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**BLOG**

# Action Plan to Address Illicit Financing Risks of Digital Assets – U.S. Department of the Treasury

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On September 16, 2022, the U.S. Department of the Treasury (Treasury), the Department of Justice (DOJ), and other U.S. government agencies released eight highly anticipated reports[1] (the Reports) on different aspects of digital asset regulation, setting forth the agencies' respective legislative, regulatory, and policy recommendations and priorities. The Reports were issued in response to White House Executive Order 14067 on Ensuring Responsible Development of Digital Assets (the Executive Order), which calls for a whole-of-government alignment of the federal government's approach to digital assets.

The Reports confirm the Biden-Harris Administration's acknowledgment that digital assets have potential benefits and are likely to remain a component of the U.S. financial system, but that the proliferation of the asset class presents unique risks that should be addressed. While the Reports provide some insight into the Administration's thinking about digital assets and articulate some recommendations and "calls to action," many significant regulatory questions remain unaddressed.

This post summarizes Treasury's Action Plan to Address Illicit Financing Risks of Digital Assets.

## Action Plan to Address Illicit Financing Risks of Digital Assets[2]

Treasury published its "Action Plan to Address Illicit Financing Risks of Digital Assets" (Action Plan) as mandated by Section 7(c) of the Executive Order, which directed the development of a coordinated interagency action plan for "mitigating the digital asset-related illicit finance and national security risks addressed in the updated strategy."[3] In the Action Plan, Treasury identifies several aspects of digital assets that are of concern for Treasury, including the use of digital assets in money laundering, ransomware crimes, revenue generation and sanctions evasions by states and groups, and financing of terrorist organizations. As a result, Treasury presented seven "priority actions" and supporting actions to address these issues.

**Features of Digital Assets**
Treasury identified several features of digital assets and digital asset businesses that pose risks to proper financial security and oversight, including:

- Gaps in AML regimes across countries;
- Anonymous features of digital assets;
- Disintermediation of virtual assets,[4] actual or otherwise; and
- Virtual asset service providers (VASPs) that are non-compliant with AML and other regulatory obligations.

Treasury focused on the obligations of VASPs and peer-to-peer (P2P) service providers who engage in the business of transacting digital assets through "unhosted" digital wallets–i.e., wallets not held by any financial institution or VASP. Treasury stated that VASPs and P2P service providers can be subject to U.S. AML obligations if they operate wholly or in substantial part in the United States, regardless of where they are located. Such businesses and individuals could be required to register with the Financial Crimes Enforcement Network (FinCEN) as money services businesses, implement an effective AML program, or abide by recordkeeping and reporting obligations such as the requirement to file Suspicious Activity Reports (SARs).  Treasury also warned that P2P service providers and decentralized finance (DeFi) services that purport to transact through unhosted wallets may nonetheless be subject to AML and countering-the-financing-of-terrorism (CFT) obligations as money transmitters when they transfer currency, funds, or assets of value.

**Priority and Supporting Actions**
Treasury introduced seven priority actions to mitigate the perceived threats and risks of digital assets. In most of the supporting actions to these priorities, Treasury identified itself as the lead department to pursue the objectives, while also recognizing the importance of interagency coordination. The priority actions listed in the Action Plan are:

- Monitoring emerging risks through collection of information and investing in technology and training;
- Improving global AML regulation and enforcement;
- Updating Bank Secrecy Act (BSA) regulations to address illicit financing risks;
- Strengthening U.S. AML supervision of virtual asset activities and promoting standardization of AML/CFT obligations across states;
- Holding accountable cybercriminals and other illicit actors through seizures, criminal prosecutions, civil enforcement, and targeted sanctions designations;
- Engaging with the private sector and exchanging information on illicit financing risks and AML obligations; and
- Supporting U.S. leadership in financial and payments technology, such as real-time payment solutions and stablecoins.

While most of the supporting actions were continuations of Treasury's previous work, some of the supporting actions were new. For example, Treasury intends to publish an illicit finance risk assessment on DeFi and its role in money laundering and terrorist financing risks by February 24, 2023. Treasury also plans to convene state supervisors to promote standardization and coordination of state licensing and AML obligations of VASPs. Furthermore, Treasury briefly noted the increasing global interest in Central Bank Digital Currencies (CBDC), which Treasury believes must be designed to comply with global AML standards. Treasury plans to monitor both domestic and foreign CBDC development initiatives and consider implications for AML/CFT controls.

For more insights on the Reports, read our full briefing: The Future of Digital Assets Regulation in the United States.

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[1] The complete Reports mandated by President Biden's Executive Order and issued by Treasury, DOJ, and White House explored in this Winston Alert can be located at the following links:

- Action Plan to Address Illicit Financial Risks of Digital Assets issued by Treasury
- Crypto-Assets: Implications for Consumers, Investors and Businesses issued by Treasury
- The Future of Money and Payments issued by Treasury
- Climate and Energy Implications of Crypto-Assets in the United States issued by the White House
- Policy Objectives for a U.S. Central Bank Digital Currency System issued by the White House
- Technical Evaluation for a U.S. Central Bank Digital Currency System issued by the White House
- The Role of Law Enforcement in Directing, Investigating, and Prosecuting Criminal Activity Related to Digital Assets issued by the DOJ
- Responsible Advancement of US Competitiveness in Digital Assets issued by the U.S. Department of Commerce

[2] On September 20, 2022, Treasury issued a notice inviting interested members of the public to comment on digital asset-related illicit finance and national security risks as well as an action plan to mitigate such risks. Comments must be received on or before November 3, 2022.

[3] Exec. Order No. 14067, 87 Fed. Reg. 40,881 (July 8, 2022).

[4] According to Treasury, virtual assets are a subset of digital assets that does not include central bank digital currencies ("CBDCs") or representations of other financial assets, such as digitalized representations of existing securities or deposits. *See* U.S. Dep't Treasury, *Fact Sheet: Action Plan to Address Illicit Financing Risks of Digital Assets* (Sept. 20, 2022), https://home.treasury.gov/system/files/136/Fact-Sheet-Action-Plan-to-Address-Illicit-Financing-Risks-of-Digital-Assets.pdf.

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## Authors


Nag Young Chu

Carl Fornaris

Kimberly A. Prior

Janelle E. Rodriguez-Mena

Daniel T. Stabile


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Nag Young Chu

Carl Fornaris

Kimberly A. Prior

[Janelle E. Rodriguez-Mena]

[Daniel T. Stabile]

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