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Crypto Regulation (and De-Regulation) in the U.S. and E.U. and the Effects of Each on Consumer Protection and Illicit Transactions

Bella Alonzo

Crypto Regulation (and De-Regulation) in the U.S. and E.U. and the Effects of Each on Consumer Protection and Illicit Transactions

By: Bella Alonzo*

The United States and the European Union face a wide disparity in regulation tactics for cryptocurrencies. With the recent rollout of the world's first comprehensive crypto-asset regulation framework, the EU's Markets in Crypto Assets Regulation (MiCA) has further exacerbated incongruities with the U.S.'s comparatively hands-off, scattered regulation strategy. The lack of uniform market regulation not only challenges compliance efforts, but it leaves critical gaps that have proved harmful for investors and opportune for criminals. Prioritizing international regulatory harmonization could result in continued growth of digital assets and a safer, more stable global crypto market, but the path forward is tense as critics argue that increased regulation will suppress the technological and financial innovation that made digital currencies possible. Harnessing a decentralized and ever evolving asset class without stifling the technology's growth potential requires a well-informed and finely tailored approach that has stumped regulators across the globe. But the emergence of the crypto space provides a novel opportunity for lawmakers to balance risk mitigation with the capacity for creativity and development. As the crypto field continues to expand, this paper contemplates the effects of different regulation strategies and suggests that powerful players in the global digital assets market establish unified regulatory frameworks that protect investors and sanction financial crimes while providing adequate flexibility and institutional support.

I. Introduction

Since the launch of Bitcoin in 2009,[1] the cryptocurrency industry has skyrocketed in popularity, with the global value of crypto assets totaling over $2 trillion in 2024.[2] Backed by blockchain technology, cryptocurrency has seen success largely because of its decentralized nature. Unencumbered by the control of a central government or other authority, and free from middlemen like banks or payment processors, cryptocurrency facilitates peer-to-peer transactions on a global scale at near-lightning speed.[3] Generally speaking, it is an encrypted digital currency (hence the name: "cryptocurrency") that has been called "the flagship of digital finance"[4] and encompasses thousands of virtual payment methods such as Bitcoin and Ethereum.[5] Cryptocurrency exchanges can occur "without the [centralized] storage of information or a central control body," making them a tool capable of bridging global financial gaps.[6]

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* J.D. Candidate, SMU Dedman School of Law, 2026; Staff Editor for the International Law Review Association.

[1] Vladlena Benson et al., *Harmonising Cryptocurrency Regulation in Europe: Opportunities for Preventing Illicit Transactions*, 57 EUR. J. L. & ECON. 37, 38 (2024).

[2] Nathan Rieff, *How Much of All Money Is in Bitcoin?*, INVESTOPEDIA (Apr. 10, 2024), https://www.investopedia.com/tech/how-much-worlds-money-bitcoin/ [https://perma.cc/RMZ7-ZQHB].

[3] *Id.*

[4] Georgios Pavlidis, *Europe in the Digital Age: Regulating Digital Finance Without Suffocating Innovation*, 13 L. INNOVATION & TECH. 464, 465 (2021).

[5] *Id.* at 466.

[6] *Id.* at 465.

But the somewhat anonymous and decentralized characteristics of digital assets are what constitute major areas for concern, ultimately allowing the cryptocurrency space to become "a Petri dish for criminals."[7] One crime report estimated roughly $39.6 billion of illicit cryptocurrency transactions in 2022.[8] While that number seems to be steadily dropping throughout 2023 and 2024, these crimes still account for tens of billions of dollars in transactions annually.[9]

From the lens of protecting consumers and deterring fraudulent transactions, the clearest solution is to impose stricter regulations.[10] But since digital assets have penetrated the global economy so rapidly, the path to regulation is far from being clearly paved, and policymakers have struggled to develop an appropriate approach.[11] One of the largest hurdles is the delicate balance between regulation and innovation.[12] As such a novel invention, the full potential of cryptocurrency technology remains untapped, which lends the argument that any regulatory schemes should leave room for growth in the industry.[13] On the other hand, cryptocurrency's capability of facilitating disruptive,[14] illegal, and sometimes dangerous activities, coupled with its volatility, warrants the necessity for imposing restrictions on the use of the asset.[15]

As two of the largest players in the global cryptocurrency market, the United States and the European Union face a wide disparity in regulation tactics for this asset class.[16] Section II of this paper plans to explore cryptocurrency's current lack of uniform market regulation, specifically comparing the facets of the European Union's Markets in Crypto Assets (MiCA) regulation strategy with the more hands-off regulation of the United States. Section III attempts to survey the legal effects of each regulatory approach on the cryptocurrency market, especially regarding consumer protection and fraudulent transactions, while also considering suggestions to resolve existing regulatory gaps.

