To remain competitive, companies find themselves increasing their efforts to digitally transform their businesses by developing new offerings based on emerging technologies and integrating these technologies into existing product and service offerings.

This is our third monthly bulletin, aiming to help companies identify important and significant legal developments governing the use and acceptance of blockchain technology, smart contracts and digital assets.

While the use cases for blockchain technology are vast, from copyright protection to voting, most of the current adoption is in the financial services section and the focus of this bulletin will be primarily on the use of blockchain and or smart contracts in that sector. With respect to digital assets, we have organized our approach to this topic by discussing it in terms of traditional asset type or function (although the types and functions may overlap), that is, digital assets as:

- Securities
- Virtual currencies
- Commodities
Digital assets can themselves be assets or instead can reflect the ownership of an underlying asset. For example, electronic records that are the equivalents of negotiable instruments and electronic chattel paper would be digital assets, as would an electronic recording of a security interest in the underlying asset, such as recording title to real or personal property and the use of tokens to represent revenue streams from otherwise illiquid assets such as patents and commercial real estate (sometimes referred to as a “tokenized” or digitized asset).

In addition to reporting on the law and regulation governing blockchain, smart contracts and digital assets, this bulletin will also report on the legal developments to support the infrastructure and ecosystems enabling the use and acceptance of these new technologies.

Each issue will feature in-depth insight on a timely and important current topic. In this issue, we take a look at the US Securities and Exchange Commission’s Strategic Hub for Innovation and Financial Technology “Framework for ‘Investment Contract’ Analysis of Digital Assets” and the SEC Division of Corporation Finance’s first “No Action” letter to a startup planning to sell digital assets.

For related information regarding digital transformation, please see our monthly bulletin, eSignature and ePayment News and Trends.

INSIGHT

Digital Asset Report: a Templum interview with DLA Piper’s John Grady

What is the legal status of blockchain regulation today? It’s almost as if the industry is having to build the plane while flying it, says John Grady, chair of DLA Piper’s Investment Management group. In this video interview with Templum co-founder Vince Molinari and journalist Patricia Wu, John discusses the work that regulators, legislators, the industry and DLA Piper are doing together to arrive at a common understanding of the terminology around blockchain and digital assets and then to craft laws and rules that make sense in this swiftly evolving landscape. See the interview.

FEDERAL DEVELOPMENTS

Securities

- **SEC tracing digital assets.** SEC Chair Jay Clayton acknowledged on June 4, 2019 that “SEC staff also trace digital asset transactions on the blockchain. This tracing has been critical to several actions, including two cases in which the Commission obtained preliminary injunctions to stop alleged frauds.”

- **SEC seeks comment on bitcoin ETF proposal.** On May 20, 2019, the SEC issued a notice to institute proceedings to determine whether to approve or disprove a proposed rule change to list and trade shares of the VanEck Solid X Bitcoin Trust. The SEC seeks comment on questions related to the proposal of Cboe BZX Exchange, Inc, which comments are due 21 days after publication in the Federal Register.

- **SEC FinTech Forum.** On May 31, 2019, the SEC hosted the second FinTech Forum to specifically cover distributed ledger technology and digital assets. This event was the first forum sponsored by the SEC’s recently created Strategic Hub for Innovation and Financial Technology (FinHub). Panels covered capital formation, trading and markets, investment management, and distributed ledger technology industry trends and specific use cases for financial markets. FinHub staff also used the forum to announce the SEC’s new visiting scholars program, which is seeking digital asset experts.

- **SEC announces Senior Advisor for Cybersecurity Policy.** On June 3, the SEC announced that Kevin A. Zerrusen will serve as Chairman Jay Clayton’s Senior Advisor for Cybersecurity Policy, coordinating across the Commission to address cybersecurity policy, engage with external stakeholders, and help enhance mechanisms for assessing cyber-related risks.
Commodities

- **FINRA podcast on digital transformation.** On June 11, FINRA released a podcast titled DXT: Transforming the Digital Experience of Firms in which members of FINRA’s technology team discussed how FINRA’s Digital Experience Transformation project can enhance compliance and reduce costs for member firms.

Virtual currency

- **SEC engaging on ETFs.** On June 6, 2019, SEC Chair Jay Clayton discussed regulation of cryptocurrency as well as the SEC’s need for more information regarding custody of digital assets and consumer protection.
- **IRS Commissioner anticipates guidance on virtual currency.** In response to a letter from Representative Tom Emmer (R-MN) and cosigned by other members of Congress, IRS Commissioner Charles Rettig stated on May 16, 2019 that he “has made it a priority of the IRS to issue guidance” on virtual currency transactions and intends to publish such guidance soon.

