NO MORE MONKEY BUSINESS: COMBATING THE RISE OF DIGITAL NFT MONEY LAUNDERING THROUGH AN EXPANSION OF THE BANK SECRECY ACT

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The COVID-19 pandemic proved to be a boon for digital currencies and assets, particularly for non-fungible tokens (NFTs), which gained massive prominence and skyrocketed in price during 2020, 2021, and 2022. With this frenzied market reaching its peak during late 2021 and early 2022, NFTs were regularly selling for millions of dollars. Because of the massive amount of money to be made in this relatively unregulated wild-west market, legitimate creators and malicious actors both jumped into the NFT space seeking to capitalize on a market hungry for NFTs. With millions to be earned, NFTs started to be regular fixtures on the secondary market for resale, where owners and creators stood to earn many multiples of their initial investment. Despite the tremendous amount of capital diving headfirst into this novel industry, government regulation and guidelines surrounding NFT transactions were and remain relatively limited.

The focus of this Note is on the capabilities and historical similarities that NFTs share in common with other regulated art-adjacent industries. Because NFT marketplaces operate in a similar manner to modern-day art and antique auction houses, it would likely be wise for regulators to place similar regulatory frameworks on these digital asset traders. Without the proper safeguards, this promising new industry in its infancy will become overrun by frauds, scams, and criminals taking advantage of everyday Americans. As this Note recognizes, this has already started to become a reality: NFT scams have proliferated due to lack of regulation and criminal actors have been able to make off like bandits. Given the importance of safeguarding Americans’ capital and financial security, it is imperative to understand how appropriate legislation and regulatory action could prevent future frauds.

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INTRODUCTION

In early 2022, the burgeoning digital art market had reached a fever pitch in trading volume, eclipsing the previous year’s amounts by nearly five times.\(^1\) Drawn in by the promise of quick and substantial returns, millions of new buyers flooded into this market, primarily drawn to exchanges like OpenSea where they could quickly and easily exchange cryptocurrencies for NFTs.\(^2\) Billions of


dollars were exchanged seemingly in the blink of an eye, lending credence to the idea that the NFT craze was the 21st century’s gold rush. This gold rush rapidly accelerated with the rise of NFT collections made up of computer-generated images; seemingly overnight, many of these collections became worth thousands, if not millions, of dollars.

One of these new NFT collections was called Frosties, a group of flamboyant ice-cream-scoop digital characters draped in silly outfits adorned with wistful facial expressions. Everything pointed towards success for this young NFT community, with the collection’s founders promising to create merchandise and a centralized fund to ensure the project’s longevity. Nothing before or during the Frosties release pointed to the self-destructive behavior that would happen later that day. Just hours after Frosties debuted its mint, the collection’s Discord server, its main avenue for communicating with buyers, sellers, and holders of the collection, simply vanished, along with the website associated with the collection. Discord moderators, who acted as unofficial staff members helping to police the community’s Discord server, were also caught off-guard when the server went offline and had no answers for frantic purchasers. Hours later, buyers’ worst nightmares came true when the official Frosties Twitter (now X) account confirmed the collection was a front for a scam through a tweet that simply read “I’m sorry” before permanently going offline.

The scam perpetrated by the creators of the Frosties NFT collection is called a rug pull, whereby the creators of an NFT project promote it up until its mint, and immediately shut down the project once the mint ends, making off like bandits with funds siphoned from the mint. In the case of the Frosties collection, this amounted to a cool $1.3 million.

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4 Id.


6 See Pimentel, supra note 2.

7 See id.

8 See id.

9 Id.

10 See id.; Beyer, supra note 5.

11 Beyer, supra note 5.
One might think that the type of fraud perpetrated with the Frosties would be policed by the digital art exchanges that control the NFT market. These exchanges, like OpenSea, describe themselves as “accessible marketplace[s]” where users can interact with the new frontier of the digital art market. OpenSea boasts about its industry backing, positioning itself as a reliable and reputable exchange. However, much of the responsibility of security and safety is placed on the platform’s users, with scant help, resources, and an almost non-existent support infrastructure. Most tips about safety come from the community itself on forums or social media, where activists often post warning stories and tutorials for keeping oneself safe when engaging with exchanges like OpenSea and NFT projects. Instead of fostering a safe ecosystem for a booming industry awash in venture capital funding and cash from fees, OpenSea has chosen to create a platform that is frequently abused, and reportedly often does nothing to alleviate problems encountered by its customers.

This Note brings attention to an unfortunate reality of the burgeoning digital art market: the experience of the Frosties buyers and many other NFT collectors is rapidly becoming the norm, and not the exception. Digital art marketplaces rarely protect users through virtuous Know-Your-Customer (KYC) regimes, leaving the platform and its users vulnerable to technically skilled criminals. To compound the challenge, Congress recently passed the Anti-Money Laundering Act of 2020 (AMLA), which, ironically, explicitly

14 Id.
excluded coverage of art, likely exempting NFTs from a significant route for oversight and government regulation. Throwing caution to the wind comes even as NFT and cryptocurrency related rug pulls have skyrocketed to a massive proportion of cryptocurrency crimes.\footnote{See Chainalysis Team, \textit{The Biggest Threat to Trust in Cryptocurrency: Rug Pulls Put 2021 Cryptocurrency Scam Revenue Close to All-Time Highs}, \textsc{Chainalysis} (Dec. 16, 2021), https://blog.chainalysis.com/reports/2021-crypto-scam-revenues/ [https://perma.cc/3XKN-49GJ].} Refusing to expand definitions enshrined in the Bank Secrecy Act (BSA) and the application of the AMLA will only lead to a continued explosion in digital crime, hurting American consumers and lowering confidence in the digital ecosystem.

In Part I of this Note, I explain how the traditional art market has always been a popular route for money laundering and include a brief history of how auction houses have historically facilitated and continue to facilitate illicit money-laundering activity. In Part II, I explore the current regulatory playing field for anti-money laundering measures, particularly the recent expansion of the BSA under the AMLA, and how these novel regime changes are already working towards severely handicapping traditional black-market money-laundering techniques. In Part III, I analyze how online digital art auction houses selling NFTs have played a largely similar role to traditional art auction houses in relation to facilitating the process of cleaning dirty money. In Part IV, I investigate legal ramifications of further expanding the BSA to digital art marketplaces as a way to prevent crypto-crimes, mainly related to NFT money laundering. I argue that the AMLA must be viewed as only a first step towards neutralizing the pervasive money-laundering black market that currently exists in the art marketplace, and needs to be revisited in order to expand the BSA to encompass the high-volume and high-value money-laundering system of high-priced artworks, with provisions specifically tailored towards combating digital art money-laundering practices. Further, centralizing the KYC ecosystem for NFTs, and other digital assets in the future, would help protect American consumers and promote safe growth. Finally, Part V identifies and addresses likely criticisms of the suggested regulatory regime and provides explanations as to why implementation issues for this solution are likely to be blown out of proportion.

The goal of this Note is to comprehensively analyze the current status of anti-money laundering regimes and to recommend the best next steps for combatting digital art money laundering. This Note does not directly address whether cryptocurrencies themselves are a
common and popular avenue of money laundering that should be addressed by further regulation; instead, this Note focuses on the money-laundering techniques utilized by digital art scammers and criminals that use cryptocurrencies as a stand-in for monetary value.

I. THE HISTORY OF CLEANING DIRTY MONEY

Money laundering through the use of high-value art to anonymously move funds is often discussed as if it were of modern vintage. However, money laundering using high-value art did not appear out of thin air, and is in fact a practice that has been ongoing for millennia, ever since the advent of monetary systems. Therefore, digital art money laundering must be understood by using historical background to contextualize the motivations and means of modern-day fraud.

