

Financial Services

Two Worlds Colliding: Regulations Will Wrangle the “Wild West” of Crypto and Drive Adoption

Ask a crypto-enthusiast what they think about the evolving digital landscape and they might use words like: new, exciting, and dynamic.

For others who believe cryptocurrency is growing at a velocity that our economic infrastructures can't support—the crypto-landscape is more reminiscent of the lawlessness and roughness of “**the Wild West**.” They might describe the crypto industry as untested, unpredictable, unsupported.

On **August 3rd, 2021** Gary Gensler, chairman of the US Securities and Exchange Commission (SEC), declared, “...We just don't have enough investor protection in crypto. Frankly, at this time, it's more like the Wild West. This asset class is rife with fraud, scams, and abuse in certain applications... I worry a lot of people will be hurt.”²

While the SEC is explicit—that there is a new sheriff in town and Gensler intends to bring law and order to this evolving digital frontier—it is worth noting that significant cryptocurrency proponents are not anti-regulation.

Comments such as these by the SEC are less about conflict over whether to place regulations on cryptocurrency, and more of a sign of the expected increase in the sense of public safety once these regulations are in place.

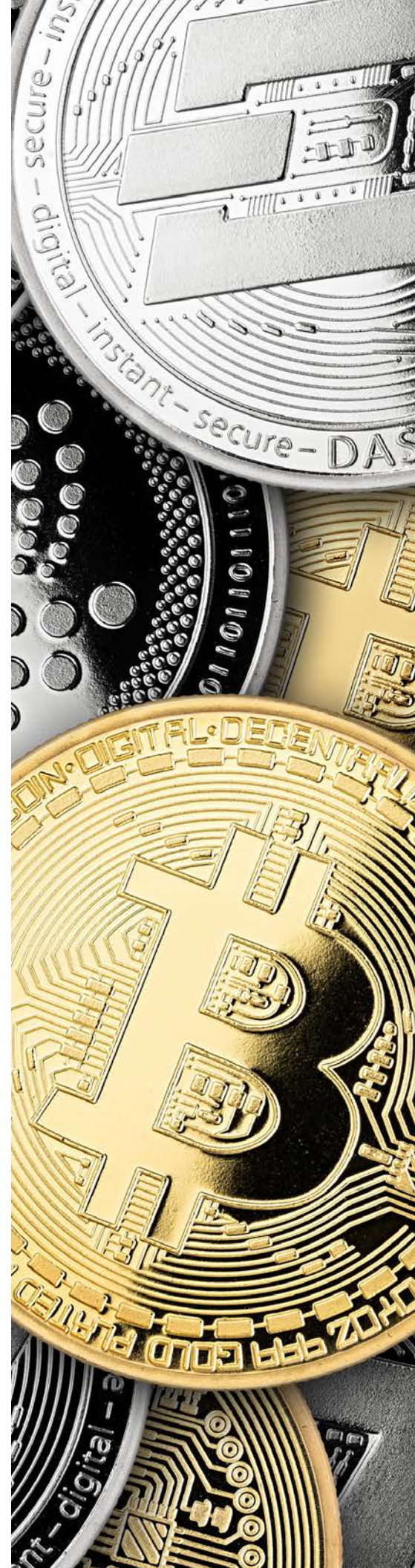
As the world saw during the advent of the internet, the adoption of a major innovation such as cryptocurrency comes with growing pains experienced by both large and small institutions. Regulations on new and unfamiliar products and services bring a sense of security to investors and consumers. Remember, many financial regulations were written when people carried cash or wrote checks, and even sent money by telegraph.

Increased regulatory attention will most likely serve to help the cryptocurrency industry. As institutions continue to adapt and develop within the crypto landscape, the industry will find that new regulations will bring greater rates of adoption and the creation of new products and services. Regulation can change the perception of cryptocurrency from unpredictable to reliable for many investors.

In Guidehouse's third edition of the Two Worlds Colliding Series, we delve into the energetic crypto environment and discuss the impacts of recent consumer, industry, and regulatory activity on the adoption of cryptocurrency in the financial services market.

1. SEC.gov, “Remarks Before the Aspen Security Forum,” Chair Gary Gensler, August 3, 2021, <https://www.sec.gov/news/public-statement/gensler-aspen-security-forum-2021-08-03>.

