Securities Regulation Daily Wrap Up, BLOCKCHAIN—S.D.N.Y.: CFTC charges KuCoin with operating illegal digital asset derivatives exchange, (Mar. 27, 2024)

Securities Regulation Daily Wrap Up

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By Suzanne Cosgrove

KuCoin allegedly dealt in multiple off-exchange commodity futures transactions, including bitcoin, soliciting and accepting orders for the products without registering with the CFTC.

The CFTC has filed a civil enforcement action in the U.S. District Court for the Southern District of New York charging Mek Global Limited, PhoenixFin PTE Ltd., Flashdot Limited, and Peken Global Limited, which collectively operate a centralized digital asset exchange under the name KuCoin, with multiple violations of the Commodity Exchange Act (CEA) and CFTC regulations (*CFTC v. Mek Global Limited*, March 26, 2024).

The complaint alleges KuCoin illegally dealt in off-exchange commodity futures transactions and leveraged, margined, or financed retail commodity transactions, soliciting and accepting orders without registering with the CFTC as a futures commission merchant (FCM) or in any other capacity.

According to the court filing, KuCoin operated a facility for the trading or processing of swaps without registering with the CFTC as a swap execution facility (SEF) or designated contract market (DCM) and failed to implement an effective customer identification program.

KuCoin is headquartered in the Republic of Seychelles, the Cayman Islands, and Singapore, with 27 million customers across 200 countries, including the United States. It posted a cumulative trading volume of $3.6 trillion in 2022.

Crypto trading facilitated. From at least July 2019 and continuing to at least June 2023, KuCoin solicited and accepted orders, accepted property to margin, and operated a facility for the trading of futures, swaps, and leveraged, margined, or financed retail transactions involving digital assets that are considered commodities, including bitcoin, ether and litecoin, the court filing states.

During that period, between 20 percent and 50 percent of KuCoin's customers were based in the U.S. according to KuCoin's own marketing material, the CFTC said, which put KuCoin squarely within the CFTC's authority and required that KuCoin register with the CFTC and comply with its applicable regulations.

"For too long, some offshore crypto exchanges have followed a now-familiar playbook by offering derivative products and falsely claiming people in the United States cannot use their platforms, when in reality, anyone in the U.S. with commonly used technology can trade without providing basic customer identifying information," said Ian McGinley, the CFTC's director of enforcement, in a prepared statement.

Disregard of KYC rules. Despite KuCoin's solicitation of U.S. investors, KuCoin disregarded numerous federal laws, including laws that require the implementation of controls designed to prevent and detect money laundering and terrorism financing—such as know-your-customer (KYC) verification procedures.

KuCoin obscured its solicitation of U.S. persons by implementing half-measures that did little to ensure compliance with applicable U.S. laws and regulations, the court filing shows. For instance, KuCoin's "Terms of Use" stated that residents of restricted locations such as the United States could not use the KuCoin platform, but the exchange did not implement any mandatory measures to verify the location or residence of its customers, or to restrict U.S. customers from accessing and trading on its platform.

And although U.S. customers that submitted KYC information were subject to certain trading restrictions, they were not prohibited from trading commodity derivatives. Even after receiving KYC information identifying

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individuals as U.S. customers, KuCoin continued to allow those customers to engage in the trading of futures, swaps, and leveraged, margined, or financed retail commodity transactions in violation of the CEA and CFTC regulations.

In its continuing litigation against KuCoin, the CFTC said it seeks disgorgement, civil monetary penalties, permanent trading and registration bans, and a permanent injunction against further violations of the CEA and CFTC regulations, as charged.

In a separate criminal matter, the U.S. Attorney's Office for the Southern District of New York filed an indictment against KuCoin and two of its founders, Chun Gan, a/k/a "Michael," and Ke Tang, a/k/a "Eric," for conspiring to operate an unlicensed money transmitting business and a substantive violation of the Bank Secrecy Act. Gan and Tang remain at large.

This is case No. 1:24-cv-02255.

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