Eric: Hi, Eric Hess with The Encrypted Economy. This week, we had Michael Mosier on the podcast. He has quite the background and most recently left who's acting director of FinCEN role for a stealth startup, which we refer to as project T, that's my own name for it. A different podcast was actually planned and then the fat of guidance came out on virtual asset service providers and virtual assets.

We went with it on this episode, we talked about his time at FinCEN, what he saw in terms of the attitudes there and at the department of treasury broadly. And it was a bit more encouraging than I anticipated. So it suggested that maybe there were actually constructive discussions going on. Of course, if we waited even just one other day, we would have also covered the treasury department's report, us stable coins with new registration and oversights requirements, specifically for stable claims to become regulated as insured depository institutions.

So much for optimism. Just kidding, but not really. Anyway. So we talked about, of course, the FATF guidance. Now, of course, it's guidance, not a formal recommendation, but it is for the world. So many jurisdictions will frame their AML regulations around it. And it does obviously carry weight all the more reason to get ahead of it and have conversations and comments around it that are shared and carefully considered.

But maybe there's a sign that they have. May moderate some of their positions on some fronts and in other cases, not so much. So obviously a continuing work in progress, some cause for concern, and we'll get into that on the podcast. We will be having Michael back on for, with his team for stealth, project T and that's just me hyping it up, but why not?

Anyway, if you enjoy this podcast, please share it. Our numbers keep going up and thank you for sharing it. You know, somebody who might like it, share it with them just once. Keep going anyway. Please keep it up with this. I bring you, Michael Mosier, on The Encrypted Economy.

Welcome to The Encrypted Economy, a weekly podcast, featuring discussions, exploring the business laws, regulation, security, and technologies relating to digital assets and data.

I am Eric Hess, founder of Hess Legal Counsel. I've spent decades representing regulated exchanges, broker-dealers, investment advisors, and all matter of FinTech companies, for all things touching electronic trading with a focus on new and developing technologies.

Okay. This is Eric Hess with the Encrypted Economy excited to have Michael mosey on the show.

Michael was previously a white house, national security council director, deputy chief, that the department of justice acting director of FinCEN, counselor to the deputy secretary on senior capacity. He was the first in-house counsel that she analyzed was an adjunct law professor at Georgetown university law center and formerly represented technology and financial services clients at a law firm.

This is funny because the first time I've ever done this, Michael and I just had a really great conversation. We said the most brilliant things ever, a man imaginable. And then I realized that we weren't taping. So I'm sorry for posterity's sake, all that brilliance, may be lost, we'll try and recapture some of it for the rest of the podcast.

But Michael, welcome again to the podcast. This time being taped. Thank you. Great to be here and warmed up. You're warmed up. We're all warmed up. We're just going to zip through it. So Michael I'm so sorry. Can you again, give the bat your background? You know, I glossed over it, but just talk about that sort of what the Genesis of your engagement on the digital asset side.

Sure. Yeah.

Michael: Yeah. Thanks, Eric. Part of my diving into crypto was from the time at the money-laundering section at justice. As well as the national security council, whereas director for transnational organized crime and. Both of those looking at emerging issues of risk, whether it's for elicit finance or also just the U.S. economy and working with cyber threats.

And one of those early on was trying to balance hacking that was happening in us financial institutions. And how do we address that in a way that isn't going to stop white hat hacking making sure that we're progressing innovation in the crypto and cyberspace? And so I think it's just one of those things where we've been looking at what's an emerging risk, but also what's an emerging opportunity to advance us foreign policy.

And so part of that I think has played out recently with Venezuela where the US treasury and OFAC specifically gave a license to allow funds from the opposition government that was here in the U S and blocked to go through USD-C and Air TM into front of thousands of frontline medical workers who needed aid in the, in Venezuela.

And that's a, I think a great example of how. The censorship-resistant nature of crypto and is, can be an advancer of foreign policy goals, not just a threat to them. And one actually really interesting point to that is because also it was crypto and it was auditable. It wasn't dumping bags of cash there which is an issue.

I think we've seen in the aftermath of Afghanistan where it turned out duffle bags full of cash in terms of aid was really hard to maintain financial integrity on and audited. And that's something where here, and you're it. It's not transporting hundreds of pounds of it.

You're, you're getting something immediately out there it's auditable. And I think that's an important piece to that. The government's looking at both. I think you hear more about the risk side of it, but they're acutely aware of.

Eric: Yeah, arguably it should permit greater traceability to ensure that the funds are going to whom you believe they are.

It doesn't mean that other things can't happen along the way, but certainly, something that maybe we don't appreciate it as much as in the US because we are generally banked, but a lot of these countries aren't and so they don't trust the government and. Digitalize, this can be a very important conduit and foreign policy tool.

So you can't really speak to what's going on at the sec, but the Department of Treasury is obviously a very big actor in the space, and we all know that Gary Gensler would love to be the secretary of it. So being so who knows there may be a blending soon, but, could you talk a little bit about maybe some of the tension that exists within, from your position, from your observation?

Within the department of treasury, as it relates to digital assets, both the, those who are extremely concerned too, about it, maybe with regards to like stable coin and money laundering, versus those who, see it as a very powerful tool and obviously the future.

Michael: Yeah. I think it's a good question.

It is important to, to note that government itself isn't monolithic, just like industry isn't monolithic and Jamie Diamond says a lot of things. And then in the background, JP Morgan is advancing blockchain internally. But Jamie's got the microphone more than the folks who are doing the building.

And I think that happens anywhere and certainly in political organizations as well and government organizations. The career folks who've been might be working with crypto issues since 2011. And before. Have a really great appreciation for all the potential of it. And I think that's usually been my experience.

