

How to figure out whether STO is the right choice for your project?

TOKYO, JAPAN, December 27, 2018 /EINPresswire.com/ -- Security token offering, Initial coin offering, and Initial public offering - which method of fundraising a company should choose? Since the beginning of the year the U.S. Securities and Exchange Commission (SEC) started taking action against crypto projects and even hedge funds. Token issuance rules are changing and in order to ensure that your company meets all the requirements you should carefully study the functions your digital asset will perform and the laws it should satisfy.

ICO, STO and the SEC



Let's start with the difference between two fundraising mechanisms based on blockchain technology. STO is a procedure through which an investor receives a security token in exchange for payment. ICO has the same working principle, but purchasers get utility tokens instead.

STO combines ICO's technological features and strictness of IPO registration process and has been invented as a response to new regulations, that seek to protect investors and consumers from cryptocurrencies frauds.

The main difference between STO and ICO is that tokenized securities are financial assets that can be backed by the company's tangible actives, such as shares, revenue of the company, the right to receive dividends or even to vote. As a result, STO solves two major problems of crypto companies – stronger regulation and return of trust.

In comparison, ICO doesn't give any rights or obligations. Due to the previous lack of regulation any company could have issued utility tokens without a prior registration. As a result, investors have lower barrier to entry but still have to take on increased risk.

However, after the SEC started investigating the real function of the tokens, things became a little bit more difficult. In case they find that investors purchased the token with the idea of selling it afterwards, the nature of this digital asset will be reclassified and the issuer will have to pay for violating Securities Law. Not so long ago, SEC has "slapped" Paragon and Airfox ICOs with \$250,000 fine. EtherDelta founder also has been charged with \$388,000 in penalties for operating "Unregistered Securities Exchange".

Is your token a utility or security?

Companies should understand the nature of their token beforehand not to repeat others' errors.

The SEC defines a security as “any transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party.” Only accredited or professional investors can buy this type of tokens.

Utility tokens, in turn, are simply app coins. It means that they enable future access to the products or services offered on the platform of a company. Thus, utility token shouldn't be used for investment purposes.

In order to issue security tokens, a business must complete a registration process similar to an IPO. But in case of STOs the fees are far less than those companies are paying to the investment banks and brokers.

STO: regulations, limitations, specific rules

The main feature of an STO in relation to any other fundraising instrument is that it has less middleman and more automation, which, in turn, corresponds to lower taxes, legal and accounting fees. But before issuing security tokens, a company must register with the SEC, unless they qualify for an exemption.

Below you can find some of restrictions and requirements that both sellers and buyers must meet. First, security tokens cannot be freely traded. According to the SEC, a security owner willing to sell a security restricted to the public has to meet five conditions:

Holding period: typically between 6–12 months

Current public information: Information regarding the nature of its business, the identity of its officers and directors, and its financial statement publicly available

Trading volume formula: <1% of the outstanding shares

Ordinary brokerage transactions

Filing a notice of proposed sale with the SEC

Because security tokens are subject to federal security regulations, issuers in the U.S. can qualify for three distinct exemptions: Reg D, Reg A+ and Reg CF.

In conclusion

Constant investigations conducted by the SEC actually play into the hands of the STO dissemination. In accordance with a level of transition from IPO and ICO mechanisms to STO, it is expected that the market [cap](#) of the last fundraising channel will reach \$10 trillion in 2020.

Overall, it's a quite challenging task to issue security tokens. STO requires a lot of time and money, unless the company is backed up by professionals who know the mechanism like the back of their hand.

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