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# Regulation A+ Offerings for Tokens: What is the SEC Waiting For?

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**Editor's note:** Robert Rosenblum is partner and Amy Caiazza and Ben Dickson are associates at Wilson Sonsini Goodrich & Rosati. This post is based on a Wilson Sonsini memorandum by Mr. Rosenblum, Ms. Caiazza, and Mr. Dickson.

In a recent article, we discussed why the Securities and Exchange Commission ("SEC") and its staff (the "Staff") continue to think most cryptocurrencies and other crypto assets ("tokens") are securities at the time they are offered.[1] If a token issuer plans to publicly offer and sell tokens that are securities, the offer and sale of those tokens generally needs to be registered (such as on a Form S-1) or qualified under Regulation A+.[2] For many token issuers, a Regulation A+ offering may be the preferable choice; among other reasons, a token offering under Regulation A+ does not need to be separately approved by state securities commissions, while a registered token offering may require state-by-state approval in addition to approval from the SEC.[3]

To date, however, the SEC has not approved any token offerings under Regulation A+. Anecdotally, we understand that a number of Forms 1-A (the form used to qualify tokens and other securities under Regulation A+) have been filed,[4] and that many of the issuers that have filed those forms have received an unusually large and daunting number of comments. This has led some people to speculate that the SEC may not intend to approve Regulation A+ offerings for tokens.

We disagree. Our answer to the question posed in the title of this article—"What is the SEC waiting for?"—is easy: the SEC is waiting for the right Form 1-A. Since the SEC has not yet

[1] Robert Rosenblum et al., *The SEC Thinks Most Tokens Are Securities, For Now*, Law360 (Aug. 10, 2018), https://www.law360.com/articles/1069514/the-sec-thinks-most-tokens-are-securities-for-now.

[2] Section 401 of the Jumpstart Our Business Startups Act ("JOBS Act"), Pub. L. No. 112-106, 126 Stat. 306 (Apr. 5, 2012), added Section 3(b)(2) to the Securities Act of 1933 ("Securities Act"). Section 3(b)(2) directed the SEC to adopt rules adding a class of securities exempt from the registration requirements of the Securities Act for offerings of up to $50 million within a twelve-month period. The SEC adopted these rules as amendments to Regulation A, and these new rules often are referred to as "Regulation A+." *Amendments for Small and Additional Issues Exemptions Under the Securities Act (Regulation A)*, Securities Act Rel. No. 33-9741 (Mar. 25, 2015), 80 Fed. Reg. 21806 (Apr. 20, 2015).

[3] Under Section 18(a) of the Securities Act, "covered securities" are not subject to state registration or qualification requirements. Securities (including tokens) sold pursuant to Regulation A+ are covered securities. *See* Section 18(b)(4)(D)(ii) (securities sold pursuant to a Regulation A+ offering to "qualified purchasers" are covered securities), and Section 18(b)(3) and Rule 256 of Regulation A (people and entities who are authorized to purchase securities in a Regulation A+ offering are qualified purchasers). In contrast, registered securities that (among other things) are not publicly traded on a securities exchange are not covered securities. *See* Section 18(b)(1) of the Securities Act. As a result, registered tokens will not be covered securities at least until a token exchange (or, perhaps, a token alternative trading system) is authorized by the SEC.

[4] Since most Regulation A+ filings are made confidentially, we generally do not yet have any way of reviewing the Regulation A+ filings that have been made.

approved any Forms 1-A, we cannot say with certainty what needs to be in a successful Form 1-A. We also believe that, because of the variety of uses for tokens and the variety of platforms on which tokens will be used, there will be no single, one-size-fits-all approach to drafting Forms 1-A.[5]

Nonetheless, there are a number of topics we can fairly confidently predict any successful Form 1-A will address. The first thing we can confidently say is that just providing the information expressly called for on Form 1-A will not result in success. Regulation A+ and Form 1-A are specifically designed for equity and debt offerings. In fact, only issuers offering equity and debt securities (or securities convertible into equity securities) technically are permitted to use Regulation A+ and Form 1-A.[6] The Staff has informally permitted token issuers to use Form 1-A, even though most tokens do not resemble either traditional equity or debt securities. (This in itself suggests that the Staff intends to approve appropriate Forms 1-A.)

Form 1-A, quite appropriately, is designed to provide investors with information about the company issuing the debt or equity securities, including information about the company that would help an investor assess the company's financial and business prospects that might bear on the likely future value of, and risks with, an investment in that equity or debt. This information may also be valuable to investors in a token offering, especially if the issuer will have significant ongoing responsibility for maintaining, operating, marketing, and improving the platform.

