To remain competitive, companies find themselves increasing their efforts to digitally transform their businesses by developing new offerings based on emerging technologies and integrating these technologies into existing product and service offerings.

This is our third monthly bulletin for 2021, aiming to help companies identify important and significant legal developments governing the use and acceptance of blockchain technology, smart contracts and digital assets.

While the use cases for blockchain technology are vast, from copyright protection to voting, most of the current adoption is in the financial services section and the focus of this bulletin will be primarily on the use of blockchain and or smart contracts in that sector. With respect to digital assets, we have organized our approach to this topic by discussing it in terms of traditional asset type or function (although the types and functions may overlap), that is, digital assets as:

- Securities
- Virtual currencies
- Commodities
Digital assets can themselves be assets or instead can reflect the ownership of an underlying asset. For example, electronic records that are the equivalents of negotiable instruments and electronic chattel paper would be digital assets, as would an electronic recording of a security interest in the underlying asset, such as recording title to real or personal property and the use of tokens to represent revenue streams from otherwise illiquid assets such as patents and commercial real estate (sometimes referred to as a “tokenized” or digitized asset).

In addition to reporting on the law and regulation governing blockchain, smart contracts and digital assets, this bulletin will discuss the legal developments supporting the infrastructure and ecosystems that enable the use and acceptance of these new technologies.

Each issue will feature in-depth insight on a timely and important current topic. In this issue, we (1) discuss the Wyoming bill on the status of decentralized autonomous organizations; and (2) review a court’s holding in a class action against a cryptocurrency exchange.

To build on our recent increasing recognition in the fintech and blockchain space, the DLA Piper IPT and Real Estate teams joined up to contribute to the inaugural edition of the *Chambers and Partners Blockchain Guide 2020*. Led by partner Scott Thiel and supported by Jonathan Gill and Kenny Tam, the team wrote the Hong Kong and China “Law and Practice” sections of the guide detailing the blockchain market and key legal and regulatory issues to note in each jurisdiction.

For related information regarding digital transformation, please see our monthly bulletin, *eSignature and ePayment News and Trends*.

**INSIGHTS**

**Court dismisses class action against cryptocurrency exchange – A review of the holding in Holsworth v. BProtocol Foundation**

By Michael Fluhr

The US District Court in the Southern District of New York has dismissed a class action lawsuit against BProtocol Foundation for an alleged unregistered offering of token securities. The suit was one of a number of similar class actions filed in April 2020 against cryptocurrency exchanges and issuers by law firms Roche Cyrulnik Freedman LLP and Selendy & Gay, PLLC. Read more.

**Wyoming takes a step ahead to clarify the legal status of decentralized autonomous organizations**

By Lin Pang and Guy E. Flynn

On March 17, 2021, Wyoming’s state senate passed a bill entitled Decentralized Autonomous Organizations Supplement, sponsored by Wyoming’s Select Committee on Blockchain, Financial Technology and Digital Innovation Technology. The bill was then introduced to the Wyoming House of Representatives and referred to its Minerals, Business and Economic Development Committee. If it becomes official law, Wyoming will be the first state in the United States to clarify the legal status of a decentralized autonomous organization. Read more.

**DEVELOPMENTS**

**FEDERAL DEVELOPMENTS**

**Virtual currency**

- **Federal Reserve staff report on pre-conditions for CBDC.** On February 24, staff members of the Federal Reserve Banks published Preconditions for a General-Purpose Central Bank Digital Currency, a report outlining...
requirements needed to support adoption and use of a “general-purpose” CBDC in the US for day-to-day payments. The report concludes that the following high-level preconditions would be required:

- clear policy objectives
- broad stakeholder support
- a strong legal framework
- robust technology and
- market readiness

**Securities**

- **SEC releases 2021 examination priorities.** On March 3, the Securities and Exchange Commission (SEC) Division of Examinations announced the release of its 2021 Examination Priorities, including priorities related to climate risks and digital assets. Examinations of market participants engaged with digital assets will continue to assess the following: whether investments are in the best interests of investors; portfolio management and trading practices; safety of client funds and assets; pricing and valuation; effectiveness of compliance programs and controls; and supervision of representatives’ outside business activities. For more information, see the DLA Piper alert SEC Division of Examinations announces 2021 exam priorities.

- **SEC publishes risk alert on digital asset securities.** On February 26, the SEC Division of Examinations published a Risk Alert, “The Division of Examinations’ Continued Focus on Digital Asset Securities.” The Risk Alert addresses assets that are issued and/or transferred using distributed ledger or blockchain technology (DLT); its observations about the process of examinations of investment advisers, broker-dealers, and transfer agents may assist firms in developing and enhancing their compliance practices.

