

# Crypto Council for Innovation

March 17, 2023

Adrienne A. Harris  
Superintendent  
New York Department of Financial Services  
1 State Street, 20th Floor  
New York, NY 10004-1561

**RE: Virtual Currency Licensee Assessments [DFS-03-23-00002-P]**

Dear Superintendent Harris:

On behalf of the Crypto Council for Innovation (“CCI”), I respectfully submit this letter in response to the New York Department of Financial Services’ (“DFS” or “the Department”) notice of proposed rulemaking regarding Virtual Currency Licensee Assessments, which would promulgate Part 102 of Title 23 of the Official Compilation of Codes, Rules and Regulations of the State of New York.

CCI is an international organization advocating for inclusive regulation of the digital asset and web3 industries. The Council has staff in four countries who provide evidenced-based analysis to inform the next stages of crypto policy. Several of our [members](#), including Block, Coinbase, Fidelity Digital Assets, and Gemini, are licensed by the Department. We believe that trusted partnership between government and business stakeholders is key to crafting inclusive policy that benefits consumers and industry alike.

CCI and its members appreciate that the Department is one of the first leaders in providing regulatory oversight over virtual currency business activity (“VCBA”). We recognize that the Department has invested a tremendous amount of resources to enact a comprehensive regulatory regime balancing innovation and consumer protection to supervise VCBA in New York. To that end, CCI supports fair and reasonable assessments on VCBA licensees, to ensure that New York will remain a hub for responsible innovation in the Web3 and digital asset ecosystem. In particular, we urge the DFS to use these assessments to provide for more timely review processes, clearly defined timelines regarding such review processes, and early, constructive supervisory feedback to licensees. The digital asset and Web3 industry is one that seeks clear guidance, timelines for product approvals, and a proper regulatory framework in order to best

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bring to market the products the U.S. customer base is demanding in a safe and secure manner, and this is an area where the Department can continue to lead.

### **The Proposed Assessments are Difficult to Predict**

The Department should clarify the underlying calculation of the assessment amounts. The proposed rule calculates assessments by dividing the VCBA-related costs among licensees based on a complicated and opaque formula, primarily focused on transaction volume and the value of custodied assets, with no consideration of the complexity of a licensee’s offerings. For example, the proposed assessment formula does not take into account the various types of digital asset businesses and the products they offer. The proposed rule would categorically treat all digital asset businesses the same for purposes of the assessment formula without taking into account any of the complexity of a licensee’s offering. The proposed rule then gives DFS the authority to levy additional special assessments on licensees where, in the superintendent’s sole discretion, “expenses associated with a specific examination, investigation or review are best allocated solely to the individual Licensee or Licensees subject to such examination or investigation.”<sup>1</sup>

Not only does DFS make the sole determination (without providing additional details) of how to allocate these costs but it also retains the sole discretion to initiate, conduct, and conclude any investigation into any licensee at any time. These investigations historically can take years, with very little transparency as to their focus or process, and certain of these investigations ostensibly do not result in any allegation or finding of wrongdoing. DFS could theoretically start an exam or investigation of multiple entities at a given time, take months or even years to conduct its investigation, and then bill each licensee separately, all without any public accounting of how DFS arrived at that number or ability to challenge the hours worked or fees charged. Future administrations could use special assessments punitively, imposing shadow fines without any finding or even allegation of wrongdoing at the end of an investigation.

As a result of the discretion afforded to the Department, licensees will be left with a regulatory structure where it will be impossible for them to predict or plan for their assessments, while at the same time, it is unclear how the Department will conduct its investigations or examinations in an efficient or consistent manner.

Without greater transparency and accountability, including the ability for licensees to challenge such special assessments, the Department’s discretion could potentially be subject to, in the extreme, misuse, or at the very least, unintended inefficiencies. While we recognize this is not the Department’s intention, it could theoretically make up for any budgetary shortfalls by charging unchallengeable special assessments to any licensee in any given year. Given the Department’s continued leadership in both the banking and digital asset space, it is important for the Department to set the standard and a positive precedent for other state regulators when it comes to assessments. If DFS is to enact this authority, at the very least licensees should be kept

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<sup>1</sup> Virtual Currency Licensee Assessments, N.Y. Comp. Codes R. & Regs. tit. 23, § 102.6 (proposed Dec. 28, 2022).

apprised of their “balance” on a monthly basis while an investigation or other qualifying activity is being conducted.

Relatedly, the proposed rule also lacks any semblance of transparency into how the assessments are distributed among licensees. In addition to either removing the special assessment provision or allowing them to be challenged, to promote further transparency and accountability, CCI recommends adding a provision to the proposed rule that requires the Department to publish an annual report, similar to reports required by the Financial Services Law, detailing the amount of assessments levied against each licensee and the corresponding percentage of assessments paid by each licensee. This would allow licensees to understand how much of the financial burden they are being asked to shoulder each year. All of our members would willingly accept public disclosure of their regular assessments in exchange for greater transparency. Additionally, instead of focusing solely on the volume of transactions and value of assets being custodied, the Department should consider how it could weigh the complexity of a licensee’s offerings into calculating assessments, with licensees with more complex offerings bearing a larger share of the assessments due to the corresponding increase in Department resources required to supervise complex offerings.

