

SB3082

Measure Title:	RELATING TO VIRTUAL CURRENCY.
Report Title:	Money Transmitters Act; Virtual Currency
Description:	Extends the money transmitters act to expressly apply to persons engaged in the transmission of virtual currency. Requires licensees dealing with virtual currency to provide a warning to consumers prior to entering into an agreement with them.
Companion:	
Package:	None
Current Referral:	CPH
Introducer(s):	WAKAI, ESPERO, GREEN, RUDERMAN, Baker, S. Chang, Dela Cruz, Gabbard, Galuteria, Harimoto, Ihara, Inouye, K. Kahele, Keith-Agaran, Kidani, Kim, Nishihara, Shimabukuro, Taniguchi, Tokuda



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TO THE SENATE COMMITTEE ON
COMMERCE, CONSUMER PROTECTION, AND HEALTH

TWENTY-NINTH LEGISLATURE
Regular Session of 2018

Friday, February 2, 2018
9:00 a.m.

TESTIMONY ON SENATE BILL NO. 3082, RELATING TO VIRTUAL CURRENCY.

TO THE HONORABLE ROSALYN H. BAKER, CHAIR, AND MEMBERS OF THE
COMMITTEE:

The Department of Commerce and Consumer Affairs (“Department”) appreciates the opportunity to testify on S.B. 3082, Relating to Virtual Currency. My name is Iris Ikeda, and I am the Commissioner of Financial Institutions for the Department’s Division of Financial Institutions (“DFI”). The Department supports this bill, which is a companion to H.B. 2257.

S.B. 3082 extends the Money Transmitters Act, Hawaii Revised Statutes (“HRS”) chapter 489D, to expressly apply to persons engaged in the transmission of virtual currency. This bill makes clear which virtual currency businesses are subject to regulation under HRS chapter 489D. It specifically authorizes DFI to accept like-kind virtual currency as permissible investments. This addresses the concern of some virtual currency money transmitters that they cannot afford to hold cash and cash-like permissible investments to cover their virtual currency transactions, as HRS chapter 489D currently requires. The bill warns consumers before they transact, that virtual currency is volatile by nature, and that they may lose all their virtual currency which is

not backed or insured by the government. The bill provides a framework for DFI to regulate this still emerging industry under the Money Transmitters Act, including requirements for licensure, license renewal, examination, record keeping, reporting, prohibited practices, sanctions and penalties.

The Department believes that this bill will allow the virtual currency companies to become licensed and operate in Hawaii and provide protections to consumers. Thank you for the opportunity to testify in support of this bill.

**TESTIMONY OF THE
COMMISSION TO PROMOTE UNIFORM LEGISLATION**

**ON S.B. NO. 3082
RELATING TO VIRTUAL CURRENCY.**

**BEFORE THE SENATE COMMITTEE on COMMERCE, CONSUMER
PROTECTION, AND HEALTH**

DATE: Friday, February 2, 2018, at 9:00 a.m.
Conference Room 229, State Capitol

PERSON(S) TESTIFYING: KEN TAKAYAMA or PETER HAMASAKI
Commission to Promote Uniform Legislation

Chair Baker and the members of the Senate Committee on Commerce,
Consumer Protection, and Health:

My name is Ken Takayama, and I am a member of the state Commission to Promote Uniform Legislation. Thank you for this opportunity to testify on this measure, S. B. No. 3082, Relating to Virtual Currency. The members of our state commission are Hawaii's representatives on the national Uniform Law Commission, or ULC. The ULC is a nonprofit organization that is made up of volunteer attorneys appointed by their states, and its mission is to develop and draft model legislation for states in areas in which uniformity is practical and desirable. The state Commission to Promote Uniform Legislation does **NOT** support S.B. No. 3082, and instead submits the following **comments**:

1. This measure seeks to regulate virtual currency businesses through the State's money transmitter statute.

2. We believe that S.B. No. 2129 which enacts the Uniform Regulation of Virtual Currency Businesses Act (URVCBA), provides a superior approach to the regulation of virtual currency businesses

3. S.B. No. 3082 attempts to stretch a law focused upon the transmission of money and legal tender to regulate virtual currencies which are not legal

tender and not necessarily being transmitted..

