

July 21, 2022

DOJ Unveils Enforcement Actions in Connection with Alleged Cryptocurrency Fraud

On June 30, 2022, the Department of Justice (“DOJ”) announced four enforcement actions involving allegations of fraud in the cryptocurrency space. The enforcement actions, which collectively bring criminal charges against six individuals, demonstrate the breadth of potential conduct that may expose participants in the blockchain industry to regulatory and enforcement risk. In connection with these cases, the DOJ alleges a wide-ranging “rug pull” scheme related to non-fungible tokens (“NFTs”), a fraudulent investment fund trading on cryptocurrency exchanges, a Ponzi scheme involving the sale of unregistered cryptocurrency instruments, and a fraudulent initial coin offering. The announcement may also signal enhanced focus on potential cryptocurrency fraud in Central and Southern California, where three of the four cases were filed.

“Baller Ape Club” NFT Crackdown

On June 28, the DOJ brought an enforcement action asserting claims of conspiracy to commit wire fraud and conspiracy to commit international money laundering against the creator of an NFT investment program called the “Baller Ape Club,” alleging the “largest known . . . NFT scheme charged to date.”¹ Baller Ape Club sold NFTs in the form of cartoon figures (frequently including the namesake “Baller Ape” character). The DOJ alleges that the defendant and his co-conspirators orchestrated a “rug pull” by abruptly closing the Baller Ape Club website shortly after commencing public sales of the NFTs, and thereafter stealing investors’ funds.² Thereafter, the group allegedly laundered the funds by “chain-hopping,” or converting one type of cryptocurrency “coin” into others and discreetly moving value across several blockchains in an effort to disguise the source and movement of the funds.³ The defendant, who, along with his co-conspirators, allegedly stole approximately \$2.6 million from investors in connection with the Baller Ape Club scheme, faces up to 40 years in prison if convicted on all counts in the indictment.⁴

EmpiresX Ponzi Scheme Charges

On June 30, the DOJ brought charges against three individuals in connection with an alleged global Ponzi scheme involving a cryptocurrency investment platform named EmpiresX.⁵ The indictment alleges that EmpiresX’s two founders and its “Head Trader” fraudulently promoted the platform. Specifically, the DOJ asserts that the defendants made misrepresentations regarding the platform’s “purported proprietary trading bot,” which they claimed would be used to make trades in the stock market after EmpiresX converted investors’ cryptocurrency into fiat currency.⁶ The defendants allegedly represented that this process would generate safe, reliable returns on a daily basis, including due to the use of advanced strategies developed by the “Head Trader”—who the defendants marketed as a trading “genius.”⁷ Additionally, the defendants purportedly hosted misleading virtual demonstrations wherein the bot was inaccurately depicted to be linked to one of several EmpiresX brokerage accounts, each represented to hold approximately \$20 to \$50 million dollars.⁸ The DOJ asserts that, in reality, the defendants did not generate returns through the proprietary trading bot, but instead operated a Ponzi scheme by paying earlier EmpiresX investors with contributions obtained from later investors.⁹ The defendants allegedly laundered investors’ funds in EmpiresX through the platform’s “cluster of cryptocurrency wallets” and a foreign cryptocurrency exchange, in order to conceal the platform’s inability to generate meaningful revenue through the promoted trading bot.¹⁰ Separately, the indictment provides that the defendants imposed restrictions upon investors’ ability to withdraw their funds, while making false and misleading representations that the funds could be readily withdrawn.¹¹

Finally, the DOJ asserts that the defendants made misrepresentations about steps they had taken to register EmpiresX’s investment program with the SEC.¹²

TBIS Initial Coin Offering

On May 13, the DOJ filed an information charging the founder of cryptocurrency platform Titanium Blockchain Infrastructure Services (TBIS) with securities fraud in connection with the platform's \$21 million initial coin offering ("ICO").¹³ The information provides that the defendant falsified white papers documenting the project's purpose and underlying technology, planted inauthentic testimonials on the platform's website, and fabricated a number of claimed governmental and corporate business relationships.¹⁴ The defendant faces up to 20 years in prison if convicted on all alleged counts. In a statement, Kristi Johnson, Assistant Director in Charge of the FBI's Los Angeles Field Office, commented that "caution is warranted" with respect to cryptocurrency investments, as "fraud associated with decentralized money investments is pervasive."¹⁵