2. See footnote 1.



The Regulators Are Watching: Regulatory Attention on Cryptocurrency Companies, Products, and Services

It seems that when the SEC's Gensler **warned that crypto platforms would not last very long outside the US regulatory framework**³ – he meant it. Within the SEC and other entities, there has been an increase in regulatory attention on cryptocurrency:

- On **September 8th**, a leading cryptocurrency exchange platform revealed that the SEC issued them a notice detailing that the agency intends to sue the company if the company proceeds with its plans to release a new product, a program that plans to allow certain customers to earn interest on assets, USD Coin (USDC), a stablecoin with value tied to the US dollar. The company has decided against the release.⁴
- On **September 1st**, the SEC charged a crypto-lending platform and certain other parties \$2 billion relating to fraud and operating what the Department of Justice called **"a textbook Ponzi scheme."**⁵ The charge asserts that defendants falsely presented that the crypto-lending platform would deploy a bot that would generate high returns for investors. Instead, the SEC alleges that investor funds were siphoned into the digital wallets of the defendant for personal benefit.⁶
- State regulators have accused a company offering loans and high-interest deposit accounts that are backed by crypto of offering unlicensed securities. **The company was served cease and desist notices** from three states in July alone (New Jersey, Alabama, and Texas).⁷
- New York authorities brought an action and won a court order against a crypto exchange on the claim that the crypto exchange was illegally acting as a broker-dealer in securities. The New York Supreme Court's **court order included a \$3 million judgement** against the defendants.⁸
- **The U.S. Department of Treasury is analyzing the risks and benefits of stablecoins.** Treasury officials met this summer to discuss potential avenues for stablecoin regulation, such as whether major stablecoins could be backed by traditional assets and whether stablecoins pose a risk to economic stability.⁹

"The volume and velocity of expanded use cases continues to demonstrate that crypto is moving into mainstream finance. The number of recent regulatory notices indicates sharpened regulatory focus and early indications that the level of scrutiny will be correlated to this accelerated adoption."

Jonathan Shierly
Director, Financial Services

3. Reuters, "SEC spat with Coinbase previews complex legal battle over crypto," September 28, 2021, <https://www.reuters.com/legal/transactional/sec-spat-with-coinbase-previews-complex-legal-battle-over-crypto-2021-09-28/>.
4. Hamza Shaban and Tory Newmyer, "Coinbase CEO says SEC has threatened to sue over crypto lending program," *The Washington Post*, September 8, 2021, <https://www.washingtonpost.com/business/2021/09/08/coinbase-sec-wells-notice/>.
5. US Department of Justice, "Director and Promoter of BitConnect Pleads Guilty in Global \$2 Billion Cryptocurrency Scheme," September 1, 2021, <https://www.justice.gov/usao-sdca/pr/director-and-promoter-bitconnect-pleads-guilty-global-2-billion-cryptocurrency-scheme>.
6. SEC.gov, "SEC Charges Global Crypto Lending Platform and Top Executive in \$2 Billion Fraud," September 1, 2021, <https://www.sec.gov/news/press-release/2021-172>.
7. Asato Avan-Nomayo, "BlockFi faces regulatory heat, a sign of possible crypto lending regulations?" *Cointelegraph*, August 1, 2021, <https://cointelegraph.com/news/blockfi-faces-regulatory-heat-a-sign-of-possible-crypto-lending-regulations>.
8. Bitcoin.com, "Coinbase Abandons Plan to Launch Lend Program After SEC Threatens Lawsuit," September 21, 2021, <https://news.bitcoin.com/coinbase-abandons-plan-launch-lend-program-after-sec-threatens-lawsuit/>.
9. PYMNTS.com, "U.S. Treasury Eyes Probe of Stablecoins' Financial Risk," September 12, 2021, <https://www.pymnts.com/cryptocurrency/2021/u-s-treasury-eyes-probe-of-stablecoins-financial-risk/>.



Creating Strategic Partnership Through M&A Activity

Cryptocurrency mergers and acquisitions (M&A) continue to showcase examples of financial institutions and crypto firms joining forces to foster strategic partnerships, enhance products and services, and ultimately try not to lag behind competitors.

