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and thus securities.

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*By Sarah Wynn, CQ-Roll Call (TNS)*

The Securities and Exchange Commission (SEC) fired a warning shot at the cryptocurrency industry when it filed an insider trading case that declared several digital assets qualify as securities, according to those closely following the agency.

The SEC last month charged a former Coinbase Global Inc. manager for tipping off

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could also be implicated.

Less certain are the immediate consequences on crypto exchanges, Reiners said. He said it's likely that exchanges are nervously reading through the SEC's complaint, looking at what is currently listed on their platforms, and comparing that to how the SEC views the nine digital assets in question.

Reiners said he does not see the SEC filing complaints against exchanges until a court has weighed in on whether the tokens in question are in fact securities.

"They'll wait and then if the court agrees with them, of course at that point the exchanges themselves will be forced to register," Reiners said. "To me, maybe it's a longer process to getting to a desired outcome, but I think in the SEC's case it's a more surefooted way to get to the desired outcome, which is to have crypto exchanges brought into the securities regulatory perimeter."

In the insider trading case, the agency charged Ishan Wahi, 32, of Seattle, with tipping his brother and a friend off about which cryptocurrencies were about to be traded on the platform, allowing them to profit from a jump in prices, according to a complaint filed in the U.S. District Court for the Western District of Washington. The Justice Department also brought charges against all three for wire fraud.

Crypto backers have criticized the SEC's approach, calling it regulation by enforcement. Critics have warned that crypto is rife with fraud and is harming retail investors. Over the past year, SEC Chair Gary Gensler has said that most cryptocurrencies are investment contracts and thus securities. Crypto exchanges are also likely trading securities and should be regulated, Gensler has said.

Reiners said the SEC's move finally backed up what Gensler has been saying for a while.

“So this is sort of like the SEC walking the talk,” he said.

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If the case goes to trial, the SEC will have to prove that at least one of those underlying assets is a security, and the precedent from that part of the litigation could bring more certainty as to when digital assets are securities, Guillén said.

“The shockwaves that this case created and the attention it is receiving may result in Congress and other regulators taking actions to create more certainty in the crypto space,” she said.

## Ripple effect

The agency has declared crypto to be securities in the past. In 2020, the SEC alleged that Ripple Labs Inc., a San Francisco-based technology company, and two of its executives raised over \$1.3 billion through an unregistered securities offering of digital assets known as XRP.

But that case is on different footing from the Coinbase insider trading action, said Christopher LaVigne, a partner in the litigation team at law firm Withers.

“The SEC has potentially sidelined the issuers of those digital assets and the SEC has put itself at a strategic advantage to secure a potential back door ruling that numerous digital assets listed on Coinbase’s exchange are securities,” LaVigne said.

He declined to predict how the lawsuit will go. It is possible that the SEC could prevail and secure a ruling from a federal court that the underlying assets are securities.

“If they do that, they can then take that and use it as a premise, for example, suing the issuers of the underlying assets directly ... they’ve already got a leg up in that hypothetical potential future lawsuit because they already have the ruling in hand,” he said.

The backers of some of the cryptocurrencies labeled as securities in the SEC's insider

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However, Bloomberg News reported on July 25 that Coinbase is facing an SEC probe into whether it improperly let people trade digital assets that should have been registered as securities, citing three people familiar with the matter.

Coinbase declined to comment on that, but the company's chief legal officer, Paul Grewal, said the exchange has faith in its process.

"We are confident that our rigorous diligence process — a process the SEC has already reviewed — keeps securities off our platform, and we look forward to engaging with the SEC on the matter," Grewal said in an emailed statement.

Shortly after the SEC's charges, Grewal said in a statement that Coinbase "100 percent" disagreed with the SEC's decision to file securities fraud charges, and emphasized that none of the cryptocurrencies in question are securities.

Coinbase also announced that it had filed a petition asking the SEC to begin rulemaking on digital assets.

"Crypto assets that are securities need an updated rulebook to help guide safe and efficient practices," said Faryar Shirzad, the company's chief policy officer, in a post on Coinbase's website. "Crypto assets that are not securities need the certainty of being outside those rules."

The industry has some regulators on its side. Caroline Pham, a commissioner for the Commodity Futures Trading Commission, in a rare cross-agency comment, called the SEC's enforcement action a "striking example of 'regulation by enforcement'" and said it could have broad implications.

The CFTC declined to comment about whether it planned to bring its own enforcement actions against the three defendants in the Coinbase case.

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