

# New Empire State of Mind? Potential Easing of Restrictions for New York Virtual Currency Business Licenses

July 22, 2020

On the fifth anniversary of the introduction of New York's virtual currency regulation, the New York State Department of Financial Services (DFS) announced a number of initiatives presumably to make it easier for virtual currency start-ups to enter the New York market and, once in the New York market, to expand virtual currency offerings in a more expedited manner.<sup>1</sup>

## KEY ANNOUNCEMENTS

On June 24, DFS announced:

- final guidance on the creation of a greenlist of all DFS pre-approved virtual currencies available for use by all New York virtual currency business licensees and the availability of a self-certification process for virtual currency business licensees to add additional virtual currencies to its offerings without prior approval from DFS;
- a proposal to create a conditional virtual currency business-licensing framework to potentially ease entrance into the New York market. Conditional licensees would be able to receive various services and support from existing virtual currency business licensees. This would allow new entrants to fill the gap between what the new entrant is able to provide/performance on its own initially and what is required until such time the entrant is able to provide all of the services by itself;
- additional procedures and resources to create a more transparent and timely process for evaluating virtual currency business license applications; and
- its entry into a memorandum of understanding (MOU) with State University of New York (SUNY) for the two organizations to explore the viability of a new SUNY-related virtual currency program where participants in the program would be able to apply for a proposed conditional virtual currency business license.

## Final Guidance Regarding the Self-Certification Process and Greenlist of Virtual Currencies

Virtual currency (VC) companies able to operate in New York State do so under the BitLicense<sup>2</sup> or through a limited purpose trust company charter<sup>3</sup> (such companies, "VC Entities"). Previously, any time a VC Entity determined to expand its offered list of virtual currencies, such entity needed to receive prior approval from DFS. To better streamline and expedite the process, DFS announced [final guidance regarding adoption or listing of virtual currencies](https://www.dfs.ny.gov/system/press_releases/pr202006241)<sup>4</sup>. VC Entities will now have the ability to self-certify the use of additional virtual currencies without prior

<sup>1</sup> N.Y. Dept. of Fin. Servs., Press Release, DFS Superintendent Laceywell Launches Series of Virtual Currency Initiatives (June 24, 2020), [https://www.dfs.ny.gov/system/press\\_releases/pr202006241](https://www.dfs.ny.gov/system/press_releases/pr202006241).

<sup>2</sup> N.Y. Comp. Codes R. and Regs., tit. 23, ch. 1, pt. 200.

<sup>3</sup> See [https://www.dfs.ny.gov/system/files/documents/2020/04/ea140311\\_proposals\\_vc\\_exchanges.pdf](https://www.dfs.ny.gov/system/files/documents/2020/04/ea140311_proposals_vc_exchanges.pdf).

<sup>4</sup> [https://www.dfs.ny.gov/apps\\_and\\_licensing/virtual\\_currency\\_businesses/gn/adoption\\_listing\\_vc](https://www.dfs.ny.gov/apps_and_licensing/virtual_currency_businesses/gn/adoption_listing_vc).

