

The Trump Administration's Response to the Blockchain Era

By Matthew R. Lyon*

During the 2016 presidential campaign, Republican nominee Donald J. Trump sent mixed signs regarding his future administration's approach to regulation of the banking and financial sector.¹ On one hand, the Republican Party platform in 2016 included a provision to reinstate the Glass-Steagall Act,² a Depression-era law requiring the separation of investment banking and commercial banking that was repealed in 1999.³ On the other hand, Mr. Trump signaled a return to traditional GOP policies of reduced regulation on banks by promising, on many occasions, to repeal the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010,⁴ one of the Obama Administration's most significant legislative achievements.⁵ Almost immediately after taking office, President Trump signed executive orders that were designed both to limit

* Associate Dean for Academic Affairs & Professor of Law, Lincoln Memorial University Duncan School of Law. College of William & Mary (B.A., 1997); Maxwell School of Citizenship & Public Affairs, Syracuse University (M.P.A., 1998); Northwestern University Pritzker School of Law (J.D., cum laude, 2005).

1. Donna Borak & Henry Williams, *Clinton vs. Trump: Where They Stand on Wall Street*, WALL STREET J., <http://graphics.wsj.com/elections/2016/where-do-clinton-and-trump-stand-on-wall-street/> (last visited Nov. 18, 2018).

2. Pub. L. No. 73-66, 48 Stat. 162 (1933) (repealed 1999).

3. Jeff Sommer, *G.O.P. Joins Democrats Urging Glass-Steagall's Revival. (Don't Hold Your Breath.)*, N.Y. TIMES (July 19, 2016), <https://www.nytimes.com/2016/07/20/business/economy/gop-joins-democrats-urging-glass-steagalls-revival-dont-hold-your-breath.html> (“The 58-page draft of the official party platform included this one short sentence: ‘We support reinstating the Glass-Steagall Act of 1933 which prohibits commercial banks from engaging in high-risk investment.’”).

4. Pub. L. No. 111-203, 124 Stat. 1376.

5. Joseph Lawler, *Seven Times Trump Has Pledged to Appeal Dodd-Frank*, WASH. EXAMINER (May 19, 2016), <https://www.washingtonexaminer.com/seven-times-trump-has-pledged-to-repeal-dodd-frank> (quoting candidate Trump as calling Dodd-Frank a “disaster” that “we have to get rid of” which “stifles business”).

regulation more generally⁶ and to signal his intent to “dismantle” Dodd-Frank specifically.⁷ Eventually the Republican-led Congress passed, and the president signed, significant reforms to the Dodd-Frank Act designed primarily to reduce regulatory burdens on small and mid-sized banks.⁸

While Mr. Trump’s rhetoric on financial regulation during the election “seem[ed] like something of a contradiction” at the time,⁹ in retrospect it actually (or perhaps accidentally) makes some sense. The return of Glass-Steagall would have had the greatest impact on a handful of very large banks. The Dodd-Frank reforms that finally passed Congress on a bipartisan basis fell well short of a full repeal of the Obama-era law and primarily helped “Main Street” rather than “Wall Street” banks—that is, if one assumes that bank holding companies with less than \$250 billion in assets are considered Main Street banks.¹⁰ So, both the GOP platform provision and statements on Glass-Steagall and the actual reforms to Dodd-Frank that were enacted in June 2018 comport with the populist elements in President Trump’s unique strain of “conservatism” that has taken hold of the Republican Party.¹¹ Further reforms to Dodd-Frank seem unlikely at this time,¹² and the threats to “gut” and “dismantle” the

6. Exec. Order No. 13771, 82 Fed. Reg. § 9339 (Feb. 3, 2017). *Presidential Executive Order on Reducing Regulation and Controlling Regulatory Costs*, WHITEHOUSE.GOV (Feb. 3, 2017), <https://www.whitehouse.gov/presidential-actions/presidential-executive-order-reducing-regulation-controlling-regulatory-costs/>.

7. Gillian B. White, *Trump Begins to Chip Away at Banking Regulations*, THE ATLANTIC (Feb. 3, 2017), <https://www.theatlantic.com/business/archive/2017/02/trump-do-dodd-frank/515646/>; Michael C. Bender & Damian Paletta, *Donald Trump Plans to Undo Dodd-Frank Law, Fiduciary Rule*, WALL STREET J. (Feb. 3, 2017), <https://www.wsj.com/articles/trump-moves-to-undo-dodd-frank-law-1486101602>.

8. Mark V. Nucchio & Richard Loewy, *Rolling Back the Dodd-Frank Reforms*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (June 13, 2018), <https://corpgov.law.harvard.edu/2018/06/13/rolling-back-the-dodd-frank-reforms/>.

9. Andrew Ross Sorkin, *One Thing Both Parties Want: To Break up the Banks Again*, N.Y. TIMES (July 25, 2016), <https://www.nytimes.com/2016/07/26/business/deal-book/one-thing-both-parties-want-break-up-the-banks-again.html>.

10. See Zachary Warmbrodt, *House Sends Major Bank Bill to Trump, Capping Years of Effort*, POLITICO (May 22, 2018), <https://www.politico.com/story/2018/05/22/bank-de-regulation-dodd-frank-603388> (quoting House Financial Services Committee Chairman Jeb Hensarling (R-TX) as stating: “I wish it did gut Dodd-Frank. It didn’t.”).

11. Sorkin, *supra* note 9 (“It’s worth noting there is little love lost between the nation’s biggest banks and Mr. Trump: Most of the country’s biggest banks haven’t lent money to him in years.”).

12. Elizabeth Dexheimer, *Top Republican Says GOP Must Move on from Dismantling Dodd-Frank*, BLOOMBERG NEWS (July 12, 2018), <https://www.bloomberg.com/news/articles/2018-07-12/top-republican-says-gop-must-move-on-from-dismantling-dodd-frank> (“[T]he GOP may have gone as far as it can [in May] in revamping the sweeping legislation.

entire law may simply have been based in one of the Trump Administration's central tenets with regard to administrative rulemaking: to take stock of what the Obama Administration did and then do the opposite.¹³

When it comes to nascent industries that were in their infancy, and basically unregulated, prior to January 2017, the Trump Administration did not have a default option to undo the work of the previous administration. This is why blockchain-based industries, in particular cryptocurrencies and the crypto-token markets, provide such a fascinating case study for the Trump Administration's "thin" approach to regulation.¹⁴ As these industries emerged into the investor mainstream, the value of cryptocurrencies such as Bitcoin and Ether rose rapidly in 2017,¹⁵ and markets for initial coin offerings (ICOs) began to overheat, it was left to the team of relatively "conservative-with-a-small-c" regulators that President Trump had appointed to adopt a measured regulatory approach.¹⁶ The good news for crypto-entrepreneurs, early crypto-investors, and the investing public as a whole is that the president's team was up to the task. Generally, President Trump's regulators have used a soft hand and chosen their words carefully, with dual goals of tempering investor expectations and weeding out bad actors in the "Wild West" of the crypto-token markets, while at the same time allowing new blockchain-based industries to mature and providing some needed guidance to the cryptocurrency markets.¹⁷

Congress approved a bill, backed by some Democrats, that mostly eases regulatory burdens on smaller banks, not the Wall Street titans largely blamed for causing the 2008 crisis."); see also Aaron Klein, *No, Dodd-Frank Was Neither Repealed nor Guttled. Here's What Really Happened*, BROOKINGS CTR. ON REG. & MKTS. (May 25, 2018), <https://www.brookings.edu/research/no-dodd-frank-was-neither-repealed-nor-guttled-heres-what-really-happened/>.

13. See, e.g., Juliet Eilperin & Damian Paletta, *Trump Administration Cancels Hundreds of Obama-Era Regulations*, WASH. POST (July 20, 2017), https://www.washingtonpost.com/business/economy/trump-administration-cancels-hundreds-of-obama-era-regulations/2017/07/20/55f501cc-6d68-11e7-96ab-5f38140b38cc_story.html.

14. See generally Eric C. Chaffee, *The Heavy Burden of Thin Regulation: Lessons Learned from the SEC's Regulation of Cryptocurrencies*, 70 MERCER L. REV. 615 (2019).

15. Stan Higgins, *From \$900 to \$20,000: Bitcoin's Historic 2017 Price Run Revisited*, COINDESK (Dec. 29, 2017), <https://www.coindesk.com/900-20000-bitcoins-historic-2017-price-run-revisited>.

16. Alex Guillén, *Trump Orders Agencies to Create Regulatory Reform Task Forces*, POLITICO (Feb. 24, 2017), <https://www.politico.com/story/2017/02/donald-trump-federal-agencies-regulatory-reform-task-force-235353>.

17. Zoë Bernard, *President Donald Trump Assigned a Task Force to Investigate Cryptocurrency Fraud*, BUS. INSIDER (July 13, 2018), <https://www.businessinsider.com/president-donald-trump-task-force-cryptocurrency-fraud-2018-7>.

Part I of this Article provides a brief description of cryptocurrencies, distributed-ledger technology (of which the blockchain is the most well-known), and the use of virtual currencies as a capital-raising mechanism through ICOs. Part II describes the approach taken during late 2017, and thus far in 2018, by the two major federal regulatory agencies that have engaged with the crypto-markets, the Securities and Exchange Commission (SEC) and the Commodity Futures Trading Commission (CFTC), as well as steps taken by other federal agencies, industry self-regulators, and some state regulators, to oversee the crypto-markets. Finally, Part III will discuss the short-term regulatory outlook for crypto-regulation and consider the lessons, if any, it might teach us regarding the Trump Administration's regulation of banks and financial markets during the second half of President Trump's first term in office.

