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The New York regulatory response to virtual currency risks

Nowojorska odpowiedź regulacyjna na ryzyka związane z wirtualnymi walutami

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Abstract: This paper indicates the main risks connected with virtual currencies and shows what the New York regulatory response to them was. Because some time has passed since the adoption of the appropriate laws, the effect of the regulation can also be assessed. Based on described research, the thesis is put forward that even an onerous regulation of virtual currency in certain jurisdictions should not lead to suppressing this financial innovation. Therefore, states should regulate crypto-assets to attract the branch which currently has a huge potential to growth.

Keywords: virtual currency, crypto-currency, crypto-assets

Abstrakt: W ramach niniejszego artykułu zostały wskazane główne ryzyka związane z walutami wirtualnymi oraz przedstawiono jaka była nowojorska regulacyjna odpowiedź na nie. Ponieważ od przyjęcia odpowiednich regulacji minęło już trochę czasu, ich skutki mogą być również ocenione. Na podstawie opisanych badań postawiona jest teza, że nawet uciążliwa regulacja waluty wirtualnej w pewnych porządkach prawnych nie powinna doprowadzić do zabicia tej innowacji finansowej. Dlatego porządki prawne powinny regulować kryptoaktywa, aby przyciągnąć branżę, która obecnie ma ogromny potencjał wzrostu.

Słowa kluczowe: waluty wirtualne, kryptowaluty, kryptoaktywa

1. Introduction

Virtual currencies, crypto-currencies and crypto-assets (terminological issues will be elaborated below) constitute currently one of the liveliest discussed topics both in practice and in the doctrine. In the European Banking Authority report, we can read: “The use of crypto-assets, which depend on cryptography and DLT, has **evolved rapidly** in recent years and is **anticipated to continue** to do so as the technologies continue to be piloted within and beyond the financial sector” (European Banking Authority 2019: 6; see also: Chohan 2018: 1) [*emphasis added* – T.T.]. With reference to them, we are able to find conflicting opinions: on the one hand, they can be presented as a salvation for indigenous people (Alcantara and Dick 2017); on the other one – they have a potential to trigger a next financial crisis (Tomczak 2019: 492-512).

Regardless of the opinions about them, we cannot fail to notice that presently there can be observed a worldwide trend towards regulating them (Polish Financial Supervisory Authority 2020: 4). As it was accurately put by J. Czarnecki, currently we are dealing with: “a regulatory arms race” (Pol. *Regulacyjny wyścig zbrojeń*).¹ Since crypto-assets, including crypto-currencies, are usually based on a quite new distributed ledger technology, their proper regulation is currently one of the greatest legal challenges (European Securities and Markets Authorities 2019: 4).

However, one of the jurisdictions which launched such a regulatory trend is the state of New York. The New York State Department of Financial Services issued the laws which are commonly referred to as **Bitlicense** (N.Y. COMP. CODES R.®S. tit. 23, § 200, 2015). What is more, this regulation entered into force some time ago, i.e., on 8 August 2015. Therefore, it seems justified to take a closer look at Bitlicense to verify what this quite early response to the main virtual currency risks is.

Even if there are already some papers dealing with Bitlicense, such research may still and especially prove useful if the Regulation of the European Parliament and of the Council on Markets in Crypto-assets and amending Directive (EU) 2019/1937 (hereinafter: **MiCA Regulation**) is not adopted and/or does not come into force soon. Currently, we are not even dealing with its final version (only a proposal) and we do not know what its final *vacatio legis*² will be. Therefore, Bitlicense still constitutes a comparative perspective how

¹ Such a statement was made by J. Czarnecki during the discussion which took place on 12 April 2021 (*Rynek kapitałowy wobec tokenizacji papierów wartościowych i decentralizacji obrotu*) and can be found here: <https://www.youtube.com/watch?v=LquD1KMhEjU> (accessed: 22.05.2021).

² The latest version can be found at: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52020PC0593>.

to quite comprehensively regulate virtual currencies, or even more broadly – the crypto-assets. It seems that such laws are likely to be quickly adopted, in particular, if there is a considerable financial fraud or crisis caused by virtual currencies, since such frauds and crises naturally trigger new and complex regulations regarding financial markets. In the paper, mainly the legal dogma method was used.

2. Definition of Virtual Currency in Bitlicense

Before discussing the main issue, i.e., the regulatory response to virtual currency risks, some remarks with reference to defining virtual currencies shall be made.

