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# Judge Orders Telegram To Produce Redacted Bank Docs

By **Philip Rosenstein**

Law360 (January 13, 2020, 9:33 PM EST) -- On Monday, a New York federal judge ordered Telegram Group Inc. to produce a trove of bank records by Feb. 26 despite foreign data privacy concerns and questions over the relevance of the documents sought, while allowing for appropriate redactions to comply with foreign privacy laws.

The U.S. Securities and Exchange Commission was **denied immediate access** to Telegram's bank records last week after Judge P. Kevin Castel of the U.S. District Court of the Southern District of New York denied the agency's emergency motion to obtain the documents in a case alleging the company engaged in an unregistered securities offering.

Responding to the SEC's **emergency motion**, Telegram raised concerns with **"foreign data privacy laws,"** adding that producing the records would impose a significant burden on Telegram and would be "ultimately unnecessary given the limited relevance of the information sought."

The SEC challenged Telegram's attempt to limit discovery in a further letter motion on Friday, characterizing the messaging company's "amorphous invocation of 'data privacy'" as a "smokescreen aimed at improperly withholding relevant, responsive documents."

"Invoking the words 'foreign data privacy' is not a talisman that exempts Telegram from its discovery obligations," the SEC said Friday.

The SEC took issue with Telegram's "vague submission," arguing that Telegram has failed to provide enough information showing a need to review the documents for compliance with foreign data privacy laws.

"United States federal courts routinely reject blanket assertions that materials are protected from production in discovery by European privacy laws," the SEC said.

Judge Castel on Monday ordered the production of the documents, allowing Telegram to redact them to comply with foreign data privacy laws. He further requested that Telegram provide a log explaining the rationale for each redaction.

"Only redactions necessitated by foreign privacy laws shall be permitted and a log stating the basis for any redaction shall be produced at the time the redacted documents are produced," the order states. "Defendants shall produce the bank records on a rolling basis and shall complete production by February 26, 2020."

Telegram runs an encrypted messenger app that claims to have 300 million monthly users worldwide and has been called the "cryptocurrency world's preferred messaging app," according to the SEC complaint filed Oct. 11.

John Reed Stark, a cybersecurity consultant and senior lecturing fellow at Duke University Law School who previously led the SEC's internet enforcement division, characterized Monday's order as a "huge win for the SEC."

"It's been pretty clear that the SEC is entitled to this information, particularly in civil litigation where the government is involved," Stark told Law360. Nevertheless, he added that the judge appears to have been cautious given that the documents might be subject to brand new regulations, including the European Union's General Data Protection Regulation.

GDPR provides EU citizens with greater control over their personal data by strengthening their rights and updates privacy rules to reflect technological developments.

Stark suggested that these issues could be debated further in the instant case.

"I have a feeling that if Telegram is aggressive in those redactions that the SEC will be back in front of the judge demanding to see more details," he said.

The SEC filed an emergency letter motion on Jan. 2, saying that reviewing Telegram's bank records to learn more about how the company used the \$1.7 billion raised in the token sale would help answer central questions that inform whether the sale of its digital token, Grams, tripped securities registration requirements.

The case alleges that the sale of the Grams violated Section 5 of the Securities Act of 1933 because the tokens are unregistered securities — **a characterization that Telegram has steadfastly denied**. The company claims the Grams were never publicly offered and instead were sold to sophisticated purchasers under an exemption known as Regulation D.

Telegram's reliance on a Regulation D exemption may be undermined, however, by some of the information the SEC is seeking, with the agency saying it has evidence of underwriting activity.

"The SEC also has evidence that certain entities tendered invoices to Telegram for commissions ranging between 10-15% to Telegram based on the sale of certain purchase agreements," the SEC wrote on Jan. 2.

"These documents undermine Telegram's claimed affirmative defense that the offering was exempt under Regulation D." The SEC filed exhibits to that effect with its Friday letter.

On Jan. 3, Telegram said the request was a "fishing expedition," and part of a "'scorched earth' approach to discovery," arguing that the detailed bank statements are "irrelevant" and producing them would be unduly burdensome.

The case launched with an Oct. 11 complaint, the same day the SEC **obtained a temporary restraining order** to block Telegram and its wholly-owned subsidiary TON Issuer Inc. from delivering approximately 2.9 billion Grams to investors that were planned for distribution no later than Oct. 31, at which time the tokens could then have been sold into U.S. markets.

Telegram **subsequently agreed not to offer**, sell or deliver any tokens until the conclusion a hearing in mid-February on the SEC's request for a preliminary injunction to indefinitely block the delivery of tokens to their 171 private purchasers from around the world.

The SEC said in its Jan. 2 letter that it had gone back and forth with counsel for Telegram on the issue of the production of bank records, with Telegram handing over what the SEC said was an "incomplete production," including "only credits, and not debits showing how Telegram spent the investors' money."

According to the SEC letter, such information would be critical to the "efforts of others" prong of the Howey test, which dictates whether a specific offering is governed by the Securities Act.

The Howey test, stemming from a 1946 U.S. Supreme Court case of the same name, broadly interprets the term "investment contract" under the Securities Act as an agreement in which a person invests money in a common enterprise, expecting profits based on the efforts of others.

The SEC is represented in-house by Marc P. Berger, Jorge G. Tenreiro, Alison Rose Levine, Kevin McGrath and Ladan F. Stewart.

Telegram Group and TON Issuer are represented by George A. Zimmerman, Christopher P. Malloy, Scott D. Musoff and Alex C. Drylewski of Skadden Arps Slate Meagher & Flom LLP.

The case is U.S. Securities and Exchange Commission v. Telegram Group Inc. et al., case number 1:19-cv-09439, in the U.S. District Court for the Southern District of New York.

--Editing by Jay Jackson Jr.

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