



A Political Economy of the 2022 Cryptoverse

by Brock Dahl

As revolutionary a year as 2021 was for the cryptoverse, 2022 promises even more significant legal developments that will shape market structure and potential. While some nations imposed outright bans on crypto activities, others, including the U.S., continued to grapple with how to manage the explosive growth. Those tensions will continue in 2022.

The legal landscape for crypto assets, however, is currently mired in conceptual chaos, in part, attributable to the sheer complexity of the underlying capabilities. But that complexity is only part of the confusion. There is an evolving political economy in the cryptoverse, driven by a conceptual competition between market actors and sovereign governments who recognize the way that key assets and activities are defined will make all the difference for their regulatory treatment and their prospects for free societies. The coming year promises to be significant in that many governments are feeling a sense of urgency to land their legal regimes around more established norms. In this brief, we review the key questions we will be asking and key concepts that we will be tracking in 2022 to try to discern the runway lights through the thickening competitive fog.

We first explore the key categories around which regulation must be wrapped: assets, activities, and infrastructure. In any given scenario, answering what activity is being conducted with what asset on what infrastructure is helpful for clarifying the interests that may be implicated by that triangulation. Without knowing those answers, we are susceptible to further semantic confusion and overly broad claims about the potential application of specific, or general, legal authorities. That triangulation also helps clarify the community of interests to which it relates; a given market configuration only

becomes meaningful through human action. In the second part of the brief, we highlight the interested communities to watch whose decisions and behavior, whether through legislation, regulation, or free market enterprise, will influence the continuing emergence of a new order. We make frequent reference to fintech concepts, merely because they provide a more concentrated target of analysis – but this analysis is equally applicable across the broader spectrum of potential to be unlocked by Web3. Indeed, one of the great challenges for the U.S. government will be how to avoid perceiving the digital assets discussed below in overly narrow, often solely financial, terms– and to facilitate the full realization of market potential in such a rapidly changing environment.

Assets, Activities, and Infrastructure

When we write of the cryptoverse, we are referencing the universe of assets and activities that are memorialized in distributed ledger technologies (the most well-known of which is the blockchain ledger for bitcoin). A blockchain is a public ledger that records events, providing the ability to publicly memorialize in an immutable fashion (i.e., which is theoretically not susceptible to later change or abuse) transactions between parties. Engaging in transactions on one of several key blockchains typically involves a token – an asset that is created and or maintained on a given distributed ledger technology.

Fundamentally, government action must be addressed at some particular asset or activity. There are myriad categories of assets and activities in the cryptoverse. The process of categorizing and clarifying the categories of assets and activities about which the government is concerned is likely to be a central piece of the 2022 crypto story. Below, we discuss the concepts and questions pertaining to assets, activities, and infrastructure that are likely to provide heavy signals in 2022.

Assets

Market Classifications: At the most basic level, there are two primary categories of tokens.

Fungible Tokens

As the name implies, fungible tokens are exchangeable with other equal units of the same denomination. The most common example of such a fungible token is a bitcoin. Fungible tokens tend to be conceptually similar to currencies, insofar as they are used for payments and/or as stores of value. Another key example are stablecoins, described further below.

Nonfungible Tokens (NFTs)

Nonfungible tokens represent unique digital assets, such as collectibles, that are stored on the blockchain. The explosion of the NFT art market, where individuals can purchase a token that represents ownership of specific digital art, is perhaps the most prolific example in 2021. NFTs can represent a variety of items, including art, music composition, specific underlying assets, tickets for an event and access to services, and more.

This distinction is hardly informative of the variety of assets available in the marketplace, but it is a good starting point for distinguishing where one is situated in a particular market triangulation.

A second layer to understanding the asset presents more specificity. For example, the Global Blockchain Convergence has proposed a classification system for tokens that offers lucid descriptions of more detailed categories of tokens. It characterizes tokens as (i) physical asset tokens; (ii) services tokens; (iii) intangible asset tokens; (iv) Native DLT tokens; and (v) stablecoins.