Virtual currency was defined in Article 200.2 letter (p) of Bitlicense as a **type of digital unit** that is used as a medium of exchange or a form of digitally stored value. Further in the definition we can read that virtual currency shall be **broadly construed** to include digital units of exchange that:

- (i) have a centralized repository or administrator;
- (ii) are decentralized and have no centralized repository or administrator; or
- (iii) may be created or obtained by computing or manufacturing effort.

The virtual currency was also defined in the UE directive 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, amending Regulation (EU) No 648/2012 of the European Parliament and of the Council, and repealing Directive 2005/60/EC of the European Parliament and of the Council and Commission Directive 2006/70/EC (hereinafter: **AML Directive**). According to Article 3 item 18 of the AML Directive, virtual currencies means a digital representation of value that is not issued or guaranteed by a central bank or a public authority, is not necessarily attached to a legally established currency and does not possess a legal status of currency or money but is accepted by natural or legal persons as a means of exchange and which can be transferred, stored, and traded electronically. In Polish legal doctrine, these two definitions have already been juxtaposed (Srokosz 2017: point 6 and point 7). It must only be highlighted that Bitlicense definition is so broad that it resembles a definition of crypto-assets more than a traditional definition of virtual currency/crypto-currency, which very often refers to the payment function of a virtual asset (European Banking Authority: 6). Especially if we compare such a definition with the definition of crypto-assets included in the MiCA Regulation or in the position of the Polish Financial Supervision Authority (Polish Financial Supervisory Authority 2020: 7). Noteworthy, in the former one, crypto-assets were defined

as a **digital representation of value** or rights which may be transferred and stored electronically, using distributed ledger technology or similar technology (Article. 3 sec. 1 item 2 of the MiCA Regulation).

Therefore, thanks to such a broad definition of virtual currency in Bitlicense, we may say that to a large extent Bitlicense regulates crypto-assets (Baker 2017). To a large extent since from the definition of virtual currency the following were excluded: in-game currency or reward points, customer affinity rewards programs and prepaid cards.³ Since in MiCA Regulation the ‘utility tokens’ have been defined as a type of crypto-asset which is intended to provide digital access to a good or service, available on DLT, and is only accepted by the issuer of that token (Article 3 sec. 1 item 5 of the MiCA Regulation), we may say that the so-called utility tokens are mainly out of the Bitlicense definition of virtual currency.

Therefore, to sum up, the Bitlicense concept of virtual currency may be understood more broadly than just as a means of payment. In other words, we do not have to be within the payment-type purposes of certain virtual asset, to be within Bitlicense definition. Noteworthy, a separate paper may be devoted to the issue of a precise delimitation of such notions as crypto-assets, virtual currency, crypto-currency and virtual money (Srokosz 2017: 28; Tomczak 2019: 497-498; Stolarski 2018: 28-29). However, this is not the main aim of this article.

3. Scope of the Bitlicense application

Bitlicense starts with the article determining its scope of application. In its essence, Article 200.1. states that Bitlicense regulates the conduct of business involving virtual currency. In Article 200.2 letter (q) of Bitlicense, we can find the following definition of virtual currency business activity:

Virtual Currency Business Activity means the conduct of any one of the following types of activities involving New York or a New York Resident:

(1) receiving Virtual Currency for Transmission or Transmitting Virtual Currency, except where the transaction is undertaken for non-financial pur-

³ More precisely, in the definition of the virtual currency we can read: “Virtual Currency shall not be construed to include any of the following: (1) digital units that (i) are used solely within online gaming platforms, (ii) have no market or application outside of those gaming platforms, (iii) cannot be converted into, or redeemed for, Fiat Currency or Virtual Currency, and (iv) may or may not be redeemable for real-world goods, services, discounts, or purchases. (2) digital units that can be redeemed for goods, services, discounts, or purchases as part of a customer affinity or rewards program with the issuer and/or other designated merchants or can be redeemed for digital units in another customer affinity or rewards program, but cannot be converted into, or redeemed for, Fiat Currency or Virtual Currency; or (3) digital units used as part of Prepaid Cards.”

poses and does not involve the transfer of more than a nominal amount of Virtual Currency;

(2) storing, holding, or maintaining custody or control of Virtual Currency on behalf of others;

(3) buying and selling Virtual Currency as a customer business;

(4) performing Exchange Services as a customer business; or

(5) controlling, administering, or issuing a Virtual Currency.

