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THEBLOCK.CO

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# TRENDS IN REGULATION OF DIGITAL ASSETS

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# OVERVIEW

The Block Research's Trends in Regulation of Digital Assets report provides an extensive analysis of the regulatory landscape and enforcement actions surrounding cryptocurrencies in the United States and various international jurisdictions. The aim is to understand the complexity of regulations, asset classification, and the impact on crypto-related businesses and third parties. The report is structured into four main sections:

## **Part 1: Introduction**

The report begins with an introduction outlining the importance of understanding the regulatory environment for cryptocurrencies. The growing popularity of digital assets has led to increased scrutiny from regulatory bodies worldwide and many jurisdictions have been focusing on developing appropriate frameworks in recent years.

## **Part 2: United States - State of Regulation and Enforcement Actions**

This section delves into the regulatory complexities in the United States, covering the current regulatory focuses, including enforcement direction, asset classification uncertainties, and the differing approaches of regulatory bodies. The report also examines the impact of regulation by enforcement, recent banking uncertainty faced by crypto firms, and the repercussions of these developments on crypto-associated third parties.

## **Part 3: International Jurisdictions - Crypto Regulation Landscape**

This section explores the regulatory landscape in several international jurisdictions, covering noteworthy trends in the Middle East, European Union, United Kingdom, Asia and Latin America. Global regulators have responded to significant crypto-related incidents in 2022 by actively developing and updating regulatory frameworks for crypto-assets. The focus is on achieving a balanced approach that brings clarity to businesses and market participants. This includes delegating regulatory authority to specific agencies, setting clear boundaries, and emphasizing the regulation of stablecoins. The report also recognizes the need for further development in addressing crypto-native concepts like DeFi regulations.

## **Part 4: Conclusions and Outlook:**

The report concludes by summarizing the key findings and highlighting three potential industry developments: a focus on safer assets, a reduction in U.S. exposure, and the segregation of activities.

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- Mitzi Chang (Partner, Goodwin Procter LLP)
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Disclaimer: While this report aims to provide a comprehensive overview of the global digital assets regulation, entity names and certain identifying information have been redacted from the report.

# PART 1

## INTRODUCTION

Crypto-assets have emerged as a new frontier in the financial ecosystem, characterized by rapid innovation and decentralization. In recent years, institutional and retail adoption has accelerated the expansion of the crypto-assets space, leading to increased scale and complexity. This growth has underscored the immediate need for comprehensive global regulations that prioritize consumer protection and safeguards financial stability.

The recent mismanagements in the crypto space have shed light on the risks associated with crypto-assets and related services, prompting global jurisdictions to hasten their efforts to bring clarity to this domain in 2023. However, designing and implementing effective regulatory frameworks for digital assets pose significant challenges. Traditional regulatory approaches often struggle to capture the unique nuances and intricacies of this emerging asset class. Furthermore, the digital asset landscape encompasses a wide range of products, services, and market participants, further complicating the regulatory process. Each segment within the digital asset ecosystem, including cryptocurrencies, non-fungible tokens (NFTs), exchanges, metaverse and wallets, presents its own distinct regulatory considerations.

The emergence of crypto-assets has prompted jurisdictions worldwide to adopt varied approaches to address the associated challenges. While some jurisdictions have proactively published comprehensive regulatory frameworks, others have taken a more reactive enforcement approach. In the subsequent sections of this report, we aim to shed light on the ongoing discussions and efforts aimed at advancing crypto regulations. We delve into the state of crypto-asset regulation in the United States, examining noteworthy regulatory developments and enforcement actions. Additionally, we look into the regulatory approaches and actions taken by international jurisdictions (Middle East, European Union, United Kingdom, Asia, Latin America), offering a global perspective on the regulation of this dynamic and rapidly evolving asset class. Through a thorough exploration of diverse regulatory landscapes and initiatives, this report strives to provide a comprehensive understanding of the dynamic regulatory environment surrounding crypto-assets.

# PART 2

# UNITED STATES

STATE OF REGULATION AND ENFORCEMENT ACTIONS



While some global regions are proactively engaging in formal rulemaking processes, the U.S. regulatory approach has been a combination of a case-by-case approach (referred to as “regulation by enforcement” within the crypto industry) and the expansion of existing traditional financial market frameworks, which has not fully addressed the uniqueness of this emerging technology. Justin Browder, a Partner at Willkie, emphasizes that the U.S. has historically been a reactive regulator, “implementing frameworks provided by Congress rather than anticipating innovation.” Browder states, “[we] have new technologies that are working [a certain] way and [we] have regulators applying existing frameworks to try to capture the activity where it might not fit perfectly well.” He adds “it’s frustrating for us because our clients are experiencing the same thing that all sorts of ecosystem participants are experiencing – it’s tough to innovate without the fear of potential regulatory retribution, but it’s sort of all by way of the technology working its way through the system, and in the same manner that new innovation in financial services has worked.” As crypto companies prepare for U.S. regulatory enforcement, they should consider current regulatory focuses, including enforcement direction, asset classification uncertainties, and the differing approaches of regulatory bodies.

## 2.1 REGULATORY COMPLEXITY AND ASSET CLASS AMBIGUITY

Mitzi Chang, a Partner at Goodwin Procter, highlights that the key regulatory challenge in the U.S. is “the overlapping and complex nature of existing laws and regulations.” Digital assets are subject to multiple federal and state-level agencies, each treating them differently based on their function. This results in an interpretive approach for reporting, Money Transmitter Licenses, and registration for Money Services Businesses. The Internal Revenue Service treats them as property for tax purposes. The Financial Crimes Enforcement Network (FinCEN) enforces anti-money laundering (AML) and know-your-customer (KYC) protocols, considering digital assets as money. The Commodity Futures Trading Commission (CFTC) is examining how digital assets can be categorized as commodities, while the Securities and Exchange Commission (SEC) primarily classifies them as securities. The Biden Administration’s Executive Order also introduces its own definitions. While there are state-level licenses, compliance with state agencies hasn’t shielded companies from federal agency scrutiny. Robert Musiala, a Partner at BakerHostetler and co-leader of the firm’s Blockchain Technologies and Digital Assets practice, states that “every agency is genuinely trying to enforce its mandate, and there’s going to be some natural tension and ambiguity regarding the boundaries of each agency’s jurisdiction.” Unless Congress intervenes with a new legislation, this complex situation is likely to persist.

