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Research Article

BLOCKCHAIN, CRYPTOCURRENCY, ANDTOKEN MARKETING AND SALES ISSUES

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ABSTRACT

This article discusses blockchain, cryptocurrency, token sales, and their associated legal issues. Blockchain and cryptocurrency and their characteristics are described, followed by the arguments for and against them. The article expounds on the federal regulations affecting blockchain and cryptocurrency, itemizing the federal agencies involved. Some of the recent significant blockchain and cryptocurrency legal cases are highlighted. The essay describes consumer finance and portrays token sales and the security regulations that govern them. The article illuminates the blockchain and cryptocurrency legal principles by reviewing the celebrity liability actions surrounding Larry David, Tom Brady, and Gisele Bündchen, a world-famous comedian, National Football League quarterback, and world-class model respectfully. The article concludes that there are a plethora of issues that a firm faces in deciding whether to offer a token sale. The critical issue is whether the SEC will decide that a token is a security token subject to government oversight, rather than a utility token where no regulation is required. For a token sale to be successful and to minimize government interference, one must carefully review a token's features from the viewpoint of the token-originating organization and a regulator's position.

Keywords: Blockchain, Consumer Finance, Crypto Federal Regulations, Crypto Market Practices, Cryptocurrency, Token Sales.

INTRODUCTION

This article aims to discuss blockchain, cryptocurrency, token sales, and the legal issues surrounding them. Blockchain and cryptocurrency and their characteristics are described, and the arguments for and against blockchain or cryptocurrency are examined. The article explains the federal regulations affecting blockchain and cryptocurrency, listing the federal agencies involved and highlighting some of the significant blockchain and cryptocurrency legal cases. The piece then segues into consumer finance and talks about token sales and the security regulations that govern them. The essay illustrates the legal principles contained therein by reviewing the celebrity liability actions encircling Larry David, Tom Brady, and Gisele Bündchen, a world-famous comedian, National Football League quarterback, and world-class model respectfully. The article concludes by observing that there are a host of issues that a firm faces in deciding whether to offer a token sale. The critical issue is whether the SEC will deem a token a security token that is subject to government oversight, rather than a utility token where no regulation is mandated. The key to a successful token sale is to carefully review a token's features, not only from the perspective of the token-originating organization but also from a regulator's standpoint. Then an entity may minimize government interference when attempting to raise capital using tokens.

BLOCKCHAIN AND CRYPTOCURRENCY

In this section, blockchain technology and cryptocurrency are defined. Second, corporate inhibitions to embracing blockchain technology and cryptocurrency are discussed. Third, the benefits of accepting these emerging technologies are highlighted. Fourth, the piece points out that there are positive and negative results when a company embraces blockchain technology and cryptocurrency. Finally, based on the arguments presented herein, the essay concludes that blockchain technology and cryptocurrencies are here to stay, even though they may not necessarily evolve in the manner that was envisioned by their creators.

Definition of Blockchain and Cryptocurrency

According to Hayes, a blockchain is a "distributed database or ledger shared among a computer network's nodes."[1] Black's Law Dictionary defines a blockchain to be a "string of bundled digital records of completed cryptocurrency transactions during a specified time on a network collectively forming a ledger that is open to public view."[2] According to Swan, a blockchain is a digital open electronic ledger that stores data about purchases and the sales of digital assets, allegedly permanently and securely.[3]

When reconsidering Hayes' definition of a blockchain, a distributed database is a "database that consists of two or more files located in different sites on either the same network or entirely different networks."[4]Parts of the database are typically stored in multiple physical locations, where the processing occurs among the various database nodes or computers.[5]A ledger is a "book in which a company or organization writes down the amounts of money it sends and receives."[6] In terms of blockchains, a distributed database is another name for the book where the entries of money spent and received are written down. Also, in this instance, an organization can be a natural person, a sole proprietorship, a partnership, an association, or a corporate entity.

A cryptocurrency is a "digital or virtual currency secured by cryptography, which makes it nearly impossible to counterfeit or

[1]Adam Hays, Blockchain Facts, What Is It, How It Works, and How It Can Be Used, *Investopedia*(Dec. 15, 2023), *available at*https://www.investopedia.com/terms/b/blockchain.asp.
[2]BLOCKCHAIN, BLACK'S LAW DICTIONARY (Thomson West 11th ed. 2019).
[3]EDWARD J. SWAN, CYBERCURRENCY LAW (Wolters Kluwer 2023).
[4]Lindsay Moore, Distributed Database, *Tech Target* (Sep. 2018), *available at*https://www.techtarget.com/searchoracle/definition/distributed-database.
[5]Adam Hayes, *supra*, note 1.
[6]Ledger, *Collins Dictionary* (n.d.), *available at*https://www.collinsdictionary.com/dictionary/english/ledger#:~:text=A%20ledger%20is%20a%20book,accounts%20More%20Synonyms%20of%20ledger.

double-spend."[7]Many cryptocurrencies exist on decentralized or distributed networks that employ blockchain technology and a distributed ledger, where the entries are enforced by a distinct network of computers.[8] A critical feature of cryptocurrencies is that they do not originate from a central authority, such as a central bank or a national government, thereby theoretically insulating them from government regulation, interference, or manipulation.[9]

Blockchains play a significant role in cryptocurrency systems by maintaining a secure and decentralized proof of transactions.[10] The use of blockchains are not limited to cryptocurrencies, but can be employed in industries where the inability to alter data is highly valued.[11] Because it is nearly impossible to change a blockchain, the point of trust is the computer where a user enters their data.[12] This feature of blockchains reduces the need for trusted parties, such as banks, auditors, etc., which can increase transaction costs or potentially make mistakes while recording transaction data.[13]

Reluctance to Use Blockchain or Cryptocurrency

According to Brown and Melchionna, companies may face seven challenges when using blockchain technology that forms the basis of cryptocurrency, including (1) lack of adoption, (2) skills gap, (3) trust among users, (4) financial resources, (5) blockchain inoperability, (6) slow development pace, and (7) lack of regulation.[14] Blockchains and cryptocurrencies are ecosystems that must be adopted broadly to be effective. Blockchain and cryptocurrency are an emerging technology, and the skills needed to employ them effectively are not common. Organizations and individuals do not necessarily trust the security of blockchain technology or the stability of cryptocurrencies.[15] Companies may need more resources to effectively employ blockchain technology or may be unwilling to invest valuable corporate resources in cryptocurrencies. Because there are no universal blockchain standards and cryptocurrency acceptance, companies may choose to develop their own blockchain technologies and cryptocurrencies that may be incompatible with other blockchain technologies and cryptocurrencies. Blockchain development is shown. Finally, there is little to no regulation of blockchain technologies and cryptocurrencies.[16]

According to the Chainanalysis Team, from 2108 to 2023, the level of illicit employment of cryptocurrencies is significant.[17] From 2018 to 2022, the total cryptocurrency value received by illicit addresses rose from $4.6 billion to $39.6 billion, despite a decline in illicit cryptocurrency value in 2023 to $24.2 billion.[18] Firms are legitimately reluctant to embrace blockchain and cryptocurrencies because cybercriminals employ them when engaging in cybercrime. It may be better for companies to avoid using blockchain technology and cryptocurrencies for fear of being embroiled in criminal activity, such as darknet market sales and ransomware activities.[19]

Another issue is cryptocurrency volatility. According to Gianti, Bitcoin (the undisputed leader in cryptocurrencies) is more volatile in the short run than in the long run (ATR 14 > ATR 200), where ATR stands for Average True Range.[20][21] Bitcoin is three times more volatile than Nasdaq in the short term, twice as volatile in the long term, and ten times more volatile than the European Union (EU) euro and the United States dollar.[22] There is a problem with viewing cryptocurrency as money. According to Krugman and Wells, money has the following three properties: (1) it is a medium of exchange, (2) a store of value, and (3) a unit of accounting.[23] Although cryptocurrency can be a medium of exchange for individuals and criminals,[24] with its significant volatility, cryptocurrency can hardly be considered a store of value or a unit of accounting. Cryptocurrencies act more like speculative stocks than money.[25] Thus, it is apparent that many companies may believe that cryptocurrencies should probably be highly regulated by governments if only to protect the asset values of its holders so the cryptocurrency value remains relatively stable.

Still, another issue is the sheer volume of blockchain technologies and cryptocurrencies. Cryptocurrencies are typically created and used to raise money for projects.[26] According to Daly, there are more than 23,000 existing cryptocurrencies, which is a far cry from a decade ago, when there were only seven cryptocurrencies.[27] Because the purpose of many cryptocurrencies is to make money for the developers, it is likely difficult for an organization to select a given blockchain technology or cryptocurrency as their preferred electronic medium. Companies may be waiting for the emerging technology of blockchain and cryptocurrency to sort itself out, while a specific blockchain or cryptocurrency dominates the market.[28]

Finally, even if a firm chooses a popular blockchain technology and cryptocurrency, such as Bitcoin, the issue to consider is how the blocks of information are connected. Different blockchains and cryptocurrencies use different hashing algorithms.[29] For example,