I. THE CRYPTO-ENVIRONMENT FACING THE TRUMP ADMINISTRATION

It is neither feasible nor fitting in this space to fully describe virtual currencies, their numerous uses, and the networks on which they operate. Suffice it to say, however, that anybody trying to understand the regulation of crypto-markets must delineate between three concepts that are sometimes used interchangeably, but which will be regulated very differently: (1) cryptocurrencies; (2) the distributed-ledger technology (DLT) on which cryptocurrency runs; and (3) crypto-tokens (also known as crypto-assets) used in ICOs, which are used to raise capital for DLT and crypto-related ventures and are usually exchangeable for services, access, or some other form of cryptocurrency.¹⁸

A. *Cryptocurrencies*

Bitcoin and other cryptocurrencies have not originated the concept of a digital currency. Indeed, our global economy has been unmoored from the concept of a physical backing for money to some degree since the 1944 Bretton Woods Agreement,¹⁹ and completely since the "Nixon Shock" of

18. See generally Kevin Werbach, *Blockchain Isn't a Revolution*, MEDIUM (June 18, 2018), <https://medium.com/s/story/blockchain-isnt-a-revolution-it-s-two-big-innovations-and-one-promising-idea-988fca6b0fca>; see also Angela Walch, *The Path of the Blockchain Lexicon (and the Law)*, 36 REV. BANKING & FIN. L. 713 (2017) (discussing the fluidity and lack of clarity in the language of blockchain and virtual currencies and the challenges those characteristics pose for regulators).

19. An international monetary conference was held in July 1944 at a resort in Bretton Woods, New Hampshire. Representatives from forty-four countries attended in an effort to develop a stable international monetary system as World War II was coming to a close. The conference established a system of fixed exchange rates in which all currencies were tied to the U.S. dollar, which, at the time, was backed by gold. For a recent detailed treatment of

1971, which suspended the convertibility of the dollar into gold.²⁰ The money that “sits” in our checking accounts, investment accounts, or wherever we choose to hold it, is really just a series of zeros and ones. Ultimately, we are willing to trust that paper notes, and more recently electronic payments, are worth something because our governments’ laws, regulations, and central banks say they are. We are living in the era of fiat currency.²¹

On September 15, 2008, Lehman Brothers, the fourth-largest investment bank in the United States, collapsed.²² Other large banks seemed sure to follow, and the world stood on the brink of economic calamity. At this time of the greatest economic insecurity since the Great Depression, when trust in the governments and banks that issued, maintained, and enforced fiat currencies was at its nadir, Satoshi Nakamoto²³ sent a nine-page document to a cryptography listserve made up of mostly academic recipients.²⁴ Satoshi’s cover email attaching the document more commonly known as “The Bitcoin Whitepaper”²⁵ stated, “I’ve been working on a new electronic cash system that’s fully peer-to-peer, with no trusted third party.”²⁶ We do not know for certain that Satoshi was motivated by the global economic crisis and requisite lack of trust in those entities responsible for maintaining the integrity of fiat currency (indeed, it is likely that Satoshi, like others, had been

the Bretton Woods conference, see generally BENN STEIL, *THE BATTLE OF BRETTON WOODS: JOHN MAYNARD KEYNES, HARRY DEXTER WHITE, AND THE MAKING OF A NEW WORLD ORDER* (2013).

20. See Roger Lowenstein, *The Nixon Shock*, BLOOMBERG BUSINESSWEEK (Aug. 4, 2011), <https://www.bloomberg.com/news/articles/2011-08-04/the-nixon-shock> (revisiting the events surrounding President Nixon’s decision on its fortieth anniversary).

21. “Fiat” is a Latin term meaning “it shall be.” *Fiat Money*, INVESTOPEDIA, <https://www.investopedia.com/video/play/fiat-money/> (last visited Nov. 18, 2018).

22. Many pages have been written about the reasons for the fall of Lehman Brothers and its impact on the broader financial crisis. Some were contemporaneous, see, e.g., LAWRENCE G. McDONALD, *A COLOSSAL FAILURE OF COMMON SENSE: THE INSIDE STORY OF THE COLLAPSE OF LEHMAN BROTHERS* (2009), while others have been written with the perspective of time, see, e.g., LAURENCE M. BALL, *THE FED AND LEHMAN BROTHERS: SETTING THE RECORD STRAIGHT ON A FINANCIAL DISASTER* (2018).

23. The true identity of Satoshi, including whether he/she is a single person or multiple people, has never been determined. Zoë Bernard, *Everything You Need to Know About Bitcoin, Its Mysterious Origins, and the Many Alleged Identities of Its Creator*, BUS. INSIDER (Nov. 10, 2018), <https://www.businessinsider.com/bitcoin-history-cryptocurrency-satoshi-nakamoto-2017-12>.

24. NATHANIEL POPPER, *DIGITAL GOLD: BITCOIN AND THE INSIDE STORY OF THE MISFITS AND MILLIONAIRES TRYING TO REINVENT MONEY* 20 (2015).

25. SATOSHI NAKAMOTO, *BITCOIN: A PEER-TO-PEER ELECTRONIC CASH SYSTEM* (2008), <https://bitcoin.org/bitcoin.pdf>.

26. POPPER, *supra* note 24, at 20–21.

working on the concept of a digital currency for some time),²⁷ but Satoshi later wrote in February 2009, “The root problem with conventional currency is all the trust that’s required to make it work. The central bank must be trusted not to debase the currency, but the history of fiat currencies is full of breaches of that trust.”²⁸

Whatever Satoshi’s motivation, in order for Bitcoin to have any chance of success, Satoshi had to create a decentralized currency that could be trusted to the same extent as a fiat currency. Satoshi did this in three ways: (1) the blockchain network on which Bitcoin exists, which a “community of dedicated users”²⁹ self-regulate to ensure that a single, chronological chain of blocks exists, thus solving the double-spending problem and ensuring that a single unit of Bitcoin can only be transferred once;³⁰ (2) the incentive structure, in which users (“nodes” or “miners”) receive Bitcoins in return for verifying transactions and creating blocks on the network;³¹ and (3) the finite number of Bitcoins, which ensures that the cryptocurrency retains or even increases in value.³²

What makes cryptocurrencies special to the initiated believers are the characteristics of (1) *disintermediation*, with no reliance on a central entity like a bank or a broker to oversee the transaction;³³ (2) *no*

27. *Id.*; see also *id.* at 7–9, 15–20; PAUL VIGNA & MICHAEL J. CASEY, *THE AGE OF CRYPTOCURRENCIES: HOW BITCOIN & DIGITAL MONEY ARE CHALLENGING THE GLOBAL ECONOMIC ORDER* 42–43, 49–57 (2015) (describing the work of the Cypherpunks and other online communities to establish a digital, decentralized currency, beginning in the 1990s).

28. VIGNA & CASEY, *supra* note 27, at 63.

29. *Id.* at 77.

30. Andreas M. Antonopoulos, *Bitcoin Security Model: Trust by Computation*, RADAR (Feb. 20, 2014), <http://radar.oreilly.com/2014/02/bitcoin-security-model-trust-by-computation.html> (arguing that “Bitcoin fundamentally inverts the trust mechanism of a distributed system” because it “implements a trust model of trust by computation.”); see also Laurence J. Trautman & Alvin C. Harrell, *Bitcoin Versus Regulated Payment Systems: What Gives?*, 38 CARDOZO L. REV. 1041, 1061 (2017).

31. POPPER, *supra* note 24, at 100; Carla L. Reyes, *Conceptualizing Cryptolaw*, 96 NEB. L. REV. 384, 393 (2017).

32. To prevent the devaluation of the currency, Satoshi set the time schedule for the release of Bitcoins in the code. Each block was worth fifty Bitcoins in the first four years. That was halved to twenty-five Bitcoins in 2012, halved again in 2016, and then will be halved every four years after that. Jacob Donnelly, *What Is the ‘Halving’? A Primer to Bitcoin’s Big Mining Change*, COINDESK (June 12, 2016), <https://www.coindesk.com/making-sense-bitcoins-halving>. That means the supply of Bitcoins will expire in 2041 and be capped at 21 million Bitcoins. As of November 18, 2018, approximately 17.3 million Bitcoins have been mined, or 82.8% of the total that ever will be available. See *Bitcoin Block Reward Halving Countdown*, BITCOIN BLOCK HALF, <http://www.bitcoinblockhalf.com/> (last visited Nov. 18, 2018).

33. Indeed, there has always been a strong libertarian impetus behind Bitcoin and other cryptocurrencies, making the whole concept of government regulation anathema to

transaction costs, because with no banks or credit card companies taking a cut or sales tax charged, it increases efficiency and allows for micropayments;³⁴ (3) *immediacy*, with transactions taking place instantaneously, or at least within hours, depending upon how quickly the miners are working;³⁵ (4) *access*, including for those in less developed countries with corrupt governments or even the unbanked here in the United States;³⁶ and (5) *security*, whereby the users maintain the system and the identities of the participants are secure.³⁷ Some of the dangers of cryptocurrencies include (1) *no protection* from a government agency like the Federal Deposit Insurance Corporation (FDIC) protecting coin holdings, so if one's coins are held on an exchange that is hacked, they can be lost forever (the most infamous example of this being the hacked Mt. Gox exchange in 2014, which resulted in the theft of approximately 850,000 Bitcoins, nearly 90 percent of which belonged to investors);³⁸ (2) *fees* charged by many virtual currency exchanges, which are anathema to the spirit of cryptocurrencies;³⁹ (3) *use of resources* by the mining

"true believers" in crypto. By way of example, Martti Malmi, widely understood to be the second Bitcoin developer after Satoshi, answered the FAQ, "Why should I use Bitcoin," on the earliest version of the Bitcoin website as follows: "Be safe from the unfair monetary policies of the monopolistic central banks and the other risks of centralized power over a money supply. The limited inflation of the Bitcoin system's money supply is distributed evenly (by CPU power) throughout the network, not monopolized to a banking elite." POPPER, *supra* note 24, at 34.

34. Kevin V. Tu, *Perfecting Bitcoin*, 52 GA. L. REV. 505, 511 (2018). Naturally, a person actually wanting to exchange her dollars for Bitcoin or any other cryptocurrency will have to do so on an exchange that will charge a transaction fee, just like a traditional currency exchange. *See infra* note 39.

35. Steven Buchko, *How Long Do Bitcoin Transactions Take?*, COIN CENTRAL (Dec. 12, 2017), <https://coincentral.com/how-long-do-bitcoin-transfers-take/>.

36. Marc Andreessen, *Why Bitcoin Matters*, N.Y. TIMES (Jan. 21, 2014), <https://dealbook.nytimes.com/2014/01/21/why-bitcoin-matters/> ("Bitcoin, as a global payment system anyone can use from anywhere at any time, can be a powerful catalyst to extend the benefits of the modern economic system to virtually everyone on the planet."); Brian Armstrong, *How Digital Currency Will Change the World*, COINBASE (Oct. 23, 2018), <https://blog.coinbase.com/how-digital-currency-will-change-the-world-310663fe4332>

(discussing the positive impact that digital currencies will have on economic freedom); Charlie Shrem, *Bitcoin's White Paper Gave Us Liberty—Let's Not Give it Back*, COINDESK (Oct. 20, 2018), <https://www.coindesk.com/bitcoins-white-paper-gave-us-liberty-lets-not-give-it-back/>.

