

**UNIFORM SUPPLEMENTAL COMMERCIAL LAW
FOR THE UNIFORM REGULATION OF VIRTUAL-
CURRENCY BUSINESSES ACT**

Drafted by the

NATIONAL CONFERENCE OF COMMISSIONERS
ON UNIFORM STATE LAWS

and by it

APPROVED AND RECOMMENDED FOR ENACTMENT
IN ALL THE STATES

at its

ANNUAL CONFERENCE
MEETING IN ITS ONE-HUNDRED-AND-TWENTY-SEVENTH YEAR
LOUISVILLE, KENTUCKY
JULY 20 - JULY 26, 2018

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By

NATIONAL CONFERENCE OF COMMISSIONERS
ON UNIFORM STATE LAWS

October 2, 2018

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UNIFORM SUPPLEMENTAL COMMERCIAL LAW FOR THE UNIFORM REGULATION OF VIRTUAL-CURRENCY BUSINESSES ACT

Prefatory Note

The Uniform Regulation of Virtual-Currency Businesses Act (URVCBA), to which this Act is a supplement, establishes a regulatory structure for businesses engaging in or offering to residents of enacting states certain virtual-currency transfer, exchange, or custodial services. The URVCBA provides certainty and protections that will enable such businesses to operate to everyone's benefit. It includes provisions to enable start-up companies offering virtual-currency services room to test products and operate prior to full licensure without violating state "money transmitter" or "money services" laws or risking federal prosecution for being unlicensed under 18 U.S.C. Section 1960.

As a regulatory act, the URVCBA provides a number of user protections. The user protections in Section 502 of the URVCBA are based on commercial law principles, but the main focus of that section is user protection, rather than commercial law rules for covered transactions. When the Uniform Law Commission approved the URVCBA in 2017, it contemplated this supplemental commercial law act as a companion to the URVCBA.

This act serves two purposes: it protects users; and provides the virtual-currency system with commercial law rules that both protect users and promote certainty and finality in transactions. It provides rights to customers of virtual-currency businesses that are comparable to the rights enjoyed by customers of securities intermediaries under Part 5 of Article 8 of the Uniform Commercial Code.

Adoption of this act in connection with the enactment of the URVCBA is strongly recommended to give users of virtual-currency businesses, and the businesses themselves, comparable certainty about their dealings with each other and with certain third parties. This act assumes that the state considering this act has enacted the URVCBA or will enact both acts substantially concurrently.

This act has further specific goals. First, it better enables owners of virtual-currency assets to offer their virtual currency as collateral under Article 9 of the Uniform Commercial Code. Secured parties obtaining virtual currency as collateral will be able to proceed in a manner comparable to traditional securities held in "securities accounts" subject to UCC Article 8.

A second goal is to enhance the "negotiability" of virtual currency when transferred or exchanged.

A third goal is to harmonize the laws governing custody of virtual currencies subject to this act or its equivalent and the URVCBA with the Convention on the Law Applicable to Certain Rights in Respect of Securities Held with an Intermediary. This Convention became effective as a matter of U.S. law on April 1, 2017, and the issues surrounding it are described more fully in the Official Comments to this act.

As a matter of user protection, this act is designed to replace Section 502 of the URVCBA, in jurisdictions that enact both the URVCBA and this act. Section 502 as approved by the Uniform Law Commissioners in July 2017 provides:

SECTION 502. PROPERTY INTERESTS AND ENTITLEMENTS TO VIRTUAL CURRENCY.

(a) A licensee or registrant that has control of virtual currency for one or more persons shall maintain in its control an amount of each type of virtual currency sufficient to satisfy the aggregate entitlements of the persons to the type of virtual currency.

(b) If a licensee or registrant violates subsection (a), the property interests of the persons in the virtual currency are pro rata property interests in the type of virtual currency to which the persons are entitled, without regard to the time the persons became entitled to the virtual currency or the licensee or registrant obtained control of the virtual currency.