[7]The Investopedia Team, CryptocurrencyExplainedwith Pros and Cons for Investment, *Investopedia* (Nov. 3, 2023),*available at*https://www.investopedia.com/terms/c/cryptocurrency.asp.
[8]*Id.*
[9]*Id.*
[10]Adam Hayes, *supra*, note 1.
[11]*Id.*
[12]*Id.*
[13]*Id.*
[14]Marisa Brown, &Mark Melchionna, 7 Challenges with Blockchain Adoption and How to AvoidThem, *Tech Target* (Oct. 6, 2023), *available at*https://www.techtarget.com/searchcio/tip/5-challenges-with-blockchain-adoption-and-how-to-avoid-them#:~:text=Blockchain%20for%20businesses%3A%20The%20ultimate%20enterprise%20guide&text=Download%20this%20entire%20guide%20for,financial%20resources%20and%20blockchain%20interoperability.
[15]*Id.*
[16]*Id.*
[17]Chainanalysis Team, 2024 Crypto Crime Trends:Illicit Activity Down as Scamming and Stolen Funds Fall, But Ransomware and Darknet MarketsSee Growth*Chainanalysis.com* (Jan. 18, 2024), *available at*https://www.chainalysis.com/blog/2024-crypto-crime-report-introduction/#:~:text=Some%20forms%20of%20illicit%20cryptocurrency,entities%2C%20have%20shifted%20to%20stablecoins.
[18]*Id.*
[19]*Id.*
[20]Stefano Gianti, Bitcoin vs Risk:UnderstandingVolatility, *Swissquote* (Apr. 7, 2021), *available at*https://medium.com/swissquote-education/bitcoin-vs-risk-understanding-volatility-472efe96e439#:~:text=Besides%2C%20we%20observe%20that%20Bitcoin,volatile%20than%20the%20EUR%2FUSD.
[21]Adam Hayes, AverageTrue Range (ATR) Formula, What It Means, and How to Use It, *Investopedia* (Dec. 20, 2022), *available at*https://www.investopedia.com/terms/a/atr.asp,
[22]Stefano Gianti, *supra*, note 20.
[23]PAUL KRUGMAN AND ROBIN WELLS, ECONOMICS (Worth Publishers 6th ed. 2021).
[24] Stefano Gianti, *supra*, note 20.
[25]Yash Majithia, 15 Most Volatile Cryptocurrenciesin 2023, *Technopedia*(Aug. 11, 2023), *available at*https://www.techopedia.com/cryptocurrency/most-volatile-crypto#:~:text=Volatile%20cryptos%20experience%20significant%20price,through%20short-term%20trading%20strategies.
[26]Jake Frankenfield, What Are Crypto Tokens, and How Do TheyWork?,*Investopedia*(Feb. 12, 2023), *available at*https://www.investopedia.com/terms/c/crypto-token.asp.
[27]Lyle Daly, How ManyCryptocurrencies Are There?,*The MotleyFoo*l (Nov. 20, 2023), *available at*https://www.fool.com/investing/stock-market/market-sectors/financials/cryptocurrency-stocks/how-many-cryptocurrencies-are-there/.
[28]*Seegenerally*, JAMES UTTERBACH, MASTERING THE DYNAMICS OF INNOVATION (Harvard Business SchoolPress 1994).
[29]Sarah Rothrie, How CryptographicAlgorithms and HashingKeep Blockchain Secure, *Devmio Blog* (Sep. 26, 2018), *available at*https://devm.io/blockchain/cryptographic-hashing-secure-blockchain-

Bitcoin employs the SHA256 hashing algorithm, which generates a 32-byte hash, whereas Dogecoin and Litecoin both use Scrypt, which is a faster and lighter cryptography algorithm than SHA256.[30] Thus, because an organization desires to keep its data and the customer data that they are entrusted to protect, it is imperative that it selects a blockchain technology and cryptocurrency that is secure, effective, and is an industry-standard so that the entity is not subject to lawsuits.

Reasons to Accept Blockchains or Cryptocurrency

According to Pratt, ten benefits of employing blockchain and cryptocurrency for business include: (1) trust is created among entities, (2) decentralized structure, (3) improved security and privacy, (4) reduced costs, (5) increased speed by eliminating intermediaries, (6) visibility and traceability of transactions, (7) immutability of transactions, (8) individual control of data, (9) tokenization or the transformation of a physical asset into a digital token, and (10) solve intractable problems and streamline cumbersome practices.[31]

Entities are likely to embrace blockchain technology and cryptocurrency when governments institute digital currencies.[32] If the federal government were to institute blockchain technology and its associated cryptocurrency, corporations may come to believe that the technology has sufficiently matured to the point where the risk of loss either has been minimized or stabilized. Even so, it should be remembered that there are political risks in that the anonymity of using cash might be eliminated, thereby reducing individual freedom.[33] Although the freedom to transact is fundamental to the libertarian perspective, it is conspicuous by its absence in "legally binding international human rights treaties such as the International Covenant on Civil and Political Rights or the International Covenant on Economic, Social and Cultural Rights (the pillars of international human rights law), nor is it found in regional instruments such as the European Convention on Human Rights, the American Convention on Human Rights or the African Charter on Human and Peoples' Rights."[34] Thus, companies may accept blockchain technology and cryptocurrency for the reason that it is not a protected legal right, and therefore, there are no limits on entity behavior.

Arguments For and Against Cryptocurrencies

Cryptocurrencies have the ability to strengthen or weaken a corporation, depending on the underlying blockchain implementation for the cryptocurrency. Strengthening a company can be interpreted to mean increasing the solvency or profitability of the firm. If the entity holds cash in the form of cryptocurrency, then at the end of its fiscal year and presuming that the cryptocurrency increased in value during that fiscal year, the asset side of its balance sheet would increase, thereby increasing net worth, presuming that liabilities were not affected by an increase in value of the cryptocurrency.[35] The opposite would be true if the cryptocurrency had declined in value.[36]If a firm created its own blockchain to manage its physical assets, then the company may have increased the security of those assets by reducing the risk of loss for the reasons specified in the benefits section above, assuming that the software implementation of the blockchain was accomplished effectively with little or no bugs. However, if the corporation's blockchain contained serious software bugs, the entity may have opened itself up for hacking attacks. If the firm used the Bitcoin open-source code,[37] there is the possibility that the version selected possesses a zero-day vulnerability that did not exist in previous versions, thereby weakening the security of the company. Finally, another issue could occur if the entity engaged in an initial coin offering (ICO) or an initial exchange offering (IEO). In these instances, the entity could run afoul of the rules and regulations instituted by the Securities and Exchange Commission (SEC) by not transparently informing investors regarding the benefits of owning the cryptocurrency[38] or by acting as an alternative trading system or broker/dealer, which by law are required to register.[39]

Blockchain and Cryptocurrency Conclusion

Based on the information above, it is evident that companies have a plethora of reasons to hesitate to adopt blockchain technology and cryptocurrency. Essentially, the technology is growing and maturing, but remains a work in progress. Firms should be cautious regarding incorporating blockchain technology and cryptocurrency. It should be remembered that when it comes to innovation, the first one that goes through the door is usually a sacrificial lamb, such as Robert M Faiella and Charles Shrem.[40][41] Even so, if a technology has merit, it will survive the slings and arrows of outrageous fortune, and be triumphant in the end.[42]

FEDERAL REGULATIONS AND BLOCKCHAIN AND CRYPTOCURRENCY

In this section, cryptocurrency applications and use cases are defined. The federal agencies that deal with blockchain and cryptocurrency are outlined, including the United States Treasury (Treasury), the Securities and Exchange Commission (SEC), the Internal Revenue Service (IRS), the Commodities Futures Trading Commission (CFCT), the United States Department of Justice (DoJ), and the Federal Reserve Bank (Fed). A host of blockchain and cryptocurrency legal cases are listed. The question of whether there

149464#:~:text=Blockchains%20hash%20each%20transaction%20before,in%20the%20blockchain%20is%20immutable.

[30]*Id.*

[31]Mary K. Pratt, Top 10 Benefits of Blockchain for Business, *Tech Target* (Sep. 23, 2023), *available at*https://www.techtarget.com/searchcio/feature/Top-10-benefits-of-blockchain-technology-for-business.

[32]Patrick Mutabazi, How Governments Can Create Digital Currencies on CryptocurrencyPlatforms:Exploring the Potential, *Linkedin.com* (Mar. 11, 2024), *available at* https://www.linkedin.com/pulse/how-governments-can-create-digital-currencies-patrick-mutabazi-lenpe/.

[33]Elizabeth M. Renieris, Crypto's "Freedom to Transact" May ActuallyThreaten Human Rights, *Center for InternationGovernance Innovation* (Mar. 15, 2022), *available at*https://www.cigionline.org/articles/cryptos-freedom-to-transact-may-actually-threaten-human-rights/.

[34]*Id.*

[35]*Seegenerally*, WAYNE THOMAS, MICHAEL DRAKE, JAKE THORNOCK, & DAVID SPICELAND, FINANCIAL ACCOUNTING FOR MANAGERS: 2024 RELEASE (McGraw-Hill Publishers 2024).

[36]*Id.*

[37]Bitcoin Staff, Bitcoin Is an Innovative Payment Network and a New Kind of Money, *Bitcoin.org* (n.d.), *available at* https://bitcoin.org/en/#:~:text=What%20is%20Bitcoin%3F&text=Bitcoin%20uses%20peer-to-peer,and%20everyone%20can%20take%20part.

[38]SEC Staff, InvestorAlert: Public CompaniesMaking ICO-Related Claims, *United States Securities and Exchange Commission* (Aug., 28, 2017), *available at*https://www.sec.gov/oiea/investor-alerts-and-bulletins/ia_icorelatedclaims.

[39]SEC Staff, Initial Exchange Offerings (IEOs) – InvestorAlert, *United States Securities and Exchange Commission* (Jan. 14, 2020), *available at*https://www.sec.gov/oiea/investor-alerts-and-bulletins/ia_initialexchangeofferings.

[40]Nathan Reiff, Who Is Charlie Shrem?,*Investopedia* (Nov. 5, 2023), *available at*https://www.investopedia.com/tech/who-charlie-shrem/#:~:text=Among%20the%20prominent%20millionaires%20who,an%20unlicensed%20money-transmitting%20business.

[41]*United States v. Faiella and Shrem*, 28 F.Supp. 544 (2014). (HereFaiellawasconvicted of operating an unlicensed money-transmitting business in violation of 18 U.S.C. § 1960 and of conspiracy to commit money laundering in violation of 18 U.S.C. § 1956(h). Shrempledguilty to beingindirectlyinvolved in transmitting $1 million in Bitcoin to the Silk Road black marketplace.), *available at* https://casetext.com/case/united-states-v-faiella.

[42]William Shakespeare, HametAct III, Scene I [To be or not to be. . .].

should be more or less enforcement is addressed, where one's position is opined to be based on one's political persuasion. The piece notes that the existing and potentially new blockchain and cryptocurrency legal structure will likely not affect the innovation leadership of the United States. The essay concludes by briefly summarizing the material presented herein.

