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**COMMENTARY**

*Implications Following the SEC's Crackdown on Cryptocurrency  
Regulation*

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Cryptocurrencies have become increasingly prevalent in financial markets globally, yet it remains unclear how this type of financial instrument will be regulated. The Securities Exchange Commission (SEC) has intensified its regulatory scrutiny of cryptocurrencies, highlighting difficulties about how such assets should be classified under U.S. securities law. The recent ruling in *SEC v. Ripple Labs* raises important questions about how these digital assets fit within the framework of U.S. securities law.

**I. The SEC's Lawsuits in the Cryptocurrency Sector**

The SEC has taken an aggressive stance in treating cryptocurrencies as unregistered securities, initiating lawsuits against major cryptocurrency platforms for alleged violations of security laws. In *SEC v. Ripple*, Judge Torres concluded that Ripple's (XRP's) institutional sales met the definition of unregistered securities, where programmatic sales to the public did not.<sup>1</sup> This distinction between institutional and programmatic sales rested on the nature of each transaction type. Institutional sales involved direct contracts with sophisticated buyers who had clear knowledge of Ripple's efforts to grow the network of technologies, applications, and services built around its digital asset, XRP.<sup>2</sup> In contrast, programmatic sales occurred anonymously on public exchanges, where buyers did not know they were transacting directly with Ripple and lacked the same basis to expect profits specifically from Ripple's management efforts.<sup>3</sup> This difference in buyer expectation underscores the regulatory gray area and highlights the challenges in applying traditional securities law to decentralized assets.

Furthermore, relying heavily on litigation to guide regulatory policy introduces significant ambiguity. A case-by-case enforcement strategy will not provide the industry

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<sup>1</sup> *SEC v. Ripple Labs, Inc.*, 682 F.Supp.3d 308, 313 (S.D.N.Y. 2023).

<sup>2</sup> *Id.*

<sup>3</sup> *Id.*

with the clarity it needs.<sup>4</sup> Going forward, the SEC must advocate for legislative reforms that clarify the classification of digital assets, particularly for platforms offering multiple types of token sales.

## II. Are Cryptocurrencies Securities?

The central question of whether cryptocurrencies qualify as securities relies on the *Howey* Test, which evaluates whether an investment is made with the expectation of profits derived from the efforts of others.<sup>5</sup> Although the SEC contends that many cryptocurrencies meet this standard, the courts have yet to provide a uniform ruling applicable to all digital assets.<sup>6</sup>

While the SEC's "Framework for Investment Contract Analysis of Digital Assets" provides some guidance, uncertainty persists.<sup>7</sup> Given the decentralized nature of most blockchain-based projects, identifying the responsible parties who generate value is difficult.<sup>8</sup> The confusion around cryptocurrency's legal classification has led to conflicting rulings, leaving the crypto industry to operate in a regulatory gray area.<sup>9</sup>

## III. Consequences for Cryptocurrency Companies

The *Ripple* decision and SEC enforcement actions have potentially far-reaching implications for cryptocurrency companies. Regulatory uncertainty has already prompted businesses to reconsider operating in the U.S.<sup>10</sup> For example, some companies have limited their services or relocated to countries with looser regulations.<sup>11</sup> If digital assets continue to be classified as securities in some circumstances without consistent guidance, compliance costs could increase tremendously.<sup>12</sup> Consequently, innovation could be stifled which is particularly problematic in an industry already grappling with rapidly changing technological demands.

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<sup>4</sup> See Jacqueline Hennelly, Note, *The Cryptic Nature of Crypto Digital Assets Regulations: The Ripple Lawsuit and Why the Industry Needs Regulatory Clarity*, 27 FORDHAM J. CORP. & FIN. L. 259, 295 (2022).

<sup>5</sup> See *id.* at 282; see also 22 AM. JUR. 3D *Proof of a "Security" under Federal and State Statutes* § 29 (2024).

<sup>6</sup> See *Framework of Investment Contract Analysis of Digital Assets*, U.S. SEC. EXCH. COMM'N, [https://www.sec.gov/about/divisions-offices/division-corporation-finance/framework-investment-contract-analysis-digital-assets#\\_edn1](https://www.sec.gov/about/divisions-offices/division-corporation-finance/framework-investment-contract-analysis-digital-assets#_edn1) [<https://perma.cc/4646-C4QD>] (last modified July 5, 2024) [hereinafter *SEC Framework*].

<sup>7</sup> See *id.*

<sup>8</sup> See generally 1 Thomas Lee Hazen, *Virtual or Crypto Currency and the Securities Law* § 1:80 (2024).

