This is our tenth 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, this bulletin will be primarily on the use of blockchain and or smart contracts in the financial services 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
- Deposits, accounts, intangibles
- Negotiable instruments
- Electronic chattel paper
- Digitized assets

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.

**INSIGHTS**

**Non-fungible tokens: What are the legal risks?**

By Katherine Roe, Chris Whittaker, Dan Jewell and Scott Thiel

The market for non-fungible tokens (NFTs) has boomed over the past year. Businesses and asset owners have been creating and selling NFTs representing a range of assets, whether digital or physical, including internet memes, digital images, event tickets and memorabilia.

Notable examples include the sale of an NFT representing the original source code for the World Wide Web, written by the Web’s inventor, Tim Berners-Lee, for USD5.4 million, and the first tweet of Twitter’s CEO, Jack Dorsey, for USD2.9 million.

This article sets out some of the key legal risks to be aware of for those thinking of investing in NFTs. Read more.

**FEDERAL DEVELOPMENTS**

**Taxation**

**Proposed infrastructure bill poses additional concerns for recipients of crypto.** We previously discussed the proposed bi-partisan infrastructure bill in our August and September 2021 issues, focusing on the wash sale and constructive sale rules and the new reporting requirements for cryptocurrency transactions. As discussed in a Research Report of the Proof of Stake Alliance, the bill also amends Section 6050I of the Internal Revenue Code. As amended, recipients of cryptocurrencies, NFTs, or other digital assets valued at more than $10,000 must disclose the personal information of the person or entity that delivered the assets to them, including providing social security numbers. Failure to disclose this information within 15 days constitutes a felony. The Report notes that compliance may be difficult in some cases as the assets may not be received from a person whose personally identifiable information can be verified or reported.

**Securities**

**SEC Chair speaks on crypto.** On September 14, Securities and Exchange Commission (SEC) Chair Gary Gensler testified before the US Senate Committee on Banking, Housing and Urban Affairs, stating, “Currently, we just don’t have enough investor protection in crypto finance, issuance, trading, or lending. Frankly, at this time, it’s more like the Wild West or the old world of ‘buyer beware’ that existed before the securities laws were enacted. The asset class is rife with fraud, scam, and abuse in certain applications.” Gensler asserted that the SEC is working with the CFTC on investor protection and with the Federal Reserve, Department of Treasury (DOT), Office of the Comptroller of the Currency and the members of the President’s Working Group in Financial Markets on broader policy frameworks.

Chair Gensler also gave the same testimony on October 5 before the US House of Representatives Committee on Financial Services.

**Senator seeks clarity from SEC Chair.** On September 24, US Senate Banking Committee Ranking Member Senator Pat Toomey (R-PA) issued a letter to SEC Chair Gensler requesting clarity on the SEC’s position regarding cryptocurrency. The letter raised concerns over the SEC’s regulation by enforcement approach to cryptocurrencies, and noted the SEC failed to “identify the securities involved or the rationale for their status as securities, which would have provided much-needed public regulatory clarity.” The letter provided a list of detailed questions seeking clarity on the SEC’s regulation of cryptocurrencies.

**SEC approves Volt Equity’s ETF.** The SEC has approved the exchange traded fund (ETF) of Volt Equity. According to a prospectus filed on October 1, the Volt Crypto Industry Revolution and Tech ETF will track the performance of “Bitcoin Industry Revolution Companies” – publicly traded companies that hold a majority of their net assets in bitcoin or make a majority of their revenue from bitcoin-related activities such as mining. At least 80% percent of the ETF’s net assets will be invested in crypto stocks, and 20 percent will be invested in more traditional stocks to offset risk. The ETF will not hold any cryptocurrencies directly.
SEC delays decision on bitcoin ETFs. On September 29, the SEC announced an extension of its decision on four other bitcoin ETFs – Global X, WisdomTree, Kryptoin and Valkyrie. The new deadline dates for each ETF approval are November 21 for Global X, December 8 for Valkyrie, December 11 for WisdomTree and December 24 for Kryptoin. For more information on pending bitcoin ETFs, see our June, May and April 2021 issues.

