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Securities and Exchange Commission vs. Kim Kardashian, Cryptocurrencies and the "Major Questions Doctrine"

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SECURITIES AND EXCHANGE COMMISSION VS. KIM KARDASHIAN, CRYPTOCURRENCIES AND THE "MAJOR QUESTIONS DOCTRINE"

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ABSTRACT

The SEC has brought some highly publicized enforcement actions against Kim Kardashian and other celebrity social media influencers who received undisclosed payments for their endorsement of cryptocurrencies. This Article describes those cases and analyzes whether the SEC exceeds its authority under the Constitutional "major questions doctrine" recently applied by the Supreme Court in West Virginia v. EPA. *That doctrine prohibits a federal agency from regulating activities that raise a major question that Congress, rather than the agency, must resolve. Such a question is one in which there is major political and economic interest and over which the agency has no clear authority from Congress to act. As this Article relates, the cryptocurrency market is of major political and economic interest to millions of individuals and businesses. It is also the subject of intense policymaking efforts in the Executive Branch and Congress. This Article further analyzes whether Congress granted the SEC clear authority to regulate the cryptocurrency market. It finds no such authority. In its absence, the SEC relies on the 1946 Supreme Court decision in* SEC v. Howey *as the basis for its jurisdictional claims. This Article finds that decision, which involved the sale of Florida orange grove investments to tourists, to be vague at best and anything but clear on whether cryptocurrencies are "securities" that are subject to SEC regulation.*

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> Any celebrity or other individual who promotes a virtual token or coin that is a security must disclose the nature, scope, and amount of compensation received in exchange for the promotion. A failure to disclose this information is a violation of the anti-touting provisions of the federal securities laws.

—Statement by the U.S. Securities and Exchange Commission.[1]

INTRODUCTION

Section 17(b) of the Securities Act of 1933 requires disclosure of payments for endorsements that may influence the price of a security.[2] The Securities and Exchange Commission (SEC) is using that provision to attack celebrities receiving undisclosed payments for their touting of cryptocurrencies.[3] One such defendant was reality show star and social media influencer Kimberly Kardashian, who failed to disclose payments received for promoting a cryptocurrency through her Instagram account.[4] In another such action, the SEC charged actor Steven Seagal with failing to disclose $1 million of payments in cash and cryptocurrency for promoting an "initial coin offering" (ICO) through his Facebook and

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[1] *SEC Statement Urging Caution Around Celebrity Backed ICOs*, SEC (Nov. 1, 2017), https://www.sec.gov/news/public-statement/statement-potentially-unlawful-promotion-icos [https://perma.cc/K4UJ-H9E9].

[2] 15 U.S.C. § 77q(b).

[3] *See, e.g.*, *Crypto Assets and Cyber Enforcement Actions*, SEC, https://www.sec.gov/spotlight/cybersecurity-enforcement-actions [https://perma.cc/87MY-S2FC] (Nov. 4, 2022) (describing other SEC cryptocurrency enforcement actions).

[4] *See* Michelle Chapman, *Kim Kardashian to Pay $1.26 Million After Settling With SEC Over Crypto Promotion*, WMUR9, https://www.wmur.com/article/kim-kardashian-sec-crypto-promotion-settlement/41495071# [https://perma.cc/7XLN-UZPV] (Oct. 3, 2022, 9:08 AM). Kardashian was promoting Ethereum Max, an online crypto trading platform that offered and sold digital "Emax tokens" to the general public. Kardashian, Securities Act Release No. 11116 at 2, 2022 WL 4922870 at *1 (Oct. 3, 2022), https://www.sec.gov/litigation/admin/2022/33-11116.pdf [https://perma.cc/R5R2-8XKV]. Although Kardashian's Instagram post disclosed that it was an advertisement ("#AD"), it did not disclose the amount and nature of the payment, which was $250,000. *SEC Sounds Alarm on Crypto Endorsements With $1.3M Kim Kardashian Fine*, PYMNTS (Oct. 3, 2022), https://www.pymnts.com/cryptocurrency/2022/sec-sounds-alarm-on-crypto-endorsements-with-1-3m-kim-kardashian-fine/#:~:text=The%20Securities%20and%20Exchange%20Commission's,her%20%24250%2C000%20fee%2C%20plus%20interest [https://perma.cc/XX3D-DZGD].

Twitter accounts.[5] Professional boxer Floyd Mayweather Jr. was similarly charged by the SEC with failing to disclose payments received for promoting ICOs.[6]

These actions were settled by consent orders in which there was no admission or denial of wrongdoing, but those settlements imposed significant monetary fines.[7] Those penalties, as well as the associated adverse publicity, were intended by the SEC to force celebrities to conform to the Section 17(b) anti-touting mandates.[8] This Article analyzes whether the SEC is overreaching its statutory authority in those cases under the "major questions doctrine" that was enunciated by the Supreme Court in *West Virginia v. EPA*.[9]

I. SECTION 17(B) OF THE SECURITIES ACT OF 1933

Section 17(b) of the Securities Act of 1933 was passed after congressional investigations into the Stock Market Crash of 1929

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[5] Press Release, SEC, Actor Steven Seagal Charged With Unlawfully Touting Digital Asset Offering (Feb. 27, 2020) [hereinafter SEC, Steven Seagal], https://www.sec.gov/news/press-release/2020-42 [https://perma.cc/3TWR-EB4G]. "An ICO is the crypto currency's counterpart to an initial public offering ("IPO") of securities." Thomas L. Hazen, *Tulips, Oranges, Worms, and Coins—Virtual, Digital, or Crypto Currency and the Securities Laws*, 20 N.C.J.L. & TECH. 493, 509 (2019) (citation omitted); *see also* Press Release, SEC, ICO "Listing" Website Charged With Unlawfully Touting Digital Asset Securities (July 14, 2021), https://www.sec.gov/news/press-release/2021-125?utm_medium=email&utm_source=govdelivery [https://perma.cc/K4DT-NAAV].

[6] Press Release, SEC, Two Celebrities Charged With Unlawfully Touting Coin Offerings (Nov. 29, 2018), https://www.sec.gov/news/press-release/2018-268 [https://perma.cc/BWF9-5FEN].

[7] *See* Chapman, *supra* note 4; SEC, Steven Seagal, *supra* note 5; SEC, *supra* note 6.

[8] *See, e.g.*, SEC, *supra* note 6; SEC, Steven Seagal, *supra* note 5. The cryptocurrency anti-touting cases are not the first effort by the SEC to garner headlines through the prosecution of statements made by a celebrity on social media. *See* Jerry W. Markham, *Securities & Exchange Commission vs. Elon Musk & the First Amendment*, 70 CASE W. RSRV. L. REV. 339, 343 (2020) (analyzing the application of the First Amendment to charges brought by the SEC against Elon Musk for statements that he made on Twitter about taking Tesla private).

[9] 142 S. Ct. 2587, 2609 (2022).

revealed a number of questionable practices in stock promotion schemes.[10] Among other abuses, professional publicists and reporters had been paid large sums of money to plant favorable reports in newspapers and radio broadcasts about the operations of publicly traded companies.[11] Before those stories were released, traders who were paying the publicists bought the stock and profited from the increase in price that followed publication.[12] In response to those revelations, Congress included Section 17(b) in the Securities Act of 1933, which declared such practices to be fraudulent.[13]

An essential element required to prove a violation of Section 17(b) is that the endorsement must concern a "security."[14] As will be described below, much uncertainty abounds over whether cryptocurrencies are securities that fall within the SEC's jurisdictional mandate. The SEC has, nevertheless, unilaterally decreed that cryptocurrency offerings are securities that it can

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[10] 23 JERRY W. MARKHAM & THOMAS L. HAZEN, BROKER-DEALER OPERATIONS UNDER SECURITIES AND COMMODITIES LAW § 2:2 at 2-9 & 2-10.

[11] *Id.*

[12] 2 JERRY W. MARKHAM, A FINANCIAL HISTORY OF THE UNITED STATES: FROM J.P. MORGAN TO THE INSTITUTIONAL INVESTOR (1900–1970) 144 (2002). One such publicist, A. Newton Plummer, was paid $300,000 to circulate 20,000 planted stories touting stocks to some 700 newspapers. *Id.* Also promoting stocks for undisclosed endorsement fees were radio personalities such as William J. McMahon, an economist and the head of the McMahon Institute of Financial Research. *Id.*; *see also* MARKHAM & HAZEN, *supra* note 10, at 2-9 & 2-10 (further describing those practices and bribes paid to reporters at leading newspapers for printing favorable stories).

[13] Section 17(b) states that:

> It shall be unlawful for any person, by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, to publish, give publicity to, or circulate any notice, circular, advertisement, newspaper, article, letter, investment service, or communication which, though not purporting to offer a security for sale, describes such security for a consideration received or to be received, directly or indirectly, from an issuer, underwriter, or dealer, without fully disclosing the receipt, whether past or prospective, of such consideration and the amount thereof.

15 U.S.C. § 77q(b).

[14] *Id.* "Congress did not . . . 'intend to create a broad federal remedy for all fraud.'" Reves v. Ernst & Young, 494 U.S. 56, 61 (1990) (quoting Marine Bank v. Weaver, 455 U.S. 551, 556 (1982)).

regulate.[15] This means that ICOs must register with the SEC under the Securities Act of 1933[16] or structure their offerings to comply with SEC exemptions from that requirement.[17]

The SEC is also using other antifraud provisions in the federal securities laws to attack cryptocurrency trading and is threatening cryptocurrency trading platforms with registration violations.[18] For example, the SEC brought insider trading charges under Section 10(b) of the Securities Exchange Act of 1934[19] against defendants engaging in cryptocurrency transactions on the basis of insider information.[20] The SEC alleged that defendants used non-public knowledge of the planned listing of tokens on Coinbase, a crypto trading platform with over 100 million users,[21] to profit from increases in the value of the tokens when their listings were made public.[22] The SEC's complaint in that action asserted that nine listings on Coinbase that were targeted by the defendants had been created through unregistered ICOs.[23] This raised the question of whether Coinbase is operating illegally as an unregistered national securities exchange since it is listing and trading what the SEC asserts are securities.[24] Although no

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[15] Jay Clayton, *Statement on Cryptocurrencies and Initial Coin Offerings*, SEC (Dec. 11, 2017), https://www.sec.gov/news/public-statement/statement-clayton-2017-12-11 [https://perma.cc/M7VS-V6VB].

[16] 15 U.S.C. § 77e.

[17] *See, e.g.,* SEC Regulation D, 17 C.F.R. § 230.500 (2021).

[18] Lydia Beyoud, *SEC's Gensler Steps Up Push to Get Crypto Exchanges to Register With Regulator*, BNN BLOOMBERG (July 28, 2022), https://www.bnnbloomberg.ca/sec-s-gensler-steps-up-push-to-get-crypto-exchanges-to-register-with-regulator-1.1798477 [https://perma.cc/HK2P-FPJE].

[19] 15 U.S.C. § 78j(b); 17 C.F.R. § 240.10b5-1 (2000).

[20] Complaint & Demand for Jury Trial at 1, 5, 11, SEC v. Wahi, No. 2:22-cv-01009 (W.D. Wash. June 21, 2022), https://www.sec.gov/litigation/complaints/2022/comp-pr2022-127.pdf [https://perma.cc/R8YJ-LTC3].

[21] *About Coinbase*, COINBASE, https://www.coinbase.com/about#:~:text=Approximately%20108%20million%20verified%20users,%2C%20earn%2C%20and%20use%20crypto [https://perma.cc/4D9Q-DW2X].

[22] Complaint & Demand for Jury Trial, *supra* note 20, at 1–2.

[23] *Id*. at 22.

