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FinTech University
White Collar Issues in Cryptocurrency and Digital Assets

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June 14, 2022

Summary



- The DOJ, SEC, State Attorneys General, CFTC, OFAC and other agencies have all targeted the FinTech industry in recent years.
- The purpose of this presentation is to provide a general overview of the enforcement landscape of the FinTech industry, where it might be headed, and what companies/individuals can do to try to avoid problems down the line.



Relevant Laws



Securities Laws

- Securities Act of 1933 (the “Securities Act”)
 - Section 2(a)(1) of the Securities Act defines a “security”
 - Section 5 provides that all issuers must register securities with the SEC unless an exemption applies
 - Section 6 lays out the registration process
- Securities Exchange Act of 1934 (the “Exchange Act”)
 - Section 3(a)(10) defines “security” in a nearly identical manner
 - Primarily regulates the secondary trading of securities
 - Extends the Securities Act’s disclosure requirement to secondary trading and requires issuers to regularly file company information with the SEC

Securities Laws

- The Investment Advisers Act of 1940 (the “Advisers Act”)
 - A manager is deemed an “investment adviser” under Section 202(a)(11) if “for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities” or “for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities”
 - Registering under the Advisers Act subjects advisers to rules and regulations, including those governing advertising, custody, record keeping, advisory contracts, and fees
- Investment Company Act of 1940 (the “1940 Act”)
 - An “investment company” is defined under Section 3(a)(1)(A) as any issuer that “is or holds itself out as being engaged primarily, or proposes to engage primarily, in the business of investing, reinvesting, or trading in securities”
 - The 1940 Act requires either an exemption or registration. It imposes strict requirements related to governance, leverage, and capital structure and operations.



SEC v. W.J. Howey Co.

- Offering of units of a citrus grove development
- Supreme Court interpreted “investment contract” in Securities Act
- An “investment contract” is 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”
- “It 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”



Reves v. Ernst & Young

- Considered what kind of instrument qualifies as a note such that it can be regulated as a security under the Exchange Act.
- Under the *Reves* test, if the note exceeds nine months' maturity, it is presumed to be a security; if not, no presumption applies.
- The presumption can be rebutted in one of two ways
 - Can show the note bears a strong family resemblance to one of 7 kinds of instruments that are not securities (for example, a note delivered in consumer financing)
 - If the balance of four factors indicates the note is not a security
 - Motivations of the buyer and seller
 - The plan of distribution
 - The reasonable expectations of the investing public
 - Risk-reducing considerations



The DAO Report

- The facts are critical
- SEC concluded DAO tokens are “securities” after analyzing under the *Howey* test
 - Investors used ETH
 - Invested in a common enterprise
 - Reasonably expected to earn profits
 - Relied on managerial and entrepreneurial efforts of co-founders and curators to generate profits
- SEC did not pursue an enforcement action



Enforcement

Enforcement Agencies

- Securities and Exchange Commission (SEC)
 - Crypto Assets and Cyber Unit
- Department of Justice (DOJ)
 - National Cryptocurrency Enforcement Team
 - Virtual Asset Exploitation Unit (FBI)
- State Attorneys General & Securities Regulators



Enforcement Agencies

**Treasury Department Office
of Foreign Assets Control
(OFAC)**



**Treasury Department
Financial Crimes Enforcement
Network (FinCEN)**



**Commodities Futures Trading
Commission (CFTC)**



Private Plaintiffs





Who is in the Crosshairs?

- Issuers
- Company Executives
- Promoters
- Exchanges
- Advisors
- Attorneys



Initial Coin Offerings

- SEC
 - DAO Report – 2017
 - Block.one – \$24 million civil penalty – 2019
 - Ripple – case ongoing – 2020
- DOJ
 - REcoin/Diamond founders plead guilty – 2018
- FinCEN
 - Ripple Labs, \$700,000 civil penalty – 2015





Exchanges

- SEC
 - Poloniex – \$10 million civil penalty – 2021
- FinCEN
 - Bitmex – \$100 million civil penalty – 2021
- DOJ
 - Bitmex founders plead guilty – 2022

| | | | |
|----------|---|--------|------------|
| Ethereum | ▼ | -8.4% | 84,294 |
| Litecoin | ▲ | +1.2% | 3,254,888 |
| Bitcoin | ▲ | +12.8% | 25,101,983 |
| Ripple | ▼ | -4.3% | 241,219 |
| Ethereum | ▲ | +2.2% | 2,829 |