- **Ethereum scaling project Polygon acquires Ethereum scaling solution Hermez in \$250 million deal** that would include the first-ever merger of two tokens, MATIC and HEZ.¹⁰
- **MasterCard has agreed to acquire cryptocurrency intelligence startup, CipherTrace.** The move is expected to allow MasterCard to differentiate its card and real-time payments infrastructure and assist customers in managing digital asset regulatory and compliance obligations.¹¹
- JPMorgan Chase entered a **“strategic deal”** to take majority ownership of Volkswagen Financial Services' payments platform. The bank asserts the deal will expand JPMorgan Chase's digital payment capabilities and that the partnership will seek to develop a platform for new markets and industries outside of the automotive sector in the future. The bank hails the deal as a **“natural fit”** for its Wholesale Payments business.¹²

Crypto's Global National Adoption Continues to Spread as Governments Evaluate

Recently, the crypto industry reached a major milestone with El Salvador's official implementation of Bitcoin as legal tender. The adoption may serve as a use case for other governments as they determine the possibility of incorporating cryptocurrencies into their own environments.

- Bitcoin became legal tender alongside the US dollar in El Salvador on **September 7th**. The implementation came with **mixed reception** as the country experienced technology issues with its wallet app and protests conducted by untrusting citizens. How the Salvadoran government and population weather the implementation of Bitcoin will surely influence how other governments treat cryptocurrency adoption globally.¹³
- **Panama unveils a bill** to make Bitcoin legal tender. The proposal came just one day after El Salvador officially adopted the cryptocurrency. Panama Congressman Gabriel Silva tweeted that the bill could create jobs, attract investment, and foster government transparency.¹⁴
- El Salvador neighbors **Honduras and Guatemala** have begun studying Central Bank Digital Currencies (CBDCs). The Central Bank of Honduras has started analyzing the feasibility of pilot tests, issuing a digital money or CBDC, and also issued a recommendation for the Central American Monetary Council (the highest monetary authority in the region) to address the adoption of cryptocurrencies.¹⁵
- An India lawmaker of the ruling Bharatiya Janata Party spoke on crypto adoption on **September 8th**. Lawmakers emphasized that crypto legislation in India will need to be “distinct and unique” from other advanced economies, as the country does not have a full capital account convertibility, meaning when a country's currency can be exchanged for a foreign currency without restrictions or controls. India's central bank is looking to unveil its digital rupee model by the end of the year.¹⁶
- Former European Central Bank official Benoit Coeure, head of the Bank for International Settlements' Innovation Hub, made remarks on **September 10th** warning central banks that they are at risk of falling behind cryptocurrency initiatives. Central banks globally, including within the US, are exploring the possibilities of CBDCs. **Eighty-one countries representing over 90% of global GDP** fall into this category.¹⁷ Coeure urged, “We should roll up our sleeves and accelerate our work on the nitty-gritty of CBDC design. CBDCs will take years to be rolled out, while stablecoins and crypto-assets are already here.”¹⁸
- China's digital yuan continues to forge ahead. China's digital yuan pilot was extended to more than two million people this summer, being utilized for more than 70.5 million payments across several sectors, such as retail, public transportation, and government services. **China is allowing certain foreign visitors** to use digital yuan during the upcoming Winter Olympics.¹⁹

10. Yogita Khatri, “Polygon acquires Hermez for \$250 million deal that includes first-ever token ‘merger,’” The Block, August 13, 2021, <https://www.theblockcrypto.com/post/114479/polygon-hermez-merger-matic-hez-tokens-ethereum-projects>.

11. Mastercard.com, “Mastercard acquires CipherTrace to enhance crypto capabilities,” September 9, 2021, <https://www.mastercard.com/news/press/2021/september/mastercard-acquires-ciphertrace-to-enhance-crypto-capabilities/>.

12. JPMorgan.com, “J.P. Morgan to Take Majority Ownership of Volkswagen Payments Business,” September 8, 2021, <https://www.jpmorgan.com/news/jpmorgan-to-take-majority-ownership-of-volkswagen-payments-business>.