(c) The virtual currency referred to in this section is:

- (1) held for the persons entitled to the virtual currency;
- (2) not property of the licensee or registrant; and
- (3) not subject to the claims of creditors of the licensee or registrant.

Official Comment 1 to Section 502 of the URVCBA provides:

This section is based on Uniform Commercial Code (“UCC”) Sections 8-503 and 8-504 and protects the owner of virtual currency that is entrusted to a licensee or registrant for a purpose governed by this act. Enforcement is by the department, but also by private rights of action under this section as mentioned in Section 407. In essence, this section takes the virtual currency under the control of a licensee or registrant off the balance sheet of the virtual-currency business and beyond the business’ right to deal with it as their own property. This formulation reduces the need for greater net worth and reserves than Section 204 requires without sacrificing user protection.

This act more comprehensively implements the user protections in URVCBA Section 502 by directly applying the provisions of UCC Article 8, Part 5, on which Section 502 was based. Also, unlike Section 502, this act covers users who are not residents of states that enact the URVCBA.

The Official Comments to this Act describe some of the provisions and effects of UCC Article 8. The Official Text and Official Comments of UCC Article 8 should be consulted for additional guidance.

The application of some of the concepts used in Article 8 has no effect on the status of virtual currency under other law.

**UNIFORM SUPPLEMENTAL COMMERCIAL LAW FOR THE UNIFORM
REGULATION OF VIRTUAL-CURRENCY BUSINESSES ACT**

SECTION 1. SHORT TITLE. This [act] may be cited as the Uniform Supplemental Commercial Law for the Uniform Regulation of Virtual-Currency Businesses Act.

SECTION 2. DEFINITIONS.

(a) In this [act]:

(1) “Article 8” means Article 8 of the Uniform Commercial Code [, as amended], in substantially the form approved by the American Law Institute and the National Conference of Commissioners on Uniform State Laws.

(2) “Control” has the meaning provided in [insert citation to Section 102(3)(A) of the Uniform Regulation of Virtual-Currency Businesses Act].

(3) “Hague Securities Convention” means the Convention on the Law Applicable to Certain Rights in Respect of Securities Held with an Intermediary, concluded 5 July 2006.

(4) “Uniform Commercial Code jurisdiction” means a state that has enacted Article 8.

(5) “Uniform Regulation of Virtual-Currency Businesses Act” means [insert citation to the Uniform Regulation of Virtual-Currency Businesses Act].

(6) “User” means a person for which a licensee or registrant has control of virtual currency.

(b) Other definitions applying to this [act] and the sections of the Uniform Regulation of Virtual-Currency Businesses Act in which they appear are:

“Licensee”. Section 102(9).

“Person”. Section 102(10).

“Record”. Section 102(12).

“Registrant”. Section 102(13).

“Resident”. Section 102(16).

“Sign”. Section 102(18).

“State”. Section 102(19).

“Virtual currency”. Section 102(23).

(c) Other definitions applying to this [act] and the sections of Article 8 in which they appear are:

“Entitlement holder”. Section 8-102(a)(7).

“Financial asset”. Section 8-102(a)(9).

“Securities intermediary”. Section 8-102(a)(14).

“Security”. Section 8-102(a)(15).

“Securities account”. Section 8-501.

(d) The definition of “agreement” applying to this [act] appears in Section 1-201(b)(3) of Article 1 of the Uniform Commercial Code[, as amended], in substantially the form approved by the American Law Institute and the National Conference of Commissioners on Uniform State Laws.

Legislative Note: *In states in which the constitution, or other law, does not permit the phrase “as amended” when statutes of other jurisdictions are incorporated into state law, the phrase should be deleted in subsection (a)(1).*

Official Comment

As explained in the Official Comments to Section 4, the applicable enactment of Article 8 of the Uniform Commercial Code (the “UCC”) will usually be that of the state whose law governs or that is otherwise chosen in the account agreement between the licensee or registrant and the user. For the purposes of this act, the applicable enactment need not be that of the enacting state. At this time there are no material differences among the Article 8 enactments of the various states on the matters addressed in this act.

