial-coin-offering-critic.html.*

[9] Bernard Marr, "Blockchain, Bitcoin, Cryptocurrency and ICOs- All You Need to Know in 10 Minutes," *Forbes*, (Sept. 15, 2017) available at *https://www.forbes.com/sites/bernardmarr/2017/09/15/blockchain-bitcoin-cryptocurrency-and-icos-all-you-need-to-know-in-10-minutes/#31ec943f6c55*.

[10] "Initial Coin Offerings Horrify a Former S.E.C. Regulator," *supra* n.8.

[11] *Id.* The article further quotes another critique by Chamath Palihapitiya, a venture capitalist, who "expressed enthusiasm about Bitcoin" but "said he thinks that '99 percent of I.C.O.s are a scam.' "

[12] *See Report on Investigation Pursuant to Section 21(a) of the Securities and Exchange Act of 1934: The DAO,* SEC Release No. 81207 (July 25, 2017) available at *https://www.sec.gov/litigation/investreport/34-81207.pdf.; See* also, "ICOs, the DAO, and the Investment Company Act of 1940," *supra* n.5.

[13] *Id.* The SEC noted that it was not analyzing the issue whether The DAO was an "investment company" under Section 3(a) of the Investment Company Act of 1940 because in part "The DAO never commenced its business operations funding projects" but noted that "[t]hose who would use virtual organizations should consider their obligations under the Investment Company Act."

[14] *See* SEC v. W.J. Howey Co., 328 US 293, 301 (1946); *see also* United Housing Found., Inc. v. Forman, 421 US 837, 852-53 (1975) (The "touchstone" of an investment contract "is the presence of an investment in a common venture premised on a reasonable expectation of profits to be derived from

the entrepreneurial or managerial efforts of others."). This definition embodies a "*flexible rather than a static principle*, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits." *Howey*, 328 US at 299 (emphasis added).

15 *See Report on Investigation Pursuant to Section 21(a) of the Securities and Exchange Act of 1934; The DAO, supra* n.12, at 11.

16 Investor Bulletin: Initial Coin Offerings, *supra* n.7.

17 *Id.*

18 *Id*.

19 Investor Alert, SEC US Securities and Exchange Commission's Office of Investor Education and Advocacy, Public Companies Making ICO-Related Claims (Aug. 28, 2017) available at *https://www.investor.gov/additional-resources/news-alerts/alerts-bulletins/investor-alert-public-companies-making-ico-related.*

20 *Id.*

21 Press Release, SEC, "SEC Announces Enforcement Initiatives to Combat Cyber-Based Threats and Protect Retail Investors" (Sept. 25, 2017) available at *https://www.sec.gov/news/press-release/2017-176.*

22 *Id.*

23 Press Release, SEC, "SEC Exposes Two Initial Coin Offerings Purportedly Backed by Real Estate and Diamonds" (Sept. 29, 2017) available at *https://www.sec.gov/news/press-release/2017-185-0.*

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28 *Id.*

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31 Dave Michaels, "App Maker Halts $15 Million Initial Coin Offering After SEC Investigation," *Wall Street Journal* (Dec. 11, 2017) available at *https://www.wsj.com/articles/app-maker-halts-15-million-initial-coin-offering-after-sec-investigation-1513012449*.

32 Proceedings Pursuant To Section 8A of the Securities Act of 1933, Making Findings, And Imposing a Cease-And-Desist Order, Administrative Proceeding File No. 3-18304 (Dec. 11, 2017) available at *https://www.sec.gov/litigation/admin/2017/33-10445.pdf.*

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34 Francine McKenna, "After Bringing ICO case, SEC's Clayton Promises More Cryptocurrency Enforcement," *MarketWatch* (Dec. 4, 2017) available at *https://www.marketwatch.com/story/secs-clayton-promises-more-cryptocurrency-enforcement-2017-12-04.*

35 Statement of Chairman Clayton and Commissioners Kara M. Stein and Michael S. Piwowar on "NASAA Reminds Investors to Approach Cryptocurrencies, Initial Coin Offerings and Other Cryptocurrency-Related Investment Products with Caution" by NASAA (Jan. 4, 2018) available at *https://www.sec.gov/news/public-statement/statement-clayton-stein-piwowar-010418.*

36 Jay Clayton, "Opening Remarks at the Securities Regulation Institute" (Jan. 22, 2018).

[37] Robert Schmidt and Benjamin Bain, "Signaling Crackdown, SEC Boss Emerges as Crypto Skeptic-in-Chief," *Bloomberg* (Jan. 31, 2018).

[38] Press Release, SEC, "SEC Halts Alleged Initial Coin Offering Scam" (Jan. 30, 2018) available at *https://www.sec.gov/news/press-release/2018-8*.

[39] *Id.*

[40] *Id.*

[41] Nathaniel Popper, "Initial Coin Offerings Horrify a Former S.E.C. Regulator," *supra,* n.8. The article further quotes another critique by Chamath Palihapitiya, a venture capitalist, who "expressed enthusiasm about Bitcoin" but "said he thinks that '99 percent of I.C.O.s are a scam.'"