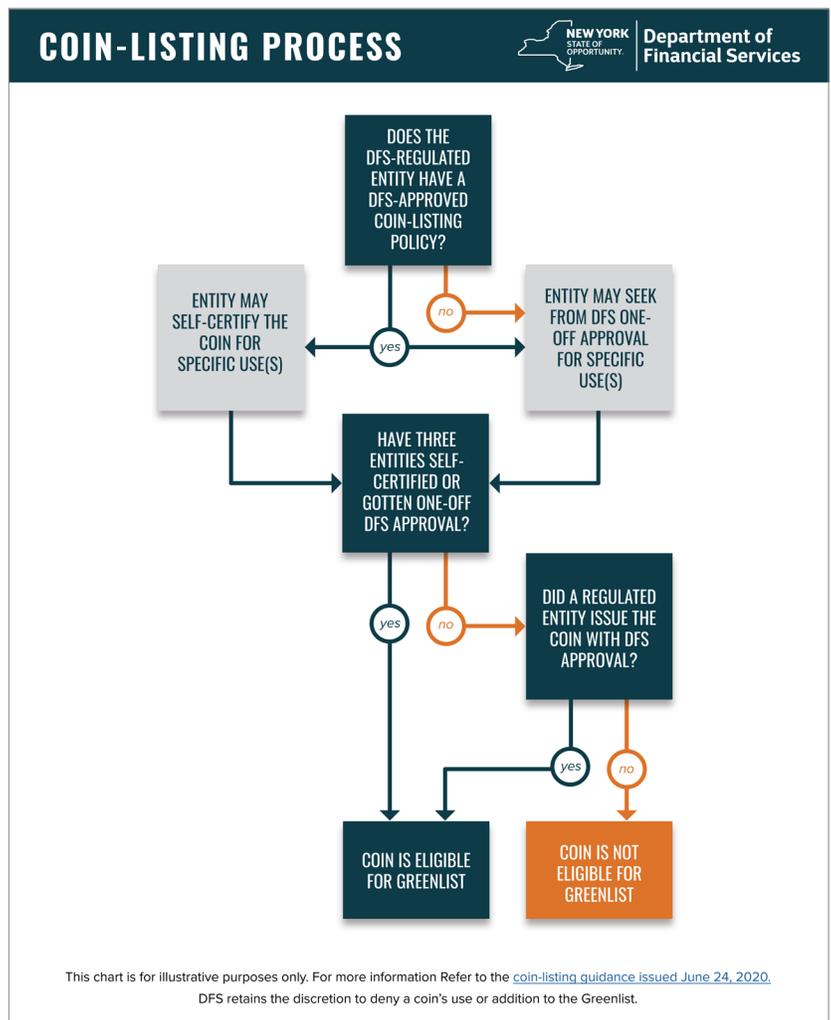
approval. To make use of the self-certification process, VC Entities will need to implement a pre-approved virtual currency listing policy. The basic requirements for the virtual currency listing policy, including elements relating to governance, risk assessment and monitoring, are outlined in the final guidance.<sup>5</sup> For example, policies should address the role of the board of directors (or equivalent body) in approving virtual currencies and reviewing and approving the virtual currency-listing policy, assessment of risks across the VC Entity (including, but not limited to, virtual currency issuance and governance, operational considerations, cybersecurity and other technological risks, market risks, risk of theft and regulatory risks), and periodic monitoring and re-evaluating of virtual currencies. Once DFS approves the VC Entity’s policy, the VC Entity may expand its virtual currency offerings in line with its policy.<sup>6</sup>

DFS also launched a [webpage](#)<sup>7</sup> containing a list of virtual currencies approved for use by all VC Entities (the “Greenlist”). If a VC Entity does not implement a self-certification process approved by DFS, it must seek DFS’s prior approval in line with the current process, unless the virtual currency is already on the Greenlist.

Other VC Entities may not piggyback off a VC Entity’s self-certification of a virtual currency. However, if three different and unrelated VC Entities self-certify the same virtual currency, six months after the date of the third self-certification, DFS may add such virtual currency to the Greenlist for use by all VC Entities. The idea here is to reward early movers and those willing to invest in the creation of a self-certification policy by getting to market with new virtual currencies faster. Use of self-certified virtual currencies or the inclusion of any virtual currencies on the Greenlist may be subject to limitation at any time by DFS. Additionally, a virtual currency may be added to the Greenlist if:

1. three separate and unrelated VC Entities get one-off approval from DFS (other than through the self-certification process) to use the virtual currency;
2. any combination of self-certifications and one-off approvals until there are three in total; or
3. if a VC Entity issues a virtual currency with DFS oversight and approval (e.g., PAX issued by Paxos Trust Company).

The following chart prepared by DFS illustrates the options outlined above.



<sup>5</sup> Creation of the policy itself should be a routine matter. Preparation of the self-certification policy should generally follow principals set forth in policies required with the initial application ([https://nationwidelicencingsystem.org/slr/PublishedStateDocuments/NY\\_Virtual\\_Currency\\_New\\_Application\\_Checklist.pdf](https://nationwidelicencingsystem.org/slr/PublishedStateDocuments/NY_Virtual_Currency_New_Application_Checklist.pdf)).

<sup>6</sup> Note that the self-certification process may not be used to self-certify privacy virtual currencies or virtual currencies used to circumvent laws and regulations (for example, gambling coins). Privacy virtual currencies allow users to conceal details of individual transactions, including wallet addresses and transaction balances, from public ledgers.

<sup>7</sup> [https://www.dfs.ny.gov/apps\\_and\\_licensing/virtual\\_currency\\_businesses/virtual\\_currencies](https://www.dfs.ny.gov/apps_and_licensing/virtual_currency_businesses/virtual_currencies).

Coin-Listing Process chart courtesy of the New York State Department of Financial Services.

Since the self-certification policy is not a requirement for an initial virtual currency business license, to avoid delaying approval of the license, it seems advisable for new applicants for a virtual currency license to seek approval for its self-certification policy immediately after approval of its license and not simultaneously with the initial application. The initial application should only cover those virtual currencies on the Greenlist to expedite approval. According to DFS staff, DFS has already approved a number of self-certification policies.