Cryptocurrency Use Cases

What are the uses of cryptocurrency? According to the Encyclopedia Britannica, nine ways to use cryptocurrency are to send money across borders efficiently, tip one's favorite creators directly, shop via e-commerce, transact directly with peers, spend and earn digital currency, support a blockchain network, keep transactions private, maximize earnings with yield farming; and pay employees and contractors.[43] Bit Panda listed five use cases for cryptocurrency, including access to personal finance, smart contracts, the Internet of Things (IoT), digitized metals, and stablecoins.[44] Finally, Daley observed that the current top blockchain applications are: money transfer, smart contracts, IoT, personal identity security, healthcare, logistics, non-fungible tokens (NFTs), government, and media.[45] Although the three lists include some duplication, it is evident that blockchain and cryptocurrency are steadily becoming ubiquitous in the economy. In terms of enforcement, it is likely that blockchain and cryptocurrency laws are trailing their applications.The federal government is developing a coordinated policy toward cybercurrency.[46] The federal agencies that respond to crypto issues are:[47]

- United States Department of the Treasury;
- Securities and Exchange Commission;
- Internal Revenue Service;
- Commodities Futures Trading Commission;
- United States Department of Justice; and
- Federal Reserve Bank.

Federal Agencies Dealing with Blockchains and Cryptocurrency

In this subsection, the blockchain and cryptocurrency issues that are addressed by the government departments and agencies listed above are highlighted. Each government agency is discussed in turn.

United States Treasury

The Treasury encourages a strong economy by creating job opportunities and promoting economic prosperity. The Treasury established the Financial Crimes Enforcement Network (FinCEN) to protect against illegal financial activities, such as illegal money transmission, the buying and selling of money orders and traveler checks, and the United States Postal Service (USPS) violations. The Treasury is also concerned with the money service business, including currency dealers and exchanges, check cashers, and issuers and sellers of money orders, travelers' checks, or stored value.[48] In May 2019, FinCEN issued guidance regulations regarding virtual currencies and advice on how to avoid virtual currency misuse. In March 2022, FinCEN published regulations on potential red flags that should warn financial institutions so they may avoid financial sanctions. FinCEN suggested that any financial institution that observes cryptocurrency and other virtual asset flows report suspicious activity to the agency.[49] The Treasury's Office of Foreign Assets Control (OFAC) is also interested in blockchain and cryptocurrency misuse.

United States Securities and Exchange Commission

The SEC regulates the buying and selling of securities or investments. In particular, the SEC is concerned with regulating exchanges, including cryptocurrency exchanges. In 2017, the SEC established an enforcement unit to observe cyber markets, including crypto and digital asset markets. In March 2022, the SEC proposed amendments to its regulations, hoping to improve and increase the reporting of cybersecurity incidents by public companies.[50] From 2013 to 2022, the SEC brought more than 90 enforcement actions relating to cryptocurrency issues that dealt with fraud or failure to register securities. Forty cases were instigated by the SEC, thirty cases were administrative proceedings, where over fifty percent of the cases were filed in the New York State federal courts, usually in the Southern District of New York. The number of crypto-related cases increased from one in 2013 to nineteen in the first quarter of 2021.[51] In May 2022, the SEC announced that it was doubling the size of its cyber unit, renaming it Crypto Assets and Cyber Unit (CACU).[52]

Internal Revenue Service

Because the IRS has frequently been involved in cryptocurrency cases, this fact has precipitated the agency's establishment of specific regulations related to blockchain and cryptocurrency.[53] According to the IRS, virtual currency is a property that possesses an equivalent value to real currency or behaves as a substitute for real currency. This means that profits from the buying and selling of cryptocurrency are taxable. In August 2022, the IRS sent a letter to virtual currency owners advising them to pay back taxes or file amended returns.[54]

Commodities Futures Trading Commission

The CFTC has assumed the position of an overseer of specific parts of the digital asset business. One concern of the CFTC is the possibility of digital assets supporting scams and other criminal activity. To counteract this issue, the CFTC has generated educational materials for the digital markets, outlining how to recognize and avoid such scams.[55] The CFTC recognizes digital assets as commodities and thus within its jurisdiction. For example, the CFTC believes that it is responsible for regulating derivative contracts based on virtual currency.[56]

United States Department of Justice

In October 2021, the DoJ created the National Cybersecurity Enforcement Team (NCET) and is responsible for conducting investigations and prosecuting over-the-counter cybersecurity crimes, such as crimes committed by virtual currency exchanges, mixing and tumbling services, and money laundering infrastructure actors.[57] On

[43]Allie Grace Garnett, Crypto Use Cases: 9 Ways to Use Cryptocurrency to Manage Money, *Britannica Money* (n.d.), *available at*https://www.britannica.com/money/crypto-use-cases.
[44]Bit Panda Staff, Five Use Cases of Cryptocurrencies, *Bit Panda* (n.d.), *available at*https://www.bitpanda.com/academy/en/lessons/five-use-cases-of-cryptocurrencies/.
[45]Sam Daley, 35 Blockchain Applications and Real-World Use Cases, *Builtin* (n.d.), *available at*https://builtin.com/blockchain/blockchain-applications.
[46]Edward J, Swan, *supra*, note 3.
[47]*Id.* at 39.
[48]*Id.* at 40-42.
[49]*Id.* at 43.
[50]*Id.* at 48-49.
[51]*Id.* at 49.
[52]*Id.* at 50.
[53]*Id.* at 63
[54]*Id.* at 64
[55]*Id.* at 68-69.
[56]*Id.* at 70.
[57]*Id.* at 79

February 17, 2022, the DoJ announced the appointment of Eun Young Choi as the first Director of NCET. Choi was the cybercrime coordinator when she was an Assistant U.S. Attorney for the Southern District of New York.[58]

Federal Reserve Bank

The Federal Reserve (Fed) is the central bank of the United States, and is responsible for United States monetary policy, including setting the reserve requirements ratio, establishing the rediscount rate, and conducting open market operations.[59] The Fed also promotes financial stability, monitors the impact of United States financial institutions, establishes safe, secure, and efficient payment settlement systems, promotes consumer protection, and issues United States currency to maintain confidence in that currency.[60]In 2021 and 2022, the Fed began discussions about creating a United States digital currency. The Fed observed that cryptocurrencies have existed for over a decade and that citizens are seemingly comfortable with their existence. In generating a United States digital currency and real currency, an American digital currency would necessarily have to be backed by the full faith and credit of the Fed and the United States government.[61] If the United States were to create a digital currency, there would be two types of legal tender, traditional currency,and digital currency, both supported by the full faith and credit of the Fed and the United States government.

Blockchain and Cryptocurrency Legal Cases

Government agencies have brought a plethora of cases before the courts.[62] In the Coinbase case, the SEC filed insider trading charges against a Coinbase product manager and two other defendants, accusing them of plotting to trade crypto assets before they were available for trading by the public.[63] In the MCC International Corp. case, the SEC alleged that the company's founders and other defendants conducted unregistered offerings and fraudulent sales of investment plans to thousands of individuals, claiming that their investments were for crypto mining and trading projects.[64] On May 6, 2022, the SEC stated that it had settled charges against Nvidia Corp. related to insufficient disclosures relating to the impact of crypto mining on its gaming business. The firm paid a $5 million penalty.[65] On March 30, 2022, the SEC settled a case involving John and Jonatina Barksdale with defrauding investors out of $124 million by employing an unregistered crypto token entitled Ormeus Coin.[66]On February 14, 2022, the SEC charged BlockFi Lending LLC with not registering its offers and sales in conformance with the Investment Company Act (ICA) of 1940, where the company agreed to settle the charges by paying a $50 million fine to the SEC and an additional $50 million to 32 states to settle similar charges.[67]There are a plethora of other SEC cases against companies that issued tokens illegally.[68]

On May 15, 2024, Anton Peraire-Bueno, 24, of Boston, and James Pepaire-Bueno, 28, of New York, were charged with conspiracy to commit wire fraud, wire fraud, and conspiracy to commit money laundering.[69]The brothers schemed to exploit the integrity of the Ethereum blockchain (i.e., its immutability) by fraudulently obtaining approximately $25 million in about twelve seconds.[70]On August 5, 2022, the IRS publicized that Alexander Vinnik, a Russian citizen, and several other individuals owned, operated, and administered BTC-e.[71] BTC-e was an online money laundering organization that permitted trading in Bitcoin, and its customers engaged in cybercriminal activities. On March 3, 2024, Vinnik pled guilty to conspiracy to commit money laundering.[72] On July 12, 2022, Jayton Gill of Durham, North Carolina, pled guilty to operating a money transmission business and failing to file a tax return.[73]In May 2021, Binance was under investigation by the DoJ, the CFTC, as well as British, Canadian, and Japanese regulators because it moved its headquarters from country to country to seemingly avoid financial regulations.[74]In 2016, the CFCT accused Bifinex and its affiliated organizations of illegally operating an exchange platform on which cryptocurrencies were not delivered to the individuals who bought them but held the cryptocurrencies in digital wallets. Bifinex agreed that it had engaged in off-exchange commodity transactions and failed to register as a Futures Commission Merchant (FCM) in violation of sections 4(a) and 4d of the Commodity Exchange Act (CEA) of 1936.Bifinexstopped the violation and paid a fine of $75,000 plus interest.[75] In 2021, the CFCT issued another order against Bifinex, stating that from March 1, 2016, to at least December 31, 2018, it violated the terms of the 2016 order by continuing to offer off-exchange financial retail commodity transactions. The CFCT levied a $1.5 million fine against Bifinex, where the company was required to comply with the new order by December 31, 2021.[76]

Also on October 15, 2021, the CFCT imposed a $41 million fine on Tether, disputing that its stablecoin was backed by United States dollars and euros. The CFCT discovered that from 2016 to 2018, the

