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Blockchain Bites: A16Z releases State of Crypto Report, Labor urged to continue crypto reforms, US Government calls for more industry input, Former BitMEX CEO sentenced to house arrest

Michael Bacina, Jade McGlynn, Luke Misthos and Jordan Markezic of the Piper Alderman Blockchain Group bring you the latest legal, regulatory and project updates in Blockchain and Digital Law.

A16Z releases State of Crypto Report

Venture capital firm Andreessen Horowitz (short titled "a16z"), has released a "State of Crypto Report" championing Web 3 trends and naming Ethereum as the number one blockchain.

The comprehensive research report was broad turning the spotlight on many parts of the industry, including Ethereum, web3, crypto adoption, Defi, and stablecoins. 5 key takeaways from the report are:

1. **The crypto market is in the middle of its 4th price innovation cycle** – the price innovation cycle is a concept a16z posed last year in its May 2020 blog, a thesis that success of the crypto market is cyclical, alternating between periods of high activity and "crypto winters." According to the post, there have been 3 cycles since BTC's inception in 2009 -the first peak in 2011, the second in 2013, and the third in 2017), which indicate that the doom and gloom of the current alleged "crypto winter" can be expected to retreat just as sure as it came; the report compares the current crypto winter to the dot-com crash of the early 2000s.
2. **Web3 is better for creators than Web2;** According to the report we are in a peak period for Web3 with Web 3 tech opening up a new wave in creativity an entrepreneurship that we can only expect to exponentially grow. The company refers to the current market climate as "a golden era of Web3" highlighting the massive wave of world-class talent that has entered Web3 over the last year. While Web 2 includes a far greater number of creators, when compared to Ethereum based NFT creators, Web 3 creators have a much higher earning capacity the report says; According to a16z last year primary sales and royalty payments of Ethereum-based NFTs, totalled a significant $3.9 billion, four times greater than the $1 billion reserved for Web 2 creators through 2022.
3. **Crypto is having a "real world impact"** – Coindesk translated this more to mean, crypto is *building up* into something that is having a real world impact – using examples of play to earn games giving individuals opportunities to earn living wages, like never seen before (think Axie Infinity – see our earlier article on Axie Infinity supporting a Philippines community during COVID) and stress testing new systems as a vital part in the development and adoption of more equitably accessible blockchain based services;
4. **Ethereum is the leading blockchain due to mindshare rather than market share** a16z recognises Ethereum as the dominant blockchain but attributes this to the blockchain being the best known, rather than the best functioning blockchain, prophesising that the technology should should expect to face increasing competition as other blockchains and their protocols become better known for their improved scalability and low gas fees; ;and
5. **How early on we are in the space:** Based on their collected data, a16z foresees that Web 3 could reach up to 1 billion users by 2031!

Despite the recent Luna/Terra debacle, the crypto space continues to grow and the launch of a USD$4.5B fund by a16z underscores their belief in the space.

New Labor Government urged to regulate crypto the right way

Australian cryptocurrency industry leaders have urged the newly elected Labor government to continue the course for crypto regulation spearheaded by the previous Coalition government. The advice notes that Labor had supported the draft regulations while in opposition and highlighted the concern from Web3 industry that the country cannot be allowed to fall behind on key reforms.

Steve Vallas – the head of Australia's leading industry association, Blockchain Australia – noted that significant changes were not expected under the new government:

> *We're moving in the same direction… [t]he issue important to Labor is on consumer protections and concerns about things like scams, and how they impact retail investors. So, we expect that to be more front and centre in the next little while.*

Prior to the election, the then financial services spokesperson for the Labor party – Stephen Jones – outlined that, if elected, a Labor government would consider crypto regulation as one aspect of a suite of framework changes to the digital payment system.

Independent Reserve's chief executive, Adrian Przelozny, did not consider crypto reform to be a policy priority for the new Labor government, but noted that the industry was confident Labor would continue the momentum gathered by the Senate Inquiry into Australia as a Technology and Financial Centre, spearheaded by Liberal senator, Andrew Bragg. Przelozny said:

> *There's a consultation paper out right now which outlines proposed regulation, so we hope the government takes that on board, and we hope they don't try to mess with all the work that's already happened in consultation with the industry…*

It remains to be seen whether the new Labor government will stay the course already set out on. What remains clear, however, is that industry is avidly looking forward to working with government to protect investors and incentivising innovation in the sector.