13. Bitcoin.com, “First Day of Bitcoin as Legal Tender: El Salvador Buys the Dip, Country's BTC Stash Grows,” September 7, 2021, <https://news.bitcoin.com/first-day-bitcoin-legal-tender-el-salvador-buys-the-dip-countrys-btc-stash-grows/>.

14. Julian Dossset, “Panama unveils bill to make Bitcoin legal tender,” C/NET, September 8, 2021, <https://www.cnet.com/personal-finance/panama-unveils-bill-to-make-bitcoin-legal-tender/>.

15. Erhan Kahraman, “As Bitcoin debuts in El Salvador, Honduras and Guatemala study CBDCs,” Cointelegraph.com, September 9, 2021, <https://cointelegraph.com/news/as-bitcoin-debuts-in-el-salvador-honduras-and-guatemala-study-cbdcs>.

16. Kevin Helms, “India's Cryptocurrency Legislation Will Be ‘Distinct and Unique,’ Says Lawmaker,” Bitcoin.com, September 9, 2021, <https://news.bitcoin.com/india-cryptocurrency-legislation-distinct-unique/>.

17. Atlantic Council.org, “Central Bank Digital Currency Tracker,” <https://www.atlanticcouncil.org/cbdctracker/>.

18. Benoit Coeure, “Central bank digital currency: the future starts today,” BIS.org, September 10, 2021, <https://www.bis.org/speeches/sp210910.htm>.

19. See footnote 17. <https://www.atlanticcouncil.org/cbdctracker/>.

Cryptocurrency

BTC
Bitcoin

ETH
Ethereum

LTC
Litecoin

ETC
Ethereum Class

New Products & Services

As M&A heats up and there is increased expectation of crypto adoption, we see the release of new products and services that combine digital assets and financial services capabilities.

- **Visa looks at plans to accept cryptocurrency payments in Brazil.** Visa has been studying ideas in the crypto space, including plans to work with local crypto companies and develop crypto payment cards.²⁰
- **Facebook announces it is ready to launch its digital wallet, Novi.** David Marcus, a Facebook executive, stated on August 18 that Novi had secured licenses and regulatory approvals in most US states. Novi is expected to offer free P2P payments and establish Facebook as a competitor in the payments industry.²¹

Consumer Adoption

Findings from recent surveys show increasing consumer adoption of cryptocurrency:

- Results from the **2021 Chainalysis Global Crypto Adoption Index** released August 18 show that worldwide crypto adoption is “skyrocketing,” with peer-to-peer (P2P) platforms driving crypto-usage in emerging markets. The increase in P2P usage does not hold for the US and China, which may be due to the increasing institutionalization of crypto trading the US and government mandates on crypto trading in China.²²
- Bakkt Holdings, LLC, a digital asset platform that enables institutions and consumers to manage digital assets, conducted its **US Consumer Crypto Survey** and reported 48% of US consumers have invested money in cryptocurrency during the first half of 2021. The survey found that major hurdles to consumer adoption have been crypto-literacy and risk aversion toward the known volatility in the market.²³

Crypto’s Contentious Reputation

While regulatory skepticism around crypto remains, new use cases and acquisitions signal a strong demand for cryptocurrency in new products. If crypto is to shake the perception that the asset class is rife with fraud, scams, and unpredictability, regulators and enthusiasts will likely need to join forces. We are undoubtedly in an exciting period with cryptocurrency, regulatory oversight will likely increase adoption and help tame the “Wild West.”

It will be interesting to see whether strong and tailored regulation could impel cryptocurrency further and faster as a key component of the global financial system. We will continue to watch it. After all, something happens every day.




20. PYMNTS.com, “Visa Considers Accepting Crypto as Payment in Brazil,” September 9, 2021, <https://www.pymnts.com/visa/2021/visa-to-accept-crypto-as-payment-in-brazil/>.

21. FT.com, “Facebook says ready to launch digital wallet,” *Financial Times*, <https://www.ft.com/content/a8512417-1fde-481a-b282-2f892e3c3b51>.

22. Insights blog, “The 2021 Global Crypto Adoption Index: Worldwide Adoption Jumps Over 880% With P2P Platforms Driving Cryptocurrency Usage in Emerging Markets,” August 18, 2021, <https://blog.chainalysis.com/reports/2021-global-crypto-adoption-index>.