The more people have worked with crypto, the more comfortable they feel with it, but also the more excited about the potential of it, which I'm glad played out through treasury with the Venezuelan aid that got there. I think that's a big, that's a bigger statement than sometimes it gets seen, but that's a precedent-setting, but I think you also have when folks are either at the end of it administration or the beginning.

A lot of the risk is on them and it's their chance to stop a risk that's on their watch. And so they tend to be very focused on the risk side of things, because they feel like the goalie more than the score, at least in the, at least as they're getting up to speed or on the way out when they feel like, Hey, there was something that is going to be considered on my watch and I want to have a big impact.

And so there is that sort of dynamic tension, including for time, a lot of people, particularly in the senior positions have a very limited time, they're trying to deal with like hundreds of new issues. And so the first question is what do I have to worry about? Give me the threat briefing.

And when I know that I'm addressing the threats, then we'll move on to the other stuff. They're multitasking for sure, but you wanna address the highest risks. And so part of what we really tried to do and FinCEN, because we have a lot of folks that have been working in the cryptos.

Since it really the very, very beginning, we put out a rulemaking in 2011, we did uh, guidance in 2013, and an updated really comprehensive one in 2019. And so we wanted to talk through the mechanics and not just the risks and when ransomware came up, we said, wait, let's stop and talk through how this actually.

Before we get into all the policy-making and what we should do, because we want to make sure everybody understands how this actually works, how a flow of payment works, how the ransomware actors are actually functioning in, in detail. There's actually quite a bit of information out there.

From folks like recorded future and others that have been, in chat rooms or they've gotten information from these folks of how they're operating. And so it's taking that pause and saying, wait, let's see how this really works. By the way. There's a lot of actors that are really positive in this space.

This isn't like a, Hey, we're all trying to evade stuff. You have digital forensics, incident response, people and insurance providers and virtual asset service providers. The exchange. That actually everybody's pretty aligned on doing the right thing and wanting to stop it. There isn't really a pro and con of it.

And so it was getting everybody together for that and including pushing to do two fins and exchanges, which is where we convene private sector actors with law enforcement and do information sharing and said, Hey, let's before. Start talking about doing new rulemakings why don't we just get everybody together and see what's really needed.

And I'm glad that's what played out. I think that's really important. And so there is, there's a bias towards action and there's a sense of risk, but I think you have a lot of people also within government that see the positives. Particularly I think the more they work with it, the more they see the potential.

And that's part of the, being out in industry again that we, that I'm hopefully to work with people of seeing, Hey, there's a lot of technical solutions to policy issues. Let's work on those and share information before we get into like new rules that, that might not appreciate what the potential.

Eric: Do you think there that there is a divide between those who are at senior levels, maybe who are eight to say older, a little more entrenched, maybe their career life cycle isn't as, as long versus those who are younger and coming up, do you see that divide or do you think it's pretty balanced all the way?

In terms of how they view digital assets and the need to impose stricter regulation or stricter controls. Yeah. That's interesting

Michael: question. I think it's, as an old guy myself, I think it's probably, it might not be age. But, uh, but I do

Eric: think you could be the exception. You could be the exception.

Hey, I'm not exactly a spring chicken either um, it's not easy being a.

Michael: No, I think it's I think there's two good points in your question. One is I think there's a, how recently you've touched or been involved with crypto, I think is tends to be an indicator of how positive you're going to be, because it is a really complex and incredibly rapidly evolving area.

And the other is where you are and seniority, partly just because you have, you're dealing with 3000 issues, you have very limited hours in the day. And so the first thing usually you're starting with is what's the risk? What could go wrong? That's on my watch. And so I think that's where the healthy dynamic is of career folks that might've been working in this space for 15 years to say, hang on, let me just do a one-on-one and how the mechanics.

The senior folks are like, I don't have time. I have an a C meeting in an hour. And it's, and it's part of it is our job. I think as career folks to say, hang on, I really need you to understand this. And here's why, and make that argument. And you're all vying for their time. And, crypto, even as director acting director of FinCEN, there was, it was like one tiny issue out of 300 issues that we had to deal with.

And then you multiply that for the treasury secretary and deputy secretary who's also. Everything else, domestic finance, international affairs, everything. And so you're constantly making those arguments of Hey, I really, really need their time on this and going to the cheapest staff and getting that and making it's an advocacy like you need to make of that argument.

And part of that is working with industry to, to help us to say Hey, wait a minute. There's this other really positive impact? Like for financial inclusion or whatever. That you're even climate impact in some positive way that maybe folks don't understand. And like there's all this talk about how Bitcoin mining actually can help ironically with some of the environmental, because you're able to like actually flex with the.

That's like an argument that doesn't, that needs to be presented. It's on us as a case in point. Yeah. It's and it needs to be explained to them when they have 50,000 other people also shouting at them and eating their time. But I do think there is that dynamic tension and it played out with the, I think with the on hosted wallets rule at the end of the month.

Administered treasury administration, at least as well, where I think you, he felt an urgency to take some action. And I think without getting too far into it, some of the career folks and law enforcement felt like it was probably being way too rushed, but he felt a sense of urgency and, and we were able to extend it which I'm very happy.

Eric: Great. Great. So Michael and I, we scheduled this podcast before Faddis came out with their updated guidance for virtual assets and virtual assets service providers. We had, we talked about, FATF before financial action task force. We had Mark Boyer and on, we talked about fight with him, and then we also had Dave Jetta.

Who was on the podcast before the MasterCard acquisition of cipher trace. And I mentioned before, he really should've given us the scoop there, but we'll forgive it. But the guidance that they released was not even a formal recommendation, but rather than me summarizing it I think probably Michael, you could probably give a little bit of background on what FATF is, who's driving it the, the, the countries that are members of it, how they participate, how they issue guidance.