## 2.1.1 STATE-LEVEL DEVELOPMENTS

Crypto regulation in the U.S. has evolved at the state level since the early 2010s, resulting in a fragmented regulatory landscape. Meagan Griffin, a Counsel at Paul Hastings, states that there has been a regulatory regime for crypto entities for nearly as long as they have existed, contrary to the perception of being unregulated until SEC enforcement in 2017-2018. FinCEN issued guidance in 2013, introducing the Money Services Business regime for administrators and exchangers of virtual currency. This prompted state banking departments and regulatory agencies to create their own frameworks.

Many legal experts highlight New York's BitLicense regime (the first detailed state licensing regime for the digital asset sector) as a key example of this development. Musiala states that "despite not receiving as much attention, the BitLicense has continued to evolve and the New York State Department of Financial Services has been building its industry knowledge and establishing a state-based regulatory framework that is the most complex and nuanced among all states. It wouldn't be surprising to see other states follow suit and implement their own state-based regulations."

Mike Selig, a Counsel at Willkie, indicates that in the absence of comprehensive SEC guidance, crypto financial services have developed within the Money Services Business regime – firms obtained state licenses, pursued trust charters, and registered as Money Services Businesses. However, recent SEC enforcement actions have shown that state licenses do not provide complete immunity from regulatory scrutiny, underscoring the importance of additional legal considerations.

## 2.1.2 ASSET CLASSIFICATION

Federal agencies, particularly the SEC and the CFTC, are in a debate over the classification of digital assets (excluding BTC, recognized as a commodity by the [SEC](#) and the [CFTC](#)). Browder highlights the differing approaches of the CFTC and the SEC in their enforcement actions within the crypto industry – the CFTC has acknowledged the utility of crypto market participants, while the SEC has expressed skepticism about the asset class and its suitability for retail investors. He states that recent CFTC enforcement cases support innovation in financial markets, whereas certain SEC policy initiatives (driven by the Chairman and Democratic lawmakers) push for alignment with traditional financial services.

The SEC's classification of digital assets as securities is opposed by crypto-natives due to the strict regulatory rules it entails. Clear asset classifications can benefit investors and regulated entities, but uncertainties persist in applying securities laws to crypto networks and tokens (e.g.

disclosure agreement, issue of decentralization). Without a unified framework, the development of long-term product strategies can be a significant challenge for investors and entrepreneurs. Many crypto entities have noted their preference of a strict regulation over a state of ambiguity. While the regulatory direction remains uncertain, there are various pathways to clarity:

1. Congress proposing new laws (notable developments shown in figure 1 below)
2. Creating a single self-regulatory organization (SRO) with combined jurisdiction of SEC and CFTC for supervising the crypto markets (new legislation not required)
3. Maintaining enforcement under current laws
4. Enhancing oversight of the federal rulemaking process – President Biden's Executive Order aims to improve and modernize the regulatory review process

**Figure 1: U.S. Crypto Bills - Notable Developments**

Proposal	Date	Proposer	Proposal Summary
Responsible Financial Innovation Act	6/7/22	<ul style="list-style-type: none"> <li>Senator Kirsten Gillibrand (D-NY; member of the Senate Agriculture Committee)</li> <li>Senator Cynthia Lummis (R-WY; member of the Senate Banking Committee)</li> </ul>	<ul style="list-style-type: none"> <li>Bill creates a regulatory framework for digital assets, addressing the uncertainty surrounding the jurisdiction of financial regulators, providing clarity on the taxation of digital assets &amp; DAOs, and establishing guidelines for disclosures and consumer protection obligations for issuers and service providers of digital assets</li> <li>Reflects Congress' efforts to modernize federal law in response to the rise of digital assets</li> <li>State of Proposal: Senator Lummis expressed interest in the 2023 Digital Asset Market Structure Proposal, saying she and Senator Gillibrand were pausing reintroduction to see what came in the House Republican document</li> </ul>
Digital Asset Anti-Money Laundering Act of 2022	12/13/22	<ul style="list-style-type: none"> <li>Senator Elizabeth Warren (D-MA)</li> <li>Senator Roger Marshall (R-S)</li> </ul>	<ul style="list-style-type: none"> <li>Legislation seeks to enforce KYC rules for crypto participants and prohibits financial institutions from engaging with digital asset mixers to obscure fund origins (grants authority to the FinCEN to introduce a reporting rule for specific transactions)</li> <li>Opponents of the bill contend that it imposes unattainable expectations on the crypto industry, as the legislation classifies nearly every component of a blockchain network (e.g., unhosted wallet providers, miners, validators, node operators, and "other validators with control over network protocols") as money service businesses that must register with the FinCEN</li> <li>State of Proposal: senators have delayed its reintroduction to find more co-sponsors</li> </ul>
Digital Commodities Consumer Protection Act of 2022	8/3/22	<ul style="list-style-type: none"> <li>Chairwoman Debbie Stabenow (D-MI; Senate Committee on Agriculture, Nutrition, and Forestry)</li> <li>Senator John Boozman (R-AR)</li> <li>Senator Cory Booker (D-NJ)</li> <li>Senator John Thune (R-SD)</li> </ul>	<ul style="list-style-type: none"> <li>Proposes that entities seeking to operate as digital commodities platforms must register with the CFTC as brokers, custodians, dealers, or trading facilities; digital commodity platforms would be classified as financial institutions under the Bank Secrecy Act, requiring them to assist in detecting and preventing money laundering</li> <li>A new draft of the bill has been released to the public, providing relief to crypto stakeholders – the draft excludes software developers from being classified as digital commodity brokers, addressing previous concerns about potential restrictions on DeFi</li> <li>Opponents of the bill contend that the bill expands the definition of a commodity and narrows the definition of a security, potentially limiting the authority of the SEC and hindering its ability to combat fraudulent activities in the crypto space</li> </ul>
Digital Asset Market Structure Proposal	6/2/23	<ul style="list-style-type: none"> <li>Chairman Patrick McHenry (R-NC; House Financial Services Committee)</li> <li>Chairman Glenn Thompson (R-PA; House Agriculture Committee)</li> </ul>	<ul style="list-style-type: none"> <li>A discussion draft of legislation to establish a statutory framework for digital asset regulation - "first step toward delivering on Republicans' commitment to develop clear rules of the road for the digital asset ecosystem"</li> <li>Joint effort aiming to close existing authority gaps between the CFTC and SEC</li> <li>The bill would give a clear definition as to when a project is sufficiently decentralized to no longer have its tokens qualify as investment contracts (providing a path for a digital token to go from being treated as a security to a commodity)</li> </ul>
Clarity for Payment Stablecoins Act	7/20/23	<ul style="list-style-type: none"> <li>Chairman Patrick McHenry (R-NC; House Financial Services Committee)</li> </ul>	<ul style="list-style-type: none"> <li>Aiming to establish the first U.S. regulations for stablecoins, the bill mandates bank-like regulations for stablecoin issuers, covering disclosure of reserves, audit standards, liquidity controls, risk management, activity limits, and broad supervision</li> <li>The bill assigns primary oversight to state regulators for state stablecoin issuers, with the Federal Reserve Board having backup authority for urgent situations</li> <li>The bill clarifies that stablecoins are not securities or commodities, removing stablecoin issuers from the SEC's jurisdiction</li> <li>The U.S. House of Representatives passed the Clarity for Payment Stablecoins Act in August (challenges persist in Senate passage)</li> </ul>

