

Fraud

SEC Halts Allegedly Fraudulent ICO That Employed a Bogus Regulatory Agency and False Claims of SEC Approval

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On October 5, 2018, at the request of the SEC, the U.S. District Court for the Southern District of California (Court) issued a **temporary restraining order** (TRO) stopping an allegedly fraudulent initial coin offering (ICO) by defendants Blockvest LLC (Blockvest) and Reginald Buddy Ringgold, III. The SEC **complaint** (Complaint) alleges that, to give apparent legitimacy to the ICO, the defendants created a bogus regulatory agency modeled on the SEC; falsely claimed that the offering was approved by the SEC and exempt from registration; and engaged in other misleading conduct.

In the **press release** announcing the action, Robert A. Cohen, Chief of the Cyber Unit of the SEC Division of Enforcement, said, “We allege that this ICO is using both the SEC seal and a made-up crypto regulatory authority to trick investors into believing the ICO was approved by regulators. The SEC does not endorse investment products and investors should be highly skeptical of any claims suggesting otherwise.” This article details the SEC’s allegations in the Complaint and the terms of the TRO.

See “**Unregistered Crypto Fund Hit With Multiple Securities Laws Violations by SEC**” (Oct. 18, 2018); and “**SEC Cyber Unit Files Charges Against Allegedly Fraudulent ICO**” (Jan. 11, 2018).

Defendants and Other Relevant Entities

Defendant Blockvest is a Wyoming limited liability company formed in 2018 that has been selling digital tokens known as “BLVs” to raise funds for “various digital asset-related financial products and services.” It registered as a commodity trading advisor with the CFTC on July 24, 2018. It is not registered with the SEC in any capacity.

According to the Complaint, Ringgold, who uses the alias Rasool Abdul Rahim El, is a “self-described ‘Financial Markets Investment Coach’ and ‘professor,’ who claims to have over 17 years of experience in the financial industry as an investment adviser, trader, and investment banker.” Ringgold has never been registered with the SEC or CFTC in any capacity and has never been associated with a registered securities firm.

Ringgold allegedly claims to be the founder of Blockvest and holds himself out as a founder and principal of five entities, none of which are named as defendants in the action:

- Blockchain Exchange Commission, LLC (BEC) is “a private company that purports to be a regulatory organization which, among other things, oversees digital asset trading platforms and ICOs.”
- Blockchain Investment Group LLC (BIG) is listed as a principal of Blockvest with the CFTC and purports to manage Blockvest’s digital assets fund and to offer investment banking services to other blockchain companies.
- Ringgold also formed a similar entity, Blockchain Investment Group LLP (BIG LLP), at the same time as BIG.
- Rosegold Investments LLP (Rosegold), which also uses the name Rosegold Investments Trust, also purports to provide investment banking and advisory services.
- Master Investment Group, Inc. (MIG) purports to provide portfolio management services.

None of the above entities are registered with the SEC or CFTC in any capacity. The defendants and these entities share common officers and the same address: a San Diego UPS store.

Sales of Digital Tokens

In early 2018, Blockvest issued a [white paper](#) for its BLV digital tokens, which are based on the Ethereum blockchain. The white paper and Blockvest’s website indicate that sales of BLVs would be used to finance four planned Blockvest products:

1. a cryptocurrency index fund, known as “Blockvest30,” managed by BIG;
2. a digital currency purportedly linked to the U.S. dollar;
3. an automated portfolio management tool; and
4. Blockvest Decentralized Exchange (DEX), which the white paper describes as “a Bloomberg for crypto economics” that would provide news and information about, and facilitate trading of, digital assets.

According to the Complaint, Blockvest capped the supply of BLVs at 100 million and planned to issue 50 million of them: 32.5 million to investors, 10 million to management, 5 million for certain “reserves” and 2.5 million for promotional activities. Blockvest has allegedly been selling BLVs since March 2018, employing various discounts and incentives. The Ethereum blockchain indicates that, through September 2018, Blockvest had issued over 10 million BLVs. It was planning a global ICO for December 1, 2018.