Is, is sort passed down and adopted by the different jurisdictions before we even get into it. Just to do a little bit of a high level of background.

Michael: Yeah, sure. Eric. Yeah, I think it's really important to put FATF guidance in context of what, who they are and what it really means FATF itself is the financial action task force, which is a global anti money laundering inter-governmental body.

So they got about 200 countries and jurisdictions that are members. Get together and they set international standards to aim, to prevent illegal activity and sort of the harm from money-laundering and it's a policy making body. So it's, it's a consensus driven UN type entity. And I think it's important to note that, they have, they do put out recommendations like capital our recommendations that are.

Standards. And those are that something that all the member entities commit to implementing and you can be peer reviewed on that. And so there are mutual evaluations that happen on sort of a multi-year cycle. And like when the U S is being mutually evaluated, they pick other countries that come in and they spend a quite a bit of time asking questions, doing sort of due diligence.

How are you actually implementing this? Did you really. And then you get graded. Usually it's a mix and it's , not, not a huge deal, but you can actually get a really low mark and get gray listed potentially. And actually it can impact your risk rating and your access to other financial, to the rest of the financial system.

So it's one of those where it's, if they're not an enforcement body, there's no compliance. I try never to talk about compliance with FATF because it's not a compliance body. There's no enforcement it's standards when they're at the formal recommendation level. And, but it's up to every jurisdiction itself to actually implement them in their own ways.

And so on the one hand, they are, tend to be relatively general because they want it. They have to get consensus among 200 people. Pizza toppings across 200 people would be a brutal undertaking, but I think this level of complexity, particularly the virtual assets to get 200, entities to agree on it.

It's going to, everybody's going to want a little wiggle room on the one hand. You want to take it seriously? The other jurisdictions could implement this in different ways. And that could impact you particularly in the crypto space because everything is basically international, but it's not the rules themselves.

And so there is always going to be a sort of certain level of lack of granularity, which is probably to some degree good, because you want to have. Some personal Liberty within jurisdictions to make different changes and stepping back to the guidance that just came out. That's not a recommendation, it's just guidance.

So it is not a formal standard that's been adopted by FATF there's no requirement or even expectation that it gets implemented. I think they feel like. Here's stuff we could agree on to help people look forward and move forward. I don't, I actually have not heard that it's even going to be moved to the recommendation stage.

I think it's more of people are asking for feedback on this and jurisdictions want to get to a, some harmonization, which is a positive thing to reduce sort of regulatory arbitrage, which is good for everybody, including builders who want to be able to build with some consistency and reliable. But it's, but it's just guidance.

So I think it's one of those things to not freak out, but to be very vigilant about, because you are going to see, you could see some jurisdictions, use this as cover to rush forward and say, see, we're going to make everything required to be intermediaries or something like that. And because fat have said, so you don't want to overestimate it, but I think you also certainly don't want to underestimate it.

It's now is the time to take what's in here and to be. Proactive about going to FATF and going to key jurisdictions for you and saying, okay, this was great. But here's five things that I think could change in a way that would help for clarity for everybody, including people that are trying to build in the right way.

Eric: Excellent. So is the fact that it's not going to a formal recommendation, is that, was that known before the release? Was that something that was gleaned from the earlier. I think that the

Michael: legal term for that is hearsay. I don't know. That's what I, that's what I'm hearing.

Eric: No. So that's alpha. That's alpha.

That is hearsay equals alpha. So it, what it probably means if it doesn't go to a formal recommendation, then it may not even be the name and shame game for it. I mean, if you're, if it's a form of recommendation and you don't comply, then it's name and shame. But if it's not a formal recommendation, And by name and shame it again, goes to the gray list of which ones aren't compliant.

Then, you're on the gray list and, it could impact you, but if it's not, then presumably it doesn't really have an how much of an impact would it have on whether your gray listed?

Michael: Yeah, it's not it's. It's specifically non-binding so I don't think it's going to impact that.

I, my worry in a vigilant sense with the, with it as guidance, is that not that it's a rule it's that there are jurisdictions that will feel like. In the bigger optics we're trying to get in line. We have other issues with FATF. We want to show that we're being a good actor in this space or, or just Hey, we're China, we'd love to crack down on this stuff and now we, and now, instead of saying, it's our idea. And it, and they will explicitly say, this is FATF guidance there they've, everybody agreed, this is the direction things should go. And so I think it's partly people and jurisdictions getting ahead of it or using it as cover because the fact is they will, I think realistically will say everybody agreed on this language.

It's just that it's, some of it's very general. And I think with any multilateral body, there's a measure of horse trading and things that some people care about. And some people don't that may feel like it could be better, but it's just not worth the. Chips that they have to vote with. So that's what worries me is more the sort of things get moving ahead of it down a line.

That's well, it basically said it had to be intermediary, so that's where we're headed and they use it as cover.

Eric: And when Dave Jevans was on the podcast, you also talked about that. There's a number of jurisdictions who will just address. Do you know, as it comes out, even in guidance form without, without too much fuss and then figure out how to regulate it.

So the same issue, but just that there may be jurisdictions that just say whatever they come out with, we adopt that that's the United nations approach to it, then we're rolling with it. Yeah. So interesting. So there's a number of things to obviously talk about in the guidance.

Obviously the guidance also covers the, to your point, a. A bit of a regulatory, possibly consensus emerging view on how to treat some of these things. There may be little disputes, but as a fat of sharpens its guidance, you would anticipate that, the most active members aren't going to radically go the opposite direction from what fat have says.