[24] Press Release, SEC, SEC Issues Investigative Report Concluding DAO Tokens, a Digital Asset, Were Securities (July 25, 2017) [hereinafter DAO Investigative Report], https://www.sec.gov/news/press-release/2017-131 [https://perma.cc/8RKA-WB4H] ("issuers of distributed ledger or blockchain technology-based securities must register offers and sales of such securities unless a valid exemption applies . . . . Additionally, securities exchanges providing for

charges have yet been brought against Coinbase, SEC chair Gary Gensler has directed the SEC staff to regulate cryptocurrency trading platforms in the same manner as securities exchanges.[25]

II. THE MAJOR QUESTIONS DOCTRINE

The SEC has made cryptocurrency cases a leading part of its securities law enforcement efforts.[26] The agency created a "Crypto Assets and Cyber Unit" in its Division of Enforcement and has brought over eighty cryptocurrency actions, which resulted in more than $2 billion in fines and restitution orders.[27] The SEC is creating a regulatory structure for cryptocurrencies through those lawsuits without legislative guidance.[28] In so doing, the SEC is ignoring the "major questions doctrine." "Under this body of law, known as the major questions doctrine, given both separation of powers principles and a practical understanding

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trading in these securities must register unless they are exempt."); *see also* Clara Hudson & Amanda Iacone, *SEC Cedes No Ground on Crypto With Coinbase Insider Trading Case*, BLOOMBERG L. (July 25, 2022, 5:00 AM), https://news.bloomberglaw.com/securities-law/sec-cedes-no-ground-on-crypto-with-coinbase-insider-trading-case [https://perma.cc/TVC3-MSX6]; Aislinn Keely, *Crypto Firms Could Face Fallout From SEC Insider Trading Case Against Former Coinbase Employee*, THE BLOCK (July 22, 2022, 8:12 PM), https://www.theblock.co/post/159239/crypto-firms-could-face-fallout-from-sec-insider-trading-case-against-former-coinbase-employee [https://perma.cc/4TX5-YZ4E].

[25] *See* Beyoud, *supra* note 18. *But see* Underwood v. Coinbase Glob., Inc., No. 21 CIV. 8353 (PAE), 2023 WL 1431965, at *5–*12, *14 (S.D.N.Y. Feb. 1, 2023) (rejecting such a claim in a class action lawsuit).

SEC Commissioner Hester Peirce has warned that Gensler's decree has created a regulatory "Catch 22" that will impede the creation of new crypto networks that are not able to register or qualify for an exemption under the federal securities laws. Hester M. Peirce, Comm'r, SEC, *Running on Empty: A Proposal to Fill the Gap Between Regulation and Decentralization* (Feb. 6, 2020) [hereinafter *Running on Empty*], https://www.sec.gov/news/speech/peirce-remarks-blockress-2020-02-06 [https://perma.cc/N5QB-J4GM].

[26] *See* Press Release, SEC, SEC Nearly Doubles Size of Enforcement's Crypto Assets and Cyber Unit (May 3, 2022), https://www.sec.gov/news/press-release/2022-78 [https://perma.cc/97SP-AGXL].

[27] *Id.*

[28] Richard Satran, *U.S. SEC Embraces "Regulation by Enforcement" as Securities Industry Morphs Beyond Rulebooks*, REUTERS (Nov. 12, 2021, 9:44 AM), https://www.reuters.com/article/bc-finreg-sec-regulation-by-enforcement/u-s-sec-embraces-regulation-by-enforcement-as-securities-industry-morphs-beyond-rulebooks-idUSKBN2HX1OR [https://perma.cc/M9QA-58QV].

of legislative intent, the agency must point to 'clear congressional authorization' for the authority it claims."[29] "Agencies have only those powers given to them by Congress, and 'enabling legislation' is generally not an 'open book to which the agency [may] add pages and change the plot line . . . .'"[30] "We presume that 'Congress intends to make major policy decisions itself, not leave those decisions to agencies.'"[31] "Under the major questions doctrine, the Supreme Court has rejected agency claims of regulatory authority when (1) the underlying claim of authority concerns an issue of 'vast "economic and political significance,"' and (2) Congress has not clearly empowered the agency with authority over the issue."[32]

As will be described below, the cryptocurrency market has vast economic and political significance, and the SEC has not clearly been empowered by Congress to regulate that market.

A. The Cryptocurrency Market Has Vast Economic and Political Significance

A new financial asset class appeared in 2008 in the form of a "cryptocurrency" called Bitcoin.[33] Bitcoins are created through computer "blockchains" that utilize decentralized networks of computers independently owned and operated, but linked in a peer-to-peer network.[34] Blockchains are touted as providing security and efficiency in creating and transferring Bitcoins without the intermediation of a third party.[35] This is a major departure from

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[29] West Virginia v. EPA, 142 S. Ct. 2587, 2595 (2022).

[30] *Id.* at 2609 (citation omitted).

[31] *Id.*

[32] KATE BOWERS, CONG. RSCH. SERV., IF12077, THE MAJOR QUESTIONS DOCTRINE (Nov. 2, 2022), https://crsreports.congress.gov/product/pdf/IF/IF12077 [https://perma.cc/RDM3-5JGR] (citation omitted).

[33] *See, e.g.,* GREGORY S. ROWLAND & TREVOR I. KIVIAT, CRYPTOCURRENCY AND OTHER DIGITAL ASSETS FOR ASSET MANAGERS, GLOBAL LEGAL INSIGHTS—BLOCKCHAIN & CRYPTOCURRENCY REGULATION 90 (1st ed. 2019), https://www.davispolk.com/sites/default/files/cryptocurrency_and_other_digital_assets_for_asset_managers.pdf [https://perma.cc/968K-S97A].

[34] *What Is Blockchain Technology?*, IBM, https://www.ibm.com/topics/what-is-blockchain [https://perma.cc/3UZB-C9CT] (describing blockchain technology).

[35] Trevor I. Kiviat, Note, *Beyond Bitcoin: Issues in Regulating Blockchain Transactions*, 65 DUKE L.J. 569, 574 (2015); *see also* Matt Levine, *The Crypto*

traditional securities markets where broker-dealers and stock exchanges act as intermediaries in the execution of customer trades.[36]

The Bitcoin concept quickly led to the creation of other cryptocurrencies, such as Dogecoin, Ethereum, Ripple, and Eos.[37] There are now over 19,000 cryptocurrencies in circulation,[38] which are sometimes referred to as "tokens."[39] The cryptocurrency market that the SEC seeks to regulate through its lawsuits is a broad one that has major economic significance. "As of 2020, almost 36.5 million people in the [United States] alone had ownership of some form of crypto."[40] "In August 2021 there were 969.5

Story: Where It Came From, What It All Means, and Why It Still Matters, BLOOMBERG (Oct. 25, 2022, 5:00 AM), https://www.bloomberg.com/features/2022-the-crypto-story/ [https://perma.cc/R36F-DZVY] (extensive discussion on crypto technology).

[36] Kiviat, *supra* note 35, at 577. The disintermediation available through blockchain technology does not conform to the business models of the exchanges and broker-dealers regulated by the SEC:

> A core benefit of a token network is its non-reliance on intermediaries; people transact directly with one another. Having to buy or sell tokens through a registered broker-dealer or on a registered exchange certainly puts a damper on the development of a thriving, decentralized crypto network. Particular problems arise because there are unique challenges related to broker-dealers and exchanges handling digital assets.

Running on Empty, supra note 25.

[37] Jonathan Berger, *Crypto Price Analysis & Overview: Bitcoin, Ethereum, Ripple, Eos, Doge Coin*, CRYPTOPOTATO, https://cryptopotato.com/crypto-price-analysis-overview-bitcoin-ethereum-ripple-eos-doge-coin/ [https://perma.cc/U3ZT-2252] (Nov. 11, 2019, 1:34 PM). Dogecoins, which were created as a joke in 2013 to mock Bitcoins, turned out to be no laughing matter with the market capitalization of dogecoins soared in value, with $50 billion outstanding in 2021. David Goldman, *What Is Dogecoin? How a Joke Became Hotter Than Bitcoin*, CNN BUS., https://www.cnn.com/2021/04/17/investing/what-is-dogecoin/index.html [https://perma.cc/47N4-H3HZ] (May 4, 2021, 10:52 AM).

[38] Arjun Kharpal, *Crypto Firms Say Thousands of Digital Currencies Will Collapse, Compare Market to Early Dotcom Days*, CNBC, https://www.cnbc.com/2022/06/03/crypto-firms-say-thousands-of-digital-currencies-will-collapse.html [https://perma.cc/YB69-77FH] (June 3, 2022, 8:12 PM).

[39] *What Is a Token?*, COINBASE, https://www.coinbase.com/learn/crypto-basics/what-is-a-token [https://perma.cc/E2DP-UXJA].

[40] Georgia Weston, *How Cryptocurrencies Have Brought A Revolution In Digital Economy*, 101 BLOCKCHAINS (May 20, 2022), https://101blockchains.com/impact-of-cryptocurrency-on-digital-economy/ [https://perma.cc/YK34-5RUQ].

million total visits to the top 60 crypto websites worldwide."[41] Cryptocurrency coins and tokens have also "established their foundations as viable forms of investment and currency."[42] Several major businesses have accepted payment in cryptocurrencies in exchange for their goods and services.[43] They include Tesla, Microsoft, Overstock.com, AT&T, Whole Foods, Starbucks, Home Depot, Dish Network, and PayPal.[44]

"[C]ourts have generally considered an agency action to be of vast economic significance if it requires 'billions of dollars in spending.'"[45] In April 2022, the cryptocurrency market that the SEC seeks to regulate through its enforcement actions was valued by SEC Chair Gary Gensler at $2 trillion.[46] That number

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[41] Similarweb, *Top Crypto Websites: Who's Winning and Why?*, DERIVED FROM DATA NEWS (Oct. 14, 2021), https://dfdnews.com/2021/10/14/top-crypto-websites-whos-winning-online-and-why/ [https://perma.cc/PUB5-53QD].

[42] Weston, *supra* note 40.

[43] *See The Rise of Using Cryptocurrency in Business*, DELOITTE, https://www2.deloitte.com/us/en/pages/audit/articles/corporates-using-crypto.html [https://perma.cc/XS8K-ATVN].

[44] Andrew Lisa, *14 Major Companies That Accept Bitcoin*, GOBANKINGRATES (Apr. 21, 2022), https://www.gobankingrates.com/money/business/major-companies-that-accept-bitcoin/ [https://perma.cc/U5VL-Q3W7]; Ofir Beigel, *Who Accepts Bitcoin as Payment?*, 99BITCOINS, https://99bitcoins.com/bitcoin/who-accepts/ [https://perma.cc/7ZX6-LA9Y] (Jan. 15, 2023).

[45] Brown v. U.S. Dep't of Educ., No. 4:22-CV-0908-P, 2022 WL 16858525, at *11 (N.D. Tex. Nov. 10, 2022) (citations omitted).

