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WILSON SONSINI

Focus on Fintech

Welcome to Wilson Sonsini's *Focus on Fintech* newsletter. This quarterly newsletter provides ongoing analysis and commentary on regulatory developments impacting the fintech industry.

In this issue, our attorneys discuss updates and developments from federal regulators, including those related to artificial intelligence (AI) in financial markets, regulated securities intermediaries, cryptocurrency and virtual currency, and consumer protection initiatives. We also discuss rule updates from the SEC, FinCEN, and the CFTC.

Enforcement Developments

CFPB Sues Early Warning Services and Banks over Zelle Fraud

The Consumer Financial Protection Bureau (CFPB) has filed a complaint against Early Warning Services, LLC (EWS), Bank of America, N.A., JPMorgan Chase Bank, N.A., and Wells Fargo Bank N.A. in the District Court for the District of Arizona, alleging failures to address fraud risks and consumer protection issues over the Zelle peer-to-peer payment network. The CFPB claims the defendants prioritized rapid market entry and failed to institute effective measures to prevent fraud perpetrated on consumers using Zelle. The complaint also claims that the defendant banks violated federal consumer financial law governing electronic fund transfers, including in sending customers' transfers to the wrong recipients because of errors and inaccuracies in the Zelle Network Directory and failing to conduct reasonable investigations when consumers approached them about certain fraudulent or otherwise erroneous Zelle transfers. The CFPB's action, brought under the Consumer Financial Protection Act and the Electronic Fund Transfer Act, seeks injunctive relief, an appropriate penalty, and redress for affected consumers.

In This Issue

CFPB Orders Apple and Goldman Sachs to Pay over $89 Million for Apple Card Failures

The CFPB entered into consent orders with Apple Inc. (Apple) and Goldman Sachs Bank USA (Goldman Sachs) on October 23, 2024, settling allegations relating to customer service breakdowns and misrepresentations that impacted hundreds of thousands

of Apple Card users. The CFPB alleged that Apple neglected to forward thousands of consumer disputes to Goldman Sachs, and Goldman failed to investigate the disputes it was forwarded as required by the Truth in Lending Act. The CFPB further found that these lapses caused delays in resolving disputed charges, left some consumers responsible for unauthorized transactions, and resulted in erroneous negative credit report entries. In addition, the CFPB alleges that Apple and Goldman Sachs misled consumers about interest-free payment plans for Apple products purchased with the Apple

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Enforcement Developments *(Continued from page 1)*

Card and that Goldman Sachs made representations about the application of refunds to consumer balances that misled consumers about their payment obligations.

Goldman Sachs has been ordered to pay at least $19.8 million in consumer redress and a $45 million civil penalty, and Apple will pay $25 million in civil penalties. The consent order also prohibits Goldman Sachs from introducing new credit card products without providing a comprehensive compliance plan.

CFPB Orders Navy Federal Credit Union to Pay More Than $95 Million for Practices Related to Overdraft Fees

The CFPB recently issued a consent order against Navy Federal Credit Union (Navy Federal) for unfair practices related to overdraft fees in violation of the Consumer Financial Protection Act. According to the CFPB's findings, Navy Federal charged overdraft fees on transactions where accounts had sufficient funds at authorization but insufficient funds at settlement, as well as in instances of delayed posting of incoming credits where cutoff times were not disclosed. The CFPB alleges that Navy Federal's disclosures did not adequately inform consumers about its cutoff times or the settlement process, leading to widespread confusion and frustration. The CFPB acknowledged that Navy Federal began refunding some of these fees in 2023.

Under the consent order, Navy Federal must pay $80.7 million in consumer redress and a $15 million civil money penalty. Navy Federal is also required to cease the unfair practices, revise its disclosure policies, and implement a comprehensive compliance plan to prevent future violations.

Federal Reserve Board Issues Enforcement Action Against Lineage Financial Network

The Reserve Board recently announced an enforcement action against Lineage Financial Network, Inc. (Lineage FN), the bank holding company of Lineage Bank. The enforcement action involved a written agreement between Lineage FN and the Federal Reserve Bank of Atlanta (Reserve Bank). In its announcement, the Reserve Board noted that the Federal Deposit Insurance Corporation (FDIC), Lineage Bank's primary supervisor, had separately issued an enforcement action with Lineage Bank in January 2024. The Reserve Board further noted that its enforcement action against Lineage FN is independent of the bankruptcy proceedings regarding Synapse Financial Technologies, Inc. Lineage Bank is among the banks that had partnered with Synapse.

The written agreement requires Lineage FN to take corrective actions to address its various financial and operational deficiencies and to take steps to ensure the bank's financial soundness and compliance with federal laws. Under the written agreement, Lineage FN's board must submit written plans to the Reserve Bank describing the measures it will adopt to improve governance and ensure board members possess necessary qualifications and must provide written statements of its annual cash flow projections for regulatory review. The agreement also restricts Lineage FN from declaring dividends, repurchasing shares, or incurring debt without prior approval from Reserve Bank and the Reserve Board. Additional requirements include compliance with laws governing affiliate transactions, executive appointments, and severance payments.

