



Insight

SEC Launches Major Crypto Offensive With Lawsuits Against Binance and Coinbase

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Executive Summary

- The Securities and Exchange Commission (SEC) signaled a major crackdown on the crypto industry with a series of lawsuits against industry giants Binance and Coinbase.
- In these lawsuits the SEC continues to assert that digital assets represent securities and appropriately come under its purview.
- The crypto industry cannot be ignored any longer; if Congress fails to pass regulation clarifying the appropriate legal treatment of digital assets and identify the appropriate regulator, the SEC will make these choices itself, expanding its own responsibilities, and in so doing create a hostile environment for future innovation.

Context

On June 5 and 6, the SEC announced major lawsuits against the world's largest digital currency exchange, [Binance](#), and the largest exchange based in the United States, [Coinbase](#). While Securities and Exchange Commission (SEC) Chair Gary Gensler has not proven reluctant to issue enforcement actions against crypto companies, particularly after [the collapse of FTX](#), these suits represent a significant new step both in the SEC's battle against crypto and its continued arrogation of regulatory responsibility over the crypto landscape.

While the two sets of lawsuits are quite different, fundamentally both Binance and Coinbase have been accused of failing to register their exchanges with the SEC, something they would only be required to do if the cryptocurrencies on their exchanges would be more appropriately considered securities rather than commodities. This represents unsettled law – digital assets as a concept being significantly newer than the decades-old securities regulatory framework that grants the SEC its regulatory scope and powers.

In lieu of a comprehensive digital asset framework, Chair Gensler asserts that cryptocurrencies are securities because he says so. It is curious, then, that these lawsuits were announced very shortly after House Republicans released a [discussion draft](#) of a digital asset framework that would invest primary regulatory authority over crypto in the Commodity Futures Trading Commission (CFTC) rather than the SEC.

The Charges Against Binance and Coinbase

On June 5, the SEC filed 13 civil charges against the Binance exchange and its founder Changpeng Zhao, alleging that Zhao had operated “a web of deception” and “mishandl[ed] billions of dollars” by sending customer funds secretly to other companies operated by Zhao. In its 136-page complaint, the SEC accuses Binance of misleading investors about the strength of its internal controls, misleading regulators about the scope of its operations, illegally allowing U.S. consumers to trade on its international platforms, and other crimes. These lawsuits are only the latest in a series of regulatory scrutiny for Binance after the CFTC levied its own

charges in March; the Justice Department is also investigating the exchange for money-laundering. The SEC subsequently filed a [motion to freeze Binance's assets](#).

On June 6, the SEC sued Coinbase for operating as “an unregistered broker, exchange, and clearing agency” making billions of dollars as the middleman on crypto transactions while failing to meet investor disclosure requirements. The SEC also specifically called out 13 crypto assets traded by Coinbase as being securities that ought to have been registered with the SEC.

Analysis

At the heart of these lawsuits is the question of whether cryptocurrencies and other digital assets represent a novel form of asset deserving of their own regulatory framework or whether they are simply, as Chair Gensler asserts, the digital version of securities already supervised by the SEC. If the primary purpose of a cryptocurrency is to be used to pay for goods and services, it would be appropriate to classify it as a commodity, like a metal. If instead a cryptocurrency is primarily a financially tradeable instrument, it would be appropriate to classify it as a security. This represents the most important question to answer when considering the appropriate regulation of digital assets, and both arguments have their strengths and weaknesses. What is not clear is whether it is appropriate that the SEC, as an involved party, should make this determination.

The ramifications of this ramp up in enforcement are clear – crypto exchanges should expect more of the same. Because most exchanges offer tokens that operate on blockchain, they should not expect to be treated any differently. But the SEC should have to answer why it has chosen to exercise dubious authorities to such a significant extent without waiting for direction from Congress. In its suit against Coinbase, the SEC noted: “By collapsing these functions into a single platform and failing to register with the SEC as to any of the three functions...Coinbase has for years defied the regulatory structures...” By the SEC’s own admission, crypto exchanges have operated with at least implied permission for years. What has changed?

These arguments are expected to feature prominently in the certain counterclaims Binance and Coinbase will bring against the SEC to preserve their businesses. Regardless of the success of any of these lawsuits, the SEC’s actions will have had a chilling effect on the crypto industry, giving crypto companies even more of a reason to pursue business outside of the United States for fear of stricter regulatory scrutiny. The irony is that crypto companies are by and large keen for regulatory clarity, although preferably less stringent than that identified by the SEC. The result of these lawsuits may not even be hugely important to the SEC; the suits could simply be the tool that the SEC leverages to force crypto companies to agree to the consent orders that will allow the agency to set the de facto regulatory standard.

Without a clearly defined regulatory apparatus, the United States cannot continue to foster innovation while protecting consumers and investors. Congress has an opportunity to set broad industry guardrails, protect consumers and investors, and create a unified vision for the new market that best employs regulatory resources and fosters innovation in U.S. financial markets. That opportunity is swiftly disappearing as the SEC sets the standard instead.

Conclusions

To give SEC Chair Gensler credit, he has not been inconsistent in his assault on crypto (although news that he had [offered to serve as an advisor to Binance's parent company](#) in 2019 should certainly muddy the waters). While the SEC’s stance on crypto has been clear since the collapse of FTX, just because something is expected does not make it appropriate. Congress should consider digital asset legislation to determine how they should be regulated and which supervisor should do so. Until it does, the SEC has demonstrated that it will continue to regulate by enforcement, do little to ameliorate the confusion surrounding digital asset regulation, further

encourage crypto companies to take their business outside the United States – and in so doing expand its own regulatory fiefdom.