



SEC Chair Warns of Increased Enforcement and Oversight of Crypto Assets

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Industry professionals are keeping tabs on the regulation of crypto assets, as the U.S. Securities and Exchange Commission (SEC) turns its attention to the burgeoning asset class. A pair of prepared remarks delivered by SEC Chair Gary Gensler over the past few months underscore the SEC's commitment to enforcement and increased regulatory oversight of crypto assets.

On November 4, 2021, Chair Gensler provided [prepared remarks at the Securities Enforcement Forum](#) that emphasized enforcement as a “fundamental pillar in achieving the SEC’s mission” to protect investors. Chair Gensler outlined certain principles the SEC Division of Enforcement (the Enforcement Division) will consider as it investigates misconduct and makes recommendations to the Commission as the SEC further investigates the world of digital tokens and cryptocurrencies.

Under Chair Gensler’s guidance, the Enforcement Division will be looking at “the underlying economic realities” of each product, instrument, or arrangement rather than taking words at face value. Chair Gensler stated that “[w]hen I see a bird that walks like a duck and swims like a duck and quacks like a duck, I call that bird a duck.” With that image in mind, Chair Gensler followed with a warning for lawyers, accountants and financial advisers alike to “think about the spirit of the law” instead of searching for some ambiguity in the text or a footnote”—adding that searching for such technicalities and “going right up to the edge of a rule” may be inconsistent with the law’s purpose of protecting investors.

The Enforcement Division has been instructed to seek admissions of misconduct by wrongdoers “where heightened accountability and acceptance of responsibility are in the public interest.” Chair Gensler highlighted that the Enforcement Division will pursue “high-impact cases” that “send a message to the rest of the market” with an aim to “change behavior.” Notably, he enumerated a specific list of such high-impact cases that included “crypto.”

Chair Gensler’s November comments follow his statements in August 2021 when he addressed the SEC’s jurisdiction over crypto assets and technology in [prepared remarks before the Aspen Security Forum](#). Chair Gensler called for increased investor protection with regards to crypto assets, which he described as “like the Wild West” in the potential for fraud and abuse in certain applications, the aggressive marketing and spin with respect to how crypto-based assets work, and the lack of “rigorous balanced and complete information” for investors.

Chair Gensler’s November statements come in the wake of the recently speculated “rug pull” scandal that saw more than 40,000 investors in a Squid Game–inspired cryptocurrency (but which had no actual affiliation with the series of the same name) left holding the bag after the token soared 23 *million* percent before becoming worthless in a matter of minutes. Between October 26 and November 1, the popularized token rose in value from a mere cent to almost \$2,900. However, in a ten-minute span on November 1, investors saw the token’s value crash from nearly \$2,900 to \$0.0007 as the cryptocurrency’s anonymous founders cashed-out their holdings of the token rendering it worthless—all before seemingly vanishing into the ether. Many commentators are alleging that this was a “rug pull” scam as the token’s website and social media channels were mysteriously taken down and emails to its developers bounced back as undeliverable once the crash occurred. The Squid Game token crash brings attention to the kind of regulatory gaps that Chair Gensler hopes the Enforcement Division will be able to fill-in in the name of protecting investors.

According to Chair Gensler, many crypto tokens are offered and sold as securities, which according to the Howey test, constitute investment contracts when “a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party.” Chair Gensler said the SEC’s focus in this regard would continue to be on certain platforms that “offer crypto tokens or other products that are priced off of the value of securities and operate like derivatives.”

Another point of emphasis for the Enforcement Division will be “crypto trading platforms, lending platforms, and other ‘decentralized finance’ (DeFi) platforms.” Trading platforms typically offer more than 50 tokens and allow people to trade tokens and, in some cases, lend tokens. To the extent that securities are offered on such platforms, Chair Gensler asserts that such crypto assets and platforms would fall within the jurisdiction of the SEC and that the Enforcement Division will make it a priority to monitor the operations of such platforms and leverage prophylactic remedies—like bars and injunctions when necessary to stamp out fraud, manipulation, and abuse, in the name of instilling trust in the markets.

Chair Gensler concluded his remarks before the Aspen Security Forum by suggesting that “legislative priority should center on crypto trading, lending, and DeFi platforms” in order to bring “the field of crypto” within regulatory frameworks similar to those already in existence for traditional securities.

Capital Markets Watch will continue to monitor developments in this area and will provide our readers with updates.

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Authors

Michael J. Blankenship

J. Eric Johnson

John P. Niedzwiecki

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