II. Scattered Cryptocurrency Market Regulation

Cryptocurrency regulation strategies vary drastically around the world, which challenges market participants when a clear and harmonized set of rules does not exist to structure operations around.[17] On one hand, regions like Europe and the Middle East are making active steps towards enacting unambiguous and comprehensive regulations.[18] But other significant financial markets

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[7] Benson et al., *supra* note 11, at 38.
[8] Chainalysis Team, *2024 Crypto Crime Trends: Illicit Activity Down as Scamming and Stolen Funds Fall, but Ransomware and Darknet Markets See Growth*, CHAINALYSIS (Jan. 18, 2024), *h*ttps://www.chainalysis.com/blog/2024-crypto-crime-report-introduction/ [https://perma.cc/7P37-7X7H].
[9] *Id.*
[10] Benson et al., *supra* note 1, at 38.
[11] *Id.* at 39.
[12] Yukun Liu & Aleh Tsyvinski, *Risks and Returns of Cryptocurrency*, 34 REV. FIN. STUD. 2689, 2689 (2020).
[13] *Id.*
[14] Pavlidis, *supra* note 4, at 465.
[15] Benson et al., *supra* note 1, at 39.
[16] *Navigating the Global Crypto Landscape with PwC: 2024 Outlook*, PWC (Dec. 2023), https://www.pwc.com/gx/en/industries/financial-services/assets/navigating-the-global-crypto-landscape-with-PwC-2024.pdf [https://perma.cc/FRJ8-C954].
[17] Alice Tchernookova, *US crypto regulation: leading by enforcement won't work*, INT. FIN. L. REV., Jun. 20, 2023, at 1.
[18] *Navigating the Global Crypto Landscape with PwC: 2024 Outlook*, *supra* note 16.

like the United States retain "complex and fragmented regulatory systems, where federal and state agencies have overlapping and sometimes conflicting mandates or rules."[19] Furthermore, in addition to the technical complications of regulating cryptocurrency, like tracking secure blockchain transactions or identifying users,[20] the "borderless nature" of digital assets poses a challenge to traditional jurisdictional boundaries.[21]

A. EU REGULATION

Home to nearly twenty percent of worldwide crypto transaction volume, the central, northern, and western Europe region constitutes a major player in the cryptocurrency space.[22] In a concerted effort "to facilitate legal certainty for businesses and attract more investment to the region,"[23] the European Union (EU) formulated the Markets in Crypto-Assets (MiCA) regulation: The world's first comprehensive regulation strategy that crosses jurisdictional boundaries.[24] Initially taking effect at the end of July 2023, these regulations are being periodically phased in across the twenty-seven EU member states through the end of June 2026.[25]

Prior to the implementation of MiCA, a survey of cryptocurrency experts in France, Germany, Italy, Liechtenstein, and the United Kingdom revealed that two resounding regulatory issues in the market were a "lack of a clear classification of cryptocurrencies and crypto assets" and a "lack of harmonized legislation."[26] Now, MiCA attempts to remedy those concerns and more, proposing four primary objectives for the regulation.[27] The first is to establish a legal framework for digital assets not already covered under EU legislation.[28] The second is to provide legal clarity with the intention of promoting innovation and the growth of cryptocurrency and its technology within both the EU and the broader global market.[29] Third, MiCA aims to afford consumers and investors greater protection, primarily by encouraging "market integrity."[30] Finally, the rules seek to "enhance financial stability" in anticipation of the continued growth of crypto-assets.[31]

MiCA intends to achieve these objectives by including within its scope of regulated services a wide array of activities, such as "custody and administration, operation of trading platforms, exchange, execution and transfer activities, [advice], and portfolio management."[32] Some notable