[58]*Id.*
[59]Paul Krugman, & Robin Wells, *supra*, note 23.
[60]*Id.*
[61]Edward J. Swan, *supra*, note 3 at 81.
[62]Edward J. Swan, *supra*, note 3, 50-78.
[63]SEC Staff, PressRelease: SEC Charges Former Coinbase Manager, TwoOthers in Crypto Asset Insider Trading Action, *U.S. Securities and Exchange Commission* (Jul. 21, 2022), *available at*https://www.sec.gov/news/press-release/2022-127.
[64]SEC Staff, PressRelease: SEC HaltsFraudulent Cryptomining and Trading Scheme, *U.S. Securities and Exchange Commission* (May 6, 2022), *available at*https://www.sec.gov/news/press-release/2022-81.
[65]SEC Staff, PressRelease: SEC Charges NVIDIA Corporation withInadequateDisclosures about Impact of Cryptomining, *U.S. Securities and Exchange Commission* (May 6, 2022), *available at*https://www.sec.gov/news/press-release/2022-79.
[66]SEC Staff, PressRelease: SEC ObtainsJudgment Against Siblings WhoOrchestrated Massive Crypto Asset Fraud, *U.S. Securities and Exchange Commission* (Mar. 30, 2022), *available at* https://www.sec.gov/litigation/litreleases/lr-25680.
[67]SEC Staff, BlockFi Agrees to Pay $100 Million in Penalties and Pursue Registration of its Crypto Lending Product, *U.S. Securities and Exchange Commission* (Feb. 14, 2022), *available at* https://www.sec.gov/news/press-release/2022-26.
[68]Edward J. Swan, *supra*, note 3 at 52-60.
[69]DoJ Staff, Two Brothers Arrested for AttackingEthereum Blockchain and Stealing $25M in Cryptocurrency, *U.S. Department of Justice* (May 15, 2024), *available at*https://www.justice.gov/opa/pr/two-brothers-arrested-attacking-ethereum-blockchain-and-stealing-25m-cryptocurrency.
[70]*Id.*
[71]IRS Staff, PressRelease:AllegedRussianCryptocurrency Money LaundererExtradited to United States, *Internal Revenue Service* (Aug. 5, 2022), *available at*https://www.irs.gov/compliance/criminal-investigation/alleged-russian-cryptocurrency-money-launderer-extradited-to-united-states.
[72]DoJ Staff, BTC-e OperatorPleadsGuilty to Money LaunderingConspiracy, *U.S. Department of Justice* (Mar. 3, 2024), *available at*https://www.justice.gov/opa/pr/btc-e-operator-pleads-guilty-money-laundering-conspiracy#:~:text=A%20Russian%20national%20pleaded%20guilty,world's%20largest%20virtual%20currency%20exchanges.
[73]IRS Staff, Durham, N.C. Man Admits to Operating an UnlicensedCryptocurrency Business and RelatedTax Charges, *Internal Revenue Service* (Jul. 12, 2022), *available at*https://www.irs.gov/compliance/criminal-investigation/durham-nc-man-admits-to-operating-an-unlicensed-cryptocurrency-business-and-related-tax-charges.
[74]Tom Schoenberg, Binance Faces Probe by U.S. Money-Laundering and TaxSleuths, *Bloomberg News* (May 13, 2021), *available at*https://www.bloomberg.com/news/articles/2021-05-13/binance-probed-by-u-s-as-money-laundering-tax-sleuths-bore-in.
[75]CFCT Staff, Press Release 7380-16: CFTC Orders Bitcoin Exchange Bitfinex to Pay $75,000 for OfferingIllegal Off-Exchange FinancedRetailCommodity Transactions and Failing to Register as a Futures Commission Merchant, *Commodities Futures Trading Commission* (Jun,2, 2016), *available at*https://www.cftc.gov/PressRoom/PressReleases/7380-16.
[76]CFCT Staff, Press Release 8450-21: CFTC OrdersTether and Bitfinex to Pay Fines Totaling $42.5 Million, *Commodities Futures Trading Commission* (Oct. 15, 2021), *available at*https://www.cftc.gov/PressRoom/PressReleases/8450-21.

company's stablecoin was backed only 30 percent of the time. Tether had relied on unregulated organizations and specific third parties to hold the "funds comprising the reserves; commingled the reserve funds with Bitfinex's operational and customer funds; and held reserves in non-fiat financial products. The CFCT also uncovered that Tether had not finished an audit of its reserves.[77]In May 2022, the CFCT filed charges against the three cofounders of BitMEX for conducting business not in conformance with federal commodities laws, including CFCT registration and Anti-Money Laundering/Know Your Customer (AML/KYC) regulations. The Southern District of New York ordered the BitMEX founders to pay $30 million in fines. Additionally, BitMEX operated an FCM without CFCT registration and did not implement a Customer Information Program (CIP).[78]

More or Less Enforcement

Should there be more or less enforcement? This is a hard question to answer because one's response may be biased by one's political persuasion. On the libertarian side, the response would likely be fewer laws and less enforcement, letting the free market establish its equilibrium. On the other side, progressives might argue that more regulation is needed because of the pervasiveness of blockchain and cryptocurrency, and its propensity for fraud and deceit. The more reasonable approach is likely somewhere in the middle, where new laws should be created to address as-now unknown blockchain applications. With that said enforcement of existing laws should not be discounted or brushed aside merely because new blockchain applications come into view. What is probably true is that government agencies should dedicate additional resources to ensure that violators of existing laws are brought to justice in a timely manner.

Because enforcement action typically occurs after the fact, it is likely that United States enforcement action will not adversely affect blockchain innovation. The reason is that the United States is well known as a haven of innovation. It seems unlikely that additional enforcement action will quell the blockchain revolution. As for other countries usurping the United States regarding blockchain and cryptocurrency, given the lack of freedom of economic opportunity in foreign lands, it does not seem likely that other countries will seize the day, and overthrow the economic power of the United States.

Federal RegulationsConclusion

Blockchain and cryptocurrency are here to stay. The current legal structure seems to address the legal issues that surround the technology. Other laws may need to be passed to deal with new crypto applications. It is an emerging technology, so new laws may be necessary as the need arises. Time will tell.

CONSUMER FINANCE

This section discusses blockchain and its ability to be used in consumer finance, including installment credit and revolving credit. The section defines consumer finance and discusses installment credit and revolving credit. Second, the piece describes four ways in which blockchain can boost consumer confidence, followed by the potential effects of employing blockchain. As a use case, credit reporting issues are outlined, arguing that credit reporting is an excellent example of where blockchain may improve a customer's purchasing experience. The risks and regulatory hurdles are then briefly highlighted. The section concludes by observing that blockchain is an evolving technology that shows promise but needs time to mature.

Definition of Consumer Finance

Consumer finance concerns the "borrowing, saving, and investment choices that people (i.e., households) make over time."[79] Consumer credit is extended by "lenders to enable consumers to make purchases immediately and pay off the balance over time with interest."[80] Consumer finance or consumer credit can be either installment credit or revolving credit.[81]

Installment credit is a loan of a specific amount that is issued in a lump sum, and is then repaid over a period of time, where payments are typically made in equal monthly installments.[82] Installment credit purchases usually include appliances, cars, and furniture.[83] Installment credit does not include purchasing real property because real property loans are backed by the real property as collateral. Installment credit purchases are classified as personal property. On the other hand, revolving credit includes credit card purchases, where the credit is revolving because the credit line typically remains the same and can be repeatedly used up to the maximum amount provided the borrower pays the minimum monthly payment on time.[84] With revolving credit, the debt may never be paid off because if a consumer pays the minimum monthly payment, the remaining debt accumulates according to compound interest rules.[85] Finally, revolving credit usually possesses a high-interest rate and is not secured by collateral.[86]

Consumer financial decisions can be quite complicated and may affect a consumer's financial well-being in the present and in the future.[87] When companies and governments establish policies, it is important to understand how consumers make financial decisions.[88]Income, consumption, savings, assets, and debts influence consumer financial decisions, particularly over time.[89]

Consumer Finance and Blockchain

Information transparency is integral in blockchain technology and can significantly influence consumer trust.[90] Blockchain technology has the potential to induce trust in online customers and possibly even on-ground customers.[91] Blockchain technology may also augment online consumption.[92] Liu et al. identified that cognitive trust (i.e., digital trust) and instantaneous trust (i.e., swift trust) in blockchain

[77] *Id.*
[78] CFCT Staff, Press Release 8522-22:Federal Court Orders BitMEX's Three Co-Founders to Pay a Total of $30 Million for Illegally Operating a CryptocurrencyDerivatives Trading Platform and Anti-Money Laundering Violations, *Commodities Futures Trading Commission* (May 5, 2022), *available at*https://www.cftc.gov/PressRoom/PressReleases/8522-22.

[79] CRS Staff, Introduction to Financial Services: Consumer Finance, *Congressional Research Service* (Jan. 5, 2023), *available at*https://crsreports.congress.gov/product/pdf/IF/IF11682#:~:text=Consumer%20finance%20refers%20to%20the,now%20and%20in%20the%20future.
[80] Julia Kagan, What Is Consumer Credit in Financial Services?Definition, Pros and Cons, *Investopedia* (Feb. 28, 2023), *available at*https://www.investopedia.com/terms/c/consumercredit.asp.
[81] *Id.*
[82] *Id.*
[83] *Id.*
[84] *Id.*
[85] *Id.*
[86] *Id.*
[87] CRS Staff, *supra*, note 79.
[88] *Id.*
[89] *Id.*
[90] Hua Liu, Ruili Ma, Guangyao He, Abdesslam Lamrabet,& Shaoling Fu, The Impact of Blockchain Technology on the Online PurchaseBehavior of Green Agricultural Products, 74 *Journal of Retailing and Consumer Services* (Sep. 2023),*available at*https://www.sciencedirect.com/science/article/abs/pii/S0969698923001340.
[91] *Id.*
[92] *Id.*

technology were significant factors in helping consumers make immediate purchases.[93]

Vereckey observed that there were the following four ways to boost blockchain in consumer finance:[94]

- Provide regulatory clarity;
- Improve collaboration across the banking system;
- Bring merchants into the blockchain fold; and
- Create a better user experience.