Without exploring the thought line too extensively, the GBC makes an appealing argument that most tokens already fall within “a well-developed legal and regulatory regime because they are simply digital representations of existing asset types.” Even if true, however, there seems to be no shortage of debate in the cryptoverse about how to agree on such a mapping. As expressed throughout this piece, that debate is likely as much a product of distinct positional pressures and considerations as it is any purely intellectual contemplation of an asset category by itself. To be certain, though, regulators are currently working within established frameworks in their own characterizations of the assetscape.

Several key categories are mentioned next.

Regulatory Classifications: The thrust of the government’s perspective (read: regulators in varying capacities) is that each of these tokens tends to look like one of several categories of assets over which one of their agencies (further addressed below) has, at least some, authority.

Securities: As is obvious to most readers, the determination that an asset is a security brings it within the ambit of the Securities Act of 1933, Securities Exchange Act of 1934, and, most critically, the Securities Exchange Commission (see below). Such qualification creates a host of costly regulatory and compliance requirements that would fundamentally alter the business of any party offering or dealing in a crypto asset deemed to be a security. In 2022, we should be watching closely for additional action by Congress, the SEC, or courts, more clearly defining the contours of this categorization.

Whether or not a given asset is a security is determined via application of the “Howey Test,” articulated by the Supreme Court in 1946. The Howey Test asks whether an activity constitutes: (i) an investment of money (ii) in a common enterprise (iii) with a reasonable expectation of profits derived from the effort of others.

The SEC has made occasional public statements (and taken more limited regulatory actions) providing one-off insights on the application of these concepts. For example, it had issued guidance in the past regarding analyzing initial coin offerings. More recently, SEC Chairman Gary Gensler has declined to speak to specific assets, such as ether, outside of an enforcement context. In a much cited 2018 speech, William Hinman, the SEC’s then director of the Division of Corporate Finance, stated that bitcoin and ether developers (in GBC’s “DLT native tokens” category above) were not sufficiently centralized to constitute a “common enterprise” under the Howey Test. Though as of the date of this publication, the speech is still available on the SEC’s website without qualification, the SEC has not subsequently repeated that position, and the SEC’s case against Ripple Labs asserts that the company’s sale of a digital asset called XRP was to fund the company’s operations (and enrich the founders). This, it alleged, was a form of capital fundraising and constituted an unregistered securities offering. Though filed before Chairman Gensler’s arrival, one might expect similar logic to be extended to other token offerings. Expect these vines to grow thorns in 2022.

Commodities: Commodities are defined in the Commodity Exchange Act as a list of certain specified agricultural commodities and then “all other goods and articles . . . and all services, rights, and interests . . . in which contracts for future delivery are presently or in the future dealt” (with certain exceptions). As with securities, there is intense debate about whether certain crypto assets should be classified as commodities. According to the ABA, the second portion of the definition was intended to grant the CFTC “expansive authority over futures markets,” but “invites questions on the limits to the CFTC’s jurisdiction.” In a letter to Judge Castel of the Southern District of New York in the *Telegram* case, (19-

cv-09439, Doc. 203), the CFTC's Office of General Counsel maintained that a "[d]igital currency is a commodity." That was a known position (see Sec. IV.A. [here](#)), but then creates an endless loop as to what constitutes a digital currency. Some [courts](#) have also recognized that "[v]irtual currencies can be regulated by [the] CFTC as a commodity[.]" The CFTC acknowledges it has limited authority over "cash markets" (as opposed to futures markets, where its authority squarely sits); the coming year will certainly give rise to heightened debate about the proper authorities necessary to regulate crypto commodities, whether Congress should expand the CFTC's purview, how to understand the rules applicable to crypto assets conceived of as commodities by the CFTC, and what, exactly, are digital currencies.

