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SEC ICO Probe Underway, But Conflict on Size of Sweep

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FEATURE

"It was a nasty piece of business."

That's how one industry lawyer described a subpoena he saw in January from the Securities and Exchange Commission (SEC), part of the agency's months-long probe into the nascent crypto fundraising mechanism, initial coin offerings (ICOs).

The roughly 25-page document, the lawyer said, was "hyper-detailed," asking for "every bit of communication around the token launch."

But while large financial institutions have the resources and procedures to handle such requests as a matter of course, complying would be a tall order for a startup.

The lawyer said:

"For any normal person trying to respond, it would be hellish."

Still, there was an alternative: instead of producing reams of documents, emails and messages, the recipient of the subpoena could instead just meet with the SEC. "Just come in and talk to us" is how the lawyer, who spoke on condition of anonymity, paraphrased the invitation.

The anecdote illustrates how the agency has been trying to quickly get its arms around the explosive growth in ICOs, which according to [CoinDesk's ICO Tracker](#) have raised nearly \$8 billion

Bitcoin

\$10,3

Ethereum

\$8

Bitcoin Cash

\$1,2

Litecoin

\$

XRP

\$0

Who should be most fearful of SEC's DAO token sale ruling?

☐ Issuers
 ☐ Investors
 ☐ Exchanges
 ☐ Nobody, very unactionable

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cumulatively, the vast majority of that in the last year.

"This is the tool they have to understand the world," said another industry lawyer of the agency's practice of issuing subpoenas and requests for information (RFIs).

A spokeswoman for the SEC declined to comment. The Wall Street Journal [reported on the probe](#) earlier Wednesday, contending that it has kicked into high gear in recent weeks.

Conflicting accounts

But much remains unclear about the ongoing dragnet, including the timing. Several lawyers interviewed by CoinDesk this week said the subpoenas and RFIs started last fall and estimated that there have been perhaps 80 in total.

"They are shotgunning these, we've been warning people about this for months now," another attorney, who wanted to remain unnamed, told CoinDesk.

Yet, others gave even higher estimates of the volume - into the hundreds - and described a recent uptick.

According to industry sources who have seen several ICO subpoenas, the requested information typically includes lists of investors, emails, marketing materials, organizational structures, amounts raised, the location of the funds and the people involved and their locations.

Not only issuers and advisors have been contacted, several sources said, but also exchanges and even investors have received requests as well.

In a recent Senate hearing, SEC Chairman Jay Clayton indicated that the SEC was pounding the beat.

"With the support of my fellow Commissioners, I have asked the SEC's Division of Enforcement to continue to police these markets vigorously and recommend enforcement actions against those who conduct ICOs ... in violation of the federal securities laws," he told lawmakers.

So far, there's been a handful of actions, with notable cases including [Munchee](#) and [AriseBank](#).

Common thread?

One possible interpretation is that the raft of subpoenas could just be a way to scare the industry.

In the view of Carol Van Cleef, CEO of Luminous, a decentralized technology solutions company, that's plausible. "Is this a deterrent or enforcement?" she asked rhetorically.

But in light of Clayton's remarks, Van Cleef said it's likely a common thread will appear in this sweep.

"There have been occasions where [the SEC] has sent out more than one subpoena at one time ...if it is not indicative of a major initiative across the space, they're all related to the same case or they're all interrelated," said Van Cleef, who was previously a longtime financial-services lawyer.

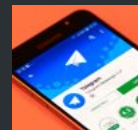
According to multiple sources, many of the ICOs under the microscope have been transactions where investors received a token that does not yet have any use because the proposed blockchain network has yet to be built.

What remains to be seen is if the Simple Agreement for Future Tokens ([SAFT](#)), a bifurcated structure introduced to the market last year to satisfy regulators, will have the intended effect.

Broader context

According to Van Cleef, other recent news in the crypto space could also hint at what the SEC's sweep is all about.

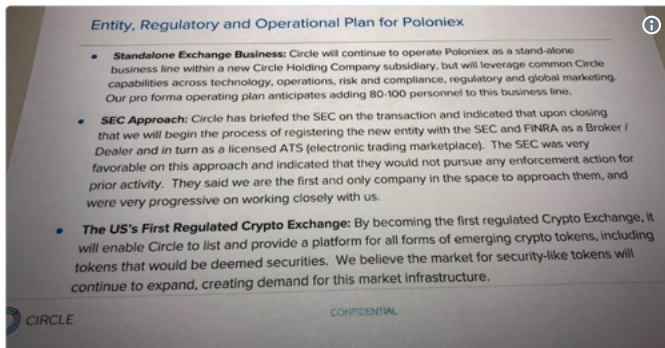
For instance, after Circle's acquisition of crypto exchange Poloniex, New York Times reporter Nathaniel Popper [tweeted](#) out a slide deck apparently showing that the SEC told Circle it would not pursue enforcement action against Poloniex if Circle moved promptly to seek the appropriate regulatory approval to operate the token exchange business.



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Entity, Regulatory and Operational Plan for Poloniex

- **Standalone Exchange Business:** Circle will continue to operate Poloniex as a stand-alone business line within a new Circle Holding Company subsidiary, but will leverage common Circle capabilities across technology, operations, risk and compliance, regulatory and global marketing. Our pro forma operating plan anticipates adding 80-100 personnel to this business line.
- **SEC Approach:** Circle has briefed the SEC on the transaction and indicated that upon closing that we will begin the process of registering the new entity with the SEC and FINRA as a Broker / Dealer and in turn as a licensed ATS (electronic trading marketplace). The SEC was very favorable on this approach and indicated that they would not pursue any enforcement action for prior activity. They said we are the first and only company in the space to approach them, and were very progressive on working closely with us.
- **The US's First Regulated Crypto Exchange:** By becoming the first regulated Crypto Exchange, it will enable Circle to list and provide a platform for all forms of emerging crypto tokens, including tokens that would be deemed securities. We believe the market for security-like tokens will continue to expand, creating demand for this market infrastructure.

CIRCLE CONFIDENTIAL

Nathaniel Popper
@nathanielpopper

Just got this slide from a confidential Circle presentation. It does more to explain Circle's acquisition of Poloniex than anything I have seen today.

1:14 PM - Feb 26, 2018

1,789 likes 1,260 people are talking about this

"On the eve of major SEC action, [Poloniex] sells for \$400 million ... it appears to have been given a huge pass," Van Cleef said.

And what that shows is that going forward, "for entities dealing with possible noncompliance, there's a need for an appropriate balance in the dialogue with the SEC and other government agencies. A failure to manage that dialogue appropriately will make the hurt much more significant."

Brady Dale and Nikhilesh De contributed reporting

SEC image via [Shutterstock](#).

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"According to multiple sources, many of the ICOs under the microscope have been transactions where investors received a token that does not yet have any use because the proposed blockchain network has yet to be built."

For crying out loud, this policy has got to change. ICOs have introduced the most efficient capital formation tool in all of history, and has unleashed innovation on a scale never seen before. And what is the SEC doing? Trying to impede it, that's what. And it's sickening. Time to start lobbying Congress for a change in the law. Public policy ought not to try and stifle this movement.

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