37. Reyes, *supra* note 31, at 392–93.

38. VIGNA & CASEY, *supra* note 27, at 104–05; Dan Awrey & Kristin van Zwieten, *The Shadow Payment System*, 43 J. CORP. L. 775, 798–99 (2018) (recounting the Mt. Gox theft and subsequent bankruptcy); Robert McMillan, *The Inside Story of Mt. Gox, Bitcoin's \$460 Million Disaster*, WIRED (Mar. 3, 2014), <https://www.wired.com/2014/03/bitcoin-exchange/>.

39. Ryan Browne, *Big Transaction Fees Are a Problem for Bitcoin—But There Could Be a Solution*, CNBC (Dec. 17, 2017), <https://www.cnbc.com/2017/12/19/big-transactions-fees->

process, which creates barriers to entry and has negative environmental externalities;⁴⁰ and (4) the *volatility* of the market for cryptocurrencies.⁴¹ This last point has impeded the use of cryptocurrencies as a payment system; investors are “HODL-ing” them as an investment item, like gold.⁴²

B. Distributed-Ledger Technology

It is important for regulators to distinguish cryptocurrencies from the technology on which they operate. Distributed-ledger technology (DLT) is the generic term for a decentralized, immutable, automated network in which anonymous or pseudonymous users verify, record, and broadcast digital transactions contemporaneous with their occurrence.⁴³

are-a-problem-for-bitcoin.html; Jorn van Zwanenburg, *Cryptocurrency Transaction Fees: A Beginner's Guide*, CNBC (Dec. 19, 2017), <https://www.investinblockchain.com/cryptocurrency-transaction-fees-for-beginners/>.

40. Eric Holthuas, *Bitcoin Mining Guzzles Energy—And Its Carbon Footprint Just Keeps Growing*, WIRED (Dec. 6, 2017), <https://www.wired.com/story/bitcoin-mining-guzzles-energy-and-its-carbon-footprint-just-keeps-growing/> (observing that Bitcoin mining consumes more energy annually than 150 countries).

41. The price of Bitcoin has fluctuated from \$710 on November 8, 2016, the date President Trump was elected, to \$19,500 on December 17, 2017, before settling to between \$6,000 and \$7,000 for most of summer and fall 2018. *Bitcoin Charts*, COIN MKT. CAP, <https://coinmarketcap.com/currencies/bitcoin/> (last visited Nov. 19, 2018); see also VIGNA & CASEY, *supra* note 27, at 107–11; Trautman & Harrell, *supra* note 30, at 1056–57 (discussing the volatility of Bitcoin from 2014 to 2016). As of this writing, there are over 2100 recognized cryptocurrencies. *All Cryptocurrencies*, COIN MKT. CAP, <https://coinmarketcap.com/all/views/all/> (last visited Nov. 19, 2018). Bitcoin, the original cryptocurrency, has far and away the largest market cap—currently \$112.4 billion. *Id.* Ether, with a market cap of \$21 billion, and Ripple, with a market cap of \$18.1 billion, are the next largest. *Top 100 Cryptocurrencies by Market Capitalization*, COIN MKT. CAP, <https://coinmarketcap.com/> (last visited Nov. 19, 2018).

42. “When it’s used as a store of value, then it’s very much like an asset, like a commodity. In fact, what we hear a lot of, is people buying and holding. If you go on to the Twitter universe you’ll see a phrase ‘H-O-D-L,’ which means hold on for dear life.” Chris Giancarlo, Chairman, U.S. Commodities Futures Trading Comm’n, Recorded Remarks During the Committee on Banking, Housing, and Urban Affairs’ Hearing Entitled, Virtual Currencies: The Oversight Role of the U.S. Securities and Exchange Commission and the U.S. Commodity Futures Trading Commission (Feb. 6, 2018), <https://www banking.senate.gov/hearings/virtual-currencies-the-oversight-role-of-the-us-securities-and-exchange-commission-and-the-us-commodity-futures-trading-commission> (remarks occur at 1:06:35); see also Shawn Langlois & Jessica Marmor Shaw, “Hodl-ing” Bitcoin: The Term Is So Popular, It Made It into Senate Testimony, MARKETWATCH (Feb. 6, 2018), <https://www.marketwatch.com/story/are-you-hodling-bitcoin-2017-09-12>.

43. Malcolm Campbell-Verduyn & Marcel Goguen, *A Digital Revolution Back to the Future: Blockchain Technology and Financial Governance*, 37(9) BANKING & FIN. SERV. POL’Y REP. 1, 1 (2018); see also Walch, *supra* note 18, at 724 (suggesting that the increased

The DLT on which Bitcoin operates is the Blockchain; the DLT for Ether is the Ethereum network.⁴⁴ Both DLT networks support other crypto-coins and other uses and operate on the same basic architecture and assumption: a “shift from hierarchical to more community-based forms of governance” in which the users, rather than central banks or government, maintain the system and verify its trustworthiness.⁴⁵ This, of course, was Satoshi’s original intent: a “system based on cryptographic proof instead of trust, allowing any two willing parties to transact directly with each other without the need for a trusted third party.”⁴⁶

Blockchain technology, which originated to support a cryptocurrency, Bitcoin, has myriad uses across different sectors of our economy that are only just starting to be realized. Many DLTs are being built on the Blockchain or Ethereum networks but are private, not public.⁴⁷ The financial sector has been one of the most aggressive in pursuing DLT-related solutions in order to streamline payments and improve financial products and services, which is ironic given the original intent behind Satoshi’s whitepaper.⁴⁸

The manufacturing sector is also using DLTs to improve effectiveness in the delivery of and payment for goods.⁴⁹ For example, say that a seafood restaurant in Knoxville, Tennessee wants to include fresh Maine lobster on its menu. Lobsters must be shipped overnight under specific conditions and held at a particular temperature to ensure the lobsters survive the journey from Maine and make it into the restaurant’s tank

use of the term “DLT” may be a “response to the extreme hype around ‘blockchain technology,’ in an attempt to sound more restrained and controlled”).

44. Brent Xu, *Blockchain vs. Distributed Ledger Technologies*, CONSENSYS, <https://media.consensys.net/blockchain-vs-distributed-ledger-technologies-1e0289a87b16> (last visited Nov. 19, 2018).

45. Campbell-Verduyn & Goguen, *supra* note 43, at 5.

46. Nakamoto, *supra* note 25, at 1; see also Adam Krellenstein, *Distributed Ledgers, Not Tokens, Are the True Heirs to Satoshi’s Vision*, COINDESK (Oct. 23, 2018), <https://www.coindesk.com/distributed-ledgers-not-tokens-are-the-true-heirs-to-satoshis-vision/>.

47. *Blockchains & Distributed Ledger Technologies*, BLOCKCHAINHUB, <https://blockchainhub.net/blockchains-and-distributed-ledger-technologies-in-general/> (last visited Nov. 19, 2018).

48. See, e.g., *The Economist: The Revolution Beyond Bitcoin*, DIGITAL ASSET (Nov. 6, 2016), <https://hub.digitalasset.com/news/the-economist-the-revolution-beyond-bitcoin>. Paul Vigna, *The Newest Bank Blockchain: Will This Be the Breakthrough?*, WALL STREET J. (Feb. 28, 2017), <https://www.wsj.com/articles/the-newest-bank-blockchain-will-this-be-the-breakthrough-1488285211>.

49. Eddie van der Walt, *Blockchain Tech Coming to Commodity Markets, Blythe Masters Says*, BLOOMBERG (Oct. 9, 2018), <https://www.bloomberg.com/news/articles/2018-10-09/blockchain-tech-coming-to-commodity-markets-masters-tells-lme> (stating that there are “tens if not hundreds” of projects underway to improve “notoriously complex and inefficient” supply chains).

in East Tennessee. There might be manual checkpoints at the point of origin and along the journey to ensure that the lobsters are being shipped under the right conditions. Under the default rules of Article 2 of the Uniform Commercial Code (U.C.C.),⁵⁰ an employee at the seafood restaurant will need to inspect all of the lobsters within a reasonable time (essentially upon delivery for a perishable good such as this) to determine whether to reject each shipment in whole or in part. If the restaurant does not reject any nonconforming (namely dead or spoiled) lobsters quickly, it is bound to pay for them.⁵¹ The supply chain is labor intensive, inefficient, and ripe for human error, even for this simple example.

Now envision a supply chain that incorporates DLT. Instead of the traditional acceptance or rejection under the U.C.C., the Knoxville seafood restaurant and the Maine lobster supplier negotiate terms in advance to cover all future shipments of lobster. These terms require certain conditions to be met along the supply chain—that the shipment takes less than twenty-four hours, the lobsters are held in water below a certain temperature for the entire voyage, etc. Each of these conditions is monitored not by a human inspector, but by electronic sensors that measure the data points and record them onto an immutable network. If all of the preset conditions, each of which has been pre-scripted by coders onto the DLT being used by the business, are met, then the contract will automatically execute upon final delivery, with no human inspection of the goods necessary. In this second hypothetical, the seafood restaurant and lobster supplier have used DLT to enter into a so-called “smart contract.” One can see from this example that DLT has the potential to disrupt not only the industries in which it is employed, but also the traditional legal framework surrounding such industries.⁵² Regulators must be careful not to stifle innovation by being bound to regulatory models that may or may not have relevance to DLT applications.⁵³

50. U.C.C. § 2-102 (AM. LAW INST. & UNIF. LAW COMM’N 2012).

51. *Id.* § 2-602(1) (“Rejection of goods must be within a reasonable time after their delivery or tender.”); *Id.* § 2-606(1)(b) (“Acceptance of goods occurs when the buyer . . . fails to make an effective rejection . . . but such acceptance does not occur until the buyer has had a reasonable opportunity to inspect them”).

52. See, e.g., Reyes, *supra* note 31, at 397–99; Carla L. Reyes, *Cryptolaw for Distributed Ledger Technologies: A Jurisprudential Framework*, 58 JURIMETRICS J. 283, 287–88 (2018); see Usha Rodrigues, *Law and the Blockchain*, 104 IOWA L. REV. 679 (2019).