BlockFi files for futures ETF. On October 8, BlockFi filed for a bitcoin futures ETF known as “BlockFi Bitcoin Strategy ETF” which would invest in futures contracts traded on the Chicago Mercantile Exchange.

Virtual currency

DOT Financial Stability Oversight Counsel upcoming meeting agenda. The US Department of the Treasury (DOT) Financial Stability Oversight Council (FSOC) recently released the preliminary agenda for the upcoming FSOC meeting to be held on October 18. The agenda will include an open session on climate-related financial risk and a closed, executive session including an update on the FSOC’s 2021 annual report and an update on the report on stablecoins being developed by the President’s Working group on Financial Markets.

Senator raises concerns over forthcoming stablecoin report. On October 8, US Senate Banking Committee Ranking Member Senator Pat Toomey (R-PA) issued a letter to Treasury Secretary Janet Yellen raising concerns over the process and the reported contents of the President’s Working Group on Financial Market’s (PWG) forthcoming report on stablecoins. Senator Toomey asserted that questions about whether and how to regulate crypto and stablecoins should begin with Congress and noted that the process used by the PWG has lacked transparency and adequate engagement with relevant stakeholders. The letter further describes a listing of issues Senator Toomey believes the administration should address in its report. For more information on the PWG pending report on stablecoins, see our August 2021 issue.

OFAC list adds first virtual currency exchange. On September 21, the DOT announced the designation of SUEX OTC, SRO, a Russia-based virtual currency exchange, on the DOT Office of Foreign Assets Control (OFAC) List of Specially Designated Nationals for its part in facilitating financial transactions for ransomware actors. OFAC asserts that over 40 percent of SUEX’s known transaction history is associated with illicit actors and enabled laundering of cyber ransoms. OFAC also released an Updated Advisory on Potential Sanctions Risks for Facilitating Ransomware Payments stating the US government’s policy to strongly discourage the payment of cyber ransom or extortion demands and providing steps companies can take to mitigate such risks.

OFAC presents guidance on sanctions compliance for virtual currency. On October 15, the DOT announced that OFAC issued Sanctions Compliance Guidance for the Virtual Currency Industry intended to help the industry prevent exploitation by sanctioned persons and other illicit actors. The guidance outlines sanctions compliance best practices and underscores the need for a collaborative approach to counter ransomware attacks, including public-private partnerships and close relationships with international partners.


DOJ announces crypto enforcement team. On October 6, the US Department of Justice (DOJ) announced the creation of a National Cryptocurrency Enforcement Team (NCET) to tackle complex investigations and prosecutions of criminal misuses of cryptocurrency, particularly crimes committed by virtual currency exchanges, mixing and tumbling services, and money laundering infrastructure actors. NCET will also assist in tracing and recovery of assets lost to fraud and extortion, including cryptocurrency payments to ransomware groups. NCET will combine the expertise of the DOJ Criminal Division’s Money Laundering and Asset Recovery Section (MLARS), Computer Crime and Intellectual Property Section (CCIPS) and other sections in the division.

On the same day, the DOJ announced the launch of its new Civil Cyber-Fraud Initiative “to combat new and emerging cyber threats to the security of sensitive information and critical systems.”

Senators and Representatives urge administration to address ransomware. On October 8, a group of Congressional Democrats issued letters to the DOJ, DOT, Department of State and Department of Homeland Security urging the agencies to “pursue all options available” to protect American communities and infrastructure from ransomware. According to the letters, “To address the growing threat of ransomware attacks, US agencies must pursue a
A comprehensive enforcement approach involving both domestic and international partners.