The information expressly required by Form 1-A, however, is not sufficient to provide investors with all of the information they need to make an informed investment decision about the tokens being offered. A successful Regulation A+ offering will therefore need to contain significant information not expressly required by Form 1-A.[7] Among the key topics that we think generally will require significant disclosure in successful Forms 1-A are the following:

- **The Tokens**: It is not enough, we think, to describe the tokens generally. The Form 1-A should describe, among other things, all the current and anticipated uses of the tokens; how and when new tokens will be issued; if applicable, how and when existing tokens will be repurchased, and whether repurchased tokens will be resold or "burned" (or destroyed); any governance rights the token holders have; any governance rights affecting the token holders or the platform that can be exercised by third parties (such as a related foundation or the issuer's board of directors); when and under what circumstances the tokens can be modified; and whether the tokens create any legal

[5] As just one example, we think the disclosure describing a new blockchain and the so-called "protocol layer" tokens for that blockchain (i.e., tokens that can be used as currency on that blockchain and that can be programmed for specific uses for new applications built on that blockchain) would look very different from the disclosure describing a platform and tokens for a blockchain-enabled baseball trading-card system.

[6] *See* Rule 261(c) of Regulation A.

[7] An overarching requirement for any disclosure document is that it must contain all material information, including material information that, if omitted, would make other statements in the disclosure document false, incomplete or misleading. *See* Rule 252(a) under Regulation A ("The offering statement consists of the contents required by Form 1-A…and any other material information necessary to make the required statements, in light of the circumstances under which they are made, not misleading"); Rule 408(a) under the Securities Act ("In addition to the information expressly required to be included in a registration statement, there shall be included such further material information, if any, as may be necessary to make the required statements, in light of the circumstances under which they are made, not misleading"); and Rule 10b-5 under the Securities Exchange Act of 1934 (prohibiting material misrepresentations and omissions in connection with the purchase or sale of any security). *See also Chadbourne & Parke LLP v. Troice*, 571 U.S. 377 (2014) (Rule 10b-5 "forbids the use of any 'device, scheme, or artifice to defraud (*including* the making of 'any untrue statement of material fact or any similar [omission]) in connection with the purchase or sale of any security'") (alterations in original; emphasis added).

obligations on the part of the issuer, such as to pay interest, dividends or other amounts to token holders.

- **The Platform**: The Form 1-A should describe the platform in detail, including what the platform will do; how users will create accounts and transact business on the platform; who can modify the platform and how; what third-parties can or must interact with the platform to make it function correctly (e.g., miners), and how those third parties will be compensated; and planned or reasonably anticipated upgrades to the platform. As part of the approval process for the Form 1-A, a token issuer should be prepared to show the Staff a working version of the platform, or at least a detailed mockup of how the platform will operate.
- **The Token Issuer**: In addition to the information expressly required by Form 1-A about the token issuer, the Form 1-A also should discuss issues such as how the token issuer will interact with and (if applicable) profit from the platform and the tokens; whether, how and to what extent the token issuer will continue to support the platform and the tokens; the token issuer's business plan and financial capacity to support development of the platform; and whether and when the token issuer and its employees and affiliates will sell additional tokens. We also expect there to be unique accounting considerations for token issuers, including considerations related to the correct treatment of prior token sales and of current token holdings, which will need to be resolved with the issuer's accountants and appropriately disclosed in notes to the financial statements and in management's discussion and analysis of the issuer's financial condition.
- **Service Providers**: The Form 1-A should describe in detail the role of and compensation to service providers, such as foundations, miners and "oracles," or others providing data relied on by the platform.
- **Distribution Issues**: There are a number of issues governing how sales of the tokens offered under Regulation A+ will be made, including how the offering circular (i.e., the part of the Form 1-A delivered to investors) will be distributed to purchasers and prospective purchasers; how the issuer and the issuer's employees will avoid being treated as broker-dealers if they are involved in the distribution; and how the tokens will be valued (see more on this below). These and similar issues should be disclosed in the Form 1-A.
- **Valuation of Tokens**: We understand that there is no commonly agreed upon method for valuing tokens. Nonetheless, token pricing may be based on factors that are not typical for other types of offerings. For example, the value of tokens may be affected by the pricing of, supply of, and demand for goods and services sold on a platform, and by expectations of future commercial usage of the platform and the resulting expected demand for tokens. A token issuer may set the price of tokens in a Regulation A+ offering based on these or similar factors, and on the price (if any) the issuer sold tokens for in earlier private sales of tokens. Certain token issuers may also use third-party valuation firms to help inform the pricing of tokens. As discussed earlier, a token issuer should discuss these types of valuation issues, as relevant, in the Form 1-A.
- **Valuation of Non-Cash Compensation Received for Tokens**: Some token issuers may use a Regulation A+ offering to distribute tokens through reward, air-drop, or similar programs, or in return for services related to the development or operation of the token platform, rather than selling the tokens for cash. These types of programs should be disclosed in the Form 1-A, and for tokens sold for non-cash compensation, the Form 1-A should discuss how the services or other non-cash compensation will be valued.