53. CFTC Commissioner Rostin Behnam’s recent remarks reflect this approach. Aditi Hudli, *CFTC Commission Cites CryptoKitties, Dogecoin When Talking DLT Uses*, COINDESK (Oct. 26, 2018), <https://www.coindesk.com/cftc-commissioner-highlights-dlt-use-cases-in-speech-to-regulators/>.

C. Crypto-Tokens Used in Initial Coin Offerings

The year 2017 saw cryptocurrencies increasingly used as a means of raising capital for (usually blockchain-related or crypto-related) business ventures through the ICO.⁵⁴ In ICOs, which are somewhat of a hybrid between an initial public offering and a crowdfunding campaign,⁵⁵ promoters create virtual coins or tokens and sell them to investors in return for either fiat currency or cryptocurrency. Investors are told that the tokens later can be exchanged to access the digital platform being built (usually using the Ethereum network), use the software being created, additionally, to obtain some appreciated amount of cryptocurrency. Put another way, “Usually, the offer is that these tokens will provide a way to buy some (unspecified) amount of some (vaguely described) product or service that the company will (maybe) build at some (indeterminate) point in the future.”⁵⁶

ICOs typically start with a white paper describing the business plan and a presale to early investors (often family and friends of the entrepreneur) at a discount.⁵⁷ The presale will often occur through a Simple Agreement for Future Tokens (SAFT).⁵⁸ The SAFT (which derives its name from the Simple Agreement for Future Equity, or SAFE, used in crowdfunding offerings) is then often used in another round of token

54. John Patrick Mullin, *ICOs in 2017: From Two Geeks and a Whitepaper to Professional Fundraising Machines*, FORBES (Dec. 18, 2017), <https://www.forbes.com/sites/outofasia/2017/12/18/icos-in-2017-from-two-geeks-and-a-whitepaper-to-professional-fundraising-machines/#32d04220139e>; Seline Jung, *2017: The Year ICOs Re-drew the World VC Map*, MEDIUM (Jan. 2, 2018), <https://medium.com/tokenreport/top-ico-cities-and-countries-e6f867bf77f6>.

55. Paul Vigna, Shane Shifflett & Caitlin Ostroff, *What Crypto Downturn? ICO Fundraising Surges in 2018*, WALL STREET J. (July 1, 2018), <https://www.wsj.com/articles/what-crypto-downturn-ico-fundraising-surges-in-2018-1530466008>.

56. Gideon Lichfield, *The Problem with ICOs Is That They're Called ICOs*, MIT TECH. REV. (Apr. 23, 2018), <https://www.technologyreview.com/s/610764/the-problem-with-icos-is-that-theyre-called-icos/>.

57. Some of the information in this section was gathered from a presentation on “Initial Coin Offerings” by John Wagster, Co-Chair of the Blockchain and Cryptocurrency Practice at Frost Brown Todd, LLP, at the Tennessee Bar Association Business Law Section’s Annual CLE Forum, held in Nashville, Tennessee on May 3, 2018 (on file with Author).

58. See The SAFT Project, a website that bills itself as “a forum for the discussion of a compliant framework for token sales” with a goal “[t]o develop an industry standard that protects the interests of network creators, investors, and users.” THE SAFT PROJECT, <https://saftproject.com/> (last visited Nov. 19, 2018). See also Lukas Schor, *Explaining the “Simple Agreement for Future Tokens” Framework*, MEDIUM (NOV. 29, 2017), <https://medium.com/@argongroup/explaining-the-simple-agreement-for-future-tokens-framework-15d5e7543323>.

presales at a lesser discount to accredited investors.⁵⁹ This process has been designed to comply with the federal and state securities laws in the absence of clear guidance from regulators. Of course, this assumes that the entrepreneurs offering the tokens have an interest in complying with the securities laws. That is not always the case.

There is no doubt that the ICO market went through a period of irrational exuberance in the first eighteen months of the Trump Administration. Over \$5.6 billion was raised in the ICO market in 2017; that figure was exceeded in the first quarter of 2018 alone.⁶⁰ The ICO market settled down somewhat beginning in the second quarter of 2018; however, the largest ICO in history, a token sale for EOS that lasted a year, was completed in June 2018.⁶¹ It created the fifth-largest cryptocurrency and raised over \$4 billion without even providing any clear guidance to investors on what the final product would be.⁶² One reason for the cooling of the crypto-token market might be the statements from regulators and initial actions from regulatory agencies that are discussed further in Part II.

In summary, any regulatory efforts must not only differentiate between these different streams in the crypto-world, but also recall the origins of and purpose of Bitcoin, the original cryptocurrency: a decentralized network that could work across borders and without government interference. Many in the cryptocurrency community continue to hold to these basic principles and stand firm against any regulation by government entities. Others, however, seeking to bring cryptocurrencies and particularly the ICO market into the mainstream, understand that regulation makes the market more predictable for both entrepreneurs and investors. Although there remains a range of opinions on the issue, the answer is no longer whether regulation will occur, but the level to which federal and state agencies will regulate the crypto-markets.

59. Jenny E. Cieplak & Conner Griffith, *Cryptocurrency and Initial Coin Offerings: Despite a Plethora of Regulators, Gaps Remain*, 37(4) BANKING & FIN. SERVS. POL'Y REP. 1 (2018).

60. Jonnie Emsley, *ICO Contributions in 2018 Already Surpass the \$5.6 Billion Raised in 2017*, CRYPTOSLATE (Apr. 20, 2018), <https://cryptoslate.com/ico-contributions-in-2018-already-surpass-2017/>; David Floyd, *\$6.3 Billion: 2018 ICO Funding Has Passed 2017's Total*, COINDESK (Apr. 19, 2018), <https://www.coindesk.com/6-3-billion-2018-ico-funding-already-outpaced-2017/>.

61. William Suberg, *EOS About to Secure a Record \$4 Bln in Year-long ICO*, COIN TELEGRAPH (June 1, 2018), <https://cointelegraph.com/news/eos-about-to-secure-a-record-4-bln-in-year-long-ico>.

62. Kate Rooney, *A Blockchain Start-up Just Raised \$4 Billion Without a Live Product*, CNBC (May 31, 2018), <https://www.cnbc.com/2018/05/31/a-blockchain-start-up-just-raised-4-billion-without-a-live-product.html>.

II. REGULATORY RESPONSE TO THE CRYPTO-MARKETS

A. *Securities & Exchange Commission (SEC)*

The “\$64,000 question”⁶³ for crypto-enthusiasts has been whether the SEC will define cryptocurrencies as securities and regulate them as such. The answer has been mixed: the SEC has shied away from virtual currencies themselves but has begun to actively regulate the ICO markets.

Securities are, of course, subject to registration and disclosure requirements under both the Securities Act of 1933 (“33 Act”)⁶⁴ and the Securities and Exchange Act of 1934 (“34 Act”).⁶⁵ Those acts, however, contain broad definitions of the term “security.”⁶⁶ Whether a particular investment product constitutes a security is defined by the well-worn test for an “investment contract” from *SEC v. W.J. Howey Co.*⁶⁷: “[A] contract, 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.”⁶⁸ Each of the four distinct components of the *Howey* test—(1) an investment of money; (2) in a common enterprise; (3) with an expectation of profits; (4) derived solely from the efforts of others—must be met in order for a particular investment product to be deemed a security, and the test has continued to be refined over the years for application to even “the most unorthodox transactions.”⁶⁹ As discussed below, the public statements made by SEC commissioners and other SEC members, as well as actions brought by the SEC’s Enforcement Division, all indicate that the SEC considers the tokens

63. Originating from a popular 1950s television quiz show, “[s]omething referred to as the \$64,000 question is usually an important issue whose outcome can’t be foreseen and on which much hinges.” *The \$64,000 Question*, GRAMMARIST, <https://grammarist.com/usage/the-64000-question/> (last visited Nov. 19, 2018).

64. Pub. L. No. 73-22, 48 Stat. 74 (codified at 15 U.S.C. §§ 77a to 77aa (2018)).

65. Pub. L. No. 73-291, 48 Stat. 881 (codified at 15 U.S.C. §§ 78a to 78qq (2018)).

66. In fact, the Supreme Court of the United States stated that the statutory definition of the term “security” “embodies a flexible rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits.” *SEC v. W.J. Howey Co.*, 328 U.S. 293, 299 (1946); see also Miriam R. Albert, *The Howey Test Turns 64: Are the Courts Grading This Test on a Curve?*, 2 WM. & MARY BUS. L. REV. 1, 5 (2011).

67. 328 U.S. 293 (1946).

68. *Id.* at 298–99.

69. Note, Kyle M. Globerman, *The Elusive and Changing Definition of a Security: One Test Fits All*, 51 FLA. L. REV. 271, 285 (1999). The securities offered in *Howey* were themselves somewhat “unorthodox”—interests in orange groves cultivated by the defendants in Lake County, Florida. *Howey*, 328 U.S. at 295.

used to fund crypto-related businesses to be securities under the *Howey* test.

1. Public Statements

President Trump appointed Jay Clayton, a partner at Sullivan and Cromwell, as his SEC Chairman, and Chairman Clayton was sworn in on May 4, 2017.⁷⁰ Two months after his confirmation, Chairman Clayton set forth several principles that would guide his chairmanship at the SEC.⁷¹ These included a focus on “the long-term interests of the Main Street investor”; an acknowledgement that the SEC must evolve along with the markets; and the importance of coordination among regulatory agencies.⁷² Chairman Clayton’s public statements regarding cryptocurrencies and ICOs have been consistent with these guiding principles. For example, he directed a public statement to both “Main Street” investors and market professionals on December 11, 2017.⁷³ The statement to “Main Street” investors clarified that the cryptocurrency and ICO markets enjoy “substantially less investor protection than in our traditional securities markets, with correspondingly greater opportunities for fraud and manipulation.”⁷⁴ It furthermore explained that “no initial coin offerings have been registered with the SEC” and that “[t]he SEC also has not to date approved for listing and trading any exchange-traded products (such as ETFs) holding cryptocurrencies or other assets related to cryptocurrencies.”⁷⁵ This illustrates a desire to protect investors from bad actors in the crypto-markets and is in harmony with the central question: “[W]hat can the Commission do to cultivate markets where Mr. and Ms. 401(k) are able to invest in a better future?”⁷⁶

At the same time, in his statement to market professionals, Chairman Clayton made clear that any such professionals who engage in initial coin offerings under the assumption that the virtual coin tokens being offered are not securities do so at their own risk. “[R]eplacing a traditional

70. Reuters, *Wall Street Lawyer Jay Clayton Confirmed as Trump’s SEC Chair*, FORTUNE (May 3, 2017), <http://fortune.com/2017/05/03/jay-clayton-wall-street-sec/>.