The development and distribution of software in and of itself does not constitute Virtual Currency Business Activity.

The following conclusions can be made based on the above definition. The scope of the application of Bitlicense is broad. The concept seems to cover almost all the activities on the basis of which it is possible to earn some money on virtual currency. It resembles a lot the definition of 'crypto-asset service' that is included in MiCA Regulation (Article 3 sec. 1 item 9 of the MiCA Regulation). On the other hand, it is noteworthy, Bitlicense does not cover all the activities connected with virtual currency. It indirectly excludes from its scope merchants and consumers that utilize virtual currency solely for the purchase or sale of goods or services or for investment purposes (Article 203 letter (b) item 2 of Bitlicense). In other words, it focuses only on **intermediaries** and eventually **issuers** of virtual currency (hereinafter both as: **intermediaries**).

4. Virtual currency risks

With reference to virtual currencies, we may speak at least about the following risks:

- risk of virtual currency market disappearance;
- risk of virtual currency exchange, account or wallet disappearance;
- risk of cyber-attacks;
- risk of money laundering;
- risk of losing access;
- risk of high transaction costs;
- risk of a transaction irreversibility;
- risk of a transaction not being 'immediate';
- risk of non-acceptance of virtual currency as a means of payment;
- regulatory risk (Article 200.19 letter (a) of Bitlicense; Tomczak 2020; 92-105).

In the next part of the paper, the Bitlicense response to such risks will be elaborated. However, we must bear in mind that not all virtual currencies will rise the same risks and issues therefore, case by case analysis is also required (European Securities and Markets Authorities: 13).

4.1. The risk of virtual currency market disappearance

For investors, the most severe risk related to virtual currencies is the risk of certain virtual currency market disappearance. As Bitlicense properly indicates the value of virtual currency may be derived from the continued willingness of market participants to exchange fiat currency for virtual currency, which may result in the potential for permanent and total loss of value of a particular virtual currency should the market for that virtual currency disappear (Article 200.19 letter (a) item 5 of Bitlicense; Polish Financial Supervision Authority 2020: 2; Polish Financial Supervision Authority 2021: 6; Cheah and Fry 2015: 32-36). In other words, if nobody is interested in certain virtual currency, its value may drop to 0. That may, of course, lead to huge investors' losses, especially if they invested in certain virtual currency when it was popular (Tomczak 2020: 92-93).

The above is, however, too general. We may speak about 'native' virtual currencies and 'non-native' ones (Polish Financial Supervisory Authority 2020: 13). The former possess an intrinsic value and are not guaranteed by any entity (Polish Financial Supervisory Authority 2020: 13). The latter are guaranteed by an identified entity on the terms specified by that entity (Polish Financial Supervisory Authority 2020: 13). Therefore, the other ones are as strong as the guarantee and the entity providing such guarantee. What is more, if we are dealing with a virtual currency which is issued by a certain entity/entities, we are talking about virtual currency business activity; therefore, such an entity shall obtain a license (Article 200.2 letter (q) item (5) of Bitlicense). Thus, the risk of collapsing of such an entity would be mitigated.⁴

Therefore, the described risk materializes especially with reference to the native virtual currencies. Bitlicense does not provide the above-mentioned distinction and does not refer, e.g., to stablecoins, but we have to bear in mind that it was a very early regulation of virtual currency.

It should be considered how Bitlicense tries to respond to the described risk. An attempt to completely eliminate it with reference to native virtual currencies would equal a ban on them. Still, it is worth noting that there are jurisdictions that take such an approach (Xie 2019; Srokosz 2021: 165).

However, this risk is inherently combined with the notion of decentralized virtual currencies which are not stablecoins and, probably because of that, Bitlicense does not go so far. It simply recognizes this risk as material and imposes

⁴ It must be highlighted that this paper does not refer to stablecoins which shall be distinguished from 'traditional' virtual currencies. More about stablecoins, see for example: D. Bullmann, J. Klemm, A. Pinna, In Search for Stability in Crypto-Assets: Are Stablecoins the Solution?, ECB Occasional Paper No. 230, Available at "SSRN": <https://ssrn.com/abstract=3444847> (accessed: 22.05.2021).

the obligation to inform customers about it (Article 200.19 letter (a) item (5) Bitlicense). Such information obviously does not eliminate this risk. However, it constitutes an important counter-narrative to many opinions on the Internet which present virtual currencies as an investment heaven. The question arises who should inform customers about this risk and the answer to this question will be provided in the next part of this paper.