You know, we'll, we'll break it down a little. W w we'll put you on the spot asking you a bunch of questions about it. The menu today is the travel rule. Then the definitions of virtual assets and virtual assets, service providers, then how they cover defy then. And if T. Stable coins peer-to-peer and you'll be noting good news along the way.

So except for that, really not that much to do, right? Yeah. This be quick. So this is why we have a whole podcast episode. So the, the travel rule let's talk a little bit about the evolving perspective of FATF toward the travel rules, starting up, maybe even an introduction of what the travel rule.

Michael: Yeah. Sure. So the travel rule at the FATF level is it's similar to the w what it is at the U S in general, which is that for certain transactions among parties, if you're a virtual asset service provider, you should be collecting information. About the originator and the beneficiary and transmitting that to the other party which should be, it shouldn't be another VASP.

And certainly that's how it is in the U S and I think part of the issue of debate with the travel rule at FATF and in the U S but as well has just been in the crypto space. It's not like the Fiat world where there's always another side of the party at another bank or financial institution.

You, you could actually have transactions with on hosted wallets. And what do you do about that? And so this is something that, that fat has been grappling with the U S it's largely at this point, settled, but there's an open rulemaking, but it, in terms of the travel rule itself, as it has existed in the current form is that it's vast of ASP and that's your obligation to collect and transmit.

There's a, there's a wallets rule and there's other things that we can talk about, but none of that's in existence right now. I think for FATF one thing that they did that I think is good and also matches close more closely to the U S. Was that they from the March draft they did limit we were clearer now to say that transaction fees related to virtual asset transfers are not in the scope of the travel rule.

So you don't need to identify the recipient of transaction fees. Sounds like a, sort of a small thing but in the crypto space, it's one more thing that has clarity about it that we can move on. I think that would have already been the case in the U S but it's just helpful that they have that in there.

And I think they also, they did try to clarify. Some of the on hosted wallet and VASP interaction piece of the travel rule. It's not quite as clear as I think it stands right now in the U S where it's really vast of ASP. And so they, they inched closer in that. They said, okay, in the case of an unhosted wallet, you still need to collect it.

So you need to go to your customer, whether it's the originary Raider or the beneficiary, and still get the information about. Who it's coming from and where it's going and the amounts and that sort of thing. But you don't need to transmit it. If there is an Avast on the other. Whereas in the U S at least right now you would, it would just be a vast Abass, there's the open self hosted wallets rule that, that could potentially require some collection of that.

But that's an open rule and remains to be seen. So I think it did advance things in a positive way to have some more clarity. And I think the question now is well, what do you do with this sort of collective. From your customer with relation to self hosted while it's that you wouldn't normally have in a Fiat world.

And I think that's a piece where you're, you'll see advocacy in the next couple of months, like whether it's with FATF probably, and also with the jurisdictions that might be impacting. And

Eric: so one thing that's interesting, maybe we could touch on a little bit is FATF is largely, a lot of people would say FATF is a construction of the U S right?

That the department of treasury was one of the major drivers. Certainly one of the major influencers behind it's a worldwide organization, but it was something that effectively the U S sort of drove to too many ways, relating to dollar adoption worldwide. AML around it. So if the us isn't adopting, on hosted wallet rule for on hosted walls, the travel rule, where is the push coming to take a stricter view potentially?

The guidance is it the U S saying, yeah, let's just make it aspirational there or is it like, we'd love everybody else to do it, but not us or are there other people pounding the table saying we have to do this? Like where is the deviation? I'm not saying it has to be a tool of U S policy, but why?

I don't like where's the stricter component of it, coming from. Yeah,

Michael: it's a good question. There's well, there's I think with any multilateral body it's, nothing's run by one. And and you know, China was the president of. In the proceeding year after the U S was when this, when the travel rule stuff kicked off in this past year, I believe it's Marcus plier from Germany.

You know, there is, it's not, it's definitely not just a, a us tool. Certainly in the Genesis of it, it was very. But you have a president at any given time. That's not the U S and if you look at the full horizon of the issues that fat is dealing with, which is way beyond just crypto you know, the, this guides itself as 103 pages and it's, and a lot of.

Even beyond crypto even though it's explicitly on that virtual assets. So I think what you get is like with any virtual, eh, any multilateral body is that there are things people care about and they're willing to really go to the mat on and things they aren't. And I think in something like the self hosted wallets issue, I don't know, having not been there, it Switzerland for instance, is decided that.

Tougher on self host as well as then the U S is like pretty meaningfully. You know, you cannot, the, the general rule is you may not send from Avast to a self hosted wallet with the exception that it can be your own. Which you have to verify. And there are some other jurisdictions that have adopted that approach, which the U S has not.

And so that may be, I don't know that it was Switzerland, China, which was the president before. When, when a lot of this was being developed, leading up to March as well. Is pretty negative on, on crypto and independence about this too. So they could have pushed for that. And it really can be really any country that just says, that's my thing.

I'm going to expend all my capital on the one thing and everything else I don't really care about. And I think you see that in general, because even the U S isn't going to want to, nobody wants us to be look like it's one countries. And so even if. The U S and you feel like geez, that's the 30th thing that I'm trying to push on.

And I'm now I'm getting pushback that this isn't just a tool of the U S and so I can only pick 19 things or whatever. I think there's probably more play in it than expected, but I do think sure, when the U S was president in particular, you set the agendas and things like.

Eric: Got it. So moving on to the definition of virtual assets in virtual assets, service providers in this guidance, the virtual asset covers it's pretty broad any digital representation of value that can be traded or transferred.

That's how it's. That's pretty broad. What do you think about these definitions? Yes, very

Michael: flexible. I think they can't be wrong. Yeah, no, I think on the virtual asset definition it's super, it's super broad. I'm not actually that surprised because it's not supposed to be a rule.

