Blockchain and Digital Assets News and Trends

Achieving Digital Transformation and Securing Digital Assets

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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.

INSIGHT

Facebook announces Libra cryptocurrency – Congress responds

By Benjamin Klein

Facebook has unveiled plans for a digital currency called Libra, which the company hopes will "transform the global economy" by offering an alternative to cash, bank transfers, and credit card transactions. The new cryptocurrency will be governed by the Libra Association, a nonprofit Switzerland-based organization that currently has 28 partners. Facebook also announced the creation of a digital wallet known as Calibra. The Libra/Calibra project has triggered bipartisan anxiety, culminating in two recent congressional hearings. During them, lawmakers repeatedly raised questions about why consumers should put their trust – and cash – in the Facebook-led cryptocurrency given the social media giant's spate of privacy and election-meddling troubles. Find out more.>

FEDERAL DEVELOPMENTS

Securities

- **SEC seeks comment on ways to harmonize private securities offering exemptions.** On Tuesday, June 18, the SEC announced it is requesting comment on its Concept Release on Harmonization of Securities Offering, which considers ways to address challenges in harmonizing the SEC’s framework for private securities offering exemptions. The comment period for the Concept Release will close 90 days after a notice is published in the Federal Register.

- **SEC approves first Regulation A+ token offerings.** On July 10, the SEC approved a $28 million offering under Regulation A+ by blockchain startup Blockstack PBC to sell digital tokens called "Stacks". The company began selling the tokens through its website on July 11. On July 14, the SEC also approved the $50 million offering of Props, a subsidiary of YouNow, Inc., under Regulation A+ for "Props" Tokens. YouNow will use the program to distribute Props Tokens as rewards and grants within YouNow’s network of digital media applications. The Regulation A+ platform was created as an alternative to traditional public offerings and allows companies to raise up to $50 million from retail investors, as opposed to only from accredited investors, and entails reduced documentation requirements. These are the first SEC-approved token offerings.

- **SEC and FINRA issue joint statement on broker-dealer custody of digital asset securities.** On July 8, the SEC and FINRA issued a Joint Statement addressing the ways in which the federal securities laws and regulations and FINRA rules apply to the intermediation of transactions in, and custody of, "digital asset securities." The staffs of the SEC Division of Trading and Markets and FINRA attempted to align the agencies’
historic approach to broker-dealer regulation and investor protection with the new world of digital asset securities. More details are available in our Financial Services Alert.

- **SEC solicits comments on EFT backed by Bitcoin and T-bills.** The SEC published a rule change proposal on June 25 which would allow Wilshire Phoenix Funds to list shares of the United States Bitcoin and Treasury Investment Trust, an exchange-traded fund, on the NYSE Arca exchange. The EFT invests exclusively in bitcoin and short-term US treasury securities. The proposal initiates a 21-day public comment period once published in the Federal Register.

- **Member firms encouraged to notify FINRA if they engage in activities related to digital assets.** On July 18, FINRA issued a Regulatory Notice encouraging its member firms to keep their Regulatory Coordinators abreast of their activities related to digital assets until July 31, 2020. As regulators continue to provide guidance regarding the regulatory challenges presented by digital assets (including the SEC/FINRA Joint Statement on Broker-Dealer Custody of Digital Asset Securities), FINRA believes it is important to maintain communication with its members on this issue.

**Commodities**

- **CFTC approves LedgerX as a designated contract market.** The Commodities Futures Trading Commission (CFTC) announced approval of LedgerX’s application for registration as a designated contract market (DCM). Reportedly LedgerX will allow US consumers to trade on its bitcoin derivatives exchange. As a DCM, LedgerX will offer bitcoin derivatives contracts.

- **CFTC grants DCO registration to blockchain company.** On July 1, the CFTC announced approval of the application of Eris Clearing, LLC as a derivatives clearing organization (DCO). This approval enable Eris to offer clearing services for fully-collateralized virtual currency futures.

**STATE DEVELOPMENTS**

**Blockchain**

- **Florida creates blockchain task force.** On June 25, 2019, the Florida governor approved a bill (HB 1393) that establishes within the Department of Financial Services a Blockchain Task Force to foster the expansion of the blockchain industry in Florida, to recommend policies and state investments, and to issue a report to the Governor and the Legislature. The task force shall study if and how state, county, and municipal governments can benefit from a transition to a blockchain-based system for recordkeeping, data security, financial transactions, and service delivery and identify ways to improve government interaction with businesses and the public. Note that this bill appears substantially similar to SB 1024, which the governor approved on May 23, 2019, and which we covered here.

