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DIGITAL ASSET REGULATION: *HOWEY* EVOLVES

*In this article, the authors provide a comprehensive look at the SEC's evolving guidance that aims to clarify when sales of digital assets are securities transactions. The authors discuss the Commission's early application of *Howey* to digital assets, its pronouncements and enforcement actions, and the response of commentators. They then turn to the SEC's Framework, issued in 2019, and other current SEC actions. They close by addressing steps the SEC should take to provide market participants with greater clarity on the application of the securities laws to digital assets.*

By Stephen P. Wink, Witold Balaban, John J. Sikora, Jr. and Miles P. Jennings*

Recent years have seen the birth and striking growth of the global cryptocurrency markets.¹ In the face of this development, the Securities and Exchange Commission has struggled to provide a clear answer to the seminal regulatory question confronting this space in the US: when is a digital asset a security? The SEC's early pronouncements and enforcement actions suggested an expansive understanding of "security" within the world of cryptocurrencies, an approach criticized by a number of commentators and one that jeopardized many cryptocurrency projects. However, in recent months, the SEC has released guidance in the form of an analytical framework for determining when a digital asset constitutes a security, as well as two no-action letters indicating that the applicable tokens would not constitute securities and several enforcement actions involving

initial coin offerings. Consequently, the marketplace is now learning how this emerging approach is applied.

BACKGROUND: THE SEC'S EARLY APPLICATION OF *HOWEY* TO DIGITAL ASSETS

The definition of what constitutes a "security" found in the Securities Act of 1933 and the Securities Exchange Act of 1934 includes a litany of common instruments, such as stocks and bonds, as well as the less familiar term "investment contract." In the 1946 case *SEC v. W.J. Howey Co.*, the Supreme Court gave meaning to this term by stating that an instrument is an "investment contract" if it involves an investment of money in a common enterprise with the expectation of profits to be derived solely from the efforts of others.² For over 70 years, *Howey* has remained the principal test for identifying securities that do not otherwise neatly fall within the listed instruments.

¹ Unless stated otherwise, the terms "digital assets," "cryptocurrency," "token," and "coin" are used interchangeably in this article, and are intended to refer to the spectrum of digital assets issued and transferred using distributed ledger or blockchain technology.

² *SEC v. W.J. Howey Co.*, 328 U.S. 293, 298-99 (1946).

*STEPHEN P. WINK, WITOLD BALABAN, JOHN J. SIKORA and MILES P. JENNINGS are partners at Latham & Watkins LLP. Their e-mail addresses are stephen.wink@lw.com, witold.balaban@lw.com, john.sikora@lw.com and miles.jennings@lw.com. Other co-authors are listed at the end of the article.

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