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SUBMISSION TO THE FEDERAL RESERVE CONCERNING SILVERGATE BANK

My name is Marc Cohodes. I am a former hedge fund manager, a long-time stock market analyst, and a short seller. I am currently a private investor. Over my 40-year career as an investor and fund manager, I have exposed many publicly traded companies and individuals who were engaged in fraud, illegal conduct, questionable accounting, and stock manipulation, including Lernout & Hauspie, Media Vision Technology, NovaStar Financial, AremiSoft, California Micro Devices, Network Associates, TakeTwo Interactive, Krispy Kreme Donuts, Boston Chicken, MiMedx Group Inc., and others. For more than 30 years, I have provided valuable and timely information to the Securities and Exchange Commission and the Department of Justice about companies engaged in fraudulent business practices. My investigations of fraud in the financial markets have been reported in The Wall Street Journal, The New York Times, Barron's, Bloomberg, Institutional Investor, CNN, award-winning books about financial fraud, and two Harvard business cases, among others.

Between 2003 and 2005, I disclosed the manipulations at aaiPharma Inc., which led to U.S. Securities and Exchange Commission and U.S. Department of Justice actions. The Harvard Business School published a case study in March 2013 about my successful efforts to expose the NovaStar fraud in NovaStar Financial: A Short Seller's Battle, <http://bit.ly/3iFFSFR>. With that background in mind, I submit the following information for your consideration. I would be happy to meet with your staff and discuss the information set out below.

Introduction:

An enormous amount of evidence, which is documented in the attached exhibits and citations, contradicts Silvergate Bank's ("Silvergate") claims about the adequacy of its KYC/AML procedures. As I explain, it is highly unlikely that Silvergate has performed the diligence and monitoring processes that it has reported. And, absent a change in management, it is doubtful that Silvergate will do so in the future because their business is based on crypto clients. Even basic online searches of many these clients of Silvergate should have revealed obvious problems, past enforcement actions, fake or fraudulent business activity, money laundering allegations, and significant risks associated with processing billions of dollars of

transactions for its crypto clients. There is more than enough evidence, and additional examples are coming to light every day, to warrant banking regulators performing an investigation of both Silvergate’s KYC/AML practices, as well as its crypto client’s transactions on its SEN private blockchain. Silvergate should seek a buyer, its management should be replaced, or it should be put through the FDIC’s resolution process. Silvergate has played a central, and incredibly irresponsible, role as a facilitator for countless illegal crypto transactions.

Background:

For most of its history, Silvergate was a small Federal Reserve member commercial bank operating in Southern California. In an interview, CEO Alan Lane explained that, following the 2008 financial crisis, Silvergate was “struggling with growing the deposit side of the balance sheet” and that it “had four branches spread out across Southern California, didn’t really have a brand name.”¹ Lane stated, “We were looking for deposit niches for the bank” and learned crypto companies were ‘getting kicked out of banks’ due to the ‘perception of risk’ associated with inherent anti-money laundering (“AML”) concerns. *Id.* Lane stated that “[if] you can mitigate that risk . . . then all of this is opportunity. . . so that’s the way we looked at bitcoin.” *Id.* Silvergate did not, however, mitigate that risk.

Lane went on to explain during this interview that he was introduced to SecondMarket, a crypto company founded by Barry Silbert, now known as Genesis Trading, which became Silvergate’s first crypto customer in January 2014. Silbert is noteworthy because he is the founder of Digital Currency Group (“DCG”). DCG invested in Silvergate in 2018 as part of a \$118 million private placement.² DCG is now both under a federal criminal investigation³, and related to a defendant in a recent SEC civil complaint.⁴ Bloomberg noted that Federal prosecutors and the SEC are investigating “internal financial dealings of Barry Silbert’s expansive crypto empire.”

Crypto-related deposits in Silvergate grew exponentially to over \$14 billion by the end of 2021, according to SEC filings. Deposits from shady crypto clients poured into the bank. In December 2022, a former Silvergate employee told the Financial Times, “This was a tiny real estate lender that went all-in on crypto. . . . It was completely weird.”⁵ The stunning deposit growth appears to have been fueled, at least in part, by Silvergate’s introduction of the Silvergate Exchange Network (dubbed the “SEN”) in or around 2017, which allowed Silvergate’s clients (crypto exchanges, crypto miners, crypto hedge funds, and crypto “whales”) to transfer money

1 The Pomp Podcast, *Alan Lane, CEO of Silvergate: Why Bitcoiners Shouldn’t Hate Banks*, (Nov. 19, 2019), <http://bit.ly/3W716dw>.

2 CoinDesk, *Digital Currency Group Invests in Bitcoin-friendly Silvergate Bank* (Feb. 27, 2018), <http://bit.ly/3H2pEQs>, Ex. 1.

3 Bloomberg, *Crypto Empire DCG Faces US Investigation over International Transfers* (Jan. 6, 2023), <http://bit.ly/3Qyrpbn>, Ex. 2.

4 *SEC v. Genesis Global Capital LLC*, No. 1:23-cv-00287 (S.D.N.Y. Jan. 12, 2023), <http://bit.ly/3QA20he>.