A. Dealing in Secrets in Renaissance Europe

Many historians trace the roots of true money laundering in artwork to the Renaissance. While art was an object of fascination of the wealthy for almost all of humankind’s existence, the most realistic analogue to the modern-day high-value art market originated in the professional trade organizations in Western Europe starting in the early 15th century.\(^\text{19}\)

Until the Renaissance was in full swing, art was generally commissioned by a patron, a wealthy individual seeking to demonstrate his status or wealth through lavish art displays.\(^\text{20}\) Most art was commissioned up to this point through this patron-artist relationship and was generally limited to the ultra-wealthy because of the costs associated with patronage.\(^\text{21}\) However, as the Renaissance progressed, it spawned a growing wealthy merchant class, and the art market expanded to serve this growing potential group of customers.\(^\text{22}\) These early art markets—the closest Renaissance analogues to Christie’s or Sotheby’s—rapidly expanded as demand grew. While still relatively limited to the upper classes, art importation and trade began to grow, especially to increasingly wealthy men in Florence and Rome.\(^\text{23}\)

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\(^{19}\) See Graham Bowley, As Money Launderers Buy Dalis, U.S. Looks at Lifting the Veil on Art Sales, N.Y. TIMES (June 22, 2023, 4:17 PM) https://www.nytimes.com/2021/06/19/arts/design/money-laundering-art-market.html [https://perma.cc/9MB7-TND6].

\(^{20}\) Id.

\(^{21}\) Holly Flora, Patronage, 33 STUD. ICONOGRAPHY 207, 207–09 (2012).

\(^{22}\) Bowley, supra note 19.

\(^{23}\) Carol M. Richardson, Locating Renaissance Art 65 (2007).
This growing market was captured by artists at the time like Frans Francken the Younger, who often created paintings centered around the growing merchant class and art galleries.\footnote{See All That Glistens, NICHOLAS HALL, https://www.nicholashall.art/all-that-glistens-exhibition-checklist/frans-francken-the-younger-death-and-the-merchant/ [https://perma.cc/7W35-JBC7].} Francken commonly featured the shameless behavior of healthy art purveyors, frequently centering his images on people surrounded by extravagant artwork. Distinctively, Francken demonstrated the outrageous and decadent wealth that moved through the art world in his painting entitled “Death and the Miser.”\footnote{Id.} As was common in almost all of Francken’s paintings, the emphasis was on the ridiculousness of the new art consumers.\footnote{Id.} Another painting, “Gallery of a Collector,” arguably references the growing art market in more explicit detail, depicting a fictional art collector’s display room in vivid detail.\footnote{See Emil Kren & Daniel Marx, Gallery of a Collector, WEB GALLERY OF ART, https://www.wga.hu/html_m/b/baellieu/gallery.html [https://perma.cc/ASQ4-65ZW].} “Gallery of a Collector” presents a massive gallery room, stocked full of famous artwork from the time period, demonstrating the growing value and ease of acquiring art.\footnote{See Bowley, supra note 19; see also Kren & Marx, supra note 27.} It also shows the ease of keeping art private; both of these paintings only show the art being viewed by the wealthy patrons and characters who are likely friends or family. These paintings help depict how these private collections often remained secret to owners and the select few they wished to see them. While artists like Francken captured what was a relatively novel environment during the Renaissance, art galleries led by wealthy purveyors continued to grow in number and become a mainstay of the upper-class.\footnote{The Renaissance, ENCY. BRITANNICA, https://www.britannica.com/topic/art-market/The-Renaissance [https://perma.cc/8RZF-VHDS].}

A key facet of this burgeoning new art market was the standard of behavior and bookkeeping; generally, the sellers of art took great measures to conceal the identities of their clients and the prices that artwork sold for.\footnote{Bowley, supra note 19.} This secrecy was abetted by early Florentine accounting measures, whereby the books for each individual merchant or consumer were closely held, the information contained
within not divulged to anyone outside of close confidants.\textsuperscript{31} By combining these secretive accounting measures with an environment that discouraged information sharing, it is not surprising that early art sellers actively sought to reduce the chance that competitors might steal their clients, and were also able to protect against the possibility that clients might find out they were being gouged at checkout through the conscious choice of withholding relevant financial information.\textsuperscript{32} It further benefited these auction-houses-in-infancy to conceal customers’ names and deal prices so that they could later turn around and flip the same work at a higher price to a new customer.\textsuperscript{33} Keeping secrets was likely a large part of staying in business and keeping food on the table, and it is readily apparent why the rich liked to use art as a place to park wealth.

\section*{B. Old Practices Die Hard: Modern Auction Houses and the Art of Money Laundering}

The modern art market is no longer the completely secretive hotbed of money laundering that it likely was throughout history. Broadly, the market is relatively less secretive than it once was, and reputable auction houses often publish information about pieces of artwork, like the expected price range of a given piece.\textsuperscript{34} Some auction houses and dealers also have voluntary anti-money laundering requirements in place in an attempt to reduce the omnipresence of illicit money in the art market.\textsuperscript{35} But while some do collect documentation related to tax compliance and other voluntary measures, there are no comprehensive anti-money laundering requirements for the vast majority of U.S.-based participants in the art market and, therefore, no explicit legal obligation for these auction houses or dealers to proactively work to snuff out illicit

\begin{footnotesize}
\begin{enumerate}
\item Bowley, supra note 19; cf. Goldthwaite, supra note 31, at 612.
\item Bowley, supra note 19.
\item \textit{Id.}; see Selling at Christie’s, CHRISTIE’S, https://www.christies.com/selling-services/selling-guide/before-the-sale?sc_lang=en#your-sellers-agreement [https://perma.cc/XB8M-AM8P].
\end{enumerate}
\end{footnotesize}
activity and report it to the appropriate law enforcement authorities.\footnote{U.S. Dep’t of the Treasury, Study of the Facilitation of Money Laundering and Terror Finance Through the Trade in Works of Art 19–20 (2022).} Because of the lack of formal regulation in this space, combined with traditionally secretive practices, money laundering continues to be all-pervasive.

Generally, individuals flock to these art auctions because of several characteristics that are baked into the art market. In particular, the high-end art market allows for one-and-done transactions for high-value pieces. In addition, there exist extremely inexpensive and loosely regulated art transportation networks. Finally, the aforementioned long-practiced culture of silence in the market persists, where buyer and seller anonymity and privacy are held paramount over moral obligations.\footnote{See Fin. Crimes Task Force of the Antiquities Coal., Reframing U.S. Policy on the Art Market Recommendations for Combating Financial Crimes (2020), https://theantiquitiescoalition.org/wp-content/uploads/2020/09/FCTF-Report.pdf [https://perma.cc/C6NC-SBM3]; see also U.S. Dep’t of the Treasury, supra note 36, at 19.}

Auction houses today continue to embrace the private nature of the earliest marketplaces, helping to keep the art market shrouded in mystery.\footnote{Patricia Cohen, Valuable as Art, but Priceless as a Tool to Launder Money, N.Y. Times (May 12, 2013, 11:25 PM), https://www.nytimes.com/2013/05/13/arts/design/art-proves-attractive-refuge-for-money-launderers.html [https://perma.cc/M77B-NVRB].} This is especially obvious when collections are being sold from “private collection[s],” an all-pervasive moniker given to sellers who wish to remain anonymous for the transaction.\footnote{Bowley, supra note 19.} Not only do sellers remain anonymous, but buyers of the expensive artwork also often remain anonymous or try to evade the limelight through extensive means. When transactions are conducted through auction houses, the buyers and sellers are oftentimes simply listed as “private collection[s],” with their exact identities not disclosed to the other party involved or to intermediaries involved in the transaction.\footnote{Amy Castor, Metakovan, The Mystery Beeple Art Buyer, and His NFT/DeFi Scheme, AMY CASTOR (Mar. 14, 2021), https://amycastor.com/2021/03/14/metakovan-the-mystery-beeple-art-buyer-and-his-nft-defi-scheme/ [https://perma.cc/U9TL-RUE3].} For example, the buyer of Beeple’s “Everydays: The First 5000 Days” NFT hid behind an online identity.\footnote{U.S. Dep’t of the Treasury, supra note 36, at 20.} While sleuths attempted to dig into the supposed background of the purchaser, there were hints about who might have been behind the purchase; however, it was not

\footnote{36 U.S. Dep’t of the Treasury, Study of the Facilitation of Money Laundering and Terror Finance Through the Trade in Works of Art 19–20 (2022).}
until much later when an individual in Singapore identified himself as the person who bought Beeple’s NFT and was confirmed officially.\(^{42}\)