4.2. The risk of virtual currency exchange, account, or wallet disappearance

However, from the risk that the market of certain virtual currency may disappear, we must distinguish the risk that virtual currency exchange, account or wallet can disappear (more details on the complex structure of virtual currencies markets: Hughes and Middlebrook 2015: 505-507; T. Tomczak 2020: 82-87). In other words, it is possible that the entity, place or platform where we store our virtual currencies will cease to exist.⁵ Such an event entails losses of stored currency, in turn, usually resulting in huge losses for investors. In practice, such situations have already occurred relatively often (Tomczak 2020: 97; European Securities and Markets Authorities 2019: 15; Bloomberg 2018). The above seems to be the main risk that Bitlicense is trying to deal with. As it was mentioned at the beginning, it focuses on the intermediaries. Those intermediaries will very often run virtual currency exchanges, accounts, wallets or platforms. Bitlicense tries to ensure that such an intermediary will not disappear overnight, leaving many investors with huge losses behind.

The following steps have been taken to mitigate this risk. Most significantly, entities which want to engage in any virtual currency business activity must obtain the license.⁶ Article 200.4. letter (a) of Bitlicense determines, in a complex manner, what should be included in and attached to the application for such a license. Bitlicense is publicly available therefore, there is no point in going into details. However, a few interesting requirements may be mentioned. The application, among other things, shall contain:

⁵ As ESMA properly notices, there are 'centralized' platforms which hold crypto-assets on behalf of their clients and 'decentralized' ones which do not (European Securities and Markets Authorities 2019: 12).

⁶ See: Article 200.3 of Bitlicense. In the article, there are two exemptions from licensing requirements. One exemption has already been mentioned and it refers to merchants and consumers that utilize virtual currency solely for the purchase or sale of goods or services or for investment purposes. The second exemption refers to persons that are chartered under the New York Banking Law and are approved by the superintendent to engage in virtual currency business activity. See: Article 200.3 letter (c) of Bitlicense.

– a list of, and **detailed biographical information** for, each individual applicant and each director, principal officer, principal stockholder, and principal beneficiary of the applicant, as applicable, including the individual's name, physical and mailing addresses, information and documentation regarding such individual's personal history, experience and qualifications, which shall be accompanied by a form of authority, executed by such an individual, to release information to the department (Article 200.4. letter (a) item (3) of Bitlicense);

– a **background report** prepared by an **independent investigatory agency** acceptable to the superintendent for each individual applicant, and each principal officer, principal stockholder, and principal beneficiary of the applicant, as applicable (Article 200.4. letter (a) item (4) of Bitlicense);

– for each individual applicant; for each principal officer, principal stockholder, and principal beneficiary of the applicant, as applicable; and for all individuals to be employed by the applicant who have access to any customer funds, whether denominated in fiat currency or virtual currency: (i) **a set of completed fingerprints** [...] (Article 200.4. letter (a) item (5) of Bitlicense);

– an explanation of **the methodology** used to calculate the value of virtual currency in fiat currency (Article 200.4. letter (a) item (14) of Bitlicense).

However, interestingly, Bitlicense not only provides a lot of requirements with reference to such an application, but also states that such an application should contain **any other additional information as the superintendent may require** (Article 200.4. letter (a) item (15) of Bitlicense). Therefore, the catalog of data which shall be provided **is not closed**.

What is also interesting, the license will be issued, among other requirements if the qualities of the applicant warrant the belief that the applicant's business will be conducted honestly, fairly, equitably, carefully, and efficiently within the purposes and intent of Bitlicense, and in a manner commanding the confidence and trust of the community (Article 200.6 letter (a) of Bitlicense). Therefore, we can see that quite subjective factors are also included in the process of assessment of applications.

The discussed risk shall also be reduced by the **capital requirements** imposed by Bitlicense. This requirement is interesting since Bitlicense does not set a fix amount of the capital. According to Article 200.8. letter (a) of Bitlicense, each licensee shall maintain at all times such capital in the amount and form **as the superintendent determines is sufficient** to ensure the financial integrity of the licensee and its ongoing operations based on an assessment of the specific risks applicable to each licensee. Further in the article we can read what factors **may** be considered in determining sufficient amount and form. It should be noted that such a solution is not very intermediaries-friendly as they cannot be

sure what amount of capital they should gather to be able to conduct virtual currency business activity. What is more, the capital should be in the form of cash, virtual currency, or high-quality, highly liquid, investment-grade assets in such proportions as are acceptable to the superintendent (Article 200.8. letter (b) of Bitlicense). Thus, the capital should not only be in sufficient amount, but also shall have **certain quality**.