Cryptocurrency Commodities Scheme

Finally, the DOJ unveiled fraud and conspiracy charges against the owner of Circle Society, a cryptocurrency investment platform founded in 2018 (unrelated to the global cryptocurrency business Circle, the developer of the prominent "USDC" stablecoin).¹⁶ Circle Society solicited funds from investors to participate in a "commodity pool," a fund that combines invested contributions to make trades on the futures and commodity markets.¹⁷ The indictment alleges that the owner of Circle Society made false representations that he was able to realize returns of 500% to 600% by using an artificial intelligence trading bot that would use "signaling technology" to trade investors' funds on various cryptocurrency exchanges.¹⁸ The defendant purportedly offered fraudulent "tests" of his trading programs to reassure prospective investors of the legitimacy of the platform.¹⁹ In reality, the DOJ alleges, Circle Society was an illegal Ponzi scheme whereby the owner of the platform would use funds obtained from early investors to pay supposed returns to new prospective investors.²⁰ The owner of the platform purportedly made numerous false representations to investors in order to induce investments, including that he was a leading application developer and programmer and had a series-7 securities broker's license.²¹ The defendant also is alleged to have enticed investments by holding investor meetings at luxury Hollywood Hills homes and traveling with armed security guards in order to create an illusion of wealth and success.²² Finally, the DOJ asserts that the defendant made various false representations to justify his failure to return investors' initial Circle Society investments, and conspired to solicit investment in another cryptocurrency trading program he falsely claimed was controlled by a third party in order to avoid investors' repayment demands.²³ The defendant, who allegedly raised approximately \$12 million from investors from these fraudulent activities, faces up to 115 years in prison if convicted on all counts in the indictment.²⁴

Trends and Takeaways

While the factual circumstances giving rise to the DOJ's recent spate of enforcement activity vary across each individual case, these four actions do bring several distinct and reoccurring themes into focus. The action involving the "Baller Ape Club" emphasizes federal authorities' focus on the emerging NFT market, which is sometimes viewed as a potential source of fraud and exploitation in light of its increasing attractiveness to a mainstream audience and ambiguous regulatory status. The case also highlights the focus of the DOJ and the Department of Homeland Security on transnational cryptocurrency business networks, which may be used to more easily conceal stolen or otherwise illicit funds in "rug pulls" and similar schemes. Separately, the EmpiresX and Circle Society actions highlight law enforcement agencies' apparent concentration on the prevalence of Ponzi schemes involving cryptocurrency instruments and platforms. Finally, the focus in the EmpiresX action on alleged fraud arising out of cryptocurrency platforms' failure to register their activities with the SEC, and the claims arising out of the ICO in the TBIS enforcement action, underscore authorities' continued position that cryptocurrency instruments often qualify as "securities" under applicable law.

If you have any questions regarding this decision or other blockchain-related issues, please feel free to contact your usual Ropes & Gray advisor.

1. 4Press Release, Department of Justice, *Justice Department Announces Enforcement Action Charging Six Individuals with Cryptocurrency Fraud Offenses in Cases Involving Over \$100 Million in Intended Losses* (June 30, 2022), <https://www.justice.gov/usao-cdca/pr/justice-department-announces-enforcement-action-charging-six-individuals-cryptocurrency>.
2. Indictment at ¶ 3, *United States v. Le Ahn Tuan*, Case No. 2:22-cr-00273-JLS (C.D. Cal. June 28, 2022).
3. *Id.* at ¶ 10.
4. Press Release, *supra* note 1.
5. Indictment, *United States v. Emerson Pires et al.*, Case No. 1:22-cr-20296-JEM (S.D. Fla. June 30, 2022).
6. *Id.* at Count I, ¶ 11.
7. *Id.* at Count I, ¶¶ 12-13.
8. *Id.* at Count I, ¶ 15.
9. *Id.* at Count I, ¶ 18.
10. *Id.* at Count I, ¶ 19.
11. *Id.* at Count I, ¶¶ 23-25.
12. *Id.* at Count I, ¶¶ 21-22.
13. Information at ¶ 22, *United States v. Michael Alan Stollery*, Case No. 2:22-cr-00207-JLS (C.D. Cal. May 13, 2022).
14. *Id.* at ¶ 21.
15. Press Release, *supra* note 1.
16. Indictment, *United States of America v. David Gilbert Saffron*, Case No. 2:22-cr-00276-DSF (C.D. Cal. June 28, 2022).
17. *Id.* at ¶ 52.
18. *Id.* at ¶¶ 20-23.
19. *Id.* at ¶¶ 28-29.
20. *Id.* at ¶ 30.
21. *Id.* at ¶ 26.
22. *Id.* at ¶ 19.
23. *Id.* at ¶¶ 35-38.
24. Press Release, *supra* note 1.