

Regulatory and Enforcement Alert

Enforcement Efforts Intensify in the Cryptocurrency Market

October 7, 2021

Key Takeaways

- *The DOJ announces the formation of a National Cryptocurrency Enforcement Team to prosecute crimes committed using cryptocurrency exchanges or facilitated by cryptocurrency.*
- *SEC Chairman Gensler's testimony before the House Committee on Financial Services reinforces the SEC's broad view of cryptocurrencies as securities.*

On October 6, 2021, Deputy Attorney General Lisa O. Monaco announced the formation of a National Cryptocurrency Enforcement Team (NCET), to be drawn from the DOJ's Money Laundering and Asset Recovery Section, its Computer Crime and Intellectual Property Section, and prosecutors from U.S. Attorney's Offices across the country. Evidencing the DOJ's concerns about the use of cryptocurrency exchanges by bad actors to engage in illicit behavior, the NCET will prosecute crimes committed using cryptocurrency exchanges or facilitated by cryptocurrency, including ransomware payments and illicit purchases made using cryptocurrency, money laundering through cryptocurrency exchanges, and crimes committed by cryptocurrency exchanges.

Notably, in announcing the creation of the NCET, the DOJ identified financial institutions working with cryptocurrency as an area of "increased investigative and prosecutorial focus." Given the growing ubiquity of cryptocurrency and digital assets it will be increasingly important for financial institutions and other clients that deal in cryptocurrency to ensure compliance with applicable tax and anti-money laundering laws and regulations.

On October 5, 2021, SEC Chairman Gary Gensler testified before the House Committee on Financial Services (the "Committee") regarding the SEC's regulatory agenda, priorities, and budget. Though the four-hour hearing spanned a gamut of topics, much of the Committee's questioning centered on the extent and scope of the SEC's legal authority to regulate cryptocurrency and whether Congress should create a separate cryptocurrency regulatory regime.

The central takeaway was Chairman Gensler's overarching focus on protecting investors by increasing regulation of cryptocurrency trading, issuance, and lending. This focus is perhaps unsurprising, given his description of the cryptocurrency asset class as "rife with fraud, scams, and abuse in certain applications" and reminiscent of the "Wild West or the old world of 'buyer beware' that existed before the securities laws were enacted." Though few

members of the Committee disputed the SEC's interest in investor protection, they questioned who should effectuate regulation of the cryptocurrency market and how it should be carried out.

First, Chairman Gensler reiterated his view that Congress “painted with a broad brush” in defining the universe of securities within the SEC's investor protection mandate. He said he views most types of cryptocurrency as securities under the federal securities laws, using the Supreme Court's *Howey* test. He also stated that there need not (and should not) be a separate regulatory regime or regulator for cryptocurrency, given risks in creating such a regime, including regulatory arbitrage. Instead, he suggested that any potential regulatory gaps, such as oversight of the platforms that allow for different asset classes to be traded, should be addressed through increased coordination among the SEC and CFTC.¹

Second, Chairman Gensler previewed how the SEC would likely regulate cryptocurrency exchanges. Specifically, he invited cryptocurrency platforms to engage in one-on-one discussions with the SEC and to voluntarily register with the SEC to receive feedback on their legal status. But he also envisioned this to be a two-way dialogue in which platforms would provide feedback on existing rules and regulations that may not be squarely applicable to cryptocurrency exchanges. As market participants have observed, the current elevated levels of enforcement scrutiny of the cryptocurrency sector raise the stakes for even voluntary engagement of the type suggested by Chairman Gensler.

Reflective of the strong focus on cryptocurrency at the federal level, Chairman Gensler's testimony, together with DOJ's creation of the NCET, portend continued, and even increasing, scrutiny and coordination among federal authorities, with the SEC taking a broad position that essentially all cryptocurrency falls within its regulatory remit so long as it constitutes the pooling of money from the public with a reasonable expectation of generating profits. At this point, and as reflected by the spirited nature of Chairman Gensler's testimony, the critical open question is whether the SEC's efforts to drive cryptocurrency actors into the existing regulatory framework will be preempted by new legislation from Congress.

¹ In addition to the CFTC, Chairman Gensler's written remarks also referred to increased coordination on regulatory policy with the Federal Reserve, the Department of Treasury, the Office of the Comptroller of Currency, and the President's Working Group on Financial Markets.

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