71. Jay Clayton, Chairman, Sec. & Exch. Comm’n, Remarks at the Economic Club of New York (July 12, 2017), <https://www.sec.gov/news/speech/remarks-economic-club-new-york>.

72. *Id.*

73. Jay Clayton, Chairman, Sec. & Exch. Comm’n, Statement on Cryptocurrencies and Initial Coin Offerings (Dec. 11, 2017), <https://www.sec.gov/news/public-statement/statement-clayton-2017-12-11>.

74. *Id.*

75. *Id.*

76. Clayton, *supra* note 71.

corporate interest recorded in a central ledger with an enterprise interest recorded through a blockchain entry on a distributed ledger may change the form of the transaction,” stated Chairman Clayton, “but it does not change the substance.”⁷⁷ Furthermore, “Merely calling a token a ‘utility’ token or structuring it to provide some utility does not prevent the token from being a security.”⁷⁸

Chairman Clayton’s subsequent February 2018 testimony in front of the Senate Banking Committee reiterated his December 2017 statements to “Main Street” investors and market professionals and struck a tone that was similarly optimistic, yet tempered with caution for the “Main Street” investor:

I am very optimistic that developments in financial technology will help facilitate capital formation, providing promising investment opportunities for institutional and Main Street investors alike At the same time, regardless of the promise of this technology, those who invest their hard-earned money in opportunities that fall within the scope of the federal securities laws deserve the full protections afforded under those laws. This ever-present need comes into focus when enthusiasm for obtaining a profitable piece of a new technology “before it’s too late” is strong and broad. Fraudsters and other bad actors prey on this enthusiasm.⁷⁹

Finally, the Director of the SEC’s Division of Corporate Finance, William Hinman, directly addressed the applicability of the *Howey* test to cryptocurrencies in a June 2018 speech.⁸⁰ Hinman observed that “in many cases, the economic substance” of an initial coin offering “is the same as a conventional securities offering. Funds are raised with the expectation that the promoters will build their system and investors can

77. Clayton, *supra* note 73.

78. *Id.*

79. Jay Clayton, Chairman, Sec. & Exch. Comm’n, Testimony on Virtual Currencies: The Roles of the SEC and CFTC (Feb. 6, 2018), <https://www.sec.gov/news/testimony/testimony-virtual-currencies-oversight-role-us-securities-and-exchange-commission>; *see also* Jay Clayton & J. Christopher Giancarlo, *Regulators are Looking at Cryptocurrency*, WALL STREET J. (Jan. 24, 2018), <https://www.wsj.com/articles/regulators-are-looking-at-cryptocurrency-1516836363> (“The SEC does not have direct oversight of transactions in currencies or commodities. Yet some products that are labeled cryptocurrencies have characteristics that make them securities. The offer, sale and trading of such products must be carried out in compliance with securities law. The SEC will vigorously pursue those who seek to evade the registration, disclosure and antifraud requirements of our securities laws.”).

80. William Hinman, Dir., Div. of Corp. Fin., Remarks at the Yahoo Finance All Markets Summit: Crypto (June 14, 2018), <https://www.sec.gov/news/speech/speech-hinman-061418>.

earn a return on the instrument.”⁸¹ Comparing ICOs to the facts in *Howey*, Hinman noted that in a typical ICO,

tokens and coins are often touted as assets that have a use in their own right, coupled with a promise that the assets will be cultivated in a way that will cause them to grow in value, to be sold later at a profit. And, as in *Howey* . . . tokens and coins typically are sold to a wide audience rather than to persons who are likely to use them on the network.⁸²

The tokens sold in ICOs are not in and of themselves securities, any more than the orange groves that were sold in *Howey* or a house that is sold for use as a residence.⁸³ “But under certain circumstances, the same asset”—including a digital asset—“can be offered and sold in a way that causes investors to have a reasonable expectation of profits based on the efforts of others.”⁸⁴ Subsequently, Director Hinman announced the SEC’s intent to release a “plain English instrument” in late 2018 or early 2019 that would draw on his June speech to “help entrepreneurs determine whether their cryptocurrency products are securities.”⁸⁵

The SEC’s public statements have made clear that while virtual currencies themselves are not securities, the sale of tokens in the ICO market may very well be securities. The agency’s enforcement actions against certain actors in the crypto-asset markets have backed up these public statements.

2. The DAO Decision

In his December 2017 public statement, Chairman Clayton urged market professionals who were either working in or considering entering the ICO market to familiarize themselves with a Section 21(a) report⁸⁶ the Commission released in July 2017.⁸⁷ That report determined that a German Decentralized Automated Organization (DAO) had violated the

81. *Id.*

82. *Id.*

83. *Id.*

84. *Id.*

85. Andrew Ramonas, *SEC Plans ‘Plain English’ Crypto Securities Guide*, BLOOMBERG L. (Nov. 5, 2018), <https://www.bloomberglaw.com/document/X4GOPF 20000000>.

86. Section 21(a) of the ‘34 Act authorizes the SEC “to investigate violations of the federal securities laws and, in its discretion, to ‘publish information concerning any such violations.’” U.S. Sec. & Exch. Comm’n, Report of Investigation Pursuant to Section 21(a) of The Securities Exchange Act of 1934: The DAO, Exchange Act Release No. 81207 (July 25, 2017) [hereinafter *The DAO Report*], <https://www.sec.gov/litigation/investreport/34-81207.pdf>.

87. Clayton, *supra* note 73.

federal securities laws by selling tokens (the DAO Tokens) to raise capital for “projects” without registering those tokens as securities.⁸⁸ The DAO in question, Slock.it, sold approximately 1.15 billion DAO Tokens in May 2016 in exchange for a total of approximately 12 million Ether, and had a market valuation of approximately \$150 million at the close of the offering.⁸⁹ The purpose of the offering was to raise funds to support the DAO’s business, which was to develop smart contract technology on Ethereum to assist with corporate governance activities.⁹⁰ A secondary market emerged on which DAO Tokens were traded for both virtual and fiat currencies.⁹¹ Unfortunately, there was a security breach, and a number of the participants’ DAO tokens were stolen, until the DAO’s managers executed a “hard fork”⁹² in the Ethereum blockchain that allowed participants to exchange their DAO tokens for Ether at an alternative address.⁹³ The SEC’s Enforcement Division undertook an investigation.

The Commission determined that the DAO Tokens met the *Howey* test and, therefore, were properly classified as securities. The participants in the offering invested virtual currency—Ether—in purchasing the DAO Tokens.⁹⁴ The objective of the DAO “was to fund projects in exchange for a return on investment”—namely, profit-sharing on contracts entered into by the DAO.⁹⁵ Finally, the investors “relied on the managerial and entrepreneurial efforts” of the DAO’s co-founders and managers to operate the DAO “and put forth project proposals that could generate profits for [its] investors,” while the investors’ own voting rights were limited.⁹⁶ Meeting the *Howey* test, the DAO tokens were securities, and thus the entrepreneurs were issuers who were required to register the offer and sale of the DAO Tokens, absent a valid exemption.⁹⁷ The

88. *The DAO Report*, *supra* note 86, at 13.

89. *Id.* at 2.

90. *Id.*

91. *Id.* at 5–6.

92. A “hard fork” is defined as “a permanent divergence in the block chain.” *Hard Fork, Hard-Forking Change*, BITCOIN, <https://bitcoin.org/en/developer-glossary> (last visited Nov. 20, 2018). This “hard fork” restored the Ethereum protocol and allowed investors to recover their DAO tokens as though they had never been lost. *The DAO Report*, *supra* note 86, at 6.

93. *The DAO Report*, *supra* note 86, at 6.

94. *Id.* at 8 (citing *Uselton v. Comm. Lovelace Motor Freight, Inc.*, 940 F.2d 564, 574 (10th Cir. 1991) (“[I]n spite of *Howey*’s reference to an ‘investment of money,’ it is well established that cash is not the only form of contribution or investment that will create an investment contract.”)).

95. *Id.* at 9.

96. *Id.* at 9–10.

97. *Id.* at 13.

Commission made clear, however, that its decision in *The DAO Report* did not apply to all ICOs: “Whether or not a particular transaction involves the offer and sale of a security—regardless of the terminology used—will depend on the facts and circumstances, including the economic realities of the transaction.”⁹⁸

3. *Zaslavskiy* and Other SEC Enforcement Actions

A September 11, 2018 decision by a federal judge in the Eastern District of New York—the first federal court to decide whether crypto-tokens are securities—was consistent with *The DAO Report*.⁹⁹ The defendant was the sole owner of two fledgling businesses that participated in ICOs: ReCOIN, which “was purportedly engaged in real estate investment and development of real estate-related ‘smart contracts,’” and Diamond, which “prportedly invested in diamonds and obtained discounts from diamond retailers for Diamond members.”¹⁰⁰ The defendant made numerous false statements in conjunction with the ICO, including that ReCOIN “was backed by domestic and international real estate investments” and was led by “an experienced team of brokers, lawyers, and developers,” and that Diamond was “a virtual ecosystem that offered ‘cryptocurrency’ tokens hedged with ‘real world assets’—this time, diamonds.”¹⁰¹ Investors in ReCOIN and Diamond who were lured in by these false statements never received tokens in return for their investment; indeed, the coins were never even developed.¹⁰² In bringing an enforcement action against Zaslavskiy, therefore, the SEC appeared to be targeting a truly bad actor who had no intent of fulfilling his obligations to his investors.

The court determined that the question of whether a particular financial instrument meets the *Howey* test for a security is a question of fact best left for the jury.¹⁰³ However, the government’s indictment was constitutionally sufficient because a reasonable jury could find that the coins offered by Zaslavskiy were securities.¹⁰⁴ First, “investors gave up money—or other assets—in exchange for ‘membership’” in the new ventures.¹⁰⁵ Second, this was a common enterprise because investors’

98. *Id.* at 14.