[46] *See* Gary Gensler, Chair, SEC, Prepared Remarks of Gary Gensler On Crypto Markets Penn: Law Capital Markets Association Annual Conference (Apr. 4, 2022), https://www.sec.gov/news/speech/gensler-remarks-crypto-markets-040422 [https://perma.cc/5Q7F-78VM]; *see also Global Cryptocurrency Market Report 2022–2027—Industry to Cross a Staggering $32.4 Trillion by 2027, Exploding with a CAGR of 58.4%*, YAHOO! (Feb. 25, 2022), https://www.yahoo.com/now/global-cryptocurrency-market-report-2022-120800380.html [https://perma.cc/5VM4-THYV]. Cryptocurrency market capitalization reached a high of $3 trillion in 2021. Yvonne Lau, *Cryptocurrencies Hit Market Cap of $3 Trillion for the First Time as Bitcoin and Ether Reach Record Highs*, FORTUNE (Nov. 9, 2021, 1:32 AM), https://fortune.com/2021/11/09/cryptocurrency-market-cap-3-trillion-bitcion-ether-shiba-inu/ [https://perma.cc/VE59-CTA5]. That number was more than Canada's GDP. *See Canada's Gross Domestic Product (GDP)*, WORLD ECON., https://www.worldeconomics.com/Country-Size/Canada.aspx#:~:text=The%20official%20estimate%20for%20Canada's,date%20GDP%20base%20year%20data [https://perma.cc/64MH-8QWV].

declined to under $1 trillion later that year, but it remained a major trading market.[47]

By suing celebrities, the SEC is tacitly conceding that the cryptocurrency market is of major economic and political interest. Kim Kardashian had 228 million followers on her Instagram account when she posted the cryptocurrency advertisement that was the subject of the SEC's suit.[48] The fact that cryptocurrencies were promoted through Super Bowl advertisements that were broadcast to some 100 million viewers is a further indication of the major social importance of this market.[49] "I[f] you watch any sports on television, it seems difficult not to notice that the crypto sector has gone on an ad-buying binge . . . . And crypto is starting to draw interest from pension funds and sovereign wealth funds."[50] "What was formerly an alternative investment solely in the domain of speculators is now being openly discussed as a viable option for a portion of any investor's portfolio, even in their retirement plans."[51]

The major economic importance of the cryptocurrency concept is further underscored by the fact that blockchain technology is being considered by governments for use as an official currency. For example, the U.S. Federal Reserve is exploring the

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[47] *See* Arjun Kharpal, *Bitcoin Turns Positive, Rebounds From Lowest Level Since June*, CNBC, https://www.cnbc.com/2022/09/07/bitcoin-btc-price-falls-as-cryptocurrency-market-drops-below-1-trillion-.html [https://perma.cc/78C6-WGTC] (Sept. 7, 2022, 3:59 PM).

[48] Taylor Locke, *Kim Kardashian West and Other Influencers Are Being Paid to Advertise Cryptocurrency on Social Media*, CNBC, https://www.cnbc.com/2021/06/15/kim-kardashian-west-charli-damelio-jake-paul-posting-paid-crypto-ads.html [https://perma.cc/RWK7-NWH7] (June 22, 2021, 9:17 AM) (describing the number of Kardashian's Instagram followers and referencing other crypto influencers on social media that have millions of followers).

[49] *See* Aimee Picchi & Khristopher J. Brooks, *Super Bowl Ads 2022: Crypto Companies Are Spending Millions to Win Over Viewers*, CBS NEWS, https://www.cbsnews.com/news/super-bowl-2022-commercials-cryptocurrency/ [https://perma.cc/4EVL-XMFH] (Feb. 11, 2022, 7:32 AM).

[50] Daniel W. Drezner, *The Political Economy of Crypto*, WASH. POST (Feb. 1, 2022, 7:00 AM), https://www.washingtonpost.com/outlook/2022/02/01/political-economy-crypto/ [https://perma.cc/AQ6L-EE85].

[51] John Csiszar, *6 Reasons Crypto Has Become So Popular in the Past Two Years*, NASDAQ (June 1, 2022, 8:00 AM), https://www.nasdaq.com/articles/6-reasons-crypto-has-become-so-popular-in-the-past-two-years [https://perma.cc/SQD9-JCFV].

use of a central bank cryptocurrency.[52] The Chinese government announced that it was creating its own cryptocurrency, the digital yuan.[53] Several other countries have also announced the introduction of digital currencies.[54] The City of Miami, Florida, created its own cryptocurrency called MiamiCoin.[55]

The cryptocurrency market is also the subject of major political interest. On March 9, 2022, President Joe Biden issued an executive order, which stated that "[w]e must take strong steps to reduce the risks that digital assets could pose to consumers, investors, and business protections; financial stability and financial system integrity; combating and preventing crime and illicit finance; national security; the ability to exercise human rights; financial inclusion and equity; and climate change and pollution."[56] The Executive Order directed a coordinated inter-agency approach to develop plans for regulating cryptocurrencies.[57] In response to the President's Order, the U.S. Treasury Department created a framework for inter-agency and international cooperation and the development of standards addressing the risks of cryptocurrencies.[58] The Treasury Department stated that "[u]neven

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[52] *Central Bank Digital Currency (CBDC)*, FED. RSRV. BD., https://www.federalreserve.gov/central-bank-digital-currency.htm [https://perma.cc/38C4-43N7] (Nov. 4, 2022).

[53] *See* Emily Parker, *China's Digital Yuan Shows Why We Still Need Cryptocurrencies Like Bitcoin*, CNN BUS. (Feb. 4, 2022, 2:09 PM), https://www.cnn.com/2022/02/04/perspectives/china-digital-yuan-cryptocurrency-bitcoin/index.html [https://perma.cc/VRJ4-8MLR].

[54] Christopher Mims, *Central Bank Digital Currencies Are Coming—Whether Countries Are Ready or Not*, WALL ST. J., https://www.wsj.com/articles/digital-currencies-banking-system-11673625716 [https://perma.cc/MA79-86S3] (Jan. 16, 2023, 10:00 AM); Nelson Renteria, *A Year On, El Salvador's Bitcoin Experiment Is Stumbling*, REUTERS (Sept. 7, 2022, 7:07 PM), https://www.reuters.com/technology/year-el-salvadors-bitcoin-experiment-is-stumbling-2022-09-07/ [https://perma.cc/WA2N-2C6R].

[55] *See* David Drucker, *How Miami Coin Works and Why People Should Keep An Eye on It*, FIU NEWS (Jan. 26, 2022, 11:30 AM), https://news.fiu.edu/2022/fiu-faculty-weigh-in-on-the-future-importance-of-miami-coin [https://perma.cc/V5QB-Q67E].

[56] Exec. Order No. 14,067, 87 Fed. Reg. 14,143, 14,143 (Mar. 14, 2022).

[57] *Id.* at 14,149.

[58] *Fact Sheet: Framework for International Engagement on Digital Assets*, U.S. DEP'T OF THE TREASURY (July 7, 2022), https://home.treasury.gov/news/press-releases/jy0854 [https://perma.cc/PZ9W-PEU2].

regulation, supervision, and compliance across jurisdictions creates opportunities for arbitrage and raises risks to financial stability and the protection of consumers, investors, businesses, and markets."[59]

By September 2022, nine governmental reports had been submitted in response to the President's Executive Order.[60] Among other things, they warned that crypto markets "risk harming everyday Americans' financial stability and our national security."[61] The Financial Stability Oversight Council (FSOC), which is responsible for assessing systemic risks to the U.S. financial system, also warned that financial institutions' "crypto-asset activities could pose risks to the stability of the U.S. financial system."[62] In its 2022 annual report, FSOC further advised of a regulatory gap in the regulation of cryptocurrencies and recommended that Congress pass legislation to cure that concern.[63] On January 27, 2023, the President's National Economic Council issued a statement that set forth the Biden Administration's policy views on regulating cryptocurrencies and called for Congress to enact legislation.[64] The Council's report asserted that:

> Congress should expand regulators' powers to prevent misuses of customers' assets—which hurt investors and distort prices—and

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[59] *Id.*

[60] *FACT SHEET: White House Releases First-Ever Comprehensive Framework For Responsible Development of Digital Assets*, WHITE HOUSE (Sept. 16, 2022), https://www.whitehouse.gov/briefing-room/statements-releases/2022/09/16/fact-sheet-white-house-releases-first-ever-comprehensive-framework-for-responsible-development-of-digital-assets/ [https://perma.cc/89SJ-XCQX].

[61] Chris Matthews, *Crypto Poses Threat to "Financial Stability" of Everyday Americans*, *Biden Administration Warns in New Report*, MARKETWATCH (Sept. 16, 2022, 6:00 AM), https://www.marketwatch.com/story/crypto-poses-threat-to-financial-stability-of-everyday-americans-biden-administration-warns-in-new-report-11663289907 [https://perma.cc/NMJ3-9UCU].

[62] Press Release, U.S. Dep't Treasury, PRESS RELEASE: Financial Stability Oversight Council Releases Report on Digital Asset Financial Stability Risks and Regulation (Oct. 3, 2022), https://home.treasury.gov/news/press-releases/jy0986 [https://perma.cc/5GRL-EWYU].

[63] FISCAL STABILITY OVERSIGHT COUNCIL, ANNUAL REPORT 11, 34, 72 (2022).

[64] Brian Deese et al., *The Administration's Roadmap to Mitigate Cryptocurrencies' Risks*, WHITE HOUSE (Jan. 27, 2023), https://www.whitehouse.gov/nec/briefing-room/2023/01/27/the-administrations-roadmap-to-mitigate-cryptocurrencies-risks/ [https://perma.cc/N9PB-JGSL].

> to mitigate conflicts of interest. Congress could also strengthen transparency and disclosure requirements for cryptocurrency companies so that investors can make more informed decisions about financial and environmental risks. To aid law enforcement, it could strengthen penalties for violating illicit-finance rules and subject cryptocurrency intermediaries to bans against tipping off criminals. It could fund greater law-enforcement capacity building, including with international partners.[65]

Perhaps most telling of whether Congress would view regulation of the cryptocurrency market to be a "major question" is through the consideration of its own actions in similar circumstances. Historically, Congress enacted legislation when it thought that new or additional regulation was needed for a commodity-related financial product.[66] Both the SEC and the Commodity Futures Trading Commission (CFTC) agree that at least Bitcoin and some other cryptocurrencies are "commodities" but differ on whether financial transactions involving cryptocurrencies are also securities.[67] In the past, jurisdictional boundary disputes between the SEC and CFTC were resolved by legislation.[68] That legislation was frequently amended as an asset class evolved or additional regulation was deemed necessary after disruptive market events.[69]

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[65] *Id*.

[66] *Cf.*, Dennis M. Kelleher et al., *The Dodd-Frank Act Is Working And Will Protect The American People If It Is Not Killed Before Fully Implemented*, 20 N.C. BANKING INST. 127, 129 (2016) (discussing the passage of the Dodd-Frank Act in response to the 2008 economic crisis). Cryptocurrencies are a new financial asset class. Brian Sozzi, *Bitcoin Is Officially A New Asset Class: Goldman Sachs*, YAHOO! NEWS (May 24, 2021), https://news.yahoo.com/bitcoin-is-officially-a-new-asset-class-goldman-sachs-103540636.html [https://perma.cc/3WSZ-T76H].

[67] *See* Daniel Kuhn, *SEC's Gensler Reiterates Bitcoin Alone Is A Commodity. Is He Right?*, YAHOO! FINANCE (June 28, 2022), https://finance.yahoo.com/news/sec-gensler-reiterates-bitcoin-alone-161257549.html [https://perma.cc/UF9G-P98E]; Leo Schwartz, *'The Million-Dollar Question': CFTC Chair on Regulating Crypto Alongside the SEC*, FORTUNE CRYPTO (Oct. 24, 2022, 12:19 PM), https://fortune.com/crypto/2022/10/24/million-dollar-question-cftc-chair-regulating-crypto-sec/ [https://perma.cc/73SN-XGUL].

[68] *See* Colleen M. Baker, *Regulating the Invisible: The Case of Over-the-Counter Derivatives*, 85 NOTRE DAME L. REV. 1287, 1311–13 (2010).