STATE DEVELOPMENTS

Blockchain

- **Florida establishes blockchain taskforce.** On May 23, 2019, Florida enacted SB1024 establishing a blockchain task force within the Department of Financial Services to develop a master plan for fostering the expansion of the blockchain industry in Florida, recommend policies and state investments to help make Florida a leader in blockchain technology, and report to the governor and the legislature.
- **Illinois enables blockchain business development.** On June 1, 2019, the Illinois legislature passed HB2540, adopting the Blockchain Business Development Act, which provides for the creation and regulation of blockchain-based limited liability companies as businesses that utilize blockchain technology for a material portion of their business activities. It also provides for various blockchain studies and reports and requires the Department of Commerce and Economic Opportunity to incorporate topics concerning blockchain technology and financial technology into business support programs, events, and activities. The bill awaits signature by the governor.
- **Illinois enables smart contracts using blockchain.** The Illinois legislature also adopted the Blockchain Technology Act, HB3575, on May 29, 2019. This act provides for the effectiveness of smart contracts, records, and signatures maintained using blockchain technology, and sets certain limitations to the use of blockchain technology. The bill awaits signature by the governor.
- **Nevada authorizes certain business entities to use blockchain technology for sending communications and storing certain records.** On June 7, 2019, the Nevada governor approved SB163 which allows certain business entities to send certain notices or other communications using blockchain technology by revising the definition of electronic transmission to include private and public blockchain technology. The law also authorizes businesses to store records on a blockchain, and it amends the Secretary of State’s current authority to adopt regulations allowing businesses to perform duties using the most recent technology by specifying that such technology includes blockchain.
- **Nevada revises its UETA for blockchain.** On June 7, 2019, the governor of Nevada approved SB162 which revises its Uniform Electronic Transactions Act to address blockchain technology. Specifically, the bill does the following: (i) it states that a public blockchain as a type of electronic record for the purposes of the Uniform Electronic Transactions Act; (ii) it provides that a person who uses a public blockchain to secure information does not relinquish any right of ownership related to that information; (iii) it requires a governmental agency to accept a certified copy of a record in electronic form under certain circumstances; and (iv) it prohibits a local government from taxing or imposing restrictions upon the use of a public blockchain.
- **Texas authorizes use of blockchain technology for businesses to maintain certain books and records.** On June 10, 2019, the governor of Texas signed into law SB1859, which amends the Business Organization Code to authorize the maintenance of books and records of any domestic filing entity using one or more electronic data systems - which includes blockchain and other distributed ledger technologies - provided that the records can be converted into written paper within a reasonable period of time.

Virtual currency
• **Nevada classifies virtual currency.** The Nevada governor signed SB164 on June 7, 2019, which clarifies that certain currencies are intangible personal property for the purposes of taxation.

**ENFORCEMENT ACTIONS**

**FEDERAL**

**Securities**

• **SEC charges issuer with conducting $100 million unregistered ICO.** On June 4, 2019, the SEC announced that it filed a complaint against a social media and messaging application startup, Kik Interactive, Inc., for conducting an illegal $100 million securities offering of digital tokens, claiming that Kik sold the tokens to US investors without registering the offer and sale as required by the U.S. securities laws. According to the SEC, Kik had lost money for years on its sole product, an online messaging application, and its management predicted internally that it would run out of money in 2017. Nevertheless, in early 2017, the company moved to a new business model that it financed through the sale of digital tokens, raising more than $55 million from US investors. The SEC seeks a permanent injunction, a civil monetary penalty and disgorgement. Kik plans to defend the case, and the Kin Foundation has launched an initiative called DefendCrypto.org with $5 million to fund the potential court battle.

• **SEC complaint filed against perpetrator of pyramid scheme.** The SEC announced on May 22, 2019, that it filed a COMPLAINT against Daniel Pacheco, a California resident and the alleged perpetrator of a multimillion-dollar pyramid scheme selling instructional packages which also provided “points” that could be converted into digital assets known as “PRO Currency.” The agency claims that the fraudulent pyramid scheme raised over $25 million between January 2017 and March 2018 in an unregistered securities offering. The SEC seeks an injunction and civil monetary penalties against Pacheco, as well as disgorgement.

• **SEC charges cryptocurrency company with fraud.** On June 5, 2019, the SEC filed a new fraud action against Longfin Corp. and its CEO for falsifying the company’s revenue and, together with a former Longfin consultant, for fraudulently securing the company’s listing on Nasdaq. The SEC’s prior charges against these defendants and two others resulted in a preliminary injunction freezing more than $27 million in allegedly illegal trading proceeds from unregistered distributions of Longfin stock.

**STATE**

**Virtual currency**

• **Southern District of California sentences operator of unlicensed money transmission business.** On May 28, 2019 Morgan Rockcoons of Las Vegas, Nevada was sentenced to 21 months in prison for wire fraud and operating an unlicensed money transmitting business and was also ordered to forfeit $80,600 in illicit profits. Rockcoons, a US citizen, pleaded guilty on March 7, 2019, admitting that he operated a bitcoin exchange without registering with the Financial Crimes Enforcement Network (FinCEN) of the US Department of Treasury.

**RECENT EVENTS**

• **Hedera Hashgraph master class.** On June 6 in London, 14 lawyers from DLA Piper offices around the world (such as Hong Kong, Silicon Valley, Sydney, Dubai, London and Washington, DC) met with a team from Hedera Hashgraph for an all-day asset tokenization master class. Hedera Hashgraph is a new distributed ledger platform (not based on blocks, so not a blockchain platform) which is designed to be used by enterprises. The Hedera team provided a briefing on how the Hedera platform works and DLA Piper attorneys described how some of their clients were considering the tokenization of their assets. The two teams focused on specific use cases and how Hedera could work with DLA Piper to implement tokenization solutions on the Hedera platform.

*Learn more about our Blockchain and Digital Assets practice by contacting any of our editors:*

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