99. *United States v. Zaslavskiy*, No. 17CR647(RJD), 2018 U.S. Dist. LEXIS 156574 (E.D.N.Y. Sept. 11, 2018).

100. *Id.* at *2.

101. *Id.*

102. *Id.*

103. *Id.* at *7.

104. *Id.*

105. *Id.* at *5.

funds were to be pooled to purchase “real world assets” (namely, real estate and diamonds) and the investors were promised tokens proportionate to the level of their investments.¹⁰⁶ Third, investors would have reasonably expected their profits from the venture to be derived from the efforts of Zaslavskiy and his associates.¹⁰⁷ In so holding, the court rejected the argument of Zaslavskiy “that the virtual currencies promoted in the REcoin and Diamond ICOs are ‘currencies,’ and therefore, by definition, not securities.”¹⁰⁸ Importantly, not only were no diamonds or real estate ever purchased, but also no crypto-coins or tokens ever developed.¹⁰⁹ “[S]imply labeling an investment opportunity as ‘virtual currency’ or ‘cryptocurrency’ does not transform an investment contract—a security—into a currency.”¹¹⁰

Other recent enforcement actions by the SEC have further honed the margins of the ICO market. In August 2018, the SEC filed an order settling an enforcement action against an oil and gas exploration company and its founder.¹¹¹ After a failed ICO, Tomahawk wound up giving away 80,000 tokens to entities that helped promote the coin offering (a so-called “air drop”).¹¹² The recipients later traded tokens they had received from Tomahawk for free on a digital-asset exchange for other cryptocurrencies or tokens.¹¹³ Despite the fact that Tomahawk gave the tokens away, the SEC held that they still constituted an “offer” of securities.¹¹⁴ “[A] ‘gift’ of a security is a ‘sale’ within the meaning of the [law] when the donor receives some real benefit.”¹¹⁵ Even though the

106. *Id.* at *6.

107. *Id.* at *6–7.

108. *Id.* at *7 (quoting 15 U.S.C. § 78c(a)(10) (2012) (a “security does not include ‘currency or any note, draft, bill of exchange, or banker’s acceptance, which has a maturity at the time of issuance of not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited’”).

109. *Id.*

110. *Id.*

111. *In re Tomahawk Exploration LLC*, Securities Act Release No. 10530, Exchange Act Release No. 83839 (Aug. 14, 2018) [hereinafter *Tomahawk*], <https://www.sec.gov/litigation/admin/2018/33-10530.pdf> (order instituting administrative and cease-and-desist proceedings); see also Dave Michaels, *Even Free Tokens Face Regulatory Heat as Coin Offerings Scrutinized*, WALL STREET J. (Aug. 14, 2018), <https://www.wsj.com/articles/even-free-tokens-face-regulatory-heat-as-coin-offerings-scrutinized-1534273134>; Brady Dale, *So Long ICOs, Hello Airdrops: The Free Token Giveaway Craze Is Here*, COINDESK (Mar. 16, 2018), <https://www.coindesk.com/long-icos-hello-airdrops-free-token-giveaway-craze/>.

112. *Tomahawk*, *supra* note 111, at 2.

113. *Id.* at 3.

114. *Id.* at 7.

115. *Id.*

tokens were free, they constituted a real benefit because they were convertible, without consideration, into equity shares of the company.¹¹⁶

The SEC has brought enforcement actions in 2018 not only against entities offering ICOs, but also trading platforms on which ICOs took place. In March 2018, the SEC Divisions of Enforcement and Trading and Markets issued a joint statement directed at online trading platforms emphasizing that if the digital assets being traded are securities, online trading platforms may trigger a variety of registration requirements under the federal securities laws, including registration as a national securities exchange, broker–dealer, transfer agent, or clearing agency, unless an exemption applies.¹¹⁷ The SEC followed up on September 11, 2018, the same day the *Zaslavskiy* decision was released, announcing that the “ICO Superstore” TokenLot, LLC operated as an unregistered broker–dealer in violation of the federal securities laws.¹¹⁸ Interestingly, unlike many of the other entities against whom the SEC has initiated enforcement actions, TokenLot was not alleged to have engaged in any fraudulent behavior. Rather, TokenLot and its promoters “advertised and sold securities, in the form of digital tokens, to retail investors” through both ICOs and the secondary trading markets.¹¹⁹ The SEC encouraged individuals engaging in or developing digital asset trading businesses to seek assistance from SEC staff regarding registration requirements or other potentially relevant securities laws.¹²⁰ In November 2018, the SEC settled with the founder of cryptocurrency trading platform EtherDelta for operating an unregistered national securities exchange.¹²¹

116. *Id.*

117. U.S. Sec. & Exch. Comm’n, Divs. of Enf’t & Trading and Mkts., Statement on Potentially Unlawful Online Platforms for Trading Digital Assets (Mar. 7, 2018), <https://www.sec.gov/news/public-statement/enforcement-tm-statement-potentially-unlawful-online-platforms-trading>.

118. *In re* TokenLot, LLC, Securities Act Release No. 10543, Exchange Act Release No. 84075, Investment Company Act Release No. 33221 (Sept. 11, 2018), <https://www.sec.gov/litigation/admin/2018/33-10543.pdf> (order instituting administrative and cease-and-desist proceedings).

119. *Id.* at 2.

120. Press Release, *SEC Charges ICO Superstore and Owners with Operating as Unregistered Broker–Dealers*, U.S. SEC. & EXCHANGE COMMISSION (Sept. 11, 2018), <https://www.sec.gov/news/press-release/2018-185>.

121. *In re* Coburn, Exchange Act Release No. 84553 (Nov. 8, 2018), <https://www.sec.gov/litigation/admin/2018/34-84553.pdf> (order instituting cease-and-desist proceedings); see also Jennifer Bennett, *SEC Settles First Unregistered Crypto Securities Exchange Case*, BLOOMBERG L. (Nov. 8, 2018), https://www.bloomberglaw.com/document/XB2K_8228000.

4. Denial of Exchange-Trade Fund (ETF) Licenses

The last area of SEC regulatory activity in 2017 and 2018 with regard to cryptocurrencies has been in the area of exchange-traded funds (ETFs). ETFs are a cousin of mutual funds. They hold assets, such as stocks, bonds, commodities, and currencies, and are traded on exchanges like those products.¹²² An ETF approval by the SEC would open up the volatile cryptocurrency market to pension funds and other institutional investors.

The SEC has raised questions regarding the viability of crypto-based ETFs, particularly due to the difficulty in valuing cryptocurrencies, the ability of virtual currencies to comply with the SEC's fund liquidity rule, and the potential for market manipulation.¹²³ To date, these unanswered questions have led the agency to continue to deny applications for licenses for crypto-based ETFs.¹²⁴ As of this writing, the SEC is accepting comments on an application for a Bitcoin-based fund, and seeks comments from third parties particularly with regard to market manipulation and surveillance.¹²⁵ The ongoing notice-and-comment period means the SEC is unlikely to approve any crypto-based ETFs until early 2019 at the soonest.¹²⁶

B. Commodity Futures Trading Commission (CFTC)

The other federal agency taking a leading role in cryptocurrency regulation is the CFTC. The mission of the CFTC is to "foster open, transparent, competitive, and financially sound" derivatives markets and protect investors in those markets from fraud, manipulation, and

122. *Exchange-Traded Fund (ETF)*, INVESTOPEDIA, <https://www.investopedia.com/terms/e/etf.asp> (last visited Nov. 16, 2018).

123. Letter from Dalia Blass, Dir. of Div. of Inv. Mgmt., U.S. Sec. & Exch. Comm'n, to Paul Schott Stevens, President & CEO, Inv. Co. Inst., & Timothy W. Cameron, Asset Mgmt. Grp. Head (Jan. 18, 2018), <https://www.sec.gov/divisions/investment/noaction/2018/cryptocurrency-011818.htm>; see also Kate Rooney, *BlackRock Won't Offer a Cryptocurrency ETF Until the Industry Is 'Legitimate,' CEO Larry Fink Says*, CNBC (Nov. 1, 2018), <https://www.cnbc.com/2018/11/01/blackrock-wont-offer-a-cryptocurrency-etf-until-its-legitimate.html>.

124. Rachel Evans & Lily Katz, *Bitcoin ETFs Won't Be Coming Any Time Soon Thanks to the SEC*, BLOOMBERG L. (Aug. 27, 2018), <https://www.bloomberglaw.com/document/X1R4FVU4000000>.

125. Rachel Evans, *Bitcoin ETFs Delayed Again as SEC Seeks Comment on Fund Plan*, BLOOMBERG L. (Sept. 24, 2018), <https://www.bloomberglaw.com/document/X9M0NQI0000000>.

126. *Id.*; see also Christine Kim, *Wealth Manager Canaccord: Bitcoin ETF Approval More Likely in 2019*, COINDESK (Aug. 6, 2018), <https://www.coindesk.com/wealth-manager-canaccord-bitcoin-etf-approval-more-likely-in-2019/>.

abuse.¹²⁷ The CFTC derives its regulatory authority from the Commodity Exchange Act (CEA)¹²⁸ and was established as an independent agency in 1974.¹²⁹

In 2015, the CFTC determined, with no accompanying analysis, that virtual currencies met the definition of “commodity” under the CEA.¹³⁰ Because the CFTC treats cryptocurrencies as a commodity, it has taken the position that it has the authority to regulate markets offering cryptocurrency derivatives products, just as it has the ability to oversee markets trading in futures contracts pertaining to more traditional commodities like oil, gas, and minerals.¹³¹ In the 2016 *Bitfinex*¹³² decision, the CFTC took action against a Bitcoin futures exchange operating in the U.S. that failed to register with the agency.¹³³ The CFTC’s regulatory authority over derivatives on virtual currencies also allowed for the establishment of the first regulated Bitcoin futures market in December 2017 on two Chicago-based derivatives exchanges.¹³⁴

In contrast to the futures markets, however, the CFTC does not have regulatory jurisdiction under the CEA over markets or platforms conducting cash or “spot” transactions in virtual currencies or over participants on such platforms.¹³⁵ The CFTC simply does not have statutory authority over cash commodity markets; it would require a legislative amendment to the CEA to confer such authority upon it.¹³⁶

127. *Mission & Responsibility*, U.S. COMMODITY FUTURES TRADING COMMISSION, <https://www.cftc.gov/About/MissionResponsibilities/index.htm> (last visited Nov. 16, 2018).