**Taxation**

- **IRS clarifies cryptocurrency question on tax form.** In our November 2020 issue, we reported that, for the 2020 tax year, the IRS has prominently repositioned the cryptocurrency question for IRS Form 1040, but there remained some issues with the wording of the question. The IRS recently clarified that it will not require investors in cryptocurrency who simply bought “virtual currency with real currency” during the 2020 tax year to answer the question affirmatively or otherwise report that transaction on their 2020 tax returns. The clarification was delivered as an update to the IRS’s on the cryptocurrency FAQ page, and effectively exempts taxpayers who bought cryptocurrency with US dollars or other fiat currency from having to check “yes” on the cryptocurrency question on Form 1040. This exemption is quite narrow, however, as it does not apply to investors who swapped one cryptocurrency for another, sold their positions, or received a token airdrop.

- **IRS to cryptocurrency holders: “We see you.”** The IRS’s Office of Fraud Enforcement (OFE) has turned its eye toward investors in cryptocurrency. In a Federal Bar Association presentation in early March, Damon Rowe, OFE Director, announced “Operation Hidden Treasure,” under which a dedicated team of IRS criminal investigation professionals is focused on identifying taxpayers who have failed to disclose income from cryptocurrency. This group comprises agents specifically trained in cryptocurrency and virtual currency tracking, since identifying virtually anonymous cryptocurrency transactions has often been a challenge for the IRS and other taxing authorities. Specifically, these trained agents, together with specialist vendors, will focus on analyzing blockchain and de-anonymizing transactions, and will reportedly be training alongside the European Union Agency for Law Enforcement Cooperation (Europol) as part of the initiative. In addition, the IRS also noted that it was working on identifying “tax evasion signatures,” for example, structuring cryptocurrency transactions in increments of less than $10,000 to avoid reporting requirements. Finally, the OFE indicated that, as a result of Operation Hidden Treasure, it expected to see more referrals for criminal prosecution and assertions of the 75 percent civil fraud penalty.

**STATE DEVELOPMENTS**

**Virtual currency**

- **New Jersey commission reports on use of bitcoin ATMs.** On February 17, the New Jersey State Commission of Investigation announced the publication of Bitcoin ATMs: Scams, Suspicious Transactions and Questionable Practices at Cryptocurrency Kiosks. The report details findings of the Commission’s inquiry into
the operation of approximately 300 cryptocurrency kiosks in the state. The report noted that state government
has no specific authority over operation of the kiosks, and federal banking guidelines have not been enforced
for the investigated state operators. The Commission endorsed enactment of pending state legislation to
establish a licensing mechanism for digital asset business activities, including the kiosks, with revisions to
include a requirement for presentation of government-issued photo identification to use the kiosks, and an
expanded record retention period of six years.

• **New York AG issues virtual currency investing and registration alerts.** On March 1, the New York Attorney
General’s office announced the issuance of two alerts in response to the “extreme risk” posed to New Yorkers
investing in virtual or crypto currencies. The first alert – Investor Alert: Virtual Currency Risks – warns potential
investors that virtual currency may be subject to “speculative bubbles that produce wild market swings.” The
second alert – Industry Alert: Registration of Commodities Brokers-Dealers, Salespersons, and Investment
Advisors Doing Business Relating to Virtual or ‘Crypto’ Currency – reminds industry members that those dealing
in virtual currencies that are commodities or securities must register with the AG’s office.

• **New York DFS announces winners of techsprint.** On March 12, the New York Department of Financial
Services (NYDFS) announced the conclusion of its techsprint on digital regulatory reporting in cryptocurrency,
and announced the winners in each of three categories:
  o Greatest industry impact – CryptoKnight for risk scoring solutions
  o Most creative implementation – Crypto Avengers for prototype and design, and
  o Most functional prototype – Block-Busters for the most usable tech

**INDUSTRY DEVELOPMENTS**

• **Coinbase IPO registration statement published.** On February 25, the SEC published the Form S-1
Registration Statement of Coinbase Global, Inc. for its proposed initial public offering, including the offering
prospectus. Coinbase will be the first major US token trading platform to trade publicly on NASDAQ through a
direct listing. We reported the announcement of the offering in our December 2020 issue.

• **Bakkt awarded BitLicense in New York.** On March 11, the New York Department of Financial Services
(NYDFS) announced the approval of the application of Bakkt Marketplace, LLC for virtual currency and money
transmitter licenses. This grant expands the virtual currency services provided by Bakkt entities in the state.
See our August 2019 issue regarding the prior grant by NYDFS to Bakkt of a charter to provide virtual currency
custody services.