5 Financial Times, *Silvergate: From Tiny Local Lender to Bank Behind the Crypto Boom* (Dec. 9, 2022), <http://bit.ly/3XmWroC>, Ex. 3.

instantaneously to other Silvergate clients, 24/7, in an opaque manner. Silvergate’s investor relations touts that its clients have used SEN to transfer over **\$1 trillion** and can send money they borrow from the bank secured by their bitcoin holdings using “SEN Leverage.”⁶

Remarkably, CEO Lane admitted that his bank’s SEN offering “doesn’t have the regulatory, *it’s not like it’s an approved product*, it’s a non-disapproved product . . .” (emphasis added).⁷ Lane went on to say “as the OCC has been issuing these pronouncements over the last year, they’ve essentially been validating things that we already believed to be true, and that we were essentially already doing...” *Id.* at 06:28. I doubt that. Silvergate’s September 30, 2022 SEC 10-Q filing states that “substantially all” of the bank’s deposits are “from our digital asset customer base.”⁸ This concentration has brought with it significant risks. It has been widely reported that Silvergate had to borrow over \$4 billion from the Federal Housing Finance Agency in 2022 as several of its crypto clients began to blow up.⁹

Silvergate Offers Banking Services to Suspect Offshore Entities

As of September 30, 2022, Silvergate’s deposits by foreign customers amounted to 39.1% of total deposits, and the bank’s ten largest depositors accounted for 47.9% of deposits. The FDIC has specifically warned that “[c]rypto-related activities may pose significant safety and soundness risks, as well as financial stability . . . concerns,” and that “insured depository institutions face risks in effectively managing the application of consumer protection requirements, including laws related to . . . new and changing crypto-related activities.”¹⁰ The Federal Reserve has similarly warned about crypto transaction safety and soundness risks in guidance to banks including that, “*crypto-assets can be used to facilitate money laundering and illicit financing.*” (emphasis added).¹¹

Silvergate’s largest customers include foreign and U.S. crypto exchanges, money remittance services, and unregulated offshore crypto hedge funds who are high-volume money transmitters. Foreign offshore actors in the crypto space should be the subject of *enhanced* due diligence and monitoring by Silvergate, not less due diligence. In fact, CEO Alan Lane acknowledged, “The biggest risk [in banking crypto companies] is that AML risk – making sure that you know who your customers are and making sure that you’re not in any way providing

6 Silvergate Capital Corp. Investor Presentation (Nov. 1, 2022), <http://bit.ly/3W994CA>, Ex. 4.

7 Real Vision, *Banking for the Future*, interview with Alan Lane and Ben Reynolds, at 20:37, (Mar. 16, 2021), <http://bit.ly/3XfaMUI>, Ex. 5.

8 Silvergate Capital Corp., SEC Form 10-Q (Sept. 30, 2022), <http://bit.ly/3IKHad6>, Ex. 6.

9 American Banker, *Silvergate’s Home Loan bank advances are further proof of crypto contagion*, (Jan. 10, 2023), <http://bit.ly/3X6yGkR>.

10 FDIC Letter No. FIL-16-2022 (Apr. 7, 2022), <http://bit.ly/3IMLs3H>, Ex. 7.

11 Federal Reserve Supervision and Regulation Letter No. SR 22-6 / CA 22-6 (Aug. 16, 2022), <http://bit.ly/3W6j3c8>, Ex. 8.

funding, financing, et cetera for illicit activity.”¹² By any measure, Silvergate has not adequately monitored its clients for AML and fraud-related activities.

Silvergate has Objectively Failed to Comply with its KYC/AML Duties

Silvergate has, not unsurprisingly, failed to comply with its statutorily mandated KYC/AML duties with regard to its client base. Silvergate has a duty to monitor and assess the risks posed by its customers. As a “financial institution” under the Bank Secrecy Act, 31 C.F.R. § 1010.100(t), Silvergate is required to comply with FinCEN’s Customer Due Diligence (“CDD”) rule and it must maintain a Customer Identification Program (“CIP”). The CDD rule *requires* that covered financial institutions:

- (1) identify and verify the identity of customers;
- (2) identify and verify the identity of the “beneficial owners” of companies opening accounts (defined as any individual who owns 25% or more of a legal entity and individuals who controls the entity);
- (3) understand the nature and purpose of customer relationships to develop customer risk profiles; and
- (4) conduct *ongoing* monitoring to identify and report suspicious transactions and, on a risk basis, to maintain and update customer information. 31 C.F.R. § 1010–24; 1026. See <http://bit.ly/3khEObO>

The CIP rule requires that banks maintain a written CIP as part of its BSA/AML compliance program. 31 C.F.R. § 1020.220. The CIP must include risk-based verification procedures that enable the bank to form a reasonable belief that it knows the true identity of its customers. 31 C.F.R. § 1020.220(a)(2). These procedures must specify the identifying information that a bank will obtain from each customer *prior to opening an account*, which at a minimum must include the customer’s name, date of birth (for an individual), address, and identification number. *Id.*

Silvergate has not Employed Experienced KYC/AML Staff

Despite the clear statutory requirement that Silvergate assess and monitor customers before and after on-boarding, Silvergate’s executive and employee roster demonstrates an overall lack of substantial prior experience managing the significant risks associated with banking numerous, high-volume, foreign money transmitters.

Until November 2022, the Bank’s Chief Risk Officer, Tyler Pearson, was the CEO Alan Lane’s son-in-law, who had no apparent outside experience or qualifications for this role (see discussion below). Similarly, Chris Lane, son of CEO Alan Lane, was the Chief Operations Officer as of 2019.¹³

Other key risk officers such as recently departed Kathleen Fraher (current Chief Risk Officer) and Michelle Sabins (Chief Anti-Money Laundering and Sanctions Officer) are

¹² What Bitcoin Did Podcast, *Banking the Corporate Unbanked with Alan Lane* (July 16, 2019), <http://bit.ly/3W8H02g>.