Derivatives: Derivatives, in their most basic form, are contracts that derive their value from the performance of some underlying market factor. Derivative transactions can include a range of categories, such as swaps, structured debt obligations, futures, options, forwards, and more. The regulatory structure wrapped around a given derivative is determined by the underlying factor. For example, the SEC has authority over swap agreements that are based on securities; the CFTC regulates all other forms of swaps, such as energy and agriculture swaps. The digitization of "the underlying" will add additional layers of contractual complexity on top of an already variegated derivatives market, and will certainly implicate a range of regulatory questions that sound in standing and emergent derivative law. This will be a fascinating [space](#) to watch market participants evolve and manage risk, and the government respond in regulatory kind.

Currencies: The CFTC defines virtual currencies as "a digital asset that encompasses any digital representation of value or unit of account that is or can be used as a form of currency," and [states](#) that a virtual currency "may be manifested through units, tokens, or coins, among other things; and may be distributed by way of digital 'smart contracts,' among other structures." It is worth considering currencies separately from commodities, however, given the varying regulatory interests that overlap with this asset category beyond the CFTC's.

For example, the Treasury Department's Financial Crimes Enforcement Network has issued [guidance](#) on the regulation of "money transmission." It explains that the definition of money transmission services, found at 31 CFR Sec. 1010.100(ff)(5)(i)(A), means "the acceptance of currency, funds, or other value that substitutes for currency from one person and the transmission of currency, funds, or other value that substitutes for currency to another location or person by any means." The guidance also sets out a range of exclusions. The guidance explains that parties considered money

transmitters under its regulations are subject to Bank Secrecy Act regulations imposing specific anti-money laundering programmatic and know-your-customer requirements. Where the activities constitute a "transmittal of funds," the entity [must also comply](#) with the "Funds Transfer Rule" and "Funds Travel Rule."

Stablecoins: Perhaps the greatest focus of U.S. Executive Branch interest has been the class of assets referred to as "stablecoins." Stablecoins [are](#) digital assets that are designed to maintain a stable value relative to a national currency or other reference assets. Their proponents frequently characterize them as being supported or "backed" by certain reserve assets – though the degree to which that holds true has been a subject of intense debate. This class is of such concern to the government, in fact, that the President of the United States convened a working group to study and [issue](#) a report analyzing risks and policy options relating to the category. The report explores a range of risks relating to stablecoins and recommends legislation and interim measures to address those risks. Even without such government action, the market has been evolving, with [increasing pressure](#) for stablecoin providers to be more transparent about the reserves they claim support their currency values. Many signals indicate that were any category to be regulated first, this would be it.

CBDC: Another looming question is the growing concern of the Fed and others regarding the impact of crypto assets on monetary stability and the ability to influence economic activity through a variety of policy tools currently accompanying sovereign authority over a single currency: the U.S. dollar. On that basis, and for other reasons too lengthy to list, some argue for the creation of a single digital currency – a central bank digital currency – that can provide a digital alternative to the current proliferation of alternative coins that (according to such regulators) threaten instability and monetary tool dilution. Some nations, like China, are already headed for a unitary digital currency. In the United States, expect 2022 to bring forth another axis of the cryptoverse debates: (i) arguments about the prudence of such centralization and the tensions between interests of privacy and [freedom](#) from potential government oversight; and, (ii) what the government would articulate as options for addressing the risks – monetary, consumer-related, and more – of private digital currencies. The Fed has released a [white paper](#) analyzing the potential benefits and risks of a central bank digital currency, sure to provide a baseline for federal policy positions in 2022 about the same

Bank Regulators: Finally, as will be explored further below, the very notion of dealing with a currency connotes a realm of activities traditionally reserved for institutions specifically chartered and authorized to

conduct such activities – banks. This highlights, of course, that in exploring the regulatory future of a given venture, it is sufficient not just to understand the asset alone, but also to understand what is being done with it. To that, we turn next.