First, many firms that do business in the cryptocurrency space are seeking regulatory guidance.[95] Second, although policymakers believe that the financial system, including banks, will operate in a different environment in the future, retail banks are hesitant to enter the blockchain space due to the substantial costs of switching to a new system, their reluctance to share data, and the fact that they are likely dealing with outdated infrastructure.[96] Third, the connection between shoppers and merchants is powerful. If it becomes easy for consumers to pay for goods and services with cryptocurrencies and merchants to accept them, virtual currencies can become part of daily life.[97] Finally, if cryptocurrencies are to become part of everyday life, a dominant cryptocurrency must emerge, such as a federal cryptocurrency. The cryptocurrency must also become seamless and easy to use.[98]

According to Schipper, blockchain significantly affects consumer lending because it improves security, speeds up transactions, and reduces costs.[99] Distributed ledgers can impact lending by redundancies and files that are not synchronized.[100] Blockchains also ensure fast and secure AML/KYC protocols.[101] In 2017, the Thompson Reuters Cost of Compliance report found that 53 percent of the companies surveyed expected their compliance budgets to increase in 2018, including increased spending on senior compliance personnel.[102] Even so, 33 percent of the participants stated that they believed that compliance concerns would affect new financial and regulatory technology.[103]

Blockchain could also be employed in credit reporting, an integral factor in consumer lending.[104] Credit scores and reports are instrumental in determining whether consumer financing is approved, how much money may be borrowed, and at what interest rate.[105] However, the current credit reporting system suffers from various flaws, including insufficient cybersecurity of personal data, lack of consumer transparency and control, and widespread credit reporting errors.[106] Consumer credit data is currently on centralized computer systems owned by Equifax, Experian, and Trans Union. In the Equifax breach of 2017, 143 million American personally identifiable information (PII) and 209,000 individuals' credit card numbers and other sensitive data were hacked, underscoring the vulnerability of these companies' credit reporting systems.[107]

The common inaccurate information consumer reports that can affect their ability to borrow money include:[108]

- ***Mixed Files***: A credit report includes data on an individual other than the consumer about who is the subject of the report;
- ***Omitted Records***: A consumer discovers that important details are not present, reported in a separate file, or have been included in another person's report; and
- ***Inaccurate Account Information***: Details about a consumer's history with a particular creditor may contain inaccurate account activity dates, credit lines, and other important pieces of information.

Given the enormity of the task and the criticality of consumer credit data, it is imperative that blockchain protect PII.

Blockchain and Consumer Risk

Although blockchain has various applications, there are possible risks to consumers and competition that need to be addressed.[109] One of the major risks of cryptocurrency is its dramatic appreciation. In 2017, the Bitcoin price appreciated from about 850 euros to 14,000 euros, or approximately 1,600 percent.[110] The immediate question that begs a response is, why buy a gallon of milk or a pint of beer when the cryptocurrency could be worth 20 percent or more the next day?[111] The same argument holds in reverse because Bitcoin decreased by 50 percent in the first quarter of 2018.[112]It should be remembered that according to Gianti, Bitcoin is more volatile in the short run than in the long run (ATR 14 > ATR 200).[113] Bitcoin is three times more volatile than Nasdaq in the short term, twice as volatile in the long term, and ten times more volatile than the European Union (EU) Euro and the United States dollar.[114] Crypto tokens digitally represent an asset or interest and are layered onto a blockchain.[115] Crypto tokens are purported to be a store of value or a medium of exchange.[116] Crypto tokens represent value digitally employing blockchain technology and are typically used to raise money for projects.[117] These facts do not give consumers confidence about using cryptocurrency as a medium of exchange.

An even more insidious issue is that cryptocurrencies are usually not backed by any real assets, including fiat currency.[118] Aside from stablecoins that are backed by real assets or sovereign currency,[119]

[93] *Id.*
[94] Betsy Vereckey, 4 Ways to Boost Blockchain in Consumer Finance, *Massachusetts Institute of Technology: Sloan Schoolof Management* (Apr. 27, 2021),*available at*https://mitsloan.mit.edu/ideas-made-to-matter/4-ways-to-boost-blockchain-consumer-finance.
[95] *Id.*
[96] *Id.*
[97] *Id.*
[98] *Id.*
[99] Steven Schipper, Blockchain and the Implications for Consumer Lending, *Lend Trade* (2019), *available at*https://www.lendtrade.com/blockchain-impact.pdf.
[100] *Id.*
[101] *Id.*
[102] Stacey English, Cost of Compliance 2017, *Thompson Reuters* (2017), *available at*https://legal.thomsonreuters.com/content/dam/ewpm/documents/legal/en/pdf/reports/cost-of-compliance-2017.pdf.
[103] *Id.*
[104] *Id.*
[105] *Id.*
[106] Oliver Browne, The PotentialEffects of Blockchain on the CreditReportingIndustry, *Seagate Blog* (n.d.), *available at*https://blog.seagate.com/human/potential-effects-blockchain-credit-reporting-industry/.
[107] EPIC Staff, Equifax Data Breach, *ElectronicPrivacy Information Center* (n.d.), *available at*https://archive.epic.org/privacy/data-breach/equifax/.
[108] Steven Schipper, *supra*, note 99.
[109] Mary Starks, Blockchain:Considering the Risks to Consumers and Competition, *Financial ConductAuthority* (Apr. 26, 2018), *available at*https://www.fca.org.uk/news/speeches/blockchain-considering-risks-consumers-and-competition.
[110] *Id.*
[111] *Id.*
[112] *Id.*
[113] Stefano Gianti,*supra*, note 20.
[114] *Id..*
[115] Jake Frankenfield, What Are Crypto Tokens, and How Do TheyWork?,*Investopedia*(Feb. 12, 2023), *available at*https://www.investopedia.com/terms/c/crypto-token.asp,
[116] *Id.*
[117] *Id.*
[118] Eswar Prasad, The Brutal Truth about Bitcoin, *Brookings Institute* (Lul. 20, 2021), *available at*https://www.brookings.edu/articles/the-brutal-truth-about-bitcoin/.
[119] Adam Hayes, Stablecoins:Definition, How They Work, and Types, *Investopedia*(Feb. 12, 2024), *available at*https://www.investopedia.com/terms/s/stablecoin.asp.

cryptocurrencies have no real value. If the Federal Reserve were to create a United States digital currency, it would coexist with the country's real currency and be backed by the full faith and credit of the United States government.[120] The disadvantage to the consumer is if they agree in the future to pay for a good or service in cryptocurrency and the cryptocurrency appreciates in value. They may be paying more for the good or service than it is worth. The opposite occurs if the cryptocurrency depreciates in value.

Blockchain and Regulatory Hurdles

A significant issue with consumers using blockchain and cryptocurrency is that governments and regulators are attempting to understand the technology so that laws dealing with a currency are updated properly to address decentralization.[121] With regard to blockchain, the law is not yet settled. This fact can be readily seen by the state-by-state analysis that was discussed in the Module 03 discussion board assignment. The common regulatory compliance issues specified by the World Economic Forum (WEF) are as follows:[122]

- Jurisdiction;
- Exit from blockchain;
- Decentralized autonomous organizations (DAOs);
- Technology-neutral regulatory regimes;
- Intellectual property;
- Documentation, governance, and access;
- Personal data and privacy;
- Liability and risks; and
- Enforceability of smart contracts.

Most, but hopefully all, of the regulatory hurdles must be addressed for blockchain to mature and become generally accepted by consumers.

Consumer Finance Conclusion

Consumer finance is integral to consumer acceptance of blockchain and cryptocurrency. A generally accepted cryptocurrency backed by a robust blockchain must be well understood by the general public to be used in retail commerce. A myriad of blockchain applications are currently being implemented. However, the consumer finance use case is critical because it has broad economic implications. In particular, credit reporting is crucial to smooth functioning markets. The blockchain risks and regulatory hurdles must be overcome so that blockchain and cryptocurrency can take their rightful place in this information age. It should be remembered that blockchain is an evolving technology that needs time to mature.

CRYPTOCURRENCY AND TOKEN SALES

This section aims to discuss what a client should understand before embarking on a token sale. The client should appreciate what a token is, what is a token sale, and how a token sale works. The different types of tokens should be explained to the client so that the client understands the legal constraints associated with each type of token. The issues with token sales, mainly the *Howey Test*, should be presented so that the client comprehends how regulators perceive the new token, whether it is a utility token where no regulation is needed or an equity or security token where government agencies may be involved with the token sale. The client should be made aware that failure to adhere to government regulations carries serious penalties and possible prison time. The features of Regulations D, S, and the Integration Doctrine should be explained to the client, along with the myths and realities of token sales. Finally, what constitutes a compliant token sale should be explained in detail.

Definition of a Token and a Token Sale

Generally speaking, a token is an "object that represents something else, such as another object (either physical or virtual), or an abstract concept."[123] For example, a gift may be spoken of the giver's appreciation or esteem for the recipient.[124]According to Daly, a crypto token is a digital asset built on a cryptocurrency's blockchain, which is a digital ledger that stores information in linked blocks.[125] The information contained in a block can be a transaction record or an actual program (i.e., smart contract) that operates on a blockchain.[126] After cryptocurrency transactions are confirmed, they are collected into a block and then added to the blockchain.[127]

A token sale is also known as an ICO, where an ICO is the "limited period of sale of a predefined number of crypto tokens to the public, typically in exchange for major cryptocurrencies (mainly Bitcoin and Ether)."[128] A token sale is a "fundraising method used by blockchain projects to raise capital by selling their native tokens to investors.[129] Token sales permit projects to obtain funding for development, marketing, and other operating expenses.[130] An advantage of token sales is that they democratize investment opportunities by supplying liquidity to projects that are in the early stage of development.[131]

What Is a Token Sale?

The first thing that occurs is that a project creates a new digital token, and the price of a token and the quantity of tokens are established.[132] New tokens are typically purchased with existing cryptocurrency, usually Bitcoin or Ether. Although token sales have been likened to initial public offerings (IPOs), there are critical differences:[133]

- IPOs are regulated by governments, while token sales are usually not;
- IPOs raise money for a company, while token sales raise money for a project;
- Investors in an IPO receive shares in the company, while investors in a token sale receive tokens.

