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Blockchain Bites: HK "re-banks" crypto, Bank of China issues tokenised notes, SEC still considering Coinbase's rulemaking petition, A dookie of a decision for Ooki DAO, Further Mt Gox related charges

Michael Bacina, Steven Pettigrove, Jake Huang, Luke Misthos, Luke Higgins and Kelly Kim of the Piper Alderman Blockchain Group bring you the latest legal, regulatory and project updates in Blockchain and Digital Law.

HK moves to "re-bank" crypto, as Bank of China issues tokenised notes

As Hong Kong rolls out its new licensing regime for crypto-trading platforms, the city's central bank, the Hong Kong Monetary Authority, is reportedly encouraging major banks in Hong Kong to bank crypto exchanges.

A spokesman for the HKMA stated that banks:

> *should endeavor to meet the legitimate business need of licensed [Virtual Asset Service Providers] ... and provide the required banking services*

According to the Financial Times, in April, the HKMA sent a letter encouraging banks not to "create undue burden" for exchanges looking to set-up in Hong Kong and has held private discussions with HSBC, Standard Chartered and Bank of China on banking services for crypto platforms.

Meanwhile, the investment banking arm of the Bank of China, BOCI, has issued tokenised notes on the Ethereum blockchain in Hong Kong.

In collaboration with UBS, a Swiss banking giant, BOCI offered CNH200 million (approximately AUD$40 million) worth of structured notes to clients in the Asia Pacific region. This marks the first instance of a Chinese financial institution issuing tokenised securities on a public blockchain in Hong Kong.

The adoption of blockchain technology for tokenising financial and real-world assets has garnered attention from major banks such as Citigroup and Bank of America, who believe it can drive widespread cryptocurrency adoption and bring trillions of dollars of value on chain. Citi has dubbed tokenisation blockchain's 'killer use case'.

Both developments highlight Hong Kong's continued ambition to become a key crypto hub, particularly as regulatory pressure on the industry intensifies in the United States. In response to the U.S. Securities and Exchange Commission's recent lawsuit against Coinbase, Hong Kong legislator Johnny Ng extended an invitation to digital asset trading platforms, including Coinbase, to establish a presence in the city. The recent media release also highlighted BOCI's deputy chief executive Ying Wang's enthusiasm about Hong Kong's digital economy and the innovative development of its financial industry.

Following several notable legislative, regulatory, and judicial developments, Hong Kong looks set to resume its position as Asia's leading hub for digital assets innovation.

Last week the U.S. Securities and Exchange Commission (SEC) filed two high-profile complaints against Binance and Coinbase, triggering heated debate over the SEC's "regulation by enforcement" approach to crypto-asset offerings.

SEC says its still considering Coinbase's rulemaking petition

In a curious twist, the SEC's lawsuit against Coinbase provoked the U.S. Court of Appeals for the Third Circuit to make a rare decision ordering the SEC to urgently respond to Coinbase's petition (called a Writ of Mandamus) requesting the SEC to exercise its rule making powers to establish a clear regulatory regime for crypto-assets.

Among other things, the Third Circuit Court ordered the SEC to explain:

1. whether the SEC has now decided to deny (i.e. by filing the complaint last week) Coinbase's petition for rulemaking; and
2. if not, how much additional time the SEC requires to decide whether to grant or deny the petition.

In a 13 June letter submitted to the Third Circuit Court, the SEC responded that it needs an additional 120 days to reply to Coinbase's petition.

In the letter, the SEC said it

> *has not decided what action to take on that petition in whole or in part*

and expressly left open the possibility that it may exercise its discretion to establish specific rules in relation to digital assets.

> *[T]hat the Commission has now brought an enforcement action against Coinbase itself in no way indicates that the Commission has decided to deny Coinbase's rulemaking petition. There is no inconsistency between the Commission's allegations that Coinbase has violated long-existing regulatory standards and the Commission's consideration of whether the current regime should be augmented or modified*

While the regulator said the Writ of Mandamus petition for rulemaking "should be denied", the SEC indicated that it expected to make a recommendation on the petition within the 120-day timeline.

In response to the SEC's letter, Coinbase's Chief Legal Officer Paul Grewal said on Twitter that the SEC

> *repeat the fallacy that they haven't made any decision on new crypto rules*

Grewal tweeted as follow:

Coinbase has long sought regulatory clarity from the SEC but to no avail. In recent times, the SEC has shifted increasingly to a position that "the rules have always been clear" for crypto-assets. This stands in stark contrast to several jurisdictions around the world, including the EU, Singapore and Hong Kong, which are working on tailored regulations for crypto-assets.

A dookie of a decision for Ooki DAO

The United States Commodity Futures Trading Commission (**CFTC**) has secured default judgment against Ooki DAO, a decentralised autonomous organisation (**DAO**). The order requires that Ooki DAO pay a civil monetary penalty of USD$643,542, cease all operations, and is permanently banned from engaging in regulated behaviour. The decision is being held up as a landmark decision in the US (the CFTC has called it a "sweeping victory") as the Court had to consider amicus curie briefs submitted by leading minds in the crypto industry which argued against the imposition of legal liability on tokenholders as a form of unincorporated association.