Source: The Block Research, Financial Services Committee, Congress.gov, Senate.gov

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**Figure 1: U.S. Crypto Bills - Notable Developments**

While there has been some progress in U.S. crypto bills, Nicholas Losurdo, a Partner at Goodwin Procter, raises concerns about pending U.S. crypto legislation. He emphasizes the need for greater collaboration between the SEC and Congress to ensure effective bills and thoughtful rulemaking. Clear communication and consultation are seen as vital for enacting laws that promote prudent regulation. Losurdo also highlights the challenges faced by advisors and industry stakeholders due to the lack of clear timelines and compliance requirements.

## 2.2 REGULATION BY ENFORCEMENT

Regulation by enforcement is a reactive strategy where enforcement actions are used to clarify and impose regulatory standards, rather than relying on rulemaking or guidance. In the context of the crypto industry, the SEC has utilized this approach by defining crypto-assets as securities and leveraging existing regulatory frameworks, such as the Securities Act of 1933 (regulates the issuance of securities) and the Securities Exchange Act of 1934 (regulates the secondary trading of securities), to justify enforcement actions. The SEC's powers include private investigations, civil litigation, administrative proceedings, and criminal referrals to the Department of Justice. The SEC's use of litigation has been a prominent feature in its relationship with the crypto industry, generating debate over regulatory clarity and fairness.

A. Kristina Littman, a Partner at Willkie, points out that "rather than proposing new crypto-specific guidelines, the SEC has attempted to make crypto fit into existing regulatory frameworks or statutes." To date, the SEC has been investigating crypto markets, initially targeting Initial Coin Offerings that were considered unregistered securities offerings against the Securities Act of 1933. In response, crypto projects adjusted their strategies by selling tokens to accredited investors and utilizing Simple Agreements for Future Tokens for future utility tokens not classified as securities. Recent enforcement actions have introduced a new theory that assets are deemed securities during secondary market trading based on the reliance of current investors on the efforts and profit expectations of associated individuals (requirement of the Howey Test). The SEC has expanded its scrutiny to unregistered crypto broker-dealers, exchanges, and intermediaries, urging them to register with the SEC.

The SEC is concerned about crypto platforms offering multiple services without proper separation, leading to conflicts of interest and inadequate supervision. To register with the SEC, companies must meet various requirements, such as regulatory filings, business conduct standards, customer protection rules, minimum net capital, AML program implementation, record maintenance, written policies and client disclosures. There are disagreements between the SEC and crypto companies regarding the clarity and feasibility of this registration process.



Despite industry complaints about “regulation by enforcement,” the SEC asserts that existing regulations provide sufficient clarity and attributes non-compliance to deliberate decisions made by crypto companies. Losurdo notes, “the agency believes there is no need for significant changes as it already possesses the required constructs and constraints. However, the agency’s limited participation in industry dialogues has resulted in capital outflow, with institutions increasingly investing outside the U.S.”

## 2.2.1 ENFORCEMENT STATISTICS AND KEY DEVELOPMENTS

**Figure 2: Number of SEC Cryptocurrency Enforcement Actions 2013 – 2023 YTD**



1: SEC's administrative proceedings refer to internal processes conducted before administrative law judges (ALJs) to enforce securities laws. The SEC acts as the prosecutor and the ALJ makes findings and decisions.

2: SEC's litigations refer to legal actions brought before federal courts, involving alleged violations of securities laws. The SEC acts as the plaintiff and the case is presented before a judge or jury.

Source: Cornerstone Research, SEC.gov, The Block Research.