In addition, the written agreement requires Lineage FN to submit quarterly progress reports to the Reserve Bank, detailing measures taken to meet the agreement's provisions and improve oversight. The agreement will remain in effect until formally terminated by the Federal Reserve.

CFPB Orders VyStar Credit Union to Pay $1.5 Million for Banking Platform Outage

The CFPB issued a consent order against VyStar Credit Union (VyStar), alleging unfair practices related to its online and mobile banking services in violation of the Consumer Financial Protection Act. According to the CFPB's allegations, VyStar's attempt to launch a new virtual banking platform in May 2022 resulted in severe technical failures, rendering the system unstable and leaving members unable to perform basic banking functions, such as accessing account balances, transferring funds, and making loan payments. The consent order noted that these issues persisted for months, during which VyStar members incurred late fees, overdraft charges, and other costs, with some members experiencing harm to their credit scores due to delayed or missed payments.

The order alleges that the technical issues were the result of VyStar's failure to implement adequate management and governance processes and its assumption

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Enforcement Developments *(Continued from page 2)*

of excessive risk throughout the launch of and conversion to the new virtual banking platform. For example, the CFPB alleges that VyStar selected an inexperienced vendor without proper due diligence, set an aggressive timeline, and ignored significant red flags about the platform's readiness. Despite the platform's known defects and inadequate testing, VyStar allegedly proceeded with the conversion, permanently disabling its previous platform, and leaving no fallback option for members. The CFPB claims that these failures were preventable and caused substantial harm to consumers.

Under the consent order, VyStar must pay a $1.5 million civil penalty, create a redress plan to reimburse affected members, establish a governance committee to ensure proper management of projects involving consumer facing banking systems, and create and implement a comprehensive compliance plan. These include establishing new risk management procedures, improving contingency planning, and enhancing governance standards to prevent similar disruptions in the future.

CFTC Takes First Enforcement Actions Against Fraud in Voluntary Carbon Credit Markets

The Commodity Futures Trading Commission (CFTC) has filed charges in the District Court for the Southern District of New York against Kenneth Newcombe, the former CEO of a Washington, D.C.-based carbon credit project developer, alleging that he orchestrated a scheme to secure millions of unearned carbon offset credits. From 2019 to 2023, Newcombe allegedly submitted false data to carbon credit registries and third-party reviewers to inflate the emissions reductions claimed by his projects. The fraudulent credits were then purportedly sold to market participants, which the CFTC asserts undermined market integrity. The Securities and Exchange Commission (SEC) and the U.S. Department of Justice (DOJ) have announced parallel filings against Mr. Newcombe for related conduct.

The CFTC has settled similar charges it had previously brought against CQC Impact Investors LLC (CQC) and its former COO, Jason Steele. As a condition of the settlement, CQC and Steele each admitted to making false reports to carbon credit registries regarding emissions-reduction projects in sub-Saharan Africa, Asia, and Central America. Based on these admissions, CQC intentionally participated in the false reporting activity by misrepresenting data to inflate the credits produced by certain projects. CQC agreed to a $1 million civil penalty and credit cancellation, while Steele entered into a formal cooperation agreement with investigators.

The CFTC's actions against Mr. Newcombe, Mr. Steele, and CQC are its inaugural enforcement efforts targeting fraud in the voluntary carbon credit market.

For further details, please see our alert here.

DOJ and FTC Take Action Against Online Cash Advance App Dave for Deceiving Consumers, Charging Undisclosed Fees

The DOJ, acting upon a referral from the Federal Trade Commission (FTC), has filed an amended complaint in the Central District of California against Dave, Inc. (Dave) and its CEO, Jason Wilk. The complaint alleges that Dave, through its personal finance app, engaged in deceptive advertising practices targeting financially vulnerable consumers. From 2019 to 2023, Dave promoted "instant" cash advances of "up to $500," but according to the complaint's allegations, only a minimal percentage of users received such amounts. The complaint alleges that most users were offered significantly smaller advances—or none at all. Additionally, Dave allegedly failed to disclose several fees, including an "Express Fee" for expedited advances and a recurring $1 monthly membership fee. Dave also allegedly misrepresented a "tip" charge as a charitable donation, while retaining the majority of the funds. Despite Dave's claims of having "no hidden fees," these charges were not clearly disclosed.

The complaint accuses Dave of violating the Federal Trade Commission Act and the Restore Online Shoppers' Confidence Act. To address these practices, the DOJ seeks a permanent injunction and civil penalties, among other forms of relief.

FTC Approves Final Order Against Rytr, Seller of an AI "Testimonial & Review" Service, for Providing Subscribers with Means to Generate False and Deceptive Reviews

The FTC has approved a final order against Rytr LLC (Rytr), settling allegations regarding its AI-enabled "writing assistant" for testimonials and reviews. The FTC's complaint alleges that Rytr's service provided subscribers with the means to generate false and deceptive written content online reviews, in violation of the FTC Act. According to the complaint, the service allegedly generated reviews that contained specific details that had no relation to the user's input, and the service set no limit on the number of reviews a user with a certain subscription level could generate and copy. The order prohibits Rytr from engaging in similar conduct in the future and bars the company from advertising, promoting, marketing, or selling any service dedicated to or promoted as generating consumer reviews or testimonials. The order remains effective for 20 years from its issuance, with extensions under specific conditions.