Activities

Suffice it to say that an entity's regulatory obligations hinge not only on the definition/categorization of the crypto asset with which it deals, but also the activities it conducts pertaining to those assets. In the much vaunted Hinman [speech](#) referenced above, the former Director makes this point, "[W]e should frame the question differently and focus not on the digital asset itself, but on the circumstances surrounding the digital asset and the manner in which it is sold." That comment could have just as easily been made yesterday without much evolution in the surrounding regulatory climate; but in 2022, market volume and concentration across certain activities is only likely to increase. As commensurate risk concerns escalate, the government may seek to regulate those activities by applying current standards to them or seek additional authorities from Congress to more directly address perceived enforcement gaps. Key activities (across asset categories) of interest to us will include:

- Initial Coin Offerings;
- Custody;
- Trading (Buying/Selling/Exchanging and facilitating such trading);
- Lending; and,
- the creation and sale of NFTs in their proliferating forms.

The regulatory agencies discussed below each have vested, sometimes overlapping, interests in various aspects of such activities. As we look to make sense of 2022, the core activity in any given situation will provide a key second aspect of the contextual triangulation process.

Infrastructure

The capabilities for transacting in crypto assets, of course, must be built and maintained in some fashion. The original vision for the bitcoin blockchain (and Ethereum and others) was one of, by its very structure, a decentralized system beyond the ability of any single party to control information or influence outcomes. Akin with that vision, many have argued that it is simply impossible to regulate blockchain activities. Yet, as described above, governments worldwide will continue to influence distributed ledger technologies largely through regulation of specific asset categories and the activities conducted on relevant infrastructure. We expect that the notion that regulation would simply push activities into other jurisdictions is untenable in a world of growing

international regulatory coordination across most significant marketplaces (where crypto activities haven't already been banned).

Protocol: The point above bears most directly on the decentralized protocol used to run many crypto initiatives. Nonetheless, there must always be some developers, some party or parties that maintain capabilities. A particular protocol itself may never be regulated; but the people involved with it will generally be accessible (the mysterious Satoshi Nakamoto being a notable, but rare, exception), as will the assets and activities the protocol facilitates. It is an unfortunate analogy, but in the world of the criminal cash markets, there is always a point of conversion into some other asset category, and that point of conversion creates a susceptibility for the converting parties. In the digital economy, unless wealth is stored perpetually in digital form and never converted, there will also be points of ingress and egress to other tangible assets. Look to such conversion points for legal friction and heightened government engagement with protocol otherwise thought by those holding the original vision to be untouchable.

Platforms: Platforms directly offering the types of services and activities mentioned above are more obviously in the regulatory ambit as bearing responsibility for the activities they facilitate. The infrastructure they provide is a medium that provides government regulatory access into the digital realm, and many of these platforms – out of an interest in continued growth and legitimacy – are likely to trend towards cooperation with more formalized and established regulatory structures. In this sense, there will be both old and new "intermediary" institutions with vested interests in propagating predictable realities. Look for these to be some of the most powerful forces shaping outcomes as they converge with government actions in 2022 and beyond.

Layer 2: Though the original vision of the cryptoverse was born of the bitcoin revolution, and debates about the bitcoin versus ether realms have taken on near religious fervor, it is indisputable that Ethereum (and other Layer 1 alternatives) provide a scalability for a range of solutions to various "problems" that a blockchain with native, currency-like tokens alone were not designed to resolve. Sitting on top such Layer 1 chains are Layer 2 solutions [intended](#) to scale various applications and handle transactions off the main chain (in the case of Ethereum, referred to as the Ethereum Mainnet). This is a burgeoning area and the growth in virtual Layer 2 infrastructure provides a seemingly endless landscape for innovation and government interest. Though it may be early to expect much federal action in 2022 related to Layer 2 capabilities; surely, it will come.

Taken as a whole, a triangulation of assets, activities, and the infrastructure on which they are housed can provide clearer terms for a discussion about the regulatory climate pertaining to that particular constellation. Yet, as much as legal outcomes are the result of a constantly emergent order, and as ideal as the vision of a digital world free from interference may have been – people will always have an influence over the shape of things to come. We turn next, therefore, to the interested parties whose interactions will be key to this emergent order.

