

# Celebrity endorsement of crypto-assets: *the case of Kim K*

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# Background

This presentation is based on an article published in the *Bulletin Droit et Banque*, issue 72, published by the Luxembourg Banking and Financial Association, titled

*‘Keeping Up With The Rules When Endorsing Crypto-Assets: Kimberly Kardashian’*

For more information, please visit [www.melvintjonakon.com](http://www.melvintjonakon.com).

# Overview

1. Case
2. Regulation
3. Conclusions

# Case



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# SEC Charges Kim K for Touting a Security

- Order US Securities and Exchange Commission, 3 October 2022

## **Facts**

- Kim posts promotional message on her Instagram account
- The post ‘touts’ the security, but does not include the compensation

## **Enforcement**

- USD 1 000 000 penalty and USD 250 000 disgorgement plus interest
- Three years not posting similar messages and receiving compensation
- ‘Message to the market’ – Chair Gary Gensler, October 2022

**Did the SEC overreach by bringing this order?**

# Regulation



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# Regulating advertising in capital markets

1. Advertisements: persuasive communications designed to stimulate sales
2. Endorsement: saying that you approve something
3. Advertisements with celebrity endorsement more effective (d'Ambrogio 2022)
4. Some celebrities and companies design content to maximize effectiveness by providing incomplete or inaccurate information
5. Some products are subject to special rules to protect consumers (e.g. tobacco)
6. Some states expressly prohibit celebrity endorsements (e.g. online gambling, NL)

# Regulating advertising in capital markets (2)

1. Securities are such a special class of products with special advertising rules
2. In most jurisdictions, there are specific rules governing advertising or marketing communications for securities
3. Positive information obligations  
They must refer to a disclosure document with prescribed content on the securities (e.g. prospectus).
4. Negative information obligations  
They cannot include certain content, in particularly misleading information
5. Rationales? Market integrity and protection of investors

# Regulating advertising in capital markets (3)

1. Crypto-assets are also subject to regulation
2. Why? MiCAR recitals 4-5:
  1. If they are economically similar to securities, they must be regulated as such
  2. Even if they are not, risks exist (e.g. holders, market abuse, financial stability)
3. In the absence of specific legislation, national regulators applied securities law
4. Member States adopted national legislation → fragmentation, arbitrage
5. EU adopted MiCAR to fill regulatory gaps and harmonize regulation

# Application and analysis



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# Qualification

- For a regulation to apply, the observed asset must fit in the definition of the asset subject to the regulation

## US qualification

- *Security* ex the 1933 Act (species: investment contract), SEC v W.J. Howey Co.

## • EU qualification

- *Financial instrument* ex Directive 2014/65/EU (MiFID II) or a *crypto-asset* ex Regulation 2023/ 0 (MiCA)
- Hierarchy MiCAR and MiFID II
- MiFID II transposed in national law, local supervision

# Content requirements

- Regulation of advertisements may include positive or negative content requirements

## US requirements

- 1933 Act: full disclosure of receipt of consideration and amount thereof

## EU requirements

- Various applicable securities law frameworks (MAR, MiFID II)
- The paper also discusses consumer and e-commerce laws

# Advertising law is like a layered cake



## Layers of regulations

E-commerce (ECD)

Market abuse (MAR)

Business conduct rules (MiFID II, MiCAR)

Consumer protection (UCPD)

General contract law (Member State)

# Security content requirements

## Market abuse regulation (MAR)

- Regulates ‘investment recommendations’
- Material scope: instruments traded on EU ‘trading venue’, applied for admission, or price/value depends on traded instruments
- ‘investment recommendations’: information concerning investment strategy
- Personal scope: person who proposes a particular investment decision
- Applies to social media communications
- Qualification unclear (‘giving back?’)
- If so, Kim should disclose receipt of payment (‘interest’)

# Security content requirements (2)

## Markets in Financial Instruments Directive (MiFID II)

- A 'marketing communication' must be 'identifiable as such'
- Personal scope: investment firms and credit institutions
- Communications directed to clients (professional and retail)
- Concepts are not defined
- Kim is not formally investment firm, or regularly behaving as such

# Crypto-asset content requirements

## Markets in Crypto-Assets Regulation (MiCAR)

- A ‘marketing communication’ must be ‘identifiable as such’
- Additional content requirements apply (e.g. consistency with whitepaper)
- Crypto-assets: asset-referenced, electronic money and utility tokens
- Personal scope: any person communication
- Concepts are not defined
- ESMA guidelines on cross-border distribution of CIU: accentuated hashtag
- Kim would fall under it, did not use the hashtag

# Consumer law content requirements

## Unfair Commercial Practices Directive (UCPD)

- A communication by a ‘professional’ is a ‘commercial practice’ if directly connected with promotion of product,
- Communication cannot be ‘unfair’ (distort decision-making)
- Kim could be a professional or acting as an agent of a professional (CJEU case law)
- Communication could be a ‘misleading omission’, where commercial intention is not apparent from the context
- Receiving payment for the endorsement is a commercial element
- Not clear if national court would find misleading omission (diverging standards)

# E-commerce law content requirements

## E-commerce Directive (ED)

- ‘Commercial communication’ disseminated using an ‘information society service’ must be ‘clearly identifiable as such’
- Communication is aimed at promoting products of an undertaking
- Social media platforms are information society services
- Kim’s post would be covered by the rule
- No clear guidance on interpretation
- Suggestion: use ESMA’s interpretation

# Enforcement

- To effectively influence behavior, a regulation needs to be enforceable by the supervisory authority

## US and EU regulation

- SEC and national regulators of Member States have similar powers
- Powers:
  - Cease-and-desist orders
  - Disgorgement
  - Pecuniary penalties (fines)
- Overlapping across MAR and MiFID II, UCPD and ED less and lower fines

# Liability of third party servicers

- Third party servicers, such as investment firms, may become exposed to liability in case the rules are violated by the celebrity
- If the servicer is not involved in the production or dissemination of the communication, there is no liability *under EU rules* (national rules may differ)
- Specific actions
  - Reposting: liability under securities, crypto-asset and consumer laws
  - Mentioned: no liability
- Reputational risk beyond legal liability

# Conclusions



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# Conclusions

- The regulation of celebrity endorsements in the crypto-asset space depends on the qualification of the asset under EU crypto-assets and securities laws
- Regardless of the qualification, EU consumer and e-commerce laws apply
- The EU regulatory approach is less encompassing than the US regulatory approach and requires less disclosure (payment amount not required)
- Celebrities must heed both EU rules and national rules