4. By comparison, the URVCBA creates a clear, comprehensive framework for regulating companies engaged in virtual-currency business activity. “Virtual-currency business activity” means exchanging, transferring, or storing virtual currency; holding electronic precious metals or certificates of electronic precious metals; or exchanging digital representations of value within online games for virtual currency or legal tender.

5. Regulation of virtual currency businesses through the money transmitter law as proposed in S.B. No. 3082 increases the risk of over inclusive regulation, potentially covering individuals merely using virtual currency to make purchases on their own behalf, or academics researching, for example, virtual currency and encryption technology and security. The URVCBA provides for exemptions for among other things, personal, family and academic uses, certain online games and certain merchant rewards programs. The URVCBA prevents these uses of virtual currency, which pose no risk of potential loss or harm to consumers, from being swept into the regulatory scheme.

6. The uniform act creates a three-tiered regulatory structure. Persons in Tier 3, whose virtual currency business activity exceeds \$35,000 in a one year period cannot operate in the State unless they obtain a license from the Division of Financial Institutions (DFI) of the Department of Commerce and Consumer Affairs. Tier 2 consists of providers with virtual-currency business activity levels between \$5,000 and \$35,000 annually, who are required to register with the DFI—which is a lighter regulatory burden than licensure. By comparison, Tier one exempts from regulation altogether those persons having virtual-currency business activity levels of under \$5,000 a year. Taken together, the three tiered regulatory structure that correlates higher levels of virtual currency business activity with stricter levels of regulation functions as a “regulatory on-ramp,” that allows companies in their early stages of business development to focus on innovation and experimentation while they are in the earliest stages of development--where they would normally face the greatest threat from the imposition of regulatory burdens.

7. The uniform act is also designed to protect consumers and their virtual currency. For example, section -51 of the URVCBA requires licensees and provisional registrants to issue disclosures to potential customers to inform them about fees, any insurance coverage for the product or service, etc. In addition, all virtual-currency businesses regulated by the Act must establish specific policies and compliance programs to guard against fraud, cyberthreats, money-laundering, and terrorist activity.

8. The URVCBA also creates an optional reciprocal licensing process with other states. The Conference of State Banking Supervisors has committed to supporting this reciprocal license framework.

9. For the foregoing reasons, we believe that the regulation of virtual currency businesses set forth in S.B. No. 2129 is superior to that proposed in this measure. We therefore respectfully request that this committee take no further action on S.B. No. 3082 until it has had a chance to review and consider the contents of S.B. No. 2129, the Uniform Regulation of Virtual Currency Businesses Act.

We reiterate our thanks for this opportunity to comment.

Via E-Mail

February 1, 2018

Senator Rosalyn H. Baker, Chair
Senator Jill N. Tokuda, Vice Chair
Committee on Commerce, Consumer Protection, and Health
Hawaii State Capitol Room 229
415 S. Beretania Street
Honolulu, HI 96813

Re: Senate Bill 3082, Relating to Virtual Currency

Dear Chair Baker, Vice Chair Tokuda and Members of the Committee:

I write on behalf of Coinbase, Inc. (“Coinbase”), a leading retail virtual currency exchange, in regards to Hawaii Senate Bill 3082. We are headquartered in San Francisco, CA and together with our affiliates, we provide a suite of services that make it easy for customers and businesses to securely buy, sell, store, and use distributed digital currency, such as Bitcoin and Ethereum. Coinbase has been registered as a Money Services Business (“MSB”) since 2013 and is currently licensed to engage in money transmission in thirty-eight jurisdictions. We work frequently with lawmakers, regulators, state and federal law enforcement agencies, and other policymakers around the world to promote the adoption of effective virtual currency policy. We understand that Hawaii Senate Bill No. 3082 (“SB3082”) proposes to extend the money transmitters act to expressly apply to persons engaged in the transmission of virtual currency, and would like to offer a few comments for your consideration.