- **Liquidity Issues**: The Form 1-A should discuss how users generally can acquire tokens, such as on an exchange or alternative trading system (if and when the SEC authorizes one or more of them), from continuing offers by the issuer, or from other sources. The Form 1-A also should discuss how holders of tokens who do not wish to use them for commercial purposes can sell the tokens, such as on an exchange or alternative trading system, by tendering the tokens back to the issuer or an affiliate, or in some other manner.
- **Regulatory Issues**: Blockchain platforms and token trading may present various regulatory issues, such as whether the platform is itself functioning as an exchange or alternative trading system that must register with the SEC; whether the issuer or certain service providers are acting as brokers, dealers, transfer agents (entities that record trades and ownership of securities), or clearing agencies (entities that act as intermediaries in making payments or deliveries in connection with securities transactions); and whether certain trading rules may be implicated by the way tokens are offered and sold, including trading rules generally prohibiting an issuer from simultaneously selling and purchasing its securities. Whether these and other regulations (including regulations administered by financial regulators other than the SEC) apply depends upon the specific uses of the tokens and the actual activities performed by or through the platform. The Form 1-A should discuss, as appropriate, any material risks associated with these types of regulatory issues, and any significant limitations of activities or services that may be performed on or provided through the platform as a result of these types of regulatory issues.
- **Securities Law Compliance of Prior Token Offerings**: Many token issuers will have offered tokens or agreements to deliver tokens (often referred to as a Simple Agreement for Future Tokens, or SAFT) prior to offering tokens pursuant to Regulation A+. If those offers and sales were not made in full compliance with an applicable registration exemption, such as Regulation D or Regulation S, the token issuer should consider the need to discuss in the Form 1-A any steps it has taken to remedy the deficiencies. These deficiencies may include, for example, impermissible sales to non-accredited investors, sales of tokens with no appropriate resale restrictions, or sales of tokens with inadequate disclosure that may give rise to potential future liability from early token purchasers.
- **Decentralization, Forking and Similar Considerations**: Many token issuers intend for the operation of the token platform, over time, to become sufficiently "decentralized" so that the token issuer no longer will have meaningful control over their development. In addition, the coding of many tokens permits third parties unrelated to the token issuer to modify, or "fork", the tokens (or the underlying blockchain) so that forked tokens may have significantly different properties or uses from those developed by the token issuer (in some cases, forks may need to be approved by a specified percentage of token holders or others to take effect). Once a token platform has become sufficiently decentralized or once a significant token fork has occurred, the token issuer may no longer have any significant involvement with the tokens or the platform, the token issuer may no longer sell the tokens under Regulation A+, and the token issuer may seek to stop making periodic reports under Regulation A+. The offering circular should describe these circumstances and the corresponding risks to token holders.
- **Risk Factors**: The Form 1-A should include tailored risk factors, such as risk factors that focus on the specific and unique risks posed by the particular tokens and platform, any risks associated with the token issuer and others and their continuing relationship (or potential lack of relationship) with the platform, and specific business or regulatory

constraints that could impede the development of the platform or the use and distribution of the tokens.

Preparation of a Form 1-A that is likely to be successfully declared effective is not a quick or inexpensive undertaking. The amount of work involved is likely at least comparable to the amount of work involved in an initial public offering. To some people familiar with Regulation A+, that sounds strange: Regulation A+, after all, was intended to be a streamlined and relatively inexpensive method for early stage issuers to publicly offer and sell their securities. The important point here, and the point that we hope we have made in this article, is that while we anticipate the SEC and its Staff will permit token issuers to use Regulation A+ and Form 1-A as a vehicle through which they can publicly offer and sell tokens, that vehicle requires significant—and costly—modifications to work for a token offering.