Not only do the rich and the criminal hide behind the guise of private collection sales or anonymous purchases, but they often also send representatives, friends, or complete strangers in their place as a proxy in order to preserve anonymity.\(^{43}\) Commonly, the ultimate owners behind any given transaction work through agents, who are under no obligation to inform the auction houses or sellers that they are acting on behalf of a different individual.\(^{44}\) For example, Saudi Arabia’s Crown Prince Mohammed bin Salman used another member of the royal family to successfully purchase Leonardo da Vinci’s painting “Salvator Mundi” for $450 million.\(^{45}\)

Some individuals have also resorted to constituting shell companies whose sole purpose is the purchase (or sale) of high-end artwork.\(^{46}\) Shell companies, due to their nature, are relatively easy to use as cover for purchases or sellers wishing to remain hidden.\(^{47}\) While these shell companies can exist for some legitimate reasons, such as protecting the reputations of the true owners in economic downturns or financial hardships, these shell companies are often used to help conceal both the identity of a buyer and seller, and help to shield the source of assets or funding from targeted regulatory oversight.\(^{48}\) Furthermore, shell companies provide high levels of anonymity because the beneficial owners are under no requirements to go through identification processes when the shell company is established or when related financial accounts are created and


\(^{48}\) *Id.* at 40.
funded.49 Because of this, shell companies are easily used as streamlined financial conduits for people who may not otherwise be allowed to purchase artwork in the United States, and can oftentimes operate without setting off alarms at financial institutions or in law enforcement bodies.50 Using these measures also help sanctioned individuals or criminals avoid further scrutiny by the auction houses, who may otherwise report their actions to law enforcement based on their voluntary (and highly ineffective) due diligence and KYC measures.51 In sum, the ability of shell companies to transfer funds and hold assets without intensive scrutiny is constantly exploited by illicit actors, which is not necessarily limited to the art market.52 Frequently, these shell companies also purchase other tangible assets to help launder the totality of their true owner’s dirty money.53 It is vital to point out that broad usage of shell companies might be circumscribed; included in the AMLA are provisions related to required disclosures of these types of shell companies, which implement beneficial ownership information reporting requirements that might help to pierce the corporate veil in a more effective way.54

However, because there are no anti-money laundering measures in place that are specifically tailored for the high-value art market, there are relatively few avenues for federal law enforcement to ensure that illicit funds do not drench the domestic art market through private, anonymized auctions and shell companies.

As one can imagine, the lack of regulation has given rise to a plethora of shady characters. Reputable art auction houses, like Sotheby’s, are frequented by representatives of sanctioned individuals, like the oligarch Rotenberg brothers from Russia.55 Despite Sotheby’s proclaimed voluntary anti-money laundering measures, a U.S.-citizen and art consultant named Gregory Baltser, acting on behalf of the Rotenbergs, successfully purchased multiple paintings for the sanctioned individuals through a variety of shell companies.56 This art consultant repeatedly patronized these auction houses, helping to wash tens of millions of dollars through reputable channels without the auction houses digging into the source of the

49 Id.
50 See id.
52 Id. at 22.
53 Id.
54 See id.
56 Id. at 78–81.
funding or questioning the veracity of his legitimacy.\(^{57}\) As demonstrated by this one example, it is relatively simple for high-powered individuals who are not allowed to engage with businesses in the United States, like sanctioned individuals, to take advantage of the lax regulations related to art sales.

Buyers and sellers interacting with high-value art can effectively remain nearly completely anonymous, even when massive amounts of liquidity are involved.\(^{58}\) The lack of transparency because of missing regulatory oversight makes ownership and transactions difficult to track; in a sense, art can become an “invisible asset,” as it stays in the personal collection of an individual and may change hands through multiple transactions without a financial institution ever being informed.\(^{59}\) These loopholes and the lack of stringent oversight enables this behavior and further presents a serious threat to the success of law enforcement efforts to prevent sanctioned or otherwise blacklisted individuals from transacting.\(^{60}\)

C. The Scope of the Illicit Art Market

The sheer scale of the art market begs for regulation, especially considering that money laundering is an increasingly common avenue for sanctioned individuals and criminal organizations to create portable value. As shell companies and representatives purchasing high-value art are repeatedly being exposed as fronts for more malicious actors, it is readily apparent that the current regulatory regime does not disincentivize illicit action as much as it should.

Broadly, the legal art market is a huge behemoth itself, drawing in tens of billions of dollars annually around the world.\(^{61}\) To put the illicit art industry into perspective, crime related to artwork (mainly high-value artwork) is estimated to be the third highest-grossing criminal trade when considering criminal activity over the past four years.

\(^{57}\) Id. at 78–82.

\(^{58}\) See id. at 36.


\(^{60}\) See STAFF OF S. COMM. ON HOMELAND SEC. & GOVERNMENTAL AFFS., supra note 35, at 147.

The art market is the largest unregulated legal industry in the world, with the companies responsible for the high-end portion of the market selling tens of billions of dollars of art annually. There has been a clear upward trajectory for the amount of sales in the art market broadly, corresponding to a similar uptrend in related art financial crimes. Recent estimates suggest that money laundering and related financial crimes routed through the art market amount to billions of dollars each year.

Several characteristics of the art market encourage illicit activity and money laundering. To start, the art industry in the United States is not required to comply with the requirements of the BSA. There are no structures or mechanisms by which regulators or law enforcement are allowed to audit art market transactions. While, as mentioned previously, auction houses engage in limited voluntary Anti-Money Laundering (AML) and KYC compliance strategies, there is no industry standard for this practice, and uneven enforcement of these measures allows easier access for criminals. These factors allow auction houses to operate largely unchecked and to accept money from individuals who should not be allowed to transact in the United States.

Similar concerns exist in the digital art space, specifically in relation to the buying and selling of NFTs. Industry insiders acknowledge the appeal of NFTs as vehicles for money-laundering and the reality that this practice is happening. Often, NFTs are one

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64 See U.S. DEP’T OF THE TREASURY, supra note 36, at 10.

65 Id. at 10–11.

66 STAFF OF S. COMM. ON HOMELAND SEC. & GOVERNMENTAL AFFS., supra note 36, at 36.

67 Id. at 37.

68 Id. at 36–37.

69 See generally STAFF OF S. COMM. ON HOMELAND SEC. & GOVERNMENTAL AFFS, supra note 35 (demonstrating how sanctioned individuals easily access the U.S. art market through auction houses).

of many methods for criminals seeking to digitally wash their funds; most commonly, NFT money-laundering has occurred in conjunction with related crypto-financial crimes. While the analysis of current NFT related money-laundering activity is limited, it is poised to explode with greater adoption of NFTs and the continued lack of regulations.

II. RECENT UPDATES TO THE ANTI-MONEY LAUNDERING REGIME

While there are significant loopholes in the current regulatory regime, it is important to acknowledge that Congress has recently taken important steps towards foreclosing the availability of another common method for money-laundering crime. In the last two years, Congress worked towards passing the AMLA, which successfully expanded the application of the BSA to antiquities dealers. The fact that Congress altered the application of the BSA is monumental; the BSA had not seen such “comprehensive reform and modernization since its inception.”

These reforms were likely spurred on by high profile cases. For example, Hobby Lobby used intermediaries from a variety of Middle Eastern countries to purchase thousands of ancient clay and stone artifacts originating from Iraq and allegedly related to biblical stories. In order to fill their family-run Bible museum, Hobby

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71 See id.


Lobby and its directors purchased these ancient artifacts through dealers in the United Arab Emirates and Israel over a period of two years.\textsuperscript{76} Because there were no anti-money laundering measures against the trade of antiquities at the time of this transaction’s settlement, there was scant required regulatory and law enforcement oversight. In fact, many of the items were originally seized only because Customs and Border Protection officials identified a handful of packages that were deemed to have packing slips indicating inaccurate countries of origin.\textsuperscript{77} Eventually, over three thousand antiquities bound for Hobby Lobby were seized.

