



March 2021

# Illicit use of cryptocurrencies

## Regulatory and market evidence

---

The Digital Regulator

## Table of Contents

Executive summary	2
1. Regulatory fears, actions and market evidence	3
2. Other Noteworthy Developments	5

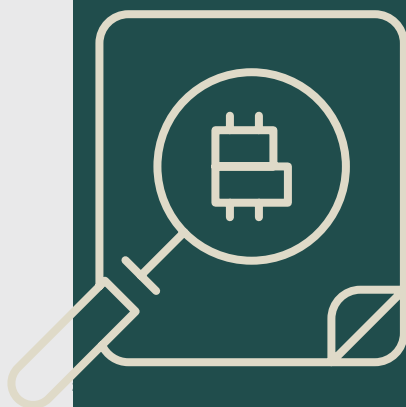
## Authors

**Mattia Rattaggi**  
External Regulatory Analyst  
METI Advisory AG

**Yves Longchamp**  
Head of Research  
SEBA Bank AG

## Contact

research@seba.swiss



## Executive summary

Two authoritative market intelligence reports on the illicit use of cryptocurrencies, released in February 2021 (by Chainalysis and CipherTrace), evidence a marked decrease in the phenomena during 2020 - compared to 2019 - but also new worrying trends in the areas of ransomware and Decentralised Finance (DeFi). Further regulatory action to combat the illicit use of cryptocurrencies is therefore expected. Progress in the implementation of existing regulatory Guidance and a further growth in overall cryptocurrencies transactions should lead to a further decline in the illicit use of cryptocurrencies in the coming years.

Regulators have feared the illicit use of cryptocurrencies since bitcoin was born. Still in 2017 about one-quarter of global bitcoin users were involved in illicit activities, for a total transactional value of around USDbn 76. The authorities took concerted action in 2018 under the leadership of the G20. The resulting Guidance issued by the Financial Action Task Force (FATF) in June 2019 basically subjects virtual assets (VA) and their providers (VASP) to the same standard and procedure governing transactions in fiat currencies and their providers. Yet, as apparent from statements by US Treasury Secretary in February 2021, the illicit use of cryptocurrencies continues to worry regulators, who see it as growing.

The last few weeks have offered several noteworthy regulatory developments in the digital space, such as steady progress of many Central Bank Digital Currencies (CBDC) projects, the approval of the first bitcoin Exchange-traded Fund (ETF) in North America, and material developments in the lawsuits in the US involving the Ripple Labs on the one hand and companies Tether and Bitfinex on the other hand.

Regulators have feared and combated the illicit use of cryptocurrencies since bitcoin was born. The adoption and regulation of cryptocurrencies is leading to less illicit transactions.

## 1. Regulatory fears, actions and market evidence

The most recent market intelligence on illicit use of cryptocurrencies made available during February 2021 by [Chainalysis](#) and [CipherTrace](#) are summarised as follows.

### A marked decrease in the illicit use of cryptocurrencies

- The year 2020 recorded a transactional value of USDbn 10 associated with illicit on-chain activities. This number represents 0.34% of the total value of cryptocurrencies transactions. One year earlier, in 2019, the same value stood at USDbn 21.5, corresponding to 2.1% of the total value of cryptocurrency transactions. While the year-on-year percentage drop is obviously influenced by the increase of overall cryptocurrencies activities in 2020, the absolute figures show that the decrease was substantial from 2019 to 2020. While cryptocurrencies remained appealing for criminals during 2020, the reduction of cryptocurrency-related crime in 2020 suggests that crypto crime decreases in line with an increase in the legitimate use of cryptocurrencies and the implementation of new regulatory requirement.

### Scams, darknet and ransomware as most noticeable categories

- In both 2019 and 2020, the first and second most important category of illicit cryptocurrency transactions were scams and darknet markets. The year 2020 saw, however, an important novelty: A 311% increase over 2019 in the ransomware category of illicit cryptocurrencies transactions (from USDm 85 to USDm 350). This category is particularly worrisome, as ransomware attacks can disrupt local governments and businesses, such as hospitals, for weeks. From a geographic point of view it emerged that Russia receives the largest share of darknet market funds; China receives the largest share of funds sent from addresses associated with stolen funds and ransomware; and the US receives the largest share of funds originating from scams and stolen funds.

### The emerging trends of 2020

- Most money laundering activities are serviced by a small group of providers. These are typically third-party services nested into one or more larger exchanges, that tap into those exchanges' liquidity and trading pairs.
- Most of the growth in darknet market activity can be attributed to the marketplace Hydra, a provider that serves uniquely Russian-speaking countries. Hydra is by far the largest darknet market in the world and accounted for over 75% of darknet market revenue worldwide in 2020.
- DeFi platforms emerge as major vectors for fraud and money laundering due to their vulnerability to hacking and the predisposition of peer to peer transactions to be used for money laundering. This pattern was virtually negligible in all prior years, as DeFi was itself negligible.