[69] *See id.*

To illustrate, Congress enacted the Grain Futures Act in 1922 to regulate trading in "commodity" futures traded on commodity exchanges in certain "enumerated" "commodities," such as wheat.[70] The SEC, which was not created until 1934, was given no regulatory responsibility under that statute.[71] Instead, the Grain Futures Act was administered by a "Grain Futures Commission," which was composed of the Secretary of Agriculture, the Secretary of Commerce and the Attorney General.[72] The Grain Futures Act proved to be ineffective and was replaced by the Commodity Exchange Act of 1936 (CEA).[73] Again, the SEC was given no jurisdiction to regulate commodity trading.[74] Instead, the renamed Commodity Exchange Commission" retained its role as regulator.[75] Also like its predecessor, the CEA applied only to commodities enumerated in the statute.[76] Several subsequent legislative amendments were needed to add additional enumerated commodities that became the subject of futures trading.[77]

The CEA proved ineffective in regulating the explosion of trading in derivative instruments that occurred in the 1970s.[78] In response to concerns raised by that trading, the CFTC Act of

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[70] *See* Grain Futures Act, Pub. L. No. 67-331, §§ 2, 3, 42 Stat. 998, 998–99 (1922) (amended 1936).

[71] *See* §§ 4–12, 42 Stat. at 1000–03.

[72] *US Futures Trading and Regulation Before the Creation of the CFTC*, CFTC, https://www.cftc.gov/About/HistoryoftheCFTC/history_precftc.html [https://perma.cc/ZYB6-9M26]. The Department of Agriculture was given principal responsibility for the day-to-day administration of that legislation. *See* JERRY W. MARKHAM, THE HISTORY OF COMMODITY FUTURES TRADING AND ITS REGULATION 15, 27 (1987).

[73] *See* Commodity Exchange Act, Pub. L. No. 74-675, § 2, 49 Stat. 1491, 1491 (1936); MARKHAM, *supra* note 72, at 22.

[74] *See* Commodity Exchange Act § 3(b), 49 Stat. at 1492.

[75] *See* CFTC, *supra* note 72.

[76] *See* §§ 2–3, 49 Stat. at 1491.

[77] *See* GAO, *The Commodity Exchange Act: Issues Related to the Commodity Futures Trading Commission Reauthorization*, GOVINFO (May 5, 1999), https://www.govinfo.gov/content/pkg/GAOREPORTS-GGD-99-74/html/GAOREPORTS-GGD-99-74.htm [https://perma.cc/PTL5-BUR4]. As described by the Government Accountability Office (GAO), "[a]s Congress periodically amended the CEA, it added other agricultural commodities to the list . . . . In aggregate, the regulated agricultural commodities became known as the enumerated commodities; all others became known as the non-enumerated commodities." *Id.*

[78] *See* MARKHAM, *supra* note 72, at 56–61.

1974[79] created the CFTC and granted it "exclusive" jurisdiction over futures and options trading on all commodities, not just the previously enumerated ones.[80] This exclusive grant of jurisdiction to the CFTC excluded the SEC from regulating commodity-related financial instruments that the SEC had previously claimed were securities.[81] For example, just before the creation of the CFTC, a number of boiler room operations were defrauding retail investors of millions of dollars through high-pressure sales of options on unregulated commodities.[82] The SEC charged those firms with federal securities law violations, which led to a debate over whether those instruments were "securities" that could be regulated by the SEC.[83] Congress intervened with the CFTC Act of 1974, which granted the CFTC "exclusive" jurisdiction over commodity options.[84]

The CFTC Act of 1974 also regulated "leverage contracts" that were used to trade precious metals.[85] Before that legislation was enacted, the SEC sued Monex International Ltd., a leader in marketing leverage transactions in precious metals to the public.[86] The SEC charged that Monex's leverage contracts were illegal unregistered securities.[87] The SEC suit was dropped after the CFTC was created and given exclusive jurisdiction over leverage contracts.[88] In 2010, Congress enacted the Dodd-Frank Wall

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[79] *Id.* at 65; *See* Commodity Futures Trading Commission Act of 1974, Pub. L. No. 93-463, 88 Stat. 1389, 1389 (1974).

[80] 7 U.S.C. § 2 (2018); *see also* Thomas A. Russo & Edwin L. Lyon, *The Exclusive Jurisdiction of the Commodity Futures Trading Commission*, 6 HOFSTRA L. REV. 57, 57–59 (1977) (describing this "controversial and ambiguous" exclusive jurisdiction provision in the 1974 amendments).

[81] Russo & Lyon, *supra* note 80, at 59.

[82] *See* MARKHAM, *supra* note 72, at 186–88.

[83] *See* Jerry W. Markham, *Regulation of Hybrid Instruments Under the Commodity Exchange Act: A Call for Alternatives*, 1990 COLUM. BUS. L. REV. 1, 16, n.91 (1990).

[84] Commodity Futures Trading Commission Act of 1974, Pub. L. No. 93-463, § 201, 88 Stat. 1389, 1395 (1974); *see* MARKHAM, *supra* note 72, at 193–95.

[85] MARKHAM, *supra* note 72, at 179–91.

[86] *See* Jerry W. Markham, *"Confederate Bonds," "General Custer," and the Regulation of Derivative Financial Instruments,* 25 SETON HALL L. REV. 1, 17 n.61 (1994).

[87] *See* SEC v. MONEX Int'l Ltd., No. CV 74-3634-HF, 1975 U.S. Dist. LEXIS 16495, at *3–4, *14–15 (C.D. Cal. Aug. 20, 1974); *see also* Markham, *supra* note 86, at 17 n.61.

[88] *See* MARKHAM, *supra* note 72, at 179–80.

Street Reform and Consumer Protection Act (Dodd-Frank Act), which broadly restructured the CFTC's regulation of leveraged OTC precious metals contracts.[89] Ironically, the CFTC is using the Dodd-Frank Act authority to compete with the SEC in regulating cryptocurrencies through enforcement actions.[90] This has led to much confusion over whether and when cryptocurrencies are "securities" that are regulated by the SEC or whether they are "commodities" regulated "exclusively" by the CFTC.[91]

Tellingly, for purposes of the major questions doctrine, the CFTC and the SEC have a long-running history of competing for jurisdiction over new commodity related financial instruments.[92] Congress was called upon to resolve those disputes on several occasions.[93] For example, the CFTC and SEC got into a jurisdictional wrangle over the regulation of options and futures on stock indexes and GNMA securities.[94] Congress resolved that fight through the Futures Trading Act of 1982, which allocated jurisdiction over those instruments between the two agencies through a somewhat complex formula.[95] Single stock security

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[89] *See* Pub. L. No. 111-203, §§ 210, 717, 805, 812, 1093 124 Stat. 1376, 1486, 1652, 1809, 1821, 2095–96 (2010).

[90] *See* John Joy, *The Race to Regulate Crypto: CFTC vs. SEC,* JURIST (Nov. 24, 2021, 7:44 AM), https://www.jurist.org/commentary/2021/11/john-joy-crypto-sec/ [https://perma.cc/JT4E-HRKZ]; ABE CHERNIN ET AL., CORNERSTONE RESEARCH, TRENDS IN CFTC VIRTUAL CURRENCY ENFORCEMENT ACTIONS 1 (2020), https://www.cornerstone.com/wp-content/uploads/2022/01/Trends-in-CFTC-Virtual-Currency-Enforcement-Actions-2015-Q2-2020.pdf [https://perma.cc/CT9E-GCXJ]; Mengqi Sun, *CFTC Signals Intent to Increase Enforcement of Crypto-Related Cases*, WALL ST. J. (May 18, 2022, 5:14 PM), https://www.wsj.com/articles/cftc-signals-intent-to-increase-enforcement-of-crypto-related-cases-11652908480 [https://perma.cc/6WSP-QP4X].

[91] *See Bipartisan Crypto Bills Could Clarify Current Regulatory Confusion—if They Tackle* Howey, DAVIS POLK (Aug. 10, 2022), https://www.davispolk.com/insights/client-update/bipartisan-crypto-bills-could-clarify-current-regulatory-confusion-if-they?utm_source=vuture&utm_medium=email&utm_campaign=bipartisan%20crypto%20bills%20could%20clarify%20current%20regulatory%20confusion%20-%20if%20they%20tackle%20howey [https://perma.cc/4E93-66E9].

[92] *See* Jerry W. Markham, *Merging the SEC and CFTC—A Clash of Cultures*, 78 U. CINN. L. REV. 537, 552 (2009).

[93] *See id.* at 569–70, 570 n.186.

[94] *See id.* at 569–71.

[95] Pub. L. No. 97-303, §§ 1–7, 96 Stat. 1409–10 (1982); *see* Don L. Horwitz & Jerry W. Markham, *Sunset on the Commodity Futures Trading Commission:*

futures contracts were another new financial instrument that was regulated and had jurisdiction allocated by Congress between the SEC and CFTC through the Commodity Futures Modernization Act of 2000 (CFMA).[96]

The Futures Trading Practices Act of 1992 allowed the CFTC to exempt swaps and other over-the-counter transactions from its jurisdiction.[97] After a number of large losses from swap transactions, the SEC and CFTC began competing for jurisdiction over the then-still-developing swaps market.[98] In 1999, the President's Working Group on Financial Markets recommended legislation clarifying that issue.[99] Congress responded with the CFMA, which allowed the CFTC to exempt institutional swaps transactions from CFTC regulation.[100] After scandals and more large losses arose from swap trading during the Financial Crisis of 2008,[101] the CFTC and SEC published a Joint Report, ironically just when Bitcoins first appeared, that expressed concern with the then-existing legal uncertainty on the issue of which agency had jurisdiction over new financial instruments. The Joint Report asserted that this uncertainty "at times has caused lengthy delays in bringing new products to market. The lack of legal certainty can be costly and confusing, and it can impede innovation and competition."[102] The Joint Report concluded that

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Scene II, 39 BUS. LAW. 67, 83, 87, 90–93 (1983) (describing that allocation of jurisdiction).

[96] Commodity Futures Modernization Act of 2000, Pub. L. No. 106-544, 114 Stat. 2763A-375, *Title II—"Coordinated Regulation of Security Futures Products."*

[97] Pub. L. No. 102-546, § 502, 106 Stat. 3590, 3629–31 (1992).

[98] *See* Markham, *supra* note 86, at 22.

[99] PRESIDENT'S WORKING GRP. ON FIN. MKTS., OVER-THE-COUNTER DERIVATIVES MARKETS AND THE COMMODITY EXCHANGE ACT 1 (Nov. 1999).

[100] *See* Pub. L. No. 106-544, § 407, 114 Stat. 2763, 2763A-461 (2000).

[101] See Jerry W. Markham, *Regulating Credit Default Swaps in the Wake of the Subprime Crisis*, *in* 6 INTERNATIONAL MONETARY FUND, CURRENT DEVELOPMENTS IN MONETARY AND FINANCIAL LAW: RESTORING FINANCIAL STABILITY 281 (2012), https://www.elibrary.imf.org/display/book/9781616350819/9781616350819.xml?rskey=TBzwLQ&result=3 [https://perma.cc/VZ4C-5ALW] (describing the role of credit default swaps during that event).