¹³ See Finastra press release, *Silvergate Bank selects Finastra’s Total Payments for payment processing and innovation*, (Feb. 26, 2019), <http://bit.ly/3X6yAtz>, Ex. 91.

longtime Silvergate employees who have no disclosed prior experience in dealing with high-volume, foreign money transmitters.¹⁴ Silvergate Bank President/Chief Strategy Officer, Ben Reynolds, who Alan Lane has repeatedly credited for his role in building the crypto business and SEN blockchain network, spent six years as a software marketer immediately before joining the bank. Reynold’s current website biography claims he is a “licensed CPA,”¹⁵ however, the California CPA website states his license has actually been delinquent since 2019.¹⁶

Despite this apparent lack of experience, Silvergate and Mr. Lane have repeatedly claimed the bank performs comprehensive customer due diligence including site visits, reviews of audits and exams, that it has a “robust compliance and risk management framework,” and reviews pending and prior litigation associated with customers.¹⁷ After a customer is on-boarded, Silvergate says it deploys significant daily monitoring capabilities that are paired with ongoing enhanced due diligence.¹⁸ In a podcast interview, Alan Lane claimed, “We only bank institutions who are also serious about regulation,” and likened his diligence process to the “Good Housekeeping seal of approval.”¹⁹

Silvergate’s Customers are Known to be Involved in Money Laundering and Other Criminal Activities

Mr. Lane’s statements appear to be directly contradicted by the actual conduct of Silvergate’s clients, which displays a highly problematic pattern of alleged criminal activity, fraud, ponzi schemes, and documented instances of money laundering amounting to *billions* of dollars. The examples below demonstrate that offshore crypto exchanges, foreign criminals, sanctioned actors, and fraudsters have all used Silvergate accounts to launder money and orchestrate scams.

For example, a law enforcement affidavit in support of a forfeiture application filed in Broward County, Florida states that Silvergate’s subpoenaed records revealed \$425 million in transfers from Silvergate crypto accounts to accounts at other U.S. banks controlled by South American money launderers.²⁰ This affidavit indicates that foreign criminals were operating

¹⁴ See Ex. 9.

¹⁵ Silvergate website, *Bank Leadership*, <http://bit.ly/3D86HJZ>, Ex 10.

¹⁶ CA.gov DCA License Search, Board of Accountancy, Certified Public Accountant, Licensing Details for: 84430, <http://bit.ly/3D86HJZ>, last accessed January 13, 2022, Ex. 11.

¹⁷ See e.g., Silvergate Capital Corp. Investor Presentation, (Jan. 2021), <https://bit.ly/3Xs5ZyB> at p.13, Ex. 12.

¹⁸ I note that Silvergate insiders sold more than \$100 million of stock at significantly higher prices in the open market, likely to investors who relied on these misrepresentations from Alan Lane and Silvergate. Marketbeat, *Silvergate Capital - SI Insider Trading & Ownership*, (Jan. 13, 2023), <http://bit.ly/3XKofnl>, Ex. 13.

¹⁹ What Bitcoin Did Podcast, *Banking the Corporate Unbanked with Alan Lane* (July 16, 2019), <http://bit.ly/3W8H02g>.

²⁰ In re: Seizure of \$2,048,229.45, No. CACE-22-012446 at pp.22-23, (Broward Cty., Fla. Aug. 23, 2022), <http://bit.ly/3DaEqm3>, Ex. 14.

from within two of Silvergate’s crypto platform clients, OSL Digital and Paxos, and were using Silvergate as a point of origin to send illicitly obtained funds into the U.S. Banking system as part of a trade-based money laundering scheme. This is not an isolated instance, but is instead part of a broad mosaic of illegal activity associated with Silvergate clients, who use the bank (and Signaturebank) as a gateway to the U.S. financial system.

While Silvergate claims it conducts site visits as part of its due diligence, Silvergate customers are domiciled in exotic jurisdictions including the Seychelles, Gibraltar, Hong Kong, Mexico City, and Kenya. I doubt that Silvergate has been sending representatives to inspect these foreign premises. Similarly, while Silvergate claims to review audits of its clients, it has been widely reported that almost all of the crypto exchanges are simply unaudited.²¹ The massive FTX/Alameda fraud, by itself, demonstrates that Silvergate is incapable of properly monitoring financial transactions to detect fraud and money laundering among its clients.

FTX:

FTX, Alameda Research, and other affiliates of Sam Bankman-Fried (collectively, the “SBF enterprise”) were, until FTX’s November 2022 bankruptcy, large and important customers of Silvergate, which prominently featured a testimonial from Bankman-Fried on its website: “Life as a crypto firm can be divided up into before Silvergate and after Silvergate...” Ex. 16. In an interview prior to FTX’s collapse, Bankman-Fried candidly discussed the difficulty of securing bank accounts and stated, “We knew the banks were going to shut us down because, before, Silvergate didn’t exist.”²²

The SBF enterprise has since collapsed, and Bankman-Fried has been indicted by the S.D.N.Y. for wire and securities fraud, as well as conspiracies to violate those statutes and the federal money laundering statutes.²³ Two of his senior former FTX officers (Caroline Ellison and Gary Wang) are cooperating against Bankman-Fried and have pleaded guilty. Prior to FTX’s collapse, in August 2022, the FDIC sent FTX a cease-and-desist letter for making false claims about the bank’s deposit insurance.²⁴ The current interim-CEO of FTX, the former liquidator of the Enron fraud, has commented, “Never in my career have I seen such a complete failure of corporate controls and such a complete absence of trustworthy financial information.”²⁵

The central role of Silvergate in the FTX fraud has not gone unnoticed. Three U.S. senators wrote to Silvergate, “Your bank’s involvement in the transfer of FTX customer funds to

21 See e.g., Forbes, *Crypto Exchanges’ A La Carte Approach to Audits a Recipe for Disaster*, (Dec. 2, 2022), <http://bit.ly/3GKc2U2>, Ex. 15.

22 Video interview of Sam Bankman-Fried attached to Tweet by @Bitfinexed, (Nov. 23, 2022), 11:46 PM, <https://bit.ly/3QJDWZt>.

