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To: Sarah Jane Hughes, Members, and Observers; ULC Regulation of Virtual Currency Businesses Act Committee.

Coin Center generally supports the current draft of the Uniform Regulation of Virtual Currency Businesses Act (RVCBA). We welcome the opportunity to submit a brief written comment to the committee outlining our residual concerns with this important model legislation.

Definition of "Bank" and Exemption for Federally Chartered Entities

As the Reporter's notes indicate, a recent decision from Office of the Comptroller of the Currency (OCC) to entertain applications for a special purpose national bank charter from so-called fintech firms[1] (virtual currency firms potentially among them) raises the question of whether the RVCBA's licensing requirements would be preempted as applied to businesses that obtain a federal fintech charter. The current draft RVCBA defines "bank" for the purposes of exemptions in a narrow manner that would leave the act's application to a future fintech-chartered bank undetermined. The OCC, however, has made it very clear that, under existing law and guidance, all licensing laws *will* be preempted as applied to fintech charter holders:

> A special purpose national bank also has the same status and attributes under federal law as a full-service national bank. State law applies to a special purpose national bank in the same way and to the same extent as it applies to a full-service national bank. Limits on state visitorial authority also apply in the same way. A special purpose national bank would look to the relevant statutes (including the preemption provisions added to the National Bank Act by Dodd-Frank), regulations (including the OCC's preemption regulations), and federal judicial precedent to determine if or how state law applies. For example, under these statutes, rules, and precedents, state laws

[1] Department of the Treasury, Office of the Comptroller of the Currency, *Exploring Special Purpose National Bank Charters for Fintech Companies* (Dec 2016) *available at* https://www.occ.treas.gov/topics/bank-operations/innovation/special-purpose-national-bank-charters-for-fintech.pdf.

would not apply if they would require a national bank to be licensed in order to engage in certain types of activity or business.[2]

No further rule needs to be promulgated for the OCC to begin chartering special purpose fintech banks, and the OCC appears to have no intention to promulgate any new rule on the subject of federal preemption or the fintech charter.[3] Therefore, existing law as described in the above passage will control. In light of this, the RVCBA should avoid conflict with federal laws and provide an exemption from licensing for *any* federally chartered bank, regardless of type.[4] This could be accomplished by broadening the definition of "bank" as follows (new language bolded and italicized):

> "Bank" means a person engaged in the business of banking. The term includes a savings bank, savings and loan association, credit union, ***and any federally-chartered entity under the the National Bank Act, 12 U.S.C Chapter 2***. The term does not include a ***state-chartered*** trust company, limited purpose trust company, or industrial loan company**.**

Virtual Currency "Exchange"

We are grateful to the committee members for their sensitivity to the issue of exempting fully automated virtual currency exchange technologies, *e.g.* sidechains. We agree that these technologies and their developers should not be swept into a licensing requirement that is aimed at custodial businesses. However, the current drafting of this definition remains somewhat convoluted. We propose moving the "custody or control" language to the top of the definition, to indicate that it is a prerequisite for any of the covered exchange activities defined therein, and including the "on behalf of a resident" language found in the other defined verbs, "transfer" and "storage." The revised definition would then read:

> (7) "Exchange" means to assume custody or control of virtual currency on behalf of a resident, at least momentarily, in order to sell, trade, or convert:
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> (A) virtual currency for legal tender or for one or more forms of virtual currency; or
> (B) legal tender for one or more forms of virtual currency.

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[2] *Id* at 5.

[3] "The OCC has authority to grant charters for national banks and federal savings associations under the National Bank Act and the Home Owners' Loan Act, respectively. That authority includes granting charters for special purpose national banks. … there is no legal limitation on the type of "special purpose" for which a national bank charter may be granted, so long as the entity engages in fiduciary activities or in activities that include receiving deposits, paying checks, or lending money. As the next section describes, the OCC has the legal authority to construe these activities to include bank-permissible, technology-based innovations in financial services." *Id*.

[4] We remain indifferent to the related but distinct question of whether *state* chartered limited-purpose banks, trust companies, or special purpose vehicles should be exempt.

Virtual Currency "Transfer"

The draft definition of virtual currency "transfer" is very clear with the exception of sub-point (C), which deals with "changing the location of virtual currency from this state to another state or from this state to another jurisdiction." Virtual currency does not exist in any state or other physical location. Keys or credentials necessary to spend virtual currency may exist recorded in physical media and kept in various locations simultaneously, however these keys are not the virtual currency itself; they are merely data necessary to transact. The particular choice of where or how to store these keys is, we believe, inconsequential to any jurisdictional, definitional, or scope-related question in this law. This act applies if one is engaged in a covered activity with a resident of the state. The question of how that activity is facilitated and where the facilities exist to enable that activity is immaterial. Either the business is engaged in a regulated activity with the resident or it is not. We therefore ask that sub-point (C) be struck from the definition. This would create clarity and, we believe, would not alter the substantive policy result of the law in any way.

