



Crypto Regulation and Policy

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November 2, 2022

About Me



Presently

- Head of Policy @ Blockchain Association
- Lawyer, but not yours
- Advisor @ Variant Fund / Board @ DeFi Education Fund

Formerly

- General Counsel @ Compound Labs, Inc.
- Government Enforcement Defense @ Kobre & Kim LLP
- Compliance and Investigations @ Baker McKenzie LLP

Futurely

- Happy to hear from you — jake@variant.fund / [@jchervinsky](https://twitter.com/jchervinsky)



Roadmap

- 1) **Introduction**
- 2) **Regulators and Frameworks**
- 3) **Current Issues and Priorities**
- 4) **Crypto Policy Infrastructure**
- 5) **Questions?**



Basics of Regulation

What are regulations?

- Rules that either prohibit conduct or condition it on compliance with specific obligations, and that call for the punishment of violators

Why do we have them?

- “The market cannot be left to its own devices”
- To control market power, facilitate competition, promote stability, attract investment, protect consumers, and achieve other governmental interests
- Also, sometimes, for wealthy incumbents to engage in regulatory capture

Are they good or bad?

- It depends on your economic philosophy!
- The devil is always in the details



Basics of Regulation

Who makes and enforces regulations?

- The US has regulations on both the state and federal level
- Legislature makes laws, executive enforces laws, judiciary interprets laws
- Elected vs. appointed officials; policymakers vs. enforcers

Where are they codified?

- United States Code (USC) and Code of Federal Regulations (CFR)
- Other administrative materials: guidance, settlements, no-action letters, etc.
- Unique systems in all fifty states, not to mention other countries

How should you think about them?

- Learn the basics for issue-spotting and use your common sense
- Hire a lawyer before you do anything risky!



Regulators and Frameworks

- 1) Introduction
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Jake Chervinsky ✓

@jchervinsky



Major US regulators for crypto:

- SEC (securities, exchanges, funds...)
- CFTC (derivatives, margin trading...)
- DOJ (crimes...)
- FINRA (brokers...)
- FinCEN (money laundering...)
- OFAC (sanctions...)
- CFPB (consumers...)
- OCC (banks...)

And they're just getting started.

11:21 PM · Dec 5, 2018 · Twitter Web Client

Securities Laws



The Securities and Exchange Commission (“SEC”)

- The SEC has a three-part mission: to protect investors, facilitate capital formation, and maintain fair, orderly, and efficient markets
- The federal securities laws originated in the 1930s after the Great Depression, which was thought to be caused by financial abuse and information asymmetry
- The SEC regulates “securities” and a broad range of securities market actors, including issuers, exchanges, advisers, brokers, dealers, investment firms, etc.

Crypto x Securities

- Securities are subject to burdensome regulatory requirements that don’t work with crypto; they have to be registered with the SEC (as in an IPO), traded on SEC-regulated venues, held by SEC-approved custodians, etc.
- Because a securities designation is a death blow for most digital assets, the crypto industry spends a lot of time and money avoiding SEC regulation



Securities Laws

Investment Contracts and the *Howey* Test

- Many types of securities: stocks, bonds, notes, investment contracts, etc.
- SCOTUS defined an investment contract in *SEC v. W.J. Howey Co.* (1948):
 - (1) an investment of money
 - (2) in a common enterprise
 - (3) with a reasonable expectation of profit
 - (4) based on the efforts of others

Regulation by Enforcement

- Bill Hinman, June 2018: bitcoin and ether are “sufficiently decentralized”
- Framework, April 2019: dozens of factors relevant to “efforts of others”
- Since then, the SEC has undertaken a pattern of regulation by enforcement under Chair Gary Gensler, who claims that the “vast majority” of digital assets are securities and that the law on *Howey* is clear (without further explanation)



Jake Chervinsky @jchervinsky · Mar 16

The SEC's tactics of regulation by enforcement are both harmful to the crypto industry & counterproductive to the SEC's own mission. My thanks to @RepTomEmmer & this amazing bipartisan group of leaders in Congress for investigating the SEC's enforcement practices 🌞



Tom Emmer @RepTomEmmer · Mar 16

This is why I sent a bipartisan letter today to SEC Chair @GaryGensler with @RepDarrenSoto, @WarrenDavidson, @RepAuchincloss, @RepDonaldsPress, @RepJoshG, @RepTedBudd, and @RepRitchie regarding the SEC's crypto information seeking process.

[Show this thread](#)

152

200

945



Jake Chervinsky @jchervinsky · Jul 22

1/ The SEC filed a complaint yesterday accusing ten companies of violating the securities laws: nine digital asset issuers & one exchange.

None of them are defendants in the case. None of them will get their day in court.

If this isn't regulation by enforcement, nothing is 📖

372

1,250

3,567



Jake Chervinsky @jchervinsky · Oct 28

Replying to @jchervinsky

2/ From our introduction and summary of argument:

“SEC Chair Gary Gensler recently opined, without significant explanation, that the ‘vast majority’ of tokens are securities. Put simply, that view should not be—cannot be—the law.”

Read the brief here: theblockchainassociation.org/wp-content/upl...