Financial Regulatory Policy Changes

OCC Reports on Key Risks in Federal Banking System

The OCC released its Fall 2024 Semiannual Risk Perspective, affirming the soundness of the federal banking system while highlighting key risks.

Operational risk remains elevated due to cyber threats and a complex operating environment, emphasizing the need for robust third-party risk management. Compliance risks require attention as banks adapt to evolving customer needs, particularly in fraud investigations, data governance, and BSA/AML monitoring.

Market risk reflects varied net interest margin performance, with deposit volumes and funding costs showing signs of stabilization. The report also highlights increasing external fraud targeting consumers and banks, urging enhanced fraud risk management and customer education.

Covering data through June 2024, the report provides insights into risks facing OCC-regulated institutions, offering guidance for maintaining resilience in a dynamic environment.

Treasury Releases Report on the Uses, Opportunities, and Risks of AI in Financial Services

The U.S. Treasury Department released a report addressing the uses, opportunities, and risks of AI in the financial services sector, based on stakeholder feedback received through a public request for information. The report highlights the expanding adoption of AI technologies, including traditional machine learning and emerging generative AI, across a wide range of financial functions, from underwriting and trading to compliance and customer service.

While AI offers transformative potential, the report identifies key risks, including data privacy concerns, bias in decision-making, concentration risks from reliance on a few large AI providers, and challenges in ensuring explainability of AI systems. Stakeholders also raised concerns about uneven regulatory oversight between banks and nonbanks, the potential for consumer harm, and the need for enhanced governance frameworks.

The report outlines recommendations for addressing these issues, such as establishing consistent AI definitions, clarifying data privacy and quality standards, enhancing consumer protections, and fostering collaboration among regulators and industry stakeholders. The Treasury emphasizes the need for further regulatory adaptation to manage emerging AI risks effectively while fostering innovation and financial inclusion.

Financial Stability Oversight Council Releases 2024 Annual Report

The Financial Stability Oversight Council (FSOC) released its 2024 annual report, emphasizing the resilience of the U.S. financial system while identifying key vulnerabilities and recommending strategies to address them. The report highlights the growing risks posed by cybersecurity incidents, noting the increasing frequency and potential for disruptions to critical financial operations. The FSOC supports ongoing collaboration among federal and state agencies, private firms, and international partners to enhance resilience and information sharing.

The report also addresses the increasing reliance of financial institutions on third-party service providers, emphasizing the importance of robust oversight. The FSOC recommends that Congress grant relevant agencies the authority to examine these providers and urges greater coordination among regulators to improve information security and regulatory consistency. The Council recommends that member agencies continuously monitor the

evolving use of AI in financial services and collaboratively enhance oversight and expertise to address potential financial stability risks, such as complexity and concentration, while leveraging AI's benefits.

In the digital assets space, the FSOC identifies stablecoins as a potential financial stability risk due to their vulnerability to runs and recommends that Congress establish a comprehensive prudential framework for stablecoin issuers and grant regulators authority over the spot market for crypto assets.

Investment funds, particularly open-end funds with liquidity mismatches, remain an area of focus. The FSOC supports continued SEC reforms to enhance fund transparency and resilience and emphasizes the importance of better data collection to monitor risks from hedge funds and private credit markets. Throughout, the report reflects the FSOC's ongoing commitment to safeguarding financial stability while addressing emerging threats.

Consumer Protection Policy

CFPB Releases December 2024 Supervisory Highlights

The CFPB recently issued its Winter 2024 Supervisory Highlights, detailing its findings from its monitoring activities during the period lasting from January to October 2024. The CFPB identified unfair overdraft and non-sufficient funds, or NSF fees charged by certain banks, as well as unfair acts or practices related to consumer requests to stop payment of preauthorized debit card transactions. The CFPB further noted that in its examinations of core processors that serve as service providers to large banks, it found that certain of these core processors had unfairly configured systems that automatically assessed these fees, harming consumers.

With respect to entities that furnish information to consumer reporting companies, the CFPB noted violations of the Fair Credit Reporting Act (FCRA) and Regulation V, with furnishers failing to respond to identity theft block requests and conduct proper investigations of disputes. The CFPB also addressed issues in the short-term small dollar lending market, including delays in dispute resolution, misleading loan terms, and practices related to loan account closures and continued debiting.

CFPB Releases Final Open Banking Rules: Key Takeaways for Fintech Companies

On October 22, 2024, the CFPB announced its long-awaited final rule on "Personal Financial Data Rights" (the Final Rule). The Final Rule implements Section 1033 of the Dodd-Frank Act, which provides consumers the right to access and port their financial information between banks and other financial entities. For an analysis of the proposed rule, please see our analysis here.

The Final Rule aims to spur greater choice and increase competition by requiring "data providers" to make consumer's financial data accessible to consumers and their authorized third parties through specified consumer and developer interfaces and portable "standardized" formats.

For further details, including information on how fintech companies can begin taking steps to strategically align with the new regime and ensure preparedness for compliance. See our alert here.