23 *United States v. Samuel Bankman-Fried*, No. 1:22-cr-673 (S.D.N.Y. Dec. 13, 2022), <https://bit.ly/3GGFVcf>, Ex. 17.

24 FDIC Letter to Brett Harrison, President of FTX US, and Dan Friedberg, Chief Reg. Off. of FTX US, (Aug. 18, 2022), <https://bit.ly/3IRdCuI>, Ex. 90

25 Daily Wire, *Lawyer Overseeing FTX Fallout: ‘Never In My Career Have I Seen Such a Complete Failure,’* (Nov. 17, 2022), <http://bit.ly/3H20DEY>.

Alameda reveals what appears to be an egregious failure of your bank’s responsibility to monitor for and report suspicious financial activity carried out by its clients,” and “Silvergate’s failure to take adequate notice of this scheme suggests that it may have failed to implement or maintain an effective anti-money laundering program. . . .”²⁶

Defrauded FTX customers have filed a lawsuit against Silvergate alleging the bank had “Knowledge and Participation in the FTX fraud.”²⁷ The lawsuit highlights specific customer due diligence and monitoring steps that it alleges Silvergate was *required* to perform that should have easily identified FTX’s fraudulent activity and caused Silvergate to its relationship with FTX.

The SEC has filed a detailed complaint (“SEC complaint”) against Ellison and Wang that recited how customer money was stolen from unsuspecting FTX customers who deposited approximately \$8 billion into Alameda-controlled bank accounts at Silvergate.²⁸

The SEC complaint also alleges that billions of dollars were sent from customers of Silvergate to a bank account at Silvergate held in the name “North Dimension, Inc.” (a subsidiary of Alameda), “in an effort to hide the fact that the funds were being sent to an account controlled by Alameda.” *SEC Complaint* ¶ 38. There are archived screenshots from FTX’s website showing that Silvergate was the receiving bank for North Dimension.²⁹

This Silvergate-Alameda-North Dimension banking relationship strongly suggests that Silvergate processed billions of dollars in wire transfers for North Dimension and Alameda. This money was subsequently transferred to an array of other Silvergate and non-Silvergate accounts controlled by Sam Bankman-Fried as part of his alleged fraud. In a public letter issued on December 5, 2022, Silvergate stated that it “conducted significant due diligence on FTX and its related entities including Alameda Research, both during the on-boarding process and *through ongoing monitoring*”³⁰ The facts belie this assertion.

A cursory search should have flagged “North Dimension, Inc.” as a Fake Electronics Retailer

An NBC News article stated that “North Dimension Inc. also appears to have been a fake online electronics retailer, an NBC news investigation found.”³¹ A cursory scan of the archived

26 Ltr. from Senators Elizabeth Warren and John Kennedy, and Congressman Roger W. Marshall to Silvergate Bank, (December 5, 2022), <http://bit.ly/3GZM01E>, Ex. 18.

27 Class Action Complaint at ¶ 85, *Gonzalez v. Silvergate Bank, et al.*, No. 3:22-cv-01981-BEN-WVG (S.D. Cal. Dec. 14, 2022), <https://bit.ly/3X7B0bC>, Ex. 19.

28 *SEC v. Ellison*, No. 1:22-cv-10794 (S.D.N.Y. Dec. 21, 2022), <https://bit.ly/3CLw041>, Ex. 20.

29 SG Crypto Information, *Remitting SGD from Standard Chartered to USD in FTX*, (July 1, 2021), Ex. 21; also <http://bit.ly/3XpWfFa>.

30 Public Ltr. from Silvergate Capital Corp. CEO Alan Lane, (Dec. 5, 2022), <http://bit.ly/3INSPLi>, Ex. 22.

31 NBC News, *This Little-known Firm with a Weird Website was Central to the Misappropriation of FTX Customers’ Money, Regulators Say*, (Dec. 27, 2022), <http://bit.ly/3XuhBkN>, Ex. 23.

North Dimension website reveals misspellings, other oddities, and no clear ability or means to purchase the purported electronic products. The website has been quietly deleted, but it is archived.³² If, as it claimed, Silvergate actually performed thorough diligence, I struggle to understand how it would not have identified this crude fabrication by one of its major clients.

North Dimension, Inc., was apparently receiving *thousands* of wires, from across the world, amounting to billions of dollars. The previously referenced screenshot (Ex. 21) suggests these wires would have also included memo instructions referencing specific FTX account numbers, as opposed to purchases of electronic equipment. If Silvergate was performing robust account monitoring, I do not understand why the bank apparently did not flag the activity as suspicious and close the account.

As the Office of the Comptroller of the Currency has explained, “activity inconsistent with a customer’s business” that should raise suspicion of money laundering includes “unusual transfer of funds among related accounts, or accounts that involve the same or related principals” and “a large volume of . . . wire transfers deposited into, or purchased through, an account *when the nature of the account holder’s business would not appear to justify such activity.*” (emphasis added).³³

FTX’s international crypto customers also presented heightened AML risks with, for example, public reports that the SBF enterprise was receiving “bags of cash” from individuals in Asia that were subsequently being funneled through a “networks of bank accounts.”³⁴ FTX also reportedly processed billions of dollars in transactions in Africa before its collapse.³⁵ An investigator sent us images of records suggesting that Silvergate opened bank accounts for African affiliates of FTX named “BTC Africa S.A.” and “B Transfer Services Limited.” See Ex 28. A press release issued by a Kenyan money transfer services, AZA Finance, claimed both of these entities as subsidiaries, and said that they were erroneously included in the FTX bankruptcy filing, but AZA finance admitted to having a “commercial partnership with FTX Africa.”³⁶ Unfortunately, FTX/Alameda is just the tip of the iceberg.