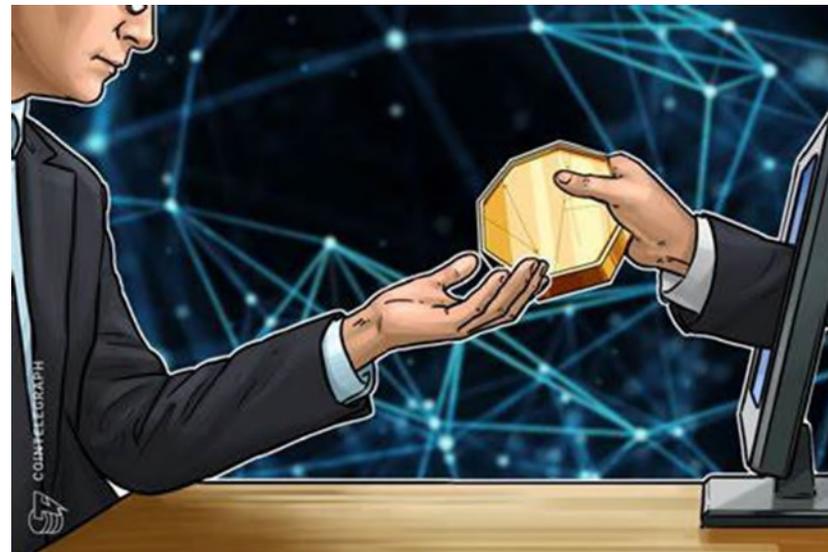
Stablecoins

- SEC
 - Tether – investigation ongoing – 2021
- DOJ
 - Tether – investigation ongoing – 2021
- CFTC
 - Tether – \$41 million fine – 2021



Lending Products

- SEC
 - BlockFi Lending LLC – \$50 million – 2022
- DOJ
 - Bitconnect founder – \$56 million liquidation, faces 20 years maximum sentence – 2021
- State Regulators
 - BlockFi Lending LLC – \$50 million to 32 states – 2022
 - Celsius – cease and desist order – 2021 (NJ, NY, TX)



Crypto Mining

- SEC
 - Mining Capital Coin – injunction and charges (2022)
 - Nvidia – \$5.5 million (2022)
- DOJ
 - Mining Capital Coin founder indicted (2022)
- Class Action
 - *Winter v. Stronghold Digital Mining, Inc., et al.* (2022)





Non-Fungible Tokens (NFTs)

- DOJ
 - Frosties NFT founders charged (2022)
 - *United States v. Nathaniel Chastain – Insider Trading* (2022)
- SEC – Purported Market Sweep (2022)
- Class Action
 - Dapper Labs sued – 2022



Where are we headed?



More Innovation - Greater Adoption

- Fidelity now offers 401(k) access to Bitcoin (Apr. 26, 2022)
- Payment apps continue to rise
- The COVID-19 pandemic enhanced adoption



More Regulation

- Executive Order on Ensuring Responsible Development of Digital Assets (March 9, 2022)
- President's Working Group Report on Stablecoins (Nov. 1, 2021)
- SEC Amendments to Rule 3b-16 expanding the definition of an "exchange" (Jan. 26, 2022)
- Responsible Financial Innovation Act (proposed in the Senate on June 7, 2022)
- Increased SEC focus on NFTs



More Enforcement

- Clean up of ICOs
- *SEC v. Ripple*
- Digital Asset Exchanges
- Increased focus on NFTs
- Downturn in market will lead to more regulatory actions



How to Minimize White-Collar Risk



How to Minimize White-Collar Risk

- Do not bury your head
- Embrace the regulatory atmosphere early
- Be willing to adapt
- If it is too good to be true, it probably is
- Think two steps ahead
- Consult with an attorney throughout the process, not just if things go south



Matthew Lindenbaum

Matthew represents companies in high-stakes litigation with an emphasis on class action defense in the automotive and financial services industries, including the emerging crypto-currency industry (including, among others, Poloniex in its August 2021 settlement with the SEC, various companies/individuals under investigation by U.S. regulators, and Poloniex in the Tether putative class action currently pending in the SDNY). He also defends companies and individuals in government investigations and enforcement actions involving the United States Department of Justice, the Securities and Exchange Commission, the Consumer Financial Protection Bureau, the Office of Foreign Assets Control, and conducts internal investigations for companies and special board committees.

