

New York State Department Financial Services

Hearings on Virtual Currencies

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January 28, 2014

I appreciate this opportunity to testify today before the Department and commend the Superintendent on his initiative to address appropriate regulatory guidelines for virtual currencies. Although Bitcoin has attracted extraordinary attention in the last year, virtual and digital currencies are not a new phenomenon. However, the issue of whether and how to regulate them attracted little attention – until very recently - yet it is an issue that is sorely in need of regulatory leadership, especially at the state level.

The first virtual and digital currencies debuted in the early to mid-1990s as the internet increasingly penetrated our offices and homes, and commercial usage of expanded. These new forms of currency were born in part of the need to facilitate online transactions and foster the growth of internet commerce. Some addressed specific needs – for example use in virtual games. Others serve as a medium of exchange to buy real goods and services. Technological advances offered by the internet have also offered the unprecedented opportunity to mobilize the value of gold and other commodities, and make the resulting “money” accessible to the masses by circulating it via the internet.

As different digital and virtual currencies have been launched over the years, and only a hearty few have survived for more than a few weeks or months, important lessons have been learned that can help inform the regulatory policy making process.

I will spend the rest of my time today discussing one such model that borrows heavily on these lessons and offers important contrasts to Bitcoin and other open-source, decentralized digital currencies.

Upon receipt of necessary regulatory approvals, a company called COEPTIS is preparing to launch the Global Standard System (System) that will issue a medium of exchange called the Global Standard Currency (Currency). This Currency, which will circulate electronically on a closed settlement platform, will be 100% backed by physical gold, providing for freedom from default and fully protecting the holder’s value.

In FinCEN’s terminology, this is a centralized virtual currency with an administrator that is responsible for issuing and redeeming it. Because the Global Standard System will operate only a closed settlement platform, no value can directly enter or leave the system. This means the Currency can only be obtained from someone who already has it - in either a person to person (P2P) transfer or in an “exchange transaction” not unlike a sovereign currency exchange at an airport.

Based on six year old legal precedent confirmed by FinCEN's March 2013 guidance on virtual currency, COEPTIS understands that the Global Standard System is a "money transmitter" subject to registration with FinCEN under the Bank Secrecy Act and to licensing to the extent required by the jurisdictions in which it operates.

To ensure compliance with the Bank Secrecy Act as well as to protect the System from potential criminal use and abuse that any provider of financial services faces, considerable time, effort and money have been invested to develop and implement a comprehensive AML Compliance Program.

This program includes rigorous customer identification and due diligence at the time a customer signs up for a Global Standard account as well as robust and ongoing transaction monitoring, reporting, record keeping, training and period reviews as required by the BSA. An experienced and certified AML compliance officer has been hired as well as other staff that are similarly trained and certified in AML compliance. The breadth and depth of this program exceeds that of many traditional money services businesses and compares favorably to the most dynamic programs in the banking system. The closed nature of the System enhances its ability to know who is conducting a transaction and to monitor all transactions using the Currency. The extensive CIP and CDD processes also enable the System's ability to comply with OFAC administered sanctions and review account holders' names against the SDN list both at the time the account is opened and on an on-going basis.

Pursuant to this same legal precedence and guidance, any person providing exchange between the Global Standard Currency and sovereign or other virtual currencies is engaging in the business of money transmission under federal law and many state laws. Accordingly, the System will permit as Exchangers only entities appropriately regulated as a financial institution - either bank, securities firm or money transmitter - in the jurisdiction in which it operates. The Exchangers themselves will undergo an enhanced level of Due Diligence, and they will be required to enter into a contract with the System that requires them to maintain certain standards with respect to customer identification, information sharing, transaction monitoring and unusual or suspicious activity, thus further protecting the System from potential criminal abuse.

The System will afford account holders with privacy and security but not anonymity. Account holders who have completed CIP and CDD will not have to share their personal financial information with merchants when using the Global Standard Currency to make payments, and their non-public personal information will not need to sit on multiple merchant servers. Effectively, the System will permit account holders to conduct transactions with the same level of privacy available when cash is used. However, the System's strong AML program will enable it to cooperate appropriately with the law enforcement community if required.

Payments will settle immediately using the same settlement protocol used by all major government monetary authorities ("RTGS" – Real-time Gross Settlement). This means the recipient will have spendable money immediately upon receiving notification of receipt of the Currency into the account.

The System carefully balances non-repudiation with payer protection. A chargeback due to credit-related default is impossible due to a “strict debit” rule. This means the merchant that fulfills its obligations may count on “getting paid, and staying paid”.

Should a claim be made that the transaction is erroneous or unauthorized, a sophisticated, largely automated dispute mechanism will provide for rapid response and mitigation. This mechanism is integrated into a broader consumer complaint mechanism that enables evaluation of potential motives for the complaint – such as a change in mind about the transaction or a possible attempt to obtain goods without paying.

The centralized closed settlement platform offers additional benefits. Certain account protections reduce the opportunity to compromise accounts and mitigate damage should a compromise occur. The system’s administration is also able to respond to and support lawful requests for information, including subpoenas in a timely manner.

Gold is the chosen reserve to back the Currency because of gold’s long-standing acceptance as a store of value and as an acceptable reserve for traditional financial institutions and governments. It is held as a reserve by central banks, has an institutional support infrastructure, has a very visible value based upon an active and liquid global market, and importantly has the same risk weighting as cash under federal bank capital requirements.

Low transactions costs are another feature of the System. The fee for the typical online transaction ranges from .01 % to 1.0%, with the size of the fee decreasing as the value of the transaction increases.

Concerns have been raised about the ability to effectively understand, report, and for the government to receive tax revenues when alternate currency payment systems are utilized by businesses and individuals. While the taxpayer is the ultimately responsible for accurately reporting income and paying their taxes, the System is able to generate the necessary data to simplify such reporting and provide it to the taxpayers in a variety of report forms.

In summary, the Global Standard System with the Global Standard Currency is designed to complement, not replace existing payments network. In the quest for frictionless payments, it offers a solution to substantially reduce existing friction, lowering costs to consumers and merchants alike and introducing greater security and assurance into the process of making payments. Important national priorities have not been sacrificed as substantial efforts have been made to adapt the System to meet existing regulatory standards, including the adoption of strong anti-money laundering policies, procedures and controls and various consumer protections.

Electronically circulating currencies – whether virtual, digital or digitized – offer substantial benefits to consumers as well as merchants and other stakeholders. I am encouraged by the DFS’ effort to consider ways to accommodate the inevitable innovation in this area. Adapting existing regulations in the short term is the most expedient way to support one of the most vibrant areas of technological innovation in the US economy.

As these different types of currencies and the infrastructures supporting them continue to evolve, more substantive regulatory changes may be required and alternative regulatory structures adopted. In all cases, the changes should be consistent.

I welcome your questions.