Bittrex:

Until it was recently deleted, Silvergate’s website featured a testimonial from the CEO of a cryptocurrency exchange named Bittrex.³⁷ According to a 2019 registration statement, Bittrex

32 Internet Archive, (Mar. 10, 2022), <https://bit.ly/3GZJuMf>, Ex. 24.

33 Off. of the Comptroller of the Currency, Money Laundering: A Banker’s Guide to Avoiding Problems, (Dec. 2002), <https://bit.ly/3IM0Ey5>, Ex. 25.

34 Financial Times, *How FTX used Hong Kong Cash-for-crypto Shop to Turbocharge Growth*, (Dec. 5, 2022), <http://bit.ly/3Zy7Yn3>, Ex. 26.

35 TechCrunch, *FTX Processed Billions Monthly in Africa Before Going Bust*, (Nov. 21, 2022), <http://bit.ly/3X7tL3b>, Ex. 27.

36 AZA Finance, Statement, *AZA Finance Issues Correction to Erroneous Inclusion in FTX Chapter 11 Bankruptcy Filing*, (2022), <https://bit.ly/3QK3LZy>, Ex. 29.

37 Bittrex Statement from Silvergate Website, Ex. 30.

was a 4.72% shareholder of Silvergate bank.³⁸ Bittrex’s website also stated it was a Silvergate customer and used the SEN network.³⁹

In October 2022, OFAC and FINCEN announced two enforcement actions against Bittrex. The actions identified violations of multiple sanctions programs and willful violations of the BSA/AML and SAR reporting requirements.⁴⁰ Specifically, “Bittrex conducted over 116,000 transactions valued at over \$260 million with entities and individuals located in jurisdictions subject to comprehensive OFAC sanctions, including transactions with entities and individuals operating openly from OFAC-sanctioned jurisdictions such as Iran, Cuba, Sudan, Syria, and the Crimea region of Ukraine.” *Id.*

In 2019, the New York Department of Financial Services issued a cease-and-desist letter to Bittrex which highlighted BSA/AML/OFAC deficiencies. The letter specifically noted how Bittrex accounts reflected false information and were registered under aliases such as “Give me my money,” “Donald Duck,” “Elvis Presley,” and other false names.⁴¹ The letter concluded, “Bittrex has failed to demonstrate responsibility, financial and business experience or the character and fitness to warrant the belief that its business will be conducted honestly, fairly, equitably and carefully.”⁴² The NY Department of Financial Services denied Bittrex’s application to engage in a Virtual Currency Business Activity, citing a litany of BSA/AML/OFAC deficiencies.⁴³

Bittrex itself is a defendant in an ongoing civil racketeering lawsuit alleging that it engaged in a fraudulent money laundering scheme with other crypto parties including Tether, Bitfinex, and Reggie Fowler.⁴⁴ The lawsuit alleges that Bittrex processed billions of transactions as part of the scheme. Fowler recently pleaded guilty to federal money laundering charges.⁴⁵

38 Silvergate Capital Corp. Registration Statement, Form S-1/A, (Oct. 28, 2019), <http://bit.ly/3CL8BzE>, p.142, Ex. 31.

39 Bittrex Corporate Account Website Excerpt, <https://bit.ly/3IlyKD5>, last accessed Jan. 13, 2023 Ex. 32.

40 U.S. Dep’t of the Treasury, *Treasury Announces Two Enforcement Actions for over \$24M and \$29M Against Virtual Currency Exchange Bittrex, Inc.*, (Oct. 11, 2022), <http://bit.ly/3H4mDio>, Ex. 33; FinCEN Press Release, *FinCEN Announces \$29 Million Enforcement Action Against Virtual Asset Service Provider Bittrex for Willful Violations of the Bank Secrecy Act*, (Oct. 11, 2022), <http://bit.ly/3QzvfB3>, Ex. 34.

41 N.Y. Dep’t of Financial Servs., Cease-and-Desist Letter: Bittrex’s Inadequate Customer Due Diligence, Ex. 35.

42 N.Y. Dep’t of Financial Servs., Cease-and-Desist Letter: Bittrex’s Inadequate Capital, Ex. 36.

43 N.Y. Dep’t of Financial Servs., (Apr. 10, 2019), full letter available here: <http://bit.ly/3kdvLZc>.

44 Class Action: *In re Tether and Bitfinex Crypto Asset Litigation*, No. 1:19-cv9236(KPF), (S.D.N.Y. June 5, 2020), <https://bit.ly/3WgAVAW>.

45 U.S. Atty’s Off., S.D.N.Y., Press Release, *Former Co-Owner of Vikings Pleads Guilty to Providing Shadow Banking Services to Cryptocurrency Exchanges*, (Apr. 25, 2022),

I question how these public filings possibly reconcile with Silvergate’s stated customer due diligence process and ‘culture of compliance’ requirements.

Binance:

Silvergate has also had an extensive banking relationship with Binance, a large cryptocurrency exchange that has repeatedly declined to reveal where its headquarters are located. Binance is reportedly being investigated by the Justice Department for money laundering.:

- Reuters, *How Binance Became a Hub for Hackers, Fraudsters, and Drug Traffickers*, June 6, 2022, <http://bit.ly/3H0nzEy>, Ex. 38.
- Reuters, *Crypto Exchange Binance Helped Iranian Firms Trade \$8 Billion Despite Sanctions*, Nov. 7, 2022, <http://bit.ly/3H2vJw6>, Ex. 39.
- Investopedia, *Binance CEO Facing Possible Money Laundering Charges*, Dec. 12, 2022, <http://bit.ly/3X7ARol>, Ex. 40.
- Wall St. J., *SEC Probes Trading Affiliates of Crypto Giant Binance’s U.S. Arm*, Feb. 15, 2022, <http://bit.ly/3QKC42D>, Ex. 41.