Federal Reserve Chair discusses crypto. On September 28, Federal Reserve Chair Jerome Powell testified before the House Financial Services Committee on Thursday. In response to a question about China’s ban on cryptocurrency and the potential for similar action in the US, Chair Powell responded that there was “no intention [for the US] to ban them.” He also added that stablecoins “are like money-market funds, they’re like bank deposits, but they’re to some extent outside the regulatory perimeter and it’s appropriate that they be regulated.”

Commodities

Coinbase applies to NFA. On September 15, Coinbase Financial Markets Inc. applied to the National Futures Association to become a member and a registered Futures Commission Merchant. According to the Coinbase Twitter feed, “This is the next step to broaden our offerings and offer futures and derivatives trading on our platforms.” If Coinbase becomes registered as an FCM, it must then register with the CFTC before listing crypto futures or derivatives products.

INDUSTRY DEVELOPMENTS

HSBC executes blockchain trade transaction. On October 4, HSBC announced that it successfully executed a blockchain enabled live trade finance transaction between ArcelorMittal Nippon Steel India Limited and Universal Tube & Plastic Industries Ltd. According to the press release, “With AM/NS India as the seller of steel goods to Universal Tube & Plastic Industries, UAE, the end-to-end paperless transaction was executed over [a] platform… which has been built on blockchain technology [and] facilitates comprehensive digitisation of the end-to-end ‘Letter of Credit’ (LC) transaction, including the e-presentation of trade documents....” “The success of this transaction reinforces the commercial and operational viability of blockchain as an alternative to conventional exchanges for paper-based documentation.”

ENFORCEMENT ACTIONS AND LITIGATION

FEDERAL

Blockchain

US citizen pleads guilty to conspiring to enable North Korea to evade sanctions. On September 27, the Department of Justice (DOJ) announced that Virgil Griffith pled guilty to conspiring to violate the International Emergency Economic Powers Act by providing services to the Democratic People’s Republic of Korea, including technical advice on using cryptocurrency and blockchain technology, to evade sanctions. According to the announcement, after the Department of State denied Griffith permission to travel to North Korea, Griffith flew to North Korea and delivered presentations at the Pyongyang Blockchain and Cryptocurrency Conference. His talks included instruction on how North Korea could use blockchain and cryptocurrency technology to launder money and evade sanctions and how blockchain technology "smart contracts" could be used in nuclear weapons negotiations with the US.

Griffith is scheduled to be sentenced in January 2022 and faces a maximum prison term of 20 years.

Virtual currency

Class action against Tether and others survives dismissal. On September 28, The US District Court Southern District of New York issued an opinion and order in the putative class action lawsuit against Tether Limited (and affiliated entities), Bitfinex, Bittrex and Poloniex (and some individuals). The order declined to dismiss most of the plaintiffs’ claims which allege that the defendants conspired to manipulate the cryptocurrency market using USDT, a stablecoin controlled by the defendants and allegedly fraudulently issued. The surviving claims include those under the Sherman Act (antitrust), the Commodity Exchange Act (CEA), and common law fraud.

Securities

Coinbase receives Wells notice from SEC. On September 7, Coinbase’s Chief Legal Officer explained in a blog post that it received a Wells notice from the SEC on September 1 stating the SEC’s intent to sue Coinbase regarding its Coinbase Lend program, a cryptocurrency lending service. Coinbase stated it is surprised by the notice because it had been "proactively engaging with the SEC about Lend for nearly six months." Lend would allow eligible customers to earn interest on select assets on Coinbase. Coinbase’s position is that the Lend program is "not an investment contract or a..."
note," and Coinbase asserts that the SEC has not provided their reasoning supporting the SEC's position that Lend is an unregulated security. The SEC has only disclosed that it assesses Lend under the standards established in the Howey and Reves cases. These standards can consider as loans redeemable on demand to be securities, for reasons including an unclear redemption date. "Coinbase continues to welcome additional regulatory clarity; mystery and ambiguity only serve to unnecessarily stifle new products that customers want and that Coinbase and others can safely deliver." As a result, Coinbase states that it will not be launching Lend until later this year.