Furthermore, a licensee shall keep and preserve appropriate books and records (Article 200.12 of Bitlicense) and submit to the superintendent certain financial statements, disclosures, and reports (Article 200.14 of Bitlicense). Such requirements, at least indirectly, shall also reduce the risk of an overnight disappearance of the licensee.

The above, briefly described requirements only reduce the discussed risk. They do not eliminate it completely. However, Bitlicense goes even further. It provides the requirement that each licensee shall maintain a surety bond or trust account (more about the common law trust: Hayton, Matthews, Mitchell, and Underhill 2016; Tomczak 2021: 239-262) in the US dollars for the benefit of its customers in such a form and amount as is acceptable to the superintendent for the protection of the licensee's customers. Therefore, even if the licensee collapses, investors, at least to some extent, shall be able to recover their losses. However, once again, we see a not very intermediary-friendly approach. The amount of the 'guarantee' was not fixed in Bitlicense. It is determined on a case-by-case basis by the superintendent. We may assume that the amount of such 'guarantee' will not be equal to the investors' assets that are in the licensee's custody. A reason for such a conclusion stems from the fact that Article 200.19 letter (a) item (10) of Bitlicense imposes an obligation to inform customers that any bond or trust account maintained by the licensee for the benefit of its customers may **not be sufficient** to cover **all** losses incurred by customers.

To sum up, Bitlicense imposes far reaching requirements to protect the investors from overnight disappearance of the intermediary. There are licensing, capital, bookkeeping and reporting requirements. What is more, even if the licensee collapses, thanks to a surety bond or a trust, the investors shall recover at least part of their losses.

4.3. The risk of cyber attacks

The very nature of virtual currency leads to the risk of cyber attacks. The constantly growing value of virtual currencies attracts more and more cyber criminals. The mentioned risk is widely recognized (European Securities and Markets Authorities 2019: 4) and Bitlicense is also not blind to it. We can find

a very elaborate section which refers only to this one risk. According to Article 200.16 of Bitlicense, each licensee shall:

- establish and maintain an effective cyber security program which shall perform certain cyber security functions (Article 200.16 letter (a) of Bitlicense) and which shall include certain audit functions like penetration testing and an audit trail (Article 200.16 letter (e) of Bitlicense);
- implement a written cyber security policy (Article 200.16 letter (b) of Bitlicense);
- designate a qualified employee to serve as the licensee’s Chief Information Security Officer (Article 200.16 letter (c) of Bitlicense) and employ adequate cyber security personnel (Article 200.16 letter (g) of Bitlicense);
- submit to the New York State Department of Financial Services, at least annually, a cyber security report (Article 200.16 letter (d) of Bitlicense).

Summarizing, we may say that Bitlicense very seriously tackles the discussed risk. It tries to ensure that licensees will be well prepared for cyber attacks and that they will be able to deal with them successfully. It seems that indirectly, by such requirements, Bitlicense tries to attract investors to store their virtual currencies at entities which are licensed. However, also in this case a complete elimination of this risk seems to be impossible, therefore Bitlicense imposes the obligation on licensees to inform customers about the risk of fraud or cyber attack (Article 200.16 letter (d) item (8) of Bitlicense).

4.4. The risk of losing access

Connected with the nature of virtual currencies is also the so-called risk of losing access. As Bitlicense properly indicates the nature of virtual currency it means that any technological difficulties experienced by the licensee may prevent the access or use of the customer’s virtual currency (Article 200.16 letter (d) item (9) of Bitlicense). This risk seems to be less serious than the one previously elaborated. However, we should bear in mind that virtual currencies are characterized by high price volatility (European Securities and Markets Authorities 2019: 6). Even a relatively short lack of access to virtual currencies may cause huge investors’ losses. Therefore, this risk is widely recognized (for example: Polish Financial Supervisory Authority 2020: 2).