There were also large social changes that likely pushed further adaptation. When considering the effect the release of the Panama Papers had across the globe, it is not surprising that governments, including the United States, have looked to take action against perceived imbalances in the economic world.\textsuperscript{78} The Panama Papers generated public outrage over the lack of regulation that existed, and the strong public opinion to move forward with new money-laundering and financial crime regulations likely contributed to the shift in sentiment seen on Capitol Hill.\textsuperscript{79}

The BSA takes proactive steps to modernize the existing anti-money-laundering regime by identifying previously unregulated transaction types that have been historically exploited to launder dirty money, transact with sanctioned individuals, or finance global terrorism; specifically, the BSA is now expanded to include individuals involved with antiquities transactions.\textsuperscript{80} The BSA’s expansion under this change is all-encompassing; the Act appears intentionally open-ended so that the Financial Crimes Enforcement


\textsuperscript{77} See Complaint ¶¶ 3, 41, supra note 75.


\textsuperscript{79} See id.

Network (FinCEN, a bureau within the Department of the Treasury responsible for analyzing information to aid in combatting financial crimes, including money laundering)\(^{81}\) can take the reins to create comprehensive guidance without the impedance of Congressional training wheels or other hurdles.\(^{82}\) The application of BSA requirements to individuals involved with antiquities deals is likely to be relatively broad.\(^{83}\) The definition of a “financial institution” under section 5312(a)(2) of the BSA is amended to include the following: “[A] person trading or acting as an intermediary in the trade of antiquities, including an advisor, consultant or any other person who engages as a business in the solicitation of the sale of antiquities . . . .”\(^{84}\)

Because of the vagueness of this expanded application, it is likely that dealers of antiquities are not the only people who are now subject to BSA requirements.\(^{85}\) In fact, it is likely that art advisors, art consultants, or any other type of intermediary who may touch the antiquities transaction at any point can feasibly fall under the coverage of the expanded BSA. Because high-value antiquities deals often include a litany of intermediaries to evaluate, grade, and otherwise ensure that the transaction goes seamlessly, this expansion is likely to impact a not insignificant number of individuals and businesses.\(^{86}\) In essence, all of the people who touch this type of transaction are now considered to be a “financial institution” for purposes of the BSA. These amendments to existing BSA language ensure that previous loopholes are not abused by individuals who are sanctioned or by terrorist or criminal groups looking for what amounts to legal funding.\(^{87}\) These changes also impose significant filing, documentation, and other related requirements on individuals covered under the expanded BSA who are involved with the antiquities trade, and they have effectively served to work towards limiting the effect of money laundering on the antiquities trade. It is notable that there have been some promising updates.

Despite these changes, there remain significant impediments to preventing money laundering in the art market. The Treasury’s recent publication, the “Study on the Facilitation of Money Laundering and Terror Finance Through the Trade in Works of Art,”

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\(^{82}\) See H.R. 2514, 116th Cong. (2019).

\(^{83}\) Blanco, supra note 80.

\(^{84}\) H.R. 2514 § 5312(a)(2).

\(^{85}\) Blanco, supra note 80.

\(^{86}\) See id.

\(^{87}\) Cf. Staff of S. Comm. on Homeland Sec. & Governmental Affs., supra note 35.
essentially dismisses longstanding concerns of money laundering in
the art market and proclaims that the art market is not a priority
because there are already some limited required disclosures for
individuals participating in the market, and there are other places
where there might be existing concerns that outweigh the illicit
money laundering happening in the art market. While an innate
aversion to a concentration of regulatory resources is understandable,
the illicit art market and the money laundering that proceeds through
it should not be allowed to run free pending better time management
and resource allocation from regulators; sanctioned individuals and
outright criminals regularly abuse the high-value art market
specifically because of this lackadaisical approach to oversight from
domestic regulators.

The current regime has improved, thanks in large part to the
expansion of the BSA under the AMLA. However, there is still room
for improvement, and continuing to build on the AMLA will help to
stem the flood of money-laundering schemes in the art markets.

III. MONKEY JPEGS AND FRAUD

Digital art auctions houses primarily transact through NFTs, a
crypto-asset based on the blockchain with a unique digital
signature. NFTs are different from traditional cryptocurrency
because each token has a unique identifying digital signature; they
therefore cannot be traded or exchanged with other users on a one-
to-one basis, hence their “non-fungible” moniker. Each token has a
digital file and an associated “smart contract,” whose code has a
specified set of strings that denote the method of the NFT’s
legitimacy. These NFTs are most commonly stored on the
Ethereum blockchain and have exploded in popularity over the past
two years as digital art has become a hot commodity.

In order to purchase an NFT, the most common method is to use

88 U.S. DEP’T OF THE TREASURY, supra note 36, at 34.
89 See id. at 21–23.
91 Id.
93 Conti & Schmidt, supra note 90.
a marketplace like OpenSea, an NFT auction house that acts as a middleman between prospective buyers and sellers. Prospective consumers most often have to use a cryptocurrency, with the most popular being Ether, the native cryptocurrency built on the Ethereum blockchain, in order to purchase NFTs through a marketplace like OpenSea. OpenSea allows prospective buyers to purchase cryptocurrency directly on its platform through a third-party provider, permitting users to easily fund NFT purchases with relative ease using debit cards. While not necessarily ubiquitous, reasons for buying NFTs generally relate to the hopes of making money through the investment of capital, and to the social prestige that can accompany ownership of certain NFTs through exclusive events and perks reserved for owners. These factors, including the ease of purchase and the social pressures pushing people towards the adoption of NFTs, lend themselves towards creating an environment where these NFT auction houses are evolving from a niche industry to one increasingly catering to a more generalized audience. NFT auction houses may be even more intimately intertwined with the purchase and exchange of NFTs when compared to traditional art auction houses, especially considering that the ability to purchase and exchange in the capital required for acquisition exists directly on large NFT auction houses’ homepages; this equates to a situation where a purchaser of a painting at Sotheby’s would be required to purchase currency through Sotheby’s in order to transact. In turn, these NFT exchanges hold tremendous power over transactions.

A. OpenSea is No Different from Sotheby’s

Digital art auctions houses, like OpenSea, are taking over the market for NFT trading. They process billions in dollars in NFT trades each quarter and position themselves as the NFT marketplaces of the future. However, in many ways, these marketplaces are

94 Andy Rosen, What Does NFT Mean? A Guide to Non-fungible Tokens, NERDWALLET (Sept. 22, 2022), https://www.nerdwallet.com/article/investing/nfts#how-do-you-buy-nfts [https://perma.cc/89AX-TNXH] (explaining the NFT buying process). It is also possible to purchase NFTs with fiat currencies, but this is relatively rare and still contains complicated methods that involve engaging with cryptocurrency exchanges or NFT platforms with built-in currency exchange mechanisms. See id.

95 See Rosen, supra note 94.


97 See Rosen, supra note 94.

98 About OpenSea, supra note 13.
surprisingly similar to traditional art auction houses, and even provide less scrutiny than a traditional art auction house. Similar to traditional art auction houses, many of the NFTs for sale on a marketplace like OpenSea are sent to an auction, where a seller has a reserve price that needs to be met for a sale to happen and prospective buyers can bid up the purchase price of the NFT through public, online bids. Buyers and sellers, instead of hiding behind “private collection” sales, hide behind Ethereum and other blockchain addresses that make tracking funds difficult and expensive.

While there are similarities between NFT marketplaces and traditional art auction houses like Sotheby’s and Christie’s, there is one main difference between the two. Christie’s and Sotheby’s, despite no required regulations, take voluntary measures to conduct rudimentary KYC and AML processes. While highly ineffective, as evidenced through reports by the Treasury Department and Congress that laid bare the vast underperformance of these voluntary systems in preventing criminals from transacting, these measures at least demonstrate that traditional art auction houses are attempting to address regulators’ and law enforcement’s concerns surrounding the abuse on their marketplaces.