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**Figure 2: Number of SEC Cryptocurrency Enforcement Actions 2013 - 2023 YTD**

The SEC, under the direction of Chair Gary Gensler, has been increasing its enforcement unit. In May 2022, the SEC nearly doubled its size (50 positions) of the Crypto-Assets and Cyber Unit in the Division of Enforcement. In March 2023, Gensler announced that the team will continue to hire as the enforcement efforts ramp up. In 2022, the SEC issued 30 cryptocurrency-related enforcement actions (24 litigations and six administrative proceedings) against 79 defendants/respondents in 2022. This was a 50% increase from 2021 and the highest number since 2013. Of the 30 enforcement actions, 70% alleged fraud, 73% alleged an unregistered securities offering violation, and 50% alleged both. The SEC is on track to eclipse its 2022 cryptocurrency enforcement action. Figure 2 shows that there have been 15 crypto-assets litigations filed by the SEC as of June 2023.

In 2023, major crypto exchanges encountered charges as enforcement measures escalated. Selig believes that this issue goes beyond exchange compliance, and can almost be viewed as “an existential battle for the industry...as [the products] simply can’t work within the context of the securities laws.” Selig argues that adhering to the SEC’s regulations would obstruct the design and functionality of blockchain networks, which rely on the essential aspect of having tokens that can be freely transferred.

Another notable development is the recent ruling on the case involving unregistered security offerings. In 2020, the SEC took legal actions against a company that developed a money transfer network, arguing that its native token should be considered a security. In July 2023, the judge ruled that the company is not liable for selling tokens to retail investors, but sales to institutional investors were deemed securities under the Howey test. The company targeted institutional investors, emphasizing the token’s speculative value proposition tied to the improvement of the blockchain infrastructure. This ruling highlights the token’s dual classification, considered both a security and a non-security based on the buyer’s expectations.

The list below highlights notable 2023 cases that focus on the SEC’s areas of focus.

- In January 2023, the SEC charged a crypto financial institution and a crypto exchange for the unregistered offer and sale of securities through the exchange’s lending program. In May 2023, the defendants filed motions to dismiss the complaint or, alternatively, strike the SEC’s requests for a permanent injunction and disgorgement.
- In February 2023, the SEC issued a Wells notice to a blockchain infrastructure platform, alleging that one of the stablecoins it issues and lists, is an unregistered security. The New York Department of Financial Services (NYDFS) also commanded the company to cease the issuance. The firm “categorically disagrees” with SEC’s classification, but indicated it would cease the issuance at the direction of the NYDFS.
- In February 2023, the SEC charged a crypto exchange for failing to register the offer and sale of their crypto-asset staking-as-a-service program. The exchange paid \$30 million in fines and agreed to a permanent injunction against its staking program.
- In March 2023, the SEC issued a Wells notice to a major exchange in the U.S., indicating potential violations of securities law. In April 2023, the company shared its response to the SEC’s Wells notice and its willingness to engage in rulemaking conversations. In June 2023, the SEC charged the company for (1) operating as an unregistered securities exchange, broker, and clearing agency and (2) unregistered offer and sale of securities in connection with its

staking-as-a-service program. In this complaint, the SEC named 13 crypto tokens listed on the platform as securities.

- In April 2023, the SEC charged a crypto-asset trading platform for operating an unregistered national securities exchange, broker, and clearing agency. In this complaint, the SEC named six crypto tokens listed on the platform as securities.
- In June 2023, the SEC filed charges against the world's largest crypto exchange, its U.S. affiliate trading company, and its founder, alleging various violations of securities laws. The SEC seeks permanent restraint and injunction to prevent further violations. In this complaint, the SEC named 12 crypto tokens listed on the platform as securities.
- In July 2023, the SEC charged a crypto lending company with unregistered sale of securities, false statements, and market manipulation related to its lending program.

## 2.3 BANKING UNCERTAINTY FOR CRYPTO FIRMS

This section examines U.S. regulators' actions in the banking sector regarding the digital assets industry, including the Joint Statement on Crypto-Asset Risks, de-banking initiatives, and crypto national bank conversion delays. It explores the evolving banking landscape's impact on the crypto industry.

### 2.3.1 JOINT STATEMENT ON CRYPTO-ASSET RISKS TO BANKING ORGANIZATIONS

In January 2023, a Joint Statement on Crypto-Asset Risks to Banking Organizations was issued by the Federal Deposit Insurance Corporation (FDIC), Office of the Comptroller of the Currency (OCC), and the Federal Reserve, urging banking organizations to refrain from holding cryptocurrencies or offering services to crypto clients. While banking organizations are not explicitly prohibited from serving specific types of customers, the agencies expressed the following specific concerns about the holding or issuance of crypto-assets:

1. The various risks, including fraud, legal uncertainties, misleading representations, volatility, stablecoin run risk, contagion risk, immature risk management practices, and vulnerabilities related to decentralized networks.
2. The need to prevent these risks from migrating to the banking system by carefully reviewing proposals regarding crypto-asset activities.

## 2.3.2 RECENT BANK CLOSURES

In the years leading up to 2022, there was a surge of new product deployments and collaborations between banking institutions and the crypto industry to meet the increasing institutional demand and make banking services more accessible to crypto entities. These banks developed specialized platforms, offering benefits like instant settlement and collateralization of digital assets. The influx of crypto customers in these banks resulted in a deposit structure heavily skewed towards crypto. Recently, the closure and FDIC receivership of crypto-friendly banks have had significant impacts on the crypto industry. Griffin has seen “licensed law abiding exchanges losing their banking partners simply because the banking partners have decided that it is no longer within their risk appetite to bank an entire industry. This trend began in February and particularly intensified after the voluntary liquidation of [a major crypto-friendly bank].”