### **Request for Comments: Proposed Framework for a Conditional Virtual Currency License**

Since the inception of New York's virtual currency regulation, DFS has only granted a total 25 BitLicenses or limited purpose trust company licenses. While the virtual currency regulation allows DFS to grant conditional licensing to an applicant who has not satisfied all licensing requirements, DFS has yet to expressly grant any such conditional licenses since the inception of the regulation.<sup>8</sup> DFS is now seeking public comment on its [proposal](#)<sup>9</sup> to implement a framework for a conditional license.

Under the proposed framework, potential applicants would collaborate with existing VC Entities through a services agreement or other arrangement to receive services and support, such as capital, systems and/or personnel, to comply with licensing requirements. The premise is that a paramount hurdle for new applicants is the capital and infrastructure costs required to maintain compliance with a BitLicense. However, the conditional licensing regime will not offer relief from the current surety bond requirement, beneficial ownership review, business plan/activity review or some of the other requirements to actually receive a virtual currency business license. It is not clear how and whether this will result in registrants being able to get to market faster. The proposed framework appears to facilitate an applicant's ability to conduct business while also complying with the BitLicense requirements rather than fast tracking receipt of a virtual currency business license.

There are also questions as to how this would work from the servicing VC Entity's perspective, including:

- What types of services could a VC Entity feasibly provide to a new entrant into the New York market?
- If a new registrant's compliance with the virtual currency regime is partially dependent on services and/or support received by a VC Entity, will the registrant be under the supervision or oversight of the VC Entity?
- Would DFS hold such VC Entity responsible for the conduct of the new registrant for any compliance violations by the registrant?
- How would a VC Entity provide support for a registrant's capital requirements?

Public comments are due by August 10, 2020.

### **Notice of Virtual Currency Business Activity License Application Procedures**

DFS announced two practices with the aim of streamlining the application review process. First, DFS will not review any application until it deems the submission sufficiently complete as a means to expedite review and to disincentivize any applicant from submitting partial applications. Second, if an applicant does not fully respond to any application deficiency letters by the listed response date, DFS may, without further notice, deny the application. In summary, review will not begin until the application is deemed to be complete. This will make it imperative for applicants to respond timely to any follow-up DFS requests (or formally request and receive a delay in writing) to avoid having their BitLicense applications denied on a technicality.

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<sup>8</sup> At the time of implementation of its BitLicense regime, DFS apparently authorized certain VC entities that were already operating in New York to continue to conduct business in the New York market during the pendency of their BitLicense application process under a safe-harbor regime that appears to have been different than a grant of a conditional license. Bittrex Inc's authority to operate in New York as a VC Entity under such authority was abruptly terminated by DFS in April 2019: <https://www.dfs.ny.gov/system/files/documents/2019/04/dfs-bittrex-letter-41019.pdf>.

<sup>9</sup> [https://www.dfs.ny.gov/apps\\_and\\_licensing/virtual\\_currency\\_businesses/gn/req\\_comments\\_prop\\_framework](https://www.dfs.ny.gov/apps_and_licensing/virtual_currency_businesses/gn/req_comments_prop_framework).

## Updated BitLicense FAQs

DFS updated and revised its [BitLicense FAQ page](#)<sup>10</sup> in an attempt to offer more clarity and transparency into the BitLicense process. Most helpful are the FAQs providing DFS's position that certain activities such as mining and selling minted virtual currencies, writing code for the virtual currency space and providing virtual currency investment advice would generally not require a BitLicense.

## DFS/SUNY MOU

DFS entered into an MOU with SUNY for the two organizations to explore the viability of a new SUNY-related virtual currency program where participants in the program would be able to apply for the proposed conditional virtual currency business license. Under the MOU, SUNY would consider establishing a SUNY-related entity authorized by DFS to conduct virtual currency business activity, under either a BitLicense or a limited purpose trust company, with the goal of providing services or infrastructure support to potential licensees wishing to apply for a conditional virtual currency business license. As with the proposal for conditional licensing framework, there are many questions on how higher education organizations would be able to facilitate entry by new registrants into the New York market and what would be their potential responsibilities for supervision oversight and potential regulatory or legal liability if things went wrong.

## Outlook for Conducting Virtual Currency Business in New York

In announcing the above initiatives, New York Superintendent of Financial Services Linda A. Lacewell emphasized DFS's desire to "boost responsible innovation" and "foster accessibility." These actions appear to be a significant step in that direction, though their ultimate impact remains to be seen.

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<sup>10</sup> [https://www.dfs.ny.gov/apps\\_and\\_licensing/virtual\\_currency\\_businesses/bitlicense\\_faqs](https://www.dfs.ny.gov/apps_and_licensing/virtual_currency_businesses/bitlicense_faqs).

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