CryptoLink

April 2024

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CryptoLink is a compilation of news stories published by outside organizations. Akin aggregates the stories, but the information contained in them does not necessarily represent the beliefs or opinions of the firm. Akin's April CryptoLink update includes developments and events that occurred between March 2024 and April 2024.

The big news in crypto policy came out of the Senate this month. On April 17, Senators Cynthia Lummis (R-WY) and Kirsten Gillibrand (D-NY) partnered once again in the digital asset space, this time introducing the Lummis-Gillibrand Payment Stablecoin Act (S. 4155). The proposed legislation would establish a regulatory framework for the payment stablecoins. Its intent is to carve out space for the growth of a safe, regulated stablecoins market in the United States that preserves U.S. dollar dominance. The bill is written with Lummis and Gillibrand's longstanding legislative priorities in mind—namely, to address policy challenges that have plagued digital assets, including how best to enhance consumer protections, combat illicit finance and ensure the supremacy of the U.S. financial market. The senators' proposal complements House Financial Services Committee Chairman Patrick McHenry's (R-NC) ongoing effort to pass his stablecoins bill, the Clarity for Stablecoins Act (H.R.4766). McHenry has secured buy-in from Ranking Member Maxine Waters (D-CA), but numerous obstacles to its passage remain, including support from the White House and the lack of legislative vehicles to attach the bill onto before the end of this Congress. However, by introducing their own stablecoins bill, Lummis and Gillibrand have kickstarted the legislative process for stablecoins in the Senate, which will allow the two chambers to more easily resolve their differences.

Earlier this month, Senate Banking Chair Sherrod Brown said during a Committee hearing that he is working to introduce a bill granting the Treasury Department additional authorities to crack down on illicit finance in the crypto space. The statement echoed calls from Treasury Deputy Secretary Wally Adeyemo, who, during the same hearing, urged the Senate Banking Committee to bestow his office with more power to combat illicit crypto finance, citing national security concerns as one such justification for the need for additional authorities.

In April, regulators brought charges against digital asset platforms, and prosecutors resolved significant criminal actions involving high-profile actors in the cryptocurrency industry. Firstly, the CFTC charged KuCoin, one of the largest cryptocurrency trading platforms, with operating an illegal digital asset derivative exchange. The CFTC alleges that KuCoin engaged in off-exchange commodity futures transactions without registering with the Commission. Additionally, the platform was charged with failing to diligently supervise its futures commission merchant activities and not implementing an effective customer identification program. This is not the first time KuCoin has faced government scrutiny. In December 2023, the New York Attorney General's Office (NYAG) secured a settlement of over $22 million from KuCoin. The NYAG had charged KuCoin with failing to register as a securities and commodities broker-dealer and falsely representing itself as a crypto exchange. As a result of the settlement, New York banned the platform from trading securities and commodities. On April 30, 2024, Changpeng Zhao ("CZ"), the founder of Binance, who had previously pleaded guilty to violating U.S. anti-money laundering requirements, was sentenced to four months in prison. Prosecutors had sought a sentence of up to three years, while CZ's counsel had requested no prison time. Despite these legal challenges, Binance has continued to thrive, with trading reaching its highest level in almost three years last month, as reported publicly.

In this issue

Key Developments

UK Regulators Launch Consultation Paper on Digital Securities Sandbox

On April 3, 2024, the U.K. Financial Conduct Authority and the Bank of England published a consultation paper outlining their proposals to implement and operate a Digital Securities Sandbox (DSS). According to the Bank of England's press release, the DSS is a regime that will allow firms to use developing technology, such as distributed ledger technology, in the issuance, trading and settlement of securities such as shares and bonds. Firms that successfully apply for the DSS will be able to operate under a set of rules and regulations that have been modified to facilitate this. The DSS lasts for five years and will help regulators design a permanent technology-friendly regime for the securities market. The Bank of England and Financial Conduct Authority will work together to operate the DSS. The closing date for responses to the consultation paper is May 29, 2024.

The Bank of England's press release can be found here and the consultation paper can be found here.