CFPB Finalizes Rule Establishing Examination Authority over Digital Consumer Payment Apps

The CFPB finalized a rule extending its supervisory authority to encompass nonbank digital payment app providers who handle covered consumer payment transaction volume of at least 50 million transactions annually and are not a small business concern. Unlike the proposed rule, which we summarized here, the final rule excludes transfers of digital assets, including crypto-assets such as Bitcoin and stablecoins. The rule grants the CFPB supervisory authority under the Consumer Financial Protection Act. The rule took effect January 9, 2025.

CFPB Proposes Rule to Cover Data Under the Fair Credit Reporting Act

The CFPB has issued a proposed rule that primarily aims to bring data brokers within the scope of the Fair Credit Reporting Act (FCRA), which we discuss in greater detail here. Historically, data brokers have argued that they do not provide "consumer reports" and are therefore not "consumer reporting agencies" subject to FCRA obligations. The proposed rule seeks to cover data brokers by clarifying key provisions within the definition of "consumer report." The proposed rule also aims to shore up consumer protections under the FCRA by interpreting the definition of "consumer reporting agency" more broadly and permissible purposes for furnishing consumer reports more narrowly, such as consumer consent and legitimate business needs. The CFPB seeks public comment on the proposed rule, which must be received on or before March 3, 2025.

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Consumer Protection Policy *(Continued from page 5)*

CFPB Issues Warning on So-Called Bait-and-Switch Credit Card Rewards Tactics

The CFPB issued a circular warning that some credit card companies operating rewards programs may be engaging in illegal practices, including devaluing points, hiding conditions for earning or keeping rewards, and failing to deliver promised benefits. The circular follows consumer complaints and findings from a May 2024 public hearing on credit card and airline rewards programs. The CFPB warned that these practices could constitute unfair or deceptive acts under the Consumer Financial Protection Act, likening them to bait-and-switch schemes. Companies such as American Express and Bank of America have faced prior CFPB actions for allegedly illegal practices related to credit card reward programs.

The CFPB also released research showing that retail credit cards often charge significantly higher interest rates than general-purpose cards, with many retail cards reporting a maximum APR above 30 percent, compared to only 38 percent of non-retail cards in a recent sample. The study noted consumer complaints about high fees, aggressive sales tactics, and difficulties redeeming promotions.

The CFPB also launched Explore Credit Cards, a tool aiming to help consumers make comparisons about options in the credit card market. The CFPB aims to increase market competition and transparency, allowing smaller issuers with better offers a chance to compete.

AI

CFTC Staff Issues Advisory Related to the Use of AI by CFTC-Registered Entities and Registrants

The CFTC has issued a staff advisory addressing the use of AI by CFTC-regulated entities, emphasizing compliance with the CEA and CFTC regulations. The advisory highlights AI's potential applications in areas such as trade processing, market surveillance, risk management, and customer protection, alongside associated compliance risks.

The advisory states that CFTC-regulated entities must ensure AI systems adhere to reliability, security, and capacity standards. Entities remain responsible for compliance with statutory and regulatory requirements when adopting AI, regardless of whether the technology is developed internally or provided by third parties. Specific focus areas include trade execution, risk assessment, customer fund segregation, and recordkeeping.

The advisory reminds entities of their obligation to notify the agency of material changes to AI systems impacting their operations. The advisory also emphasizes the need for robust risk analysis, governance, and adherence to existing safeguards. The CFTC continues to evaluate AI developments and may issue further guidance as necessary.

SEC Charges Rimar Capital Entities and Owner Itai Liptz with Defrauding Investors by Making False and Misleading Statements About Use of AI

The SEC has announced a consent order against Rimar Capital USA, Inc. (Rimar USA), Rimar Capital, LLC, and their respective principals, Itai Royi Liptz and Clifford Todd Boro.

The order alleges that Liptz, Boro, and Rimar USA fraudulently raised almost $4 million through Simple Agreements for Future Equity (SAFEs) by, among other things, making misleadingly exaggerated statements to prospective investors regarding use of AI. The SEC ordered the respondents to cease and desist from violating federal securities laws, imposed civil penalties, and barred Liptz from associating with securities-related entities for five years. These measures underscore the SEC's commitment to addressing deceptive practices in the investment advisory sector. The parties have agreed to settle and pay $310,000 in civil penalties.

Regulation and Enforcement Involving Regulated Securities Intermediaries

U.S. District Court for the Northern District of Texas Vacates the SEC's Dealer Rule

On November 21, 2024, in the orders granting plaintiffs' motions for summary judgments in *Nat'l Ass'n of Priv. Fund Managers v. SEC* and *Crypto Freedom All. Of Tex. v. SEC*, the U.S. District Court for the Northern District of Texas vacated SEC rules 3a5-4 and 3a44-2 (together, the "Dealer Rule") of the Securities Exchange Act of 1934 (Exchange Act), finding that the SEC exceeded its statutory authority under the Exchange Act in adopting the Dealer Rule. The court determined that the Dealer Rule's interpretation of the term "dealer" was inconsistent with the text, history, and structure of the Exchange Act, emphasizing that dealers have traditionally been defined as entities with customers.