And I think if anything, they're just messaging. Hey guys this could be anything. Actually it's interesting to me that they limited it to didn't. I think there were, there are folks in the U S in particular at FinCEN that have. Virtual means it's it could be anything. It doesn't have to just be digital.

Theoretically. It could be a representation on a napkin, makes it virtual and not an actual asset. And um, I think they would, they'd take even

Eric: more changes, killed a whole napkin token economy.

Michael: I, something tells me now it's a security, but we'll see. But I think, but I think, I think it's more of just them indicating like, This is all could be pretty broad.

Interestingly, like they, they carved out central bank, digital currencies from that and set them in a higher pedestal, but not, that was not that surprising to me. I more surprising to me was the vast definition and virtual assets service provider. Which was similarly expansive, but that one I think is tougher and it makes it tougher to build.

From on the one hand, it's not surprising. They took a very functional approach, which is how fence and also takes it, which is don't. Tell me what you are. Tell me what you. And I think overall, this goes into the defy aspects of the guidance. There's a certain calling out of the dyno decentralized in name, only aspects that you see in some projects, which is not surprising at all.

I think that there's been a little theater around that, but I think part of the problem is in, in trying to correct for that, there's a bit of an overcorrection on some level though, in fairness, it's not a rule, it's just a. Binding guidance, but they, they define this as any natural illegal person that's doing activities or operations on behalf of the.

And in, in the exchange of assets transfer and which sounds generally fine and functional approach rather than than, uh, what you call yourself makes I think a lot of sense, the part that I think is confusing and makes it difficult for people building is that they talk about conducts these transfers and exchanges, and that includes the provision or active facilitation of service.

So on the one hand they did scale back from the March guidance, which talked more about, just is involved with which really is so broad it, and they actually included marketing and sort of things like that, that I think are helpfully scaled back in this new guidance, which is good.

And I know they're trying to play to jurisdictions that want to implement in their own ways. But when you talk about conducts being defined as provision or active facilitation of a service, there's a question of okay, great. But what is that here I am, I'm building something, I'm with a stealth project right now, that's working on configurable, privacy and auditability.

And we want to obviously do the right thing. You know, immediately folks are saying great, what's active facilitation. Is that

Eric: they even called out, yeah, they even called out multisig on smart contracts. That's yeah, that was a little bit shocking.

Michael: Yeah, I think so. You know, what is that exactly?

Like? What, what's the factor test? I think what would be great is some sort of here it is, here's the piercing, the corporate veil kind of question or whatever that you have in corporate law. Here's what it is. So I do think that sort of active facilitation piece is going to be.

The big question that folks want to, we need to dig into and say, okay. And actually I think this goes to all of the FATF stuff. And even regardless of fat of just engaging with regulators, like I think it would be great for industry to come back and I include myself in that and come back. Yeah. Hey we've drafted our own FAQ and here's the answer we propose, what is active facilitation.

Here's what it is. We think it's, these five factors and we weight them in this way or whatever. It's always going to be facts and circumstances, but I think having more clarity of what's facilitation, would be, would be really helpful in getting people that want to do the right thing out there, because what you don't want to do is have people.

Okay, then I'm just going to put stuff out there and drop it and walk away and minimize risk to me while maximizing risk to users, because I'm going to leave it on the side of the road versus be there at the launch and do more to make sure that there isn't a massive exploit and keep a key for a little while, or be more involved in the test net for a little long.

Things like that or just have people that say geez, I'm part of a Dao and there's a multisig here so that we can address like exploits. But how do I do that in a way that isn't going to make us actively facilitating when we're actually just helping people and not making money on it or not controlling.

And don't have the admin key that sort of.

Eric: Alright, admin keys, a big one in the decentralization debate. So I guess we're shifting into the defy. There's a number of things to cover here. Particularly along the functional test, as you started to go into, there was a paragraph in there's a few paragraphs that were interesting.

One specifically called out creators who may control or as you noted, sufficient influence may become themselves of VASP. Is that a surprise?

Michael: Well, it was not a surprise on some level. I think it goes to the disorder, the decentralized in name only piece when it was a little surprised that there wasn't more meat on the bones for it so that people could say, okay, here's what it is.

And I think particularly the sort of sufficient influence piece, I wasn't that surprised to have them call. So the governance piece a little bit, and I think to some degree, they're looking at well, sure you decentralize it. You gave out tokens and now here's an entity. You guys retain 70% of them and you can basically come up with your own proposals and make and do everything you want.

And sure. It's decentralized in name, but you could, you can push through anything you want. So I do think there's a call out to that. But again, like how that really, what that really means in practice. Even if you have a, let's say, even if you what is the critical mass? Is it 51% of the governance tokens?

That may not still be enough to pass a proposal depending on how you weight your voting. The, the, I think the evolution and the governance. And decentralized projects and dowels is phenomenal right now. And people are trying to figure out, do we do reputational waiting? Like how do we do this?

How do we democratize this in the, in to the maximum degree, in a way that's also effective? Because if it's truly just like a million people get a vote that can be very complicated to, to actually get something done or address an exploit. But how do you do that in a right way? And, folks like Gabe Shapiro and others that are doing so much work on the governance piece is really important.

So let's empower folks like that, that are thinking in really creative terms, like quadratic voting and all these other things that are gonna allow us, allow them to build to it, but also effectively so that you aren't just pushing people to say no, really just drop it on the side of the road.

And people will fend for themselves. Let's advance the governance piece and figure out like what are you really concerned about when you say controller sufficient influence? Is it really just this sort of decentralized enabled? Where it's clear that somebody has got an admin key or they have 90% or 70% of the governance and they can just do whatever they want or is it like a circumstances of intent?