When looking at OpenSea and other large NFT marketplaces, a difference in policy stands out when compared to traditional art auctions houses like Sotheby’s. These digital art auction houses often do not engage in even the simplest KYC or AML measures. In fact, there is almost universally no verification of customer identities in these marketplaces, meaning that buyers and sellers alike do not have their banking and other financial information checked for impropriety. This demonstrates both the appetite for risk that NFT auction houses hold for engaging with individuals who may not have acquired their capital through entirely legal means. It also represents an absolution of responsibility towards protecting the integrity of the digital space that is, at least, somewhat considered by traditional art


101. STAFF OF S. COMM. ON HOMELAND SEC. & GOVERNMENTAL AFFS., supra note 35.

102. See Kauflin, supra note 70.

103. See id.
auction houses. The gaping hole left by the rejection of KYC and AML requirements demonstrates clear vulnerabilities in the digital art market that can likely be abused and have in fact been abused. This divergence in policy makes OpenSea and other NFT marketplaces more similar to historical art markets, where the identities of buyers and sellers were held closely, and financial information was not shared as part of the regular course of business.\textsuperscript{104} Instead of heading towards the new transparent and utopian future promised by many crypto visionaries, NFT marketplaces instead have chosen to devolve to medieval standards of transparency that went out of style over a hundred years ago. The broad NFT community also appears aligned with patronizing non-KYC forums for exchange.\textsuperscript{105}

\begin{itemize}
    \item B. NFTs Are Used to (In)Directly Money-Launder
\end{itemize}

While cryptocurrencies themselves act as the main vehicle for digital money laundering currently, NFTs have a variety of appealing characteristics that are increasing their adoption for explicit money-laundering means.

In early 2022, the Department of Justice announced its largest ever financial seizure, amounting to over $4.5 billion in illicit proceeds and stolen funds.\textsuperscript{106} The individuals involved had stolen cryptocurrency from the 2016 hack of the cryptocurrency exchange Bitfinex.\textsuperscript{107} While the criminals used a variety of means to launder their money, one explicit means was the purchase and sale of NFTs.\textsuperscript{108} The suspects had used OpenSea to list and transact NFTs.\textsuperscript{109}

\textsuperscript{104} See supra Part I.A.
\textsuperscript{107} Press Release, Off. of Pub. Affs., \textit{supra} note 106.
\textsuperscript{108} Complaint at 9–10, United States v. Lichtenstein & Morgan (D.D.C. Feb. 7, 2022) (No. 22-00022) [hereinafter Lichtenstein Complaint].
\textsuperscript{109} Sarah Emerson, \textit{The NFTs They Bought from the Crypto Rapper Disappeared. Now They Want a Refund}, \textsc{BuzzFeed News} (Feb. 12, 2022, 9:01 AM), . https://www.buzzfeednews.com/article/sarahemerson/crypto-
These NFTs were created using the stolen cryptocurrency, and creating and selling NFTs was one way that the criminals could easily launder money without broad scrutiny. In fact, law enforcement only discovered the NFT purchases after combing through the criminals’ personal blockchain data without much formal help from corresponding marketplaces, demonstrating how the lack of frontline regulatory behavior on the part of OpenSea allowed criminal activity to proliferate. Had OpenSea ever flagged this account for money laundering? One would have probably guessed the answer by now: no. If OpenSea had flagged this account after a regular KYC check, as numerous other cryptocurrency exchanges had previously done, it would have found that these criminals were unable to properly identify the sources of the funds and may have been able to prevent this illegal money laundering from happening.

There are other helpful fronts for criminal actors to engage in money-laundering activity. The most prominent is a rug pull, whereby a purported NFT collection creator or founder solicits outside investment or purchases of their NFTs and then proceeds to immediately abandon or wipe the collection’s existence from the Internet while keeping customer funds raised during the process. These scams often also promote exclusive perks to be obtained through the purchase of the NFTs, like VIP access to special events or discounts from partnered vendors. For example, in 2021, a new NFT drop was being hyped in the NFT community under the name of the “Baller Ape Club,” which promised would-be purchasers various perks, including limited edition merchandise for holders of the collection and access to a holder-only second NFT collection. Furthermore, the founders purportedly promised to give substantial amounts of the proceeds to charitable organizations and invest some of the money furnished by the sale to help finance a Baller Ape Club fund where holders could help determine the course of action for the funds. While this NFT pitch seemed similar to that of many NFTs being released during the 2021 craze, soon after the public mint and release of the NFT collection, the founder deleted all Internet

 rapper-nft-opensea-owner-money-laundering [https://perma.cc/X5XD-KRY7].

110 Lichtenstein Complaint, supra note 108, at 16.
111 Emerson, supra note 109.
112 See Lichtenstein Complaint, supra note 108.
114 See id.
115 Id. at 6–9.
presence for the NFT collection and removed the only two online sources where news and information were being passed to purchasers. The would-be owners of the NFTs did not even receive the NFTs after minting them; the Baller Ape Club website was engineered to display messages indicating failed minting transactions, even though the money was being siphoned into the founder’s accounts. In total, the founder and associated criminals made off with almost $3 million worth of customers’ cryptocurrency and proceeded to launder this money through a variety of methods to evade scrutiny. In essence, this NFT collection served as a convenient avenue to steal funds for money laundering.

These types of frauds show no sign of slowing down. In early 2022, adult film star Lana Rhoades raised over $1.5 million in cryptocurrency from the launch of her NFT collection, but shortly after—allegedly because fans and detractors alike heavily criticized the rollout of the collection—deleted her personal Twitter (now X) account and stopped interacting with the Discord channel related to her NFT collection. Rhoades had rug-pulled the NFT she had released. In late 2022, a popular OnlyFans creator with millions of fans around the world, including the United States, rug-pulled supporters of her NFT collection, allegedly making off with hundreds of thousands of dollars in cryptocurrency. Instances like these demonstrate how scams are affecting ordinary Americans, sometimes involving the loss of large amounts of cash. Without regulation, it is clear that these schemes will proliferate.

C. Industry-Related Firms Intentionally Downplay the Scope of NFT Money-Laundering to the Detriment of Customers

Industry claims that the amount of money washed through NFTs numbers in the low millions, but this is misleading. Leading
blockchain analysis firm Chainalysis concluded that the fourth quarter of 2021 saw relatively modest use of NFTs for money laundering; however, the definition of money laundering through NFTs that Chainalysis used to collect samples was incredibly narrow.\textsuperscript{122} Because of this, Chainalysis did not include the tens of millions of dollars, if not hundreds of millions of dollars, that have traveled through NFT mints and other associated activities.\textsuperscript{123}

This underreporting is likely a detriment to further adoption of NFTs and other related digital assets. Instead of addressing issues head on and fully acknowledging the problems that exist, firms have seemingly chosen to ignore problems for as long as they can.\textsuperscript{124} While underreporting may have led to some limited cost-savings in the short term, recent events in the broader space of digital assets, NFTs, and crypto have led regulators to look for a more direct and confrontational approach, tacitly acknowledging that allowing the space to regulate itself has not worked so far.\textsuperscript{125}

In an ideal world, the NFT auction houses, digital asset exchanges, and other stakeholders would take proactive steps to address issues that have continued to flourish in their space. In fact, taking these steps would likely prove to regulators, politicians, and the public that NFT exchanges and auction houses are looking to correct past wrongs and protect customers, which could lead to greater legitimacy for the space. However, because these measures have not been taken, and are even outright rejected by major industry players,\textsuperscript{126} it is likely that regulators will look at the industry with an even more skeptical eye. Taking these steps could also serve to create goodwill among regulators and politicians, especially considering the eye-popping public imploding of the crypto exchange FTX in late

\textsuperscript{122}See id.
\textsuperscript{123}See id.
\textsuperscript{125}See generally Ann Saphir & Dan Burns, \textit{Fed’s Barr: Concerned About Blowback to Financial System From Crypto}, \textsc{Reuters} (Nov. 15, 2022, 1:31 PM), https://www.reuters.com/markets/us/feds-barr-concerned-about-non-bank-risks-including-crypto-that-can-blow-back-2022-11-15/ [https://perma.cc/Y53X-ZPAN] (highlighting Federal Reserve Governor Barr’s opinions and concerns about the growing frauds and scams occurring in the space, and pointing out how the increased visibility and high-profile nature of a lot of NFT scams, and the industry’s lack of a response, have led to increased regulatory scrutiny).
IV. CLOSING DANGEROUS LOOHOPES AND INCREASING TARGETED ENFORCEMENT

While promising, the AMLA was just the first of many steps towards a more comprehensive and effective anti-money-laundering regime. There are a series of proactive steps that can be taken to prevent this illicit money-laundering marketplace from proliferating. First, Congress should revisit the AMLA and further amend the BSA to include both traditional art dealers and individuals involved with digital art transactions. By doing this, regulators will be able to work towards enforcing the laws more completely against criminals and better prevent illicit proceeds from entering the marketplace. Second, the Treasury Department should start to construct a centralized KYC database system, whereby any individual that has purchased any type of item, or transacted in any type of amount, that would require scrutiny under the BSA would have a profile constructed that is held by the federal government. This would help to streamline the KYC process and ensure that individuals who are either criminals or otherwise sanctioned are not allowed to participate in the domestic marketplace. This would also help to reduce the current dependency regulators have on the participants of the system to act as de facto regulators. As a final part of this comprehensive solution, the Treasury Department should create and staff a new federal law enforcement agency specifically tasked with rooting out BSA and related money-laundering offenses.