The Dealer Rule, adopted in February 2024, sought to expand the definition of "dealer" to include entities engaged in buying and selling securities for their own accounts under specific qualitative tests, focusing on activities such as regular buying and selling of securities, even without customer relationships. These provisions could have extended dealer registration requirements to entities engaging in proprietary trading, including private funds and their managers and crypto market participants operating without traditional customer bases. Various private fund manager associations challenged the rule, arguing it was unauthorized and arbitrary. The court agreed, focusing on the statutory intent to distinguish dealers from traders and rejecting the SEC's argument that customer relationships were unnecessary for dealer status.

The court emphasized that the Exchange Act's definition of a dealer presupposes customer relationships and liquidity provision, rejecting the SEC's argument that entities without customers could fall within the definition. This interpretation provides a safeguard for crypto firms engaged in market-making or trading for their own accounts from automatic dealer classification under the invalidated rule.

While the ruling invalidates the Dealer Rule, the decision does not preclude SEC enforcement under existing guidance, which considers activities such as market quoting and regular securities trading as indicative of dealer status. The SEC's recent enforcement actions in the convertible debt market, although based on statutory definitions rather than the Dealer Rule, remain unaffected. The SEC's potential appeal and future enforcement focus under the incoming administration remain uncertain.

SEC Division of Examinations Announces 2025 Priorities

The SEC Division of Examinations (Division) has announced its priorities for Fiscal Year 2025. The Division examines SEC-registered investment advisers, investment companies, broker-dealers, clearing agencies, and self-regulatory organizations (SROs). In addition to continued examinations in core areas such as disclosures and governance practices, the Division will examine for compliance with new rules, use of emerging technologies such as AI and crypto, and soundness of controls intended to protect investor information, records, and assets.

For investment advisers, examinations will prioritize adherence to fiduciary duties, compliance program effectiveness, and the handling of conflicts of interest, particularly in relation to high-cost and illiquid products. Examinations of private fund advisers will review disclosures, fee calculations, and policies addressing conflicts of interest. Investment companies will be examined for their compliance programs, governance practices, and adherence to disclosure requirements.

Broker-dealer exams will focus on compliance with Regulation Best Interest, Form CRS, financial responsibility rules, and trading-related practices, with particular scrutiny on complex or higher-risk products. The SEC will also assess the operations of self-regulatory organizations, including national securities exchanges, FINRA, and the Municipal Securities Rulemaking Board, and clearing agencies for their oversight and regulatory compliance.

Emerging risk areas that will be prioritized include cybersecurity, operational resilience, the integration of financial technology, and activities related to crypto assets. Generally, the Division will examine how registrants address technological risks, safeguard customer information, and comply with AML requirements. The Division will also put a specific focus on assessing whether firms have implemented adequate policies and procedures to monitor and/or supervise their use of AI. With respect to crypto assets, the examinations will review whether registrants have met and follow standards of conduct when advising on crypto assets, and whether registrants routinely review, update, and enhance their compliance practices, risk disclosures, and operational resiliency practices (when required).

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Regulation and Enforcement Involving Regulated Securities Intermediaries *(Continued from page 7)*

SEC Settles with Former Representative of Advisory Firm SeaCrest with Cherry-Picking

The SEC has issued a settlement order against SeaCrest Wealth Management, LLC (SeaCrest) for alleged failures related to the recommendation of complex financial products to retail investors in light of supposed inadequate supervision and compliance practices regarding the sale of leveraged exchange-traded funds (ETFs).

SeaCrest's investment adviser representative, Eric Cobb, is alleged to have routinely placed clients with conservative investment objectives into high-risk, leveraged ETFs. These products, which reset daily, are designed for short-term use, and allegedly carry heightened risks due to compounding effects over extended holding periods. Despite these risks, Cobb allegedly failed to conduct appropriate suitability analyses or discuss the risks with his clients. Many of the trades were allegedly inconsistent with the clients' stated risk tolerances and investment objectives.

SeaCrest allegedly did not implement or enforce policies to prevent unsuitable recommendations. The SEC asserts that SeaCrest's compliance team failed to identify or address the inappropriate trading activity, and the firm neglected to monitor adherence to its fiduciary obligations to retail clients. The SEC also alleges that SeaCrest's Form ADV brochures contained misleading statements regarding the suitability of its investment advice and the risks associated with leveraged ETFs.

SeaCrest has agreed to be censured and pay a $375,000 penalty without admitting or denying the SEC's findings.

SEC Charges Three Individuals with Impersonating Financial Professionals in Fraud Scheme Targeting Retail Investors

The SEC has filed a complaint in the District Court for the District of New Jersey against Chibuzo Augustine Onyeachonam, Stanley Chidubem Asiegbu, and Chukwuebuka Martin Nweke-Eze, alleging a fraudulent scheme that involved these individuals impersonating registered U.S. securities professionals to defraud investors out of at least $2.9 million. The complaint alleges violations of the anti-fraud provisions of the Securities Act of 1933, Exchange Act, and Advisers Act.

The scheme allegedly involved creating websites and investment entities using the identities of 22 real securities professionals, advertising fictitious investment services, and directing victims to transfer funds and cryptocurrencies. The SEC asserts that victims were promised high monthly returns of 15 percent–25 percent, with fake online platforms showing fabricated profits to encourage further investments, and that funds were misappropriated rather than invested, with withdrawal requests met with demands for additional fees.

The SEC seeks disgorgement of ill-gotten gains, civil penalties, and a permanent injunction to prevent future violations.

