

What the Veto of California's Digital Financial Assets Law Means for the Future of Cryptocurrency Regulation

3 min read

Oct 12, 2022

By: Bonnie E. Dye

On September 23, 2022, California Gov. Gavin Newsom vetoed [Assembly Bill 2269](#), known as the Digital Financial Assets Law, which would have implemented a new licensing regime for digital asset businesses operating within California. Without the Governor's veto, these businesses would have been subject to ongoing oversight and examination by the California Department of Financial Protection and Innovation (DFPI) and substantive requirements with respect to consumer disclosures and development of policies and procedures to address perceived risk concerns.

In his [veto message](#), Gov. Newsom wrote that “[i]t is premature to lock a licensing structure in statute without considering both [previous research and outreach] work and forthcoming federal actions.” He added that “a more flexible approach is needed” and “standing up a new regulatory program is a costly undertaking, and this bill would require a loan from the general fund in the tens of millions of dollars for the first several years.” In addition to the financial and logistical concerns surrounding the implementation of a new licensing regime, his veto likely took into account President Biden's framework for responsible development of digital assets issued a week before.

The Digital Financial Assets Law was introduced in June 2022 to provide consumer protection in the cryptocurrency market and to cover crypto business activity likely outside the scope of the California Money Transmission Act. AB 2269 proposed that subject to limited exceptions, a license would be required to “engage in digital financial asset business activity or hold [oneself] out as being able to engage in digital financial asset business activity with or on behalf of residents.” The legislation defined “digital financial asset” as a digital representation of value that is used as a medium of exchange, unit of account, or store of value, and that is not legal tender, whether or not denominated in legal tender.

AB 2269 further defined “digital financial asset activities” to mean any of the following:

1. Exchanging, transferring, or storing a digital financial asset or engaging in digital financial asset administration, whether directly or through an agreement with a digital financial asset control services vendor.
2. Holding electronic precious metals or electronic certificates representing interests in precious metals on behalf of another person or issuing shares or electronic certificates representing interests in precious metals.
3. Exchanging one or more digital representations of value used within one or more online games, game platforms, or family of games for either of the following:
 - a. A digital financial asset offered by or on behalf of the same publisher from which the original digital representation of value was received; or
 - b. Legal tender or bank or credit union credit outside the online game, game platform, or family of games offered by or on behalf of the same publisher from which the original digital representation of value was received.

AB 2269 would have required applicants to satisfy net worth and surety bond requirements in an amount to be left to the DFPI's discretion. It also would have required applicants to develop and maintain operational policies and procedures addressing concerns relating to information and operational security, business continuity, disaster recovery, anti-fraud, money laundering prevention, and prevention of funding terrorist activities.

Another feature of AB 2269 was to require licensees to provide specific consumer disclosures before engaging in digital financial asset business activity with a resident. These disclosures concerned fees and charges, whether products or services would be covered by a form of insurance, and information relating to transaction after initiation—such as whether a transfer or exchange is irrevocable or options in light of unauthorized, mistaken, or accidental transfers or exchanges. Additionally, a licensee would have been required to provide the consumer after a transaction with notice of the licensee's name and contact information, details regarding the time and value of the transaction, and fees charged for the transaction.

Even though AB 2269 was ultimately vetoed, California is likely to adopt a regulatory scheme for oversight of crypto-businesses operating in the state at some point in the future. A focus on consumer protections in this way aligns with California [executive order](#) dated May 4, 2022, describing “[i]t shall be the goal of the State to create a transparent and consistent business environment for companies operating in blockchain, including crypto assets and related financial technologies, that harmonizes federal and California laws, balances the benefits and risks to consumers, and incorporates California values, such as equity, inclusivity, and environmental protection.” What is left unclear is whether future proposed regulatory schemes will incorporate features of the Digital Financial Asset Law, but that will likely come into focus as more guidance is provided at the federal level.

Hinshaw & Culbertson LLP is a U.S.-based law firm with offices nationwide. The firm's national reputation spans the insurance industry, the financial services sector, professional services, and other highly regulated industries. Hinshaw provides holistic legal solutions—from litigation and dispute resolution, and business advisory and transactional services, to regulatory compliance—for clients of all sizes. Visit www.hinshawlaw.com for more information and follow @Hinshaw on LinkedIn and X.

Topics

California, Cryptocurrency, Digital Financial Asset Law, California Department Of Financial Protection And Innovation