**Virtual currency**

- **New York DFS grants virtual currency licenses to seed CX companies.** On July 15, the NY Department of Financial Services (DFS) announced that it has approved the applications of Seed Digital Commodities Market LLC (SCXM) and Zero Hash LLC for virtual currency licenses and has approved Zero Hash for a money transmitter license. SCXM and Zero Hash are both subsidiaries of Seed CX Ltd. SCXM will serve as a matching engine and platform for cryptocurrency buyers and sellers. Zero Hash will function as the money transmitter for SCXM’s trading activity. Since 2015, DFS has licensed virtual currency exchanges, technology-based money transmitters, and online lenders operating in New York.

- **Utah regulatory sandbox launched.** On July 2, the second US fintech regulatory sandbox launched in Utah. The sandbox was created under HB378 – see DLA Piper’s coverage of this development here. The sandbox enables money transmission, blockchain, cryptocurrency, and peer-to-peer lending companies in the state to seek regulatory relief as they work on innovative financial projects. No applications for the Utah sandbox have yet been received. Arizona was the first state to launch a fintech sandbox in July 2018, which we reviewed in the September issue of eSignatures and ePayments News and Trends.

- **New licensing and bonding requirements in Rhode Island.** Rhode Island enacted HB 5847 on July 15 to require virtual currency businesses who provide currency transmission to be licensed and bonded in the state. Such businesses must also to provide specified disclosures to their users. The law excludes from the definition of “virtual currency” − (1) value given in a merchant rewards program which value which cannot be exchanged for legal tender, bank credit or virtual currency; (2) value issued by a publisher and used exclusively within an
online gaming platform; and (3) any “native digital token used in a proprietary blockchain service platform.”

**INDUSTRY DEVELOPMENTS**

- **NIST publishes white paper on blockchain digital management approaches.** On July 9, 2019, the National Institute of Standards and Technology published a draft white paper titled “A Taxonomic Approach to Understanding Emerging Blockchain Identity Management Systems.” NIST notes that blockchain technology has the potential to support novel data ownership and governance models with built-in control and consent mechanisms, which may benefit both users and businesses by alleviating concerns over single points of failure, lack of interoperability, and privacy issues such as encouraging mass data collection and user tracking. This paper categorizes these systems based on differences in architecture, governance models, and other salient features. The white paper describes emerging standards and use cases. Comments are due by August 9, 2019.

**ENFORCEMENT ACTIONS**

**FEDERAL**

**Commodities**

- **CFTC enforcement action against bitcoin trading and investment company.** On June 18, the CFTC announced it filed a complaint against Control-Finance Limited and Benjamin Reynolds, the company’s principal. The complaint alleges violations of the Commodity Exchange Act in conducting a fraudulent investment scheme and pyramid scheme, soliciting from investors more than $147 million in bitcoin. The complaint seeks an injunction, restitution, disgorgement, and monetary penalties.

**STATE**

**Securities**

- **Bitcoin investment platform operator sentenced for securities fraud.** On July 12, the US Attorney for the Southern District of New York announced that Jon Montroll, a/k/a Ukyo, was sentenced to 14 months in prison for securities fraud and obstruction of justice for defrauding investors in BitFunder, his bitcoin-denominated trading platform. BitFunder was hacked in 2013, and Montroll had failed to inform investors or regulatory authorities of the theft of 6,000 bitcoin or that the company was insolvent. Montrol was also ordered to pay a forfeiture of more than $160,000.

**Virtual currency**

- **Texas federal court orders restitution in fraudulent Bitcoin solicitation using social media.** On July 10, the CFTC announced that the Northern District of Texas, Fort Worth Division ordered Morgan Hunt, d/b/a Diamonds Trading Investment House, and Kim Hecroft, d/b/a First Options Trading, to pay restitution and nearly $400,000 in civil monetary penalties for violations of the Commodity Exchange Act in conducting an investment Ponzi scheme. The defendants used Facebook to solicit Bitcoin from potential investors seeking to invest in foreign currency contracts, binary options, and diamonds. The defendants reportedly stole the investors’ Bitcoins, using fake account statements and forged CFTC documents.

**Trending**

FATF updates its anti-money laundering and counter-terrorist financing standards.

**More from DLA Piper**

DLA Piper is pleased to announce the release of a special report, “Cryptocurrency and its impact on insolvency and restructuring,” prepared on behalf of INSOL International. Among its findings: the rise in the use of cryptocurrencies has begun to create difficulties for the administration of bankruptcy cases.

**Read this next**
Effective January 1, 2020, a game-changing privacy law will go into effect in California, the California Consumer Privacy Act of 2018. The CCPA will have profound implications for businesses that collect personal information about persons in California, even if the business is not based in the state. Find out more on our CCPA focus page.

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