And, I think they speak to there's elements of that where they talk about whether you're getting fees back and your ability to make the decisions on it. Sufficient influence. Isn't really a term that's in any sort of existing regulation or law that I've seen. And so if you're going to be a good actor that wants to build to this, I don't really know how you're going to do that.

I think the good news is like all of this guidance, the, you the there's no, this has to be turned into a rulemaking. If the U S was going to actually implement it, which would, be. It would happen in a way that actually I would love to see fat a function, which is a public rulemaking.

You get noticing comment. Everybody gives their comment. If it changes meaningfully based on incorporating the comments, it comes back up for notice and comment again. And there's a requirement that the entity address all the comments. And so if you had this as a rule making in the U S they would be defense and would be required to say, Everybody gets a comment and we're going to address all of them in the next iteration.

And if it's changed, meaningfully, everybody gets a comment again, which I think is the way it should go. And that's what gets people to get it right. Because we all get to spot the collateral impacts that somebody couldn't see fat, if it's there was a public comment period, and then they did a closed door, picked a few people.

And then they decided what they were going to take, which turned out to be more of the technical stuff and less of the policy stuff. And then just put it out, which I think is not a great, it's not the best way to inform people, including yourself. Who's the drafter at the time. So I would love to see that more, but, that's what would come at least in the U S I think that's the question.

And when we think about other jurisdictions, like you said, that just may take this and say, all right, let's do this. And they could make it whatever which could be. And I think some people including mark, I think boy around have looked at this and said, I think the default at this point is probably that everybody's of VASP and you're all on the hook.

And so you're going to have an intermediary or function like an intermediary and which, that's not maximizing the benefits and efficiencies of crypto. So I think getting that sufficient influence piece defined is going to be a key next. For

Eric: everybody. Right. Did, did, it did seem to be you know, when they, particularly, when they talked about peer-to-peer they did raise the notion of intermediaries.

He said it was higher risks, which was good news because it, it, it wasn't as firm, but yet they talked a lot about intermediaries, which kind of says, Hey, this is where we're leaning. Another thing that came out on the defy before we jumped to some of the other items and Mark Boiron also brought up.

Which was the notion of a risk assessment for the, you know, the, the use of an automated process for smart contracts to carry out those functions does not relieve the other parties of, for vast obligations. That was a, that's a very broad statement. What are your thoughts on that? Yeah,

Michael: actually, I'm glad you brought that up.

I'm not sure exactly what's meant there or aware that where that. Drops off that obligation. I get it, my supposition without having been there is what they're trying to get towards is this idea of and you heard people calling for this, I think in this sort of DM space, as well as people have said, look, build in risk mitigation at the stage that you're building it in.

So be thinking about risk. So I think the most generous well-meaning read of that is we just met. Look, if you know that you're putting out a protocol, that's going to be used for financial issues. Please, can you not address some of the risks, like thinking forward, even if you're going to put it out there and it's going to run autonomously, which is a sentiment that is, that sounds extremely reasonable.

It's just the way it's worded it. W I don't know what that means. And what the obligation is. And when does that obligation ever end or, and I think the least charitable read of it. Is what they're really saying is yeah, nothing's impossible, but you probably can't do it. Because you need to basically, it's basically sure you can build it in as decentralized, as long as there's uh, an automated intermediary.

But if that's what they mean, you mean an automated intermediary. That's like a smart contract functioning as a blacklisting system, that's automatically bouncing things that are, that have been deemed high risk or a blacklisting API of some sort, then just. If that's what you mean, but I think there's no clear path in there of okay, I want to do it.

How do I do it? And where, what is the line? And, and that's, and again, I think that's a spot where the ideal, I think is is we as industry go back and say, okay, here's my FAQ. What does this mean? I think it means this. I think. Did it, it did. And, and here's the best practice. How about adopting that?

Eric: So shifting gears a little bit to, to preserve your time, they talked about NFTs they said NFTs are not considered virtual assets, except when used for payment investment purposes or to transfer value. Who's going to enforce this. If you adopt this language, what are you going to do as a country?

What are you going to tell your enforcement body to do around NFT?

Michael: Yeah, this is a, this was an interesting one. I think on the one hand, it's not surprising because I think you see, art itself can be used to launder money. And so I think to some degree they're doing making a nod to that. And then to some degree, making a nod to the fact that, Hey, everybody says the thing that's groundbreaking about NFTs is that they're multifunctional.

They're programmable. They're going to revolutionary. They revolutionized the way that you can fractionalize ownership, unlock new ways of transferring property. Or membership in groups, that sort of thing. So in that sense, it's, it's not surprising that the issue was broached because it is a more liquid way to transfer all kinds of things that are not that you wanted to be non-functional fund non fungible, whether it's art or a representation of property or something like that.

So I'm not that surprised about that. It's more just that it's so general. I don't know what you do. Other than you know, I think in the U S there's already, art is already a potential money laundering vector that that the U S department of justice has looked at, money laundering through art before and done some cases on it.

So fat or FinCEN was, it was originally tasked through the AML act to look at, do a study on arts and antiquities in the, in the process. It became just antiquities. I think probably. I won't speculate on lobbying, but let's just say that fell out and it became antiquities. So I think you're right.

It's on the one hand, I'm not surprised, but I don't know how you, if somebody gave this to FinCEN and said, okay, enforce it. They would say I'm probably going to need to do a rulemaking. But I think what you'd get is in the reality is you'd get the edge cases where it's. We have demonstrable intent that this oligarch over here was just laundering hundreds of millions of dollars through what was clearly art, that he had no interest in collecting.

