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Opening Statement
New York State Department of Financial Services
Hearings on the Regulation of Virtual Currency
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As Prepared for Delivery

On behalf of the New York State Department of Financial Services (NYDFS), I'd like to welcome everyone to the first of two days of hearings on the regulation of virtual currencies.

As you may know, over the last six months, our agency has been conducting an extensive inquiry into virtual currencies.

We've had dozens and dozens of meetings with a wide range of industry participants. We've spoken to leading academics and law enforcement officials. And we've reviewed thousands of pages of documents, reports, and other materials.

Today's public hearing is the next step in that inquiry.

Ultimately, it's our expectation that the information we've gathered in this fact-finding effort will allow us to put forward, during the course of 2014, a proposed regulatory framework for virtual currency firms operating in New York.

I believe we would be the first state in the nation to do so. Clearly, when it comes to virtual currencies, regulators are in new and unchartered waters.

However, the legal action that we saw yesterday underscores how critically important it is that we put in place guardrails for this industry to help root out money laundering and other misconduct.

The goal of these hearings is to provide a 360-degree view of this new and constantly evolving industry – both its promise and its potential pitfalls.
We've sought to bring together a diverse group of witnesses with an array of different perspectives.

We believed that it was important to hear from law enforcement and regulators. But we also wanted to bring in investors, technologists, merchants, and a number of other individuals on the ground floor of this fledging industry to provide their views.

Of course, this hearing will neither be the first nor last word on virtual currencies.

But we hope to make a positive contribution to the public dialogue on this issue as NYDFS and other regulators try to grapple with the appropriate regulatory guidelines for this industry.

Let me step back then and say that our agency approaches the issue of virtual currencies without any prejudgments.

A lot of people initially react to a very outside-the-box idea like virtual currencies with immediate skepticism. I think we should resist being completely overtaken by that urge.

It's hard to say precisely what the future holds for virtual currency and its associated technology. Currently, there is not widespread adoption of virtual currencies among the general public. And some doubt whether there will ever be.

But the same has been said about many other technologies that have since become everyday features of our lives.

It's generally a difficult proposition for financial regulators to forecast technological trends. It's not something we do particularly well.

That said, serious people – in the technological and investment community – are taking virtual currencies seriously. They are putting significant amounts of time, attention, and capital behind them. We, as a regulator, cannot turn a blind eye to something like that. We don't really have a choice.

Moreover, the Department of Financial Services – like many other state financial regulators – has a specific legal responsibility to license and regulate money transmission. And to the extent that some virtual currency service providers are engaged in money transmission, we do have an important role in writing and enforcing the rules of the game for financial firms.

Our role is perhaps best described as that of a referee. We want to make sure everyone is playing by the rules and preventing misconduct, such as money laundering. But, at the same time, we also want to make sure that we don't clip the wings of a fledgling technology before it gets off the ground. We want to make certain that New York remains a hub for innovation and a magnet for new technology firms.

Indeed, virtual currency could ultimately have a number of benefits for our financial system. It could force the traditional payments community to "up its game" in terms of the speed, affordability, and reliability of financial transactions.

I think many consumers – myself included – are perplexed that, in a world where information travels around the globe in a matter of milliseconds, it can often take several days to transfer money to a friend's bank account.

Moreover, the open-source nature of this technology, relatively low (financial) barriers to entry, and nascent nature of this industry mean its constantly evolving.

The virtual currency industry – as currently constituted – may or may not ultimately see wide-spread adoption among the general public. It's open for debate. There are, for example, serious questions about whether – given its volatility – it can serve as a stable source of value for transactions.

But regardless of that, there might be – at the very least – a kernel of something here that has a profound impact on the future of payments technology and the financial system. That's why we want to proceed without any prejudgements.

By the same token, however, regulators have to remain vigilant about the potential dangers that the current level of anonymity provided by virtual currencies presents for money laundering, drug-trafficking, gunrunning, and other illegal activities.

No industry should be defined entirely by its bad actors. But it's very clear that there are serious and documented dangers about the use of virtual currencies to subvert critical anti-money laundering requirements.

There are, of course, vulnerabilities and dangers associated with money laundering in the traditional financial system, such as at banks. As you may know, that's an area where we've been particularly active at the Department of Financial Services.

But one issue that we have to consider with virtual currency firms – unlike banks or traditional money transmitters – is that there is not currently a robust regulatory regime to help spot red flags and root out illegal activity.

Right now, the regulation of virtual currency industry is akin to a virtual Wild West. (There is even a modern day Gold Rush among miners in the virtual currency community.) That lack of regulation, however, is simply is not tenable for the long term.

Fashioning appropriate guardrails for virtual currencies presents challenging questions for regulators. Virtual currency is not easily categorized within the divisions we traditionally think about when it comes to the financial system (such as banks, insurers, or money transmitters). It's neither fish nor fowl.

And while we want to set up clear rules of the game, we also want to preserve sufficient flexibility given the constantly evolving nature of this new technology.
That is, in part, why we're evaluating whether our agency should issue a so-called 'BitLicense' specifically tailored to virtual currencies.

When people say the word money transmission, they usually think of – if anything at all – firms that were formed more than 150 years ago when our country was still exploring the western frontier.

The question, then, is what type of licensing, examination, and collateral requirements for the virtual currency industry will provide appropriate guardrails to protect consumers and our national security – without stifling beneficial innovation.

There is, we acknowledge, distrust among some in the virtual currency community about regulation. However, we believe that – for a number of reasons – putting in place appropriate regulatory safeguards for virtual currencies will be beneficial to the long-term strength of the virtual currency industry.

First, serving as a money changer of choice for terrorists, drug smugglers, illegal weapons dealers, money launderers, and human traffickers can expose the virtual currency industry to extraordinarily serious criminal penalties. Taking steps to root out illegal activity is both a legal and business imperative for virtual currency firms.

Second, safety and soundness requirements help build greater confidence among customers that the funds that they entrust to virtual currency companies won't get caught in a virtual black hole. Indeed, some consumers have expressed concerns about how quickly their virtual currency transactions are processed. There have also been public reports of virtual currency lost – perhaps irretrievably – through hacking and other cyber security vulnerabilities. Addressing those issues through enhanced safety and soundness requirements would be important to building greater confidence in this technology among the general public and promoting wider adoption.

We look forward to a spirited discussion on all of these issues.