[120]Edward J, Swan, *supra*, note 3.
[121]WEF Staff, Legal and Regulatory Compliance, *World Economic Forum* (n.d.), *available at*https://widgets.weforum.org/blockchain-toolkit/legal-and-regulatory-compliance/index.html.
[122]*Id.*

[123]TechTargetContributor, Token, *TechTarget* (Dec. 2021), *available at* https://www.techtarget.com/whatis/definition/token.
[124]*Id.*
[125]Lyle Daly, What are Crypto Tokens?,*The MotleyFool* (Feb. 10, 2024), *available at*https://www.fool.com/terms/c/cryptotokens/#:~:text=Crypto%20tokens%20are%20digital%20assets,which%20are%20called%20smart%20contracts.
[126]*Id.*
[127]*Id.*
[128]PwC Staff, Introduction to Token Sales (ICO) Best Practices – PwC, *Price Waterhouse Cooper* (2021), *available at*https://www.pwc.com/gx/en/financial-services/pdf/introduction-to-token-sales-ico-best-practices.pdf.
[129]Coin360 Staff, Token Sale, *Coin360* (2024), *available at*https://coin360.com/glossary/token-sale.
[130]*Id.*
[131]*Id.*
[132]Faster Capital Staff, What Is a Token Sale and How Do They Work, *Faster Capital* (n.d.), *available at*https://fastercapital.com/content/What-Is-a-Token-Sale-and-How-Do-They-Work.html.
[133]*Id.*

Tokens can be employed to access the product or service of a project, or they can be traded on a cryptocurrency exchange. Token sales are:[134]

- Open to everyone regardless of their investor status;
- Fast in that raise millions of dollars in several hours;
- Flexible because there are typically no purchasing limitations;
- Transparent because they are usually conducted on a public ledger that is visible to everyone;
- Global in the sense that they are open to investors around the planet.

A significant benefit of a token sale is that an entity can raise money without giving up equity, thereby permitting projects to maintain control of an organization. Tokens are also a mechanism for investors to invest at a relatively low cost in a potentially profitable project. If successful, the token can significantly increase in value. However, if the project is unsuccessful, the token's value could fall to zero or near zero.[135] Two other risks are that the project could be a scam or hackers could steal tokens out of a digital wallet. Even so, token sales are currently a popular way to generate money for new projects, and as blockchain technology matures, there will likely be more token sales in the future.[136]

How Does a Token Sale Work?

A token sale is a fundraising methodology that trades a future cryptocurrency for an existing cryptocurrency. Typically, only a percentage of the tokens are sold to ICO participants, while a percentage of the tokens is kept by the company for private investors. Token sales are often used to fund the development of new cryptocurrencies. When a firm desires to raise money via an ICO, it generates a whitepaper plan that states the purpose of the project, what needs the project will fulfill, how much money is required to complete the venture, how many tokens will be kept by the founders, what kind of money is acceptable, and how long the ICO will exist.[137] Tokens can usually be purchased with real or virtual currency. If an entity raises the minimum funds required, the firm returns the money to the purchasers, and the ICO is deemed a failure. If the fund requirements are achieved, the money raised can be used to begin a new scheme or complete the specified project.[138]

Key questions that a potential investor should ask before investing in a token sale are:

- ***Who is behind the token sale?***The team should consist of developers, business professionals, and early investors who have a proven blockchain and cryptocurrency track record and can effectively articulate their project vision.
- ***What is the project's roadmap?***The roadmap should include the development, marketing, and business milestones.
- ***What exchanges will the tokens be listed on?***The majority of token sales are conducted on Binance, Huobi, and OKEx, which are all Ethereum-based exchanges.

Types of Tokens Offered at a Token Sale

The three different types of tokens are equity tokens, utility tokens, and security tokens. Equity tokens represent ownership in the blockchain project. Utility tokens permit an owner to access the products or services of the completed project but do not grant ownership rights to the project. Security tokens are similar to tokens in that they are an investment in a blockchain project, but are subject to regulatory restrictions.[139]

Equity tokens are usually offered in the early stages of a project but do not bestow voting rights on the project's assets or profits. Equity tokens must be registered with the SEC before they are sold to investors.[140] Utility tokens only provide holders with access to the products or services offered by the completed blockchain project. They have no ownership rights and are not subject to securities laws or regulations.[141] In other words, utility tokens may be offered to investors without registering them with the SEC. Security tokens confer ownership rights and are subject to regulatory restrictions before being offered to investors.[142]

The type of token offered in an ICO depends on the nature of a project and the associated regulatory environment. Equity tokens are usually offered when a project is in its early stages, whereas utility and security tokens can be offered at any stage of the project's development.[143]

Issues with Token Sales

United States law broadly defines a security. The SEC and U.S. courts employ the *Howey Test* in defining a security to be any contract, transaction, or scheme where a person:[144]

- Invests money or anything else of value;
- In a typical enterprise, which different courts define differently;
- Is led to expect profits; and
- Predominantly is from the efforts of senior management.

If a utility token has security-like features or meets the *Howey Test*, it is a security and should be treated as such.

Myths, Reality, and What to Remember

Here are some myths, realities, and things to remember regarding token sales.[145]

- ***Myth:*** If a company does not sell to United States investors, it does not need to do AML/KYC mitigation.
  Reality:AML/KYC requirements are distinct from securities regulations, dealing with money laundering issues, and are governed by FinCEN, not the SEC. Without doing AML/KYC, one does not know whether an investor is from the United States or another country.
  Remember: Selling unregistered securities to United States investors is a strict liability offense.

- ***Myth:*** A company can just require investors to certify that they are not Americans.

[134]*Id.*
[135]*Id.*
[136] Id.
[137]*Id.*
[138]*Id.*

[139]*Id.*
[140]*Id.*
[141]*Id.*
[142]*Id.*
[143]*Id.*
[144]*SEC v. W.J. Howey Co. et al.*, 328 U.S. 293 (1946), *available at*https://supreme.justia.com/cases/federal/us/328/293/.
[145] How to Launch a Token Sale Legally in the U.S., *Dilendorf Khurdayan PLLC* (n.d.), *available at*https://dilendorf.com/wp-content/uploads/2018/05/How-to-Launch-ICO-In-the-US-1.pdf.

Reality: It is illegal to sell unregistered securities in the United States, regardless of whether one knows the buyer is American or intends to sell to Americans.
Remember: Issuers are strictly liable.

- ***Myth:*** One can only sell to professional or institutional investors in the United States.
Reality: Accredited investors do not have to be professional or institutional investors.
Remember: An accredited investor includes a natural person who earned income that exceeded $200,000 (or $300,000 together with a spouse) in each of the prior two years and reasonably expects the same for the current year or has a net worth over $1 million, either alone or together with a spouse (excluding the value of the person's primary residence). An accredited investor may also be an entity such as a bank, partnership, corporation, nonprofit, or trust when the entity satisfies certain criteria.

- ***Myth:*** If the company uses a Simple Agreement for Future Tokens (SAFT), it does not need to worry about securities regulations.
Reality: Everyone agrees that a SAFT is a security.
Remember: Tokens may be securities.

- ***Myth:*** If a firm uses a SAFT, the tokens it issues under the SAFT will not be securities.
Reality: Tokens may be securities whether or not a SAFT is used.
Remember:Using a SAFT does not transform a security into a non-security. There is no bright-line rule, and the timing of others' efforts is irrelevant.

- ***Myth:*** A company must register with the SEC to sell tokens in the United States.
Reality: If a token is a security, it may qualify for an exemption from registration.
Remember: As a practical matter, there is usually no need to register because one can typically structure an ICO to qualify for an exemption.

Securities Regulations

Here is information about SEC Rule 506(c) (Regulation D), SEC Rule 901 (Regulation S), and the Integration Doctrine. The section also lists the characteristics of a compliant token sale.

Overview of Regulation D

The following is a summary of Rule 506(c) of Regulation D:[146]

- No restrictions on advertising and general solicitation is permitted;
- No prospectus is required, although issuers generally release a private placement memorandum;
- Only accredited investors may participate in a token sale;
- Issuers can raise an unlimited amount of funds;
- Form D must be filed with the SEC after the sale but does not need SEC approval;
- State securities laws are pre-empted, which means that there is no need to seek registration or exemption on a state level;
- Purchasers cannot transfer their securities for one year, subject to certain exceptions; and
- No financial reporting requirements for the issuer.

Concurrent Regulations D and S

Although not as well-known as Regulation D, token sponsors should structure a concurrent offering under Regulation S for non-U.S. investors.[147]

- ***Advantage:*** Non-U.S. investors under Regulation S do not have to undergo the same accreditation process as U.S. investors under Regulation D. If a firm does not use Regulation S for foreigners, it must accredit all their investors under Regulation D, not just U.S. investors.
- ***Advantage:*** *Non-U.S. investors who are not distributors or affiliates of the issuer or distributors can resell immediately to non-U.S. investors.*

Overview of Regulation S

Rule 901 says that offers and sales outside the United States do not have to be registered. However, the SEC has never clearly explained when an offer and sale occur outsidethe United States, so one should not rely only on Rule 901. Fortunately, Rule 903 provides a safe harbor, provided an offer and sale satisfy the following requirements:[148]

- The sale occurs outside the United States:
- The offer and sale are conducted in an offshore transaction;
- No directed selling efforts are made in the United States; and
- Specific other requirements described in 903(b) are satisfied.

Integration Doctrine

The SEC can treat multiple offerings under different exemptions as a single offering. In other words, using one exemption might destroy one's ability to use another exemption. Both offerings could fail. For example, Rule 506(c) (Regulation D) says that one can openly advertise securities in the United States, but Rule 903 (Regulation S) says that one cannot make directed selling efforts in the United States. These two rules are potentially contradictory. Although the SEC has stated that concurrent offerings are fine, it has not provided clear guidance as to what sorts of activities might cross the line and require integration.

A Compliant Sale under Regulations D and S

For a compliant sale, here are the issues:[149]

- ***How long does the token sale take?*** Three to four weeks.
- ***What's involved in a token sale?*** At a minimum, what is needed is a:
  - Determination of the appropriate sales structure;
  - Preparation of a private placement memorandum;
  - Preparation of a purchase agreement;
  - Preparation of necessary investor questionnaires;
  - AML/KYC checks and investor verifications; and
  - Filing Form D with the SEC.