[102] U.S. COMMODITY FUTURES TRADING COMM'N & U.S. SEC. & EXCH. COMM'N, A JOINT REPORT OF THE SEC AND THE CFTC ON HARMONIZATION OF REGULATION 3 (2009), https://www.sec.gov/news/press/2009/cftcjointreport101609.pdf [https://perma.cc/7ELJ-SH86].

a "mechanism should be developed to break deadlocks between the CFTC and the SEC over disagreements regarding jurisdiction over new products."[103] The Joint Report recommended the enactment of legislation

> that would provide a process for expedited judicial review of jurisdictional matters regarding new products. Specifically, the SEC and the CFTC support legislation to establish and clarify: (i) legal certainty with respect to the agencies' authority over products exempted by the other agency; and (ii) a review process to ensure that any jurisdictional dispute is resolved by the Commissions against a firm timeline.[104]

Congress declined to adopt such a regulation by enforcement approach in which the courts would act as referee.[105] The CFMA's hands-off approach was abandoned in the Dodd-Frank Act.[106] That legislation imposed broad regulation over swaps and allocated jurisdiction over those instruments between the CFTC and SEC.[107]

Another commodity-related financial product that was the subject of specific legislation that set jurisdictional boundaries were derivative transactions in foreign currencies. The so-called "Treasury Amendment" in the CFTC Act of 1974 allocated jurisdiction over trading in foreign currencies among the CFTC and bank regulators.[108] The CEA was amended in 1982 to divide jurisdiction over foreign currency contracts traded on exchanges between the CFTC and SEC.[109] In 2000, the CFMA amended the CEA to clarify that the CFTC could regulate retail over-the-counter

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[103] *Id*.

[104] *Id*. at 12.

[105] *See* Pub. L. No. 111-203, §§ 717, 805, 812, 1093, 124 Stat. 1376, 1652, 1809, 1821, 2095–96 (2010).

[106] *Id.; see* Commodity Futures Modernization Act of 2000, Pub. L. No. 106-544, 114 Stat. 2763, *Title II—"Coordinated Regulation of Security Futures Products*."

[107] *See* Jerry W. Markham, *Regulation of Swap and Other Over-the-Counter Derivative Contracts*, 263 BLOOMBERG BNA SECURITIES PRACTICE PORTFOLIO SERIES at Part I.D (2021), https://www.bloomberglaw.com/product/blaw/document/26291241512 [https://perma.cc/338E-RUK8] (describing that regulation).

[108] *See* Dunn v. CFTC, 519 U.S. 465, 466–67 (1997) (addressing the jurisdictional reach of the Treasury Amendment).

[109] Horwitz & Markham, *supra* note 95, at 73.

foreign currency futures contracts.[110] Thereafter, the CFTC Reauthorization Act of 2008 granted the CFTC rule-making authority over off-exchange retail foreign currency futures contracts.[111] In 2010, the Dodd-Frank Act divided regulatory jurisdiction over trading in over-the-counter foreign currency instruments among the CFTC, SEC and federal bank regulators.[112]

An agency's action is also politically significant if Congress has engaged in "robust debates" over legislation addressing the agency's action.[113] The Infrastructure Investment and Jobs Act that was enacted by Congress in 2021 has already set requirements for reporting and taxing cryptocurrency trading profits.[114] Hearings have been held,[115] and debates are ongoing in Congress over some fifty bills that have been introduced to allocate regulation of the crypto asset market and set policy for government involvement in cryptocurrencies and other digital assets.[116] Among

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[110] *Advisory on Foreign Currency Trading*, CFTC (Feb. 5, 2001), https://www.cftc.gov/sites/default/files/opa/press01/opaadv06-01.htm [https://perma.cc/W2BR-XNXQ].

[111] *See* Pub. L. No. 110-246, § 13001(a)(B)(i)(I), 122 Stat. 1651, 2189 (2008). The CFTC Reauthorization Act of 2008 is a part of the Food, Conservation, and Energy Act of 2008. §§ 1, 13001.

[112] Pub. L. No. 111-203, §§ 717, 805, 812, 1093, 124 Stat. 1376, 1652, 1809, 1821, 2095–96 (2010).

[113] Brown v. U.S. Dep't of Educ., No. 4:22-cv-0908-P, 2022 WL 16858525, at *12 (N.D. Tex. Nov. 10, 2022) (citing West Virginia v. EPA, 142 S. Ct. 2587, 2620–21 (2022)).

[114] *See* Pub. L. No. 117-58, § 80603, 135 Stat. 429, 1339–40 (2021).

[115] Leo Schwartz, *Star-Studded Senate Hearings Illustrates Massive Divide Over Crypto in D.C.*, FORTUNE CRYPTO (Dec. 14, 2022, 2:27 PM), https://fortune.com/crypto/2022/12/14/star-studded-senate-banking-committee-divides-crypto/ [https://perma.cc/G3DK-H5QC]; Zachary Warmbrodt, *Crypto CEOs to Congress: We Want Regulation, Our Way*, POLITICO (Dec. 8, 2021, 2:38 PM), https://www.politico.com/news/2021/12/08/cryptocurrency-ceos-congress-regulation-523950 [https://perma.cc/L2SN-VPGC]; Samuel Wan, *Cardano Founder Steals the Show at Congressional Hearings on Crypto Regulation,* cryptoslate.com (June 24, 2022, 12:30 PM), https://cryptoslate.com/cardano-founder-steals-the-show-at-congressional-hearing-on-crypto-regulation/ [https://perma.cc/RWK4-GGFV].

[116] Jason Brett, *Congress Has Introduced 50 Digital Asset Bills Impacting Regulation, Blockchain, and CBDC Policy*, FORBES (May 19, 2022, 11:59 PM), https://www.forbes.com/sites/jasonbrett/2022/05/19/congress-has-introduced-50-digital-asset-bills-impacting-regulation-blockchain-and-cbdc-policy/?sh=3916a4914e3f [https://perma.cc/PNU6-ZB4M]; *see also* Thomas Franck, *Bipartisan*

other things, those bills address the regulation of cryptocurrencies by the SEC and CFTC, including the possible designation of the CFTC as the principal regulator of cryptocurrencies and other digital assets.[117]

FTX, a multibillion-dollar cryptocurrency trading operation, which had been a high profile advertiser during the Super Bowl, became the subject of hot debate in the financial services industry[118] and in congressional hearings over the regulation of its operations[119] and whether it should be regulated by the CFTC rather than the SEC.[120] Congressional debates on the need for legislation became even more robust after FTX reported billions of dollars in missing assets and declared bankruptcy in 2022.[121]

Crypto Regulatory Overhaul Would Treat Most Digital Assets as Commodities Under CFTC Oversight, CNBC (June 7, 2022, 3:08 PM), https://www.cnbc.com/2022/06/07/bipartisan-crypto-bill-lummis-and-gillibrand-want-to-empower-cftc-treat-digitals-assets-like-commodities.html [https://perma.cc/VA3U-K8H9] (providing the CFTC "with the authority to regulate the trading of digital commodities . . . .").

[117] *See, e.g.*, *The Digital Commodities Consumer Protection Act Closes Regulatory Gaps* U.S. SENATE COMM. AGRIC. NUTRITION & FORESTRY, WASHINGTON D.C. (Aug. 3, 2022), https://www.agriculture.senate.gov/imo/media/doc/crypto_one-pager1.pdf [https://perma.cc/U8UD-TJNG].

[118] Alexander Osipovich, *Futures Giant CME Considers Brokerage, Taking Cue From Crypto Rival FTX*, WALL ST. J. (Sept. 30, 2022, 10:48 PM), https://www.wsj.com/articles/futures-giant-cme-considers-brokerage-taking-cue-from-crypto-rival-ftx-11664592510 [https://perma.cc/4SF4-J6EN]; Sam Haysom, *Larry David's Super Bowl Ad Is Really Dividing People*, MASHABLE (Feb. 14, 2022), https://mashable.com/article/larry-david-ftx-super-bowl-ad [https://perma.cc/2G94-LGJZ].

[119] Jeff Reeves, *US Congress Questions Industry on Merits and Risks of FTX's Non-Intermediated Model*, FIA (May 12, 2022), https://www.fia.org/marketvoice/articles/us-congress-questions-industry-merits-and-risks-ftxs-non-intermediated-model [https://perma.cc/3P98-6VN5].

[120] *See* Paul Kiernan, *FTX's Collapse Upends Sam Bankman-Fried's Washington Play*, WALL ST. J., https://www.wsj.com/articles/ftxs-collapse-upends-sam-bankman-frieds-washington-play-11669545002 [https://perma.cc/TQ2A-RNUV] (Nov. 28, 2022, 3:29 PM) (describing the maneuvering by FTX executives to influence congressional action on cryptocurrency trading that would allocate jurisdiction over its operations to the CFTC rather than the SEC).

[121] *See* Nikhilesh De, *FTX Collapse Sparks Alarm From US Lawmakers*, COINDESK, https://www.coindesk.com/policy/2022/11/10/ftx-collapse-sparks-alarm-from-us-lawmakers/ [https://perma.cc/RF2A-XZRU] (Nov. 11, 2022, 10:08 AM); Dave Michaels, *FTX Collapse Draws Senate Scrutiny as Lawmakers Push for Crypto Oversight*, WALL ST. J., https://www.wsj.com/articles/ftx-collapse-draws

Its failure resulted in worldwide consternation, and the fallout from that scandal dominated the financial business press and social media.[122]

The SEC is seeking to preempt the ongoing legislative efforts to regulate cryptocurrencies through its enforcement actions.[123] That is not an appropriate approach for policymaking on major questions of national economic and political interest.[124] As CFTC Commissioner Caroline Pham has observed, the SEC claims over cryptocurrency trading jurisdiction is a "striking example of regulation by enforcement."[125] Moreover, after the failure of FTX, it was clear that the SEC's "regulation by enforcement isn't working and merely fuels market uncertainty."[126] As charged in the press:

-senate-hearing-scrutiny-as-crypto-oversight-in-focus-11669868740 [https://perma.cc/P6S4-VFDZ] (Dec. 1, 2022, 2:27 PM); A Martínez, *Lawmakers on Capitol Hill Hold Hearings Into the Failed Cryptocurrency Giant FTX*, NPR (Dec. 14, 2022, 7:18 AM), https://www.npr.org/2022/12/14/1142704783/lawmakers-on-capitol-hill-hold-hearings-into-the-failed-cryptocurrency-giant-ftx [https://perma.cc/9CJE-9GKB].

[122] *See, e.g.,* Allison Morrow, *The Crypto Meltdown, Explained*, WRAL NEWS (Nov. 18, 2022, 2:31 PM), https://www.wral.com/the-crypto-meltdown-explained/20584481/ [https://perma.cc/25W7-XC3K] ("The failure of FTX, shook the foundations of the entire ecosystem.").

[123] *See* Jay Clayton & Timothy Massad, *How to Start Regulating the Crypto Markets—Immediately*, WALL ST. J. (Dec. 4, 2022, 8:00 AM), https://www.wsj.com/articles/how-regulate-cryptocurrency-markets-11670110885 [https://perma.cc/G2C8-XW7V] (former CFTC and SEC chairs propose a CFTC and SEC dictated regulatory structure over cryptocurrencies without awaiting legislation).

[124] *See* Tessa E. Shurr, Comment, *A False Sense of Security: How Congress and the SEC are Dropping the Ball on Cryptocurrency,* 125 DICK. L. REV. 253, 253 (2020). As one law review comment asserts, "policymaking by enforcement is harmful to the financial technology industry and perpetuates the lack of clarity surrounding regulation of digital assets." *Id.* at 253.

[125] Hudson & Iacone, *supra* note 24. This was not the first time that the SEC had been the target of such criticism. *See* ROBERTA S. KARMEL, REGULATION BY PROSECUTION: THE SECURITIES AND EXCHANGE COMMISSION VS. CORPORATE AMERICA 15–17 (1982).

[126] *The FTX Crypto Fiasco*, WALL ST. J. (Nov. 10, 2022, 6:50 PM), https://www.wsj.com/articles/the-ftx-crypto-fiasco-cryptocurrency-sam-bankman-fried-alameda-coindesk-binance-11668122004 [https://perma.cc/63DU-KRNR]; Paul Kiernan, *FTX Collapse Puts Pressure on SEC's Enforcement Strategy*, WALL ST. J. (Dec. 22, 2022, 2:01 PM), https://www.wsj.com/articles/ftx-collapse-puts-pressure-on-secs-crypto-enforcement-strategy-11671735703 [https://perma.cc/BZ4Y-A8T9].