23. Businesswire.com, “Bakkt Study Finds Nearly Half of Reported U.S. Consumers Have Invested in Crypto,” September 1, 2021, <https://www.businesswire.com/news/home/20210901005756/en/Bakkt-Study-Finds-Nearly-Half-of-Reported-U.S.-Consumers-Have-Invested-in-Crypto>.

What Leaders and Luminaries are Saying



“We should break the paradigms of the past... El Salvador has the right to advance toward the First World.”*

Nayib Bukele
President of El Salvador

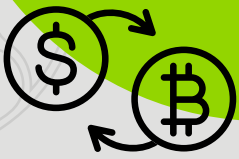
“Crypto is the new shadow bank...It provides many of the same services but without the consumer protections or financial stability... it’s like spinning straw into gold.”*

Elizabeth Warren
US Senator




“A CBDC’s goal is ultimately to preserve the best elements of our current systems while still allowing a safe space for tomorrow’s innovation. To do so, central banks have to act while the current system is still in place – and to act now.”*

Benoit Coeure
Head of the BIS Innovation Hub



“At the heart of finance is trust. And at the heart of trust in markets is investor protection. If this field is going to continue, or reach any of its potential to be a catalyst for change, we better bring it into public policy frameworks.”*

Gary Gensler
Chairman of the SEC

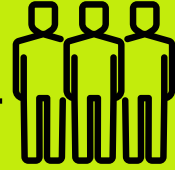
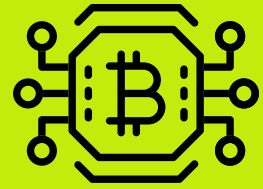


***The person named has not endorsed Guidehouse’s product.**

How Guidehouse Can Help

Our Cryptocurrency and Digital Asset Services team can assist companies with the strategic planning and risk management program design needed to execute and optimize. As regulations and policies evolve, our Bank Secrecy Act/Anti-Money Laundering team has the expertise to guide your organization through the regulatory and compliance environment and address the mounting complexities.

Our Business Transformation and M&A experts provide diligence, strategy, integration management office, and execution support. We focus on digital enablement, operational improvement, and margin improvement, as well as accelerating the integration of firms through rapid due diligence and agile and practical M&A integration advisory and execution.

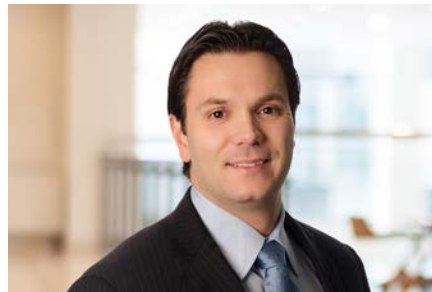


Authors



Alma Angotti

Partner and Global Legislative & Regulatory Risk Leader
alma.angotti@guidehouse.com



Jonathan Shiery

Director, Financial Services
jonathan.shiery@guidehouse.com

Thanks for contributions by **Shantel Silva**



guidehouse.com/financialservices



linkedin.com/showcase/guidehouse-financial-services



twitter.com/GuidehouseFSAC

guidehouse.com

About Guidehouse

Guidehouse is a leading global provider of consulting services to the public sector and commercial markets, with broad capabilities in management, technology, and risk consulting. By combining our public and private sector expertise, we help clients address their most complex challenges and navigate significant regulatory pressures focusing on transformational change, business resiliency, and technology-driven innovation. Across a range of advisory, consulting, outsourcing, and digital services, we create scalable, innovative solutions that help our clients outwit complexity and position them for future growth and success. The company has more than 12,000 professionals in over 50 locations globally. Guidehouse is a Veritas Capital portfolio company, led by seasoned professionals with proven and diverse expertise in traditional and emerging technologies, markets, and agenda-setting issues driving national and global economies. For more information, please visit: www.guidehouse.com.

©2021 Guidehouse Inc. All rights reserved. W327600

This content is for general informational purposes only, and should not be used as a substitute for consultation with professional advisors. This publication may be used only as expressly permitted by license from Guidehouse and may not be otherwise reproduced, modified, distributed, or used without the express written permission of Guidehouse.