1. Industry and Coinbase Background

The digital currency industry is an exciting space with enormous growth potential and entrepreneurial opportunity. The open, global, and decentralized nature of digital currency networks presents limitless opportunities for technological development. More specifically, the central innovation at the core of digital currency networks, the distributed ledger, allows for inexpensive, reliable, and public recordkeeping that can be utilized in a myriad of productive and innovative ways.¹

¹ The bitcoin blockchain, the first and most popular decentralized digital ledger, is used to effect and track payments among network participants, but other applications include: (i) tools which allow users to prove the existence of documents (e.g., contracts, wills and testaments, interests in property) at specific points in time; (ii) the ability for individuals to digitally "sign" and timestamp works of digital art; (iii) cryptographically activated physical property, the ownership or transfer of which may be recorded in the distributed ledger; (iv) a decentralized data storage and communications network where participants are incentivized to contribute storage capacity, computing power, or content through peer-to-peer micro-transactions; and (v) an open and transparent voting system.

Since its inception, Coinbase has strived to be the most trusted brand in the digital currency industry and to foster responsible innovation in the space by working directly with regulators, policymakers, and law enforcement agencies. Headquartered in San Francisco, California, Coinbase is the world’s largest retail digital currency exchange. We operate a safe, reliable, and compliant platform that allows customers to purchase, sell, store, and use digital currencies, such as bitcoin and ethereum. Coinbase is a federally registered Money Services Business (“MSB”), a licensed financial institution in 38 U.S. states and territories, and is one of only four entities to have received the Bitlicense, New York’s license for digital currency businesses. Our teams have been recognized by state, federal, and international law enforcement agencies as among the industry leaders in compliance, and we have trained multiple federal and state law enforcement agencies and task forces on digital currency networks.

2. State Policy Approaches to Digital Currency

Over years of work with regulators, law enforcement, and state legislatures, we have seen two policy approaches emerge among state policymakers, either of which can allow digital currency companies to operate in an innovative and sustainable way.

The first approach, adopted by a majority of states, is simply to exclude digital currency businesses from regulation. States which take this position acknowledge that heavy regulation of this nascent industry may stifle innovation. The size and adoption of the digital currency industry is minimal compared to other financial services, and most regulators have determined that it does not militate in favor of regulation. These states continue to monitor the growth of the space, emerging uses, and potential consumer risks that may arise as the industry grows.

The second and alternative approach, adopted by a minority of states, is to regulate digital currency operators—*i.e.*, businesses which, like Coinbase, offer digital currency exchange, transmission, and/or custody services—under existing state money transmission laws. We have found this approach to be successful where both regulators and licensees are mindful of the unique challenges presented by the regulations of digital currency activity. Licensees must acknowledge and commit to the serious compliance obligations that arise under state money transmission law, while regulators must be flexible in finding ways to help licensees meet those requirements and satisfy consumer protection priorities in a practicable manner.²

² In this second category, most state banking departments have interpreted broadly written money transmission statutes to authorize regulation of digital currency businesses with no legislative action. In one case, New York, the state banking department has created a special licensing structure pursuant to authority that arises under existing financial code. In other states, such as Washington, lawmakers have taken legislative action to amend money transmission laws to explicitly authorize regulation of digital currency businesses.

Separate from both of these approaches is the proposed adoption of the ULC’s Uniform Regulation of Virtual Currency Businesses Act³ (“URVCBA”). The URVCBA is a statutory framework for the regulation of companies engaging in virtual-currency business activity. The URVCBA’s three-tiered structure clarifies whether an individual or company engaging in virtual currency business activity is (1) exempt from the act; (2) must register; or (3) must obtain a license. The URVCBA also contains numerous consumer protections. This approach has been favored by a handful of industry representatives, however, we have not yet seen the practical application of the URVCBA, and therefore it would be at the discretion of the Hawaii Division of Financial Institutions to implement accordingly.

