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Blockchain Bites: SEC approves first Ethereum Futures ETF, UK to launch Digital Securities Sandbox, Finder Trial to Find Out if Yield Product a Debenture, SBF trial begins in New York, US anti-CBDC Bill progresses, Singapore detailed Three Arrows founder, Australia's BlockFold bought by Fireblocks

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

SEC approves the first Ethereum Futures ETF

On 28 September 2023, Valkyrie Investments received a greenlight from the Securities and Exchange Commission (**SEC**) to launch the first Ethereum futures ETF in the US. The new product builds on top of their existing Bitcoin ETF, transforming it into a combined fund which offers both Bitcoin and Ethereum futures. Valkyrie's chief investment officer Steven McClurg revealed that the hybrid Bitcoin and Ether Strategy ETF (**BTF.O**) is scheduled to launch on the following Monday. He commented:

> We are thrilled to be the first to offer ether futures to our investors

McClurg further reflected the firm's recognition of the growing potential of digital assets:

> Digital assets is a growing allocation across all investors, and we only expect further interest in this area

The approval was likely accelerated by concerns of potential government shutdown which would slow down operations and limit resources. SEC's Chair, Gary Gensler reflected concerns that 'the public won't have somebody, really at full force, overseeing the markets or companies that want to go public'.

The approval follows the 2021 SEC approval of the first Bitcoin-linked ETF from ProShares. Since then, there has been a rush of applications from numerous investment firms including Grayscale and Bitwise for Ethereum futures ETFs. Valkyrie Investments, BlackRock and Fidelity have also aspired to launch spot Bitcoin ETFs. However, the regulator has maintained a cautious approach towards this product type, having previously rejected Grayscale's Bitcoin Spot ETF, due to market manipulation concerns.

Unsurprisingly, SEC has delayed its decision on a series of other Spot Bitcoin ETF applications. In particular, Ark 21 Shares spot Bitcoin ETF's decision was postponed to early 2024, with the SEC commenting in an official statement that it requires:

> Sufficient time to consider the proposed rule change…and the issues raised therein

While there has been no approved spot Bitcoin ETF to date, the recent approval of Valkyrie's Ethereum futures ETF marks a significant milestone for the cryptocurrency industry. The regulator's willingness to support futures-based crypto ETFs has been celebrated by the market, sparking optimism that further cryptocurrency linked ETF applications may be approved in the future.

By M Bacina, K Kim

UK to launch Digital Securities Sandbox to play with tokenisation

The British Treasury is looking to launch a Digital Securities Sandbox (**DSS**) next year for interested parties to test digital technologies and functions, such as tokenisation of real world assets. The DSS is expected to be available at the end of Q1, 2024.

The Head of Capital Markets at the Financial Conduct Authority (**FCA**) in the United Kingdom, Helen Boyd, speaking at CCData's Digital Asset Summit recognised the innovation of the DSS:

> It's a completely new way of us making regulation. In the past, we've tended to wait for activity to come along and regulate it. This is a much more iterative process, we expect it to be a learning curve.

While digital asset regulation is seemingly a top priority for overseas regulators, and the FCA is committing to practical learnings and embracing the innovative technology, Australia is still awaiting consultation on licensing and custody rules, which has been expected to arrive for months now.

Although Australia's Reserve Bank's CBDC Pilot for Digital Finance Innovation report recommends a sandbox approach to enable future industry experimentation and test new financial products and services, there is no word on any plans for such a sandbox in future.

Similarly, the New Zealand Parliament's Finance and Expenditure Committee released a report recommending a sandbox approach for digital assets and even argues the success of similar sandboxes in the UK, but has not announced a sandbox collaboration with stakeholders as yet.

Meanwhile, the European Union is moving ahead with its sandbox for Distributed Ledger Technology launched earlier this year in parallel with its efforts to provide a comprehensive framework to regulate crypto assets under the Markets in Crypto Assets Regulation which will enter in force beginning next year.

With the existing Australian regulatory sandbox not viewed as appropriate for crypto-assets and a regulation by enforcement narrative taking hold, the flight risk for Australian founded crypto-businesses seems only likely to increase. The opportunity remains for Australia to join the global digital assets race by launching its own blockchain sandbox to enable testing of new blockchain based offerings and help develop the right regulatory settings for innovative products and services.

By M Bacina, S Pettigrove and L Misthos

Finder Trial to Find Out if Yield Product a Debenture in Australia

Late last year, in the wake of the FTX collapse, Finder Earn, offered by Finder Wallet, swiftly "sunsetted" and ceased being available to users. Shortly after that occurred, the Australian Securities and Investments Commission (**ASIC**) commenced proceedings against Finder Wallet, arguing that Finder Earn was in substance a debenture offered by Finder Wallet. This came after Block Earner's yield product was attacked by ASIC, being called a 'financial investment' but interestingly not a debenture.

