

BETWEEN THE LINES

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Deltec Cryptic About Crypto Reserves

Introduction

An author using the name Crypto Anonymous posted an article called "The Bit Short: Inside Crypto's Doomsday Machine" on *Medium* on January 14, 2021. The former bitcoin investor alleged that Tether, a stablecoin supposedly backed one-to-one by U.S. dollars, is a fraud. Among the concerns raised in the article was that Tether is not fully backed. Eight days later, Gregory Pepin, Deputy CEO of Deltec Bank and Trust, Tether Limited's Bahama-based bank, was interviewed on the January 22, 2021, YouTube Unchained Podcast "Unconfirmed." Mr. Pepin claims that Tether's stablecoin is fully backed by reserves. We applied our Tactical Behavior Assessment[®] (TBA) methodology to analyze Mr. Pepin's responses to questions in the interview to evaluate the reliability of his statements. Below, we show what our unique behavioral lens reveals about Mr. Pepin's perspective on Tether's reserves.

Reserve Reservations

In the *Medium.com* article, Crypto Anonymous builds the case that Tether was not fully funded by referencing data showing that from January 2020 through September 2020, the amount of foreign currencies held by all Bahamian domestic banks increased by B\$ 600 million, going from B\$ 4.7 billion to B\$ 5.3 billion. However, Crypto Anonymous says that during the same timeframe, total Tether issued increased by B\$ 5.4 billion, going from B\$ 4.6 billion to B\$ 10 billion. The assumption is that if all Tether issues were fully backed with reserves, the foreign currencies held in Bahamian domestic banks would be much higher. When Mr. Pepin is asked to explain the discrepancy, he begins his response, instead, by attacking the credibility of Crypto Anonymous, characterizing him/her as a "so called expert" and questioning his/her motives. His impulse to do so rather than simply answer the question suggests that the accusations have some merit. Indeed, when he does eventually address the question, his response falls short of setting the record straight. Mr. Pepin explains that because Deltec is not a domestic bank, the currencies the bank holds would not be reflected in regulatory reports about domestic bank holdings. However, he goes on to say that the size of the overall banking market in the Bahamas is around \$200 billion and that "we are part of that." Mr. Pepin highlights this information to imply that Tether is fully backed, but he does not provide specifics to prove the point. Instead, he merely states that "every Tether is backed by 'a reserve'" and "I can confirm that." Without facts to substantiate his claims, his statements fall short of conclusive evidence. Furthermore, the phrase that he can confirm Tether is backed by "a" reserve is not the same as saying Tether is fully backed. Also, while he *now* says he "can confirm" that every Tether is backed, this may not have been the case during the January to September 2020 timeframe, leaving open the possibility that at that time, Tether was not fully backed.

As follow-up, the interviewer asks if all of Tether's reserves are held by Deltec, Mr. Pepin initially attempts to gloss over the question, saying that "the entire reserve is there" and does not indicate whether the bank holds the reserves. When asked a second time, however, Mr. Pepin says the reserve is held by Deltec and "probably" other institutions. This is an attempt to give the impression that Tether is fully backed, but at the same time provide an excuse for why an examination of Deltec's holdings may not square with Tether's issuance. This suggests that Mr. Pepin is unable to confirm that Tether is fully backed. Furthermore, Mr. Pepin shifts the conversation away from the question and back to the article. He launches into a lengthy, overly detailed explanation of how currency trading and banking work, saying he wants to "clarify" other points in the article. But this information has nothing to do with the topic of Tether. This maneuver doubles as yet another attempt to discredit the "so-called trading expert" and distract from the topic of Tether's reserves. In the end, Mr. Pepin's repeated effort to discredit the accusations, coupled with his qualified statements and efforts to refocus attention, **provides behavioral evidence to conclude that the accusation that Tether is not fully backed has merit, and that Deltec's claim that Tether is fully backed is likely not completely accurate.**

Cash Equivalents Equivalent to What?

