

Practice Update

Consumer Regulators' Role in Biden Administration's Framework on Digital Assets

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Earlier this year, President Biden issued an Executive Order on Ensuring Responsible Development of Digital Assets (“Digital Assets EO”). [1] The Digital Assets EO directed over 20 federal agencies to provide the Administration with cryptocurrency policy recommendations that the White House intended to incorporate into a federal regulatory framework. The results of this work were announced on September 16th.

Background

The Digital Assets EO highlighted six priorities:

1. consumer and investor protection;
2. financial stability;
3. illicit finance;
4. U.S. leadership in the global financial system and economic competitiveness;
5. financial inclusion; and
6. responsible innovation.

The Digital Assets EO directed the Consumer Finance Protection Bureau (along with the Attorney General and the FTC) to focus on the “effects the growth of digital assets could have on competition

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policy” and “the extent to which privacy or consumer protection measures within their respective jurisdictions may be used to protect users of digital assets and whether additional measures may be needed.”[2] Additionally, the Treasury was tasked with developing an action plan with the Attorney General and other agencies to address “digital asset illicit finance risks” and evaluate “opportunities to mitigate such risks through regulation.”[3]

Overview of Framework

On September 16th, the White House released a broad framework for the federal regulation of digital assets.[4] The framework is contained in a series of nine reports released at the same time by various federal agencies.[5] Although the framework does not create any new statutes or regulations, it represents a significant step towards clarifying regulatory expectations and increasing federal oversight of digital assets, which have fundamentally disrupted the traditional financial landscape and “present potential opportunities to reinforce U.S. leadership in the global financial system and remain at the technological frontier.”[6] Among other things, this framework signals the likelihood of enhanced regulatory oversight by two federal agencies that focus on consumer issues—the CFPB and FTC—and the potential future enactment of legislation to clarify legal obligations and to crack down on illicit financial activities related to digital assets.

Framework’s Treatment of Consumer Protection Issues

The framework calls for broadening the scope of regulatory oversight, pointing to the volatility and recent decline in market capitalization of digital assets. It directs the SEC and CFTC, to “aggressively pursue investigations and enforcement actions against unlawful practices in the digital assets space.”[7] It also calls on the CFPB and FTC to “redouble their efforts” to monitor crypto-related consumer complaints, which have increased

significantly in the past few years.[8] A report issued by the Treasury noted the CFPB Complaint Database contained 2,404 published crypto-asset consumer complaints in 2021 compared to 983 in 2020—which amounts to an increase of over 140%. As of July 15, 2022, the CFPB had 906 complaints year-to-date and 1,870 published complaints in the prior 12 months.
[9]

The Treasury Report explains the CFPB does have jurisdiction over some crypto products. Specifically, the Treasury asserts the CFPB is in a position to regulate “the offering of consumer financial products and services—which, depending on the facts and circumstances, may include a variety of crypto-asset related offerings—under the federal consumer financial laws, including (among others) the Dodd-Frank Act’s prohibition against unfair, deceptive, or abusive acts or practices for consumer financial products and services.”[10] This appears to be the first concrete recognition by the federal government (albeit not the CFPB itself) that the CFPB has jurisdiction over at least some crypto products.

The framework tasks agencies with issuing supervisory guidance relating to crypto-assets in plain language in order to protect vulnerable consumers. For instance, the Treasury Report cites concerns by the Department of Labor with the use of cryptocurrencies as investments in defined contribution plans—including 401(k) plans—demonstrating the need for more plain language guidance.[11]

The framework also encourages collaboration among federal agencies to promote thorough and consistent regulatory oversight of digital assets. For instance, an agency’s sharing of consumer complaints and data with other agencies may “help identify relevant clusters of unlawful activity and spot trends in scams and fraud types.”[12] The Treasury Report noted the increasing volume of crypto-related scams in recent years, citing 46,000 incidents of fraud reported to the FTC between

January 1, 2021, and March 31, 2022—with losses exceeding \$1 billion worth of cryptocurrency assets.
[13]

Illicit Finance Regulations

The framework additionally explores how to prevent the use of digital assets for money laundering and other illicit activities. The White House’s statement on the framework explains, “digital assets have facilitated the rise of ransomware cybercriminals; narcotics sales and money laundering for drug trafficking organizations; and the funding of activities of rogue regimes...”[14] The framework attempts to address these emerging issues through a proposed expansion of the Bank Secrecy Act (BSA), anti-tip-off statutes, and laws related to unlicensed money transmitting, which the framework would have explicitly apply to certain digital asset service providers.

