

Podcast: Cryptocurrency – Wild West or Wall Street?

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Every day, the mainstream media and social media are filled with references to cryptocurrency. Depending on who you ask, it's either simply the next way to spend your money, or it's a haven for criminal activity.

In this episode of More with McGlinchey, **Dan Plunkett** (New Orleans), Co-Chair of the Government and Internal Investigations team, asks his fellow Co-Chair **Bob Driscoll** (Washington) and **Robert Savoie** (Cleveland), Chair of McGlinchey's FinTech practice, to weigh in on this question. Cryptocurrency: Wild West or Wall Street?

Dan Plunkett: Most of the world learned about cryptocurrency in 2009 when Bitcoin appeared on the scene as the first decentralized cryptocurrency. Since then more than 6,000 other different "cryptos," as they're called, with a market value of exceeding \$2 trillion, have appeared.

Joining me are my colleagues, Robert Savoie, from our banking and regulatory compliance office in Cleveland, Ohio, and also Robert Driscoll from our DC office, our co-chair of our government investigations team. I'm Dan Plunkett, resident in the McGlinchey Stafford New Orleans office, and the other chair of the government investigations team.

So this morning, as we explore the regulatory side of cryptocurrency, I'd like to start with Robert Savoie to ask the question: How can it be that this thing that I can't hold, I can't touch, and whose value fluctuates wildly based on who hosts Saturday Night Live, be considered a legitimate currency?

Robert Savoie: Well, I don't think that the manner or the particular reasons of fluctuation are impactful as to whether it's considered a currency. Plenty of currencies fluctuate a lot, and based upon a lot of different things, particularly in smaller countries. You can see variations between the U.S. and other country values based on macro-economic things, or news articles about what people think are going to be long-term trends. Now, I acknowledge it's different, because it's more driven by things that are in the public view via social media, and that is new. But the fact that social media and the fact that the internet is impacting our daily lives is hardly new. And so the integration of currency into sort of popular media is just something new that has arisen. I don't think it is intrinsically devaluing the currency or that it inherently creates any sort of risk or de-stabilizing nature.

I mean, look, it is an asset class. It goes up and down with value, and there are plenty of asset classes that people trade in that go up and down in value substantially. And so to me, in terms of how currency is regulated and the ebbs and flows of that, I think the real reason there's concern is that U.S. is the reserve currency of the world. And so they're used to currency being associated with this extremely stable value, but that's not necessarily true across the world. And so I think that's a little bit of a warped perception that we have as Americans.

Dan Plunkett: Well, let's look at it from the American perspective. How does the U.S. government regulate cryptocurrency? Is there a new set of laws that were passed starting in 2009, or do we treat it as we do the U.S. dollar?

When I look at cryptocurrency, it is certainly not an unregulated world. You have Anti-Money Laundering/Bank Secrecy Act requirements, FinCEN regulates that on the federal level. And then you look at the multi-state regulatory framework. All the cryptocurrency exchanges that handle the assets themselves have to be regulated.

Robert Savoie: Cryptocurrency is already regulated. And that's one of the interesting things about, I think, a blend of new companies that have been quicker to jump into cryptocurrency and adopt it, you know, as you look at the exchanges. But as a regulatory lawyer, when I look at cryptocurrency, it is certainly not an unregulated world. You know, you have Anti-Money Laundering/Bank Secrecy Act requirements, FinCEN regulates that on the federal level, just as it does with currency transactions that have fiat currency. And then you look at the multi-state regulatory framework, right? I mean, all the cryptocurrency exchanges that handle the assets themselves have to be regulated. They either have to be a chartered depository institution or a licensed money services business. And so if you look at the prominent cryptocurrency exchanges that operate in the United States, you will look across them and see that they are licensed and regulated, not by one regulatory agency, but by 50. And they have licenses all across the country and are regulated by 50 different regulatory agencies that all have their own strict supervisory guidance, both in terms of how they operate, the disclosures that they make, how they handle the money, how their permissible assets are handled, and are subject to supervisory exams that are occurring constantly. And when you enter a 50-state regulated world, you know, you're having exams by a dozen state regulators every single year on a rolling basis that all look independently at your operations. And so when I look at this, to me, it is not unregulated at all.