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[19] *Id.*
[20] Benson et al., *supra* note 1, at 41.
[21] *Id.* at 37.
[22] Chainalysis Team, *2023 Geography of Cryptocurrency Report: Institutions in Central, Northern, and Western Europe Broaden Horizons with DeFi and Web3 Experimentation*, CHAINALYSIS (Oct. 18, 2023), https://www.chainalysis.com/blog/western-europe-cryptocurrency-adoption/. [https://perma.cc/BRJ7-RC8L].
[23] Jack Schickler, *MiCA, EU's Comprehensive New Crypto Regulation, Explained*, COINDESK (Sep. 7, 2023) https://www.coindesk.com/learn/mica-eus-comprehensive-new-crypto-regulation-explained/ [https://perma.cc/S46R-SNHH].
[24] *Navigating the Global Crypto Landscape with PwC: 2024 Outlook*, *supra* note 16, at 15.
[25] *Id.*
[26] Benson et al., *supra* note 1, at 46.
[27] ISSAM HALLAK, MARKETS IN CRYPTO-ASSETS (MICA), 2 (2023).
[28] *Id.*
[29] *Id.*
[30] *Id.*
[31] *Id.*
[32] *Navigating the Global Crypto Landscape with PwC: 2024 Outlook*, *supra* note 16, at 15.

provisions of MiCA include requirements that issuers and service providers register and be authorized by a national competent authority of a member state, comply with existing anti-money laundering and counter-terrorism financing laws that other financial institutions are subject to, "provide clear and accurate information to consumers about the risks associated with crypto assets," and maintain efforts to reduce their environmental impact.[33]

Additionally, the text of MiCA names three categories of assets not previously included in legislation,[34] specifically (1) asset-referenced tokens (ART), which tether their value to tangible assets and/or one or more currencies, (2) electronic money tokens (EMT), which are tied to a single official currency, and (3) other previously unregulated crypto assets.[35] The legislation further details that the three types "should be distinguished from one another and subject to different requirements depending on the risks they entail."[36] Any asset that falls into one of those categories is subject to the corresponding regulations encompassing the EU member states, although a handful of member states are supplementing the MiCA rollout with their own legislation.[37]

This framework is not without critique, as MiCA does not cover all types of digital assets; there are still gaps in the law for innovations like decentralized finance (DeFi).[38] Additionally, some financial experts claim that MiCA sets standards that are too stringent, then punishes with fines that can stretch into the tens of millions of euros.[39] Nonetheless, the EU's regulation strategy is a movement in the direction of increasing legal clarity, enhancing investor protection, and imposing sanctions for illegal activities.[40]

B. U.S. REGULATION

In contrast to the EU's comprehensive MiCA regulatory scheme, crypto-asset regulation in the United States (U.S.) is relatively sparse.[41] The significance of U.S. regulation tactics lies in the fact that its "cryptocurrency markets are the largest and most influential in the world, standing out globally by a large margin."[42] North America represents over twenty-two percent of global crypto activity, "with an estimated $1.3 trillion in on-chain value received between July 2023 and June 2024."[43] Additionally, roughly one in six U.S. adults report having "ever invested in, traded or

[33] *The EU and the Markets in Crypto-Assets (MiCA) Regulation*, SHAREID, https://www.shareid.ai/blog/mica-regulation#:~:text=The%20fines%20for%20non%2Dcompliance,annual%20turnover%2C%20whichever%20is%20greater (last visited Oct. 31, 2024).
[34] *See* Hallak, *supra* note 27, at 1.
[35] Council Regulation 2023/1114, 2023 O.J. (L 150) 44.
[36] *Id.*
[37] *Navigating the Global Crypto Landscape with PwC: 2024 Outlook*, *supra* note 16, at 14.
[38] Benson et al., *supra* note 1, at 50-51.
[39] *See The EU and the Markets in Crypto-Assets (MiCA) Regulation*, *supra* note 33.
[40] *Id.*
[41] Tchernookova, *supra* note 17, at 1.
[42] Chainalysis Team, *2024 Geography of Cryptocurrency Report: North America: Institutional Momentum and U.S. Bitcoin ETPs Propel Crypto Further Into the Mainstream*, CHAINALYSIS (Oct. 17, 2024), https://www.chainalysis.com/blog/north-america-crypto-adoption-2024/ [https://perma.cc/Y478-JLT6].
[43] *Id.*

used a cryptocurrency," making this asset class relevant to an increasing portion of the population.[44]