The BSA currently imposes anti-money laundering obligations on “money services businesses” (MSBs). [15] The BSA requires MSBs to register with the Financial Crimes Enforcement Network (FinCEN), implement anti-money laundering controls, and comply with recordkeeping and reporting requirements. But not all digital asset service providers are explicitly covered by the BSA, even when they operate as MSBs. A Department of Justice (DOJ) report recommends amending the BSA to expand its coverage to reach certain types of digital asset providers that may currently not be subject to the Act because they did not take custody over the cryptocurrency or fiat currency.[16] The DOJ also recommends expanding the anti-tip off prohibition to include all criminal offenses under the BSA and other relevant federal laws.[17]

The framework seeks to strengthen the federal law prohibiting operation of an unlicensed money transmitting business, described by the DOJ as a “key prosecutorial tool in digital assets cases.”[18] A business that operates as a money transmitter

without a required state license or federal registration can be criminally prosecuted under 18 U.S.C. § 1960. Yet digital currency exchanges often are not required to comply with registration and licensing requirements. The DOJ report proposes changing the statute to clarify it applies to platforms “providing services that allow consumers to transfer digital assets in a manner analogous to traditional money transmitting businesses.”[19] It also contemplates larger penalties and fines for unlicensed money transfers (including through virtual currency) by amending 18 U.S.C. § 1960. The proposed amendment would increase the statutory maximum sentence from five to ten years imprisonment. An amendment would also include an enhanced penalties provision, under which individual criminal fines would double—and corporate criminal fines would triple—for violations involving a money transmitter’s business of more than \$1 million in a 12-month period.[20]

Impact of this New Regulatory Framework

Although the framework does not create any new statutes or regulations, it attempts to address issues posed by the current patchwork of fragmented and often inconsistent agency directives on digital assets. By delegating specific regulatory responsibilities among federal agencies, it lays the groundwork for a more unified, predictable regulatory environment for cryptocurrency in the future.

Going forward, businesses in the digital assets space should prepare for compliance with more extensive regulatory requirements—including disclosure requirements for registered exchanges, products, and intermediaries designed to provide investors and consumers with relevant, material information, as well as market conduct requirements.

We would be happy to discuss the impact of this framework as regulatory enforcement activity by the CFPB and other agencies predictably rises.

Citations

[1] The White House, *Executive Order on Ensuring Responsible Development of Digital Assets*, (Mar. 9, 2022) at <https://www.whitehouse.gov/briefing-room/presidential-actions/2022/03/09/executive-order-on-ensuring-responsible-development-of-digital-assets/>.

[2] *Id.*

[3] *Id.*

[4] The White House, FACT SHEET: White House Releases First-Ever Comprehensive Framework for Responsible Development of Digital Assets (Sept. 6, 2022) at <https://www.whitehouse.gov/briefing-room/statements-releases/2022/09/16/fact-sheet-white-house-releases-first-ever-comprehensive-framework-for-responsible-development-of-digital-assets/>.

[5] *See e.g.*, U.S. Dep’t of Treasury, *Crypto Assets: Implications for Consumers, Investors, and Businesses*, (Sept. 2022) at https://home.treasury.gov/system/files/136/CryptoAsset_EO5.pdf

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[6] The White House, FACT SHEET, *supra*.

[7] *Id.*

[8] *Id.*

[9] U.S. Dep’t of Treasury, *supra* at 27.

[10] *Id.* at 39.

[11] *Id.* at 52.

[12] *Id.* at 51.

[13] *Id.* at 27.

[14] The White House, FACT SHEET, *supra*.

[15] 31 U.S.C. §§ 5311 *et seq.*

[16] U.S. Dep't of Justice, *The Report of Law Enforcement in Detecting, Investigating, and Prosecuting Criminal Activity Related to Digital Assets* (Sept. 2022) at <http://www.justice.gov/ag/page/file/1535236/download>.

[17] *Id.* at 37.

[18] *Id.* at 36.

[19] *Id.* at 37.

[20] *Id.* at 38.

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