US Government calls for more industry input

Officials from the US Treasury, the Commerce Department and the New York State Department of Financial Services (**NYDoFS**) has welcomed increased involvement from digital asset industry members at a recent blockchain conference hosted by Chainalysis. The invitation also follows President Biden's executive order signed in March 2022 directing federal agencies to study and report on digital currencies.

The US Commerce Department's International Trade Administration issued a notice asking for public input in its endeavour to develop a framework for enhancing economic competitiveness in, and leveraging of, digital assets.

The notice poses 17 questions related to competitiveness, comparisons to traditional financial services and financial inclusion considerations. The director of cybersecurity and secure innovation at the National Security Council, Carol House, recently noted that the comment requests were essential to help the administration make informed decisions on digital assets policies. House said:

> *[the comment requests] are completely earnest… these opportunities, with the government… putting out requests for comments, we mean it, we need that data, we need that input.*

According to the US Treasury's Financial Crimes Enforcement Network's (**FinCEN**) associate director for enforcement and compliance, Alessio Evangelista, FinCEN received over 10,000 comments from crypto industry stakeholders in response to its 'travel rule' regulatory proposal. The rules, as drafted, would require cryptocurrency trading platforms and banks to keep records of customers' cryptocurrency transactions and counterparties for those transactions exceeding US$3,000.

Evangelista went on to say:

> *It is important to use that we hear from you… we read every single comment and we are carefully considering them as we move forward. Addressing the illicit finance and national security risks related to the travel-rule compliance and unhosted wallets remain top of mind for us.*

Meanwhile, the NYDoFS is seeking to streamline its licencing and business registration process for digital assets, whilst also issuing increased guidance for the industry, according to superintendent Adrienne Harris.

Harris recently commented that she was:

> …a firm believer that we can be good for consumers, good for markets, but also cement New York's place as the financial capital of the world, [and] be a great place to do business whether you're in crypto or other areas of financial services.

It is clear that regulatory authorities sees participation from the private sector as imperative for technological advancement, but also to ensure that the digital assets industry won't be at risk of being used for harmful purposes. Domestically, there have also been calls for the newly elected Labor government to heed the involvement of the private sector in several crypto-initiatives spearheaded by its predecessor.

Former BitMEX CEO sentenced to house arrest

Co-founder and former CEO of BitMEX, Arthur Hayes, has been sentenced to house arrest for six months along with a two year probation period for breaching United States anti-money-laundering law under the Bank Secrecy Act.

The US Federal Court found that while operating BitMEX, a cryptocurrency exchange and derivative trading platform, Hayes and other founders failed to establish a compliant anti-money-laundering program.

The prosecution argued Hayes wilfully ignored US anti-money-laundering rules when operating BitMEX offshore, while the defense claimed he had little guidance from regulators as to the application of US law on offshore cryptocurrency exchanges.

The court found that BitMEX carried out a minimum of USD$209 million in transactions with known darknet markets, or unregistered money services businesses. Before US District Judge John Koeltl delivered the sentence, US Attorney Samuel Raymond told him:

> *There were real consequences. When individuals like Mr. Hayes operate platforms without anti-money-laundering programs or know-your-customer programs, they become a magnet for people to launder money.*

Although BitMEX did eventually engage lawyers and attempt to comply with regulation, breaches of the Bank Secrecy Act had already occurred. Along with the six-month house arrest, Hayes paid a USD$10 million penalty in connection with a settlement with the US Commodity Futures Trading Commission.

Samuel Raymond also warned that allowing Hayes to avoid prison:

> *would send a message to him that the cost of doing business is merely a fine, and he could continue to violate the law for huge amounts and pay any fine*

The case highlights the importance of anti-money-laundering (and counter-terrorism-financing) obligations for cryptocurrency exchanges and serves as a warning for other exchanges which may not be adequately compliant. In Australia, those offering digital currency conversion services under the *Anti-Money Laundering and Counter-Terrorism Financing Act* must be registered and enrolled with AUSTRAC.