The Finder Earn product offered users the ability to earn interest on True AUD (TAUD), not on fiat currency, that is users had to first convert fiat currency to TAUD, and then deposit that TAUD with Finder. Finder had a real time interest payment calculator showing interest earned and paid out all interest promised to customers.

As we noted at the time:

> ASIC alleges that the product offered by Finder Wallet is a debenture because customers deposit money with the understanding their money would ultimately be repaid, this is a marked difference from the allegation made in relation to Block Earner by ASIC.

The case against Finder is listed for hearing today, which is co-incidentally on the same day that the trial against FTX founder Sam Bankman-Fried commences. Crypto-asset companies in Australia will be watching the Finder hearing and judgment closely given the absence of clear guidance in Australia around what crypto-asset products require licensing and just how licensed products can be offered in Australia.

Attempts to offer licensed crypto-asset products have previously come under attack, in the case of Holon, which fund subsequently closed, or have failed to attract sufficient interest to remain in market, in the case of Cosmos' Bitcoin ETF.

By M Bacina

SBF trial begins in New York

The trial of Sam Bankman-Fried (known as **SBF**), founder of the collapsed crypto exchange FTX, starts in New York today with SBF facing multiple counts of alleged fraud and conspiracy charges.

FTX, then one of the world's largest cryptocurrency exchange, quickly collapsed and filed for Chapter 11 bankruptcy protection in November 2022. Following the collapse of other major crypto firms such as Three Arrows Capital and Celsius, FTX's implosion marked the ongoing "crypto winter".

SBF was arrested in December 2022 on eight criminal charges initiated by the US Department of Justice. SBF later agreed to be extradited from the Bahamas – where FTX was based, to the USA. The number of charges was subsequently increased, and now includes allegations of wire, securities and bank fraud, conspiracy to operate an unlicensed money transmitting business, money laundering, campaign finance violations and foreign bribery. Certain of those charges will be tried separately.

SBF was previously released on a USD$250 million bail, but was later detained after his bail was cancelled.

Since his arrest, SBF has repeatedly spoken and written about his views of the case. His narrative is one of a young founder facing a rapidly growing business and he denies knowingly committing fraud.

SBF's defense team has said the case against him was a "classic rush to judgment" and cited the lack of detailed factual particulars in the original charges. The defense team has also told the court that SBF intends to argue in-house FTX attorneys and external lawyers "were involved" in certain decisions that the company made – a so-called "advise-of-counsel" defense.

On Sunday, the US federal judge overseeing the case upheld a Government motion, finding that SBF's Counsel team cannot blame his lawyers for the collapse or operations of FTX in opening statements to the jury, because:

> the risk of confusion and unfair prejudice to the government were defendant to focus on the pretense or involvement of lawyers at or for FTX and Alameda, without any degree of specificity…is palpable.

The judge held SBF could still try and make this argument at trial on a case by case basis.

The US Department of Justice (**DOJ**) has said they want to call former FTX customers, investors and employees. The ex-employees are expected to include former FTX Chief Technology Officer Gary Wang, former FTX Head of Engineering Nishad Singh and former Alameda Research CEO Caroline Ellison as cooperating witnesses, each of whom has pled guilty to charges tied to the exchange.

According to the DOJ's brief, customers and investors who owned FTX shares can speak to their expectations of how FTX would hold customer funds, while the cooperating witnesses can speak to:

> their interactions with the defendant and their understanding of the purpose of certain statements and actions of the defendant.

The trial commences today US time with jury selection and is expected to last for six weeks.

By J Huang and S Pettigrove

US anti-CBDC Bill progresses, but is there more than meets the eye?

The CBDC Anti-Surveillance State Act, introduced into US Congress as a Bill in February of this year has moved through the powerful House Financial Services Committee, taking a step closer to being voted for on the floor of the US Congress for a vote. The Bill's author is US Representative Tom Emmer.

The Bill aims to prevent the US Federal Reserve from issuing a Central Bank Digital Currency (**CBDC**), or a digital asset that is substantially similar, and require the Federal Reserve's Board of Governors to obtain congressional authorisation before issuing a CBDC. The concern appears that the Federal Reserve might issue a CBDC too similar to the Chinese digital yuan, which has been accused by Wired as "open[ing] up new forms of government surveillance and social control".

