ACAMS

Anti-Financial Crime Briefing

Crypto Market Developments

In this briefing, we consider how recent crypto market developments will affect financial crime trends and compliance. This briefing builds on an **infographic previously published by ACAMS** relating to cryptoassets and the war in Ukraine.

Crypto Winter

The term "crypto winter" was coined to describe the ongoing bear market in cryptoasset value and investor sentiment, with some coins losing over 70% of their value. Fundamental issues have become apparent around the stability of cryptoassets, the viability of certain business models, and holistic risk management. A shakeout in the market may lead to a realignment in the application of underlying blockchain technology, a shift away from high-risk projects, and more regulatory oversight of centralized and decentralized applications.

Cryptoassets have experienced major corrections in the past, but current conditions – with businesses defaulting, algorithmic stablecoins collapsing, and retail investors losing their life savings – could reshape the market. Calls for a joined up regulatory rulebook, restrictions on retail offerings, and further consumer protection rules around financial promotions are likely to follow. Financial crime professionals in the cryptoasset sector and financial institution (FI) counterparties should monitor regulatory developments and update policies on a timely basis, to demonstrate legal and regulatory compliance.

Regulatory Developments

The pace of events and the urgency of the response to the turmoil in the market has heightened debate around future regulation of cryptoassets. Until recently, the primary focus has been on regulating the sector through an anti-money laundering (AML)/counter-terrorist financing (CTF) framework, with little attention given to wider issues. This has led to a paradigm where regulators have limited oversight of the sector, the sector has felt held to a higher standard for AML compliance, and FIs have remained cautious around exposure to cryptoassets due to perceived gaps in regulation.

National security and financial crime remain top of policy makers' lists of concerns. FATF has been vocal around its call for the international travel rule to be implemented quickly and effectively. Rules around stablecoins and the traceability of cryptoassets are being brought into scope. In late June, the European Union finalized its Markets in Crypto-Assets (MiCA) legal and regulatory framework, the first effort to put in place a comprehensive regime governing cryptoassets. Even then, the framework does not cover decentralized finance (DeFi) protocols or non-fungible tokens (NFTs). Compliance officers should review current FATF, domestic, and international guidance to proactively manage financial crime risks.

Stablecoins

Stablecoins attempt to peg their value to fiat currency such as the US dollar. They are not subject to regulation and are a core part of the DeFi market, with underpinning DeFi protocols providing stability for investors. In May, TERRA, an algorithmic-based stablecoin, and its governance coin LUNA collapsed in value leading to a run on the token. Significant money laundering risks linked to stablecoins include their perceived lack of volatility, liquidity, trading volume, and decentralized features with a lack of built in know-your-customer (KYC) checks.

Since the collapse of TERRA, governments including the United States, Japan, and the United Kingdom have announced measures to bring stablecoins into regulation and ensure adequate protections, such as sufficient collateralization, and to guard against systemic risk. Stablecoins are also likely to be incorporated into the AML regime and supervised like other cryptoassets for illicit finance risk.

Market Abuse

Attempted market abuse, including insider trading, market manipulation, front running, and typologies such as pump and dump schemes or spoofing, is prevalent throughout initial coin offerings, cryptoasset exchanges, NFT dealerships, and on enabling platforms such as social media.

Cryptoassets are an attractive platform for committing and monetizing market abuse. As a matter of urgency, cryptoasset firms should put in place policies setting out rules to tackle market abuse. Where potential abuse is observed through transaction monitoring, intelligence could be provided to other firms through established information sharing mechanisms. First line of defense staff should be trained to identify crystalized and emerging red flags.

Criminal Activity

Cryptoassets have suffered from their association with criminal activity, since their early links to darknet marketplaces, such as Silk Road, and criminally complicit exchanges like Liberty Reserve and BTC-e. In recent years, projected criminal use of the blockchain and its infrastructure has declined in proportion to legitimate usage, whilst still growing in pure numbers. As criminal activity has morphed over the years, current conditions may alter how organized criminals exploit cryptoassets.

Criminals will closely monitor what current market conditions mean for them. Some will have lost money as their investments fell in value and certain coins have become too volatile or illiquid, reducing their appeal. Some criminals may adopt a flight to stability, using other platforms for money laundering such as payment service providers or other FinTech solutions. Regulators will be watching how cryptoasset firms respond and whether they release any compliance employees. Firms should update their financial crime risk appetite statement accordingly.

Key Takeaways

- Crypto winter will have a profound effect on the cryptoasset industry and the application of its underlying technology. Although the market crash has had a detrimental impact on businesses and individuals' confidence in blockchain stability, uptake in the technology at institutional level, the growth in DeFi, and the push towards Web 3 will drive future growth.
- Broader regulatory coverage is inevitable and will encompass enhanced risk management, bringing the sector closer in line with other FIs. Financial crime regulation will continue to develop, often in response to nascent technology or emerging threats. The sector will come under increasing political pressure to abide by existing regulation and cooperate on future regulatory and legislative proposals.
- The shakeout in the market has implications for business models, restrictions on access to high-risk products, and on criminal activity. Given the damage caused to investors – many of whom lost significant savings from the collapse of stablecoins – crypto lending platforms, and cryptoasset hedge funds, the sector will realign, with some decentralized services being offered by a tighter group of market participants.
- Money laundering and broader national security concerns (including sanctions evasion and terrorism) remain top of policy makers' concerns. Given the considerable focus on financial crime and domestic regulatory attention on supervising firms under AML/CTF, future efforts will look to join up the regulatory rulebook (including market abuse, fraud, and wider risk management).

Author

Joby Carpenter, Global SME – Cryptoassets and Illicit Finance

July 11, 2022

About ACAMS

ACAMS is the largest international membership organization dedicated to providing opportunities for anti-financial crime (AFC) education, best practices, and peer-to-peer networking to AFC professionals globally. With over 90,000 members across 180 jurisdictions, ACAMS is committed to the mission of ending financial crime through the provision of anti-money laundering/counter-terrorism financing and sanctions knowledge-sharing, thought leadership, risk-mitigation services, ESG initiatives, and platforms for public-private dialogue. The association's CAMS certification is the gold-standard qualification for AFC professionals, while the CGSS certification is its premier specialist qualification for sanctions professionals. ACAMS' 60 Chapters globally further amplify the association's mission through training and networking initiatives.

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