

The Crypto Wars Escalate

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The gloves are off. The SEC's recent enforcement actions against leading crypto exchanges suggest that the SEC has decided that time's up for the crypto industry as it currently exists in the United States.

After spending years urging industry participants to come in and register, the SEC has made clear, by going after some of the biggest players in the space, that it does not intend to tolerate exchange operators' offering of unregistered crypto trading in the United States, at least as to retail investors where the tokens are securities. From the SEC's perspective, most crypto tokens are securities, so, if a company wants to provide the securities-like infrastructure to trade those tokens, it must be registered with the SEC – whether as an exchange (matching buyers and sellers), a broker-dealer (trading crypto on behalf of others), or a clearing agency (facilitating trade settlement).

At one point, we might have thought that the SEC was refraining from suing exchanges because it did not want essentially to hamstring the U.S. crypto industry and the U.S. retail investors who have put money into crypto trading. But now, one cannot help wondering whether the SEC believes there is no way for crypto intermediaries to comply with the Securities Exchange Act. Virtually no crypto tokens are registered as securities, so if they *are* considered securities, a registered exchange, broker-dealer, or clearing agency [will have trouble providing services for them](#) in a manner fully compliant with the Exchange Act.

The SEC seems to have lost patience and concluded that the simpler path is to go after the exchanges and limit retail crypto trading, rather than to undertake the more laborious (and perhaps fruitless) task of identifying unregistered tokens or fraudulent vaporware projects one by one. The SEC does not want to allow another FTX to happen. The regulators may be acknowledging (however reluctantly) that they might end up stamping out some innovation while justifying doing so in the interest of preventing further violations.

Coinbase makes an interesting argument in [its Wells response](#) – one that we likely will see in its motion to dismiss to dismiss the SEC’s action: even if crypto or tokens might have been part of a securities offering when they were initially sold to the public, they are just tokens – rather than securities – by the time they trade on Coinbase’s platform. The brands of crypto traded on the exchange do not entitle the traders to profits based on an underlying business at that point; they are only utility instruments and have value only as an asset. Thus, for example, if a crypto offeror initially sells only to a venture-capital firm in an unregistered offering pursuant to a simple agreement for future tokens (SAFT), the transaction is mostly compliant because it does not require registration. Later, when the venture-capital firm sells the tokens after a waiting period, the tokens are no longer part of an “offering.” They are just assets, and they are no longer subject to contractual obligations from the offeror or the seller. We will see whether this argument works at the pleading stage, if Coinbase chooses to raise it there.

As for the SEC’s position: Chairman Gensler might say that, if Congress had told the SEC that it does not have jurisdiction over crypto, or if Congress had enacted legislation that specifically applied to crypto, the SEC would step back and do what Congress says. But Congress has not said anything, so, if the SEC thinks that tokens and other types of crypto are securities under existing law (the *Howey* test), it has no choice but to apply that regulatory framework unless and until the law changes. The exchanges and other defendants in crypto proceedings might need to run out the clock for a bit to see whether Congress can get its act together to write new rules or provide a path to compliance.

Proskauer continues to follow these developments. In the meantime, you might find our blog post, [Crypto Contagion – Managing Risk on Multiple Fronts](#), and *Voice of Litigation* video [Navigating the Legal Landscape of Crypto](#) with partner, [Seetha Ramachandran](#) of interest and helpful.

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