Interested Parties

The sections above hinted at a variety of regulatory interests that will continually be explored in 2022, but those will interact with several other influencers whose positions on market activity and regulation will constantly interact to shape the cryptoverse in 2022.

Regulators

SEC: The current Chairman of the SEC, Gary Gensler, has been very clear about the fact that he considers the crypto markets to be the “Wild West.” He has declined to publicly articulate specific standards for assessing crypto assets as securities, but has described the SEC’s priorities when it comes to digital assets. In those, he lists: (i) the offer and sale of crypto tokens; (ii) crypto trading and lending platforms; (iii) stable value coins (stablecoins); (iv) investment vehicles providing exposure to crypto assets or crypto derivatives; and (v) custody of crypto assets. Expect to see more in 2022 along these lines.

CFTC: As described above, the CFTC considers virtual currencies, and an undescribed set of other crypto assets, to be commodities. However, it acknowledges that its authority to regulate activities is circumscribed, and it may indeed seek expanded powers in 2022. In that light, in an appearance before the Senate Agriculture Committee in February 2022, CFTC Chairman Rostin Behnman beseched Congress to develop a more fulsome regulatory framework with respect to digital assets. In particular, he called for greater CFTC oversight of “digital asset commodity cash markets” and greater coordination among federal regulators.

Fed: The sprawling Federal Reserve System conducts a range of activities as the U.S. central bank, but among them include conducting monetary policy, monitoring risk to and promoting stability of financial and payment systems, and supervising and regulating specified financial institutions and activities. The Board of Governors recently announced policy sprints conducted with the OCC and FDIC that involved “preliminary analysis on various issues regarding crypto-assets.” The Fed’s statement focused on banking organizations’ potential involvement in “crypto-asset-related activities.” This focus on currently chartered

banks bears a slight distinction from OCC Comptroller Hsu’s comments that could be understood to seek an expansion of the banking regulatory perimeter (see more below). Though results of the “sprint” have not yet been announced, the sprint focused on developing common terminology around crypto-asset use, assessing risks of crypto-asset activities by banking organizations, and identifying areas where existing regulations and guidance may benefit from clarification.

Along with the OCC and the FDIC, the Fed has articulated a crypto-asset roadmap it intends to pursue in 2022.

The priorities include:

- Custody activities and ancillary custody services;
- Facilitation of customer purchases and sales of crypto-assets;
- Loans collateralized by crypto-assets;
- Issuance and distribution of stablecoins;
- Activities involving the holding of crypto-assets on a balance sheet; and,
- Application of bank capital and liquidity standards to crypto-assets activities by U.S. banking organizations.

OCC: The Office of the Comptroller of the Currency oversees national banks and federal savings associations. Comptroller Michael Hsu has also touted the joint “crypto sprint” with the Federal Reserve and the FDIC. In addition, however, Hsu has focused on what he calls a strategic vision for expanding the “bank regulatory perimeter,” asserting that fintechs are “rebundling” banking services and supervision of crypto firms is fragmented, yielding significant risks to “consumers, businesses, and financial stability” and demanding a “clarifying” of the “bank regulatory perimeter[.]” He hinted that forthcoming announcements (apparently beyond the Fed’s November announcement above) will be consistent with that vision, and noted that “at the OCC, we have begun to increase our focus on the banks that provide services to large fintechs and facilitate synthetic banking outside of the bank regulatory perimeter.” Look for the perimeter to expand in 2022.

FinCEN: The Financial Crimes Enforcement Network possesses certain regulatory functions under the constellation of legislation referred to as the Bank Secrecy Act. The BSA authorizes the Secretary of the Treasury to require banks and certain financial institutions to take certain measures against financial crime, including the establishment of AML programs and filing reports on certain categories of financial transactions described above. It will continue to be engaged in the government’s mission to limit abuse of the cryptoverse by illicit actors, such as ransomware gangs seeking payment in digital currencies, organized crime seeking to launder money through the crypto system, and more.