[146] *Id.*

[147] *Id.*
[148] *Id.*
[149] *Id.*

- ***Anything else that needs to be done?*** Additional tasks may include:
  - Review of advisory and marketing arrangements;
  - Referral and bounty programs advice;
  - Arrangements with ICO platforms; and
  - Broker-dealer licensing.

Questions to Ask the Client

There are various questions that a client could be asked. Initially, general questions such as what follows could be asked:

- What is the desired name of the token?
- How much money is to be raised?
- How many tokens are outstanding?
- How many tokens are expected to be sold?
- What is the nature of the project?
- Why raise money through selling tokens rather than traditional methods such as borrowing money from a financial institution, issuing bonds, or selling shares of stock?
- How familiar is a client with the mechanics of ICOs?

Presuming that the client is adamant about raising money via an ICO, the client should be made aware that not all tokens will be immune from SEC and FinCEN scrutiny. The client should be advised that if the token to be issued is an equity or security token, the appropriate regulatory agencies must be notified, and the proper forms submitted for government approval before the new token is marketed or sold. If the client wants to issue a utility token, they should be advised that the *Howey Test* could apply, transforming the token in the eyes of the federal government from a utility token to either an equity or security token. The Munchee, Inc. case should be discussed, where the SEC halted an ICO because of registration concerns.[150] It should also be pointed out that a token sale could still proceed if the token is exempted from registration. Finally, the client should be made aware of the myths and realities of token sales so that if the token sale proceeds to fruition, the client has no illusions regarding the transactions. This is important to achieve if only to avoid surprises along the way to raise the needed money.

Token Sales Conclusion

Token sales as a mechanism for raising capital seem to be gaining traction. The issue with token sales is that if the sale satisfies the *Howey Test*, then the token is a security token that needs to be regulated by the SEC, whereas if a fails the *Howey Test*, it is likely a utility token where token owners can use the token to purchase goods or services from the token-originating firm. The critical issue facing a company that desires to offer tokens to the public or a select group of individuals is that the token cannot walk like, quack like, or fly like a security. Token sales are an alternative to raising capital via a bond or equity sale. However, if an organization ignores the stringent SEC requirements regarding token sales, it may find itself in legal hot water that may be difficult to extradite itself.

QUESTIONABLE MARKET PRACTICES

In this section, the contents of the Larry David, Tom Brady, and Gisele Bündchen commercials are described. The class action suit against Sam Bankman-Fried and a host of celebrities that endorsed FTX Trading Ltd. (FTX) are highlighted. The arguments for and against the celebrities being liable are analyzed using the Issue, Rule, Analysis, and Conclusion (IRAC) method. The issue is whether celebrities who endorse a product or service are liable if the product or service causes harm. Three possible rule violations are discussed based on 16 CFT 255. The standard of proof in a civil action is the preponderance of the evidence. In the analysis subsection, it is shown that David, Brady, and Bündchen are likely not crypto experts. It is also demonstrated that they probably did not have knowledge that FTX accounts were fraudulent and that the accounts were not securities according to the *Howey* test. The existing federal case law (Kardashian et al. case) seems to indicate that David, Brady, and Bündchen are not liable. Finally, reasons why the celebrities were likely not actual consumers are outlined. The essay concludes that the arguments pointing to liability are weak, while the arguments against liability are strong. Thus, the court will probably not find the celebrities liable.

Content of Larry David Advertisement

In the Larry David commercial, David plays a series of short roles that reveal his response to inventions over thousands of years.[151] In the first scenario, David comments that a wheel is useless. In the second role, David is a Catholic monk who decries a fork. The third scenario depicts David as reviewing a toilet, remarking that humans should relieve themselves outside rather than inside. In the fourth scene, David rejects drinking coffee, and feels like he “has a big job coming on.”[152] In the fifth role, David is portrayed as one of the signers of the Declaration of Independence, where he grabs the document because stupid people will be allowed to vote. In the next scene, David complains to Thomas Edison, one of the greatest inventors of the 19th Century, that the electric light bulb invention stinks. David then negatively critiques automatic dishwashers, followed by sending an individual to the moon. In the ninth short, David criticizes the Sony Walkman at a meeting of Japanese managers because it will always need batteries. Finally, David is introduced to FTX but rejects it, claiming that he is never wrong about these things.[153] In the all scenes in this commercial, David’s characters are against what is being presented. The implication of this commercial is that if David or David’s characters are against something, you, the viewer, should be for it.

Larry David is an American comedian, writer, actor, and television producer.[154] David and Jerry Seinfeld created the television sitcom *Seinfeld*, where David was head writer and executive producer for the first seven seasons.[155]Because of David's work on *Seinfeld*, he received two Primetime Emmy Awards in 1993, for *Outstanding Comedy Series* and *Outstanding Individual Achievement in Writing in a Comedy Series*.[156]David was nominated but did not win 17 other times.[157] Thus, Larry David is an accomplished comedian, writer, actor, and television producer who is well-known by the public.

[150]SEC Staff, PressRelease:CompanyHalts ICO After SEC Raises Registration Concerns, *U.S. Securities and Exchange Commission* (Dec. 17, 2017), *available at*https://www.sec.gov/news/press-release/2017-227.

[151]FTX, FTX Super Bowl Don't miss out with Larry David, *YouTube* (Feb. 14, 2022), *available at* https://www.youtube.com/watch?v=hWMnbJJpeZc&t=1s.
[152]*Id.*
[153]*Id.*
[154]Adam Augustyn, Larry David, *Encyclopedia Britannica* (Apr. 11, 2024), *available at*https://www.britannica.com/biography/Larry-David.
[155]*Id.*
[156]Larry David, *TelevisionAcademy* (n.d.), *available at*https://www.emmys.com/bios/larry-david.
[157]Larry David, *TV.com* (n.d.), *available at*https://web.archive.org/web/20080222014739/http://www.tv.com/larry-david/person/8236/biography.html.

Content of Tom Brady Advertisement

In this commercial, Tom Brady and his then-wife, Gisele Bündchen, are having a conversation in their kitchen.[158]Bündchen tells Brady about FTX and asks him to call all of his friends. Brady and Bündchen then proceed to call everyone they know, inquiring whether "they are in," meaning that they will or are invested in FTX. Brady and Bündchen call ten of their friends, and everyone says that they are in. It is important to note that there are 10 scenarios in the David commercial and 10 people that Brady and Bündchen call.[159] The implication is that one person who is invested in FTX can convince 10 other people to invest in FTX. In other words, knowledge about FTX is growing exponentially, and the average individual would be prudent to also invest in FTX.Tom Brady was the quarterback for the New England Patriots for twenty seasons.[160] In his final three seasons in the National Football League (NFL), Brady played quarterback for the Tampa Bay Buccaneers. As quarterback, Brady led the Patriots to seventeen division titles (including eleven consecutive from 2009 to 2019), thirteen AFC Championship Games (including eight consecutively from 2011 to 2018), nine Super Bowl appearances, and six Super Bowl titles.[161] As a member of the Buccaneers, with Brady at the helm, the team won the Super Bowl in 2021.[162] In the quarterback position, Brady is considered to be the greatest of all time (GOAT).[163]Bündchen is a famous Brazilian fashion model who is also likely a billionaire in her own right.[164]

FTX Class Action Suit

When the FTX crypto exchange collapsed in December 2022, the attorneys for the plaintiffs filed a class-action suit against Sam Bankman-Fried and various celebrities, including Larry David, Tom Brady, and Gisele Bündchen, who lent their names as endorsers to the cryptocurrency exchange.[165] The complaint posited that FTX customers were purchasing unregistered securities that were regulated by the SEC. Thus, David, Brandy, Bündchen, and the other celebrities were required to reveal details regarding their financial agreements with FTX. The plaintiffs argued that the celebrities violated Florida securities and consumer protection laws by not disclosing specific information about how much they were paid by FTX. The suit also claimed that the celebrities did not perform due diligence before they promoted the company.[166]

The Arguments For and Against Celebrities Being Liable

This section presents the arguments for and against celebrity liability. The issue is whether celebrities who endorse a product or service are liable to consumers or clients if the product or service causes harm.[167]According to 16 CFR 255.5, an "advertiser should clearly and conspicuously disclose either the payment or promise of compensation prior to and in exchange for the endorsement or the fact that the endorser knew or had reason to know or to believe that if the endorsement favored the advertised product some benefit, such as an appearance on television, would be extended to the endorser."[168]According to 16 CFR 255.1(d):[169]

> "Advertisers are subject to liability for false or unsubstantiated statements made throughendorsements, or for failing to disclose material connections between themselves and theirendorsers [see § 255.5]. Endorsers also may be liable for statements made in the course of theirendorsements."

Also, according to 16 CFR 255.2(c):[170]

> "Advertisements presenting endorsements by what are represented, directly or byimplication, to be 'actual consumers' should utilize actual consumers in both the audio and video or clearly and conspicuously disclose that the persons in such advertisements are not actual consumers of the advertised product."

The analysis is divided into four parts. The first part states the standard of proof in civil litigation. The second part addresses whether David, Brady, or Bündchen are experts in crypto markets. The third part deals with whether David, Brady, or Bündchen are liable in the course of their endorsements. The final part concerns whether the commercials should have disclosed that neither David, BradynorBündchen were actual consumers of FTX.