> Over the last two U.S. administrations, the U.S. Securities and Exchange Commission (SEC) has promoted an all-encompassing policy of "regulation by enforcement" for U.S.-based digital asset markets like Coinbase and the enterprise blockchain industry . . . . This "enforcement" produces little clarity for the market or protection of investors, which is the ostensible point of the regulatory exercise.[127]

As an industry participant complained, the SEC is inhibiting the expansion of cryptocurrencies through its "one-dimensional approach of regulation by enforcement" and that the agency's actions are forcing "American investors to use offshore crypto businesses 'with less protection and oversight.'"[128]

1. Congress Has Not Clearly Granted the SEC Authority to Regulate Cryptocurrencies

Before the *Kardashian* case, SEC Chairman Jay Clayton advised Congress that the SEC "does not have direct oversight over transactions in currencies or commodities, including currency trading platforms."[129] Clayton nevertheless asserted that "financial products that are linked to underlying digital assets, including cryptocurrencies, may be structured as securities products subject to the federal securities laws even if the underlying cryptocurrencies are not themselves securities."[130]

In *West Virginia v. EPA*, the Supreme Court held that agency claims of authority to regulate a matter that raises a major question are to be treated with "skepticism."[131] The agency

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[127] Roslyn Layton, *SEC Spin Doctors Trying to Hide Crypto Regulation Disaster*, FORBES (Jan. 8, 2023, 7:41 AM), https://www.forbes.com/sites/roslynlay-ton/2023/01/08/sec-spin-doctors-trying-to-hide-crypto-regulation-disaster/?sh=436ee9762039 [https://perma.cc/8ZEJ-PV4A].

[128] Jesse Coghlan, *SEC's 'One-Dimensional' Approach Is Slowing Bitcoin Progress: Grayscale CEO*, COINTELEGRAPH.COM (Jan. 24, 2023), https://cointelegraph.com/news/sec-s-one-dimensional-approach-is-slowing-bitcoin-progress-grayscale-ceo [https://perma.cc/YN9S-WXKD].

[129] Jay Clayton, *Chairman's Testimony Before the Senate Banking Committee on Virtual Currencies: The Roles of the SEC and CFTC*, SEC (Feb. 6, 2018), https://www.sec.gov/news/testimony/testimony-virtual-currencies-oversight-role-us-securities-and-exchange-commission [https://perma.cc/9RZE-BX5N].

[130] *Id.*

[131] West Virginia v. EPA, 142 S. Ct. 2587, 2614 (2022).

must point to "clear congressional authorization" for regulatory action that involves a major question.[132] As described below, there is no clear authority in the federal securities laws for the SEC's regulation of cryptocurrencies as "securities."[133] Rather than seeking clarifying legislation, or even conducting formal rule-making, the SEC published a unilateral investigative report (the DAO Investigative Report)[134] and some muddied staff guidance (*SEC Staff Crypto Advice*)[135] on how the agency would determine whether cryptocurrency transactions are securities.[136] The SEC asserts in those documents that cryptocurrencies are securities if their offerings meet the so-called *Howey* test that was articulated in a 1946 Supreme Court decision.[137]

In *Howey*, the Court formulated a test that is to be used to determine whether a transaction is an "investment contract," which is a form of "security" under the Securities Act of 1933.[138] The *Howey* case involved an orange grove owner in Florida who sold tourists deeded property rights for small plots of land

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[132] *See id.* at 2595.

[133] *See When It Comes To Analyzing Utility Tokens, The SEC Staff's "Framework For 'Investment Contract' Analysis of Digital Assets" May Be the Emperor Without Clothes (Or, Sometimes an Orange Is Just an Orange) (Part IV)*, WINSTON & STRAWN, LLP (Dec. 18, 2019), https://www.winston.com/en/crypto-law-corner/when-it-comes-to-analyzing-utility-tokens-the-sec-staffs-framework-for-investment-contract-analysis-of-digital-assets-may-be-the-emperor-without-clothes-part-iv.html [https://perma.cc/U8TK-UFVR]; *see also Recent Guidance: Securities Regulation—Financial Technology—SEC Provides Analytical Tools for Assessing Digital Assets.—SEC, Framework for "Investment Contract" Analysis of Digital Assets (2019)*, 132 HARV. L. REV. 2418, 2423 (2019) (describing the lack of clarity in the *SEC Staff Crypto Advice*).

[134] DAO Investigative Report, *supra* note 24. The purpose of that report was to provide guidance on the applicability of the federal securities laws "to a new paradigm—virtual organizations or capital raising entities that use distributed ledger or blockchain technology to facilitate capital raising and/or investment and the related offer and sale of securities." Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: The DAO, Exchange Act Release No. 81,207, at 2 (July 25, 2017).

[135] SEC, *Framework for "Investment Contract" Analysis of Digital Assets*, 1 [hereinafter *SEC Staff Crypto Advice*], https://www.sec.gov/files/dlt-framework.pdf [https://perma.cc/TH9E-6RJD] (2019).

[136] *Id.* at 2–3.

[137] *See* S.E.C. v. W.J. Howey Co., 328 U.S. 293, 298–99 (1946).

[138] *See id.*; 15 U.S.C. § 77b(a)(1) (defining the term "security" to include an "investment contract" but providing no definition of the latter term).

planted with citrus trees.[139] The defendants also offered separate service contracts for maintaining the trees, marketing their fruit and transmitting the net proceeds from sales to investors.[140] The Court held that this arrangement was an "investment contract" that fell within the SEC's jurisdiction.[141] In so doing, the Court adopted a four-prong test (which, evidencing its lack of clarity, is sometimes broken down into two, three, or even five prongs[142]) that has the following elements: (1) an investment of money; (2) in a common enterprise; (3) with a reasonable expectation of profit; (4) that is to be derived "solely" from the efforts of others.[143]

Under the major questions doctrine, "extraordinary grants of regulatory authority are rarely accomplished through 'modest words,' 'vague terms,' or 'subtle device[s].'"[144] On its face, equating cryptocurrency transactions to investments in an orange grove through the vague and subtle term "investment contract" is quite a stretch.[145] It is also confusing and unclear, causing market participants concern and curbing what is otherwise legitimate conduct. As SEC Commissioner Hester Peirce has observed, the broad application of the *Howey* test by the agency "has limited secondary trading and has had disastrous consequences for the ability of token networks to become functional."[146] Peirce further noted that "[t]he SEC has tried to apply the *Howey* analysis to crypto but doing so is not particularly easy."[147]

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[139] *See Howey*, 328 U.S. at 295.

[140] *See id.*

[141] *Id.* at 299–300.

[142] *See supra* note 133 and accompanying text.

[143] *See Howey*, 328 U.S. at 298–99.

[144] West Virginia v. EPA, 142 S. Ct. 2587, 2609 (2022) (citation omitted).

[145] *See* WINSTON & STRAWN, LLP, *supra* note 133; M. Todd Henderson & Max Raskin, *A Regulatory Classification of Digital Assets: Toward an Operational* Howey *Test for Cryptocurrencies, ICOs, and Other Digital Assets*, 2019 COLUM. BUS. L. REV. 443, 443 (2019) ("neither Congress nor the SEC has formally elucidated which digital assets are securities and which are not"); Michael J. O'Connor, *Overreaching Its Mandate? Considering the SEC's Authority to Regulate Cryptocurrency Exchanges*, 11 DREX. L. REV. 539, 578, 581 (2019) (analyzing whether cryptocurrency trading platforms are securities exchanges). *But see* Hazen, *supra* note 5, at 508 (advocating treating cryptocurrencies as securities).

[146] *Running on Empty*, *supra* note 25.

[147] *Id.*

The *Howey* test's application to cryptocurrencies is problematic because it "does not foster reproducible results that market participants can rely on with reasonable confidence."[148] The *SEC Staff Crypto Advice* is indeed troublesome. Among other things, it advises consideration of "a non-exclusive list of 50 or 60 'characteristics,' none of which is 'necessarily determinative,' on the understanding that when their 'presence' is 'stronger' it is 'more likely' that the digital asset is an 'investment contract' and thus a security."[149]

The *SEC Staff Crypto Advice* asserts that "[t]he first prong of the *Howey* test is typically satisfied in an offer and sale of a digital asset because the digital asset is purchased or otherwise acquired in exchange for value, whether in the form of real (or fiat) currency, another digital asset, or other type of consideration."[150] This broad application of the *Howey t*est is somewhat meaningless since almost every commercial transaction involves an exchange of value. For example, a purchase by a consumer of a commodity in a grocery store involves an exchange of value, *e.g.*, dollars for donuts.[151]

The *SEC Staff Crypto Advice* declares that the second prong of the *Howey* test, i.e., a "common enterprise," is met by cryptocurrencies.[152] "Based on our experiences to date, investments in digital assets have constituted investments in a common enterprise because the fortunes of digital asset purchasers have been linked to each other or to the success of the promoter's efforts."[153] Again that guidance is too vague to be of any real assistance in determining whether a cryptocurrency transaction is a security. The same could be said equally of circumstances that are not considered to be investment contracts. For example, an employee is in a common enterprise with the promoter of the business and with fellow employees, but that arrangement is not an "investment contract."[154] Contracts for the building of a residence involve

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[148] DAVIS POLK, *supra* note 91.

[149] *Id.*

[150] *SEC Staff Crypto Advice*, *supra* note 135, at 2.

[151] *See Breakfast Breads, Donuts & More*, FOOD LION, https://shop.foodlion.com/shop/categories/36 [https://perma.cc/84C3-3HMH].

[152] *SEC Staff Crypto Advice*, *supra* note 135, at 2.

[153] *Id.* at 13 n.11 (citation omitted).

[154] Gillian Emmett Moldowan & Jai Garg, *Chapter 135: The 1933 Act, in* EXECUTIVE COMPENSATION GUIDE: IMPACT OF THE FEDERAL SECURITIES LAWS,

a contract for a common enterprise between the homeowner and the builder, but that does not create an "investment contract."[155]

The "commonality" prong in the *Howey t*est also raises the vexing question of whether the commonality must be "horizontal" or "vertical."[156] That exercise is rendered more confusing by the fact that the *SEC Staff Crypto Advice* states that the agency "does not require vertical or horizontal commonality *per se*, nor does it view a 'common enterprise' as a distinct element of the term 'investment contract.'"[157]

The third prong of the *Howey* test, i.e., an expectation of profits, provides no real help in determining whether a cryptocurrency is a security. The *SEC Staff Crypto Advice* states that a reasonable expectation of profit is present where, among other things, there is an expectation that the value of the digital asset will appreciate and be resold for a profit.[158] However, there are a wide variety of non-security transactions in which purchases are made of commodities that, like Bitcoins, carry an expectation, or at least a hope, they will increase in value. For example, it is common for investors to make purchases of real property with

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THE 1933 ACT 1, 4 (Bloomberg L. ed., 2021), https://www.shearman.com/-/media/files/perspectives/2021/03/ecg_800_impact_of_federal_securities_laws_1933_act_03_02_2021a.pdf [https://perma.cc/D8WE-J6QD]. "An employment agreement under which an employee provides services to an issuer in exchange for compensation doesn't qualify as a security under the Howey test." *Id.* (citing International Brotherhood of Teamsters v. Daniel, 439 U.S. 551, 558 (1979) (citing the *Howey* test)).

