

## SEC Announces First Enforcement Actions Against Unregistered Investment Adviser and Broker-Dealer in Cryptocurrency Sale

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On September 11, 2018, the Securities and Exchange Commission (“SEC”) announced its first enforcement actions alleging that entities offering certain investments in cryptocurrencies should be registered as an investment adviser or broker-dealer. The SEC issued a settled order against Crypto Asset Management LP (“CAM”) and its principal, Timothy Enneking, for failing to register with the SEC as an investment adviser and misleading investors regarding the registration status of the digital asset fund they managed. The SEC also alleged that CAM and Enneking caused the fund to violate registration requirements despite marketing the fund as the “first regulated crypto asset fund in the United States.” The SEC also issued a settled order against TokenLot LLC and its two owners, Lenny Kugel and Eli Lewitt, for the online sale of digital coins associated with initial coin offerings (“ICOs”) without registering with the SEC as broker-dealers.

CAM and Enneking raised more than \$3.6 million from 44 investors over a four-month period in 2017 while falsely claiming that the digital asset fund they managed was regulated by the SEC and had been registered with the agency. By the end of 2017, CAM’s digital assets were worth nearly \$37 million. But by engaging in an unregistered non-exempt public offering and investing more than 40 percent of the fund’s assets in cryptocurrency securities, CAM violated the registration requirements under Section 5(c) of the Securities Act and caused the fund to operate as an unregistered investment company, thereby violating federal securities law.

Kugel and Lewitt advertised TokenLot’s website as a platform for investors to buy and trade digital coins associated with ICOs. TokenLot received orders from more than 6,100 retail investors and handled more than 200 different types of digital coins, with TokenLot taking a percentage of the money raised for every ICO. But because the SEC deemed some of the traded cryptocurrencies included securities, TokenLot, Kugel, and Lewitt were required to—but did not—register with the SEC as broker-dealers. The SEC also alleged that the respondents violated the registration requirements of Section 5 of the Securities Act.

After being contacted by the SEC, CAM ceased its public offering and offered buybacks to impacted investors, while TokenLot voluntarily began winding down and refunding investors’ payments for unfilled orders. Ultimately, CAM and Enneking agreed to pay a penalty of \$200,000, TokenLot agreed to pay \$471,000 in disgorgement plus \$7,929 in interest, and TokenLot’s owners each agreed to pay additional penalties of \$45,000.

The enforcement actions against CAM and TokenLot are the first of their kind since the SEC issued its July 2017 DAO Report, an investigative report that cautioned market participants that the offering and sale of cryptocurrencies may be subject to the requirements of federal securities law, including registration requirements. The actions also follow the SEC’s recent appointment of a Senior Advisor for Digital Assets and Innovation, a new advisory position created to guide the SEC’s application of federal securities laws to emerging digital asset technologies and innovations,

including cryptocurrencies and ICOs. In addition, the SEC announced the actions on the same day the Financial Industry Regulatory Authority (“FINRA”) announced its first disciplinary action involving cryptocurrencies.<sup>1</sup>

These actions are a reminder that the SEC is looking very closely at investment activities related to digital assets. Entities selling, trading, investing in, or otherwise dealing with digital assets like cryptocurrencies must ensure that they understand the nature of those investments and are complying with any relevant regulatory requirements. Concerned entities can contact Haynes Boone for assistance in analyzing registration and other securities law requirements.

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<sup>1</sup> See Press Release, FINRA, [FINRA Charges Broker with Fraud and Unlawful Distribution of Unregistered Cryptocurrency Securities](#) (Sept. 11, 2018)