



October 25, 2016

Drafting Committee for the Uniform Regulation of
Virtual Currency Business Act
Uniform Law Commission

**Re: EFF Comments on October 2016 Committee Meeting Draft of the
ULC's Regulation of Virtual Currency Business Act**

Dear Members of the Drafting Committee:

The Electronic Frontier Foundation (EFF) appreciates this opportunity to comment on the October 2016 Committee Meeting Draft of the Regulation of Virtual Currency Business Act (Act).

EFF is pleased with the Act's definition of "control." The definition's inclusion of the word "unilaterally" is essential for protecting future innovation aimed at protecting consumers. These two goals—protecting innovation *and* consumers—are both something that EFF cares deeply about, as a member-supported non-profit organization working to protect the interests of both technology creators and users in the digital age. Entities that cannot unilaterally transmit virtual currency do not present a risk to consumers or institutional solvency, and adoption of an overbroad regulation that needlessly regulates entities that lack unilateral control over virtual currency will deter future innovation in this nascent industry. EFF therefore applauds the Act's adoption of a clear definition of virtual currency business activity that relies on entities' ability to unilaterally control virtual currency, rather than a "facts and circumstances" approach that would not provide adequate notice or guidance.

EFF remains highly concerned, however, about the Act's failure to include a clear exemption and safe harbor for new and growing virtual currency businesses.

The Act currently does not include an exemption for small virtual currency businesses—*i.e.*, entities who do not have custody or control of virtual currency on behalf of others that is valued in the aggregate at less than some qualifying amount (*e.g.*, \$1,000,000). Without a simple exemption for small entities to the Act's licensure requirements that grants qualifying entities a reasonable time after growing out of the exemption to make good faith efforts to apply for a license, the Act will scare away innovators and chill future innovation in the developing digital currency industry.

Instead of a clear, simple exemption, the Act imposes a provisional license requirement on small entities and new businesses. One of goals of this provision, contained within Section 210, is to protect small virtual currency businesses and encourage innovation while still creating a regulatory regime for those entities. Unfortunately, a provisional license requirement will not achieve this goal.

There are three core problems with Section 210's provisional license requirement:

- First, it is unduly complicated. Requiring start-ups to apply for provisional licenses, instead of merely granting such entities an exemption, will place on them a host of legal requirements. While these requirements may be less onerous than the requirements of full licensure, ensuring compliance with provisional licensure requirements across multiple states will prove confusing, costly, and resource-intensive. Requiring start-ups and small businesses to apply for even "provisional licenses" will therefore chill innovation.
- Second, a small entity's failure to obtain a provisional license before beginning any activity in a state could be seen as a basis for liability under federal criminal law, specifically 18 U.S.C. § 1960. This is particularly troubling because small entities are the ones most likely to be unsophisticated and thus unaware that their actions could potentially give rise to strict criminal liability under section 1960. ULC should not adopt a bill that could lead to such dramatic unintended consequences.
- Third, Section 210 requires provisional licensees to apply for a full license when they exceed 75% of their next fiscal quarter's projections, regardless of whether or not those projections come anywhere near the qualifying threshold. Because the requirement for applying for a full license is tied to a company's internal projections rather than the qualifying threshold, different businesses will be required to apply for a full license at different times. Not only will this prove confusing for small business—making compliance with the "on ramp" requirements even more costly and resource intensive—but some businesses will be required to apply for a full license when they are far below the qualifying threshold.

To protect innovation and ensure that small businesses are not subject to liability under federal criminal law, the Act's protections for new businesses should be simplified. Namely, **the ULC should adopt a straightforward exemption that applies across the board to all virtual currency startups and new businesses.** Pennsylvania's draft virtual currency amendment, for example, provided a clear exemption for "[p]ersons or entities with third party control¹ of virtual currency on behalf of residents of the [State] that is valued in the aggregate at less than one million dollars (\$1,000,000) according to a rolling thirty-day average of outstanding balances, as converted into a dollars amount utilizing each day's prevailing exchange rate." Amendments to House Bill No. 850, p. 2:17-22 (Mar. 15, 2016).

¹ The amendment defined "third party control" as "the ability to unilaterally execute or prevent a virtual currency transaction on behalf of others, except if the ability to prevent a transaction is reasonably time limited to accomplish a service, such as escrow or transaction management." Amendments to House Bill No. 850, p. 1:5-9 (Mar. 15, 2016).

The exemption should also (a) grant qualifying entities a *reasonable time* (e.g., 30 or 90 days) after growing out of the exemption to make good faith efforts to apply for a license; and (b) explicitly provide that so long as an entity makes such timely, good-faith efforts to obtain a license, it will not (i) be held liable under the Act for operations that occurred before obtaining the license or (ii) be seen as operating without a license during that pre-license period. These provisions are necessary to ensure that such entities avoid liability under 18 U.S.C. § 1960.

EFF is open to a “safe harbor” window of anywhere between 30 and 90 days. If the Committee is concerned about virtual currency businesses bypassing the \$1,000,000 threshold before obtaining a license, EFF believes lowering the license threshold to somewhere slightly below \$1,000,000 would be preferable to adoption of a complicated “on-ramp” procedure, such as that currently provided for in Section 210.

A provisional licensing regime will not allow sufficient freedom to innovate. This proposal—*i.e.*, adoption of a clear exemption with a safe harbor for small entities—avoids that outcome. A simple exemption that applies across the board to all virtual currency startups and small businesses, which grants qualifying entities a reasonable time after growing out of the exemption to make good faith efforts to apply for a license, is the best way to protect and promote continued innovation in this space.

We thank the Committee for the opportunity to highlight our concerns and for its efforts to create an Act that protects both consumers and innovation alike. Should you have any further questions about these topics, please contact Jamie Williams at (415) 436-9333 ext. 164 or jamie@eff.org.

Sincerely,

/s/ Jamie Williams

Jamie Williams
Staff Attorney