NFTs and other crypto-related assets are obviously on the cutting edge of technology and represent relatively contemporary innovations. As Chief Justice John Roberts stated in Carpenter v. United States, we have entered an age of technological transformation that requires innovative solutions, new ways of thinking, and different approaches to long-standing legal doctrines. It is, therefore, imperative that Congress and other government agencies approach NFT-associated crimes with novel schemes to best prevent further deterioration of the rule-of-law in the digital financial ecosystem.

A. Expand the BSA to Art Dealers, as the ENABLERS Act

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Intended

It appears that Congress is increasingly taking the threats of money laundering in the art market seriously. In late 2021, after the passage of the AMLA, a bipartisan group of congressmen introduced a further amendment to the BSA entitled “Establishing New Authorities for Business Laundering and Enabling Risks to Security Act (ENABLERS Act).”129 This bill sought to expand the BSA through further amendments to section 5312(a)(2) and specifically included provisions tailored towards the art market that included several broad buckets of professions the regulation would apply to:

(Z) a person engaged in the business of providing investment advice for compensation;

(AA) a person engaged in the trade in works of art, antiques, or collectibles, including a dealer, advisor, consultant, custodian, gallery, auction house, museum, or any other person who engages as a business in the solicitation or the sale of works of art, antiques, or collectibles;

(BB) an attorney, law firm, or notary involved in financial activity or related administrative activity on behalf of another person;

(CC) a trust or company service provider, including—

(i) a person involved in forming a corporation, limited liability company, trust, foundation, partnership, or other similar entity or arrangement;

(ii) a person involved in acting as, or arranging for another person to act as, a registered agent, trustee, or nominee to be a shareholder, officer, director, secretary, partner, signatory, or other similar position in relation to a person or arrangement;

(iii) a person involved in providing a registered office, address, or other similar service for a person or arrangement; or

(iv) any other person providing trust or company services, as defined by the Secretary of the Treasury;

(DD) a certified public accountant or public accounting firm;

(EE) a person engaged in the business of public relations, marketing, communications, or other similar services in such a manner as to provide another person anonymity or deniability;

(FF) a person engaged in the business of providing third-party payment services, including payment processing, check consolidation, cash vault services, or other similar services designated by the Secretary of the Treasury…

While at first glance, this proposed change to the BSA appears complex in implementation and difficult to understand, it is actually relatively simple. Seven professions are covered under this proposed expanded version of the BSA, including art dealers, investment advisors, attorneys involved in financial activities, trust or company services providers, accountants and accounting firms, public relations advisors, and third-party payment service providers. However, disappointingly, the version of the ENABLERS Act that eventually was added to the National Defense Authorization Act of 2023 (NDAA of 2023), which passed the House in the early fall of 2022, explicitly did not include three of the aforementioned seven professions: investment advisors, art dealers, and public relations firms. Instead, it narrowed the proposed changes to include only four remaining professions: trust providers, third-party payment facilitators, specifically circumscribed legal service providers, and some accounting services. While promising, these edits significantly altered the impact of the bill, with industry insiders calling the modifications “convoluted.” The alterations likely also leave art market loopholes relatively intact, leaving systematic room

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130 Id.
132 H.R. 7900, 117th Cong. § 5401(c) (2021).
133 Wolf, supra note 131.
for abuse that could be countered with a reversal of these profession exclusions.

Despite the bipartisan momentum that followed this bill from its inception, the Senate refused to include it in its final version of the NDAA of 2023 after intense lobbying by multiple industry groups,134 and the House subsequently passed a similar version without any of the ENABLERS Act included.135 The Senate could have added these provisions back in when considering the House’s amended version, but any hope of this was dashed when the final version of the bill was released.136

In order to fix these systemic issues, it is again important to acknowledge the size and scope of the illicit art market; billions of dollars in money-laundering proceeds alone flow through financial systems every year, with hundreds of millions more likely unaccounted for.137 Simple fixes exist, and there is no reason to complicate something that Congress has evidently thought worthwhile.

One path forward would be for Congress to pass the original version of the ENABLERS Act as an individual bill during the upcoming legislative session and to add coverage to people engaged in the transactions of digital art. By doing so, Congress would cover the industry more completely. Without these specific expansions of the BSA through Congressional action, it is likely that the legal implementation and rulemaking process led by FinCEN and other regulators could come under significant industry pressure that could lead to vague rules with disjointed application. Another fix would be to introduce another amendment to the BSA for the NDAA of 2024,

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136 The version of the 2023 NDAA that included the ENABLERS provisions was excised from the bill while under Senate consideration and was not added back in any subsequent reviews. See Will Fitzgibbon, US Senate Blocks Major Anti-Money Laundering Bill, the Enablers Act, INT’L CONSORTIUM OF INVESTIGATIVE JOURNALISTS (Dec. 12, 2022), https://www.icij.org/investigations/pandora-papers/us-senate-blocks-major-anti-money-laundering-bill-the-enablers-act/ [https://perma.cc/4KWJ-BG28].

137 See supra Part II.C.
again trying to package this bill’s language into a larger omnibus bill to make passage less contentious. Waiting longer to implement these new requirements might bring a host of benefits that might not otherwise have been available; for instance, waiting would allow regulators and policymakers to continue to review how failing to pass even a defanged ENABLERS Act could help reduce money-laundering efforts by criminals. This unavoidable delay also poses another cynical benefit: by waiting another year, Congress has tacitly allowed more money laundering to occur, which could place increased pressure on the next Congress to implement these measures. While not ideal, especially considering each year without regulation means another year of billions of dollars of unchecked money-laundering in the art space and tens of millions more of money laundering in the NFT space, this approach will at least reach the end goal of regulating this unregulated industry. Late is still better than never.

It is vital to note that Congress should include digital art dealers, marketplaces, and those who transact in digital art, under coverage of an expanded BSA. For example, the new BSA section 5312(a)(2) as edited through the ENABLERS Act could be amended as follows to include digital art:

(AA) a person engaged in the trade in works of *physical* art, *digital art*, antiques, or collectibles, including a dealer, advisor, consultant, custodian, gallery, auction house, museum, or any other person who engages as a business in the solicitation or the sale of works of *physical art, digital art, antiques, or collectibles* . . . .

When comparing my proposed edited section with the original ENABLERS Act included above, there are scant changes. In fact, the alterations that ensure digital art would come under regulatory scrutiny only include the addition of six words. I added an adjective to describe traditional art with “physical,” as I felt that this would encompass the vast majority of artwork that is transacted through auction houses like Sotheby’s, which this act should still aim to expand BSA requirements to. Further, I added another category of coverage: digital art. It is self-explanatory what this would cover, but this language would be able to encompass NFTs and other forms of digital art that may appear in the future. I deliberately chose not to include specific language and naming conventions surrounding “NFTs,” as the crypto world is a burgeoning industry, and NFTs may be only the current vessel for digital art transactions.

Importantly, including these language changes in the bill leaves no room for misinterpretation or incorrect rulemaking. As has been shown in the past, when Congress passes vague bills that leave
regulatory interpretation open for industry influence, outcomes often lead to regulations with large loopholes. By explicitly defining the expansion of the BSA to cover individuals helping or aiding in the transacting of digital art, Congress would help to foreclose the possibility that digital art marketplaces like OpenSea could lobby FinCEN and other rulemaking bodies out of actually regulating them.

