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Blockchain Bites: Crypto crime concentrated in 270 connected wallets, New technology not immune to the same old scams, Ether ETF debuts in Canada, Mastercard, Visa and Bahama's CBDCv

Michael Bacina, Barbara Vrettos and Jade McGlynn of the Piper Alderman Blockchain Group bring you the latest legal, regulatory and project updates in Blockchain and Digital Law.

Crypto crime concentrated in 270 connected wallets

Reading articles on digital currency in the business press, you would be forgiven for thinking that digital currency is just used by criminals and money launderers. This (regretfully widespread) narrative is increasingly crumbling in the face of facts. The way public blockchains work, however, provide a good basis to publicly track and identify dirty money, something which is not possible with traditional cash or payments.

The recent Chainalysis 2021 Crypto Crime Report covers off just this kind of information, reporting, that despite digital currency use soaring:

> Cryptocurrency-related crime is falling, it remains a small part of the overall cryptocurrency economy, and it is comparatively smaller to the amount of illicit funds involved in traditional finance.

A surprising finding in the current report concerns just how few addresses are involved in the majority of money laundering, specifically only:

> 270 service deposit addresses drive 55% of money laundering in cryptocurrency

A deeper look into these wallets leads Chainalysis to consider that the wallets have very significant legitimate activity. Often, the volume of *legitimate* digital currency received by these illicit addresses is 90% of the total volume of digital currencies in those wallets. That is only 10% of the volume of payments is dirty money.

This suggests that these addresses are in fact legitimate businesses which may have AML/CTF or other compliance failures which place them at risk of money laundering. If the operators of these addresses engage in robust AML/CTF monitoring and enforcement, it may be that a key part of the already small money laundering which goes on in digital currency can be further crimped.

Uncovering and stopping the sources of illicit funds connected to crime is important for any payments system, and the increasing sophistication of law enforcement agencies in understanding digital currency and moving to stop crime and laundering in the space is both welcome and important for the ongoing development and adoption of this technology.

New technology not immune to the same old scams

Australian citizen Stefan Qui, aged just 24, has pleaded guilty in the USA to cheating 100 investors out of USD$90M invested into his hedge fund, Virgil Capital, following an investigation and prosecution by US Securities and Exchanges

Commission (**SEC**).

Since 2017, the self-proclaimed math prodigy had claimed to have devised an algorithm that monitored the digital currency market to take advantage of price fluctuations – 'Profiting off bitcoin's wild swings' asserting that the fund was 'not exposed to the ups and downs of the cryptocurrency market'.

Just over a year into the advent of Virgil Capital, Quin was already boasting the fund was generating 500% returns in 2017, '*a claim that produced a flurry of new money from investors*.'

Bloomberg reported that:

> [Quin] became so flush with cash, [he] signed a lease in September 2019 for a $23,000-a-month apartment in 50 West, a 64-story luxury condo building in the financial district with expansive views of lower Manhattan as well as a pool, sauna, steam room, hot tub and golf simulator.

However, upset investors began to make complaints about missing assets and incomplete transfers. New York lawyer Audrey Strauss explained:

> Stefan He Qin drained almost all of the assets from the $90 million cryptocurrency fund he owned, stealing investors' money, spending it on indulgences and speculative personal investments, and lying to investors about the performance of the fund and what he had done with their money.

To meet the redemption demands of the increasingly upset investors in the former fund, Qin turned his attention to another fund he controlled, the VQR fund. But to Quin's dismay, his attempt to withdraw $1.7 million dollars from the fund aroused the suspicions of VQR's head trader, Antonio Hallak who refused to accept Quins claims that the money was destined for "*Chinese loan shark*" that "*might do anything to collect a debt*". To surpass Hallak, Quin tried to take over the VQR fund, but by this point it was too late for Quin; the Securities and Exchange Commission was already on the case and within a week had filed a lawsuit against Quin for fraud. Quin returned to the USA and turned himself in to authorities, and expressed his guilt.

Even in the most regulated areas Ponzi schemes can occur. Importantly this is not a reflection of the digital asset industry more broadly, just a demonstration that old tricks can permeate new technologies.

Ether ETF debuts in Canada

Canada's largest digital asset investment manager 3iQ launched the world's first Ether-based Exchange Traded Fund (ETF) on the Toronto Stock Exchange.

Although a delay in closing the funds' IPO prospectus made keen traders begrudgingly wait two hours after the market opened to start trading, an impressive 345,331 shares were traded across the day. In terms of performance, the fund opened for trading at $10.80 a share, progressing to reach $11.48 at its highest, with a closing price of $11.02. In layman terms this represents an overall gain of 2.5% and a solid start in the market for the fund.

This is not 3iQ's first attempt at making digital assets more accessible to investors. Last year April, the company launched its Bitcoin Fund which crossed the $100 million market cap threshold, by October 2020. Considering the significant growth in these shares indicates the recognisable demand for digital asset ETF's, it is no surprise that 3iQ has developed yet another way to give exposure to digital assets to investors.

Cointelegraph explains:

> The fund was launched by Canada's biggest digital asset investment manager 3iQ, as a way for traders and investors to gain exposure to the Ethereum market without having to purchase, store or sell ETH themselves. At an average price of $565 per ETH, each share of QETH.U represented roughly 0.0187 ETH at the beginning of the trading day. The coins backing the fund's shares are being held by Gemini Custody, the custodial arm of crypto exchange giant Gemini.

The movement by international markets to accept financial products backed by digital assets is a call to action for Australian markets and regulators to understand how these products could be offered to Australian investors.

Mastercard, Visa and Bahama's CBDC

Digital currencies are entering to the Mastercard network and will soon be available globally to card holders. Mastercard recently announced their support of digital currencies, quickly following Visa's move to recognise the value of digital currencies in payments. These two announcements bring the two biggest payment providers closer to digital currency integration in the daily lives of millions.

Mastercard's justification is customer centric: it's about offering users more choice. Raj Dhamodharan, Executive Vice President, Digital Asset & Blockchain Products & Partnerships said:

> We are here to enable customers, merchants and businesses to move digital value — traditional or crypto — however they want. It should be your choice, it's your money.

Mastercard has collaborated with Wirex and Bitpay previously to create 'crypto cards' so that individuals could transact using their digital currencies. However, these cards did not allow digital currencies to move through the Mastercard network, companies would convert the digital currencies into fiat currencies which funds then moved through the Mastercard network. Now, Mastercard proposes to support digital currencies directly within their network.

The announcement also lends key support to central bank digital currencies with a collaboration between Mastercard and Island Pay to launch "the world's first central bank digital currency linked card". The Central Bank of the Bahamas was an early mover in issuing their central bank digital currency which has also claimed to be the world's first retail CBDC. Users will be able to instantly convert their non-CBDC digital currency to a stable "Sand Dollar" (A Bahamian dollar) to pay for goods and services through the Mastercard network, being any of the 700(!) islands which make up the Bahamas, and critically also in the global Mastercard network.

As digital currencies enter payment provider's networks the ease of customer adoption will only increase. This is a particularly crucial use case to follow, given Mastercard intends to allow payments using the Sand Dollar outside of the Bahamas itself.

There is a very real prospect that a CBDC which gains enough adoption globally could start to become a de facto standard, particularly in countries where there are concerns around the reliability of the local reserve currency, such as islands using US dollars.

This will also likely place pressure on other countries to investigate and move towards developing their own CBDCs not just as an innovative step to improve payments, but to protect their own monetary sovereignty.

As always, convenience is king, and citizens of a country may have no qualms using a foreign currency CBDC as part of their daily lives if it is convenient and more reliable in value than a local currency.