Thomas Murray Digital

Digital Asset Risk for Institutional Investors

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Last week the Ukraine government asked crypto exchanges to block addresses of Russian users. The request was rejected by all the major exchanges, including Binance, Coinbase, and Kraken, which is no surprise considering crypto's libertarian beginnings. Despite this, five South Korean exchanges announced they are blocking Russian IP addresses and freezing accounts registered to certain Russian users – although four of these exchanges are only available to users in South Korea, meaning this only prevents Russians in South Korea from accessing their crypto-assets.

Amidst fears that Russia could use cryptocurrencies to evade economic sanctions – perhaps the motivation behind President Putin's support for the Ministry of Finance to support the legalisation and regulation of crypto in the country, against the wishes of its Central Bank – governments worldwide have been intervening to broaden sanctions to include digital assets and the crypto ecosystem. The US Treasury Department published new regulations banning US persons from supporting Russian oligarchs and entities that the government has sanctioned, including with "the use of digital currencies or assets." Accordingly, crypto providers based in the US are required to block sanctioned persons and associated addresses. Meanwhile, the EU has also announced similar measures to extend Russian sanctions to include cryptocurrencies, while Singapore and Japan announced their intentions to introduce sanctions that similarly restrict Russian cryptocurrency transactions.

In an unanticipated development, Switzerland has broken its longstanding tradition of political neutrality by announcing it will match the full range of sanctions imposed on Russia by the EU. It is believed that a considerable portion of Russian president Vladimir Putin's wealth can be linked to Switzerland's financial industry, which has consequently come under considerable pressure to act against Russia and therefore reverse its commitment to neutrality. A senior official at the finance ministry confirmed that Switzerland's sanctions will include freezing crypto-assets, which they claim is necessary to protect the integrity of its world-leading blockchain industry.

Despite the fears of Russia evading sanctions through cryptocurrencies, exchange and on-chain data suggests this has not been happening. The volume of transactions that can be linked to Russia is significantly lower than pre-invasion levels, and a fraction of the all-time highs seen last May. Meanwhile, a blog written by Coinbase's chief legal officer Paul Grewal highlights the historical ease with which individuals and entities have been able to evade sanctions through fiat currencies and traditional financial infrastructures. He says this is achieved "by transacting through shell companies, incorporating known tax havens, and leveraging opaque ownership structures." Grewal goes on to argue that it is much harder to evade sanctions using cryptocurrencies as the transactions are inherently public, traceable, and permanent. Crypto lawyer Jake Chervinsky agreed with this prognosis, arguing that it is impossible for governments to use cryptocurrencies to evade sanctions as "trying to obscure large transactions using open and transparent crypto technology would be far more difficult than other established methods."

Digital Asset Developments

EU lawmakers have now removed language from the Markets in Crypto-Assets (MiCA) Directive that appeared to ban proof-of-work blockchains. This follows last week's news that the European Parliament has delayed a key vote on MiCA over fears the directive could be interpreted as a *de facto* ban on bitcoin. Stefan Berger, chair of the European Parliament's Economics Committee and rapporteur for the legislation, confirmed the passage regarding "environmentally unsustainable consensus mechanisms" had been removed. A new draft bill has been released, in which the passage in question has been redacted, with Berger's office confirming the delayed vote will go ahead in two to four weeks. If approved, the directive will then be negotiated between the European Parliament, the European Commission, and the Council of the European Union.

The US Securities and Exchange Commission (SEC) is considering new crypto recommendations for investment advisors to facilitate compliance with the custody rule. The Advisors Act, commonly known as the custody rule, mandates that registered investment advisors use designated qualified custodians to custody clients' funds and securities. William Birdthistle, Director of the Division of Investment Management at the SEC, stated that he is aware of concerns regarding the impact of crypto-assets on compliance with the custody rule, and that he is therefore considering ways to "bring order" to the industry.

The UK's Financial Conduct Authority (FCA) has revealed that last year that it opened over 300 investigations into crypto-asset firms relating to unauthorised businesses. It also confirmed 50 ongoing investigations into unauthorised businesses in the UK. This is part of the FCA's attempts to protect investors from unregulated ventures and potential scams. It previously issued draft regulations proposing restrictions on how high-risk financial products, including cryptocurrencies, may be marketed.

Last week the Swiss National Bank (SNB) confirmed that DLT Trading Facilities (DLTTFs) can have Central Bank accounts, and access to the Swiss Interbank Clearing (SIC) payment system, operated by SIX Interbank Clearing. The main objective and subsequent benefit of this model enables blockchain firms that are licensed and regulated by the Swiss regulator, FINMA, under the Financial Market Infrastructure Act (FinMIA) to deliver atomic settlement – the act of settling an asset against payment instantaneously on a DLT/blockchain settlement platform.

The SNB has stated that it will also consider offering access to other DLT applications, so long as they do not pose major risks to the system, operate a securities settlement system, and settle payments in Swiss Francs via SIC. One of the upshots of DLTTFs having access to the SIC is that it reduces inefficiencies in the trading of digital assets, and furthermore, is expected to increase competition in the market. Interestingly, SIX Digital Exchange is not licensed as a DLTTF, and for that reason is not able to service retail customers. This may limit its opportunities, particularly in the cryptocurrency markets, which for now continue to be largely retail-oriented and overwhelmingly the most traded type of digital asset.

News Links

- Swiss City of Lugano to Make Bitcoin and Tether 'De Facto' Legal Tender (CoinDesk)
- US Virginia Senate Allows State Banks to Offer Crypto Custody Services (Cointelegraph)
- SEC Investigating NFT Market Over Potential Securities Violations: Reports (Cointelegraph)
- Experts Weigh In on New Crypto Regulations in South Africa (Cointelegraph)
- Trinidad & Tobago Central Bank on Cryptocurrencies: No Restrictions on Purchases (Trinidad Express)
- State Street Works with Regulators on 'Mega' Crypto Custody Push (Bloomberg)
- JP Morgan Invests in Blockchain Intelligence Platform TRM Labs (Finextra)

	Cambridge University Launches Crypto Research Project with IMF and BIS (Cointelegraph)
	South Korean Crypto Market Grows to $45.9B in 2021 Despite Strict Regulations (Cointelegraph)
	Sygnum Bank Set to Release Soccer-Themed Sculptures as AST's (Cointelegraph)
	Ukraine to Sell NFTs to Fund its Military (Pymnts)

Key: Regulation Technology Ecosystem Markets

CBDC Corner

The Monetary Authority of Singapore (MAS) has signalled to the market that it believes Singapore is now technically ready to implement its CBDC, the digital Sing dollar. In the same parliamentary reply however, MAS stated it does not believe there is any great need to issue one currently, and furthermore dismissed ideas that it would be retail-focused, suggesting that financial inclusion is not a problem in Singapore and that electronic payments in the country are seamless, widely used, and efficient.

DCash Service to Resume Next Week (Eastern Caribbean Central Bank)

Central Bank Completes Sand Dollar's Link to Automated Clearing House (The Nassau Guardian)

A Report Card on China's Central Bank Digital Currency: the e-CNY (Atlantic Council)

Brazil's Central Bank Selects Nine CBDC Projects to Move Forward in Innovation Challenge (The Block)

Taiwan to Debut Retail CBDC by September (Pymnts)

Philippines Central Bank to Launch CBDC Research Effort (The Block)

The Potential Effects on the Israeli Banking System of Issuing a Digital Shekel (Bank of Israel)

The Central Bank of Uruguay Publishes Two CBDC-Related Papers (Banco Central Del Uruguay)

Rwanda Central Bank to Pronounce Itself on Digital Currency by December (The New Times)