<sup>9</sup> See *id.*

<sup>10</sup> William Chao, *Crypto exchange's jurisdiction-shopping: a regulatory problem that requires a global response*, COLUM. J. OF TRANSNAT'L L. (Feb. 23, 2009), <https://www.jtl.columbia.edu/bulletin-blog/crypto-exchanges-jurisdiction-shopping-a-regulatory-problem-that-requires-a-global-response>.

<sup>11</sup> See generally Jacob G. Stanley, Note and Comment, *A Disruptive Ripple in the SEC's Regulation of Crypto Assets*, 28 N.C. BANKING INST. 476, 502 (2024).

<sup>12</sup> See generally CONGRESSIONAL RESEARCH SERVICE, *DIGITAL ASSETS AND SEC REGULATION* 19, <https://crsreports.congress.gov/product/pdf/R/R46208> (last updated June 23, 2021).

A key challenge for cryptocurrency companies is the SEC broadly categorizing all crypto assets as securities, regardless of the nuances that may apply under the Howie test. While the SEC maintains a consistent approach in treating cryptocurrencies as securities, ambiguity arises once these cases reach the courts, as judges assess each crypto asset's unique characteristics.<sup>13</sup> For example, although Ripple's institutional sales of XRP were deemed securities, the courts did not apply the same classification to Ripple's programmatic sales.<sup>14</sup> This judicial variability creates uncertainty, making it difficult for crypto companies to anticipate how their assets will be classified in enforcement actions.<sup>15</sup>

To resolve this uncertainty, the SEC and the courts need to coordinate their respective efforts. While the SEC's enforcement actions set out an initial rule, ultimately it is the courts that define the legal standards and applications in practice. Greater collaboration or more consistent guidance from both entities could provide cryptocurrency companies with a clearer framework for compliance.<sup>16</sup> This would support judicial efficiency by reducing the need for each asset to be litigated on a case-by-case basis. In the meantime, cryptocurrency companies should invest in legal expertise to equip themselves to navigate the uncertain regulations.

#### **IV. Investor Reactions and Market Consequences**

The SEC's regulatory actions have led to increased market volatility, with investor confidence fluctuating in response to legal rulings.<sup>17</sup> Regulatory uncertainty has contributed to significant swings in cryptocurrency prices, as seen in the aftermath of the SEC's lawsuit against Ripple.<sup>18</sup>

The speculative nature of cryptocurrency investing possesses a risk to unsophisticated investors, many of whom may not fully understand the legal implications of holding assets that could later be deemed securities. SEC enforcement aims to protect these investors, but the current framework may unintentionally harm the broader market by discouraging investors to invest in these types of emerging technology.<sup>19</sup>

The SEC should balance its enforcement actions with education initiatives aimed at both investors and businesses. Clearer guidance on what constitutes a security will help investors make informed decisions, reducing the market's reliance on speculation.<sup>20</sup> Additionally, this would align with the policy supporting security regulations to build transparency and trust between companies and investors.<sup>21</sup> This solution is likely to lead to

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<sup>13</sup> See Hennelly, *supra* note 4, at 268-72.

<sup>14</sup> *Ripple Labs, Inc.*, 682 F.Supp.3d at 313.

<sup>15</sup> See Hennelly, *supra* note 4, at 283.

<sup>16</sup> *Id.*

<sup>17</sup> See Chao, *supra* note 10.

<sup>18</sup> See Stanley, *supra* note 11, at 500.

<sup>19</sup> See Thomas Lee Hazen, Article, *Rational Investing or Speculative Fever? SPACS, Robinhood, and Digital Assets- Securities Markets or Casinos?*, 18 FIU L. REV. 565, 598 (2024); see also 10 Harold S. Bloomenthal & Samuel Wolff, *SEC v. Ripple – Other distributions* § 4A:40 (2024).

<sup>20</sup> *Id.* at 607.

<sup>21</sup> See Stanley, *supra* note 11, at 483.

greater stability in cryptocurrency markets and ensure that protections are in place for all types of investors, not just large institutional players.

**V. Conclusion**

The SEC's approach to cryptocurrency regulation has sparked questions about the future of digital assets in the U.S. While the ruling in *Ripple* offers some insight, it also highlights the needs for a coordinated effort between the SEC and the judiciary to establish clearer regulatory boundaries. Without such collaboration, both institutional and individual investors will continue to face inconsistencies on cryptocurrency classification and subsequent regulation.