Unregistered Offering of Securities

The SEC alleged that BLVs constitute securities for purposes of the federal securities laws because:

- The defendants publicly stated that the offering complied with federal securities laws. For example, in one video presentation, Ringgold stated, “The SEC says it’s a security so we registered with the SEC.” See [“Federal District Court in New York Rules That ICOs May Be Securities”](#) (Oct. 4, 2018).
- The defendants filed a Form D with the SEC, which is required when relying on the exemption from registration under [Rule 506\(c\)](#) of Regulation D of the Securities Act of 1933

(Securities Act).

- Blockvest’s website indicated that the offering of BLVs was being conducted pursuant to the exemption from registration under Securities Act Regulation A.
- BLVs have the characteristics of traditional securities:
 - Blockvest’s website and offering materials indicate that investors will share in the profits of Blockvest’s business, including Blockvest30.
 - Those profits would be derived from the skill of Blockvest’s and BIG’s management.
 - Blockvest is referred to as “a closed-end hybrid fund with a profit-sharing smart contract that pays quarterly digital dividends.”
 - BLV holders would earn “passive” income.

For more on ICOs and what constitutes a security, see “[Compliance Corner Q3-2018: Regulatory Filings and Other Considerations That Hedge Fund Managers Should Note in the Coming Quarter](#)” (Jul. 19, 2018); and “[HFLR Cryptocurrency Webinar Examines Regulatory Developments, ICOs, Cryptocurrency Sweep, Custody and Other Compliance Issues](#)” (May 3, 2018).

Consequently, the SEC claimed that the Blockvest ICO is a securities offering that must be registered with the SEC unless an exemption applies. The defendants allegedly have not, however, complied with either exemption from registration. First, although Rule 506(c) permits general solicitation of investors, there is no indication that all purchasers of BLVs were accredited investors, as required by that rule. The offering was not limited by number of investors that may have satisfied other provisions of Rule 506. Second, the offering did not satisfy Regulation A because the defendants failed to file Form 1-A, as required by that rule, and the SEC had not issued a notice of qualification of the offering.

See “[SEC Staff Discuss ‘General Solicitation’ and Other Regulation D Issues](#)” (Jun. 9, 2016); and “[SEC Commissioners and Staff Discuss Possible Amendments to Definition of Accredited Investor](#)” (Jun. 2, 2016).

Material Misrepresentations and Omissions

The Complaint alleges that Blockvest or Ringgold made several material misrepresentations and omissions in connection with the offering and sale of BLVs in the white paper, in online materials or in public statements at blockchain conferences, including that:

- the BLV ICO is “SEC Reg A+ Securities Offering Approved” and “registered with the SEC”;
- DEX has “SEC Reg A+ Approval”;
- Blockvest is a “U.S. SEC approved platform” and has “Reg A approval from the SEC”;
- Blockvest operates “under the helpful eye of the CFTC and NFA”;
- BIG LLP and Rosegold are registered with the CFTC;
- BIG LLP is a member of the NFA;
- George B. Freeman, a member of Blockvest management, is “licensed with FINRA/NFA”; and
- Blockvest funds would be audited by Deloitte Touche Tohmatsu Limited (Deloitte), and the defendants had “partnered with Deloitte” to build an audit technology. Deloitte has no past or present relationship with the defendants or any of their affiliates.

In June 2018, the NFA sent Blockvest a cease-and-desist letter regarding those claims and its misleading use of the NFA logo.

Ringgold allegedly knew or was reckless in not knowing that the representations outlined above were false. He also acted “without reasonable care in claiming to have nonexistent regulatory approvals” or a relationship with Deloitte.

For CFTC regulation of virtual currencies, see “[NFA Mandates New Disclosures on Certain Virtual Currency Activities](#)” (Sep. 20, 2018); “[What Fund Managers Investing in Virtual Currency Need to Know About NFA Reporting Requirements and the CFTC’s Proposed Interpretation of ‘Actual Delivery’](#)” (Mar. 1, 2018); and “[Virtual Currencies Present Significant Risk and Opportunity, Demanding Focus From Regulators, According to CFTC Chair](#)” (Feb. 8, 2018).