9

88

731



Commodities Laws



The Commodity Futures Trading Commission (“CFTC”)

- The CFTC's mission is to promote the integrity, resilience, and vibrancy of US derivatives markets: futures, options, swaps, etc.
- The CFTC was created in 1974 when most futures trading occurred in agricultural markets and is still overseen by the House and Senate Ag Committees
- The CFTC's role and responsibilities greatly expanded after the Global Financial Crisis under the Dodd-Frank Act due to the impact of complex financial derivatives

CFTC vs. SEC “Turf War”

- Are digital assets securities (SEC) or commodities (CFTC)?
- The battle for jurisdiction over crypto spot markets: Gensler vs. Behnam
- General industry preference for CFTC given commodity-like characteristics of digital assets and historically “pro-crypto” positions — until Ooki DAO

Anti-Money Laundering Laws



The Financial Crimes Enforcement Network (“FinCEN”)

- FinCEN enforces the Bank Secrecy Act (“BSA), our anti-money laundering / countering the financing of terrorism (“AML/CFT”) laws
- The BSA requires regulated financial institutions to comply with certain AML compliance program requirements, including “know your customer” (“KYC”)
- This includes centralized crypto institutions like exchanges and custodians

Crypto x AML

- In essence, the BSA deputizes financial intermediaries to perform the task of surveilling our transactions and reporting on them to the government
- How does the BSA work in a disintermediated financial system like crypto?

“The right of the people to be secure in their persons, houses, papers, and effects, against unreasonable searches and seizures, shall not be violated...”

Sanctions Laws



The Office of Foreign Assets Control (“OFAC”)

- Sanctions are a foreign policy tool used to influence the behavior and diminish the capabilities of foreign actors through economic penalties
- OFAC administers US sanctions by designating specific targets on the Specially Designated Nationals (“SDN”) List, who are then cut off from the US markets: it’s illegal for any US person to transact with anyone on the SDN List

Crypto x Sanctions

- Because sanctions laws are so broad, violations are strict liability offenses, and crypto is borderless by nature, sanctions compliance is paramount
 - Bittrex: \$24m settlement in 2022 for violations from 2014-2016
 - Virgil Griffith: 63 months imprisonment for assisting North Korea
- Policymakers think crypto is particularly useful for sanctions evasion (it isn’t), with the exception of Lazarus Group generating revenue via DeFi hacks



Tax Laws

Internal Revenue Service (“IRS”)

- The IRS is responsible for collecting US federal taxes and administering the US Tax Code, including how it applies to digital assets
- There are many unanswered questions about how crypto should be taxed:
 - Mining and staking?
 - Hard forks and airdrops?
 - DeFi transactions and interest income?

Infrastructure Bill

- Last year, the Infrastructure Investment and Jobs Act (“IIJA”) amended the Tax Code with five new provisions specific to crypto — all problematic
 - KYC through the back door of the Tax Code
 - We are awaiting guidance or rulemaking on implementation



And on, and on, and on

Alphabet Soup

- There are many other US regulatory frameworks relevant to crypto:
 - Consumer Protection Laws (CFPB, FTC)
 - Banking Laws (Fed, FDIC, OCC)
 - Unique State Regimes (NY BitLicense, WY SPDI)

President Biden's Executive Order ("EO")

- In March, POTUS issued an EO identifying crypto's benefits and risks, and assigning agencies to study and write reports on them
- In September, POTUS released a "comprehensive framework for responsible development of digital assets" based on those reports
- Industry reaction: disappointment at failure to appreciate benefits, overemphasis on risks, and lack of a clear path forward





Current Issues and Priorities

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Current Issues and Priorities

- 1) **Privacy after Tornado Cash**
 - Does OFAC have the authority to make software illegal in the US?
- 2) **Stablecoins after Terra**
 - Will centralized stablecoins get preferential treatment due to UST?
- 3) **DAOs after Ooki**
 - Are DAO voters personally liable for operating DeFi protocols?
- 4) **DeFi after Lazarus**
 - Can DeFi stay permissionless despite concerns about illicit finance?
- 5) **DCCPA, RFIA, DCEA, etc.**
 - Will Congress grant the CFTC jurisdiction over crypto spot markets?
- 6) **Politics!**
 - How will the midterms change the outlook for US crypto policy?



Crypto Policy Infrastructure

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Navigating Crypto Regulation

Law Firms

- US-based crypto companies have to budget a lot of money for legal fees to address the heightened regulatory risk that comes with working in this field
- Law firms help companies reduce the likelihood of violating regulations by avoiding regulated activity or by satisfying compliance obligations; they also defend companies in government investigations and enforcement actions
- Crypto startups also tend to hire in-house counsel earlier than most others

Policy Professionals

- In recent years, the industry has invested heavily in dedicated policy organizations and full-time in-house roles
- Most large US crypto companies are members in either the Blockchain Association or the Crypto Council for Innovation, and also have their own policy or government relations department

Blockchain Association Members





Digital Rights Advocacy

A Cypherpunk's Manifesto

- Crypto is more than just business — it has the potential to profoundly impact how much *freedom* we enjoy in our digital lives, and to restore what we've sacrificed to Web2 architecture and incumbents (okay, I'll stop preaching)

Civil Society Organizations

- Because of crypto's promise for individual liberty and self-sovereignty, digital rights advocacy groups like the Electronic Frontier Foundation and Fight for the Future have taken an interest in crypto-related policy issues
- Coin Center is the leading independent nonprofit focused on crypto

Grassroots Activism

- Crypto is lucky to have an extremely passionate community of builders and users willing to make their voices heard in favor of good crypto policy — I hope you'll be one of them too!



Questions?