Bitlicense responds to the described risk in three ways. Firstly, it imposes the obligation on each licensee to establish and maintain a written business continuity and disaster recovery plan reasonably designed to ensure the availability and functionality of the licensee’s services in the event of an emergency or other disruption to the licensee’s normal business activities (more about the plan: Article 200.17 of Bitlicense). Secondly, each licensee shall promptly

notify the superintendent of any emergency or other disruption to its operation that may affect its ability to fulfill regulatory obligations or that may have a significant adverse effect on the licensee, its counterparties, or the market. It may be assumed that if certain licensee notifies such emergencies or disruptions too often, probably the superintendent will take a closer look at it. That may result in suspension or revocation of the license (Article 200.6 letter (c) of Bitlicense). Lastly, Bitlicense requires that the licensee will inform customers about this risk (Article 200.6 letter (c) of Bitlicense). To sum up, this risk also appears to be handled with due care.

4.5. The risk of money laundering

The possibility of money laundering is a risk which is very often associated with virtual currencies (Houben and Snyers 2018: 58-70; Dyntu nad Dykyi 2018). Currently the majority of virtual currencies are based on the distributed ledger technology (more about DLT: European Securities and Markets Authorities 2017). Such technology enables the functioning of a given virtual currency only on the Internet and in the decentralized, global and physically not related to any country manner (Szostek 2019: 115). Because of these qualities, virtual currencies may try to be out of any state supervision. Such features increase the risk of money laundering and attract money launderers. This problem is widely recognized and was also the reason for the amendment of the AML Directive.⁷

As it may be expected, also Bitlicense responds to the described risk. Again, we are dealing with well-elaborated provision (Article 200.15 of Bitlicense). Each licensee shall establish, maintain, and enforce a complex anti-money laundering program. As a part of it, among other things, each licensee shall:

- create a written anti-money laundering policy reviewed and approved by the licensee's board of directors or equivalent governing body (Article 200.15 letter (d) of Bitlicense);
- maintain records of virtual currency transactions and notify certain transactions to the New York State Department of Financial Services (Article 200.15 letter (e) of Bitlicense);
- maintain a customer identification program (Article 200.15 letter (h) of Bitlicense).

⁷ Directive (EU) 2018/843 of the European Parliament and of the Council of 30 May 2018, amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, and amending Directives 2009/138/EC and 2013/36/EU, OJ L 156, 19/6/2018.

Therefore, we can see that Bitlicense, as a part of the anti-money laundering program, tries to tackle the problem of the lack of transparency on virtual currencies markets (more about this problem, for example: Dyntu and Dykyi 2018). However, we have to bear in mind that it does not deal with it completely. As it was mentioned at the beginning (Section II), Bitlicense does not refer to merchants and consumers that utilize virtual currency solely for the purchase or sale of goods or services or for investment purposes. Therefore, if they buy or sell virtual currency without any intermediaries, they are outside this Bitlicense anti-money laundering scheme.

A broader consideration of this risk exceeds the scope of this paper. It may only be indicated that a detailed comparison of Article 200.15 of Bitlicense with the AML Directive may constitute a remarkably interesting subject of future studies.

4.6. Residual risks

Some other risks which may be associated with virtual currencies are as follows:

- 1) risk of high transaction costs;
- 2) risk of a transaction irreversibility;
- 3) risk of a transaction not being ‘immediate’;
- 4) risk of non-acceptance of virtual currency as a means of payment;
- 5) regulatory risk.

All these risks shall be briefly discussed. Often, based on the lack intermediaries and the lack of a complex regulatory compliance scheme, virtual currencies are presented as free of transaction costs (Tomczak 2020: 95; Szostek 2019: 116). If there are intermediaries and an onerous regulatory scheme imposed on them, such costs will usually arise (European Securities and Markets Authorities 2019: 12). What is more, with reference to this aspect, certain virtual currency may be a victim of its own popularity (Tomczak 2020: 95).

Secondly, transactions in virtual currency may be irreversible (European Securities Markets Authorities 2019: 11 and Alcantara Dick 2017: 31-32). Therefore, losses due to, e.g., an accidental transaction, may not be recoverable (Tomczak 2020: 98).

Thirdly, usually virtual currency transactions are deemed to be made when recorded on a public ledger (Article 200.19 letter (a) item (4) of Bitlicense). This is not necessarily the time that initiates a transaction. Several years of bitcoin’s existence have shown that the DLT is not as perfect as it is often presented and is constantly being improved. Lags and delays may occur (European Securities

and Markets Authorities: 10) and this may be problematic if we consider the high volatility of the value of virtual currencies (Tomczak 2020: 96).