128. Pub. L. No. 74-675, 49 Stat. 1491 (1936) (codified at 7 U.S.C. § 1 (2018)).

129. Commodity Futures Trading Commission Act of 1974, Pub. L. No. 93-463, 88 Stat. 1389 (codified at 7 U.S.C. § 2 (2018)).

130. *In re Coinflip, Inc.*, CFTC No. 15-29, 2015 WL 5535736 (Sept. 17, 2015).

131. Indeed, CFTC Chairman Chris Giancarlo testified before Congress that “the CFTC does have both regulatory and enforcement jurisdiction under the CEA over derivatives on virtual currencies traded in the United States.” Written Testimony of J. Christopher Giancarlo, Chairman, Commodity Futures Trading Comm’n, Before the Senate Banking Committee 4 (Feb. 6, 2018), <https://www.banking.senate.gov/imo/media/doc/Giancarlo%20Testimony%202-6-186.pdf>.

132. *In re BFXNA Inc.*, CFTC No. 16-19 (June 2, 2016).

133. *Id.*; see also *CFTC Orders Bitcoin Exchange Bitfinex to Pay \$75,000 for Offering Illegal Off-Exchange Financed Retail Commodity Transactions and Failing to Register as a Futures Commission Merchant*, U.S. COMMODITY FUTURES TRADING COMMISSION (June 2, 2016), <https://www.cftc.gov/PressRoom/PressReleases/pr7380-16>.

134. Written Giancarlo Testimony, *supra* note 131, at 6.

135. *Id.* at 4; see also Rostin Behnam, *Remarks at the BFI Summit: “Fostering Open, Transparent, Competitive, and Financially Sound Markets” United Nations Plaza*, U.S. COMMODITY FUTURES TRADING COMMISSION (June 4, 2018), <https://www.cftc.gov/PressRoom/SpeechesTestimony/opabehnam7>.

136. Written Giancarlo Testimony, *supra* note 131, at 6.

The lack of regulatory jurisdiction over the underlying spot markets has caused some concern among those who otherwise might be interested in offering cryptocurrency-based derivatives products.¹³⁷ The CFTC does “have enforcement jurisdiction to investigate through subpoena and other investigative powers and, as appropriate, conduct civil enforcement action against fraud and manipulation” in both derivatives markets and in underlying spot markets for virtual currencies.¹³⁸

Two recent federal court decisions have shed more light on the CFTC’s regulatory authority over derivative products related to cryptocurrencies. In *CFTC v. McDonnell*,¹³⁹ the defendants defrauded investors in their venture, Coin Drop Markets, which purported to offer trading and investment services related to virtual currency.¹⁴⁰ After receiving payments from their investors, the “defendants deleted their ‘social media accounts’ and ‘websites and ceased communicating with . . . customers.’”¹⁴¹ “When customers asked for a return of their membership fee, or virtual currency investment, the defendants refused and misappropriated the funds.”¹⁴² *McDonnell* is the first federal court decision to agree with the CFTC’s interpretation that it could regulate cryptocurrencies as commodities (“goods’ exchanged in a market for uniform quality and value”).¹⁴³ Whether based upon common usage, because they provide a “store of value,” or because they serve as a type of monetary exchange, the United States District Court for the Eastern District of New York believed it made sense to classify cryptocurrencies as commodities.¹⁴⁴ The court also clarified that the CFTC has the authority to bring suit against defendants scheming to defraud investors in commodity spot markets.¹⁴⁵ Specifically, the court observed that while the “CFTC does not have regulatory authority over simple quick cash or spot transactions that do not involve fraud or manipulation,” it may regulate spot markets, including those for virtual currencies, where

137. NASDAQ CEO Adena Friedman, for example, stated that because the “exchange environment for the actual physical instrument is unregulated[, t]hat creates a different level of risk.” Annie Massa & Matthew Leising, *Cboe Signals Big Plans for Trading Cryptocurrency Derivatives*, BLOOMBERG (Mar. 14, 2018), <https://www.bloomberg.com/news/articles/2018-03-14/cboe-signals-big-plans-for-trading-cryptocurrency-derivatives>.

138. Written Giancarlo Testimony, *supra* note 131, at 4.

139. 287 F. Supp. 3d 213 (E.D.N.Y. 2018).

140. *Id.* at 217.

141. *Id.* at 218.

142. *Id.*

143. *Id.* at 228.

144. *Id.* at 224–25.

145. *Id.* at 227.

“there is evidence of manipulation or fraud.”¹⁴⁶ Because the CFTC made a prima facie showing of fraud by the *McDonnell* defendants, the court allowed the case to proceed.¹⁴⁷

More recently, in *CFTC v. My Big Coin Pay, Inc.*,¹⁴⁸ the defendants enticed customers to buy My Big Coin, a virtual currency, by making blatantly misleading statements, including that the new cryptocurrency was “backed by gold” and could be used anywhere that accepted MasterCard.¹⁴⁹ As there was no futures market for My Big Coin, the defendants argued it was not a commodity and, thus, not subject to the CFTC’s regulation.¹⁵⁰ The United States District Court for the District of Massachusetts agreed with the CFTC’s argument that even though My Big Coin was not the subject of a futures contract, a better-known virtual currency, Bitcoin, was.¹⁵¹ The court held that the definition of commodity under the CEA “is broader than any particular type or brand of that commodity.”¹⁵² By this rationale, an active futures market for one type of virtual currency subjects all of them to CFTC regulation.¹⁵³ *My Big Coin Pay* is the broadest view of the CFTC’s regulatory authority over cryptocurrencies taken by any federal court to date.

C. Other Regulatory Activities

1. Other Federal Regulation

While the SEC and the CFTC have taken on a role as primary regulators of the virtual currency industry, they are also working together with other federal agencies which have established some form of jurisdiction over the crypto-markets. These include

- The *Internal Revenue Service (IRS)*, which treats virtual currencies as property, thus subjecting profitable sales of cryptocurrencies to capital gains tax;¹⁵⁴

146. *Id.*

147. *Id.* at 229–30.

148. 334 F. Supp. 3d 492 (D. Mass. 2018).

149. *Id.* at 494.

150. *Id.* at 496.

151. *Id.* at 496–97.

152. *Id.* at 496.

153. *Id.* at 497–98.

154. *United States v. Coinbase, Inc.*, No. 17-cv-01431-JSC, 2017 U.S. Dist. LEXIS 111756, at *1 (N.D. Cal. July 18, 2017) (“In March 2014, the IRS issued Notice 2014-21, which describes how the IRS applies U.S. tax principles to transactions involving virtual currency. In Notice 2014-21, the IRS stated its position: virtual currencies that can be converted into traditional currency are property for tax purposes, and a taxpayer can have a gain or loss on the sale or exchange of a virtual currency, depending on the taxpayer’s

- The *Office of the Comptroller of the Currency (OCC)*, which recently began accepting applications for national bank charters from non-depository fintech companies engaged in the business of banking;¹⁵⁵
- The *Financial Crimes Enforcement Network (FinCEN)*, which has assessed civil penalties against virtual currency exchanges for violating anti-money laundering laws¹⁵⁶ and anticipates an increased role in regulation of virtual currency businesses under the Bank Secrecy Act;¹⁵⁷ and
- The *Consumer Financial Protection Bureau (CFPB)*, which is currently working on a regulatory “sandbox” or fintech banks¹⁵⁸ and has hired the former director of a similar program in Arizona to run it.¹⁵⁹

2. Self-Regulation by the Industry

The Financial Industry Regulatory Authority (FINRA) is an industry organization designed to self-regulate and protect the fairness of the financial markets.¹⁶⁰ FINRA issued a Regulatory Notice in July 2018

cost to purchase the virtual currency.”); *see also* Evan S. Strassberg & Brad R. Jacobsen, *Regulation of the Unregulated: How Bitcoin and Cryptocurrencies Show that the Government can Regulate Anything*, 24-4 WESTLAW J. SEC. LITIG. & REG. 1 (June 21, 2018); Tara Siegel Bernard, *When Trading in Bitcoin, Keep the Taxman in Mind*, N.Y. TIMES (Jan. 18, 2018), <https://www.nytimes.com/2018/01/18/your-money/bitcoin-irs-taxes.html>.

155. *Ex-Comptroller Ludwig Backs Special Fintech Charter*, BLOOMBERG L. (Aug. 13, 2018), <https://www.bloomberglaw.com/document/X5UM03KO000000>; *but see* Lydia Beyoud, *State Regulators File Suit to Block Federal 'Fintech Charter'*, BLOOMBERG L. (AUG. 13, 2018), <https://www.bloomberglaw.com/document/X3O816M K000000>.

156. *Application of FinCEN's Regulations to Persons Administering, Exchanging, or Using Virtual Currencies*, FIN. CRIMES ENFORCEMENT NETWORK (Mar. 18, 2013), <https://www.fincen.gov/resources/statutes-regulations/guidance/application-fincens-regulations-persons-administering>; *see also* Strassberg & Jacobsen, *supra* note 154.

157. Pub. L. No. 91-508, 84 Stat. 1114 (1970); Lydia Beyoud, *FinCEN Hangs Help Wanted Sign for Crypto Enforcement*, BLOOMBERG L. (Sept. 17, 2018), <https://www.bloomberglaw.com/document/X84U7LRG000000>.

158. *BCFP Office of Innovation Proposes "Disclosure Sandbox" for Fintech Companies to Test New Ways to Inform Consumers*, CONSUMER FIN. PROTECTION BUREAU (Sept. 13, 2018), <https://www.consumerfinance.gov/about-us/blog/bcfp-office-innovation-proposes-disclosure-sandbox-fintech-companies-test-new-ways-inform-consumers/>; *see also* Lydia Beyoud, *CFPB Exploring Regulatory Sandbox, Mulvaney Says*, BLOOMBERG L. (June 4, 2018), <https://www.bloomberglaw.com/document/X892KDS4000000>.

159. *Consumer Financial Protection Bureau Announces Director for the Office of Innovation*, CONSUMER FIN. PROTECTION BUREAU (July 18, 2018), <https://www.consumerfinance.gov/about-us/newsroom/bureau-consumer-financial-protection-announces-director-office-innovation/>.