3. Coinbase Operations in Hawaii

As you may know, Coinbase ceased operations in Hawaii in early 2017 as a result of an untenable double reserve policy implemented by the Hawaii Division of Financial Institutions. According to the Division of Financial Institutions, a company that holds virtual currency for customers in Hawaii is required to keep a cash reserve in an amount equal to the aggregate face value of all virtual currency funds held on behalf of its customer. This policy forces virtual currency custodians like Coinbase to hoard huge sums of cash, even though we secure and fully-reserve customer virtual currency. As a result, Hawaii has shut down all lawful virtual currency operators, even while unlawful, offshore service providers persist.

We understand that SB3082 proposes to resolve this issue by extending the Hawaii Money Transmitters Act (the “Act”) to expressly apply to companies engaged in the transmission of virtual currency. SB3082 will also require that licensees dealing with virtual currency provide a warning to consumers prior to entering into an agreement with them. Since this is the approach that a handful of states have already taken, this solution will ultimately allow for Coinbase and other credible virtual currency custodians and exchanges to resume safe and lawful operations in Hawaii. Thereby allowing Hawaii residents to seek virtual currency custodial and other services from compliant, licensed businesses, not offshore unregulated companies.

We recognize that several different bills have been proposed regarding the regulation of digital currency in Hawaii. Coinbase’s goal is to open the door to allow residents of Hawaii to seek virtual currency custodial and exchange services from licensed businesses, and therefore, we will support any bill that allows for this resolution.

* * *

Coinbase stands ready to work with you and fellow policymakers in Hawaii to ensure that Coinbase and other law abiding digital currency companies can re-open business in Hawaii and

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http://www.uniformlaws.org/shared/docs/regulation%20of%20virtual%20currencies/URVCBA_Final_2017oct9.pdf

provide valued services to the residents of Hawaii. We appreciate your time and consideration with respect to this matter and look forward to working with you to find a solution that is in the best interest of Hawaii's residents. Please consider us a resource for you, and do not hesitate to reach out to me if we can be of any help on this or another issue.

Sincerely,

Mike Lempres
Chief Legal and Risk Officer

SB-3082

Submitted on: 2/1/2018 9:10:14 AM

Testimony for CPH on 2/2/2018 9:00:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
William Doom		Oppose	No

Comments:

I strongly oppose this bill. It is clear that the introducers do not have a clear understanding on blockchain technology.

Rather than a kneejerk reaction to a new technology that will change the future the introducers should take the time to understand what they are opposing.

This bill is analogous to stating in 1994 the state should block all access to the internet.

History will not look kindly upon the individuals introducing this bill, you will cripple the economy and place Hawaii and its residence at a disadvantage.

Startups will continue to leave the state and you will accelerate the brain drain.

SB-3082

Submitted on: 2/1/2018 12:55:35 PM

Testimony for CPH on 2/2/2018 9:00:00 AM

Submitted By	Organization	Testifier Position	Present at Hearing
Brian Zisk		Oppose	Yes

Comments:

Dear Honorable Legislators,

As a technologist/business owner who has relocated his family to Maui, did want to point out that Hawaii already has one of the toughest legal regimes for Digital Currency Regulation, being one of only 4 states with such tough laws that CryptoCurrency Exchanges are unwilling to serve your citizens, putting your constituents at a major disadvantage in the global markets, and putting your citizens at risk by forcing them to deal with unlicensed exchanges, as no licensed ones have find it viable to operate.

The existing regulations have caused local residents to lose out on major gains, and has already cost Hawaii a lot of benefit in lost taxes.

If this bill passes expanding the onerous regulations to individuals, it will prevent high net worth individuals and companies from moving here, and will actually force some of us to leave to do what is becoming more and more commonplace around the world.

Expanding what is already a tougher regulatory atmosphere than exists in 46 other states does not benefit Hawaii or its citizens.

Please reconsider expanding the already onerous regulations.

Thank you!

-Brian Zisk

Typed on my iPhone.