

[Securities Regulation Daily Wrap Up, TOP STORY—S.D.N.Y.: Telegram settles token charges with SEC, \(Jun. 26, 2020\)](#)

Securities Regulation Daily Wrap Up

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By [Mark S. Nelson, J.D.](#)

Telegram Group, Inc. agreed to pay a civil penalty and a massive disgorgement amount that is to be offset by various payments.

The SEC announced that Telegram Group, Inc. and TON Issuer Inc. have settled charges that they issued unregistered securities by offering Grams tokens to buyers. Specifically, Telegram will pay a civil money penalty of \$18.5 million and a massive disgorgement amount of \$1.244 billion, although the disgorgement amount will be offset by more than \$1.193 billion in payments, including funds returned by Telegram to buyers of Grams. The SEC said via a [press release](#) that Telegram and TON Issuer agreed to the court-approved settlement without admitting or denying the SEC's charges (*SEC v. Telegram*, June 25, 2020).

Battle over injunction. The SEC had [sued](#) to shut down the Grams offering, and the case rapidly evolved into one many in the digital asset industry thought might set a precedent about whether there is a way to get tokens to buyers without actually transferring something that is a security at the early stages of developing a digital platform. The district court [ruled](#) in the SEC's favor with respect to the SEC's request for a preliminary injunction.

The SEC also appeared to fend off Telegram's attempt to persuade the court that a [California appellate decision](#) aided Telegram's cause in fighting the preliminary injunction. In the California case, as in the Grams purchase agreements, the purchase agreement expressed uncertainty about the securities status of the thing involved; the district court's ruling on the SEC's preliminary injunction never cited the California case. The SEC later withstood a challenge to the extraterritorial scope of the [preliminary injunction](#) entered by the court.

Settlement terms. The SEC asserted in a [letter](#) accompanying its proposed judgment that the settlement with Telegram is fair and reasonable and in the public interest, and consistent with the Second Circuit's *Citigroup* opinion. Telegram will be subject to a permanent injunction regarding Securities Act Section 5. The company also will have to, for a period of three years, provide the SEC with 45-days' notice of its plans to participate in any digital asset offering.

Moreover, Telegram will have to pay a civil money penalty of \$18.5 million and pay disgorgement of \$1.224 billion. However, the disgorgement amount would be substantially offset by, among other things, amounts Telegram has or will return to buyers of Grams. Although the U.S. Supreme Court decided *Liu v. SEC*, upholding the SEC's ability to obtain disgorgement limited to a defendant's net profits and provided the award aids fraud victims, three days before the SEC submitted its proposed judgment, the proposed judgment did not explicitly mention Telegram's net profits, although the contemplated offsets may address the topic.

Was Telegram about something more? While the *Telegram* case was pending, SEC Commissioner Hester Peirce gave a [speech](#) in which she proposed a rule change that would seemingly accommodate the situation in which Telegram had found itself regarding the SEC's charges. "Many crypto entrepreneurs are seeking to build decentralized networks in which a token serves as a means of exchange on, or provides access to a function of the network. In the course of building out the network, they need to get the tokens into the hands of other people," said Peirce. "But these efforts can be stymied by concerns that such efforts may fall within the ambit of federal securities laws. The fear of running afoul of the securities laws is real. Given the SEC's enforcement activity in this area, these fears are not unfounded."

Although it remains unclear if current SEC Chairman Jay Clayton will [depart](#) the Commission for the U.S. Attorney post in the Southern District of New York, if he did so, the composition of the Commission would

change and the more digital asset-friendly views of Commissioner Peirce could shape the evolution of the Commission's thinking on many digital asset issues. Clayton has previously testified to the effect that many initial coin offerings (ICOs) involve securities, and the SEC has brought numerous enforcement actions against ICOs, albeit while SEC staff also developed a [framework](#) for evaluating the securities status of ICOs.

The case is [No. 19-cv-09439](#).

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Companies: Telegram Group. Inc.; TON Issuer Inc.

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