Tiffany J. Smith, a Partner at WilmerHale, stresses the need for “additional safeguards” to ensure consistent standards and regulatory stability across industries. She expresses concerns about potential risks for retail customers, such as the inability to withdraw fiat if a crypto platform loses its banking partner. Smith emphasizes the importance of considering the existing industry and taking actions that protect those already involved in the market.

Musiala also advises regulated entities to develop diversified and well-capitalized business models beyond the digital asset industry, addressing concerns raised by banking regulators about over-reliance on a single sector. This could involve traditional financial institutions entering the space (e.g., launch of a new crypto exchange backed by a consortium of traditional Wall Street firms) or FinTech startups creating holistic institutions that cater to both traditional financial needs and the digital asset sector.

Despite the banking turmoil, a handful of major institutional financial players are still continuing to expand their presence in the digital assets sector. This is evident through their engagement in activities like applying for ETF approvals and introducing crypto services for retail investors. Amidst challenges, these developments reflect a growing interest and commitment from established financial entities in the cryptocurrency space.

## 2.3.3 CRYPTO NATIONAL TRUST BANK CONVERSIONS

The OCC has also shown hesitancy in granting regulatory approvals to crypto banks, leading to the expiration of banking charters. With only one OCC-approved crypto trust company, the crypto industry in the U.S. is facing a notable setback due to the decline of crypto-friendly banks and the absence of new national charter approvals for regional crypto trust companies.



- In January 2023, the United State Federal Reserve Board rejected a Wyoming-chartered special purposes depository institution's application to join the Federal Reserve System. The Federal Reserve Board stated that the firm's proposed focus on crypto-assets posed significant safety and soundness risks. In February 2023, the Federal Reserve Board denied the institution's request for Fed supervision.
- A trust bank, which received conditional approval from the OCC in February 2021, saw its national banking charter application expire in February 2023. The bank has the option to reapply to the OCC or seek a state authority to operate as a state bank.
- A New York-chartered trust company, granted conditional approval in April 2021, saw its national banking charter application expire in March 2023. However, the institution's existing business remains unaffected due to its regional charter.

## 2.4 IMPACT ON CRYPTO-ASSOCIATED THIRD PARTIES

The U.S. regulatory approach to date has impacted various crypto-related parties:

- **NFT Issuers:** In February 2023, a federal judge allowed a securities class action lawsuit against an NFT company to proceed in the Southern District of New York (final determination pending). Considering allegations regarding the company's private blockchain and its influence on NFT values, the court determined that the promise of profit relied on the company's contributions (Howey Test requirement). While not classifying all NFTs as securities, this ruling sets a legal precedent for future enforcements and encourages purchasers to pursue legal remedies against issuers.
- **DeFi Liquidity Providers:** In March 2023, the SEC proposed rules to expand the definition of regulated dealers, raising concerns for DeFi. The proposal requires DEXs to ensure that their smart contract-controlled automated market makers register as dealers. However, requiring registration for thousands of individual liquidity providers may pose practical challenges. The lack of explicit mention of DeFi in the proposal has also led to speculation about the SEC's intentions and limitations.
- **DEXs:** In April 2023, the SEC extended the comment period for proposed amendments to redefine exchanges, indicating its regulatory authority over existing crypto exchanges, including DeFi protocols. Smith states that the SEC operates under the assumption that "there will always be a group or entity to regulate," even for decentralized protocols. She stresses the necessity for a targeted regulation addressing DeFi's unique risks beyond existing frameworks.

- **DAO Token Holders:** In March 2023, a California court denied motions to release DAO members from liability in a class-action lawsuit after a \$55 million hack. Token holders were classified as general partners, and the court deemed the protocol a general partnership due to their governance abilities. In September 2022, the CFTC charged the same protocol, its founders and a successor DAO for violations. The crypto industry submitted amicus briefs to argue for individual member identification and accountability, but the court ruled that the DAO, as an unincorporated association, could be sued. In January 2023, the CFTC sought a default judgment against the DAO after it failed to respond to the charges. These developments have prompted considerations about the liability of governance token holders in DAOs.
- **Crypto Staking Services:** SEC Chair Gary Gensler previously stated that staking could potentially fall within the boundaries of the Howey Test, emphasizing the similarity between staking through intermediaries and lending. Recent legal enforcements on staking services have raised considerations for the SEC's approach to staking activities in the U.S., the feasibility of offering such services for crypto companies, and the need for SEC guidance to mitigate regulatory issues.
- **Crypto Custody:** In February 2023, the SEC proposed a new rule under the Investment Advisers Act of 1940, which adds crypto-assets within the custody scope and requires investment advisers to store client's crypto-assets with a "qualified custodian." The SEC noted that its list of companies offering crypto-assets custody services includes "one OCC-regulated national bank, four OCC-regulated trusts, approximately 20 state-chartered trust companies and other state-chartered, limited purpose banking entities, and at least one [futures commission merchant]." The SEC has not provided explicit names, leading to ambiguity regarding the definition of qualified custodians and their specific qualifications.

# PART 3

## INTERNATIONAL JURISDICTIONS

### CRYPTO REGULATION LANDSCAPE

In response to a series of significant crypto-related incidents in 2022, regulators worldwide have actively been developing and publishing updated regulatory frameworks for crypto-assets. Their focus is on refining their stance on crypto regulation while striving for a balanced approach that brings clarity to businesses and market participants. Global regulators have been actively delegating regulatory authority to specific agencies, setting clear regulatory boundaries. Furthermore, they are launching licensing regimes aligned with the AML/CTF measures commonly associated with traditional markets. Another significant area of emphasis has been the regulation of stablecoins, which closely interact with fiat currencies. Although some frameworks do not yet address crypto-native concepts like DeFi regulations, global regulatory bodies appear to be moving in the right direction. This section will discuss noteworthy regulatory advancements in regions such as the Middle East, the European Union (EU), the United Kingdom (U.K.), Asia, and Latin America.