Binance directed its international customers to deposit funds into a Silvergate bank account for an entity named “Key Vision Development Limited.”⁴⁶ This was a Seychelles shell company that a Seychelles government notice says was struck off the corporate register in June 2021. In June 2021, Silvergate reportedly discontinued its banking relationship with Binance’s International arm.⁴⁷ However, Silvergate declared that Binance.US, a purportedly independent entity, remained a “customer in good standing.”⁴⁸

Reuters reported that Binance.US is *not* independent but instead there is ample evidence to conclude that it is controlled from abroad by Binance International.⁴⁹ Reuters stated, “Almost half the U.S. compliance team quit by mid-2022 after a new U.S. boss was appointed by [Changpeng] Zhao, according to four people who worked at Binance.US. The staff left, these people said, because *the new chief pushed them to register users so swiftly that they couldn’t conduct proper money laundering checks.*” *Id.* (emphasis added). *Id.* A crypto investigator with a history of detecting fraud has also raised questions about whether Binance.US is essentially a “fake exchange.”⁵⁰

<http://bit.ly/3GFg5FH>, Ex. 37.

46 See Ex. 42.

47 The Block, *Silvergate Bank Cuts Ties with Binance, Disabling USD Deposits and Withdrawals*, (June 10, 2021), <http://bit.ly/3WbChNr>, Ex. 43.

48 Binance.US, Tweet by @silvergatebank, (June 10, 2021), 4:07 PM, Ex. 44.

49 Reuters, *How Binance CEO and Aides Plotted to Dodge Regulators in U.S. and UK*, (Oct. 17, 2022), <http://bit.ly/3GYVA7h>, Ex. 45.

50 Dirty Bubble Media, *Is Binance.US a Fake Exchange?* (Dec. 18, 2022), <http://bit.ly/3CMrJxq>, Ex. 46.

Bitso:

Bitso, a Mexican and Colombian crypto exchange, is another Silvergate banking customer. Barry Silbert's DCG lists Bitso as a Portfolio company on its website.⁵¹ Bitso's slogan is "Send money as easy as ordering a pizza." It is a large money remittance service, reportedly sending \$1 billion between Mexico and the US during the first half of 2022.⁵² Bitso's website declared customers have "total protection since Silvergate Bank, Bitso's partner bank, is backed by the Federal Deposit Insurance Corporation (FDIC)."⁵³ The representation of FDIC insurance is a false statement that should have been spotted and corrected by Silvergate, in light of the FDIC's August 2022 cease-and-desist letter to FTX.

A Reuters article describing how drug cartels launder money through crypto specifically identified a notorious sex trafficker who was caught laundering money through Bitso.⁵⁴ News reports also describe how cartels use a money laundering technique called "smurfing," which involves splitting funds into small (under \$10,000) deposits or transfers (presumably to avoid CTRs). A Brazilian gang, using Bitso, was caught using this method to launder a kidnapping ransom.⁵⁵

Houbi/Tron/Justin Sun:

Silvergate also banks Huobi, a Chinese crypto exchange which is apparently registered in Gibraltar.⁵⁶ Instances of criminal activity and problems at this exchange include:

- A 2020 report by Blockchain analytics company Chainalysis stated that Huobi and Binance were used for billions of dollars of transfers by criminal elements.⁵⁷
- A Reuters article in June 2022 found that North Korea's Lazarus hacking group, which aims to fund North Korea's nuclear weapons program, used Binance and Huobi to launder money.⁵⁸

51 Digital Currency Group, *Portfolio*, <https://bit.ly/3IJ13S3>, Ex. 47.

52 CoinDesk, *Bitso Processed \$1B in Crypto Remittances Between Mexico and the US So Far in 2022*, (June 16, 2022), <http://bit.ly/3iC4iQt>, Ex. 48.

53 Bitso Website Excerpt, *Frequently Asked Questions: Dólares Americanos*, (translated to English with Google Translate), <https://bit.ly/3IOTiKr>, Ex. 49.

54 Reuters, *INSIGHT-Latin American Crime Cartels Turn to Crypto to Clean Up Their Cash*, (Dec. 8, 2020), <http://bit.ly/3iz94OP>, Ex. 50.

55 Criptofacil, *Criminals Who Kidnapped and Extorted Bitcoin from Investor are Identified Thanks to Blockchain*, (English translation) (June 27, 2022), Ex. 51.

56 See Ex. 53.

57 Cryptoslate, *Chainalysis Says Binance and Huobi Allegedly Used for Billions of Dollars in Criminal Bitcoin Activity*, (Jan. 17, 2020), <http://bit.ly/3H2DORs>, Ex. 54.

58 Reuters, *How Crypto Giant Binance Became a Hub for Hackers, Fraudsters and Drug Sellers*, (June 6, 2022), <http://bit.ly/3H0nzEy>, Ex. 55.

- Crypto investigators found a high volume of direct interactions between Huobi and Binance with the now-seized Hydra Market, in an article that specifically cited KYC laxity at these exchanges.⁵⁹

BNC: You used fake Borat and Taylor Swift identities to successfully pass the first tier of KYC on KuCoin and Huobi. For the exchanges to approve these identities, what do you think was happening on their end?