U.S. Senators Probe CFTC Chair's Interactions and Meetings with Sam Bankman-Fried

On April 15, 2024, U.S. Senators Elizabeth Warren, a member of the Senate Banking, Housing and Urban Affairs Committee, and Chuck Grassley, a member of the Senate Agriculture Committee, sent a letter to Rostin Behnam, Chair of the Commodity Futures Trading Commission (CFTC), requesting an accounting of all meetings and correspondence between Chair Behnam and Sam Bankman-Fried during his tenure as Chair. Immediately after FTX collapsed in November 2022, Chair Behnam testified before the Senate Agriculture Committee that he and his team met in the CFTC offices with Sam Bankman-Fried and his team 10 times over the prior14 months. In order to understand the nature of Chair Behnam's correspondence with Sam Bankman-Fried in the months leading up to the public revelation of Mr. Bankman-Fried's crimes, the senators are asking Chair Behnam to provide a full accounting of all meetings, phone calls and correspondence with Mr. Bankman-Fried by April 29, 2024.

The letter can be found here and the associated press release can be found here.

Bipartisan Legislation Introduced in the Senate to Establish a Regulatory Framework for Stablecoins

On April 17, 2024, Senators Cynthia Lummis and Kirsten Gillibrand introduced the Lummis-Gillibrand Payment Stablecoin Act. The proposed bipartisan legislation would create a regulatory framework for the payment of stablecoins. Its intent is to carve out space for the growth of a safe, regulated stablecoins market in the United States that preserves U.S. dollar dominance. The bill provides regulators with novel tools to combat illicit finance, including by defining new enforcement powers for federal and state supervisors, granting regulators the authority to take enforcement actions against stablecoin issuers and authorizing the Federal Reserve Board to remove or prohibit issuers. The bill also includes consumer protection provisions akin to what exist for traditional depository institutions, such as both capital requirements and one-to-one reserve requirements, a requirement that depositary institutions and non-banks wishing to issue stablecoins create a firewalled subsidiary for that practice, and Federal Deposit Insurance Corporation (FDIC) conservatorship for insolvent issuers.

The Act can be found here and our client alert discussing the Act can be found here.

IRS Releases New Draft Digital Assets Reporting Form

On April 18, 2024, the U.S. Internal Revenue Service (IRS) released a draft of a form digital asset brokers will have to use to disclose their digital asset sales to the IRS for the first time. The draft Form 1099-DA includes instructions for taxpayers whose transactions are subject to the reporting requirements, which specify that brokers must report proceeds from digital asset dispositions to the IRS and may be required to recognize gain from such dispositions. According to the instructions, reporting is also required where a broker knows or has reason to know that a corporation in which it owns a digital asset that is also stock has had a reportable change in control or capital structure. In addition, brokers may be required to recognize gains from the receipt of cash, services, digital assets or other property that was exchanged for a digital asset that is also the corporation's stock.

The draft Form 1099-DA can be found here.

Key Enforcement Actions

CFTC Charges KuCoin with Operating Illegal Digital Asset Derivatives Exchange

On March 26, 2024, the CFTC announced it filed a civil enforcement action in the U.S. District Court for the Southern District of New York (SDNY) charging Mek Global Limited, PhoenixFin PTE Ltd., Flashdot Limited and Peken Global Limited, which collectively operate a centralized digital asset exchange under the name KuCoin, with multiple violations of the Commodity Exchange Act and CFTC regulations. The complaint alleges that, among other things, KuCoin illegally dealt in off-exchange commodity futures transactions and leveraged, margined or financed retail commodity transactions and solicited and accepted orders for such transactions without registering with the CFTC as a futures commission merchant. Director of Enforcement Ian McGinley stated that the enforcement action makes clear that "the CFTC will charge such entities with failing to register with the CFTC and failing to comply with the agency's rules that protect U.S. customers and prevent and detect terrorist financing and money laundering." In its continuing litigation against KuCoin, the CFTC seeks disgorgement, civil monetary penalties, permanent trading and registration bans, and a permanent injunction against further violations of the Commodity Exchange Act and CFTC regulations.

The CFTC's press release can be found here and the complaint can be found here.