Furthermore, there is no assurance that a person who yesterday accepted a virtual currency as payment will continue to do it today. A perfect example of this problem is Tesla Inc. For quite a long time the company was accepting Bitcoins as payment for their cars. However, on 13 May 2021 its CEO Elon Musk wrote on twitter that due to the climate concerns Tesla will no longer accept Bitoins (Cellan-Jones 2021).

Lastly, there is a possibility that legislative and regulatory changes or actions at the national or international level may adversely affect the use, transfer, exchange, and value of virtual currency (sec. 200.19 letter (a) item (2) of Bitlicense). Such changes or actions are especially probable if virtual currencies cause a bigger or smaller financial crisis (Tomczak 2019: 508-509. Worldwide and very strict regulation of virtual currency may kill this financial innovation (Srokosz 2020: 644-645).

The above-mentioned risks seem to be connected with nature and/or novelty of virtual currencies and DLT. An attempt to reduce them (for example, by establishing a maximum transaction fee) would probably cause more harm than good to virtual currencies markets. Therefore, Bitlicense does not provide a strong regulatory response. There is only an obligation imposed on each licensee to disclose them to customers in clear, conspicuous, and legible writing (Article 200.19 letter (a) of Bitlicense).

5. Effects of entry into force

It is an important fact from the research perspective that Bitlicense entered into force on 8 August 2015. The fact that some time has passed allows us to assess the effects of it on the New York market of virtual currency. When it came into effect, the phenomena called “Great Bitcoin Exodus” occurred (Chohan 2018: 3). Intermediaries, at least officially, left New York State. However, for the first bitlicense we did not wait long since it was granted in September 2015 (Chohan 2018: 3). Since July 2020, 25 bitlicenced entities have been in operation in New York.⁸

The following conclusions can be made based on the above. On the one hand, even such a rigorous regulation as Bitlicense did not totally kill the virtual currency business activity as some licenses have been granted. On the other hand, we cannot ignore the fact of how big the market of virtual currency currently is and that **only** 25 licenses have been granted. Bitlicense may be seen

⁸ <https://www.nasdaq.com/articles/bitlicense-recipients-2020-06-24> (accessed 20.05.2021).

as an onerous regulatory barrier which prevents many start-ups from entering this market (Chohan 2018: 3; Handagame and Kalra 2020).

6. Conclusions

This paper started with considerations regarding the definition of virtual currencies and some remarks regarding the scope of application of Bitlicense. Such introductory remarks provided appropriate context for the core of this article, i.e., a verification what Bitlicense response is to the main virtual currency risks.

Some may say that this article presented a simplified picture of Bitlicense and others may argue that some additional risks should be discussed. However, the most importantly, this paper at least to some extent proves that even an onerous regulation of virtual currencies should not eliminate them from the market. It seems that virtual currency industry has already matured enough to be regulated. Investors are able to pay a higher price (commission fees) if an additional level of security goes along. Also at least some intermediaries are able to comply with even high regulatory standards.

Therefore, the conclusion shall be made that virtual currencies, or even more broadly crypto-assets, ought to be regulated. Otherwise, we often have a very strange situation. On the one hand, supervisory authorities provide opinions that certain virtual currency/crypto-assets schemes fall under existing regulations regarding, e.g., securities (Polish Financial Supervisory Authority 2020: 19-32). On the other one, the supervisory authorities highlight, at least indirectly, that they do not have competences to supervise the crypto-assets markets (Polish Financial Supervisory Authority 2021: 2). In other words, without crypto-assets regulation, the virtual currency market is very often deprived of legal certainty (for example: European Securities and Markets Authorities 2019: 18). Intermediaries are not eager to engage in crypto-currency market in such countries, since they are not sure how they will be treated. Investors are also deprived of detailed and systemic solutions which could make it easier for them to pursue claims against unreliable intermediaries (Polish Supervisory Authority Warning 2021: 3).

Some may ask what the point is of taking regulatory efforts, e.g., in Poland, if there is a perspective of EU MiCA Regulation which will regulate, at least to some extent, crypto-assets. However, we must bear in mind that currently we do not even have the final version of the act. What is more, when the final version is adopted, probably we will find in MiCA Regulation at least a one-year *vacatio legis* period. In other words, we will wait some time before this EU act comes into force. This time should be used by those countries which still

do not have such a regulation, to adopt one and thanks to that, to attract the crypto-currency industry to their jurisdictions. Especially since this industry seems to have enormous potential and it would be a waste not to at least try to take advantage of it.

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