The United States remains engaged in a live debate over where cryptocurrency regulation would most appropriately lie.[45] Currently, crypto-asset regulation in the U.S. takes place primarily by ex-post enforcement actions as opposed to ex-ante legislation or rulemaking.[46] But it is still unclear where the bulk of such power should fall.[47] High tensions exist between the two federal agencies grappling for regulatory power over digital assets: the Securities and Exchange Commission (SEC) and the Commodity Futures Trading Commission (CFTC).[48] While the federal government has generally taken a more hands-off approach thus far, "the SEC has been the most aggressive regulator, with a total 100 actions and lawsuits against digital asset companies on grounds of violations of registration of securities, registration as a national security exchange or as a broker dealer, or as a clearing agency."[49] Second to the SEC in such regulation attempts is the CFTC, bringing "[nineteen] enforcement actions and four arrest-related lawsuits in 2022," considerably increasing its scrutiny compared to the SEC's thirty enforcement actions that same year.[50]

The SEC argues that as the main regulator of the securities industry, it is also the proper regulatory authority for crypto assets.[51] It is well-established by the Securities Act that the SEC has dominion over securities including "investment contracts," defined by the Supreme Court in 1946 through the *Howey* test: "a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of [others]."[52] Many argue that digital assets fit within the *Howey* definition, including previous SEC Director of Enforcement, Gurbir Grewal, who expressed in one statement that because the definition of "security" is meant to be sufficiently broad "to allow for the flexibility that comes with innovative investment products," the cryptocurrency market should have to comply with securities laws.[53]

The CFTC, on the other hand, which generally regulates commodities, states that assets like Bitcoin fall under the definition of a "commodity" as described by the Commodity Exchange Act.[54] The CFTC holds that their authority over crypto assets "is implicated when a virtual currency is used in a derivatives contract, or if there is fraud or manipulation involving a virtual currency

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[44] Michelle Faverio & Olivia Sidoti, *Majority of Americans aren't Confident in the Safety and Reliability of Cryptocurrency*, PEW RSCH. CTR. (Apr. 10, 2023) https://www.pewresearch.org/short-reads/2023/04/10/majority-of-americans-arent-confident-in-the-safety-and-reliability-of-cryptocurrency/ [https://perma.cc/4PDW-RPGD].
[45] Jacob G. Stanley, *A Disruptive Ripple in the SEC's Regulation of Crypto Assets*, 28 N.C. BANKING INST. 467, 471 (2021).
[46] Tchernookova, *supra* note 17, at 1.
[47] *Id.*
[48] *Id.*
[49] *Id.*
[50] *Id.*
[51] Gurbir S. Grewal, Dir. Div. Enf't, Sec. Exch. Comm'n, What's Past is Prologue: Enforcing the Federal Securities Laws in the Age of Crypto, Speech at William & Mary Business Law Review's Third Annual Symposium: "Regulating Finance in a Changing Administrative State" (July 2, 2024).
[52] *SEC v. W.J. Howey Co.*, 328 U.S. 293, 298-99 (1946).
[53] Grewal, *supra* note 51.
[54] BITCOIN BASICS, U.S. COMMODITY FUTURES TRADING COMMISSION 1 (2019).

traded in interstate commerce."[55] Each of the agencies' arguments can be strengthened by those who agree that at its core, cryptocurrency "fulfills similar functions as other, more traditional assets."[56] Furthermore, the agencies can draw a parallel to the EU, where cryptocurrency exchanges "fall into the same regulatory framework as banks and other financial services."[57]

But outside of these government agencies, many in the crypto industry reject SEC and CFTC attempts to regulate, "arguing that laws designed for traditional finance are ill-suited to regulate their innovations."[58] SEC Chairman Gary Gensler claimed this evasion is a result of certain industry participants exploiting "jurisdictional gaps," as well as a general "lack of compliance with existing legal requirements."[59]

