

NYAG Delivers on Promise to Rein In Unregistered Crypto Lending with New Suit

Article By:

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On September 26, 2022, New York Attorney General Letitia James (the “NYAG”) took definitive action in the wake of her warning last year that crypto lending platforms must register with her office or face legal action, filing a [complaint](#) against Nexo Inc. and Nexo Capital, Inc. (collectively “Nexo”) alleging that Nexo violated New York’s Martin Act and Executive Law by acting as an unregistered securities and/or commodities broker-dealer within the state. Specifically, the complaint alleges that Nexo improperly offered and sold securities and commodities by allowing users to purchase, sell, deposit, trade, borrow against, and earn interest on virtual currency, while unregistered. The complaint further alleges that Nexo made various misrepresentations regarding its operations. The NYAG seeks an injunction, disgorgement, restitution, and a permanent bar prohibiting Nexo from purchasing or selling securities or commodities in New York.

On November 18, 2021, the NYAG issued a [press release](#) stating that she had directed two crypto lending platforms to cease their alleged unregistered and unlawful activities in New York, providing a copy of an October 18, 2021 [cease-and-desist letter](#) with the entity’s name redacted alongside the release. In her press release regarding the Nexo action, the NYAG revealed that Nexo was one such recipient of a cease-and-desist letter in October 2021. As such, the NYAG has made good on her promise in last year’s press release to take action to prevent violations of New York law. The action serves as an important reminder that companies operating as crypto exchanges or offering interest-bearing crypto products in the state should ensure that they are appropriately registered under New York law and their public statements are accurate.

New York General Business Law (“GBL”) § 352, *et seq.*, also known as the Martin Act, requires that securities and commodities broker-dealers register with the Office of the Attorney General prior to any offer to purchase or sell securities or commodities. Businesses engaging in persistent illegality or fraud may also be deemed in violation of New York’s Executive Law § 63(12). Misstatements made in connection with securities and commodities transactions can constitute separate fraudulent acts under GBL § 352-c and Executive Law § 63(12).

The NYAG alleges that Nexo sold securities or commodities while unregistered in connection with its “Exchange” marketplace and Earn Interest Product (“EIP”). The Exchange allows users to buy, sell, and exchange a wide range of cryptocurrencies via a website and mobile app, with Nexo charging approximately 1% on each transaction. The EIP allows users to receive interest on crypto they

deposit with Nexo. Nexo then pools users' EIP assets with "similar Nexo-owned assets" and deploys those assets to generate revenue from which it pays users interest and retains the difference as profit, according to the complaint. The revenue-generating activities purportedly include: (1) staking, lending, arbitrage, and provision of liquidity on decentralized finance platforms, (2) lending to retail and institutional borrowers, (3) investing in selected virtual currencies, and (4) entering into swap and options transactions.

Notably, the allegations pertaining to failure to register do not distinguish between Nexo's securities, commodities, broker, and dealer activities, and instead state only that Nexo acted as an "unregistered securities broker or dealer and/or commodity broker-dealer." This imprecision renders it difficult to determine what specific conduct required registration and when. It also limits the utility of the complaint as an educational tool for industry onlookers assessing whether their activities may require registration.

The NYAG further alleges that misleading statements by Nexo gave users the false impression that Nexo did not operate in New York, their investments were low-risk, and they were transacting with a company that was fully licensed and operating in compliance with applicable law, despite operating unlawfully in New York. The NYAG claims this conduct violates antifraud provisions of both the Martin Act and Executive Law.

Last year, the NYAG announced that her office would be taking aim at unregistered cryptocurrency platforms offering interest-bearing crypto products within the state's borders. The action against Nexo appears to be in furtherance of that directive. In light of these developments, crypto companies should carefully consider whether their activities require securities and/or commodities broker-dealer registrations and vet public statements to ensure their accuracy and avoid a run-in with New York's top cop.

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