Given that Tether has acknowledged that their reserves include traditional currency, cash equivalents, and may include other assets and receivables from loans, Mr. Pepin is asked if Deltec holds the cash equivalent components of Tether's reserves, Mr. Pepin initially skirts the question by casting Deltec's treasury management of Tether's assets as routine and vaguely explaining the cash equivalents might be t-bills, time deposits and "things like that." When pressed whether he knows what the cash equivalents are, he purses his lips and says "mmm, yep" and pauses before saying that Deltec is the custodian of the cash equivalents, signaling discomfort with the topic. Notably, he takes the opportunity to emphasize that Deltec is not involved with these investments. This, coupled with his reluctance to admit that Deltec holds the cash equivalents, indicates that he has undisclosed concerns about the assets.

Mr. Pepin is then asked what risks Tether's cash equivalent reserves pose to investors. Mr. Pepin immediately reemphasizes that Deltec is not involved in Tether's investments to distance the bank from any responsibility. He then goes on to protest several times that "as far as I can tell," Tether is "following the regular treasury management you would imagine for managing such reserve[sic]." The phrase "as far as I can tell" suggests that Mr. Pepin suspects that Tether may not be fully compliant with treasury management protocols, and the protests that Tether is "following the regular treasury management" fall short of addressing what type of risk these cash equivalent assets pose to investors. In fact, it is notable that Mr. Pepin does not take the opportunity to say that these assets pose little or no risk. **The behavioral indicators in these responses provide strong behavioral evidence to conclude that Mr. Pepin believes Tether's cash equivalent reserves pose a meaningful risk to investors.**

Bitcoin in Tether's Back Pocket?

Deltec recently announced that it is investing some customer funds in bitcoin, which has raised questions in the media of whether the purchases were made to back Tether. Mr. Pepin is asked plainly what the purpose of the purchases was. He answers, saying that the purpose of Deltec's purchases of bitcoin were part of an "overall strategy" for the bank's high-net-worth asset management customers. While this may be true, his response is coupled with concerted efforts to dismiss the validity of claims that these purchases were made for Tether and to boost the credibility of his own claims. He again discredits the claims of "so-called journalists" and then repeatedly reminds viewers that the bank is 70 years old to convince them that Deltec would not engage in illegal or unethical activity. His need to shape perceptions of his explanation in this way suggests there is more behind the purpose of these purchases than disclosed. Furthermore, he qualifies his statement that "I believe" Tether denied that Deltec purchased bitcoin for them, which affords Mr. Pepin latitude should it come out that some of these purchases were indeed made on behalf of Tether. Mr. Pepin's statement that "we try to deny it" but that in the end "they have their own truth and we have ours" and that "you can't convince everyone" on the surface seems like a legitimate frustration. However, it is notable that he does not take the opportunity to specifically say that the bitcoin purchases were not made on Tether's behalf. Ultimately, **this response does not reliably rule out the possibility that Deltec did, in fact, purchase bitcoin for Tether.**

Audit Schmaudit!

The interviewer references Mr. Pepin's previous statement that Deltec holds Tether's reserves and the fact that Tether has famously never had a true audit of its books. She then asks if this gives Deltec pause. Mr. Pepin does not deny the idea, and is somewhat defensive. He dismisses the value of audits, protesting that they are "usually very useful" but in the cases of Wirecard and Enron, audits "didn't unveil the fraud that was there." He also goes to great lengths to convince viewers that since Deltec conducted thorough due diligence and that "we don't trust, we verify," there is no risk associated with Tether's finances. His concerted effort to downplay the value and need for a closer look at Tether's finances reveals significant anxiety around the potential of an audit. Furthermore, Mr. Pepin qualifies several of his statements. He protests that Tether is "pretty much" following what everybody is expecting them to follow, which suggests that there are some rules or procedures they are not following. Mr. Pepin also qualifies that Deltec "from time to time" checks to make sure that Tether's reserve "in general" is "pretty much matching" and that there are "no crazy things going on." The phrases "time to time," "in general" and "pretty much" suggest that Deltec is not as diligent in monitoring Tether and holding them accountable as he implies. Furthermore, the characterization of "crazy" only rules out the extreme, suggesting that Deltec has or will tolerate some level of deviation from the rules on Tether's part. Altogether, **the behaviors Mr. Pepin exhibits in this response suggest that he is indeed uncomfortable with the fact that Tether has not been duly audited, but also that Deltec is to some degree culpable for the state of Tether's finances.**

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