Bitcoin's unique features of being at the same time a public blockchain while granting anonymised users' addresses makes it amenable to anonymous yet traceable digital payments. In 2018, a [study](#) extrapolated from a sample of users known to be involved in illegal activities that about one-quarter of global bitcoin users were involved in illicit activities – corresponding to a value of all sort of illicit transactions of around USDbn 76 in 2017. The authors set this figure against a transactional value focused on the US and on drugs of around USDbn 100 in 2010.

In July 2018, the [G20](#) tasked the FATF to address the anonymity surrounding cryptocurrency payments. The [FATF](#) completed its work on 21 June 2019 and issued a [Guidance](#) clarifying the application of anti-money laundering and counter-terrorist financing requirements on VA and VASP. On 25 February 2021, the [FATF](#) re-affirmed the strategic importance of mitigating money laundering and terrorist financing risks of VA and anticipated updating the Guidance to facilitate its implementation and to tackle the risks in DeFi.

The regulatory fears remain however as strong as ever. To illustrate, less than one month ago, the US Treasury Secretary raised again the concern that cryptocurrencies may be used mainly for illicit purposes and noted this as a [“growing problem”](#).

The [United Nations](#) estimated the amount of money laundered globally in one year is 2 to 5% of the global Gross Domestic Product, or USD 800 billion to USD 2 trillion. The reports summarised above suggests that the role of cryptocurrencies-related illicit activities in the global criminal context is relatively small. The summary evidence also confirms that even though cryptocurrencies transactions lend themselves to anonymous transactions, such transactions are better suited for investigative analyses than traditional financial transactions. Going forward, we expect regulators to strengthen Know-Your-Customer (KYC) focus at crypto exchanges, seek ubiquitous implementation of FATF Guidance across the cryptofinance space, and start focusing on reinforcing KYC and Anti-Money Laundering (AML) practices at DeFi applications. Together with a steady growth of cryptocurrencies transactions, these regulatory measures should lead to a further decrease in the illicit use of cryptocurrencies.

## Conclusion

Like transactions in paper money and coins, also cryptocurrencies transactions lend themselves to anonymous transactions. Compared to paper and coins fiat transactions, however, cryptocurrencies are transparently traceable on the blockchain of distributed ledger. Market intelligence shows that the combination of strengthened regulatory requirements surrounding VA and VASP and a steady growth of cryptocurrencies transactions is leading to a decrease in the relative and absolute value of the illicit use of cryptocurrencies.

The last few weeks have offered several noteworthy regulatory developments in the digital space, including the ban of companies Tether and Bitfinex from the State of New York, the approval of the first bitcoin ETF in North America and steady progress of several CBDC projects.

## 2. Other Noteworthy Developments

### Steady progress of many CBDC initiatives

- A survey published by the [Bank for International Settlements](#) (BIS) showed that in general central banks (CB) are progressing from conceptual research to practical experimentation with CBDCs. The BIS expects that CBs collectively representing a fifth of the world's population are likely to issue a general purpose CBDC in the next three years.
- The [BIS](#) also informed that its Multiple CBDC initiative will be joined by the CBs of China and the UAE, adding to a membership comprising the CBs of Hong Kong and Thailand. The project aims to develop a proof-of-concept prototype to facilitate real-time cross-border foreign exchange payments on distributed ledger technology (DLT).
- The [ECB](#) informed that it may only allow digital euro holdings up to a threshold around EUR 3,000. The rationale of the threshold is to discourage large holdings of digital EUR and avoid competition with commercial banks. The ECB confirmed an implementation timeline by 2025. The work is still at the conceptual stage currently.
- The [US Federal Reserve Bank](#) said that a digital dollar may be attractive in that it promotes a more efficient payment system in terms of speed, cost and security. It confirmed being looking into a concept of a digital dollar.

### The first bitcoin ETF becomes reality in North America.

- [Canada](#) becomes the first North American country to introduce a bitcoin ETF. The Ontario Securities Commission approved the request filed by Accelerate Financial Technologies for its Accelerate Bitcoin ETF. The fund will offer units denominated in both United States and Canadian dollars with a 0.7% management fee.
- The [Australian](#) Securities and Investments Commission clarified that a bitcoin ETF is possible, so long as there are appropriate rules in place in the market on which it is traded.

### Two material lawsuits development in the US.

- The [Securities Exchange Commission](#) (SEC) and Ripple Labs released jointly a press release updating the investors and the broad public that the settlement of the lawsuit opened by the SEC against Ripple is unlikely to happen anytime soon.
- The [New York State](#) Attorney banned cryptocurrency companies Tether and Bitfinex from doing business in the State and issued fines to them. The companies were found guilty for having produced false statements regarding Tether's backing and for covering up losses at Bitfinex.