Hill Committees and Members

Influential Hill Committees and Members have conducted a steady stream of hearings on crypto assets and made regular public statements relating to the same. The issues identified in those hearings and concerns expressed in those statements all signal further focus on these issues in 2022. Whether sufficient momentum will give rise to legislation, as always, depends on extraneous factors and future events having no direct bearing on the questions at hand. In the absence of Congressional action, of course, the regulatory lines will continue to be defined by enforcement actions by the agencies above. Interested parties can look to several places for further action in 2022:

- **Senate Banking Committee:** The Senate Banking Committee has held a number of hearings in 2021 on issues touching upon the cryptoverse or otherwise discussed it during its regular oversight activities. Though not necessarily speaking for the whole Committee, Senate Pat Toomey, the Committee's Ranking Member, has expressed a desire for greater regulatory clarity and guidance on "cryptocurrencies."
- **House Financial Services Committee:** Similarly, the House Financial Services Committee has held hearings on crypto and Members have conducted a range of related discussions and engagement on topical issues. Most recently, key crypto industry leaders appeared to discuss the relative merits of more robust (or limited) regulation. Such hearings are used to inform Member statutory proposals, and regardless of the partisan perspectives, the consistent theme across these engagements has been the need for greater regulatory clarity.

Institutional Actors: The main protagonists of the crypto explosion will, of course, continue to have a vested interest in engaging in public debates about the regulatory outcomes of the near future. Some are starting to converge around shared interests, such as those articulated by the Blockchain Association. Yet, this is by no means a monolithic category of actors. Dissecting their interests in accordance with their specific activities and offerings would require an entirely distinct essay. The various interests have been present on the Hill, and include payments infrastructure providers, exchanges, infrastructure product and service providers, and more. These interests span the regulated, unregulated, and to-be-regulated.

Traditional Intermediaries: The founding vision of bitcoin was, of course, to replace institutional intermediaries as a necessary component of payments systems. The world of crypto has expanded far beyond payments alone, but traditional financial institutions will

continue to have a strong interest in the products and services they currently offer, new opportunities to evolve such offerings, and completely greenfield endeavors. Of course, one would expect them to have vested interests in an extension of the regulatory frameworks to which they are already subject, but the inflection point could also provide opportunities to shape improvements to the regulatory climate in key respects. Such institutions had a more limited presence in public policy debates in 2021, but they are likely to engage in the 2022 discussions. Like the more nascent institutional actors, their interests will be products of their own service offerings, business strategies and current compliance and regulatory obligations and hopes.

Consumers: One interest group that has limited to no voice are the disparate, but growing, number of individual consumers who engage with crypto assets. This, of course, is a varied group with a variety of intentions, but the debate about consumer protection is bound to be a central focus of 2022. Keep an eye, however, on how that topic is entangled with questions of market access. The solution sets that appear are likely to circulate around how regulation can protect such consumers while not creating high barriers to entry for market participants who can benefit from healthy, fair and honest product and service offerings, but may be disadvantaged by current market norms.

Conclusion

It is impossible to speak singularly of regulatory action covering "crypto." There are a range of categories, activities, and interested actors, all of which will continue to converge into a constantly emergent order. Interested parties must track a variety of questions and issues to discern meaning from the current complexity. For our part, we will look to triangulate assets, activities, and infrastructure – and seek to understand how a variety of actors interests bear and converge on such groupings. To be certain, these capabilities have applications far beyond what they imply for financial technology alone – to all of Web3. These observations apply equally beyond fintech, but fintech provides a helpful microcosm for that broader universe. The coming year promises to be fascinating and surprising. Rarely do we confront epochs of such disruptive potential. In the free world, what comes in the next twelve to eighteen months will shape human potential for a long time to come.



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