• **BitGo awarded New York Trust charter.** On March 4, BitGo, a major US cryptocurrency services company,
announced it obtained a New York Trust license to operate as a regulated qualified custodian under New York
State banking law. The NYDFS charter enables BitGo to provide custodial services for New York clients seeking
to secure digital assets.

**ENFORCEMENT ACTIONS**

**FEDERAL ENFORCEMENT ACTIONS**

**Securities**

• **SEC delists blockchain company.** In an order filed by the SEC on February 22, the SEC delisted shares of
Long Blockchain Corp. because it had failed to file an annual report since December 2017, and failed to file
quarterly reports since September 2018. Long Blockchain consented to entry of the order without admitting or
denying the SEC’s findings.

• **Co-founder of crypto company sentenced to eight years for ICO fraud.** On March 4, the US Attorney’s
Office for the Southern District of New York announced that Sohrab Sharma, AKA Sam Sharma, was sentenced
to eight years in prison for his role in a scheme to induce victims to invest more than $25 million worth of digital
funds in Centra Tech, Inc., a Miami-based company he co-founded which purported to offer cryptocurrency-
related financial products. Sharma previously pled guilty to conspiring to commit securities fraud, wire fraud,
and mail fraud in connection with his and his co-conspirators’ use of material misrepresentations and omissions
to solicit investors to purchase securities, in the form of digital tokens issued by Centra Tech, through fraudulent fundraising efforts that included an initial coin offering beginning in July 2017. For more information, see our August 2020 and July 2020 issues.

- **Cryptocurrency fraudster pleads guilty to securities fraud and money laundering.** On March 4, the Department of Justice (DOJ) announced that Roger Nils-Jonas Karlsson, a citizen of Sweden, pled guilty to securities fraud, wire fraud and money laundering, resulting from a scheme that defrauded more than 3,500 victims of more than $16 million. The criminal complaint was filed in March 2019 against Karlsson and his company Eastern Metal Securities. For more information on the case, see our December 2019 issue.

- **SEC files emergency enforcement action against Idaho man.** On March 5, the SEC filed a complaint against Shawn Cutting, his wife Janine Cutting, their firm Crypto Traders Management, LLC, and related entities for violations of the Securities and Exchange Act based on an alleged fraudulent Ponzi scheme which raised at least $6.9 million from over 450 investors. According to the complaint, Cutting falsely represented himself as an experienced financial advisor who would pool the investors’ money to trade digital assets for profit and Cutting used the money for personal expenses and to make Ponzi-like payments to other investors. Since February 2020, Cutting had ignored or denied investor requests to withdraw their funds. The SEC seeks an injunction and disgorgement of the invested funds.

**Commodities**

- **CFTC charges two individuals in multi-million pump-and-dump scheme.** On March 5, the Commodity Futures Trading Commission (CFTC) announced filing of a complaint in the US District Court for the Southern District of New York charging John McAfee and Jimmy Gale Watson for engaging in a digital asset “pump-and-dump” scheme. According to the complaint, the defendants secretly accumulated positions in digital assets, deceptively promoted the digital assets through social media as valuable long-term investments, then sold their holdings as prices rose sharply following McAfee’s deceptive endorsements, resulting in profits in excess of $2 million. The CFTC seeks restitution, disgorgement, civil monetary penalties, permanent trading and registration bans, and a permanent injunction.

In related actions, the US Attorney’s Office for the Southern District of New York announced the indictment of McAfee and Watson on charges based on the same scheme. Additionally, see our October 2020 issue for information related to the SEC’s charges against McAfee.

**Virtual currency**

- **North Korean military hackers indicted in cyberattacks and financial crimes.** On February 17, the DOJ announced the unsealing of a federal indictment against three North Korean computer programmers for participating in a wide-ranging criminal conspiracy to conduct a series of cyberattacks, to steal and extort more than $1.3 billion of money and cryptocurrency from financial institutions and other companies, to create and deploy malicious cryptocurrency applications and to develop and fraudulently market a blockchain platform. The US Attorney’s Office and FBI also obtained seizure warrants authorizing the FBI to seize from two cryptocurrency exchanges $1.9 million in cryptocurrency stolen by the North Korean hackers from a victim in the indictment.

**STATE ENFORCEMENT ACTIONS**

**Securities**

- **Texas regulator obtains emergency cease and desist order.** On March 15, the Texas State Securities Board (TSSB) announced it entered into an emergency cease and desist order targeting Delta Crypt Limited, an unregistered online cryptocurrency asset investment platform. Following an advisory from the Philippines Securities and Exchange Commission, Delta Crypt removed its website and began similar operations under the name Binanace Assets and Bit Kind LTD.

