

Virtual Currencies and Blockchain Technology: The Intersection of Innovation and Regulation

Cleary Gottlieb recently hosted a timely discussion about the innovations relating to cryptocurrencies and the potential the underlying technology has to be a transformative force in global finance, as well as the emerging regulatory issues that will shape the future of this technology. Joining the discussion were some of the leading voices on these topics, including:

- **Paul Vigna** and **Michael J. Casey**, journalists and co-authors of *The Age of Cryptocurrency: How Bitcoin and Digital Money are Challenging the Global Economic Order*
- **Charles Cascarilla**, CEO and co-founder of itBit Trust Company
- **Daniel Alter**, former General Counsel of the New York Department of Financial Services (NYFDS)
- **Peter Van Valkenburgh**, Director of Research at Coin Center

The event was centered around two panel discussions. The first panel was moderated by Paul Vigna, who, in addition to co-authoring *The Age of Cryptocurrency*, is a journalist for *The Wall Street Journal*, reporting on markets and virtual currencies. Paul led a Q&A with Charles (Chad) Cascarilla from itBit, which received its trust company charter from the NYFDS in May becoming the first US-chartered virtual currency exchange, and Cleary Gottlieb partner **Michael Krimminger**, who guided itBit through the charter process. Discussion highlights include:

- Paul opened the Q&A by talking about the beginnings of bitcoin and how the focus initially tended to be on the use of bitcoin and other altcoins purely as a new form of currency.
- As a result of some of the early failures, pricing volatility, and misuse of virtual currencies for criminal purposes, some members of the public have remained skeptical about the potential of bitcoin and other virtual currencies. Of course that is to be expected – it is still very early in the development cycle.
- Chad mentioned that the functionality is still not yet in place to make bitcoin more efficient than current systems, e.g., credit cards, but it is evolving. Much like the development of the internet, it will take time to reach a mass audience. Bitcoin is currently where the internet was in the '90s.
- Chad and Mike discussed how regulation can be important to the acceptance of virtual currencies by the public and by the marketplace. Recent regulatory milestones, including itBit's charter and the BitLicense regulations subsequently released by the NYFDS, have helped bitcoin gain legitimacy. Still, given the infancy of virtual currency developments, it is vital that regulation foster, not hinder, innovation.
- Chad and Mike then discussed that while the use case for bitcoin as currency is important, much of the focus now is on the seemingly limitless potential of the underlying distributed ledger technology or blockchain that facilitates the exchange of bitcoin.
- Blockchain represents what could be a fundamental shift in the way we move and trade assets and information, and the implications could be enormous for everything from finance to real estate to intellectual property.



- Mike discussed how itBit recognized from its beginnings that for a technology struggling to be understood by the general marketplace and hoping to interface with a highly regulated financial industry, it must have regulatory structures and compliance programs in place which assisted in the company's trust company charter process with New York.
- Chad described how businesses hoping to become part of the larger financial infrastructure will need similar protocols and should welcome thoughtful regulation as it will help facilitate growth and greater acceptance.
- California, New Jersey and Connecticut are currently working on regulation and legislation and it is also critical that when these legislators and regulatory agencies are considering these new technologies that they allow for significant flexibility so as not to stifle innovation.
- Finally, the panelists discussed the maturation of these technologies and how there is an overall improvement in the underlying fundamentals of cryptocurrencies and blockchain technology, leading to less speculation and instead, more investment and a focus on development to improve functionality.
- This maturation is evidenced by the interest of major financial institutions in experimenting with virtual currency and blockchain technologies which will undoubtedly lead to more innovation and greater acceptance.

The event's second panel was moderated by Cleary Gottlieb partner **Pamela Marcogliese** who led a lively conversation with Daniel Alter, Peter Van Valkenburgh and Cleary Gottlieb associate **Colin Lloyd**.

- The discussion began by exploring whether bitcoin is considered a currency or not and what that means for how it is regulated and utilized going forward.
- Peter noted that, as mentioned during the first panel, bitcoin certainly has use as currency, particularly for people outside the traditional banking system, however it is the underlying blockchain technology that could revolutionize the way individuals and institutions trade virtually anything.
- Daniel, who helped create New York's BitLicense regulations during his time with the NYDFS, discussed the challenges of regulating a still-emerging technology and underscored the need to balance technological evolution and free market access with consumer protections and anti-money laundering (AML) issues.
- The panel discussed how regulation is currently being addressed on a state-by-state basis. There has been little direction from federal agencies other than the guidance issued by FinCEN last fall that considered bitcoin businesses and exchanges to be money transmitters for the sake of AML regulation, etc. even if exchanges behave more like traditional securities or commodities exchanges, where no money is transferred.
- Colin noted that to-date the CFTC has avoided the topic of bitcoin and its regulation, likely because of the issue of categorization. The question is whether it would be considered an excluded commodity, like a currency, or an exempt commodity, like gold or oil. How it is eventually categorized will have significant consequences in terms of the tools available to the CFTC to deal with potential market manipulation relating to cryptocurrencies.
- The question of how to regulate cryptotechnology businesses will continue to be raised both domestically and internationally. The panelists noted the importance of achieving some consistency between states in the U.S. and, eventually, between nations in an effort to maintain ease of use and continue to promote the acceptance of these technologies.

While no one is certain what the future holds for virtual currencies and blockchain technology, recent developments and steps towards a regulatory framework are attracting interest from major global banks, financial industry stalwarts as well as major retailers, investors and entrepreneurs. The possibilities and opportunities are seemingly endless, particularly for the applications relating to the blockchain. Cleary Gottlieb is excited to be a pioneer in this emerging area at the intersection of finance, technology and law and we will continue to lead the discussion.