The class action suit against Bankman-Fried and the above celebrities is a civil action. This means that the standard of proof is the preponderance of the evidence (51 percent). To show that David, Brady, Bündchen, and other celebrities are liable, the plaintiffs must demonstrate that it is more likely than not that they violate one or more of the three rules stated above.The first thing to observe is that neither David, Brady norBündchen are experts in the cryptocurrency marketplace. David is a comedian, writer, actor, and producer, Brady is a former NFL quarterback, and Bündchen is a world-class Brazilian model. None of these individuals, nor any of the other celebrities listed in the class action suit, seemingly have expertise in crypto markets, where 16 CFR 255.0(e) states that "an expert is an individual, group, or institution possessing, as a result of experience, study, or training, knowledge of a particular subject, which knowledge is superior to what ordinary individuals generally acquire."[171]

If one argues that any of the celebrities are experts in cryptocurrency, one would have to demonstrate their expertise in a court of law. David's commercial demonstrates his comedic expertise, not his cryptocurrency expertise. In the commercial, David explicitly states that he does not think highly of cryptocurrency. As for Brady and Bündchen, they were portrayed in their commercial as a married couple who were considering getting into cryptocurrency via FTX. There is nothing in this commercial that gives any indication that they were experts in crypto assets.Thus, in both commercials, there is no evidence to suggest that David, Brady, or Bündchen were crypto

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[158]FTX, FTX: You in? Tom Brady, Gisele Bündchen, *YouTube* (Dec. 7, 2022), *available at*https://www.youtube.com/watch?v=-2nqN3uGi98.

[159]*Id.*

[160]*Seegenerally*, NFL Staff, Tom Brady AdmitshisDeparture from Patriots Was Due to Bill Belichick, *Fox Sports* (Feb. 14, 2024), *available at*https://www.foxsports.com/stories/nfl/tom-brady-admits-his-departure-from-patriots-was-due-to-bill-belichick.

[161]*Id.*

[162]Russell Lewis, Tom Brady Leads Tampa Bay Buccaneers To Super Bowl Win Over Kansas City Chiefs 31-9, *National Public Radio* (Feb. 7, 2021), *available at*https://www.npr.org/2021/02/07/965185605/tom-brady-leads-tampa-bay-buccaneers-to-super-bowl-win-over-kansas-city-chiefs-3.

[163] Neil Paine, All The Ways That Tom Brady Is Football's GOAT, *FiveThirtyEight* (Feb. 9, 2021), *available at*https://fivethirtyeight.com/features/all-the-ways-that-tom-brady-is-footballs-goat/.

[164]Stephen A. Silverman, Gisele Bündchen: First BillionaireSupermodel?, *People Magazine* (Jun. 3, 2011), *available at*https://people.com/celebrity/gisele-Bündchen-forbes-names-richest-supermodel/.

[165]Ari Redbord, Tom Brady And Other A-ListersSued For Fumbling FTX Endorsements, *Forbes* (Feb. 1, 2023), *available at*https://www.forbes.com/sites/ariredbord/2023/02/01/tom-brady-and-other-a-listers-fumble-ftx-endorsements-but-will-they-be-held-liable/?sh=3fb81e367d8c.

[166]*Id.*

[167]*Id.*

[168]FTC Staff, 16 CFR Part 255:Guides Concerning the Use of Endorsements and Testimonials in Advertising, Federal Trade Commission (Nov. 4, 2018), available at https://www.ftc.gov/sites/default/files/attachments/press-releases/ftc-publishes-final-guides-governing-endorsements-testimonials/091005revisedendorsementguides.pdf.

[169]*Id.*

[170]*Id.*

[171]*Id.*

market experts. For the court to hold a celebrity endorser liable, the plaintiffs must show that the endorsers knew of the false and misleading statements made by Sam Bankman-Fried at the time that the commercials were made. In Example 4 of 16 CFR 255.1, a well-known celebrity (David, Brady, and Bündchen qualify) appears in a commercial for roasting chickens perfectly in thirty minutes. In the commercial, the celebrity places an uncooked chicken in an oven-roasting bag and then takes a chicken from a roasting bag from a second oven, takes the chicken out of the bag, and proudly declares that the chicken was cooked perfectly. However, during the shooting of the commercial, the celebrity watches five attempts (knowledge by the celebrity) that the chicken is undercooked after thirty minutes and requires sixty minutes of cooking time. In Example 4, the celebrity knew of the misrepresentation.

For the plaintiffs of the class action suit to show that 16 CFR 255.1(d) was satisfied, they would have to show that David, Brady, Bündchen, and other celebrities had actual knowledge that FTX was fraudulent at the time the commercials were made. However, to have such knowledge, FTX would have had to disclose such knowledge to these celebrities or the celebrities would have had to be crypto experts. It has already been shown that the celebrities were not experts in the field, so what remains is the disclosure possibility. However, the disclosure that FTX was fraudulent months after the commercials were made. Thus, it is highly unlikely that the celebrities knew that FTX accounts were fraudulent.According to the Howey test, the FTX accounts were securities because they were a “contract, transaction or scheme whereby 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.”[172] If the FTX accounts were securities, then the celebrities would be subject to a higher standard of care when endorsing the crypto exchange. The problem is that at the time the commercials were made, government agencies had yet to opine on whether the FTX accounts were securities. David, Brady, Bündchen, and others were not experts in the crypto space, and so their opinion, if they had one, carried little or no weight. One cannot know for a surety what the future holds. In other words, the celebrities were not omniscient. FTX accounts were deemed to be fraudulent in December 2022, months after both commercials were made. Thus, the higher standard of care argument does likely not apply.

According to Redbord, other celebrity endorsers have been sued after promoting a cryptocurrency-related product.[173] Kim Kardashian (a television reality star), Floyd Mayweather Jr. (a former boxer), and others were sued for endorsing the EthereumMax (EMAX) token.[174] Kardashian agreed to pay millions in fines to the SEC for not disclosing that they were paid to endorse EMAX tokens. However, in December 2022, a California federal judge dismissed the lawsuit.[175] The court opined that investors should behave reasonably before placing their bets based on the comments of these celebrities. The opposing argument would have to demonstrate that their investment in FTX accounts was reasonable based on the endorsement of the celebrities listed in the case. This would probably be quite difficult to show. Thus, it is again unlikely that David, Brady, Bündchen, and others will be liable. In the David commercial, he is portrayed as a skeptic, not as a consumer of an FTX account. This means that David cannot be held liable for violating 16 CRF 255.2(c). However, in the Brady and Bündchen commercial, they are depicted as consumers who are telling their friends about FTX. From this fact, it could be construed that Brady and Bündchen actually possess an FTX account. Even so, they are celebrities, and it is publicly well-known that celebrities endorse products for a fee. Both Brady and Bündchen are quite wealthy, so it would be naïve to believe that they are actual consumers. Besides, the commercial has a comic twist at the end, where the final individual with whom Brady shares information about FTX hates him. The person says that he is into FTX but still hates Brady. This verbal exchange likely indicates that Brady and Bündchen were not necessarily actual customers but paid to promote FTX for a fee.

If it is shown that David, Brady, Bündchen, and other celebrities are liable, then a precedent has been set for other celebrity endorsements for products or services that have nothing to do with crypto markets. The result would likely be that celebrities would no longer want to endorse any product or service for fear of being sued. For example, if a celebrity was a spokesperson in an automobile commercial, would the celebrity be liable if the car was recalled to fix a defect? This would have dramatic economic consequences that stifle advertising in general. Thus, for economic reasons, the court would likely decide not to hold the celebrities liable.

This subsection presented both positive and negative arguments regarding whether David, Brady, Bündchen, and other celebrities are liable for endorsing FTX accounts when they knew or should have known that FTX accounts were or were not securities. Based on the arguments above, the arguments favoring liability seem to be weak, whereas the arguments against liability are likely quite strong. Thus, the case against David, Brady, Bündchen, and other celebrities should probably be dismissed.

Market Practices Conclusion

In this section, the issue was whether a celebrity is liable when they promote a token, particularly when the token-originating organization faces intense legal scrutiny, such as in a bankruptcy or indicted for criminal fraud. If a celebrity is using a communication medium that is commonly employed to express personal opinions (e.g., Facebook, Twitter, etc.), there may be a liability case to be made. On the other hand, if the communication medium is a thirty or sixty-second television commercial, there seems to be little likelihood that the general public can be deceived into believing that the celebrity is voicing their personal opinion. The general public has seen tens of millions of television commercials and is sufficiently sophisticated to recognize that a celebrity has been hired as a spokesperson, not necessarily asserting their personal opinion. In other words, when television commercials are the communication medium, it is unlikely that a viewer will be swayed by the words spoken by a celebrity.

CONCLUSION

In conclusion, there are a host of issues that a firm faces in deciding whether to offer a token sale. The critical issue is whether the SEC will deem a token a security token that is subject to government oversight, rather than a utility token where no regulation is mandated. There are plenty of myths surrounding token sales that have the potential of embroiling a company in legal action if it does not pay particular attention to the purpose of the token, the documentation associated with the token, who is authorized to sell the token, what regulations govern the sale of the token, and who are the intended customers. The key to a successful token sale is to carefully review a token’s features, not only from the perspective of the token-originating organization but also from a regulator’s standpoint. Then, and only then, will an entity likely conduct a successful token sale with the minimum degree of government interference. It is the nature of the beast.

[172] *SEC v. W.J. Howey Co. et al.*, *supra*, note 144.
[173] Ari Redbord, *supra*, note 165.
[174] *Id.*
[175] *Id.*

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LIST OF ABBREVIATIONS

Abbreviation	Description
AML/KYC	Anti-Money Laundering/Know Your Customer
ATR	Average True Range
CACU	Crypto Assets and Cyber Unit
CEA	Commodity Exchange Act of 1936
CFCT	Commodities Futures Trading Commission
CIP	Customer Information Program
DoJ	United States Department of Justice
EMAX	EthereumMax
FCM	Futures Commission Merchant
Fed	Federal Reserve Bank
FinCEN	Financial Crimes Enforcement Network
FTX	FTX Trading Ltd.
GOAT	Greatest Of All Time
ICA	Investment Company Act of 1940
ICO	Initial Coin Offering
IEO	Initial Exchange Offering
IoT	Internet of Things
IRAC	Issue, Rule, Analysis, and Conclusion
IRS	Internal Revenue Service (IRS)
NCET	National Cybersecurity Enforcement Team
NFL	National Football League
NFT	Non-Fungible Tokens
OFAC	Office of Foreign Assets Control
PII	Personally Identifiable Information
Regulation D	SEC Rule 506(c)
Regulation S	SEC Rule 903
SAFT	Simple Agreement for Future Tokens
SEC	Securities and Exchange Commission
Treasury	United States Treasury
USPS	United States Postal Service
WEF	World Economic Forum

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