SEC Obtains Final Judgment Against Ryan Felton, FLiK and CoinSpark for Fraudulent ICOs

On March 28, 2024, the Securities and Exchange Commission (SEC) obtained a final judgment against Ryan Felton, FLiK and CoinSpark, whom the SEC had previously charged for their involvement in two fraudulent initial coin offerings (ICOs). The SEC's complaint was filed on September 10, 2020, in federal district court in Atlanta, Georgia. The complaint alleged that Felton promised to build a digital streaming platform for FLiK, and a digital asset trading platform for CoinSpark. Instead, Felton allegedly misappropriated the funds raised in the ICOs, secretly transferred FLiK tokens to himself and sold them into the market and engaged in manipulative trading to inflate the price of SPARK tokens. Felton allegedly used the funds he misappropriated and the proceeds of his manipulative trading to buy a Ferrari, a million-dollar home, diamond jewelry and other luxury goods. Felton, FLiK and CoinSpark consented to the entry of a final judgment, which included ordering joint and several disgorgement in the amount of $2.8 million, plus prejudgment interest in the amount of $704,981.

The SEC's press release can be found here.

Head of Legal and Compliance for Multibillion-Dollar Cryptocurrency Pyramid Scheme 'OneCoin' Sentenced to Four Years in Prison

On April 3, 2024, the U.S. Attorney for the SDNY announced that Irina Dilkinska was sentenced to four years in prison by U.S. District Judge Edgardo Ramos for her role in the massive OneCoin fraud scheme. OneCoin, which began operations in 2014 and was based in Sofia, Bulgaria, marketed and sold a fraudulent cryptocurrency by the same name through a global multi-level marketing network. As a result of misrepresentations made about OneCoin, victims invested over $4 billion in the fraudulent cryptocurrency. Dilkinska previously pled guilty to conspiracy to commit wire fraud and conspiracy to commit money laundering. Dilkinska was the purported Head of Legal and Compliance for OneCoin. According to the U.S. Attorney's Office press release, rather than ensuring that OneCoin complied with the law, Dilkinska assisted in running its day-to-day operations and laundered money for OneCoin, including arranging for the transfer of $110 million in fraudulently obtained OneCoin proceeds to a Cayman Islands entity. In addition to the prison term, Dilkinska was sentenced to one month of supervised release and ordered to forfeit $111,440,000.

The U.S. Attorney's Office press release can be found here.

Crypto Company Fined $700,000 for AI Trading Scam

On April 3, 2024, the Connecticut Department of Banking concluded its case against Burns Capital Investment LLC (BCI) and Thomas Zachary Burns for violating certain provisions of the Connecticut General Statutes and the Connecticut Uniform Securities Act. According to the order, from approximately December 2021 through August 2022, Burns, on behalf of himself and BCI, raised at least $148,000 from at least nine investors, at least five of whom were Connecticut residents, for the purported purpose of pooling and investing in cryptocurrency on behalf of the investors. The regulator determined Burns, and BCI, provided false information to investors, claiming that BCI (the cryptocurrency investment firm) utilized patented artificial intelligence software to engage in continuous trading. They also falsely asserted that BCI executed trades on a Coinbase cryptocurrency exchange and that BCI's cryptocurrency was stored offline in cold storage when it was not actively being traded. In reality, BCI did not have a Coinbase account and never purchased cryptocurrency in the name of BCI and the funds were commingled with Burns' own money and diverted for his own use.

The order can be found here.

Cryptocurrency Trader Consents to SEC Judgment in $4.3 Million Fraud Case

On April 10, 2024, Gabriel Edelman, a cryptocurrency trader, consented to a judgment to end the SEC's fraud charges against Edelman and his affiliated entities, Creative Advancement LLC and Edelman Blockchain Advisors LLC (together the Defendants), for fraudulently raising funds and misappropriating funds from investors. Under the order, Defendants are permanently enjoined from violating certain provisions of the Securities Exchange Act and the Securities Act of 1933, and the court shall determine whether it is appropriate to order disgorgement of ill-gotten gains and/or a civil penalty upon motion of the SEC.

The order can be found here.

