Securities Regulation Daily Wrap Up, BLOCKCHAIN—S.D.N.Y.: Ex-Celsius executives charged in connection with multibillion-dollar fraud and market manipulation scheme, (Jul 13, 2023)

By Suzanne Cosgrove

U.S. law enforcement officials and three federal regulators announced parallel charges against former Celsius CEO Alexander Mashinsky and Roni Cohen-Pavon, the company's ex-chief revenue officer.

The U.S. Attorney for the Southern District of New York, the FBI, the SEC, the CFTC and the FTC Thursday announced a litany of charges against Alexander Mashinsky, the founder and former chief executive officer of Celsius Network LLC and their affiliated entities, including securities fraud, commodities fraud and wire fraud (*U.S. v. Mashinky*, unsealed on July 13, 2023).

In addition, officials charged Mashinsky with defrauding customers and misleading them about core aspects of the company he founded, including Celsius's success, profitability and the type of investments made by the company with customers' funds.

According to press reports, Mashinsky was arrested in New York early Thursday. Cohen-Pavon, an Israeli citizen, is still at large, U.S. Attorney Damian Williams said in a live-streamed briefing with the FBI, CFTC and SEC. Mashinsky pleaded not guilty to the federal fraud charges.

Celsius filed for bankruptcy on July 13, 2022. At that time, the company's liabilities reportedly exceeded its assets by more than one billion dollars.

"Exactly one year ago today, Celsius Network, a crypto platform that, at its height, managed approximately $25 billion in customer assets, filed for bankruptcy protection in the Southern District of New York," Williams said in a statement. "We have worked quickly to get to the bottom of what led to Celsius' collapse and to understand how a platform that advertised itself as the 'safest place for your crypto' could have left investors holding billions of dollars in losses. Today we have the answer," he added.

CEL inflation. A criminal indictment unsealed Thursday in Manhattan federal court detailed the executives' alleged wrongdoings, stating that from at least 2018 through about June 2022, Alexander Mashinsky, together with Cohen-Pavon, orchestrated a scheme to defraud customers of Celsius Network LLC and inflate the price of Celsius' proprietary crypto token, CEL.

"In sum and substance, Mashinsky portrayed Celsius as a modern-day bank, where customers could safely deposit crypto assets and earn interest," the filing stated. "In truth, however, Mashinsky operated Celsius as a risky investment fund, taking in customer money under false and misleading pretenses and turning customers into unwitting investors in a business far riskier and far less profitable than what Mashinsky had represented."

In a second phase of the scheme, Mashinsky, Cohen-Pavon, and other Celsius employees illicitly manipulated the price of CEL, causing the public to purchase the digital token at inflated prices, the filing states. The purchases benefited Mashinsky and Cohen-Pavon because they secretly sold CEL at prices that they knew did not reflect its true market value. FBI New York Special Agent Michael Brodack Thursday estimated Mashinsky made more than $40 million in profits from the manipulation scheme and Cohen-Pavon made about $3.6 million.

SEC charges. In its parallel complaint, the SEC also charged Celsius Network Limited and its founder and Mashinsky for violating registration and anti-fraud provisions of the federal securities laws, including by failing to register the offers and sales of Celsius' crypto lending product, the Earn Interest Program, making false and misleading statements to investors in the Earn Interest Program and CEL, and by engaging in CEL market manipulation. The Earn Interest Program allowed investors to tender their crypto assets to Celsius in exchange for interest payments.

"Celsius lied to investors by presenting itself as a safe investment opportunity and a chance to gain financial freedom, but, behind the scenes, the company operated a failing business model and took significant risks with investors' crypto assets," said Gurbir Grewal, director of the SEC's Enforcement Division.

CFTC weighs in. The CFTC complaint alleged Celsius acted as an unregistered commodity pool operator and Mashinsky operated as an unregistered associated person of a CPO. The CFTC and Celsius agreed to resolve the complaint against the company by imposing a permanent injunction prohibiting future violations of the Commodity Exchange Act.

In its continuing litigation against Mashinsky, the CFTC seeks restitution, disgorgement, civil monetary penalties, permanent trading and registration bans, and a permanent injunction against further violations of the CEA and CFTC regulations.

FTC proposes settlement. Separately, the FTC announced a settlement with the Celsius Network that will permanently ban it from handling consumers' assets and charged three former executives with tricking consumers into transferring cryptocurrency onto the platform by falsely promising that deposits would be safe and always available.

The proposed settlement with Celsius and its affiliates would permanently ban the companies from offering, marketing, or promoting any product or service that could be used to deposit, exchange, invest, or withdraw any assets. The companies also agreed to a judgment of $4.7 billion, which will be suspended to permit Celsius to return its remaining assets to consumers in bankruptcy proceedings.

The former executives—Mashinsky and other Celsius co-founders Shlomi Daniel Leon and Hanoch Goldstein—have not agreed to a settlement and the FTC's case against them is expected to proceed in federal court, the Commission said.

More to come? The latest flurry of filings was preceded by a complaint filed in January by New York Attorney General Leticia James, who charged Mashinsky with defrauding investors. The AG's complaint sought to ban Mashinsky from doing business in New York and require him to pay damages, restitution and disgorgement.

When asked Thursday by a reporter if Celsius customers would get any money back, and if more cases crypto-related fraud cases are forthcoming, U.S. Attorney Williams stated that "Our hope is to see a robust recovery for the victims, but it's a process that's more complicated, of course, by the bankruptcy proceedings." As for future crypto cases, Williams said, "We continue to be very busy."

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