### The Organisation for Economic Co-operation and Development (OECD) released a report summarising the regulatory approaches to assets tokenisation

- The [OECD report](#) established that different jurisdictions have approached tokenisation in different ways. Some have applied existing financial regulations to tokenised assets; others have introduced new tailor-made frameworks or adapted existing rules to accommodate the application of DLTs in tokenisation. The level of development of the market for tokenised assets seems to explain to an extent the policy choice. Regulators in most jurisdictions with active tokenised markets have adopted a technology-neutral approach to policies around tokenised assets and their markets. This is the case for instance in Switzerland.

## Disclaimer

This document has been prepared by SEBA Bank AG ("SEBA") in Switzerland. SEBA is a Swiss bank and securities dealer with its head office and legal domicile in Switzerland. It is authorized and regulated by the Swiss Financial Market Supervisory Authority (FINMA). This document is published solely for information purposes; it is not an advertisement nor is it a solicitation or an offer to buy or sell any financial investment or to participate in any particular investment strategy. This document is for distribution only under such circumstances as may be permitted by applicable law. It is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction where such distribution, publication, availability or use would be contrary to law or regulation or would subject SEBA to any registration or licensing requirement within such jurisdiction.

No representation or warranty, either express or implied, is provided in relation to the accuracy, completeness or reliability of the information contained in this document, except with respect to information concerning SEBA. The information is not intended to be a complete statement or summary of the financial investments, markets or developments referred to in the document. SEBA does not undertake to update or keep current the information. Any statements contained in this document attributed to a third party represent SEBA's interpretation of the data, information and/or opinions provided by that third party either publicly or through a subscription service, and such use and interpretation have not been reviewed by the third party.

Any prices stated in this document are for information purposes only and do not represent valuations for individual investments. There is no representation that any transaction can or could have been elected at those prices, and any prices do not necessarily reflect SEBA's internal books and records or theoretical model-based valuations and may be based on certain assumptions. Different assumptions by SEBA or any other source may yield substantially different results.

Nothing in this document constitutes a representation that any investment strategy or investment is suitable or appropriate to an investor's individual circumstances or otherwise constitutes a personal recommendation. Investments involve risks, and investors should exercise prudence and their own judgment in making their investment decisions. Financial investments described in the document may not be eligible for sale in all jurisdictions or to certain categories of investors. Certain services and products are subject to legal restrictions and cannot be offered on an unrestricted basis to certain investors. Recipients are therefore asked to consult the restrictions relating to investments, products or services for further information. Furthermore, recipients may consult their legal/tax advisors should they require any clarifications. SEBA and any of its directors or employees may be entitled at any time to hold long or short positions in investments, carry out transactions involving relevant investments in the capacity of principal or agent, or provide any other services or have officers, who serve as directors, either to/for the issuer, the investment itself or to/for any company commercially or financially affiliated to such investment.

At any time, investment decisions (including whether to buy, sell or hold investments) made by SEBA and its employees may differ from or be contrary to the opinions expressed in SEBA research publications.

Some investments may not be readily realizable since the market is illiquid and therefore valuing the investment and identifying the risk to which you are exposed may be difficult to quantify. Investing in digital assets including cryptocurrencies as well as in futures and options is not suitable for every investor as there is a substantial risk of loss, and losses in excess of an initial investment may under certain circumstances occur. The value of any investment or income may go down as well as up, and investors may not get back the full amount invested. Past performance of an investment is no guarantee for its future performance. Additional information will be made available upon request. Some investments may be subject to sudden and large falls in value and on realization you may receive back less than you invested or may be required to pay more. Changes in foreign exchange rates may have an adverse effect on the price, value or income of an investment. Tax treatment depends on the individual circumstances and may be subject to change in the future.

SEBA does not provide legal or tax advice and makes no representations as to the tax treatment of assets or the investment returns thereon both in general or with reference to specific investor's circumstances and needs. We are of necessity unable to take into account the particular investment objectives, financial situation and needs of individual investors and we would recommend that you take financial and/or tax advice as to the implications (including tax) prior to investing. Neither SEBA nor any of its directors, employees or agents accepts any liability for any loss (including investment loss) or damage arising out of the use of all or any of the Information provided in the document.

This document may not be reproduced or copies circulated without prior authority of SEBA. Unless otherwise agreed in writing SEBA expressly prohibits the distribution and transfer of this document to third parties for any reason. SEBA accepts no liability whatsoever for any claims or lawsuits from any third parties arising from the use or distribution of this document.