Beyond agency enforcement and fairly minimal federal legislative action, many states have begun to take digital asset regulation into their own hands, predominantly through their own legislative processes.[60] The National Conference of State Legislatures reported last year that "[t]hirty-nine states, Puerto Rico and the District of Columbia have introduced or [have] pending legislation regarding cryptocurrency, digital or virtual currencies and other digital assets in the 2023 legislative session."[61] For example, Wyoming enacted the Wyoming Stable Token Act and established the Wyoming Stable Token Commission.[62] Utah also created the Decentralized Autonomous Organization Act, outlining requirements for organization formation and recognition.[63] Additionally, North Dakota adapted its money transmission law to include additional definitions and create licensing requirements for participation in the money transmission business.[64] Such trends imply that without further federal action, digital asset regulation will continue to arise at the state level.[65]

III. The Need for Uniform Cryptocurrency Regulation Balanced with Innovation

As previously discussed, the cryptocurrency market lacks a uniform regulation strategy, which creates a dangerous environment for consumers and investors.[66] Ample criminal opportunities arise in the absence of regulation, most notably money laundering, which "is the main criminal activity associated with the illicit use of cryptocurrencies."[67] Furthermore, without an adequate regulatory framework in place to promote accountability, crypto investors are vulnerable to fraud,

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55 *Id.*
56 Liu & Tsyvinski, *supra* note 12, at 2689.
57 CRYPTOCURRENCIES - TRACING THE EVOLUTION OF CRIMINAL FINANCES, 7 (Eur. Union Agency for L. Enf't Coop., Dec. 2021 ed., 2021).
58 Stanley, *supra* note 45, at 473.
59 Timothy G. Massad & Howell E. Jackson, *How to improve regulation of crypto today – without congressional action—and make the industry pay for it*, 1-2 (Hutchins Ctr. on Fiscal & Monetary Pol'y, Working Paper No. 79, 2022).
60 CRYPTOCURRENCIES - TRACING THE EVOLUTION OF CRIMINAL FINANCES, *supra* note 57, at 3.
61 *Cryptocurrency 2023 Legislation*, NATIONAL CONFERENCE OF STATE LEGISLATURES (Mar. 26, 2023), https://www.ncsl.org/financial-services/cryptocurrency-2023-legislation [https://perma.cc/JRU8-P6EE].
62 *Id.*
63 *Id.*
64 *Id.*
65 *Id.*
66 *Navigating the Global Crypto Landscape with PwC: 2024 Outlook*, *supra* note 16.
67 Benson et al., *supra* note 1, at 39.

which the EU Agency for Law Enforcement Cooperation reports as "the most frequently identified predicate [offense] in the illegal use of cryptocurrencies."[68] In one notable case, *SEC v. Terraform Labs*,[69] the jury unanimously found that Terraform was liable for defrauding investors by lying "about the false use of Terraform blockchain to settle transactions and about the stability of their crypto asset security."[70] The company "orchestrated one of the largest securities frauds in U.S. history" and left numerous victims with their life savings drained after wiping out over forty billion dollars in market value in a matter of days.[71] Tragedies like this illustrate the risks that investors face in a largely unregulated market.[72]

Regulation on the consumer protection front is especially important because cryptocurrency returns tend to "experience high probabilities of extreme losses and gains" compared to other securities, exposing investors to high risk.[73] In an environment where asset prices can plummet or skyrocket overnight, resulting in the collapse of numerous firms, investors' "calls for better regulation of the crypto industry" have increased.[74] One study showed that "investor attention," measured in Google searches and Twitter post counts,[75] is one of the most dispositive factors in predicting crypto returns.[76] This finding hints towards the substantial swaying power that investors have over the market and why their voices should not be ignored.[77] But potentially due to regulatory gaps, and as mentioned in Section II, "the industry does not comply with investor protection standards comparable to other financial markets, and hundreds of thousands of people have suffered losses."[78]

Still, while investor protection is key in a volatile market, that consideration should be underscored by the need to balance regulation and innovation.[79] The emergence of digital assets has created a novel opportunity to craft a regulatory landscape that intertwines risk mitigation with "the promotion of digital financial innovation."[80] But with a globe full of government entities, technology developers, market participants, and legal scholars chiming in, the path to an ideal scheme is murky.[81]