And some of that you may see, which is a, it's an old school money-laundering is just, somebody puts up a piece. That Bobby drew. And they're like, yeah, I'll buy it for a hundred million dollars. And, and stiff gets just traded. That's clearly not worth it. And there was even some money laundering that would happen in the early days of iTunes where somebody would try to, they put up a, like a dummy album and people would try to buy.

$50,000 worth it. So the money just went and it was laundered through iTunes or something. And that quickly becomes not scalable. Right. But I think you'd see, you'd look for edge cases. The problem which goes back to the other issues is this is a, such a rapidly evolving area that, that has so many creative uses.

That people see this and they freeze up. And so I think this is another one where it'd be great to put in our own FAQ or get more clarity on of well, what do you really mean? You mean when there's demonstrable intent? Like a sort of criminal intent. Okay. That stuff happens all the time, but what, what is it that you mean?

Eric: This is something that they probably should be well advised to go slow on since it's the NFT. Getting it wrong could have a lot more unintended consequences. I think given all those potential use cases, right? I would love them to,

Michael: I would love to see them do a whole series on NFT of public consultation.

There's just so you could go and crypto Twitter, like any day and learn something new of what NFTs can do. So like why not have a whole series of learning in this space?

Eric: Right. I think it's early days. I think countries would be poorly positioned to try to adopt this because it's just too broad, too undefined.

Michael: Yeah. And your, and you'd be taking away, what's a key piece of NFTs, which is like everything on blockchain is the auditability. You have art pieces that disappear. For generations or, and including the Nazis, like stealing art that you know, is still getting re returned. And here's like a provenance.

I mean, there's just so many for property ownership. There's just so much uses that, that I think you could spend months on. And to get it right.

Eric: And maybe they're not trying to get it. Great. Maybe that certainly that's the hope. I don't know how they could. So shifting to stable coins can be vast if a settled developer or governance body that covers out that carries out management functions.

Sounds broad CBD. Are they off the hook? They're Fiat's or they're covered elsewhere but w where did, where does it, if you're a CBDC are you saying I'm glad I'm not covered by stable coins. Are you saying well, I'm kinda bound by almost the same thing elsewhere. Yeah, I think you're, I think you're saying analyzing the CPDC.

Yeah,

Michael: no, I think it's, it's broad and you're, there's so much open here. I think they're just, they're even probably seeing what's playing out in the U S and feeling like we're just going to keep this really broad. I, it interesting the way they carved CBD seas out, but, if it's coming from the sovereign authority, I expect there were some sovereign authorities that said, don't tell me what to do.

And so this does leave it open for them to be slightly carved out to the side. And maybe that's a positive thing to separate them out. I think that it's really important to have the option optionality of privately issued currency in this space that can provide different options for people.

And I think there's so many versions of CVCs out there. Some of which would be purely. Settlement mechanism that wouldn't even really touch retail that, that stable, that privately issued stable coins then could go, the, the last mile piece of it and provide that additional privacy that, which I still think you've you obviously have to build in privacy to central bank digital currencies but you could create a greater amount of faith in that privacy as well as optionality.

And by the way, speed by just setting clear standards for folks that are already out there too, to interface with, I take a lot of the stable coin stuff to be addressing the tether issue in general, which is what's it really backed by. And I think there, even if they say this is an AML document, I think in general, governments are mainly worried at first aside from China with.

Capital flight issue, I think at least, or the U S they're much more concerned at stable coins in terms of the what's it really backed by. And is there going to be a run that's going to get laid at our feet at some point than they are even the AML.

Eric: So our CPDC is getting a free pass in that regard.

Yeah, that's a good

Michael: question. I just think, I think the CBD C's are going to be subject to so many multilateral discussions because everybody's concerned about how somebody else's Fiat, somebody else's currency is going to impact their. It's going to play out on a different level. Whereas the, cause the idea is well, the government's going to discuss with the EU when we're rolling something out and vice versa.

Whereas if it's just tethered or anybody can just come up with something and say, Hey, it's got a backed by some stuff. We'll let you know later. We've spent, I don't know how many years trying to figure out what tethers back by. I think it's not to pick on them. It's just, it's out there in public records that it's taken a long time.

I think it's now beginning a lot more transparent but that's what I take a lot of this.

Eric: But there's you know, does this incentivize like a stable coin or ripple to get to go to, let's say Vanuatu and I'm picking up an idea, but doesn't have to be in say, listen, I'd really rather this just be a CBDC out of an ad to let's just do a public private partnership and, we'll make it ripple then add to, I know it's crazy.

But what you know is that, there may be an incentive for that anyway. Do you see the guidance evolving in such a way where it actually becomes more, more compelling? Yeah, that's

Michael: interesting. I don't know that played it out that far it's possible, but I think the, I think if you're a ripple the regulatory protection you might theoretically get, because this is just guidance, there's not even a recommendation for sure.

And you've still got all those touch points to the. So you're still going to be subject to whatever the U S rules are, which, and I don't think this is going to undo rules in the U S that's for sure. I mean, yeah, FATF past or made the formal recommendation of beneficial ownership in 2003 and it's 2021 and we're still working on it and not in a sense of being slow, there were political decisions deliberately made through Congress and various administrations that were not going to do that yet. So I don't think people are going to take in the U S certainly take a piece of guidance and say, all right, we're changing it. And if you're ripple and you're getting Vanuatu to adopt, you'd be there digital, current, like how many people are really using.

I don't even know what the currency I should know, but I don't know what the currency of want to watch it is. Now, if it's a, if it's a dollar peg. If it's a dollar peg, if it's dollar peg currency, that's a different story. If it's a backdoor into, to being like, sure, it's this other jurisdiction, but it's effectively follows the dollar.