SEC Settles with Three Broker-Dealers for Allegedly Filing Deficient Suspicious Activity Reports

The SEC has issued settlement orders against Webull Financial LLC, Paulson Investment Company, LLC, and Lightspeed Financial Services Group LLC, alleging violations of the reporting and recordkeeping requirements of the Exchange Act due to deficient filings of Suspicious Activity Reports (SARs). These deficiencies stemmed from purportedly incomplete narratives that failed to provide essential details of reported transactions, allegedly undermining the reports' effectiveness.

SARs must contain reports of transactions that a broker-dealer has reason to suspect

might be derived from illegal activity or activity that has no lawful purpose. The allegations from the SEC cover the period from 2018 to 2022 and involve supposed failures to include key elements required by FinCEN guidance, such as the 'who, what, when, where, and why" of suspicious activities. The orders each provide purported examples of firm missing critical transaction details, customer information, and descriptions of any remedial actions taken by the firms. The orders also claim that despite policies and procedures aimed at ensuring compliance, the firms filed SARs that did not meet regulatory standards.

All three firms have agreed to settle the charges without admitting or denying the findings. As part of the settlements, the firms agreed to be censured, to cease and desist from violating the charged provisions, to pay civil penalties of $125,000 for Webull and $75,000 each for Paulson and Lightspeed, and to undertake remedial actions, including reviews of their AML compliance programs by independent consultants.

SEC Settles with Advisory Firm WisdomTree for Allegedly Failing to Adhere to Its Own Investment Criteria for ESG-Marketed Funds

The SEC has issued a settlement order with WisdomTree Asset Management, Inc. alleging violations of the Investment Advisers Act and the Investment Company

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Regulation and Enforcement Involving Regulated Securities Intermediaries *(Continued from page 8)*

Act in connection with its management of environmental, social, and governance (ESG)-focused ETFs. The alleged violations occurred between March 2020 and November 2022.

According to the SEC's order, WisdomTree marketed three ESG ETFs as excluding investments in companies involved in fossil fuels and tobacco, regardless of revenue measures. The SEC alleges that WisdomTree failed to implement adequate screening processes, leading to investments in companies involved in coal transport, natural gas distribution, and tobacco retail sales. These issues purportedly arose from limitations in third-party data used by WisdomTree. The SEC also asserts that data failed to screen out all companies involved in fossil fuel and tobacco-related activities, which the firm then failed to disclose to its board and investors.

The SEC further alleges that WisdomTree did not establish written policies and procedures to ensure compliance with its advertised ESG investment criteria. According to the order, in November 2022, WisdomTree updated its disclosures to reflect the limitations of its screening process, and the adviser liquidated the ESG ETFs in February 2024.

Without admitting to or denying the findings, WisdomTree agreed to cease and desist from future violations, the imposition of a $4 million civil penalty, and censure.

SEC Chair Gary Gensler Announces Departure After Influential Tenure

Gary Gensler, the SEC's 33rd Chair, stepped down on January 20, 2025, ending a nearly four-year tenure during which he led the SEC through modernizing reforms and enforcement initiatives. Chair Gensler's resignation closely followed that of fellow Democrat and SEC Commissioner Jamie Lizárraga, who left office on January 17, 2025. As a result of these departures, the SEC is poised to transition from its current Democratic 3-2 majority to a Republican majority following President Donald Trump's inauguration.

Appointed amidst market instability in April 2021, Chair Gensler presided over frequent rulemakings, including those targeted at modernizing equity trading rules, enhancing cybersecurity and climate risk disclosures, and updating corporate governance standards.

Under Chair Gensler's leadership, the SEC pursued high-impact enforcement actions, filing over 2,700 cases, and securing approximately $21 billion in penalties and disgorgements, with about $1.5 billion awarded to whistleblowers. A key focus of Chair Gensler's tenure was on cryptocurrency markets, where the SEC pursued a broad range of enforcement actions. Chair Gensler also championed reforms to money market funds, Treasury markets, and hedge fund reporting.

President Trump has nominated Paul Atkins, a former SEC commissioner and current cryptocurrency advocate, as Chair Gensler's successor. Atkins is expected to adopt more industry-friendly regulatory strategies for cryptocurrency and financial technology development.

Cryptocurrency and Digital Assets Enforcement

SEC Charges Three So-Called Market Makers and Nine Individuals for Market Manipulation and Unregistered Offerings Involving Crypto Assets

On October 9, 2024, the SEC filed five separate complaints in the United States District Court for the District of Massachusetts against three companies and nine individuals, alleging the defendants had attempted to manipulate various crypto asset securities markets and engaged in unregistered securities offerings, among other fraudulent practices. According to the SEC's complaints, crypto asset promoters Russell Armand, Maxwell Hernandez, Manpreet Singh Kohli, Nam Tran, and Vy Pham to artificially inflate the price and trading volume of various crypto assets, including Saitama Inu and Robo Inu Finance tokens. These individual promoters hired two so-called market makers, ZM Quant and Gotbit, to provide market-manipulation-as-a-service. The SEC also alleges that a third company, CLS Global, engaged in similar manipulative trading to artificially inflate price and trading volume.