The CTFC initiated the lawsuit in September 2022, concurrently with an administrative order against Ooki DAO's predecessor, bZeroX, and its founders. The CFTC's argument was built around whether a DAO and its governance token holders could be held liable for the actions of other individuals within the organisation.

The judgment refers Tom Bean and Kyle Kistner, the founders bZeroX LLC transfering control of the bZeoX software protocol to the bZx DAO, which was later renamed Ooki DAO, deliberately to seek to escape the CFTC's jurisdiction.

The CFTC alleged:

the bZx Founders believed that transition to a DAO would insulate the bZx Protocol form regulatory oversight and accountability for compliance with U.S law

Ooki DAO was accused of unlawfully offering leveraged and margined retail commodity transactions outside of operating as a registered exchange, it was also charged with failing to comply with obligations under the US *Bank Security Act*. In the suit, Ooki DAO was treated as an unincorporated association, meaning the CFTC viewed the token holders themselves as parties operating the legal equivalent of a business.

The judgment means that DAOs similar to Ooki DAO are more likely to be seen by the US Courts as unincorporated associations with potential personal liability for token holders or those involved in governance decisions. It is unclear if the CFTC will take enforcement action against individual token holders having settled with the original founders of Ooki DAO.

A particular area of controversy was how the CFTC was to serve notice of the lawsuit to a DAO in the first place, given the absence of any physical business entity or physical address. In the end, the CFTC was granted permission by the court to serve the lawsuit via the chatbox on the Ooki DAO website, and to post the lawsuit on Ooki DAOs online forum.

Ooki DAO did not respond to the lawsuit by the deadline of 10 January 2023, giving the CFTC the opportunity to seek entry of default judgment. The decision serves as a warning to DAOs which seek to be entirely decentralised, or those operating products or protocols which, if centralised, would be plainly financial products or services, as regulators in the US continue an approach of regulation by enforcement.

The regulatory sherpas scale the peaks with further Mt Gox related charges

The U.S. Department of Justice (**DOJ**) has recently unsealed an indictment against Russian nationals Alexey Bilyuchenko and Aleksandr Verner in a further enforcement in the long-running Mt Gox hack fallout. The duo is accused of orchestrating money-laundering in connection with the infamous 2011 Mt. Gox hack, which led to the theft of approximately 647,000 Bitcoin (**BTC**) tokens, and subsequently laundering the stolen assets through the now-defunct BTC-e digital asset exchange.

The Mt. Gox hack, one of the most notorious in the history of cryptocurrency, played a significant role in the exchange's downfall in 2014. The indictment alleges that the Russian nationals, along with their co-conspirators, gained unauthorised access to Mt. Gox's server, transferring stolen BTC to wallets under their control. The stolen funds were then allegedly laundered through accounts at BTC-e and the San Francisco-based Trade Hill exchange, which ceased operations in 2013.

Bilyuchenko is also implicated in assisting Alexander Vinnik, another Russian national, in operating BTC-e from 2011 to 2017. Mr Vinnik was recently sentenced to 5 years prison in France. The indictment further alleges that the accused used a fraudulent contract to conceal and liquidate their stolen tokens, convincing a New York-based Bitcoin brokerage service to wire over USD$6.6 million into various offshore bank accounts under their control.

The case is currently being handled by the U.S. Attorney's Office for the Southern District of New York's Complex Frauds and Cybercrime Unit, with assistance from the Federal Bureau of Investigation (**FBI**) and the Internal Revenue Service's Criminal Investigation (**IRS-CI**) division.

The indictment was originally filed in December 2019, and it remains unclear why the charges have only now been made public. Neither Bilyuchenko nor Verner are currently in U.S. custody and their whereabouts is not clear. The DOJ's announcement also includes a second indictment, accusing Bilyuchenko of involvement with Vinnik and others in the operation of BTC-e from its 2011 launch to its shutdown by U.S. authorities in July 2017.

This indictment, filed in the Northern District of California (**NDCA**), clarifies Vinnik's role in BTC-e, including actions previously attributed to other individuals.

BTC-e hosted over 1 million customers during its peak with some customers using the exchange to launder criminal proceeds of illegal activities, according to the indictment. The indictment also claims a substantial portion of the proceeds of the CryptoWall ransomware scheme was sent to BTC-e.

The indictment alleges that the defendants intentionally created, structured, and operated BTC-e as a criminal business venture, with a complete disregard for anti-money laundering and Know Your Customer (**KYC**) controls. The U.S. Attorney's Office for the NDCA is getting help from the FBI, the IRS-CI, as well as the Secret Service Investigative Division, and Homeland Security Investigations in this case.

This case marks a significant step in the ongoing efforts to bring to justice those involved in one of the largest cryptocurrency theft and money laundering operations in history and stands as an example of how the immutable trail of

crypto transactions persists and can be used to identify wrongdoers long after the fact.