

Allens › ‹ Linklaters

A Moving Target

Conducting ICOs in a time of regulatory change

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Allens is an independent partnership operating in alliance with Linklaters LLP.





Overview

> Overview

ICOs and Regulatory Change

Our experience working on ICOs

How can your legal advisors assist you in navigating the regulatory framework?

What have the regulators been focussing on and what are they looking at now?



Our Experience

➤ Our Experience

POWER



LEDGER



ivykoin

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Types of tokens

➤ Token Categories

We have seen a variety of different token offerings as part of providing advice on ICOs. The most common of these can generally be separated into three categories:

- Currency Token
- Loyalty or Rewards Token
- Platform Access Token


➤ Token Categories

Currency Token

Payment network facilitating data transmission



Potentially integrates compliance and audit information;
token acts as a redeemable unit of exchange on a network



Token holders can participate in transactions

➤ Token Categories

Loyalty or Rewards Token

Platform enabling stakeholders to incentivise users to interact

Rewards users for certain actions; must be acquired from third party markets

Functions as a unit of reward but gives no other rights; transferable to any third party

➤ Token Categories

Platform Access Token

Platform facilitating peer-to-peer transactions of tokenised 'assets', separated from tokens in a token sale

Token holders can access the platform, exchange into Asset Tokens, and receive services from the platform

Access Tokens give no rights other than use of the platform; transferable to any third party

The background features a dense network of fiber optic cables. Some cables are in sharp focus, showing their individual strands and glowing at the ends, while others are blurred in the background. The color palette is dominated by deep blues, purples, and magentas, with bright white and cyan light points scattered throughout. A large, semi-transparent white arrow shape points from the left side towards the center, framing the text.

Types of financial products

➤ Possible financial products

Tokens issued in an ICO may be any one (or more) of the following financial products:

- Interest in a Managed Investment Scheme
- Security (shares)
- Derivative
- Non-cash payment facility

➤ Interest in a Managed Investment Scheme (MIS)

What is an MIS?	Application to ICOs
<ul style="list-style-type: none">• People contribute money / assets (digital currency) to obtain an interest in a scheme• Any contributions are pooled for a common enterprise to produce financial benefits• The contributors do not have day-to-day control of the scheme	<p>The rights that attach to tokens issued under an ICO is the key consideration.</p> <p>Rights are defined broadly in Corporations Act.</p>

➤ Securities

What is a security?	Application to ICOs
<p>A share is a collection of rights relating to a company.</p> <p>The rights include: ownership of the company, voting rights, rights to future profits, etc.</p> <p>Doesn't need to have all characteristics of a share to be a security.</p>	<p>When an ICO is created to fund a company (similar body), then, if the rights that attach to the token are similar to those that might attach to a share, then the token may fall within this definition.</p>

➤ Derivatives

What is a derivative?	Application to ICOs
<p>A 'derivative' is a product that derives its value from another 'thing' (ie, an underlying asset').</p> <p>This could include a share, share price index, commodity price, etc.</p>	<p>If an ICO produced a token that is priced on factor such as another financial product (ie, a hedge to the price of a commodity), this may fall within the definition of a derivative.</p>

➤ Non-cash payment facility (NCPF)

What is a NCPF?	Application to ICOs
<p>An arrangement through which a person makes payments (or causes payments to be made) other than by physical delivery of currency.</p>	<p>A token may be a NCPF if it is the currency of the platform or allows:</p> <ul style="list-style-type: none">• Payments to be made to a number of payees in this form; and/or• Payments to be started in this form and then converted to \$ to enable completion of the payment

➤ ICOs regulated by Corporations Act

- If the characteristics of a token result in it being classified as an interest in a MIS, security, derivative or NCPF, certain disclosure obligations and potentially licence requirements will apply.
- In many cases, in place of the white paper, it will require the preparation of a formal Prospectus or offer document.
- This, in turn, requires detailed planning in relation to:
 - Due diligence
 - Verification
 - Advice re liability exposure and mitigation
- PDS for other financial products:
 - Licence.

The background features a complex network of fiber optic cables. The cables are dark, with bright blue and purple light emanating from various points, creating a sense of depth and connectivity. The overall color palette is dominated by cool blues and purples, with some warmer tones from the light sources. A large, semi-transparent white arrow points from the left side of the frame towards the center, partially overlapping the text.

Structuring an ICO and the role of legal advisers

➤ ICO Documentation

Most ICOs usually involve the person conducting the ICO preparing:

- the White Paper;
- a Pre-Sale Commitment Letter (commonly referred to as a SAFT) and/or Token Sales Agreement; and
- marketing materials (investor slide deck / public announcements).



➤ What is the role of legal advisors?

As part of a typical ICO, legal advisors can:

- Review the White Paper and marketing materials for misleading or deceptive statements
- Review the White Paper and provide advice on the likelihood of the token (and the broader product offering) being a regulated financial product
- Consider any tax implications
- Interface with the regulators (ASIC / ASX / ATO / APRA / AUSTRAC) as required
- Provide general advice as to conduct of the ICO and token issue
- Liaise with financial / technical advisers



Regulator Focus

➤ Media Release: ASIC takes action on M&DC in ICOs

FINANCIAL REVIEW

NEWS WEBSITE OF THE YEAR

ASIC cracks the whip on misleading and deceptive ICOs, creates taskforce

✉ G+ f t in



The corporate regulator is cracking down on misleading and deceptive ICOs. Shutterstock.com



On 7 May 2018, ASIC published media release 18-122MR 'ASIC takes action on misleading or deceptive conduct in ICOs'

➤ Information Sheets

- Misleading or deceptive conduct is prohibited under the Australian Consumer Law ('ACL') and the ASIC Act
- Information Sheet (INFO 225) '*Initial coin offerings and crypto-currency*' explains how M&DC applies to ICOs

Initial coin offerings and crypto-currency



This information sheet (INFO 225) gives guidance about the potential application of the *Corporations Act 2001* (Corporations Act) to entities that are considering raising funds through an initial coin offering (ICO) and to other crypto-currency or digital token (referred to as 'crypto-asset') businesses. This information sheet covers:

- › Part A: What is the [legal status of ICOs or crypto-assets?](#) This part discusses when laws prohibiting misleading or deceptive conduct, or the Corporations Act, would apply to an ICO or crypto-asset.
- › Part B: [When could an ICO be an offer of a financial product?](#)
- › Part C: [When could a platform for secondary trading of ICO tokens or other crypto-assets become a financial market?](#)
- › Part D: [What about financial products that reference ICO tokens or other crypto-assets?](#)
- › Part E: [How can prospective ICO issuers and crypto-asset businesses obtain informal assistance from ASIC?](#)

➤ How ASIC will take action on M&DC in ICOs

ASIC received delegated powers from the ACCC to act under the ACL

- Applies to 'Crypto-assets' that are either financial or non-financial products

ASIC has made comments about establishing an internal taskforce

- The taskforce will be used to control ICOs – specific details unknown

A recent example:

- ASIC identified misleading statements in a white paper
- The offer was an unregulated managed investment scheme
- The offeror would have been in breach of the Corporations Act if it proceeded

Not an empty threat...

ASIC makes first moves against Australian ICOs after dividend structure throws up red flags

DOMINIC POWELL / Thursday, May 3, 2018



Logo source: The Ethereum Foundation.

The Australian Securities and Investments Commission (ASIC) has taken action against an Australian company poised to commence its own initial coin offering (ICO) after "fundamental concerns" were raised over the token sale's offering to investors.



Questions?



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