B. Centralizing KYC Stops Criminals from Transacting

Through their deliberate inaction and commitment to supporting anonymous criminal activity, NFT marketplaces and other related exchanges have demonstrated that they are both unwilling to police their own marketplaces appropriately and would be a dubious enforcer of violations at best. It is, therefore, imperative that the United States government take a leading role in ensuring that KYC regimes are properly conducted and centralize the system under the Treasury Department as an additional bulwark against illegal transactions conducted by criminal actors.

Anti-government rhetoric has long been endorsed by leading proponents of cryptocurrency adoption. Cryptocurrency has further been used to help fund and promote protest movements and to circumvent groups or organizations viewed as oppressive. One of the most recent uses of cryptocurrency in direct furtherance of objectives counter to widely-accepted government activity was the use of cryptocurrencies during 2021. Protestors used cryptocurrency to help fund the truck convoy in Canada that unlawfully blocked and obstructed traffic in a major Canadian city, disobeyed repeated law enforcement requests for dispersal, and became increasingly belligerent towards other citizens, resulting in significant hardship for many. Despite the costs and disruptions caused by this unlawful protest, Vitalik Buterin, one of the creators of the Ethereum blockchain, came out in strong support of the

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140 Id.
141 Id.
protestors’ use of cryptocurrency to raise funds and harshly criticized government crackdowns on cryptocurrency transfers to these protestors. Buterin went further, ignoring the unlawful and inappropriate nature of the protest, and stated that the decentralized system backing most cryptocurrencies serves as a check on “lawless” government activity.142 This statement came even as the federal government in Canada invoked emergency powers, an entirely legal act of government power, in order to prevent the continued use of cryptocurrencies to fund the unlawful protest.143 In fact, Buterin and other thought leaders in the space have often railed against the “lawless” government activities that have taken anti-cryptocurrency positions based on their legal regimes or adopted cryptocurrencies with ideas opposite their specific vision of decentralization.144 Such criticisms showcase how this sort of anti-government rhetoric is heavily intertwined with the highest levels of the cryptocurrency and digital asset communities.145 Popular NFT and crypto-related blogs also promote marketplaces that do not endorse or use KYC regimes, further demonstrating the community’s propensity to behavior that borders on, or is outright, criminal.146 Compounding these problems is the reality that cryptocurrencies and related digital assets have been widely adopted by criminals as a means for continuing their nefarious activity and preying on vulnerable individuals.147

142 Id.
143 Id.
144 Cf. Andrew R. Chow, The Man Behind Ethereum Is Worried About Crypto’s Future, TIME (Mar. 18, 2022, 6:00 AM), https://time.com/6158182/vitalik-buterin-ethereum-profile/ [https://perma.cc/NLF5-SLWG] (explaining how cryptocurrencies and digital assets can be used to protest against governments that he views as authoritarian or oppressive); see also Marco Iansiti & Karim R. Lakhani, The Truth About Blockchain, HARV. BUS. REV 118 (2017).
146 See Thompson, supra note 105.
147 See generally Chainalysis Team, supra note 72 (demonstrating the
Another cautionary example is the story of the XRP cryptocurrency. Despite an ongoing legal battle, which may determine whether the company behind XRP unlawfully sold an unregistered security, believers (or, as they call themselves, HODLERS) in the company consciously sought workarounds to a nationwide ban on purchasing the digital currency, looking to overseas exchanges where XRP continues to be traded. In simple terms, the Securities and Exchange Commission (SEC) alleged that a company was likely violating long-standing legal reporting standards (that are, ironically, aimed at protecting customers and investors) and cryptocurrency investors immediately worked to, likely through illegal streams, gain access to new foreign platforms to continue investing. Industry groups that have historically aligned closer with regulators on other issues, like centralized cryptocurrency exchange Coinbase, also came out in explicit opposition to the SEC’s current position, further demonstrating the omnipresence of anti-government beliefs in the broader space.

As demonstrated, the broader cryptocurrency community, and by extension, the NFT community, cannot be trusted to police itself and is unlikely to voluntarily comply with the sort of reporting requirements that established financial institutions regularly use. Those in favor of lax regulations often point to the idea of the free market helping to prevent corporate abuse and crime. This serves to underline how the industry lacks legitimate arguments to stand on other than these broad political appeals. Free-market wheeling and dealing and the wild west were only good for those who won, and, criminal potential embedded in digital assets).

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oftentimes, those were criminal actors.\textsuperscript{152}

This anti-government undercurrent that exists in the broad cryptocurrency space demonstrates how traditional government mechanisms, controls, and market pressures that ensure compliance from long-standing financial institutions would not impose the same type of market punishment on NFT auction houses. Broadly, traditional financial institutions, like Wells Fargo or JPMorgan Chase, serve a customer base that is incredibly sensitive to illegal and inappropriate behavior on their respective platforms.\textsuperscript{153} Illegal activity, either committed by employees or customers of these traditional financial institutions, can lead to reduced levels of trust in the given financial institution and can lead to customers removing funds and discontinuing patronization of a certain institution.

It is more likely that NFT auction houses and related cryptocurrency firms would not be faced with these similar headwinds if similar scandals occurred in the space. In fact, a scandal similar to those that rocked the traditional financial space occurred on OpenSea during the NFT craze of 2021. In summary, OpenSea ran a featured section on their homepage where it posted a collection of NFTs on a regular schedule to help bring light to what the platform determined were undervalued artists or collections of NFTs. The featured posts were curated by a group of employees at OpenSea, one of whom was an executive who used insider knowledge in order to personally profit.\textsuperscript{154} The executive purchased large numbers of soon-to-be-featured NFTs and sold them for gains, sometimes in the thousands of dollars, to customers drawn to the collection because of OpenSea’s conspicuous promotion.\textsuperscript{155} In June 2022, the Department of Justice charged the former OpenSea executive charged with trading NFTs


\textsuperscript{155} Id.
on insider information.\textsuperscript{156} Despite this scandal, customers did not turn away from OpenSea and continued to embrace it, leading OpenSea to continue to have a monopoly-sized market share with respect to transactions involving NFTs.\textsuperscript{157}

Only recently has OpenSea started to lose market share, primarily due to macroeconomic factors unrelated to this scandal.\textsuperscript{158} Market participants are increasingly leaving OpenSea, which has now instituted limited KYC measures, for NFT exchanges that lack KYC guidelines and other checks that help to prevent illicit transactions.\textsuperscript{159} The lack of regulations and active involvement of these alternative NFT exchanges in individual transactions, in fact, is viewed as a positive by many in the space and helps to explain their rise in market share compared with OpenSea.\textsuperscript{160} Therefore, it is unrealistic to expect these NFT marketplaces to voluntarily police themselves.

Because of the industry’s conscious effort not to seriously police itself and NFT customers’ lack of appreciation for the need for KYC and other measures to prevent criminal actors from taking over the space, it is imperative that the Treasury Department work to centralize KYC for NFT exchanges, with an eye towards expanding to digital asset and cryptocurrency exchanges in the future. Because the NFT market is in such an early stage of growth and there are a limited number of stakeholders to consider in the process of centralizing KYC, it is likely that this process could be done with limited industry pushback, especially in the face of hearings surrounding the recent collapse of crypto exchanges like FTX.\textsuperscript{161} By demonstrating proactive willingness to participate in centralizing KYC side-by-side with the U.S. government, the industry could generate goodwill at a time when cryptocurrencies and digital assets (and the companies that help regular Americans acquire them) are coming under heavy scrutiny.\textsuperscript{162} This sentiment is already being

\textsuperscript{156} Id.
\textsuperscript{157} See Ng, supra note 12.
\textsuperscript{158} See id.
\textsuperscript{159} See id.
\textsuperscript{160} See id.; Thompson, supra note 105.
conveyed by the CEO of Coinbase, the largest centralized cryptocurrency exchange.\textsuperscript{163} Despite the fears of NFT promoters, regulations created jointly between industry insiders and regulators will give the industry more freedom as opposed to allowing regulators to hammer the industry without industry cooperation. Regulators, both domestic and foreign, are already increasingly skeptical about non-illicit use cases for NFTs.\textsuperscript{164}

The centralization of KYC for digital assets could be teed up as an expansion of the Patriot Act, landmark legislation passed after 9/11 that helped to expand appropriate government power into spaces that were otherwise previously unregulated to a dangerous degree.\textsuperscript{165} Among its provisions were those related to money laundering activity.\textsuperscript{166} This centralization of KYC would prevent criminal actors and terrorists from accessing an unregulated facet of the burgeoning digital U.S. financial system, and would further help to protect Americans from dangerous organizations.\textsuperscript{167} If the Patriot Act is an unappealing avenue for implementation, these centralization measures could also be grouped with the remaining ENABLERS Act language included in the NDAA of 2023.