The term “user” includes but is not confined to a “resident” as defined in the Uniform Regulation of Virtual-Currency Businesses Act (referred to in these Official Comments as the “URVCBA”). The broader term “user” is necessary so that the same protections afforded to a “resident” of the enacting state under this act are afforded to non-residents for whom the licensee or registrant controls virtual currency. If the protections of this act were afforded only to a “resident” of the enacting state, the “resident” would be able to benefit from the protections of this act in the enacting state but could also make claims under the laws of another jurisdiction to the prejudice of residents of the other jurisdiction and other non-residents. UCC Article 8 takes an approach consistent with the coverage of “users” by not limiting the term “entitlement holder” to residents of the enacting state.

SECTION 3. SCOPE. This [act] applies to:

(1) a person or transaction governed by the Uniform Regulation of Virtual-Currency Businesses Act; and

(2) a user that is not a resident if the user or transaction with the user would be governed by the Uniform Regulation of Virtual-Currency Businesses Act if the user were a resident.

Official Comment

This uniform act is designed to work in conjunction with the URVCBA.

SECTION 4. INCORPORATION OF ARTICLE 8.

(a) The relationship between a licensee or registrant and a user must be evidenced by an agreement in a record signed by the licensee or registrant and by the user. The agreement:

(1) must specify the jurisdiction whose law governs the agreement;

(2) if governed by the law of a jurisdiction that is not a Uniform Commercial Code jurisdiction, must:

(A) specify a Uniform Commercial Code jurisdiction as the securities intermediary’s jurisdiction for the purpose of Article 8; and

(B) state that the law in force in the Uniform Commercial Code jurisdiction under subparagraph (A) applies to all issues specified in Article 2(1) of the Hague Securities Convention;

(3) must state that:

(A) the licensee or registrant is a securities intermediary;

(B) the control of virtual currency by the licensee or registrant for the benefit of the user creates a securities account of which the user is the entitlement holder;

(C) the parties agree that the virtual currency is to be treated as a financial asset credited or held for credit to the securities account of the user; and

(D) the licensee or registrant will not grant a security interest in virtual currency which the licensee or registrant is obligated to maintain under Section 8-504(a) of Article 8;

(4) may not provide a standard for the licensee or registrant to comply with its duties under Part 5 of Article 8 which is less protective of the user than the standard that would apply under Part 5 of Article 8 in the absence of an agreement concerning the standard; and

(5) may not provide that:

(A) the securities intermediary's jurisdiction for the purpose of Article 8 is a jurisdiction that is not a Uniform Commercial Code jurisdiction; or

(B) the law in force in a jurisdiction that is not a Uniform Commercial Code jurisdiction applies to all issues specified in Article 2(1) of the Hague Securities Convention.

(b) To the extent that there is no agreement that complies with subsection (a), the relationship between a licensee or registrant and a user is determined as if the licensee or registrant and the user have an agreement that complies with subsection (a) and specifies that the law of this state governs the agreement.

(c) The effect of this section may not be varied by agreement.

Official Comment

1. General. A primary goal of this act is to provide commercial law rules for licensees and registrants under the URVCBA and their customers – “users” under the definitions of this act – so that both sides of a relationship that involves the licensee or registrant taking “control” of virtual currency (as defined in the URVCBA) know what their respective rights and duties are. The approach taken requires the parties to “opt in” to the provisions of Part 5 of UCC Article 8 as a substitute for compliance with Section 502 of the URVCBA.

A distinct advantage of this approach is that it provides a clear path for users that seek to grant, and to secured parties that seek to enforce, UCC Article 9 security interests in virtual currencies. Under this act, for purposes of UCC Articles 8 and 9, virtual currencies under the “control” of licensees or registrants as that term is defined in the URVCBA is “investment property” and not “general intangibles”. Another advantage of this approach is to provide virtual currencies with the same benefits of negotiability as are provided for indirectly-held securities under UCC Article 8. These advantages are further explained in Official Comment 5.

