

## One Size FITs All? Proposed US Crypto Legislation to Receive Vote in House of Representatives

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On May 10, 2024, Representative Patrick McHenry, Chairman of the House Financial Services Committee for the United States Congress, stated that the United States House of Representatives will vote on whether to approve the *Financial Innovation and Technology for the 21st Century Act* (FIT21, or the Act).<sup>1</sup> If passed, FIT21 would mark a critical step towards establishing a clearer regulatory framework for digital assets in the United States.

While proponents of FIT21 argue that comprehensive regulation is necessary for achieving regulatory clarity for digital assets, some stakeholders do not believe that the proposed legislation will fare well in the Senate,<sup>2</sup> where key members, including the Chairman of the Senate Banking Committee, Senator Sherrod Brown, have a history of staunch opposition to bespoke digital asset legislation.

Regardless of whether FIT21 becomes legal statute, this proposed framework for digital asset regulation provides an insight into the direction of potential digital asset-focused regulation in the United States. FIT21 also provides a potential precedent for digital asset regulation in may take in Canada and other jurisdictions.

### NOTABLE ELEMENTS OF REGULATION

#### CFTC and SEC Regulatory Authority

First introduced on July 20, 2023, the proposed legislation aims to establish a regulatory framework for digital assets, delineating responsibility among the Commodity Futures Trading Commission (CFTC) and the Securities and Exchange Commission (SEC), depending on the form of the digital asset. Among other important consumer protections and regulations for digital assets, under FIT21, if a digital asset is on a blockchain that is functional and decentralized, it is classified as a commodity and will fall under the purview of the CFTC. However, if a digital asset is on a blockchain that is functional and not decentralized, it is classified as a security and it falls under the purview of the SEC. FIT21 also recognizes a means by which an SEC regulated digital asset, referred to as a “restricted digital asset”, can transition into a digital commodity through decentralization, which in turn shifts jurisdiction from the SEC to CFTC for same asset. FIT21 categorizes a blockchain as decentralized if, among other requirements, no single person has unilateral authority to control the blockchain or its usage, and no issuer or affiliated person has control of 20% or more of the digital asset or its voting power.<sup>3</sup>

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FIT21 also provides the CFTC with regulatory authority over cash or spot markets for digital commodities. Notably, FIT21 excludes permitted stablecoins from CFTC and SEC regulation, except regarding anti-fraud regulation, and regarding specified transactions on registered entities. In addition, FIT21 requires that the CFTC and SEC must jointly define terms and exempt dually registered exchanges from duplicative rules.

## **Proposed Exemptions to Prospectus Requirements**

There are also specific proposed exemptions to prospectus requirements and other SEC mandated rules for digital assets. The following non-exhaustive list provides examples of exemptions proposed in FIT21. A transaction in digital assets is exempt from the prospectus requirement, and therefore a restricted digital asset if, among other requirements:

- (a) the digital asset issuer has sold less than \$75 million in the preceding 12 months;
- (b) the purchaser (who is not an accredited investor) is not expending more than the greater of 10% of annual income or net worth, as applied to all transactions in digital assets;
- (c) the post transaction purchaser does not own more than 10% of digital assets sold on reliance on exemption; and
- (d) the sale constitutes an investment contract.

## **Consumer Protection in FIT21**

FIT21 imposes comprehensive customer disclosure, asset safeguarding, and operational requirements on all entities that are required to be registered with the CFTC and/or the SEC.<sup>4</sup> The Act seeks to protect consumers by strengthening transparency and accountability with market participants by requiring digital asset developers to provide accurate, relevant disclosures which includes information relating to the digital asset project's operation, ownership and structure. Furthermore, customer-serving institutions such as exchanges, brokers, and dealers will also be required to provide customers with appropriate disclosures, segregate customer funds from their own, and reduce conflicts of interest through registration, disclosure and operational requirements.

## **THE FUTURE OF FIT21 IN THE UNITED STATES**

This proposed legislation could provide the regulatory clarity necessary for the digital asset ecosystem to thrive in the United States, and promote [further innovation in the industry](#). For example, digital asset developers would have a pathway to raise funds and participants would also be able to determine which digital asset transactions are subject to either the SEC or the CFTC's jurisdiction. The establishment of

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clear lines between the SEC and the CFTC will also protect customer-serving digital asset institutions by creating comprehensive regulatory and registration regimes that permit them to operate in digital asset markets.

## NEXT STEPS

The United States House of Representatives is set to vote on FIT21 in the second half of May or early June 2024. If FIT21 is passed by the House, it will then move on to a vote from the United States Senate at a later date, likely with at least some revision. We will continue to monitor the evolution of this proposed legislation given the significant overlap between American and Canadian securities regulation and policy.

We will also continue to monitor the Canadian regulatory environment to see whether the proposed omnibus digital asset legislation in the United States encourages Canadian regulators or legislators to introduce a more comprehensive, streamlined approach to regulation. In the meantime, if you or your organization have questions regarding fulfilling obligations to Canadian regulators, or if you or your organization are concerned about the impacts of FIT21, we encourage you to reach out to members of our [Blockchain & Digital Assets](#) group for assistance.

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<sup>1</sup> H.R.4763 - 118th Congress (2023-2024): Financial Innovation and Technology for the 21st Century Act, H.R.4763, 118th Cong. (6 May 2024), <[congress.gov/bill/118th-congress/house-bill/4763](https://congress.gov/bill/118th-congress/house-bill/4763)> (FIT21).

<sup>2</sup> Damilola Lawrence, "U.S. House Gears Up to Decide on Landmark Cryptocurrency Legislation" (11 May 2024), online: <[msn.com/en-us/news/politics/us-house-gears-up-to-decide-on-landmark-cryptocurrency-legislation/ar-BB1mb9nP?ocid=BingNewsSerp](https://msn.com/en-us/news/politics/us-house-gears-up-to-decide-on-landmark-cryptocurrency-legislation/ar-BB1mb9nP?ocid=BingNewsSerp)>.

<sup>3</sup> FIT21, *supra* note 1.

<sup>4</sup> Financial Services Committee, "House to Consider Financial Innovation and Technology for the 21st Century Act" (10 May 2024), online: <[financialservices.house.gov/news/documentsingle.aspx?DocumentID=409251](https://financialservices.house.gov/news/documentsingle.aspx?DocumentID=409251)>.