160. *About FINRA*, <http://www.finra.org/about> (last visited Nov. 19, 2018) (“FINRA is not part of the government. We’re a not-for-profit organization authorized by Congress to

requesting that member firms report any current or planned digital asset-related activities.¹⁶¹ Then, in September 2018, FINRA, for the first time, brought a disciplinary action against a member firm.¹⁶² That firm had purchased a majority of the total outstanding amount of the (regretfully named) cryptocurrency HempCoin in exchange for stock in the company and promised to reimburse holders of HempCoins with the common stock of the company.¹⁶³ FINRA determined that, under the *Howey* test, this transformed the digital currency into a security, and that nearly every statement filed with the over-the-counter markets regarding the transaction was false.¹⁶⁴ Thus, the self-regulating agency for the financial markets has taken a similar approach to the government regulators by focusing, at least initially, on fraudulent actors in the cryptocurrency markets.

3. State Regulation

Many states have also undertaken efforts to regulate cryptocurrencies. Some have been enforcement focused, while others have done so with an eye toward attracting crypto-businesses. The most notable is New York, which established in 2015 “BitLicense,” a licensing regime by which any cryptocurrency business seeking to engage in business activity in New York had to abide.¹⁶⁵ By May 2018, only four crypto-businesses had succeeded in obtaining the license; many had left the state.¹⁶⁶ Most recently, New York has allowed virtual currency firms to use the National Multistate Licensing System,¹⁶⁷ a number of other states are

protect America’s investors by making sure the broker–dealer industry operates fairly and honestly.”).

161. *FINRA Encourages Firms to Notify FINRA If They Engage in Activities Related to Digital Assets*, FINRA (July 6, 2018), <http://www.finra.org/industry/notices/18-20> (regulatory notice).

162. *FINRA Charges Broker with Fraud and Unlawful Distribution of Unregistered Cryptocurrency Securities*, FINRA (Sept. 11, 2018), <http://www.finra.org/newsroom/2018/finra-charges-broker-fraud-and-unlawful-distribution-unregistered-cryptocurrency> (news release).

163. *Id.*

164. *Id.*; see also Aisha Al-Muslim, *FINRA Wades into Cryptocurrency Enforcement*, WALL STREET J. (Sept. 11, 2018), <https://www.wsj.com/articles/finra-wades-into-cryptocurrency-enforcement-1536695686>.

165. Trautman & Harrell, *supra* note 30, at 1081–83.

166. Jen Wieczner, *Inside New York’s BitLicense Bottleneck: An ‘Absolute Failure?’*, FORTUNE (May 25, 2018), <http://fortune.com/2018/05/25/bitcoin-cryptocurrency-new-york-bitlicense/>.

167. Evan Weinberger, *N.Y. OKs Virtual Currency Firms to Use Nationwide Licensing Tool*, BLOOMBERG L. (Oct. 1, 2018), <https://www.bloomberglaw.com/document/X3453VLG000000>.

also using this system or exempting virtual currency businesses from licensing requirements altogether.¹⁶⁸ A Uniform Law on the Regulation of Virtual Currency was passed by the Uniform Law Commission in 2017 and has been introduced in three states: Connecticut, Hawaii, and Nebraska.¹⁶⁹ One state, Vermont, has even approved by statute a new business entity, the blockchain-based limited liability company, or “BLLC,” designed to attract blockchain-related businesses.¹⁷⁰ It remains to be seen whether the states will be permitted to be laboratories of innovation in the cryptocurrency regulatory world or whether the federal government, through either legislative or (more likely) regulatory action, will preempt the field.

III. PROSPECTS FOR FURTHER CRYPTO-REGULATION IN THE TRUMP ADMINISTRATION

With the results of the 2018 midterm elections still being finalized, the Trump Administration’s regulation of the financial sector is at a crossroads. With the Democratic takeover of the House of Representatives, any further legislation to repeal portions of Dodd-Frank is unlikely.¹⁷¹ However, the work of the executive branch to continue to trim back what it deems to be burdensome regulations will likely continue at agencies such as the Treasury Department and the Consumer Financial Protection Bureau. One issue for the administration to consider is whether the regulation of cryptocurrencies, DLT-related technologies, and the once-overheating but now-simmering crypto-token market should continue down their current path.

Thus far, the Trump Administration’s regulatory efforts in this arena have generally taken an appropriate tenor. The SEC and CFTC are

168. Lydia Beyoud, *Colorado Exempts Some Crypto Exchanges from Licensing Rules*, BLOOMBERG L. (Sept. 24, 2018), <https://www.bloomberglaw.com/document/XD8J7QV800000>.

169. *Virtual-Currency Businesses Act*, Regulation of, UNIF. L. COMM’N, <https://my.Uniformlaws.org/committees/community-home?CommunityKey-e104aaa8-c1of-45a7-a34a-0423c2106778>.

170. Michaela Ross, *Cannabis, Crypto Startups Eye Vermont’s Blockchain LLC Class*, BLOOMBERG L. (July 9, 2018), <https://www.bloomberglaw.com/document/XFLHJUGC000000>.

171. Indeed, the likely new Chair of the House Financial Services Committee, favorite Trump target Maxine Waters (D-CA), could not be more ideologically opposed to the previous chair, Jeb Hensarling (R-TX). Congresswoman Waters “has opposed Republican-led efforts to roll back the Dodd-Frank financial reform law and is promising colleagues that she will prioritize protecting consumers from abusive financial practices.” *Here are the House Democrats Who Will Soon Be Running the Show*, CBS NEWS (Nov. 11, 2018), <https://www.cbsnews.com/news/here-are-the-house-democrats-who-will-soon-be-running-the-show/>.

regulating different sectors of the cryptocurrency markets, with the SEC focused on ICOs and crypto-tokens and the CFTC focused on virtual currency derivative markets and fraud and deception in the cryptocurrency spot markets. However, a similar pattern between the two agencies' regulatory approaches has emerged: focus on the worst actors and gradually regulate at the margins, make public statements to both reassure Main Street investors and provide guidance (and sometimes warnings) to financial professionals who are involved in the crypto-markets, and set the stage for cooperation among agencies in future regulatory activities. Both agencies clearly see the potential upside in the crypto-markets and thus want to avoid stunting growth and investment in those markets through overregulation.¹⁷² This measured approach seems likely to continue with the SEC's appointment of long-time regulator Valerie Szczepanik as the agency's senior advisor for digital assets, or "crypto-czar."¹⁷³ Ms. Szczepanik's emphasis appears to be on fostering communication with individuals and entities working with digital assets and taking a proactive approach of preparing crypto-products for registration, rather than relying simply on enforcement.¹⁷⁴ The SEC and CFTC will also likely continue to increase their efforts at educating investors on cryptocurrencies and crypto-assets, as illustrated by products such as "Howeycoins," the SEC's website modeling an ICO that leads potential investors to an informational webpage,¹⁷⁵ and the CFTC's "Primer on Virtual Currencies."¹⁷⁶

Recently, Congress has shown some desire to get involved and not simply cede regulatory ground to the agencies. Prior to the midterm

172. "Cryptocurrency has extraordinary upside if a regulatory and taxation system is correctly designed—but a tremendous downside if a system is poorly designed. Like all things, it is less likely to be used if it is prohibitively cumbersome to comply with regulatory and tax requirements." Sami Ahmed, *Cryptocurrency and Robots: How to Tax and Pay Tax on Them*, 69 S.C. L. REV. 697, 704 (2018).

173. Ben Bain & Matt Robinson, *SEC's New Crypto Czar Wants Coin Industry to Step out of Shadows*, BLOOMBERG L. (Aug. 6, 2018), <https://www.bloomberglaw.com/document/XF7NM6PO000000>.

174. *Id.*; see also Jeff John Roberts, *SEC's 'Crypto Czar' Says Smart Contracts Can Help Regulation*, FORTUNE (June 7, 2018), <http://fortune.com/2018/06/07/valerie-szczepanik-sec/> ("We never turn down a request for a meeting. We've met dozens and dozens of entrepreneurs and lawyers. We're not going to do the innovating for people. But we want people to come in and propose solutions they want to accomplish.")

175. HOWEY COINS, <https://www.howeycoins.com/index.html> (last visited Nov. 19, 2018).

176. See generally LABCFTC, A CFTC PRIMER ON VIRTUAL CURRENCIES (2017), https://www.cftc.gov/sites/default/files/idc/groups/public/documents/file/labcftc_primercurrencies100417.pdf.

elections, members of the House were working on legislation that would preempt state licensing of cryptocurrency.¹⁷⁷ In September 2018, the Congressional Blockchain Caucus asked the SEC to issue formal guidance regarding when crypto-assets should be treated as securities.¹⁷⁸ Congress's concern is that a lack of clarity in the regulatory regime in the United States—or simply too much or too little regulation—will cause crypto-businesses to flee overseas and set up shop there. Anyone seeking a quick fortune would be better off investing in the ICO market than betting on Congress to act in a bipartisan, proactive manner, particularly in this new era of divided government in Washington. Thus, most of the regulatory action likely will remain with the agencies traditionally charged with overseeing the financial markets.

Cryptocurrencies originated out of a desire to harness the power of technology to circumvent the governments and central banks that have been controlling the money supply for so long. Their regulation has, therefore, naturally met with some resistance, but also with open arms from some in the industry who believe that maturity of the crypto-markets will only truly come with regulatory certainty. The collective decision of the Trump Administration's regulators to take a patient, measured approach to these new technologies—characteristics for which their boss is not exactly known—should continue to serve the industry well.

177. Lydia Beyoud, *House Lawmakers Plan Bill to Preempt State Crypto Regulation*, BLOOMBERG L. (Sept. 25, 2018), <https://www.bloomberglaw.com/document/X2T6T9PS000000>.

178. Lydia Beyoud, *Blockchain Caucus Lawmakers Ask SEC for Crypto Clarity*, BLOOMBERG L. (Sept. 28, 2018), <https://www.bloomberglaw.com/document/X2O9FPMS000000>; see also Kate Rooney, *Congress Members Ask SEC Chairman for Clarity on Cryptocurrency Regulation*, CNBC (Sept. 28, 2018), <https://www.cnbc.com/2018/09/28/congress-ask-sec-chairman-for-clarity-on-cryptocurrency-regulation.html>.