The fraudulent schemes in which the

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Cryptocurrency and Digital Assets Enforcement *(Continued from page 9)*

defendants allegedly engaged include coordinated purchases, "wash trading," and fraudulent market-making services. "Wash trading" occurs when market makers use the fees they collect from token offerors to pay for services that artificially inflate trading volumes by using multiple accounts to trade against the hiring market maker's own quotation, while no actual change in beneficial ownership occurs. Such activities can fraudulently mislead the public into purchasing securities under false pretenses.

The SEC also contends that these crypto assets were sold in unregistered securities offerings in violation of federal securities laws. Some defendants are accused of using deceptive promotional tactics, including false claims about token functionality and misleading statements regarding their own holdings. For example, the distributors of Saitama Inu, including Pham, allegedly misrepresented their intentions to hold tokens while selling large portions to retail investors.

The SEC seeks permanent injunctions, disgorgement of ill-gotten gains, civil penalties, and prohibitions on participating in securities offerings for those involved.

California DFPI Revokes Crypto Lender BlockFi's Finance Lending License

The California Department of Financial Protection and Innovation (DFPI) announced it has revoked the California Financing Law (CFL) license of crypto lender BlockFi Lending LLC (BlockFi). BlockFi has agreed to the license revocation as part of its settlement agreement with DFPI, which also requires BlockFi to cease its violations and discontinue unsafe or harmful practices. BlockFi offered consumer and commercial loans to the public, secured by digital asset collateral, and operated as a licensed finance lender and broker.

The DFPI determined that BlockFi violated the CFL by failing to assess borrowers' ability to repay loans, charging interest before loan disbursements, neglecting to provide credit counseling, failing to report payment performance to credit bureaus, and inaccurately disclosing annual percentage rates in loan documents.

BlockFi filed for bankruptcy in 2022, shortly after the collapse of cryptocurrency exchange FTX Trading Co. Its bankruptcy plan administrator has since announced that sufficient assets have been recovered to fully repay all customers.

The settlement initially imposed a $175,000 fine for BlockFi's CFL violations. However, the DFPI Commissioner subsequently waived the penalty to prioritize consumer recovery, citing BlockFi's bankruptcy status, cessation of operations, and inability to resume business in the future.

Federal Court Orders Five Individuals to Pay over $5 Million for Digital Asset Fraud and Misappropriation Scheme

The District Court for the Central District of California has issued a consent order and order of default judgment against the individuals doing business as Icomtech. These orders are rooted in a complaint filed in May 2023 by the CFTC alleging fraud in connection with the company's digital asset scheme and misappropriation.

The default judgment order finds four out of five defendants named in the original complaint liable for all named violations of the Commodity Exchange Act (CEA) and CFTC regulations, including the claims that they fraudulently solicited over $1 million from 190 individuals to supposedly trade Bitcoin and other digital asset commodities for the victims, and misappropriated client funds. The order requires the four liable defendants to pay over $1 million jointly and severally in restitution to the victims of their schemes. Each of these defendants is also ordered to pay a $1 million civil monetary penalty. The order also permanently enjoins all defendants from engaging in conduct that violates the CEA, as charged, and permanently bans them from registering with the CFTC and trading in any CFTC-regulated markets.

The consent order finds the fifth defendant not named in the default judgment order, David Ochoa, also engaged in the fraud scheme with the other defendants, which Ochoa admits. The order requires him to pay, jointly and severally with the other defendants, restitution to the Icomtech victims. The order also imposes a permanent injunction and permanent trading, solicitation, and registration bans against Ochoa.

Crypto.com Files Complaint Against SEC After Receiving Wells Notice

Foris DAX Inc. (d/b/a Crypto.com) has filed a complaint against the SEC in the

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Cryptocurrency and Digital Assets Enforcement *(Continued from page 10)*

District Court for the Eastern District of Texas, challenging the agency's efforts to regulate secondary-market sales of network tokens—such as SOL, ADA, BNB, FIL, FLOW, ICP, ATOM, ALGO, NEAR, and DASH—as securities. Crypto.com argues that these tokens are not securities under existing federal securities laws and that it does not act as an unregistered securities broker-dealer or clearing agency. Crypto.com's filing follows its receipt of an SEC notice letter regarding an anticipated enforcement action against Crypto.com for operating as an unregistered broker-dealer and securities clearing agency based on transactions in digital assets.

Crypto.com claims that the SEC has asserted jurisdiction over these tokens by classifying them as "Crypto Asset Securities," a term not found in statutory law, and that the SEC has relied on an enforcement action-based strategy without formal rulemaking, thereby allegedly violating the Administrative Procedure Act. Crypto.com further contends that its secondary-market transactions are legally indistinguishable from similar transactions involving Bitcoin and Ether, crypto assets which the SEC does not regulate as securities.

Crypto.com seeks declaratory and injunctive relief to block the SEC from relying on its classification of network tokens as securities as a basis for enforcement actions.

SEC Charges Cumberland DRW for Operating as an Unregistered Dealer in the Crypto Asset Markets

The SEC has filed a [complaint] in the District Court of the Northern District of Illinois against Cumberland DRW LLC (Cumberland), alleging that the company operated as an unregistered securities dealer in violation of Section 15(a) of the Exchange Act. The complaint accuses Cumberland of engaging in billions of dollars' worth of crypto asset transactions, many of which involved crypto assets the SEC classifies as securities.