Circle discloses investigative subpoena. On October 4, Circle Financial made a regulatory filing which disclosed that Circle received an investigative subpoena from the SEC in July. The filing states that, "[I]n July 2021, we received an investigative subpoena from the SEC Enforcement Division requesting documents and information regarding certain of our holdings, customer programs, and operations. We are cooperating fully with their investigation."

Commodities

CFTC settles with Kraken. On September 28, the Commodity Futures Trading Commission (CFTC) announced it issued an order filing and settling charges against Payward Ventures, Inc. dba Kraken for illegally offering margined retail commodity transactions in digital assets, including bitcoin, and failing to register as a futures commission merchant (FCM). The order found that Kraken, a US digital asset exchange, offered margined retail commodity transactions in digital assets to US customers who were not eligible contract participants, and the transactions did not take place on a designated contract market (DCM). Additionally, by soliciting and accepting orders for and entering into retail commodity transactions with customers and accepting money or property (or extending credit in lieu thereof) to margin these transactions, Kraken illegally operated as an unregistered FCM. Without admitting or denying the findings of the order, Kraken agreed to pay a $1.25 million civil monetary penalty and to cease and desist from further violations of the Commodity Exchange Act.

Commissioner Dawn Stump released a concurring statement to the Kraken settlement order, asserting that "it is incumbent upon the Commission to undertake a rulemaking proceeding to supersede the [2020 Final Interpretive] Guidance [on retail commodity transactions involving certain digital assets] by adopting binding and enforceable rules that will provide certainty to the marketplace and a shared understanding of the "rules of the road." Commissioner Stump further questioned the CFTC's finding that Kraken operated as an unregistered FCM with respect to the retail commodity transactions prohibited unless traded on or subject to the rules of a DCM, stating, "Absent these transactions occurring on a DCM, they would continue to be illegal even if Kraken had an FCM registration. Furthermore, how Kraken would be regulated as an FCM is not entirely clear, because many of the Commission's rules governing its regulation of traditional FCMs do not fit Kraken's role as an exchange."

CFTC charges 12 entities for failing to register as FCMs for crypto transactions. On September 29, the CFTC announced that it filed charges against 12 entities for failing to register as futures commission merchants (FCMs) while acting as FCMs by offering to the general public the opportunity to purchase binary options based off the value of cryptocurrencies including bitcoin, and encouraging customers to transfer money or assets to them. The entities are: Tradingforexpay, Cryptofxtrader, Bitxfprofit, Globalnationfx, BinanceFxTrade, MaxForexOption, ProCryptoMiners, ProFX-Capitals, Smarter Signals, Prime Expert Trade, Star Fx Pro, and Excotradeoptions.

CFTC files complaint against Prime FX. On September 30, the CFTC announced the filing of a civil enforcement action in the US District Court for the District of Massachusetts against 8 individuals tied to the operation of the website Primefx.org in a scheme to fraudulently solicit and misappropriate over $1.2 million from US and international customers for purported trading in foreign currency and bitcoin. The FTC seeks restitution, disgorgement, civil monetary penalties, trading and registration bans, and injunctions against further violations.

STATE

Securities

State regulators charge Celsius Network. Over the prior month, securities regulators from the states of states of Texas, New Jersey, Alabama and Kentucky each took actions against Celsius Network, a Delaware-based cryptocurrency trading, lending and borrowing platform, alleging that Celsius's "Earn Rewards" program constitutes securities in the form of investment contracts in exchange for the deposit of assets with the company. The investment contracts allow passive investors to earn profit in the form of interest on the assets deposited with Celsius, allegedly in violation of state securities laws. Kentucky and New Jersey issued cease and desist orders against Celsius. Alabama issued an order to show cause,
and Texas a Notice of Hearing, compelling Celsius to respond or a cease-and-desist order will be entered.

