



## Industry Alert:

# Registration of Commodity Brokers-Dealers, Salespersons, and Investment Advisors Doing Business Relating to Virtual or “Crypto” Currency

New York Attorney General Letitia James issues this alert to remind industry members that people and entities dealing in virtual or “crypto” currencies that are commodities or securities in the state of New York, and who do not qualify for an exemption, must register with the Office of the Attorney General. Failure to do so exposes them to both civil and criminal liability.

## Background

For over a quarter of a century, commodity broker-dealers, salespersons, and investment advisors doing business within or from New York have been required by statute to register with the Office of the Attorney General.<sup>1</sup>

Last year the Appellate Division, First Department, held that a virtual currency was a commodity under New York’s Martin Act, and that the Martin Act’s definition of a commodity was broader than the federal definition under the Commodity Exchange Act.<sup>2</sup> Over the past three years, federal and state agencies, as well as courts that have considered the issue, have determined that virtual currencies qualify as commodities, or securities, under the law.<sup>3</sup>

There is also broad consensus in both the state and federal law enforcement spheres concerning the gravity of the risks posed by those operating on the fringes of this market. A recent report by the U.S. Department of Justice concluded that segments of the virtual currency industry are not only enabling old-fashioned versions of international crime (ranging from financing terrorism to money laundering),<sup>4</sup> but are also directly defrauding investors.<sup>5</sup> The Department of Justice echoed findings from a 2018 report issued by the Office of the Attorney General, which found that virtual currency platforms are “highly susceptible to abuse” and that protections for customers are often “illusory.”<sup>6</sup>

And yet, notwithstanding New York’s longstanding registration laws, there is significant non-compliance with registration obligations.<sup>7</sup>

## Failure to Register is a Violation of the Law and Will be Prosecuted

Failure to register as a commodity broker-dealer, salesperson, or investment advisor is both a fraudulent practice and a crime under the Martin Act.<sup>8</sup>

The Martin Act grants the attorney general the authority to bring an action in the name of the people of the state of New York to enjoin fraudulent practices and the doing of any acts in furtherance thereof. Penalties for violation include permanent injunction from selling, offering to sell, or acting as a broker or investment advisor concerning securities or commodities in New York,<sup>9</sup> as well as disgorgement of profits and restitution to victims.<sup>10</sup>

In addition, the Executive Law grants the attorney general the authority to bring an action against a person or entity engaged in repeated fraudulent or illegal acts in the transaction of business, and similarly permits the attorney general to seek an order enjoining future conduct, and to award disgorgement, restitution, and damages.<sup>11</sup>

## Scope of this Alert

This alert is not intended to, and does not, confer any additional substantive or procedural rights beyond the underlying statutes, regulations, and case law.

## Endnotes

<sup>1</sup> Gen. Bus. L. § 359-e(14)(b).

<sup>2</sup> See *James v. iFinex*, 185 A.D.3d 22, 28 (1<sup>st</sup> Dep't 2020).

<sup>3</sup> See *CFTC v. McDonnell*, 287 F.Supp.3d 213 (E.D.N.Y. 2018) (bitcoin is a commodity under the federal Commodity Exchange Act); *SEC v. Kik Interactive, Inc.*, 19 Civ. 5244 (S.D.N.Y. Sep. 30, 2020) (unregistered “initial coin offering” of virtual currency “Kin” violated Section 5 of the Securities Act).

<sup>4</sup> The U.S. Department of Justice's report observed that, “despite its relatively brief existence, this technology already plays a role in many of the most significant criminal and national security threats our nation faces.” U.S. Department of Justice, *Cryptocurrency: Enforcement Framework*, at viii (Oct. 2020).

<sup>5</sup> *Id.* at 15-16.

<sup>6</sup> Office of the Attorney General, *Virtual Markets Integrity Initiative report*, at 5 (2018).

<sup>7</sup> In addition to being commodities, certain virtual currencies are securities under New York law. The Martin Act requires those offering securities to be similarly be registered as a securities dealer pursuant to Gen. Bus. L. § 359-e.

<sup>8</sup> See Gen. Bus. L. § 359-e(14)(j), (l).

<sup>9</sup> See Gen. Bus. L. § 353 (l).

<sup>10</sup> See Gen. Bus. L. § 353(3) (“[u]pon a showing by the attorney general that a fraudulent practice as defined by this article has occurred, [s]he may include in an action under this article an application to direct restitution of any moneys or property obtained directly or indirectly by any such fraudulent practice”); *People v. Ernst & Young, LLP*, 114 A.D.3d 569 (1<sup>st</sup> Dep't 2014) (“where, as here, there is a claim based on fraudulent activity, disgorgement may be available as an equitable remedy, notwithstanding the absence of loss to individuals or independent claims for restitution”).

<sup>11</sup> Executive Law § 63(12); *People v. Greenberg*, 27 N.Y.3d 490, 497-98 (2016).