There are several major benefits for the centralization of KYC. A centralized KYC ecosystem, run by a single regulatory agency, would help to ease the onboarding of new customers and lower transaction costs over time.\textsuperscript{168} This, in turn, could help small businesses stay in the market by reducing their exposure to compliance costs and other regulatory requirements that they may not be able to afford. This centralization would also improve compliance; because the KYC would be centralized under a government agency, there would be no way for participating companies to circumvent the process, and sanctioned individuals and criminal actors would be locked out of transacting with the NFT ecosystem. By doing this, growing money-laundering efforts in the

\begin{itemize}
\item \textsuperscript{163} Id.
\item \textsuperscript{165} USA Patriot Act, FIN. CRIMES ENF’T NETWORK, https://www.fincen.gov/resources/statutes-regulations/usa-patriot-act [https://perma.cc/496R-WT2J].
\item \textsuperscript{166} See id.
\item \textsuperscript{167} See id.
\end{itemize}
NFT space could be quickly and handily dismantled through this proactive, targeted system.

V. IMPLEMENTATION PROBLEMS ARE OVERBLOWN AND MISLEADINGLY SELECTIVE

Current critiques attempting to curtail any future regulations are commonly rooted in critiques about the free market and frame proposed regulations like those discussed above as hurting small businesses, and often highlight the difficulties in overcoming a divided legislature. Industry attacks generally center on the significant implementation requirements that would have to be shouldered by firms; something, they claim, that will lead to a mass exodus of small businesses in the space.\(^{169}\) I acknowledge that this is likely to be true; firm behavior in relation to legal and regulatory actions is significantly impacted by size.\(^{170}\) Because of the unincorporated nature and the small number of employees working at a majority of America’s small businesses, regulatory regime changes, especially ones that impose increased costs and burdens on businesses, have an outsized effect on small business performance and viability.\(^{171}\)

There is not any doubt that there will likely be strong headwinds for implementation. First and foremost, this language would have to survive Congress’s vast bill-editing process, something that is no guarantee, even for the most mundane of issues considering the current state of political partisanship.\(^{172}\) As we have seen, Congress


\(^{171}\) See id. (explaining how small businesses are impacted by differing regulatory regimes when compared with competitors who are larger).

\(^{172}\) See Lee Hamilton, Bipartisanship Isn’t Dead, but It’s Not in Good Health, Either, IND. UNIV. CTR. ON REPRESENTATIVE GOV’T (May 4, 2022) https://corg.iu.edu/programs/hamilton-views/comments-on-
has already caved once to lobbyist demands to prevent adding more stringent money-laundering regulations for the art market. However, larger implementation risks come from the strength of the art marketplace industry’s lobbying power.

Industry experts may argue that these are special rules that only apply to them, but this is simply false. Application of the regulations and laws under the BSA is standardized and regularly applied across a spectrum of industries similar to the art market in order to combat money laundering and other related crimes. Therefore, it is illogical to continue to exempt art from regulation and oversight under the BSA, as these protections arguably cover every other industry that has comparable money-laundering risks. Expanding the BSA to include art and digital art would simply bring them in line with the requirements already applied to those involved in precious metal, stones, jewel, casino, and pawn shop transactions. Despite the art market being substantially larger than the mom-and-pop pawn shop around the corner, huge billion-dollar companies like Sotheby’s have consciously been excluded from oversight.

It is also important to note that other similar industries, like precious jewels, that have come under increased anti-money-laundering regulations have continued to expand and expect growth despite these regulatory headwinds. Therefore, it is disingenuous for the industry to suggest that regulations being considered could

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See Kupfer, supra note 135.


See id.

provide a chilling effect on adoption and further innovation. Just like other industries that came under renewed AML scrutiny and proceeded to succeed, digital art and physical art will likely take the same path.

There might be infighting between regulatory agencies as to who gets to review and approve the new centralized version of KYC, as has already been seen to occur for cryptocurrencies. However, while these jurisdictional issues will hinder initial implementation, problems related to this are less urgent than stymying criminal activity in its infancy before it is allowed to explode and hurt hundreds of thousands of Americans.

CONCLUSION

Regulations and the legal structure of legislation should work to protect the greatest number of Americans through means that minimally impact innovation and entrepreneurial behavior. The BSA and its applications are not perfect, and there are times when the application of this legal regime can lead to uneven application across business sizes and industries. There may have even been times when the application of the BSA, and the compliance requirements that accompany it, forced small businesses from markets. However, without the application of the BSA and its accompanying required disclosures and regulatory measures, money laundering has exploded in the art sector. Money laundering will only increase when criminal actors invent and perfect schemes involving the new digital landscape available through NFTs. To counter this, there are options to strengthen the current regulatory regime and to prevent this explosion in illicit activity from engulfing an otherwise emerging and promising nascent industry.

First, Congress must take steps towards expanding the AMLA through a further expansion of the BSA. Because of the massive loopholes that currently exist in the anti-money-laundering regimes, along with conscious efforts by both politicians and industry insiders to carve out these loopholes, criminal activity has been allowed to proliferate with limited oversight alongside lackadaisical enforcement. To fix this, the expanded BSA would extend application to traditional physical art and digital art (namely, NFTs).

\[177\] See St Onge, supra note 151.


\[179\] See supra Part IV.B.
This expansion would be powered through specifically tailored language that would target the businesses and individuals who would engage with these mechanisms most frequently, allowing specific and targeted enforcement.\textsuperscript{180}

Second, a regulatory agency like the SEC, Commodity Futures Trading Commission, or Internal Revenue Service should be tasked with centralizing the KYC for customers engaging in NFT transactions, with an eye towards centralizing KYC for all digital assets in the future. This centralization can be done through multiple means; in the past, the Patriot Act has acted as a means towards expanding anti-money laundering regimes and could serve as a method for these regulations to be created.\textsuperscript{181} If this path is not used, centralized KYC could likely be packaged into the aforementioned expansion of the BSA through the NDAA of 2023.\textsuperscript{182} There are several benefits of centralizing KYC, including the reduction of transaction and compliance costs for businesses (including small businesses) and uniform compliance. This would likely reduce criminal activity and criminal adoption of these emerging digital assets for their use in illicit behavior.

While issues regarding the implementation of these two posited solutions exist, they are overblown by stakeholders. Most prominently, traditional art auction houses and crypto exchanges (along with limited participation by NFT auction houses) often complain that increased regulations will only push smaller players out of the market and will in fact force market consolidation that could be improper for the industry. They also complain that these measures are unfairly targeting a market when there are other avenues that criminal actors exploit more. While I am sympathetic to concerns like this, the industry actually misleads the public with these concerns and would be better served through appropriate regulations and effective, targeted enforcement measures. These drawbacks are heavily outweighed by the protections that will be created for everyday Americans. When crimes occur in the NFT space, they have overwhelmingly impacted ordinary Americans, who can lose substantial sums of money invested.\textsuperscript{183} Therefore, the government would be doing a favor to all Americans by protecting those who are at high vulnerability of exploitation. This expansion of the BSA would enable the government to more effectively and completely control an industry often characterized as the “Wild West.”\textsuperscript{184} Centralizing KYC would also help to reduce transaction

\begin{footnotes}
\item[180] See supra Part V.A.
\item[181] See USA Patriot Act, supra note 163.
\item[182] See supra Part V.A.
\item[183] See Pimentel, supra note 2.
\item[184] Madana Prathap, \textit{NFTs Are the New Crypto Wild West—Artists and}
\end{footnotes}
costs, actually improving sustainability for small businesses, and could reduce liability because the centralized KYC regime would be controlled by a government agency.

Although NFTs are used for a limited portion of the criminal behavior that occurs in the increasingly omnipresent digital ecosystem, it is incredibly important for the government to send a clear message regarding the future of this space; regulations are here to stay, and the gold rush is no more.