Dan Plunkett: Bob Driscoll, despite all of that, you would agree with me, I suspect, that cryptocurrency is the currency of choice for illicit activity worldwide.

Bob Driscoll: I think I might disagree with that a little bit. First of all, to give you some background that there was reason for concern: if you type "Bitcoin" into the DOJ website right now you come up with 800 hits. And you'll see words like "terrorist financing," "child exploitation," "dark web," "narcotics," and "Ponzi scheme" will all come up. What I'm saying is not necessarily disagreeing with Robert Savoie, but coming at it from a different perspective, which is the key qualifier Robert had was "in the United States." And because crypto is a virtual currency and it exists on the internet, there are plenty of places you can transact crypto that are not the regulated places Robert is talking about. So just like, for example, with cash, how there are proper and improper uses of cash under U.S. law, with crypto, consumers or holders of the currency have a choice to deal with the regulated entities that Robert's talking about, that he works with that are kind of on the right side of the line, so

to speak. But there's also the ability to go to the dark web, to do business with outfits that are trading platforms out of Panama or out of Isle of Man, or out of various places in the world that are not as strictly regulated. And that is predominantly what the government is concerned of.

Clearly in the drug-running world and the gun-running world, cash is still king. But because there's something new, [crypto] is operating in this space that's probably not quite as highly regulated as doing a wire transfer through Wells Fargo, but not necessarily a suitcase full of cash.

It's funny, you mentioned "currency of choice" for illicit activities. I think cash is still king in that regard. In fact, the former head of the CIA testified before Congress recently that something like a lower percentage of the average crypto transaction was likely for illicit money laundering purposes than the percentage of cash transactions. Clearly in the drug running world and the gun running world, all that stuff, cash is still king. But because there's something new, [crypto] is operating in this space that's probably, you know, not quite as highly regulated as doing a wire transfer through Wells Fargo, but not necessarily a suitcase full of cash. It's in that interstitial space there. That's where the government is kind of a little bit freaked out on some of the enforcement, and that they start to hear crypto and Bitcoin, and prosecutor's eyes go up that, why is this entity dealing with this? Is it a way to evade a kind of more traditional banking regulation by traditional U.S. Institutions?

Robert Savoie: So Bob, one question then to follow up on that as a FinTech innovation lawyer by trade: Does the data tell you that it would be more helpful for policing criminal activity to ban the U.S. Dollar than it would be to ban crypto?

Bob Driscoll: Well, you could certainly make that argument! I will tell you this. I think one of the arguments that the folks in your space are going to have to make to the government is that putting crypto outfits in the United States out of business is probably not a good idea, because their competitors are off shore. I think what the U.S. — I would hope, at least from my experience working with clients, that the U.S. Would take the long view, which is that eventually these outfits will be up and running like traditional financial institutions and can be partners with law enforcement and other folks. I have a client that has responded to 300 subpoenas in the past year from U.S. Attorneys' offices, DOJ National Security Division, other law enforcement, looking to track certain transactions to their customers. And they file Suspicious Activity Reports or SARS, just like regular financial institutions. If that type of entity is kind of taken offline in the U.S., in that space, this particular narrow space within the trading platform, numbers two, three, four, and five in the world in that space are all offshore and essentially unregulated. And so I think that hopefully we'll see a situation where the U.S. government kind of comes down like a ton of bricks where it can on those that are unregulated and operating outside the system, and maybe cuts a little slack for people getting up to speed inside the system who are on the right side of the line.

Dan Plunkett: Robert Savoie, do you anticipate that the next turn in cryptocurrency regulation will be at an international level?

The mechanisms to stop both digital and paper use of the U.S. dollar or foreign currencies are established through the banking systems nationally and internationally. But my guess is that there's going to have to be a focus at the federal level, "What do we do on this? Does it require different methods or not?"