- Indeed, the KYC at Huobi is apparently so lax that a crypto investigation firm, CipherBlade, was able to open accounts at Huobi using fake IDs posing as a bearded Taylor Swift and as the comedian Borat.⁶⁰
- Even the Chinese government has cracked down on a large money laundering gang using Houbi, Binance, and OKEX (an exchange mentioned later in this memo).⁶¹
- Thailand revoked Houbi’s license in 2022, citing compliance deficiencies.⁶²
- Fraudsters perpetrating scams allegedly run rampant on Huobi, yet lawyers for victims are left with only a Seychelles mailing address, where Huobi *has no physical presence*, allowing criminals to “escape with their loot.”⁶³

Justin Sun reportedly acquired Huobi in 2022 after the exchange was purchased by an unknown party. Sun has been called “the Theranos of China,” and an outright fraud.⁶⁴ Sun is reportedly under FBI investigation for fraud and money laundering.⁶⁵ According to the same article, Sun would scream “**fake the KYC! . . . Fake it!**” to employees of a different exchange

59 U.S. Dep’t of Just., Off. of Pub. Affs., Press Release, *Justice Department Investigation Leads to Shutdown of Largest Online Darknet Marketplace*, (Apr. 5, 2022), <http://bit.ly/3CLv12M>, Ex. 56; Verdict, *Dirty Bitcoin: Exchanges’ KYC Laxity Eases Money Laundering – Report*, (Oct. 27, 2021), <http://bit.ly/3Wbk96r>, Ex. 57.

60 Brave New Coin, *Security Expert Says KuCoin and Huobi Epicly Fail Softball KYC Test*, (Dec. 14, 2020), <http://bit.ly/3QzYGCZ>, Ex. 58.

61 CoinCu, *Crypto Criminals Have Lent the Hands of Major Exchanges to Launder Money*, (Oct. 13, 2021), <http://bit.ly/3w3c09i>, Ex. 59.

62 TechCrunch, *Crypto Exchange Huobi Thailand Closing Down in July After License Revoked*, (June 16, 2022), <http://bit.ly/3XvLO2Q>, Ex. 60.

63 Global Anti-Scam Org, *How Huobi and Other Exchanges Work for Scammers*, (July 3, 2022), <https://bit.ly/3GHZHUK>, Ex. 61.

he ran, Poloniex. *Id.* The article also states that Sun is described as a “connoisseur of bank accounts” because “banks froze his money so frequently he needed to spread his fortune across numerous accounts.” *Id.* In a 2019 interview in which he praised Silvergate, Sun said crypto bankers would “get arrested or even charged for money laundering” before Silvergate emerged.⁶⁶

In an online video posted on Twitter, Sun stated that he “collaborated with Silvergate” for a coin issued by his company, Tron. Tron had earlier forged a relationship with Alameda Research as a “whitelisted institution.”⁶⁷

There are numerous publicly available articles documenting the alleged serial frauds carried out by Justin Sun, his company Tron, and the Huobi crypto exchange. Why did Silvergate’s KYC/AML compliance team overlook them? Where was the due diligence?

Stefan He Qin:

A 24-year-old Australian national named Stefan He Qin was sentenced to prison last year after orchestrating a \$90 million Ponzi scheme.⁶⁸ Documents included in a filing by the SEC revealed that Silvergate had opened *twelve* accounts under various names for Qin.⁶⁹

Brendon Blumer:

In November, Brendan Blumer, a Hong Kong crypto operator (who has renounced his U.S. citizenship), and his company Block.one, purchased more than 9% of Silvergate stock.⁷⁰

Blumer is also the Chairman of a Gibraltar-registered crypto exchange named Bullish.com.⁷¹ Bullish.com’s website states that “Silvergate Bank is our fiat custody partner for deposits and withdrawals.”⁷² A Bloomberg article describes a research paper alleging that Block.one engaged in market manipulation of a token it issued and states, “The U.S. Securities and Exchange Commission fined Block.one \$24 million in 2019 for failing to register the ICO,

⁶⁴ Observer, *Warren Buffet’s 28-Year-Old Power Lunch Guest is a Fraud, Say Those Close to Him*, (July 24, 2019), <http://bit.ly/3QH0Dxl>, Ex. 62; Crypto.News, *Tron Founder Justin Sun Takes over Huobi Global*, (Nov. 16, 2022), <http://bit.ly/3GHL6Zy>, Ex. 63.

⁶⁵ The Verge, *The Many Escapes of Justin Sun*, (Mar. 9, 2022), <http://bit.ly/3w23TKk>, Ex. 64.

⁶⁶ Abra, *Money 3.0: Justin Sun from TRON*, (Dec. 3, 2019), <http://bit.ly/3GGK00k>, Ex. 65.

⁶⁷ Tweet by @trondao, (June 22, 2022), 12:03 AM, <https://bit.ly/3kb0PsC>. See also Ex. 66.

⁶⁸ U.S. Atty’s Off. S.D.N.Y, Press Release, *Founder of \$90 Million Cryptocurrency Hedge Fund Sentenced to More Than Seven Years in Prison*, (Sept. 15, 2021), <http://bit.ly/3XxSGwR>, Ex. 67.

⁶⁹ See [Proposed] Temporary Restraining Order Freezing Assets at 4, *SEC v. Qin*, No. 1:20-cv-10849-LGS (S.D.N.Y. Dec. 22, 2020), <https://bit.ly/3X9EtGB>, Ex. 68.

⁷⁰ Wired, *EOS Was the World’s Most Hyped Blockchain. Its Fans Want It Back*, (May 10, 2022), <http://bit.ly/3XbvDba>, Ex. 69; B1, Press Release, *B1 Acquires Significant Equity Stake in Silvergate Capital Corp.*, (Nov. 24, 2022), <http://bit.ly/3iJbbiS>, Ex. 70.

⁷¹ Bullish.com, *About Us*, <https://bit.ly/3GGW1ms>, Ex. 71.