Another primary goal is to apply to the licensee and registrant the duties discussed in Official Comment 2.b to this Section for the protection of the user.

Subsection 4(a) is the key provision by which a licensee or registrant operating under the URVCBA and user opt in to UCC Article 8. These Official Comments describe the effect of their doing so. When they do so in compliance with provisions of this section, the parties substitute their rights and duties under UCC Article 8 for their rights and duties under Section 502 of the URVCBA. See the Legislative Note to Section 12 of this act. Official Comment 6 explains protections provided in this section that are in addition to protections provided in UCC Article 8.

Subsection 4(a) requires that the agreement between the licensee or registrant and the user be governed by, or otherwise point to, UCC Article 8 as enacted by a Uniform Commercial Code jurisdiction, so that the commercial law rules of Article 8 will apply. In the absence of such a requirement, the agreement could avoid the commercial law rules intended for this act. The choice-of-law rules affecting the agreement are discussed in Official Comment 3 to this section.

Subsections 4(a)(2)(B) and 4(a)(5)(B) refer to the law “in force” in a particular jurisdiction. This language specifically addresses the fact that the “law in force” in every jurisdiction in the United States includes the treaty obligations of the United States, such as the Hague Securities Convention.

2. Summary of the Substantive Provisions of UCC Article 8. Article 8 sets forth a statutory scheme for the holding and transfer of investment property, including investment securities such as stocks and bonds, and other “financial assets.” The statutory scheme relevant to this act applies to assets held indirectly by an investor through a bank, broker or other intermediary (so-called “indirectly-held securities”). Although the primary focus of UCC Article 8 is generally on investment securities, Article 8’s indirect holding system has a broader scope

that covers all security entitlements, as Official Comment 9 to UCC Section 8-102 explains.

a. Terminology. Under UCC Article 8, a bank, broker or other person that in the ordinary course of its business maintains securities accounts for others and is acting in that capacity is referred to as a “securities intermediary.” UCC Section 8-102(a)(14). A “securities account” is an account to which a “financial asset” is or may be credited in accordance with an agreement under which the person for whom the account is maintained is entitled to exercise the rights that comprise the financial asset, as these terms are defined in UCC Sections 8-501(a)(1) and 9-102(a)(9), respectively. A financial asset under Article 8 includes not only a “security” as defined in UCC Section 8-102(a)(15), but also “*any property* that is held by a securities intermediary for another person in a securities account if the securities intermediary has expressly agreed with the other person that the property is to be treated as a financial asset.” UCC Section 8-102(a)(9)(i), (iii) (emphasis added).

Once the securities intermediary has indicated by book entry that a financial asset has been credited to a person’s securities account, the person is referred to as an “entitlement holder” (UCC Section 8-102(a)(7)), and the person has a “security entitlement” with respect to the financial asset. UCC Section 8-501(b)(1). A security entitlement encompasses the rights and property interest of an entitlement holder with respect to a financial asset as specified in UCC Section 8-102(a)(17).

b. Securities Intermediary’s Duties and Protections in the Indirect Holding System. The rights comprising a security entitlement with respect to a financial asset include the rights of the entitlement holder to enforce the duties of the securities intermediary under Part 5 of Article 8. Those duties (the “Part 5 Duties”) consist of the duty to maintain sufficient financial assets to satisfy all security entitlements to the financial assets (UCC Section 8-504), the duty to take action to obtain a payment or distribution made by the issuer of the financial asset (UCC Section 8-505), the duty to exercise rights in respect of the financial asset as directed by the entitlement holder (UCC Section 8-506), the duty to comply with the entitlement holder’s instruction (referred to in Article 8 as an “entitlement order,” which is defined in UCC Section 8-102(a)(8)) to transfer or redeem a financial asset (UCC Section 8-507), and the duty to change the security entitlement to another form of holding for which the entitlement holder is eligible, or to deliver out a financial asset, at the request of the entitlement holder (UCC Section 8-508).

