



STATE OF CALIFORNIA

Department of Business Oversight

GOVERNOR Gavin Newsom • COMMISSIONER Manuel P. Alvarez

IN REPLY REFER TO:
FILE NO: _____

July 28, 2020

VIA EMAIL ONLY

Re: _____

Dear Mr. _____:

Thank you for your letter to Oscar Lumen, Assistant Deputy Commissioner of the Money Transmitter Division, dated June 26, 2020. As Senior Counsel for the Legal Division, I have been assigned to respond to this matter. In your letter, you explained the proposed business models of _____ (“_____”) and requested that the Department notify _____ if the proposed activities would require a license from the Department.

_____’s Proposed Activities

In your letter, you explained two proposed business models: the Tri-Party Repo and the Prime Brokerage.

Tri-Party Repo

For this business model, you explain that _____ acts as a third party to a repurchase transaction related to borrowing and lending cryptocurrency. After two parties agree to the terms of the transaction, each party places the agreed-upon amount of margin from their digital wallet to their designated _____ escrow accounts. The escrow accounts are owned by _____ and only _____ can move the funds between the accounts and send funds to the originating wallet.

If a situation occurs where additional funds are needed to rebalance the repurchase, the owing party will deposit the additional funds into their escrow account, _____ will move the funds from the owing party’s escrow account to the owed party’s escrow account, and then move the funds to the owed party.

When the transaction has concluded, and if no default has occurred, _____ sends the escrow balances back to the originating wallet. If a default has occurred, the non-defaulting party then has access to the defaulting party’s escrow account. _____ will transfer the escrow funds from the defaulting party’s escrow account, to the non-defaulting party’s escrow account, and then to the non-defaulting party.

Prime Brokerage

_____ proposes a second model whereby its customers can open accounts through _____ to facilitate exchanges on a variety of cryptocurrency exchanges where _____ maintains corporate accounts at the exchange. If a customer funds a brokerage account with cryptocurrency, the customer sends the cryptocurrency from the customer's wallet to a _____ wallet at an exchange where _____ has a corporate account. If a customer funds the brokerage account with fiat currency, the customer first wires the funds to _____'s account at _____ Bank, and then it is transferred to _____'s account at an exchange. You explained that _____ has control and ownership of the accounts at _____ Bank and the accounts and wallets at the cryptocurrency exchanges and that customer funds are only moved at the request of the customer.

Analysis

As you recognized in your letter, the Department continues to study the cryptocurrency industry closely. Whether cryptocurrencies are a viable form of money or a speculative non-money asset is widely debated. Given this ongoing debate, the Department has not concluded whether cryptocurrencies are a form of money or whether they may trigger the application of the California Money Transmission Act. Therefore, the Department will not require _____ licensed and supervised for those transactions under the Money Transmission Act at this time. Please be aware, however, that this is subject to change. At any time, the Department may determine that _____'s activities are subject to regulatory supervision. The Department may also adopt regulations or issue interpretive opinions that significantly restrict _____'s business operations.

This letter only addresses _____'s licensing obligations under the Money Transmission Act. However, _____'s business models, particularly the Tri-Party Repo business model, may be subject to the California Escrow Law (Financial Code 17000 et seq.) and any unlicensed escrow activity may subject it to enforcement action.

You may contact me at _____ with any questions.

Sincerely,

Manuel P. Alvarez
Commissioner
Department of Business Oversight

By

Senior Counsel

JJ:ss

cc: Robert Venchiarutti, Deputy Commissioner, Money Transmitter Division
Mona Elsheikh, Deputy Commissioner, Financial Services Division