Virtual Currency "Storage"

The definition of virtual currency storage could be simplified without changing its meaning. As currently drafted it includes both "maintaining custody or control of virtual currency" and "maintaining custody or control of virtual currency credentials." The definition of "control" already includes "possession of sufficient virtual currency credentials" therefore the second part of the "storage" definition relating to credentials is superfluous and prone to causing confusion. A simpler definition of "storage": "maintaining custody or control of virtual currency on behalf of a resident" is sufficient to cover those in possession of credentials (as per the definition of control). Additionally, the language that follows: "by any person other than the resident" is unnecessary and confusing given the exemption of personal activities within the scope section (and discussed in the next part of this letter). For clarity we prefer a streamlined definition of storage as follows:

> (20) Storage means "maintaining custody or control of virtual currency on behalf of a resident."

Exemption for Personal Use

We strongly agree with the substantive policy goal behind the exemptions at §103(5), (6), (10)(b), and (10)(c). Individuals should *only* be required to seek licenses when dealing with *another person's* virtual currency and *never* when dealing merely with *their own virtual currency* (regardless of whether they obtained it via mining, investing, in return for the sale of a good or service, etc.). We believe that these four separate exemptions could be simplified into a single exemption to provide clarity with regard to this essential point. Our suggestion is as follows, §103 should include one passage (rather that four) which exempts:

(#) a person that mines, manufactures, exchanges, or otherwise obtains convertible virtual currency and uses it solely for personal purposes if the person does not engage in any virtual currency business activity on another person's behalf. Personal purposes include buying or selling virtual currency as an investment, and obtaining virtual currency as payment for the purchase or sale of goods or services.

Dual Licensure

A virtual currency business that also deals in legal tender (*e.g.* an exchange) should not need to acquire both a money transmission license and a virtual currency license. Both types of licenses aim to accomplish the same thing. They are meant to ensure that companies are well-run, well-capitalized, and adequately serve consumers in a compliant manner. If a state MTL regulator has authorized a business with only one license to perform both activities and has, via her discretion, sought additional security necessary to guarantee the solvency of the business, then there is no apparent public benefit from going through the expense and trouble of formally acquiring a second license.

While we might reasonably expect state regulators who enforce both existing MTL law as well the RVCBA to consolidate their licensing and examination of exchanges into a single proceeding that results in two licenses, this outcome should not be left to chance and regulatory discretion alone. The RVCBA should include language within its scope section that explicitly exempts licensed businesses as follows:

(#) a person licensed as a money transmitter in this state who has been authorized by the [superintendent][5] to deal in virtual currencies as well as legal tender.

Similarly, a legislative note within the RVCBA should suggest that the legislature amend the state's money transmission law to include a reverse exemption for licensed virtual currency businesses:

(#) a person licensed as a virtual currency business in this state who has been authorized by the [superintendent] to deal in virtual currencies as well as legal tender.

Minimum Net Worth, Permissible Investments, UCC Article 8.

Each of these topics deals with the essential question of guaranteeing the solvency of a licensed business, and the safety of a customer's property right to the custodied valuables. On these topics we believe that the RVCBA should, as best as possible, mirror existing MTL law and avoid creating heightened or incongruous obligations for virtual currency firms. Both MTL law as well as this proposed model law aim to protect consumers from risks posed by businesses that hold their valuables (whether as dollars in the MTL context or virtual

[5] We note that the term superintendent is not currently used or defined in the RVCBA. We suggest following the definition found in the UMSA: "§101(22) '[Superintendent]' means the [state superintendent of banks or other senior state regulator]."

currency in the RVCBA). If there are perceived inadequacies in the current regulatory approach taken to protect money transmission customers, then they should be addressed in *both* the re-drafting of MTL law *and* a new model law for virtual currency. To only address these issues in the virtual currency context while leaving money transmitters with existing, lower-burden compliance obligations is to impose barriers to entry for new technologies and favor incumbents. To that end we advocate for a simplified minimum net worth requirement—resembling state MTL laws—that specifies a range of possible discretionary requirements that a regulator may impose, from a flat minimum to a flat maximum. For example:

> "the [superintendent] at her discretion may require the licensee to provide evidence of and maintain a net worth of at least $35,000 and not greater than $1,000,000 to ensure ongoing business operations and sufficient reserves for winding down operations."

Similarly on the question of permissible investments we advocate for parity with MTL law. In typical money transmission licensing, reserve requirements can usually be satisfied by holding cash. California, for example, lists cash as an eligible security for the purposes of capital requirements in money transmission licensing. Allowing the transmitter to hold cash avoids a situation in which the business must hold illiquid assets alongside and in duplication to any liquid (*i.e.* cash) assets held in order to quickly make good on outstanding payment orders which are, of course, also denominated in dollars. Virtual currency businesses should face similar standards. If the business holds virtual currency assets in the form and amount deposited by their customer, it should not have to also hold duplicative reserves in some other form. Therefore, rather than guaranteeing that the licensee will be permitted "to hold a [percentage to be determined] of its permissible investments in the type or types of virtual currency in which it may deal in the ordinary course of business under this act[,]" the RVCBA should *always* allow the licensee "to hold virtual currency in equivalent type and quantity to its outstanding virtual currency business obligations under this act."

Finally, while we find the policy questions inherent in Commissioner Smith's comment on UCC Article 8 to be compelling, we believe it is premature to subject virtual currency firms to a requirement to "opt in" to Article 8 given that no such mandate exists in money transmission law.

Thank you for your time and please always feel free to email me at peter@coincenter.org if you have any questions.

Sincerely,

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Director of Research