**Blockchain**

**Texas appoints members to blockchain work group.** On September 30, the governor of Texas announced the appointment of four persons to the Work Group on Blockchain Matters formed under HB1576, which bill became effective September 1. The work group will develop a master plan for the expansion of the blockchain industry in Texas and recommend policies and state investments in connection with blockchain technology. The work group must submit its report no later than October 31, 2022. For more information on HB 1576, see our July 2021 issue.

**SPOTLIGHT ON INTERNATIONAL DEVELOPMENTS**

**BIS and central banks publish CBDC guidance.** On September 30, the Bank for International Settlements (BIS) joined seven central banks to issue a series of reports which explore how central bank digital currencies (CBDCs) may meet users’ future needs through cooperation between public and private institutions to “ensure integration with existing payments systems; to anticipate customers’ future needs; and to support innovation while preserving public trust, privacy and stability in the broader financial system.”

**BIS announces consultation guidance on stablecoins.** On October 6, the BIS Committee on Payments and Market Infrastructures and the International Organization of Securities Commissions announced publication of a public consultation entitled Application of the Principles for Financial Market Infrastructures to Stablecoin Arrangements that confirms and clarifies that stablecoin arrangements should observe international standards for payment, clearing and settlement systems.

**IMF publishes global financial stability report.** On October 1, the International Monetary Fund (IMF) announced the publication of a Global Financial Stability Report which “describes the risks posed by the crypto ecosystem and offers some policy options.” According to the announcement, “The total market value of all the crypto assets surpassed $2 trillion as of September 2021—a 10-fold increase since early 2020.”

**FSB publishes progress report on implementation of FSB recommendations.** On October 7, the Financial Stability Board (FSB) announced the publication of Regulation, Supervision and Oversight of “Global Stablecoin” Arrangements: Progress Report on the implementation of the FSB High-Level Recommendations. In the report, “fostering the soundness of ‘global stablecoins’ is Building Block 18 of the FSB roadmap to enhance cross-border payments.” This report:

- discusses key market and regulatory developments since the publication of the FSB high-level recommendations in October 2020
- takes stock of the implementation of the FSB high-level recommendations across jurisdictions
- describes the status of the review of the existing standard-setting body (SSB) frameworks, standards, guidelines and principles in light of the FSB high-level recommendations and
- identifies areas for consideration for potential further international work.

**China moves against virtual currencies.** The Chinese government has been ramping up its efforts to stamp out cryptocurrency businesses over the past year via a mixture of announcements, policies and enforcement actions. An example of this is the ongoing crackdown against cryptocurrency-mining activities in the PRC. In September 2021, the People’s Bank of China published the Notice on Further Preventing and Handling of Speculation Risk in Virtual Currency Trading (PBOC Notice), which sets out wide-ranging restrictions against various cryptocurrency-related services and activities, including offering cryptocurrency exchange services to PRC nationals, issuing tokens for fundraising purposes, and providing technological or marketing support to businesses engaging in activities prohibited by the PBOC Notice. While the PBOC Notice expressly refers to bitcoin, ether and tether as “virtual currencies” that cannot be used as legal tender in China, it does not provide a general definition for “virtual currencies.” In our view, it remains to be seen whether asset-backed tokens or security tokens would receive the same regulatory treatment. In effect, the PBOC Notice emphasizes the Chinese government’s regulatory posture on cryptocurrencies and related business activities by imposing a blanket ban against cryptocurrency-related activities in China. Unlike previous similar announcements on cryptocurrency regulations made by the Chinese government or regulators, the PBOC Notice was jointly issued by ten government bureaus, including law enforcement agencies and judicial authorities – this may suggest a more forceful approach by the Chinese government against the cryptocurrency industry going forward. It is likely that PRC authorities will start taking enforcement action against various actors in the cryptocurrency industry in the coming months, which
would lead to further clarity about enforcement risk and activities which may be most susceptible to regulatory scrutiny.