[155] *See generally* United Housing Foundation, Inc. v. Forman, 421 U.S. 837 (1975) (ownership interests in a cooperative housing project were not investment contracts).

[156] *See*, *e.g.,* Long v. Shultz Cattle Co., Inc., 881 F.2d 129, 140 (5th Cir. 1989) (describing the split in circuit courts on whether to apply vertical or horizontal commonality under the *Howey* test). In *SEC v. SG Ltd*., a pre-cryptocurrency case, the First Circuit applied a horizontal commonality test and held that virtual shares in a virtual enterprise were securities. *See* SEC v. SG Ltd., 265 F.3d 42, 50 (1st Cir. 2001). The court pointed to the fact that the defendant "unambiguously represented to its clientele that participants' funds were pooled in a single account that was used to settle participants online transactions. Therefore, pooling is established." *Id.* The court noted that horizontal commonality also requires investors to share in the profits and risks of the business. *Id*.

[157] *SEC Staff Crypto Advice*, *supra* note 135, at 13 n.10 (citations omitted).

[158] *Id*. at 2–3.

the goal of making profits from an increase in its market value.[159] The acquisition of works of art, the purchase of coins by a numismatist, and stamp purchases by philatelists may be made for the purpose of making a profit from an increase in their value.[160] As SEC Commissioner Peirce has observed:

> If the token seller is simply discussing the potential for an increase in the value of a token in the same manner that a seller of any number of other consumer products might appeal to purchasers' desire to buy a product of lasting or even increasing value, is there an investment contract? The subjective intent of any particular purchaser should not be controlling. If it were, then is there any end to the Commission's authority? How would that logic apply to a shoe company, which, as it sells you a pair of sneakers, promises to hire some prominent athletes to promote the brand, thus focusing your mind on how sky high the price will go on StockX [an online consignment store] rather than on how high your new kicks will enable you to jump on the basketball court?[161]

An ICO is different from an initial public offering (IPO) of a security because the ICO participants are not being sold an ownership or debt interest in a corporate or corporate-like organization. Instead, the crypto purchaser is buying a "commodity" in the form of a crypto token.[162] This makes them purchasers of a "thing" that may or may not increase in value. The mere purchase of a "thing," such as real estate, artworks, or stamps, does not bestow voting, dividend, liquidation, interest payments or principal repayment, or other rights commonly associated with a security investment.[163]

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159 *See* Troy Adkins, *How to Invest in Land*, INVESTOPEDIA, https://www.investopedia.com/articles/investing/050614/there-are-more-ways-invest-land-you-think.asp [https://perma.cc/Z94C-RJUH] (June 10, 2022).

160 *See* Dan Moskowitz, *The Risks of Investing in Art and Collectibles*, INVESTOPEDIA, https://www.investopedia.com/articles/personal-finance/061815/risks-investing-art-and-collectibles.asp [https://perma.cc/8HEB-XHU9] (Sept. 11, 2022).

161 *Running on Empty*, *supra* note 25.

162 *See* Jake Frankenfield, *Initial Coin Offering (ICO): Coin Launch Defined, with Examples*, INVESTOPEDIA, https://www.investopedia.com/terms/i/initial-coin-offering-ico.asp [https://perma.cc/7NYR-LR7L] (Aug. 18, 2022).

163 *See* Moskowitz, *supra* note 160.

The SEC's DAO Investigative Report addressed a token that varies from the Bitcoin model. The target of that investigation was an unincorporated Decentralized Autonomous Organization (DAO),[164] which the SEC described as "a 'virtual' organization embodied in computer code and executed on a distributed ledger or blockchain."[165] The DAO was created with the object of raising funds through the sale of DAO tokens in exchange for Ether, a cryptocurrency.[166] The sponsors of the DAO used the ether tokens to fund "projects" they selected for investment returns.[167] The SEC likened the purchasers of DAO tokens to investors in a company that pays dividends, i.e., the DAO token purchasers were to be given "rewards" by sharing in the anticipated earnings from the "projects" selected by the DAO promoters.[168] That sharing would also occur through an increase in the value of the DAO tokens.[169]

The *Howey*-oriented co-owner profit sharing analysis in the DAO Investigative Report equates DAO tokens to a "stock" investment, i.e., "the voting rights of DAO Token holders [was] akin to those of a corporate shareholder."[170] Using a "stock" analogy in a *Howey* analysis of whether this arrangement created an "investment contract" ignores the fact that "stock" is treated as a "special case" under the federal securities laws with its own distinctive meaning,[171] i.e., "an instrument bearing the name 'stock' that, among other things, is negotiable, offers the possibility of

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[164] DAO Investigative Report, *supra* note 24; *see also* Aaron Wright, Th*e Rise of Decentralized Autonomous Organizations: Opportunities and Challenges*, STAN. J. BLOCKCHAIN L. & POL'Y 2, 4, 14 (June 30, 2021), https://stanford-jblp.pubpub.org/pub/rise-of-daos [https://perma.cc/2B9M-KVZ6] (describing DAOs and their regulation); Laila Metjahic, *Deconstructing the DAO: The Need for Legal Recognition and the Application of Securities Laws to Decentralized Organizations*, 39 CARDOZO L. REV. 1533, 1547–49 (2018) (describing regulatory concerns with DAOs).

[165] Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: The DAO, Exchange Act Release No. 81,207 at 1 (July 25, 2017).

[166] *See id.* at 2–3.

[167] *See id.* at 4.

[168] *Id.*

[169] *See id.* at 11–12.

[170] *Id.* at 15.

[171] *See* Reves v. Ernst & Young 494 U.S. 56, 62–64 (1990) (citing Landreth Timber Co. v. Landreth, 471 U.S. 681, 694 (1985)).

capital appreciation, and carries the rights to dividends contingent on the profits of a business enterprise . . . ."[172]

The DAO tokens offered the possibility of capital appreciation, a form of dividend, and at least titular voting rights, so why did the SEC not categorize them as "stock" instead of an "investment contract?"[173] This may be due to the fact that the DAO was a "new paradigm" that was created in order to "supplant traditional mechanisms of corporate governance and management with a blockchain such that contractual terms are 'formalized, automated and enforced using software.'"[174] As stated in the *SEC Staff Crypto Advice,* "[b]oth the Commission and the federal courts frequently use the 'investment contract' analysis to determine whether unique or novel instruments or arrangements, such as digital assets, are securities subject to the federal securities laws."[175] The SEC was also faced with the fact that, unlike the DAO tokens, holders of Bitcoins and other similarly created decentralized cryptocurrencies do not normally receive dividends and have no voting or other rights commonly associated with stock.[176] Instead, those cryptocurrencies will make or lose money based, not on investments made by the creator of the token, but on their price valuations as a *commodity*, ever how ephemeral the way in which that value is derived or perceived.[177]

The SEC avoids the differences between stocks and most cryptocurrencies by labeling them "investment contracts" under the subtle, catch all provisions of the *Howey* test.[178] That claim ignores the admission of an SEC chair that Bitcoins and other decentralized cryptocurrencies are "commodities" rather than "securities."[179] To illustrate how classification as a "commodity" places cryptocurrencies outside the scope of the SEC's jurisdiction consider the case of "notes." Like "stock," "notes" are a separate category of securities regulated under the federal securities laws.[180]

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172 *Id.* at 62.

173 Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: The DAO, Exchange Act Release No. 81,207 at 11 (July 25, 2017).

174 *Id.* at 3.

175 *SEC Staff Crypto Advice*, *supra* note 135, at 1.

176 *See* Metjahic, *supra* note 164, at 1556–57.

177 *See id.*

178 *See SEC Staff Crypto Advice*, *supra* note 135, at 1–3.

179 *See* Clayton, *supra* note 129.

180 *See* 15 U.S.C. § 78c(a)(10).

Notes are defined, not by the *Howey test*, but by a separate test set forth by the Supreme Court in *Reves v. Ernst & Young*.[181] There, the Court rejected the *Howey* test for use in defining "notes" in favor of a four part "family resemblance test."[182] Under the family resemblance test, such things as pawn shop loans and consumer promissory notes secured by automobiles or residential homes are not "securities."[183]

Cryptocurrencies normally bear no family resemblance to notes that are regulated under the federal securities laws.[184] Cryptocurrencies also do not ordinarily bear a family resemblance to the "margin" loans secured by stock that fall within the SEC's jurisdiction.[185] Bitcoin and other commodities may be traded on "margin," but that trading is not subject to the federal securities laws.[186] This is because commodity margins bear no family resemblance to stock "margin" loans.[187] Stock margin regulations impose maximum loan limits on loans secured by stocks.[188] Those limits are set by the Federal Reserve Board and enforced by the SEC.[189] They are designed to limit speculation by restricting the leverage obtained from a loan used to buy stock.[190]

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[181] *See* 494 U.S. 56, 67 (1990).

[182] *See id.* at 67.

[183] *See id.* at 63–64.

[184] *See id* at 56. This is not to say that cryptocurrencies cannot be used for loans. The SEC charged a crypto lending operation called BlockFi Lending LLC with violations of the Investment Company Act of 1940 (15 U.S.C. §§ 80a-1 et seq.). *See* Press Release, SEC, BlockFi Agrees to Pay $100 Million in Penalties and Pursue Registration of Its Crypto Lending Product (Feb. 14, 2022), https://www.sec.gov/news/press-release/2022-26 [https://perma.cc/BUE2-E35B]. There, the respondent borrowed more than $10 billion in cryptocurrencies from some 570,000 investors. *See* Patrick Thompson, *SEC chief Gary Gensler fires warning shot at 'crypto' companies*, COINGEEK (Aug. 26, 2022), https://coingeek.com/sec-chief-gary-gensler-fires-warning-shot-at-crypto-companies/ [https://perma.cc/5KBT-EPJZ]. The investors' cryptocurrencies were placed in "BlockFi Interest Accounts," (BIA) which the SEC charged were securities. *See* Press Release, *supra*. BIA investors were promised a variable rate of interest as a return on their loan. *See id.* BlockFi pooled the BIA accounts and loaned the cryptocurrencies to institutional investors. *See id.*

[185] *See* 15 U.S.C. § 78g(a)(2)(A).

[186] *See* 15 U.S.C. § 78g.

[187] *See generally id.*; *Reves*, 494 U.S. at 67–68.

[188] *See* 15 U.S.C. § 78g(a).

[189] *See* § 78g(c)(2)(B).

[190] *See* § 78g(a).

In contrast, commodity margins act only as a "good faith" deposit of money to ensure performance on the contract.[191] Historically, minimum commodity futures margin requirements were set by the commodity exchanges.[192] Debates raged in Congress decades before and after the creation of the CFTC over whether commodity futures margins should be federally regulated.[193] Those debates included unsuccessful efforts by the SEC to have Congress authorize the Federal Reserve Board to set margins on all stock index contracts in order to assure uniformity in margin requirements for stock index contracts traded on commodity and security exchanges.[194] Further evidencing the existence of a "major question," Congress granted the CFTC only limited authority over commodity futures margins through the Futures Trading Act of 1982.[195] In 2010, Congress enacted the Dodd-Frank Act that, among other things, adopted federal margin requirements for swap contracts and allocated that jurisdiction among the CFTC, SEC and bank regulators.[196]

The fourth prong of the *Howey* test, i.e., expectation of profits derived "solely" from the efforts of others, is even more problematic and complex. Indeed, the *SEC Staff Crypto Advice* writes out the "solely" requirement,[197] citing *SEC v. Glenn W. Turner Enter., Inc.*[198] In that case, the Ninth Circuit concluded that "the word 'solely' should not be read as a strict or literal limitation on the definition of an investment contract, but rather must be construed realistically, so as to include within the definition those schemes which involve in substance, if not form, securities."[199] Some "courts have eased the rigidity of the need to have

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[191] *See* Jerry W. Markham, *Federal Regulation of Margin in the Commodity Futures Industry—History and Theory*, 64 TEMPLE L. REV. 59, 105 n.335 (1991) (describing the differences between stock and commodity margin trading).