Matthew is the leader of Nelson Mullins' Boston Litigation Team, a 2021 Massachusetts Super Lawyer, and has been repeatedly recognized as a Super Lawyer "Rising Star." He has developed in-depth knowledge of the business of digital assets, auto financing, mortgage loan origination, servicing and securitization, commercial real estate, and automotive manufacturing and sales businesses. Matthew advises and represents corporations, officers, and boards of directors and their committees in business litigation matters. He also assists clients with a wide range of general commercial litigation matters and has advised clients on disclosure, corporate governance, litigation avoidance, employee discipline, and other matters.



Robert Lindholm

Rob focuses his practice on government investigations and whitecollar defense, high stakes business litigation and class action defense, and e-discovery and litigation readiness. He represents companies/individuals involved in the FinTech/Cryptocurrency space (including, among others, Poloniex in its August 2021 settlement with the SEC, various companies/individuals under investigation by U.S. regulators, and Poloniex in the Tether putative class action currently pending in the SDNY), financial institutions, Fortune 500 companies, and other clients in a wide array of internal/government investigations, commercial litigation, and class action litigation. Rob is also the Chair of the White-Collar Crime/Government Investigations Section of the Mecklenburg County Bar.



Daniel Newman

Dan began his career as an enforcement attorney with the Northeast Regional Office of the U.S. Securities and Exchange Commission. He regularly represents individuals and entities in government investigations and litigation initiated by agencies including the SEC, CFTC and FTC. Those investigations have included issues involving registration, promotion and fraud relating to digital currency offerings. Dan also conducts internal investigations for companies and represents individuals in those investigations. Dan's practice also includes representation of both plaintiffs and defendants in a variety of private business and securities-related litigations in federal and state courts, involving among others, common law and statutory securities fraud, shareholder derivative actions, class actions, and commercial torts, contracts. Dan has been recognized by Chambers for his knowledge in Securities Litigation.



Richard B. Levin

Richard is chair of the FinTech and Regulation Practice and was one of the first lawyers to focus on the regulation of blockchain and digital assets. He is considered a thought leader in the FinTech space. Richard brings his experience as a senior legal and compliance officer on Wall Street and in London to bear in advising clients on corporate, FinTech, securities, and regulatory issues. A problem-solver by nature, he has been advising FinTech clients on legal and regulatory issues since the start of electronic trading in the late 1990s. His practice focuses on helping financial services and technology clients identify and address regulatory issues as they build their businesses.

Richard's practice focuses on the representation of early stage and publicly traded companies in the FinTech space, including investment banks, broker-dealers, investment advisers, peer-to-peer lending platforms, digital currency trading platforms, alternative trading systems (ATs), exchanges, and custodians. He represents these firms before the U.S. Securities and Exchange Commission (SEC), the U.S. Commodity Futures Trading Commission (CFTC), the Financial Industry Regulatory Authority (FINRA), the U.S. Department of the Treasury, the Office of the Comptroller of the Currency (OCC), state regulators, and Congress. Richard has represented clients before regulators in Australia, Canada, France, Germany, Hong Kong, Ireland, Japan, Singapore, South Korea, and the United Kingdom. His current and past clients include leading national financial institutions, multinational financial services holding companies, leading firms in the FinTech space, and institutions engaging in global investment banking, investment management, securities, and other financial services with institutional clients.

Richard has been identified by Chambers and Partners as one of the leading lawyers in the Blockchain and Cryptocurrencies category since the inception of the category. He has been recognized by Chambers for his knowledge on regulatory matters, great relationships with regulators, for helping clients push the boundaries of the FinTech sector, and for his advice on matters such as broker-dealer licensing and alternative trading systems.

Before joining Nelson Mullins, Richard was the chair and founder of the Chambers-rated FinTech and Regulation Practice of another leading U.S. law firm. The team he built was recognized by Chambers in the FinTech Legal in the USA category and in the FinTech Legal: Blockchain & Cryptocurrencies category. The team was recognized for its FinTech, blockchain, and cryptocurrency knowledge and as a leading firm on FinTech matters.

Richard is routinely quoted by leading publications including Bloomberg, the New York Times, Reuters, and the Wall Street Journal and is a frequent speaker at conferences around the world on the regulation of FinTech, blockchain, and digital assets.



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