### **The Proposed Rule’s Determination of Custody Basis Should be Limited to Assets of New York Customers**

The proposed rule calculates assessments, in part, based on the licensee’s “Custody Basis,” which is determined by examining “the total United States Dollar value of virtual currency held on behalf of customers by each Licensee. . .” This term, however, is overinclusive, and unfairly considers funds held on behalf of customers who have no relationship or nexus to New York. By considering non-New York customer assets, this definition could lead to unfair and unequal treatment for similarly situated licensees. Some licensees have established New York-specific entities that only conduct business in New York and have a sister company conduct business in the other forty-nine states, while other licensees have a single entity operate across the United States, including New York. Take for example, two licensees, one of which has limited its operations to New York and the other operates nationally. In a situation where both of these licensees have identical amounts of New York-customer assets, the national operator will be assessed at a much higher rate.

This treatment is inconsistent and problematic when considering that in analogous circumstances, the Department limits the calculation of assessments to economic activity generated in New York. One obvious example is the proposed rule’s calculation of the Transaction Volume Basis, which is limited to transactions that solely occur in New York.<sup>2</sup> Similarly and fairly, other DFS assessment rules also calculate assessments based only on New York activity. *See* N.Y. Comp. Codes R. & Regs. tit. 23, § 101.2(g)(2) (in determining assessments for mortgage-related entities, the rule limits the consideration of total gross revenues

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<sup>2</sup> *Id.* at § 102.2(l).

to only that which is generated from New York State operations; *id.* § 101.2(g)(3)(limiting assessments for Licensed Financial Services Providers to activities that occur in New York).<sup>3</sup> There is no reason not to follow previous DFS assessment rules for VCBA licensees as well.

### **Imposition of Assessments Should Come with Corresponding Enhancements and Accountability**

Over the last several years, the Department has been subject to wide ranging criticism regarding its review of VCBA applications and supervision of VCBA licensees. CCI respectfully encourages the DFS to adhere to its own requirements to approve or reject VCBA applications within 90 days.<sup>4</sup> Licensees have previously noted that DFS ignores its own regulations by disregarding or extending approval timelines for applications related to new products, services, name changes, changes in ownership, and other routine matters.<sup>5</sup>

In both cases, the explanation is often that the “clock has not started,” because an application is “incomplete.” While CCI respects the need for the Department to have adequate time to review and approve such applications, the Department should also provide clarity regarding timelines at the onset of an application. Otherwise, it is extremely difficult for companies to consider operational costs, which can impact market entry decisions and commercial growth for New York. Applicants are often not provided details of what’s required to make an application complete until three, four, sometimes twelve months after the application was originally submitted, which is well beyond the approval timeline provided in the Department’s regulations or the supervisory agreement. Applicants and licensees are also not provided a template for approval or a substantive roadmap. Most often, licensees are simply given ad hoc explanations for what is required for DFS to “get comfortable with it” at a given moment in time, but without any assurances that compromises or limitations by the applicant will advance the application in a meaningful way.

CCI understands the need for the Department to have adequate resources to foster safe and innovative digital asset markets in New York. With such additional resources being contributed by licensees, the Department should continue to build on the improvements made under this Administration in its responsiveness and adherence to statutory and regulatory deadlines. This is critically important, as it will allow the DFS and its regulatory framework to best keep pace with

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<sup>3</sup> In contrast to the other Banking Division Assessments, which limit consideration to New York-based activity, the calculation of the Industry Financial Basis for Depository Institutions Group considers “total assets of all institutions in the group.” N.Y. Comp. Codes R. & Regs. tit. 23, § 101.2(g)(1). For banking organizations chartered in New York and supervised by DFS, however, DFS is the primary state regulator and responsible for supervising the bank’s interactions with customers from across the country. This is distinguishable from DFS’s authority to regulate VCBA licensees, many of which are licensed in almost every state, and where DFS’s authority is limited to activity that occurs within the state. See N.Y. Comp. Codes R. & Regs. tit. 23, § 200.2(q) (limiting the definition of “Virtual Currency Business Activity” to certain enumerated activity “involving New York or a New York Resident.”).

<sup>4</sup> N.Y. Comp. Codes R. & Regs. tit. 23, § 200.6.

<sup>5</sup> See, e.g., *id.* at § 200.11(a)(4), (b)(2).

digital asset innovation. CCI was heartened to learn that the ability to levy assessments was met with an increase in hiring at DFS. Industry estimates are that DFS has added approximately 40 individuals to the virtual currency bureau. CCI sees this as a productive first step. Consumers and industry are better off with more experienced and knowledgeable public servants to uphold the integrity of crypto markets and provide robust consumer protections. However, industry also requires greater predictability, accountability, and clarity when it comes to supervision. If the Department is going to levy substantial assessments, then we respectfully submit that the DFS must also improve its responsiveness to licensees and improve application approval timelines.

We appreciate the opportunity to provide feedback on this important rulemaking, and we look forward to working with the Department and other stakeholders on these important issues.

Sincerely,

A handwritten signature in black ink, appearing to be 'S. Warren', with a long horizontal flourish extending to the right.

Sheila Warren, Esq.  
Chief Executive Officer  
Crypto Council for Innovation