I think that would be an interesting different development. You'd get bilateral. I suspect Vanuatu would get some immediate direct bilateral input from the state department and treasury,

if

Eric: that were the case. I'm sure to finish up on two things here. Cause I know you've got. One is P2P. What was your thoughts on the peer to peer guidance?

It seemed actually marginally favorable.

Michael: I, I think it's not that surprising. I think they, on the one hand it is positive. Like you said, like they, they stepped back from the de-risking the full de-risking, they said it's risky, but, in the March guidance they had, they suggested that vaster.

Not or countries should consider denying the licensing of vast if they even allow transactions from non obliged entities, which they mean is private and on hosted wallets. So I think stepping back from that was very positive because if you're going to actually use a decentralized and democratized financial system, you've got to allow people to make those choices.

And by the way, I think as somebody who spent time at Jane analysis and also at treasury in this space, The idea that you can't mitigate risk or address it on a massively auditable public ledger, where you can see transactions practically indefinitely in every direction versus, a Fiat system where at most you can guess which banks to subpoena and then, and hope you get it right.

And that you can get information. It just doesn't make sense to be that harshly negative on, on peer-to-peer transactions, particularly when they're also saying in other places like, Hey, you should be building in a measure of risk mitigation. So it's still, I think there's still with the travel rule piece that they're keeping that's not like the U S they're still collecting, asking you to collect information and you still have places like Switzerland that are going to be tougher on it.

But at least they came back from the full de-risking. I think it will just be on us to keep engaging on them of Hey, look, this is, there's a lot of risk mitigation here. I'd much, most law enforcement would rather do a case with crypto than with Fiat. You're talking about like getting on a public ledger and finding exactly.

In minutes which VSP do you want to subpoena versus guessing which bank might have a correspondent that you can send a subpoena to might have a correspondent relationship with a bank over there that we assume it might be because that bank does a lot of business in that region. That's a, that's a five to seven year process to get mutual legal assistance treaties and data privacy issues.

Whereas it's like, Hey, here's the welcome to video case. 70 jurisdictions or whatever. I can tell you every vast that was involved and I can go right to them with a public ledger that says, this is the, this is what I need. So I it's, it's silly to say that you can't manage risk in this

space, things real quick.

What's the guidance definition of ASPs, a good news for minors and validate. Ah,

yes. Yeah. I think actually they, they took, this is FinCEN took this position in 2019, explicitly in the guidance that these are, that this is not Abass if you're just verifying transactions, that's not, you're not of ASP.

And I think that clarity is welcomed for

Eric: sure. In reference to closed loop systems. Was that a positive? Not a surprise.

Michael: Yeah, I didn't, I actually didn't even spend much time on the closed-loop systems one.

Eric: Okay. So it says the FATF similarly does not seek to capture the types of closed, loose loop systems that are non-transferable non exchangeable and cannot be used for payment or investment purposes, airline miles, credit card awards, or similar loyalty program rewards or points in which an individual can not sell onward in a secondary market outside of the closed system.

Michael: Yep. Yep. Your airline miles are still saying.

Eric: But it could be very valuable for like social tokens and other networks where absent the clarity it could raise just you know, cause obviously it's not, this is not about airline miles. This is an example, everybody references, everybody goes to airline miles and say, Hey, we're like airline miles.

We're like Disney points. Th th the uses are evolving.

Michael: Oh, for sure. I think. Most interesting is going to be to where people take this example and clarity and even with DAOs and NFTs and deciding okay, I think it's Lex DAO has a non-transferrable token that allows you to vote, but you can't transfer it out, and I think there's going to be continuing evolution in that space. And I will say and FinCEN was, we were, when I was there in 2019 doing the guidance, like we were very deliberate about saying. Even if it's a risk, we want to specifically carve things out that we don't. Have jurisdiction over so that people can build in it.

And, we can expand as we need to go as risks evolve, but we specifically right away said miners and validators, no software developers. No, let's draw some lines of things that we don't think are covered so people can move forward. And I'm glad that fad has taken that position.

'cause he like we're sitting here right now, already brainstorming like, oh, that opens all sorts of creative things that, that also maintains the risk management, but it allows people to think really creatively. And that's the promise of this space is to be, is that sort of financial expansion and the democratization.

That's going to bring more people in to do that.

Eric: All right. So I know you have to go and I'm not going to get in trouble with your other engagement. That wouldn't be good. We have to have you back on the show. Now I don't know if I emphasize this. Michael is part of a stealth project known as. T I'm just calling a T and at some point we got to bring you back to talk about stealth project T if you miss that episode, you'll forever regret it.

But anyway so, so before I let you go, maybe one sentence to describe your reaction to the I didn't warn you, so this isn't fair, but I'm giving you a little bit leeway. One sentence to describe your reaction to the guide. Yeah, I think

Michael: it was, I think it was on the one hand, it was frustration.

It was relief that it was just guidance and that it didn't go further in a negative direction in terms of on defy, because I think there's just so much opportunity that can be created. While managing risk. And the more you fence people in from the creative building in that space, the more you're going to miss out on the opportunity, but also frustration that there wasn't more of an ongoing notice and comment and and addressing comments that people gave that weren't implemented.

I feel like as if we're public servants and we're getting one, it's our job to serve the public, which means getting their feedback to get. And then when we don't take their recommendations too, to say, Hey, we didn't take this because of this. And I think if you want the best answer, you engage in that discourse ongoing.

I know you have to stop it at some point, but I think I would love to see it in more of a and more of a notice and comment and rulemaking the way like a FinCEN would do.

Eric: Yeah. It's too important. It's way too important. It's, this is not a passing fad. So anyway, Michael, this was great, and I look forward to having you back on the show and talking about stealth project T.

Michael: Thank you, Eric.

Eric: Thanks so much. We'll talk soon.

Michael: Thanks.