Robert Savoie: I don't know. It's going to be interesting to see. International cooperation on things like that is very difficult, you know? And I'm not, not an international lawyer by trade, but my guess would be that, before that, the U.S. would have to establish a more comprehensive federal framework around it that is a little bit more tailored to cryptocurrency. There are requirements that apply at present, but if you think about it, they are styled in a traditional way. And when you think about this, the mechanism to me about how you would stop terrorist financing overseas, right? You all are much more expert on the criminal side than I am, but the CIA has methods to track use of paper currency and track it for international terrorist financing or other things. What is that for crypto, right? Where there's not an actual paper trail, it's all electronic. And I don't know what those tools are. And so I guess the question would be that, you would have to frame that in, because the mechanisms to stop both digital and paper use of the U.S. dollar or foreign currencies are established through the banking systems sort of nationally and internationally. But my guess is that there's going to have to be a focus at the federal level on sort of "What do we do on this? Does it require different methods or not?" And maybe it doesn't, but I think that's something that policymakers are debating. But to me, as Bob said, it's not a concern about within the U.S. That is more external facing, which is a traditional focus of law enforcement, right? How do you prevent that those funds from being used for illicit purposes?

Dan Plunkett: Bob Driscoll, I know that I've heard you say in other regards that the U.S. government often resorts to control through regulation and legislation by regulation. Robert Savoie, I think, would agree with us that we've taken existing laws and applied them to this new technology. And that may be a regulatory framework specific to crypto will be the next turn. Until then, are we going to continue to see regulation through enforcement at the DOJ?

Bob Driscoll: I think for sure. Right now, particularly, the things that create "problems" (and I'm using kind of air quotes; you can't see it cause it's a podcast). The thing that creates problems for the government is not, again, not so much the folks that go find the government and register and follow the rules that exist. The problem is that even internationally, even if you had an agreement (which you don't) [with] crypto, because it's virtual, you know, you have the possibility of non-state actors. And it's not like a bank where if you establish a bank in a country, you're going to hold that country somewhat responsible for what the bank does because the bank's operating under the auspices of that country.

And so I think we've seen it to do, something topical from today. We're looking at the recent hacks on energy companies in Louisiana and other places, which the FBI came out and said were essentially a non-state actor that operates out of Russia, which is different than saying it is a Russian-backed entity or a Russian intelligence entity. That problem is there. And so I think in a lot of ways, the issues are going to be technological as much as they are regulatory because you are dealing with blockchain technology and you'll have ability to look back on the chain and see the history of transactions, which is why one of the things DOJ is prosecuting are essentially transactions that wash crypto. That essentially put it in a "mixer," they call it, where you can do a series of crypto transactions. And essentially you buy back bits, subparticles of other Bitcoins to essentially make it much more difficult to track the provenance of that Bitcoin. And so, for example, if you got Bitcoin in a ransomware attack, you want them to put it through a mixer. And so the government would go after those mixers, for example, as criminal activity.

It's going to be a combination of technological advancement of law enforcement, being able to track the blockchain, and then providing carrots, not just sticks, carrots to folks dealing in the U.S., dealing through regulated entities.

So I think it's going to be very different in the sense that there is not a discrete industry that can be regulated as easily as has been in the past. And so with some of these, it's going to be a combination of technological advancement of law enforcement, being able to track the blockchain, and then providing carrots, not just sticks, carrots to folks dealing in the U.S., dealing through regulated entities. Kind of in the same way, you have some benefit in terms of being able to establish your bona fides by dealing with the U.S. banking system on certain transactions.

Dan Plunkett: Robert Savoie, in closing, we'll let you vote first. Cryptocurrency: wild west or Wall Street?

Robert Savoie: Well, listening to this and taking my cue from Bob, I guess I would say in the U.S., it's Wall Street, and outside of the U.S. it's the wild west!

Dan Plunkett: Bob Driscoll, how say you?

Bob Driscoll: I think it can be either from any place, and that's what makes crypto so unique. You know, you could do wild west from the U.S. by using international participants, and you could do Wall Street from outside the U.S. by using some of Robert's clients, the U.S. participants. So I think it's a very fascinating issue and it's one we'll be confronting more and more as time goes on.

Dan Plunkett: I agree with both of you, and I appreciate you this morning. Thank you for your insights on the evolving world of cryptocurrency. Thank you.

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