The SEC's allegations center on Cumberland's extensive activities in the crypto asset market, including providing liquidity through its single-dealer platform, proprietary trading strategies, and transactions on third-party trading platforms. Since 2018, Cumberland reportedly traded over $2 billion in crypto assets offered and sold as securities, generating more than $400 million in revenue and $27 million in profit. According to the SEC, Cumberland failed to register with the SEC as a dealer or qualify for an exemption.

The SEC's complaint asserts that Cumberland marketed crypto assets such as MATIC, SOL, ATOM, ALGO, and FIL as investment opportunities, often amplifying promotional statements from issuers that encouraged expectations of profit tied to the success of blockchain ecosystems. Cumberland also allegedly conducted research, published reports, and communicated with counterparties to reinforce these expectations. According to the complaint, Cumberland's activities included providing quotes with substantial spreads, publishing trading reports, and promoting speculative investment value through its communications and operations.

The SEC is seeking disgorgement of ill-gotten gains, civil penalties, and a permanent injunction to prevent future violations.

Select Publications

Fintech in Brief
Win Some, Lose Some: Recent Developments in the Regulation of Private Funds
October 14, 2024

Wilson Sonsini Alert
CFPB Releases Final Open Banking Rules: Key Takeaways for Fintech Companies
November 4, 2024

Wilson Sonsini Alert
CFPB Issues Proposed Rule to Cover Data Brokers Under the Fair Credit Reporting Act
December 12, 2024

Wilson Sonsini Alert
Treasury and IRS Release Final Regulations Applicable for Front-End Service Providers Facilitating Digital Asset and Cryptocurrency Transactions
January 8, 2025

Practice Highlights and Speaking Engagements

Wilson Sonsini Partner Jess Cheng Moderates AI Technology Panel at the Clearing House Annual Conference

Fintech and financial services partner Jess Cheng moderated a panel titled, "In the Absence of AI Regulation, Why are There So Many Hurdles to Its Use?" at the Clearing House's Annual Conference on November 13, 2024. The panelists, who included Sandra Lee (U.S. Treasury), Bert Fuqua (Wells Fargo), Terah Lyons (JPMorganChase), the Honorable Eugene A. Ludwig (former Comptroller of Currency, Ludwig Advisors, Canapi Ventures) and Aviad Levin (Socure), discussed the regulatory and supervisory perspectives on AI implementations, including potential risks and effective mitigants.

Wilson Sonsini Partner Jess Cheng Speaks on Risk Management for Instant Payments

Fintech and financial services partner Jess Cheng recently led a panel titled, "The Legal & Compliance Landscape of Instant Payments: What You Need to Know" at the Smarter Faster Payments Conference on December 4, 2024. The panelists discussed the legal and regulatory frameworks governing instant payments and examined the liability and risk management concerns associated with instant payment transactions.

Wilson Sonsini Partner Amy B. Caiazza Speaks on Investment Funds Using Blockchain and AI Technologies at PLI New York's FinTech 2024 Program

Fintech and financial services partner Amy B. Caiazza recently joined Susan Gault-Brown (A&O Shearman), Kelley A. Howes (Morrison Foerster LLP) and Ryan Louvar (WisdomTree Digital Management, Inc.) on a panel titled, "Investment Funds: A Focus on Tokenization and the Use of AI" at the Practising Law Institute's FinTech 2024 program, held in New York City on December 6, 2024. The panelists discussed various issues arising from registered investment companies' use of contemporary blockchain and AI technologies, particularly concerns related to tokenized securities.

Wilson Sonsini Fintech Practice and Partner Jess Cheng Ranked in *2025 Chambers FinTech Guide*

Wilson Sonsini's fintech and financial services practice was included in Chambers and Partners's 2025 ranking of the leading law firms in the fintech market. The fintech practice was recognized for its general fintech legal practice and in the corporate, securities, and financing subcategory. In addition, fintech and financial services partner Jess Cheng was ranked as an outstanding lawyer in the fintech industry. The rankings noted the fintech and financial services practice's outstanding regulatory expertise and ability to advise start-ups on a wide range of transactional and financing issues. Jess was recognized for her significant expertise in payments and cryptocurrency regulations, including her "one-of-a-kind expertise" and "unique experience from her years in both private practice and at the Federal Reserve."

Wilson Sonsini's Fintech Practice Hosts a Series of Events at Money 20/20

Wilson Sonsini partners Amy Caiazza and Jess Cheng hosted the Wilson Sonsini Fintech Reception at Mott 32 during the Money 20/20 conference in Las Vegas, Nevada on October 27, 2024, joined by partners Mark Baudler, Adam Bloom, Jonathan Chan, and Seth Helfgott. In addition, partners Amy Caiazza and Jess Cheng hosted the Wilson Sonsini Women in Fintech Cabana Drop-In at the Venetian Pool Deck, celebrating women across fintech. Wilson Sonsini looks forward to connecting with current and future fintech industry leaders at Money 20/20 2025 from October 26 to 29, 2025.

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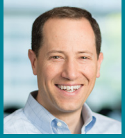

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