## 3.1 MIDDLE EAST REGULATIONS (DUBAI)

The Middle East is rapidly developing frameworks for crypto businesses with regions like Dubai aiming to become “the capital of the Future Economy anchored by Metaverse, AI, Web3.0 and Blockchain.” In March 2022, the Virtual Assets Regulatory Authority (VARA) was established in the Emirate of Dubai to regulate all activities related to the virtual assets sector. In February 2023, VARA issued the Virtual Assets and Related Activities Regulations 2023, built on principles of economic sustainability and cross-border financial security. These regulations set out the regulatory framework governing virtual assets and all related activities in the Emirate, including the general and specific supervision and enforcement powers of VARA. The regulations encompass aspects such as custody and segregation of client money, prudential requirements (insurance and liquidity reserves), Financial Action Task Force (FATF) considerations (AML-CFT, KYC, Client Due Diligence, Travel Rule), and market manipulation/abuse prevention (data privacy and information security).

Virtual Asset Service Providers (VASPs) meeting VARA’s licensing requirements must adhere to the Compulsory Rulebooks: Company, Compliance and Risk Management, Technology and Information, and Market Conduct. They also need to comply with activity rulebooks corresponding to their specific services, including Advisory, Broker-Dealer Services, Custody Services, Exchange Services, Lending and Borrowing Services, Transfer and Settlement Services, and Management Investment Services. Additionally, there is the Virtual Asset Issuance Rulebook for virtual assets issued by entities in the Emirate, operating alongside the regulation of virtual asset activities. Over the past year, VARA has actively sought crypto businesses, resulting in firms securing Minimal Viable Product preparatory licenses and launching with Minimal Viable Product operational licenses (can offer approved services to institutional clients and Qualified Investors). VARA is



slowly also releasing their Full Market Product license, allowing services to retail customers.

At a federal level, the UAE Government also issued Cabinet Resolution No.111 of 2022, effective from January 15, 2023, to regulate VASPs. This resolution complements Dubai's Law No. 4 of 2022 and establishes a unified federal regulatory framework applicable across all Emirates. The regulation applies to companies within the mainland and free zones except the two financial free zones, Dubai International Financial Centre and Abu Dhabi Global Market. The regulatory framework aligns with FATF guidelines for virtual assets and covers activities such as crypto exchange, brokerage, payment services, and token control.

## 3.2 EUROPEAN UNION REGULATIONS

With the approval of Markets in Crypto-Assets (MiCA) regulation, the EU became the first major jurisdiction in the world to introduce a comprehensive framework for crypto regulation. MiCA, proposed by the European Commission in September 2020, aims to enhance transparency, protect investors, and establish a comprehensive framework for the crypto-asset sector in the EU. It covers various types of tokens, including utility tokens, asset-referenced tokens, and stablecoins, as well as service providers such as trading venues and wallets. MiCA will take precedence over conflicting national legislations approved by EU member states, replacing the fragmented regulatory environment currently in place. Member states will be expected to ensure compliance with MiCA by updating their local legislations to align with the proposed framework. After securing a license from a regulator in one country, crypto-asset service providers will be allowed to operate cross-border across 27 member states under this new framework.

The EU's Economic and Financial Affairs Council (ECOFIN) adopted its negotiating mandate on MiCA in November 2021. After the trilogues between the co-legislators, the European Parliament endorsed the bill in April 2023. In May 2023, the ECOFIN unanimously approved the adoption of the regulation. In conjunction with MiCA, the EU also adopted the Transfer of Funds Regulation (TFR), an anti-money laundering legislation that requires crypto transfers to be traced similarly to traditional money transfers (customer identification), expanding the Travel Rule to crypto-assets.

MiCA and the TFR were published in the Official Journal of the European Union on June 9th, 2023 (laws will be entered into force 20 days later). The provisions regarding the regulation of stablecoins under MiCA will be applicable 12 months after the date of entry into force. The remainder of the provisions under MiCA together with the TFR will be applicable 18 months after the date of entry into force.

MiCA creates a uniform legal framework across the EU – it appoints the European Securities and Markets Authority as the primary regulator with the authority to approve licenses and impose

restrictions on crypto platforms. Stablecoin issuers and custody services providers are also obligated to fulfill respective security and risk management criteria, such as capital reserves and liquidity requirements. To address the carbon footprint concerns, service providers will be required to disclose their energy consumptions as well. The regulation still leaves room for additional trends in the industry, such as NFT regulations and the use of DeFi platforms/DAOs, to be addressed.

### 3.2.1 EU CRYPTO-SPECIFIC TAXATION POLICIES

The EU is also working on its tax transparency rules for crypto-asset transactions (DAC8). Introduced in December 2022, the proposal requires all crypto-asset service providers, including those outside the EU, to report domestic and cross-border transactions by EU clients. The scope covers various types of crypto-assets, including stablecoins, e-money tokens, CBDCs and certain NFTs. The proposal aims to help reduce the risk of tax fraud/evasion by providing consistent application of crypto-asset reporting rules across the EU. The DAC8 proposal aims to integrate OECD's Crypto-Asset Reporting Framework and Common Reporting Standard into the EU's legal framework. The draft text will undergo consultation with the European Parliament and the Council before adoption. Once approved, the new rules are expected to be in force as of January 2026 (post-MiCA implementation).

## 3.3 UNITED KINGDOM REGULATIONS

The U.K. declared in April 2022 that it wishes to make the "U.K. a global crypto-asset technology hub." In February 2023, the U.K. government announced its plans for robust regulation of crypto-asset activities to provide clarity and protection for consumers and businesses. The U.K. HM Treasury intends to lay out its first set of crypto regulations, which applies and adapts existing traditional finance frameworks to crypto exchanges, custodians and other financial intermediaries. U.K. regulatory priorities include crypto-asset disclosure requirements, data reporting, consumer protection, location policy, and operational resilience. Upon regulation implementation, qualifying entities must obtain a license, meet capital/liquidity requirements, and comply with the Financial Conduct Authority's (FCA) bespoke custody rules.