[192] *See id.* at 69.

[193] *See id*. at 66–99 (describing those debates).

[194] *See id.* at 91–99.

[195] *See* Pub. L. No. 97-444, § 225, 96 Stat. 2294, 2315–16 (1983). That authority could be invoked by the CFTC only during market emergencies. *See* Markham, *supra* note 191, at 94 n.232 (describing that legislation).

[196] *See* Markham, *supra* note 107, at 36–37 (describing that legislation).

[197] *See SEC Staff Crypto Advice*, *supra* note 135, at 13 n.14.

[198] *See* 474 F.2d 476 (9th Cir. 1973).

[199] *See id.* at 482. The Supreme Court took notice of this broadening of the "solely" requirement in United Housing Found., Inc. v. Foreman, 421 U.S. 837, 852 n.16 (1975).

the profits derived 'solely' from the efforts of others by including profits that come 'primarily,' 'substantially,' or 'predominantly' from the efforts of others."[200] That disparity further demonstrates that there is nothing clear about the application of the *Howey* test to cryptocurrencies.

In the case of Bitcoins and many other cryptocurrencies, participants in decentralized blockchain peer-to-peer transactions may operate more like a business partnership or a joint venture than as an investment contract.[201] To be sure, some participants may be more active than others. This raises the issue of whether the role of each participant must be analyzed to determine whether they have the requisite participation in management to make them something more than just passive investors.[202] The *SEC Staff Crypto Advice* tried to draw such a distinction by focusing on "Active Participants" (APs) in a blockchain as persons on whom others might depend for profits.[203] APs would include persons creating or maintaining a market in a digital asset, as opposed to "an unaffiliated, dispersed community of network users (commonly known as a "decentralized"

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[200] *See* Miriam R. Albert, *The Howey Test Turns 64: Are the Courts Grading This Test on a Curve?*, 2 WM. & MARY BUS. L. REV. 1, 19 (2011) (footnote omitted).

[201] *See* Metjahic, *supra* note 164, at 1554–62.

[202] *See SEC Staff Crypto Advice*, *supra* note 135, at 2–3. "A general partnership interest is presumed not to be an investment contract because a general partner typically takes an active part in managing the business and therefore does not rely solely on the efforts of others." *See* SEC v. Merchant Capital, LLC, 483 F.3d 747, 755 (11th Cir. 2007). In contrast, a passive participant's ownership interest in a partnership or in a limited liability company may be viewed to be a security. *See* James B. Porter, *Modern Partnership Interests as Securities: The Effect of RUPA, RULPA, and LLP Statutes on Investment Contract Analysis*, 55 WASH. & LEE L. REV. 955, 968 (1998) ("[L]imited partners' positions are analogous to those of corporate stockholders because limited partners have limited liability, cannot dissolve the partnership, cannot bind other partners, and have no authority to actively manage the partnership." (footnote omitted)). *See generally*, 2 LOUIS LOSS & JOEL SELIGMAN, SECURITIES REGULATION 961–63 (3d ed. 1989) (analyzing circumstances in which partnership interests may be securities); Elaine A. Welle, *Limited Liability Company Interests As Securities: An Analysis of Federal and State Actions Against Limited Liability Companies Under the Securities Laws*, 73 DENV. U. L. REV. 425, 446 (1996); Marc H. Morgenstern, *Real Estate Joint Venture Interests as Securities: The Implications of Williamson v. Tucker*, 59 WASH. U. L.Q. 1231, 1246 (1982).

[203] *See SEC Staff Crypto Advice*, *supra* note 135, at 2–3.

network).”[204] Again, this vague guidance does not reflect a clear authorization from Congress on how cryptocurrencies are to be regulated.

To date, there has been only limited judicial consideration of whether cryptocurrencies are securities under the *Howey* test.[205] None of those courts directly considered the major questions doctrine.[206] However, in *SEC v. Ripple Labs, Inc.*,[207] the district court denied an SEC motion to strike an affirmative defense, which asserted that the defendant’s due process rights were violated

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[204] *Id.* at 4. This guidance further asserted with respect to the “solely” requirement that:

> We recognize that holders of digital assets may put forth some effort in the operations of the network, but those efforts do not negate the fact that the holders of digital assets are relying on the efforts of the AP. That a scheme assigns “nominal or limited responsibilities to the [investor] does not negate the existence of an investment contract.” If the AP provides efforts that are “the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise,” and the AP is not merely performing ministerial or routine tasks, then there likely is an investment contract . . . . Managerial and entrepreneurial efforts typically are characterized as involving expertise and decision-making that impacts the success of the business or enterprise through the application of skill and judgment.

Id. at 13 n.16. *See generally* Henderson & Raskin, *supra* note 145, at 460–63 (proposing a “Bahamas Test” for determining whether a digital asset is sufficiently decentralized to avoid being classified as a security).

[205] *See* U.S. v. Zaslavskiy, No. 17 CR 647 (RJD), 2018 WL 4346339, at *4 (E.D.N.Y. Sept. 11, 2018) (a reasonable jury could determine that an ICO was an investment contract under the *Howey* test); SEC v. Shavers, No. 4:13-CV-416, 2013 WL 4028182, at *2 (E.D. Tex. Aug. 6, 2013) (Bitcoin investment promising daily interest was an investment contract under the *Howey* test); SEC v. Blockvest LLC, No. 18CV2287-GPB(BLM), 2019 WL 625163, at *7 (S.D. Cal. Feb. 14, 2019) (*Howey* test applied to find that an offering of digital tokens was a “security” transaction); Balestra v. ATBCOIN LLC, 380 F. Supp. 3d 340, 346 (S.D.N.Y. 2019) (applying the *Howey* test, the district court denied a motion to dismiss a class action which charged that an ICO of a digital asset was an illegal unregistered security); Audet v. Fraser, 605 F. Supp. 3d 372, 299 (D. Conn. 2022) (a jury acted unreasonably in finding that a cryptocurrency did not meet the *Howey* test).

[206] *See Zaslavskiy*, 2018 WL 4346339, at *4; *Shavers*, 2013 WL 4028182, at *2; *Blockvest LLC*, 2019 WL 625163, at *7; *Balestra*, 380 F. Supp. 3d at 346; *Audet*, 605 F. Supp. 3d at 399.

[207] *See* SEC v. Ripple Labs, Inc., No. 20 Civ. 10832(AT)(SN), 2022 WL 748150 (S.D.N.Y. Mar. 11, 2022).

because it lacked fair notice that dealings in digital tokens were in violation of the federal securities laws.[208] That seems to suggest that the SEC's authority to regulate the cryptocurrency space is not clearly evident.

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[208] *Compare* SEC v. Brigadoon Scotch Distrib. Co., 480 F.2d 1047, 1052 n.6 (2d Cir. 1973) (claim that the term "investment contract" was unconstitutionally void for vagueness rejected in "light of the many Supreme Court decisions defining and applying the term." (citations omitted)) *with* SEC v. LBRY, Inc., No. 21-cv-260-PB, 2022 WL 16744741 (D.N.H. Nov. 7, 2022) (the district court found that a token was offered as a security under the *Howey* test, and it struck an affirmative defense of selective enforcement. In fact, the SEC has been selective in its application of Section 17(b) to celebrity cryptocurrency endorsers). Among those not sued were actor Matt Damon and comedian Larry David who starred in Super Bowl advertisements touting cryptocurrency trading. *See* Ryan Smith, *Why Kim Kardashian Was Fined For Her Ad and Matt Damon Wasn't*, NEWSWEEK (Oct. 3, 2022, 12:43 PM), https://www.newsweek.com/why-kim-kardashian-was-fined-crypto-ad-matt-damon-wasn't-1748453 [https://perma.cc/ZCH2-J5KC]. Recently retired NFL star quarterback Tom Brady, an investor in FTX, made promotional advertisements for that platform. *See* Dan Jackson, *Why Larry David Was Awkwardly Shilling Crypto at the Super Bowl*, THRILLIST (Feb. 14, 2022, 4:29 PM), https://www.thrillist.com/entertainment/nation/super-bowl-crypto-commercials [https://perma.cc/EDZ4-7ZPU]; Kate Gibson, *Tom Brady and Larry David Among Those Accused of Defrauding Investors in FTX Collapse*, CBS NEWS (Nov. 18, 2022, 2:57 PM), https://www.cbsnews.com/news/ftx-tom-brady-gisele-bundchen-stephen-curry-larry-david-sam-bankman-fried-cryptocurrency-bankruptcy-fraud/ [https://perma.cc/DNS5-2LEE]; Jeff Beer, *Crypto Crash Draws Fresh Outrage Over Celebrity Endorsements That Didn't Age Well*, FAST CO. (May 12, 2022), https://www.fastcompany.com/90751640/crypto-crash-draws-fresh-outrage-over-celebrity-endorsements-that-didnt-age-well [https://perma.cc/64BN-SEHW]; Sead Fadilpašić, *Alec Baldwin Hired by eToro, But Baldwins Are Not New to Crypto*, CRYPTONEWS (Oct. 30, 2019, 7:20 AM), https://cryptonews.com/exclusives/alec-baldwin-hired-by-etoro-but-baldwins-are-not-new-to-cryp-4965.htm [https://perma.cc/7YYX-49NE]; Jen Wieczner, *What's the Deal With the Spike Lee Crypto Ad?*, N.Y. MAG.: INTELLIGENCER (July 16, 2021), https://nymag.com/intelligencer/2021/07/whats-the-deal-with-the-spike-lee-crypto-ad.html [https://perma.cc/C4SQ-66FU]; Jade Scipioni & Cameron Albert-Deitch, *Shaq Distances Himself From Crypto and FTX Collapse: 'I Was Just a Paid Spokesperson,'* CNBC, https://www.cnbc.com/2022/12/15/shaq-on-crypto-ftx-post-collapse-i-was-just-a-paid-spokesperson.html [https://perma.cc/937H-HGQK] (Dec. 19, 2022, 3:48 AM). Several of those celebrities have been targeted in a class action lawsuit. Corinne Ramey et al., *Celebrities Who Endorsed Crypto, NFTs Land in Legal Crosshairs After Investor Losses*, WALL ST. J., https://www.wsj.com/articles/celebrities-who-endorsed-crypto-nfts-land-in-legal-crosshairs-after-investor-losses-11675097150 [https://perma.cc/Y9HB-CNFX] (Jan. 30, 2023, 12:34 PM).

Conclusion

The SEC is running afoul of the major questions doctrine in seeking to unilaterally regulate cryptocurrency transactions through enforcement actions and staff declarations. The cryptocurrency market has major economic and political significance, and the SEC has not clearly been empowered by Congress to regulate that market. Instead, the agency is relying on the vague standards in the *Howey* decision that were formulated over seventy-five years ago in a completely different context.[209] That decision was written decades before the appearance of blockchain technology or even computers.[210] The subtle differences between securities, on the one hand, and Bitcoins, DAO-like tokens and other cryptocurrencies, on the other, needs to be sorted out by Congress through express language or by delegating specific rule-making authority to what it deems to be the appropriate agency or agencies.

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[209] *See supra* Section II.A.1.

[210] *See* S.E.C. v. W.J. Howey Co., 328 U.S. 293, 301 (1946); Timothy Williamson, *History of Computers: A Brief Timeline*, LIVE SCI., https://www.livescience.com/20718-computer-history.html [https://perma.cc/W5TD-DDKJ] (Jan. 25, 2022).