Former Security Engineer Sentenced to Three Years in Prison for Hacking Two Decentralized Cryptocurrency Exchanges

On April 12, 2024, the U.S. Attorney for the SDNY announced that Shakeeb Ahmed was sentenced to three years in prison by U.S. District Judge Victor Marrero for hacking two separate decentralized cryptocurrency exchanges and stealing cryptocurrency worth over $12 million. Ahmed previously pled guilty to computer fraud. Ahmed was a senior security engineer and used his experience with smart contracts and blockchain audits to execute the hacks. For one of the attacks, he allegedly used fake pricing data to generate approximately $9 million in inflated fees, then withdrew those fees in the form of cryptocurrency. U.S. Attorney Damian Williams stated that "Ahmed was sentenced to prison in the first ever conviction for the hack of a smart contract and ordered to forfeit all of the stolen crypto. No matter how novel or sophisticated the hack, this Office and our law enforcement partners are committed to following the money and bringing hackers to justice." In addition to the prison term, Ahmed was sentenced to three years of supervised release, ordered to forfeit approximately $12.3 million and a significant quantity of cryptocurrency and pay restitution in the amount of over $5 million.

The U.S. Attorney's Office press release can be found here.

Nebraska Man Indicted for Multi-Million Dollar 'Cryptojacking' Scheme

On April 15, 2024, the U.S. Attorney's Office for the Eastern District of New York unsealed an indictment charging Charles O. Parks III, also known as CP3O, with operating a large-scale illegal "cryptojacking" operation. As part of the scheme, Parks defrauded two well-known providers of cloud computing services out of more than $3.5 million worth of computing resources in order to mine cryptocurrency worth nearly $1 million. Parks was charged with wire fraud, money laundering and engaging in unlawful monetary transactions in connection with the scheme. As alleged in the indictment, from in or about January 2021 through August 2021, Parks created and used a variety of names, corporate affiliations and email addresses to register numerous accounts with the cloud providers and to gain access to massive amounts of computing processing power and storage that he did not pay for. Parks used those fraudulently obtained resources to mine various cryptocurrencies and tricked providers into approving heightened privileges and benefits.

The U.S. Attorney's Office press release can be found here.

Judges Approves Genesis Settlement

On April 16, 2024, U.S. Bankruptcy Judge Sean H. Lane approved a settlement agreement between Genesis Global Capital, LLC, Genesis Asia Pacific Pte. Ltd. and Genesis Global Holdco, LLC (collectively the Debtors), the ad-hoc group of Genesis lenders and the official committee of unsecured creditors for the chapter 11 cases. The settlement agreement resolves all issues among the parties, including the adversary proceeding commenced by Gemini in October 2023 against the Debtors and the counterclaims asserted by the Debtors. Under the settlement, Genesis will return 97% of digital assets lent to it under the 'Earn' program to Gemini within five days of the agreement going into effect. The agreement will take effect at the end of April.

The Settlement Agreement can be found here.

Man Convicted for $110 Million Cryptocurrency Scheme

On April 18, 2024, a federal jury in New York convicted Avraham Eisenberg, a man residing in Puerto Rico, of commodities fraud, commodities market manipulation and wire fraud in connection with the manipulation on the Mango Markets decentralized cryptocurrency exchange. According to court documents and evidence presented at trial, Eisenberg engaged in a scheme to fraudulently obtain approximately $110 million worth of cryptocurrency from Mango Markets and its customers by artificially manipulating the price of certain perpetual futures contracts. Eisenberg is scheduled to be sentenced on July 29 and faces a maximum penalty of 10 years in prison on the commodities fraud count and the commodities manipulation count, and a maximum penalty of 20 years in prison on the wire fraud count. This serves as the first-ever cryptocurrency open-market manipulation case. U.S. Attorney Damian Williams for the SDNY stated that this "ground-breaking prosecution epitomizes this office's ability to employ innovative methods and cutting-edge law enforcement tools to continue to protect all financial markets."

The U.S. Department of Justice's press release can be found here.

Akin Thought Leadership

Bipartisan Legislation Introduced in the Senate to Establish a Regulatory Framework for Stablecoins (April 22, 2024)

Coinbase Court Embraces 'Ecosystem' Approach to Identifying Crypto-Asset Securities (April 3, 2024)

Are Crypto Tokens Securities? *Terraform* Court Says 'Yes' in Extensive Decision (January 12, 2024)

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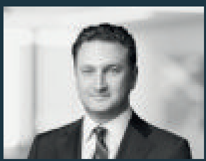

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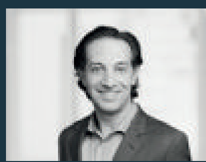

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