After the U.K.'s announcement in April 2022, ~40 companies have registered with the FCA (15% approval rate for applications submitted since January 2020). In March 2023, the FCA shared its feedback on good and poor quality applications to help the firms prepare their applications and improve the registration rate.

In general, the U.K. has made several targeted regulatory advancements, likely in response to MiCA in the EU. Other notable developments include:

- The U.K.'s Financial Services and Markets Bill (FSMB) aiming to bring significant changes to the U.K. financial services post-Brexit. In the context of crypto, the passage of this bill will "ensure crypto is treated as a regulated activity and give the FCA and Payments Systems Regulator power to regulate the sector and protect consumers."
- The HM Treasury recently addressed the industry concerns "about the small number of Financial Conduct Authority (FCA) authorized crypto-asset firms who can issue their own promotions" and introduced a time limited exemption that allows FCA-registered crypto-assets businesses to issue their own promotions while the broader regulatory framework is being put in place. In May 2023, the U.K. lawmakers voted in favor of this amendment.
- The Law Commission of England and Wales has published its final report on digital assets, covering various aspects of the crypto market and its nuances.

## 3.4 APAC REGULATIONS

While countries like China and India continue to maintain a conservative stance, other nations are taking significant steps forward in bringing additional clarity for the industry. For instance, Japan is enforcing stricter AML/CFT requirements for crypto exchanges, and South Korea's parliament approved its first Virtual Asset User Protection Act, empowering the Financial Services Commission to regulate crypto-asset operators. The section will dive deeper into two noteworthy regions in regulatory development – Singapore and Hong Kong.

### 3.4.1 SINGAPORE REGULATIONS

Singapore has implemented the Travel Rule and other AML measures since January 2020 through Notice PSN02 issued by the Monetary Authority of Singapore (MAS). Digital payment token (DPT) service providers, including crypto exchanges and stablecoin players, must obtain the Major Payment Institution (MPI) license for regulated payment services. The scope of DPT activities was expanded to include custodial wallet services and DPT transfers in January 2021.

In October 2022, MAS released two consultation papers to introduce regulations for DPT service providers and establish stablecoin-related measures. The DPT proposal focuses on consumer protection, imposing restrictions on retail customer incentives, credit facilities, leveraged

transactions, and credit card payments. MAS will issue guidelines based on consultation feedback, allowing for a transition period of six to nine months before implementing regulatory requirements and draft legislation. The stablecoin proposal introduces a regulated activity called stablecoin issuance service for single-currency-pegged stablecoins (SCS) tied to the Singapore dollar or G10 currencies. Non-SCS remain classified as digital payment tokens under current regulations. MAS proposes licensing criteria based on circulation value and labeling to distinguish regulated SCS, with requirements including reserve asset backing, timely redemption, customer disclosure, and financial solvency.

In July 2023, MAS announced that crypto service providers in Singapore are required to segregate customer assets and hold them in a trust, while also placing restrictions on lending and staking of tokens for retail customers. This decision was made after considering consultation feedback, and MAS remains open to receiving further input from the industry.

In terms of collaborative efforts, MAS launched Project Guardian in May 2022, exploring open networks and asset tokenization with a DeFi-focused pilot. In June 2023, MAS and the Bank for International Settlements (BIS) published a report proposing an interoperable network framework for digital assets. Project Guardian expanded to test asset tokenization across various financial asset classes and welcomed the Japan Financial Services Agency (JFSA) as the first overseas regulator. MAS also released a whitepaper proposing an interoperable protocol called Purpose Bound Money (PBM) for digital money, allowing senders to set conditions for its use. Financial institutions and companies like Amazon, FAZZ, and Grab are piloting PBM for online retail payments.

### 3.4.2 HONG KONG REGULATIONS

Hong Kong, once a leading crypto hub, faced a decline amid stricter regulations and concerns about its autonomy following China's crypto ban. However, Hong Kong has now shifted its approach to preserve its status as an international finance center. In December 2022, Hong Kong passed the Anti-Money Laundering and Counter-Terrorist Financing (Amendment) Bill, establishing a licensing framework for VASPs. The Securities and Futures Commission (SFC) released a consultation on regulatory requirements for virtual asset trading platforms (VATPs) in February 2023, followed by the publication of AML/CTF guidelines in May 2023 (live since June 1, 2023). As of June 2023, Hong Kong has opened its doors to retail investors based on the SFC's consultation conclusion on VATPs. VATPs seeking a license must undergo assessment by an external assessor and existing operators have nine months from the regulation publication (until end of February 2024) to complete the licensing process.

Licensed platforms are now allowed to offer trading services to retail customers, with strict requirements for tokens admitted for retail trading, including safe custody, asset segregation, and conflict of interest avoidance. The Hong Kong Monetary Authority (HKMA) plans to establish a regulatory framework for retail investors to trade stablecoins and virtual asset derivatives in 2024. The new regime also includes statutory AML/CTF obligations and an update on the Travel Rule (VATPs have 6 months for data transfers). These developments mark a significant departure from Hong Kong's previous prohibition on retail crypto trading, highlighting its renewed focus on embracing the crypto industry.

In January 2023, HKMA concluded its stablecoin regulation consultation, addressing topics such as governance, issuance, stabilization, and wallets. The regime may include requirements for local incorporation and adherence to principal business. It ensures stablecoins are fully backed by high-quality assets, redeemable at a value equivalent to fiat currencies.