Scheme to Defraud

In addition to the misrepresentations detailed above, the defendants allegedly sought to “perpetuate an illusion that that the BLV investment is safe and legitimate by misusing the SEC’s and others’ seals and logos, and through the pretense that is the BEC.” First, the defendants, without authorization, displayed the seals of the SEC, CFTC and NFA, as well as the logos of Deloitte and Vanguard, “amongst other purported partners or affiliates” of their businesses.

Second, Ringgold allegedly created and used the BEC as a “purported regulatory agency that mimics the SEC in numerous ways”:

- the BEC’s logo and mission statement are substantially similar to those of the SEC;
- its LinkedIn webpage lists the SEC’s address as BEC’s address, and the hyperlink in the BEC logo brings users to the SEC website; and
- Ringgold allegedly sought to create the impression that Blockvest was affiliated with a self-regulatory organization.

Ringgold allegedly knew, was reckless in not knowing or acted without reasonable care in using those agency seals and business logos, and in using the existence of the BEC to promote his business and the Blockvest ICO.

Specific Violations and Relief Requested

The SEC charged that, by reason of the alleged unregistered offering of securities and the various misrepresentations and deceptive conduct outlined above, both Blockvest and Ringgold violated the following provisions of the federal securities laws and rules:

- *Securities Fraud (First through Fourth Claims)*: Both defendants violated the antifraud provisions of [Section 10\(b\)](#) of the Securities Exchange Act of 1934 (Exchange Act) and [Rule 10b-5](#) thereunder, as well as [Section 17\(a\)](#) of the Securities Act. Those provisions make it unlawful, in connection with the offering, purchase or sale of securities, to use fraudulent schemes or devices; to make untrue statements or omissions of material fact; and to engage in fraudulent or deceptive business practices.
- *Sale of Unregistered Securities (Fifth Claim)*: Both defendants also violated [Sections 5\(a\) and 5\(c\)](#) of the Securities Act, which make it unlawful to offer or sell securities in interstate commerce unless a valid registration statement is in effect.

The SEC sought the following relief:

- a finding that the defendants engaged in the alleged misconduct;
- temporary, preliminary and permanent injunctions against the defendants' violations of the referenced provisions of the Securities Act and Exchange Act, and against their participation in the offer or sale of any securities, including digital securities;
- an order freezing the defendants' assets, prohibiting them from destroying evidence, requiring an accounting and granting expedited discovery; and
- disgorgement of ill-gotten gains, prejudgment interest and civil penalties.

Temporary Restraining Order

On October 5, 2018, the Court **granted** the SEC's *ex parte* application for the TRO. It agreed that the BLV offering involved the sale of securities and that the SEC had established a *prima facie* case that the defendants had engaged in a scheme to defraud and had acted with culpable intent.

The Court granted the TRO without prior notice to the defendants because of the ongoing nature of the alleged fraud and the possibility that the defendants would seek to dissipate or hide funds, a risk exacerbated by the fact that the case involved "digital assets which can be transferred or secreted instantly and are difficult to trace." The TRO:

- enjoins the defendants from (1) violating the referenced antifraud provisions of the Exchange Act and Securities Act; (2) violating Section 5 of the Securities Act; and (3) participating in any offer or sale of securities or making any misrepresentation about regulatory approval in connection with an offering;
- enjoins the defendants from transferring, dissipating, mortgaging or concealing any of their respective assets and the assets of their subsidiaries or affiliates, including BIG, BIG LLP, BEC, Rosegold and MIG;
- freezes all of the assets of both defendants, as well as of BIG, BIG LLP, BEC, Rosegold and MIG;
- enjoins defendants from damaging, destroying, modifying, concealing or transferring any documents, digital records or other information "pertaining in any manner" to either defendant;
- orders the defendants to provide a detailed and complete schedule of all of their assets, including digital assets, exceeding \$5,000 in value;
- orders any holder of the defendants' assets that receives actual notice of the TRO to provide the SEC with information about those assets; and
- provides for expedited discovery.

The TRO also binds the defendants' officers, employees, agents and attorneys, along with any "other persons in active concert or participation with" the defendants or those persons who receive actual notice of the TRO.

On October 15, 2018, the Court issued an order extending the TRO until November 2, 2018, when there was a hearing on the SEC's request for a preliminary injunction against Blockvest and Ringgold during the pendency of the enforcement action.

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