[42] Speech, SEC, "Governance and Transparency at the Commission and in Our Markets," *supra* n.25.

[43] As noted recently in one judicial order dated December 20, 2017 and indicating the volatility and ballooning value of certain cryptocurrency, the cryptocurrency including Bitcoin collected by the ICO that was initially valued at $232 million is now valued "at more than $1 billion." Order Denying Application for Temporary Restraining Order, MacDonald v. Dynamic Ledger Solutions, Inc. No. 17-cv-07095-RS (N.D. Cal Dec. 20, 2017), ECF. No. 35.

[44] Gaviria v. Dynamic Ledger Solutions, Inc., Case No. 17-cv-01959-ORL (M.D. Fl. Nov. 13, 2017).

[45] Those cases are: GGCC, LLC v. Dynamic Ledger Solutions, Inc., et al., Case No. 17-cv-06779-RS (complaint filed Nov. 26, 2017); Okuso v. Dynamic Ledger Solutions, Inc., et al., Case No. 17-cv-06829 (complaint filed Nov. 28, 2017); Baker v. Dynamic Ledger Solutions, Inc., et al., Case No. 17-cv-06850-RS (complaint filed Nov. 29, 2017); MacDonald v. Dynamic Ledger Solutions, Inc., et al., Case No. 17-cv-07095-RS (complaint filed Dec. 13, 2017).

[46] MacDonald v. Dynamic Ledger Solutions, Inc., et al., Case No. 17-cv-07095-RS ECF No. 1 (complaint filed Dec. 13, 2017).

[47] Order Denying Application for Temporary Restraining Order, *supra* n.35).

[48] In *Okuso* responses to complaint are due February 5, 2018 (Breitman) [ECF No. 33] and Mar. 21, 2018 (The Tezos Foundation) [ECF No. 21], respectively. In *Baker,* plaintiff filed a Motion to Remand to state court (San Francisco Superior Court) [ECF No. 13] scheduled to be heard on February 8, 2018. In *MacDonald,* parties stipulated that defendants had until March 6, 2018 to respond to the complaint [ECF No. 54]. Recently, plaintiffs filed a Motion to Expedite Discovery [ECF No. 57] and defendants were ordered to respond to the Motion by Jan. 17, 2018.

[49] Rensel v. Centra Tech, Inc. et al., No. 1:17-cv-24500-JLK, (S.D. Fla. Dec. 13, 2017); StormsMedia LLC v. Giga Watt Inc. et al, No. 2:17-cv-00438-SMJ, (E.D. Wash. Dec. 28, 2017); United States v. Coinbase, Inc., No. 3:17-cv-01431-JSC; (N.D. Cal. Mar. 16, 2017). Clark et al v. Payward, Inc. (dba Kraken), No. 8:17-cv-01623-RAL-TGW (M.D. Fla. Jul. 5, 2017); *Leidel et al v. Coinbase, inc.*, No. 9:16-cv-81992-KAM (S.D Fla. Dec. 13, 2016).

[50] Jack Newsham, "$70M Weed Cryptocurrency Offering Was Illegal, Suit Says," LAW 360 (Jan. 31, 2018), available at *https://www.law360.com/california/articles/1007541/-70m-weed-cryptocurrency-offering-was-illegal-suit-says*.

[51] News Release, Texas State Securities Board, $4 Billion Crypto-Promoter Ordered to Halt Fraudulent Sales, (Jan. 4, 2018), available at *https://www.ssb.texas.gov/news-publications/4-billion-crypto-promoter-ordered-halt-fraudulent-sales.*

[52] North American Securities Administrators Association, "NASAA Reminds Investors to Approach Crypto Currencies, Initial Coin Offerings & Other Crypto Currency-Related Investment Products with Caution," (Jan. 4, 2018), available at *http://www.nasaa.org/44073/nasaa-reminds-investors-approach-cryptocurrencies-initial-coin-offerings-cryptocurrency-related-investment-products-caution/.*

[53] Benjamin Bain, "CFTC Warns of Bitcoin-Futures Dangers, After Allowing Them," *Bloomberg* (Dec. 15, 2017), available at *https://www.bloomberg.com/news/articles/2017-12-15/cftc-warns-of-dangers-from-bitcoin-futures-after-allowing-them.*

[54] LabCFTC, "A CFTC Primer on Virtual Currencies," at 4 (Oct. 17, 2017), available at *http://www.cftc.gov/idc/*

groups/public/documents/file/labcftc_primercurrencies 100417.pdf. LabCFTC is the CFTC's office for promoting responsible "fintech" innovation. It is designed to make the CFTC more accessible to fintech innovators and to create informational documents (referred to as "primers") to educate the public about emerging fintech innovations. These primers, however, are not intended to be the CFTC's official policy or position or limit the CFTC in the future. *See* CFTC, "LabCFTC Overview," available at *http://www.cftc.gov/LabCFTC/Overview/index.htm.*

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