**SPOTLIGHT ON INTERNATIONAL DEVELOPMENTS**

- **European Central Bank seeks broader role over stablecoins.** On February 19, the European Central Bank
(ECB) issued an opinion on the EU’s proposal for a regulation on markets in cryptoassets and amending Directive (EU) 2019/1937. The opinion was issued at the request of the Council of the European Union and the European Parliament. The opinion includes a detailed review of each provision of the proposal text along with amendments proposed by the ECB to such text. Notably, the ECB asserts that “where an asset-reference arrangement is tantamount to a payment system or scheme, the assessment of the potential threat to the conduct of monetary policy, and to the smooth operation of payment systems, should fall within the exclusive competence of the ECB (or the national central bank of issue of the relevant Union currency).”

- **FATF updates guidance for virtual assets.** On February 25, the Financial Action Task Force (FATF) announced the results of its plenary meetings, including the release of additional Guidance on Risk-Based Supervision, and the release of updates to its existing guidance on virtual assets and virtual asset service providers (VASP) for public consultation. The updates will address how to apply FATF standards to stablecoins, implementation of the travel rule, and peer-to-peer transactions and will be published for consultation in March. Feedback from the consultation will inform the final guidance, which is expected in June 2021.

- **Hong Kong digital asset trading platform goes live.** On March 15, OSL Digital Securities Limited, a regulated crypto exchange, announced its official go-live to commence live trading. OSL holds Type-1 (securities trading) and Type-7 (digital assets trading) licenses from Hong Kong’s Securities and Futures Commission. The press release explains that the platform enables institutional and professional investors to buy, sell and securely store digital assets.

- **New Zealand dollar stablecoin launched.** On March 10, New Zealand registered financial service provider Techemynt announced the launch of the first New Zealand dollar stablecoin $NZDs. Each $NZD is backed 1:1 by the New Zealand dollar in a cash and cash-equivalent treasury, and $NZD was deployed on the Ethereum blockchain.

- **BitMEX publishes Travel Rule principles.** On February 9, BitMEX, a cryptocurrency exchange based in Seychelles, announced its publication of Travel Rule Data Storage Principles to address data storage in light of the FATF Travel Rule which goes into effect in June. The Principles were drafted by BitMEX IT security and compliance teams and are offered as a starting point for discussion by all stakeholders. The Principles, released as non-copyright open source, provide guiding principles for good data storage practices by virtual asset service providers (VASPs), focused on access management, security, information protection, logging and monitoring, incident management, and privacy.

- **Thailand securities regulator seeks feedback on qualifications of crypto investors.** On February 25, the Securities and Exchange Commission, Thailand (SEC-Thai) announced it seeks public comment on its proposed qualifications of cryptocurrency investors and the proposed requirement of a knowledge test to be conducted on investors by digital asset business operators before providing digital asset investment services. The SEC-Thai will hold a live talk on the SEC-Thai Facebook page on March 24. Comments may be submitted by March 27 through the SEC-Thai website or by email at ekarit@sec.or.th or chawin@sec.or.th.

**Trending**

Coronavirus: US federal and state governments work quickly to enable remote online notarization to meet global crisis

**In case you missed it**

Legal developments in categorising and tracing cryptoassets – DLA Piper FinBrief blog

Our analysis of the July 31, 2020, FCA policy statement PS19/22: Guidance on Cryptoassets, which sets out the FCAs final guidance on whether dealings involving cryptoassets require authorisation under FSMA.

**Read these next**

The latest issue of eSignature and ePayment News and Trends
The latest issue of our bulletin *Bank Regulatory News and Trends*

**Contacts**

Learn more about our Blockchain and Digital Assets practice by contacting any of our editors:

Margo H.K. Tank  
Mark Radcliffe  
Liz Caires  

**Contributors**

Martin Bartlam  
Mary Dunbar  
Tom Geraghty  
Claire Hall  
Jeff Hare  
Andrew Ledbetter  
Victoria Lee  
Deborah Meshulam  
Curtis Mo  
Scott Thiel  
David Whitaker  
Brian Cadoustau  
Benjamin Klein  
Andrew W. Grant  
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Richard Mar  
Alan Macek  
Lin Pang  
Guy E. Flynn  
Brooke Goodlett  
Adam Dubin  
Ryan Black  
Eric Belli-Bivar  
Tyson Gratton

**AUTHORS**

**Margo H. K. Tank**  
Partner  
Washington, DC | T: +1 202 799 4000  
margo.tank@dlapiper.com

**Mark F. Radcliffe**  
Partner  
Silicon Valley | T: +1 650 833 2000  
mark.radcliffe@dlapiper.com