## 3.5 LATIN AMERICA REGULATIONS

Brazil's crypto regulation is a significant milestone in Latin America, potentially inspiring neighboring countries to expedite the finalization of their own regulatory frameworks. The regulation, established in December 2022 and effective from June 2022, grants authority to the Central Bank of Brazil to regulate virtual asset service providers, while token projects classified as securities fall under the supervision of the Comissão de Valores Mobiliários. The new regulation introduces penalties for fraud involving virtual assets and mandates that companies, including exchanges, obtain licenses as virtual service providers. The central bank governor has also shown support for blockchain technology and has plans to launch a CBDC by the end of 2024.

Other Notable LATAM Regulatory Updates:

- Argentina: The Central Bank of Argentina (BCRA) banned banks from facilitating crypto transactions (individuals can still use their bank accounts on local exchanges). Argentine crypto exchanges currently operate without a financial institution license and primarily function as payment service providers regulated by the BCRA – they are closely monitoring regulatory development. Mariano Biocca, the Executive Director at Argentina's fintech association, stated that the organization is actively working with the government to publish a regulatory framework for VASPs in 2023.

- Colombia: Colombia released its draft crypto regulations in July 2022, covering areas such as risk management for money laundering, and transaction tracing. The country also launched a regulatory sandbox and witnessed increased crypto adoption. In June 2023, Banco de la República initiated its CBDC pilot project, signaling Colombia's exploration of blockchain technology for high-value payments. This initiative aligns with the country's efforts to utilize blockchain in the public sector.

**Figure 3: Global Crypto Regulations Overview**

Jurisdiction	Regulatory Framework	AML / CTF	Travel Rule	Stablecoins Regulation
Argentina	In progress	In progress	In progress	In progress
Bahamas	✓	✓	✓	✓
Brazil	✓	✓	✓	In progress
Cayman Islands	✓	✓	✓	✓
China	✗	✗	✗	✗
Colombia	In progress	In progress	In progress	In progress
European Union	✓	✓	✓	
Hong Kong	✗	✓	✓	In progress
Japan	✓	✓	✓	
Singapore	✓	✓	✓	In progress
South Korea	✓	✓	✓	In progress
United Arab Emirates	✓	✓	✓	
United Kingdom	In progress	✓	✓	In progress
United States	In progress	✓	✓	In progress

Source: The Block Research, PwC, legal filings.

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**Figure 3: Global Crypto Regulations Overview**



# PART 4

## CONCLUSIONS & OUTLOOK

Initial expectations of a compromise between U.S. crypto businesses and regulators have shifted, with crypto firms now being encouraged to operate like traditional financial institutions and comply with existing frameworks. Experts suggest enacting new legislation to provide regulators with a specialized toolkit for addressing the unique characteristics of this asset class. The absence of comprehensive laws may perpetuate regulatory ambiguity and reactive approaches. At a global level, some jurisdictions have implemented tailored frameworks, creating a diverse regulatory landscape where countries compete to attract the crypto industry. Global regulators are focused on establishing frameworks targeting crypto activities closest to traditional markets (e.g., AML/CTF measures and stablecoin rules). Navigating this heterogeneous regulatory environment will be crucial for stakeholders as the industry evolves.

Given our report findings and discussion with practitioners, we see four possible industry developments: focus on safer assets, U.S. exposure reduction, segregation of activities, and emphasis on compliance effectiveness.

Firms are looking into opportunities in “safer” assets and products with clearer regulatory precedents. Musiala has observed “a lot of quiet developments for derivative products based on Bitcoin and Ether, such as futures and options.” The derivative products have been gradually gaining approval from the CFTC to be traded on regulated marketplaces like Chicago Mercantile Exchange and Chicago Board Options Exchange. This presents an area where new products can be launched with a relatively higher level of regulatory certainty.

Legal experts indicated that U.S. crypto platforms have been expressing concerns of potential targeting after recent SEC complaints. Smith notes that “as the SEC tightens its control, other jurisdictions may seize the opportunity to establish themselves as industry leaders.” With escalating legal stakes, attorneys at Willkie have acknowledged an increase in discussions regarding shifting new product development outside the U.S. to target non-U.S. customers. There are talks about relocating to the EU or the U.K. to operate with greater regulatory clarity. Firms are also placing renewed emphasis on enhancing KYC processes. Karen Ubell, a Partner at Goodwin Procter, also points out that the entrepreneurs are being hesitant in entering the digital asset space due to uncertainty and chilling effects of the current landscape.

Regulators and financial market agencies stress the need for segregation of activities within businesses to address regulatory and market integrity concerns. Separate licenses may be required for businesses to align with their various functions. Musiala anticipates a push in the next five years to identify and segregate activities performed by companies in the crypto industry. He has been advising firms to proactively assess how they can adapt their models to align with the evolving landscape.

Mike Carter, Senior Managing Director at FTI Technology notes, “despite global regulatory nuances, digital asset companies are commonly expected to deploy robust compliance programs that are well-designed, appropriately resourced, and tested for function. That includes developing thorough product assessment, safety, listing, and disclosure programs, mitigating traditional and digital asset-specific fraud risks, and prioritizing safety and soundness measures that include anti-financial crimes, sanctions, data privacy, and asset accounting.”

Jeremy Sheridan, a Managing Director within FTI Technology, and the former Secret Service Assistant Director of Investigations, adds that lessons learned from independent program audits, investigations, whistleblower reports, and regulatory examinations should routinely be incorporated back into compliance program processes, controls, and training. Sheridan states, “digital asset based crimes continue to evolve, but a mature compliance program continues to be a foundational requirement to not only prevent regulatory sanctions but also fortify defenses against criminal activity. Organizations that apply compliance standards to on-boarding, in-process, and off-boarding of digital assets are much more resilient against an ever-changing landscape of digital risks.

# DISCLOSURES

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Beginning in 2021, Michael McCaffrey, the former CEO and majority owner of The Block, took a series of loans from founder and former FTX and Alameda CEO Sam Bankman-Fried. McCaffrey resigned from the company in December 2022 after failing to disclose those transactions.

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