

SEC and the NYDFS Take Aim at Paxos

FEBRUARY 21, 2023

On February 13, 2023, Paxos Trust Company, LLC (Paxos), a New York State-chartered trust company regulated by the New York State Department of Financial Services (the Department), confirmed via a [statement](#) that it received a Wells Notice from the Securities and Exchange Commission (SEC) on February 3, 2023 (the Notice). (Through the Wells notice process, the SEC informs the recipient that it intends to bring an enforcement action and provides an opportunity for the recipient to respond before any formal charges are brought.)

While the Notice is not public, Paxos confirmed its existence and indicated that the Notice focuses on allegations that its stablecoin, BUSD, is a security under U.S. law. A “stablecoin” is a digital asset that is pegged to a “stable” reserve asset like the U.S. dollar or gold. Stablecoins are designed for purposes such as facilitating fast and efficient payment in online transactions.

In its statement, Paxos categorically disagreed with the SEC and maintained that BUSD is not a security.

Separately, on February 13, 2023, the Department also [announced](#) that it ordered Paxos to cease minting Paxos-issued BUSD because of several unresolved issues related to Paxos’ oversight of its relationship with Binance in relation to BUSD. Paxos [notified](#) its customers of its intent to end its relationship with Binance for BUSD, effective February 21, 2023, and clarified that BUSD will always be backed 1:1 with U.S. dollar-denominated reserves, fully segregated and held in bankruptcy remote accounts.

Although the full scope of the investigations is unclear, this activity is significant because it represents escalating efforts to regulate the digital asset industry. Specifically, this move represents one of the SEC’s first indications of an enforcement action involving stablecoins, and it may signal a wider probe of stablecoins, generally. Stablecoins were previously in the news with the rapid [collapse of TerraUSD \(UST\)](#) in September 2022, but many observers differentiated UST because it fell within the riskier category of “algorithmic” stablecoins, which are not backed by any reserve assets.

The SEC has not yet commented on the matter or provided insight as to why it regards BUSD as a security.

Please contact your Winston relationship partner should you have any questions or to request further information. We will continue to monitor developments and provide friends of the firm with updates as they become available.

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Authors

[Sabrina Rishmague](#)

[Kimberly A. Prior](#)

[Daniel T. Stabile](#)

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Sabrina Rishmague



Kimberly A. Prior



Daniel T. Stabile

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