**French regulator warns against ICO.** On September 30, the Autorité des Marchés (AMF), France’s stock market regulator, issued a public warning about the risk of fraud associated with the initial coin offering (ICO) prepared by the company Air Next. Air Next sought a visa from the AMF for its proposed ICO, but the AMF suspected that some of the documents submitted by Air Next were forgeries and did not grant the visa. The AMF urges potential investors to be vigilant regarding Air Next solicitations for the ICO and to refrain from passing on such solicitations to third parties.

**New Zealand reserve bank issues consultations on CBDCs.** On September 30, the Reserve Bank of New Zealand announced the issuance of Future of Money – Stewardship and Future of Money – Central Bank Digital Currency which seek public input regarding how the bank “should perform our role as steward of money and cash, and how we should assess the case for central bank money in a digital form alongside cash.” Comments must be submitted by December 6.

**Peru launches its first stablecoin.** On September 25, Latin American digital token issuer ANCLAP announced the launch of Peru's first stablecoin, sol Digital (PEN). PEN is backed by Peru’s currency, the sol, and available on the Stellar blockchain.

**Swiss regulator approves digital asset stock exchange and depository.** On September 10, the Swiss Financial Market Supervisory Authority (FINMA) announced its “first-ever approval for a stock exchange and a central securities depository for the trading of tokens.” FINMA authorized SIZ Digital Exchange AG to act as a central securities depository and approved the associate company SDX Trading AG to act as a stock exchange. SIX Digital Exchange also announced the achievement, stating that it was approved “to go live with a fully regulated, integrated trading, settlement, and custody infrastructure based on distributed ledger technology for digital securities.”

**Swiss regulator approves crypto fund.** On September 29, Switzerland’s FINMA announced the approval of the Crypto Market Index Funds, the first Swiss fund that will invest primarily in crypto assets. The fund is restricted to qualified investors.

**Bank of England announces membership of CBDC forums.** On September 29, the Bank of England and HM Treasury announced the memberships of the SBDC Engagement and Technology Forums. The Engagement Forum consists of senior stakeholders from industry, civil society and academia to gather strategic input on policy considerations and functional requirements pertaining to CBDC. It will have an important role in helping the Bank and HM Treasury understand the practical challenges of designing, implementing and operating a CBDC. The Technology Forum engages stakeholders and gathers input on all technology aspects of CBDC from a diverse cross-section of expertise and perspectives and will help the Bank to understand the technological challenges of designing, implementing and operating a CBDC.

**Read this next**

Embracing digital evolution: Our new business report

**Trending**

DLA Piper attorneys Michael Malloy, Ilya Bulgakov, Alexei Kolesnikov and Alexander Klochkov have contributed a chapter on Russia: Law and Practice to the Chambers Blockchain 2021 Global Practice Guide, published in summer 2021. The guide provides the latest legal information on decentralised finance; updates to tax systems to consider blockchain and cryptocurrencies; non-fungible tokens; initial coin offerings; smart contracts; data privacy and protection; and mining and staking.

Listen to our podcast, Episode 1: Non-fungible tokens and their potential application in the financial services sector, featuring DLA Piper partner Anthony Lloyd and Macgregor Duncan, who is the General Manager - Corporate & Business Development of Westpac and CEO of Westpac's new digital bank

Listen to excerpts from the NACD Northern California Chapter's program on How the Future of Blockchain will Impact the Boardroom Level Set, featuring DLA Piper partner Mark Radcliffe

You may also enjoy our podcast, FinTech: Cashless societies and post-pandemic growth, featuring DLA Piper partner Bryony Widdup and Tom Hambrett, Group General Counsel and Company Secretary of Revolut
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Blockchain is spreading its chains

Whatever your sector, ransomware attacks are changing how to think about platform security risk: Action steps

Non-fungible tokens Q&A

Overview and primer — Financial entities and Canada’s anti-money laundering and anti-terrorist financing regime

Cybersecurity considerations for executives and boards of directors: How recent cyberattack trends and developments inform strategies for reducing cyber-risk

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The latest issue of eSignature and ePayment News and Trends

The latest issue of our bulletin Bank Regulatory News and Trends

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