Research will initiate, update and cease coverage solely at the discretion of SEBA. The information contained in this document is based on numerous assumptions. Different assumptions could result in materially different results. SEBA may use research input provided by analysts employed by its affiliate B&B Analytics Private Limited, Mumbai. The analyst(s) responsible for the preparation of this document may interact with trading desk personnel, sales personnel and other parties for the purpose of gathering, applying and interpreting market information. The compensation of the analyst who prepared this document is determined exclusively by SEBA.

Austria: SEBA is not licensed to conduct banking and financial activities in Austria nor is SEBA supervised by the Austrian Financial Market Authority (Finanzmarktaufsicht), to which this document has not been submitted for approval. France: SEBA is not licensed to conduct banking and financial activities in France nor is SEBA supervised by French banking and financial authorities. Italy: SEBA is not licensed to conduct banking and financial activities in Italy nor is SEBA supervised by the Bank of Italy (Banca d'Italia) and the Italian Financial Markets Supervisory Authority (CONSOB - Commissione Nazionale per le Società e la Borsa), to which this document has not been submitted for approval. Germany: SEBA is not licensed to conduct banking and financial activities in Germany nor is SEBA supervised by the German Federal Financial Services Supervisory Authority (Bundesanstalt für Finanzdienstleistungsaufsicht), to which this document has not been submitted for approval. Hong-Kong: SEBA is not licensed to conduct banking and financial activities in Hong-Kong nor is SEBA supervised by banking and financial authorities in Hong-Kong, to which this document has not been submitted for approval. This document is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of or located in Hong-Kong where such distribution, publication, availability or use would be contrary to law or regulation or would subject SEBA to any registration or licensing requirement within such jurisdiction. This document is under no circumstances directed to, or intended for distribution, publication to or use by, persons who are not "professional investors" within the meaning of the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) and any rules made thereunder (the "SFO"). Netherlands: This publication has been produced by SEBA, which is not authorised to provide regulated services in the Netherlands. Portugal: SEBA is not licensed to conduct banking and financial activities in Portugal nor is SEBA supervised by the Portuguese regulators Bank of Portugal "Banco de Portugal" and Portuguese Securities Exchange Commission "Comissao do Mercado de Valores Mobiliarios". Singapore: SEBA is not licensed to conduct banking and financial activities in Singapore nor is SEBA supervised by banking and financial authorities in Singapore, to which this document has not been submitted for approval. This document was provided to you as a result of a request received by SEBA from you and/or persons entitled to make the request on your behalf. Should you have received the document erroneously, SEBA asks that you kindly destroy/delete it and inform SEBA immediately. This document is not directed to, or intended for distribution to or use by, any person or entity who is a citizen or resident of or located in Singapore where such distribution, publication, availability or use would be contrary to law or regulation or would subject SEBA to any registration or licensing requirement within such jurisdiction. This document is under no circumstances directed to, or intended for distribution, publication to or use by, persons who are not accredited investors, expert investors or institutional investors as defined in section 4A of the Securities and Futures Act (Cap. 289 of Singapore) ("SFA"). UK: This document has been prepared by SEBA Bank AG ("SEBA") in Switzerland. SEBA is a Swiss bank and securities dealer with its head office and legal domicile in Switzerland. It is authorized and regulated by the Swiss Financial Market Supervisory Authority (FINMA). This document is for your information only and is not intended as an offer, or a solicitation of an offer, to buy or sell any investment or other specific product.

SEBA is not an authorised person for purposes of the Financial Services and Markets Act (FSMA), and accordingly, any information if deemed a financial promotion is provided only to persons in the UK reasonably believed to be of a kind to whom promotions may be communicated by an unauthorised person pursuant to an exemption under the FSMA (Financial Promotion) Order 2005 (the "FPO"). Such persons include: (a) persons having professional experience in matters relating to investments ("Investment Professionals") and (b) high net worth bodies corporate, partnerships, unincorporated associations, trusts, etc. falling within Article 49 of the FPO ("High Net Worth Businesses"). High Net Worth Businesses include: (i) a corporation which has called-up share capital or net assets of at least GBP 5 million or is a member of a group in which includes a company with called-up share capital or net assets of at least GBP 5 million (but where the corporation has more than 20 shareholders or it is a subsidiary of a company with more than 20 shareholders, the GBP 5 million share capital / net assets requirement is reduced to GBP 500,000); (ii) a partnership or unincorporated association with net assets of at least GBP 5 million and (iii) a trustee of a trust which has had gross assets (i.e. total assets held before deduction of any liabilities) of at least GBP 10 million at any time within the year preceding the promotion. Any financial promotion information is available only to such persons, and persons of any other description in the UK may not rely on the information in it. Most of the protections provided by the UK regulatory system, and compensation under the UK Financial Services Compensation Scheme, will not be available.

© SEBA Bank AG, Kolinplatz 15, 6300 Zug. 2021. All rights reserved.