⁷² Bullish.com, *Viewing FX (fiat exchange) Rates*, <https://bit.ly/3khy5yg>, Ex. 72.

and token holders sued Block.one last year, calling the sale a ‘fraudulent scheme’ and alleging that the company violated securities laws by making ‘false and misleading statements about EOS, which artificially inflated the prices for the EOS securities and damaged unsuspecting investors.’”⁷³ In 2020, investors filed a class action lawsuit alleging that Block.one orchestrated the “biggest of all crypto frauds” in a “coin-offering scam netted company billions.”⁷⁴

Celsius Network:

Bankruptcy documents associated with this collapsed crypto lender that we reviewed show that it had Silvergate bank accounts and executed a mutual non-disclosure agreement with Silvergate.⁷⁵ The New York Attorney General recently filed a civil lawsuit alleging the founder of Celsius defrauded investors out of billions of dollars.⁷⁶

Okcoin:

Okcoin is the US crypto exchange of the OK Group, which also operates an international exchange named OKX (aka OKEx) and which has a sister exchange in the U.S., OKCoin.⁷⁷ OK Coin’s website states that it uses Silvergate’s SEN Network and solicits users to deposit funds via Silvergate.⁷⁸ OK’s Chinese founder, Star Xu, has reportedly been arrested twice by the Chinese government.⁷⁹ A 2018 report issued by an experienced crypto trader concluded that “approximately 93% of OKEx’s volume was fabricated.”⁸⁰ In March, 2022 OKX reportedly rejected calls to ban Russian crypto transactions.⁸¹ Hackers who drained FTX of over \$450 million in assets after it filed for bankruptcy reportedly used OKX to launder the money.⁸²

73 BNN Bloomberg, *Billionaire-backed Exchange Funded by Alleged Scheme to ‘Pump’ Price*, (Sept. 2, 2021), <http://bit.ly/3IH7HIu>, Ex. 73.

74 Class Action Complaint, *Hong v. Block.One*, No. 1:20-cv-03829 (S.D.N.Y. May 18, 2020) <https://bit.ly/3IJ2jo3>, Ex. 74; see also <http://bit.ly/3CLL5CP>, Ex. 75.

75 Celsius Network Bankruptcy Documents, <https://bit.ly/3CLjr99> at p.264, Ex. 76.

76 Wall St. J., *Celsius Co-founder Sued by New York Attorney General*, (Jan. 5, 2023), <http://bit.ly/3H3AcPh>, Ex. 77; see also CoinDesk, *Celsius Resembled Ponzi Scheme at Times, Vermont Regulator Says*, (Sept. 7, 2022), <http://bit.ly/3CHP435>, Ex. 78.

77 The Ascent, *OKX Review: Robust Trading Suite for Cryptos, Derivatives, Staking, and Lending*, (May 16, 2022), <http://bit.ly/3vZMx0q>, Ex. 79.

78 Okcoin.com, *Okcoin Fee Rates*, <https://bit.ly/3X82gXf>, Ex. 80.

79 Forbes, *Chinese Founder Of OKEx Crypto Exchange ‘Arrested’ Again; Whales Bail*, (Oct. 16, 2020), <http://bit.ly/3H2H5jX>, Ex. 81.

80 Investopedia, *Are Crypto’s High Trading Volumes a Scam?* (Sept. 1, 2021), <http://bit.ly/3GBIFJj>, Ex. 82.

81 PYMNTS.com, *Binance, OKX Reject Calls to Ban Russian Crypto Transactions*, (Mar. 2, 2022), <http://bit.ly/3XrXeod>, Ex. 83.

82 Cointelegraph, *FTX Hacker Reportedly Transfers a Portion of Stolen Funds to OKX After Using Bitcoin Mixer*, (Nov. 29, 2022), <http://bit.ly/3iCCawK>, Ex. 84.

Voyager:

Bankruptcy documents we reviewed for Voyager state that it also had a Silvergate bank account.⁸³ A civil lawsuit against Voyager, filed after its collapse, has accused Voyager of operating a “massive” Ponzi scheme.⁸⁴ The FDIC previously issued a Cease and Desist letter to Voyager for falsely claiming it was FDIC insured.⁸⁵

Silvergate has a Questionable Relationship with the Government of El Salvador

Silvergate also works with the El Salvador government, on a project with Bitso, to facilitate payments for the government’s Bitcoin Chivo Wallet. The U.S. Treasury department has stated, “Salvadoran President Nayib Bukele’s administration provided financial incentives to Salvadoran gangs MS-13,” and has moved to designate and sanction officials close to the administration.⁸⁶ I do not understand how Silvergate could have addressed, let alone managed, risks associated with processing payments for this foreign government’s crypto project.

If, as Alan Lane has claimed, Silvergate has robust KYC/AML procedures, how has Silvergate missed all of these enormous red flags?

The exhibits referenced in this letter may also be downloaded as a single (large) PDF file from this Dropbox address:

I am available to meet you and to discuss the documentary records and additional knowledge I have pertaining to Silvergate, if you feel that would be useful.

Thank you.

Marc Cohodes.

83 Voyager Bankruptcy Document Excerpt, Ex. 85.

84 Class Action Complaint, *Robertson v. Cuban*, 1:22-cv-22538 (S.D. Fla. Aug. 10, 2022) <https://bit.ly/3WdX8zA>, Ex. 86; *see also* <http://bit.ly/3X61x94>, Ex. 87.

85 FDIC, Joint Letter Regarding Potential Violations of Section 18(a)(4) of the Federal Deposit Insurance Act, to Stephen Erlich, CEO, Voyager, (July 28, 2022), <https://bit.ly/3QKGVRY>, Ex. 88; *see also* Voyager Tweet claiming up to \$250,000 in FDIC Insurance for USD accounts, Ex. 89.

86 CoinDesk, *Bitso is Providing the ‘Core Service’ for El Salvador’s Chivo Bitcoin Wallet*, (Sept. 8, 2021), <http://bit.ly/3QBdBwL>, Ex. 52.