A security entitlement with respect to a financial asset also includes, to the extent necessary to satisfy the security entitlements with respect to a particular financial asset, a pro rata property interest in all interests of the securities intermediary in that financial asset. UCC Section 8-503(b). For example, if an entitlement holder has 100 shares of XYZ stock credited to its account with a securities intermediary, and nine other entitlement holders have an aggregate of 900 shares of XYZ stock credited to their accounts with the same securities intermediary, and the securities intermediary has 1,000 shares of XYZ stock credited to its account at a clearing corporation (such as Depository Trust Company), then the entitlement holder has a property right to 100 of the 1,000 shares of XYZ stock as its pro rata share of the “fungible bulk” of XYZ stock held by the securities intermediary.

By contrast, if in violation of its obligation under UCC Section 8-504, the securities intermediary has only 800 shares of XYZ stock credited to its account at the clearing corporation (and no other XYZ stock held in other ways), then the entitlement holder has a property right to only 80 shares of XYZ stock, with an unsecured claim against the securities intermediary for the value of the remaining 20 shares. See Official Comment 1 to UCC Section 8-503.

As the last example suggests, the Part 5 Duties are generally enforceable by the entitlement holder against the securities intermediary under the UCC. As UCC Section 1-305(b) explains: “Any right or obligation declared by [the UCC] is enforceable by action unless the provision declaring it specifies a different or limited effect.” The United States Court of Appeals for the Sixth Circuit concluded that an entitlement holder has no private right of action under Part 5 of UCC Article 8 unless a provision in Part 5 expressly provides for a private right of action. See *Harris v. T.D. Ameritrade, Inc.*, 805 F.3d 664 (6th Cir. 2015). However, the court did not address UCC Section 1-305(b). Accordingly, the opinion is not persuasive authority. In addition, Subsection 407(c) of the URVCBA explicitly confers a private right of action for a violation of its Section 502. When this act becomes effective to replace Section 502 of the URVCBA as contemplated by the Legislative Note to Section 12 of this act, there will still be a private right of action under Subsection 407(c) of the URVCBA as well as under UCC Article 8.

The securities intermediary also has certain protections under UCC Article 8. For example, under UCC Section 8-115, a securities intermediary that transfers a financial asset pursuant to an effective entitlement order generally cannot be held liable to an adverse claimant, whether in conversion or otherwise, unless, among other things, the securities intermediary acted in collusion with the wrongdoer in violating the rights of the adverse claimant. See generally Official Comment 5 to UCC Section 8-115.

c. Claims of Creditors of the Securities Intermediary. A financial asset is generally not subject to the claims of creditors of the securities intermediary, to the extent necessary for the securities intermediary to satisfy all security entitlements with respect to the financial asset. UCC Sections 8-503(a), 8-511(a). However, if the securities intermediary has granted to the creditor a security interest in the financial asset, and the creditor has “control” of the financial asset as defined in UCC Section 8-106(d), then the claim of the secured creditor has priority over the claims of the entitlement holders (to the detriment of the entitlement holders if the securities intermediary has not complied with its duty to maintain sufficient financial assets). UCC Section 8-511(b).

Control for purposes of UCC Article 8 is a different concept from “control of virtual currency” as defined in Section 103 of the URVCBA. Under UCC Section 8-106(d), control generally requires that the creditor become the entitlement holder, or that the creditor have a so-called “control agreement” under which the securities intermediary agrees that it will comply with entitlement orders originated by the creditor without further consent of the entitlement holder. Under UCC Section 8-106(g), the securities intermediary may not enter into a control agreement in respect of a securities account without the consent of the entitlement holder. Pursuant to UCC Section 8-504(b), the securities intermediary similarly is not permitted to grant a security interest in the financial asset without the consent of the entitlement holder.