In his press release, Representative Emmer, the Majority Whip of the House of Representatives, stresses the importance of the Bill as protection against consumer tracking:

> In short, a central bank digital currency is government-controlled programmable money that, if not designed to emulate cash, could give the federal government the ability to surveil and restrict Americans' transactions.

CBDCs have taken a reputational hit in 2023, with models being analyzed and structural problems found including:

> potential privacy issues, including mass surveillance, misuse and abuse of CBDC data by central banks and intermediaries, and more

For many, CBDC seems to be a shorthand for government surveillance, with Governor DeSantis promising to ban CBDCs if elected President. Representative Emmer believes in the decentralised potential of Web3, saying:

> [the] future digital economy [needs to be] open, permissionless, and private – just like cash.

While the Bill may be seen as stifling innovation by those wanting to see CBDCs move forward (and the CBDC tracker shows a huge number of pilots underway), the real purpose of the Bill, given Representative Emmer's views, is to champion privacy for consumers and prevent:

> [communist]-style surveillance tool that can be weaponized to oppress the American way of life.

The Bill is set for a congressional hearing where, following discussion, debate and a vote, could be enacted as legislation preventing the issuance of a CBDC in the US without congressional authorisation, which would definitely slow down CBDC pilots or adoption in the US given how fractured the US congress presently is.

In Australia, such privacy concerns have not gained traction, and the Reserve Bank of Australia and the Digital Finance Co-operative Research Centre have released a report on how a CBDC could benefit Australia's payment system with positive views on implementing digital asset technology. It remains unclear just how much privacy would be protected in any potential Australian CBDC.

By M Bacina and L Misthos

Singapore seizes Arrow before flight as 3AC founder detained

Su Zhu, co-founder of collapsed hedge fund Three Arrows Capital, was reportedly arrested at Changi airport on Friday while trying to leave Singapore, according to the company's liquidator Teneo.

Three Arrows Capital, founded in 2012 by Su Zhu and Kyle Davis – was known in the crypto-industry for its bullish investment strategies and conviction in a so-called "crypto super cycle". At its peak, Three Arrows reportedly had around US$10 billion in assets under management.

The company filed for bankruptcy in 2022, and was one of the catalysts that set off the ongoing crypto winter due to its interconnected relationships with other major crypto ventures such as FTX, Celsius and Voyager. Three Arrows was placed into liquidation in the British Virgin Islands and Teneo was appointed as liquidator.

The liquidators allege that Zhu and Davies had failed to cooperate with their investigations, and ultimately sought committal orders from the Singapore Court for failing to comply with Court orders. It is understood that Zhu faces up to four months' imprisonment.

In September 2023, the Monetary Authority of Singapore imposed a nine-year ban on Zhu and Davies, prohibiting them from owning or managing any registered capital markets firm. In May 2023, the duo were reprimanded by Dubai's crypto regulator for running a new venture called OPNX, which allows trading in claims in defunct crypto firms, without proper authorisations.

Su Zhu is not the only former crypto tycoon facing legal troubles. Sam Bankman-Fried, the founder of the crypto exchange FTX, was arrested in the Bahamas last December and later charged with orchestrating an allegedly vast fraud and other offences. His criminal trial will begin in a US federal court on 4 October 2023 and is expected to last for 6 weeks.

In March 2023, Do Kwon, the founder of the crypto company Terraform Labs, was also charged with fraud and arrested in Montenegro as he tried to board a private jet to Dubai. He is currently fighting extradition to the USA and South Korea.

By J Huang and S Pettigrove

Aussie Blockchain Business BlockFold bought by Fireblocks

The depths of a the crypto winter has been warmed by Fireblocks announcing it has paid US$10 million (AUD$15.6 million) to acquire Melbourne-based start-up BlockFold. The acquisition has not been publicly announced by either company, but is being reported as complete.

Fireblocks is a well known providers offering crypto custody and infrastructure around storing and issuing digital assets, and they count financial institutions like BNP Paribas and the Tel Aviv Stock Exchange amongst their clients.

BlockFold provides smart contract development, auditing and blockchain development to help the adoption of digital assets, including to financial services companies, building more capabilities for Fireblocks to deliver on what Fireblocks CEO, Michael Shaulov, said when he travelled to Australia for Blockchain Week:

> When you think about the opportunity for the bank… if I'm a customer I have all my assets in the bank, if this extends to a digital wallet … it doesn't matter what you are holding … banks can capture the range of Web3 value in their offering.

This acquisition comes close on the heels of the US Federal Reserve's paper on tokenisation, which is a further indication of the importance of Web 3, and those who are building the expertise to take advantage of the technology will be better equipped when the "if" becomes a "when", with Fireblocks clearly aiming to be ready for that time.

By M Bacina and L Misthos