For instance, some believe that the MiCA regulatory rollout "aims to strike a fair balance between addressing different levels of risk posed by each type of crypto-asset and the need to foster financial innovation."[82] Others criticize the EU for pushing too hard to regulate, and thus living

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[68] CRYPTOCURRENCIES - TRACING THE EVOLUTION OF CRIMINAL FINANCES, *supra* note 50, at 3.
[69] *Sec. & Exch. Comm'n v. Terraform Labs Pte. Ltd.*, 684 F. Supp. 3d 170, 201 (S.D.N.Y. 2023).
[70] Press Release, U.S. Sec. & Exch. Comm'n, Terraform & Kwon to Pay $4.5 Billion Following Fraud Verdict (Jul. 2, 2024).
[71] *Id.*
[72] *Id.*
[73] Liu & Tsyvinski, *supra* note 12, at 2690.
[74] Massad & Jackson, *supra* note 59, at 1.
[75] Liu & Tsyvinski, *supra* note 12, at 2691-92.
[76] *Id.* at 2724-25.
[77] *Id.*
[78] Massad & Jackson, *supra* note 59, at 1.
[79] Pavlidis, *supra* note 4, at 467.
[80] *Id.*
[81] *Id.*
[82] *Navigating the Global Crypto Landscape with PwC: 2024 Outlook*, *supra* note 16, at 14.

in the U.S.'s shadow when it comes to digital innovation.[83] This illustrates the continuous tension that constitutes a barrier to developing a comprehensive strategy.[84]

Some scholars, including Timothy Massad, former Chairman of the CFTC, and Howell Jackson, Professor of Law at Harvard Law School, suggest an alternate approach to crypto regulation that would not require congressional action.[85] They propose "the creation of a new self-regulatory organization (SRO) . . . formed and supervised by regulators, whose mission would be to protect investors and financial markets by developing and enforcing much-needed standards for the crypto industry."[86] Proponents of an SRO believe it could be a viable solution, at least in the U.S., if jointly supervised by the SEC and CFTC.[87] Because these two agencies have the power to establish such an SRO without the help of Congress, this approach could expeditiously provide clear, consistent standards "that could apply to all assets traded on [crypto trading] platforms."[88] The creation of a jointly overseen entity also remedy "the need to litigate whether digital assets are securities or commodities."[89] Such a proposal would likely not be the last stop on the journey towards comprehensive regulation, and might only serve as a tool "to determine whether further legislation is needed and . . . build consensus on what that legislation should look like."[90] But it could be a step towards properly regulating one of the largest crypto markets in the world.[91]

IV. Conclusion

As the crypto "Wild West" continues to evolve, it is imperative that regulatory bodies attempt to keep pace with digital developments.[92] The present lack of uniform market regulation[93] not only challenges market participants seeking to comply,[94] but it leaves gaps in the system that have proved harmful for investors[95] and opportune for criminals.[96] The regulatory strategy of the EU is relatively comprehensive, unified, and strict compared to the scattered, multi-level, and developing strategy of the U.S.;[97] but with both markets playing such a substantial role in the global crypto space, the need for harmonization remains crucial.[98] "Regulatory uncertainty . . . emphasizes the need for balanced innovation, clear regulatory frameworks, and sustained institutional support to ensure the continued growth and stability of the crypto industry at large."[99]

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[83] Pavlidis, *supra* note 4, at 465.
[84] *Id.*
[85] Massad & Jackson, *supra* note 59, at 1.
[86] *Id.* at 2.
[87] *Id.*
[88] *Id.*
[89] *Id.* at 2-3.
[90] *Id.* at 3.
[91] *See* Chainalysis Team, *supra* note 22.
[92] Stanley, *supra* note 45, at 469.
[93] *Navigating the Global Crypto Landscape with PwC: 2024 Outlook*, *supra* note 16, at 6.
[94] Tchernookova, *supra* note 17, at 1.
[95] Massad & Jackson, *supra* note 59, at 1.
[96] Benson et al., *supra* note 1, at 38.
[97] *Navigating the Global Crypto Landscape with PwC: 2024 Outlook*, *supra* note 16, at 11.
[98] Benson et al., *supra* note 1, at 38.
[99] *See* Chainalysis Team, *supra* note 42.