3. Summary of the Choice-of-law Rules of Article 8 relating to the Indirect Holding System; Effect of the Hague Securities Convention.

a. The Article 8 Choice-of-law Rules. UCC Article 8's choice-of-law rules are set forth in UCC Section 8-110. As a general matter, in a dispute in a court of a jurisdiction that has adopted the UCC (a "Uniform Commercial Code jurisdiction"), the court would apply the law of the jurisdiction that governs the account relationship between the securities intermediary and the entitlement holder to determine an issue addressed under Article 8 with respect to the indirect holding system. UCC Section 8-110(b), (e). There are currently no material differences among the Article 8 enactments of any Uniform Commercial Code jurisdiction in respect of matters relating to the indirect holding system. If the account agreement were governed by a law of a jurisdiction that had not adopted the UCC and the account agreement did not provide that a particular Uniform Commercial Code jurisdiction is the "securities intermediary's jurisdiction" for purposes of the UCC, then the non-UCC substantive law of the jurisdiction whose law governed the account relationship would determine the rules for transactions in indirectly-held securities, including whether financial assets were subject to the claims of the securities intermediary's creditors. *Id.*

b. Effect of the Hague Securities Convention. UCC Article 8's choice-of-law rules for securities credited to a securities account are affected by the Hague Securities Convention, which became effective as a matter of U.S. law on April 1, 2017. The Convention applies only to "securities" as defined in the Convention, but it is possible that that definition might be construed to include virtual currency.

The definition of "security" in the Convention, like the definition of the same term in UCC Article 8, is independent of its definition for purposes of federal or other regulatory law, because both the language and the purposes of the definitions differ from one another.

The choice-of-law rules of the Hague Securities Convention pre-empt the choice-of-law rules of UCC Article 8 for the issues covered by Article 2(1) of the Convention. Those issues substantially overlap with the issues addressed in the choice-of-law rules in Article 8 for securities held in the indirect holding system. Even so, the choice-of-law rules of the Convention, in most cases, will produce the same results as under the choice-of-law rules of Article 8.

Under Article 4(1) of the Hague Securities Convention, as a general matter, the court would determine an issue covered by Convention Article 2(1) by applying the law of the jurisdiction that expressly governs the account agreement between the securities intermediary and the entitlement holder, if the securities intermediary has an office that maintains securities accounts in the country of the jurisdiction (a "qualifying office"). The second sentence of Article 4(1) of the Convention sets forth the minimal activity that is required for this qualifying office test to be met. The United States is a "multi-unit State," so the qualifying office test is met for account agreements selecting the law of a particular U.S. state if the office in question is located in any U.S. state. Hague Securities Convention, Art. 12(1)(b). As a result, assuming that the qualifying office test is met, the issues to be determined by the choice-of-law rules of either the Convention or Article 8 generally would be determined by the law that expressly governs the

account agreement.

c. Parties' Autonomy to Modify Choice of Law. Under UCC Article 8, if the parties wish the law of a different jurisdiction than just discussed to apply, they can provide in the account agreement for the “securities intermediary’s jurisdiction” to be that different jurisdiction. UCC Section 8-110(e)(1). Under the Convention, the same wish is accommodated if the account agreement expressly provides that law of the different jurisdiction applies to all of the Article 2(1) issues, provided that the qualifying office test is met.

4. Application of Article 8 to Virtual-Currency Transactions. UCC Article 8 is a statute of broad coverage that in some circumstances permits parties to opt into its scheme by agreement, and for their transactions to be governed by the rules of UCC Article 8, for purposes of the indirect holding relationships to which they have agreed.

a. Application of Terminology. For a licensee or registrant to be subject to UCC Article 8, the licensee or registrant must be a “securities intermediary” maintaining a “securities account” to which a “financial asset” is or may be credited. The definitions of these three terms, taken together, indicate that a licensee or registrant who maintains accounts for users to which virtual currency is or may be credited, can expressly agree with the users to be subject to the rules of UCC Article 8.

The definition of “securities intermediary” is not confined to a bank or broker, nor to a person who is regulated under banking or securities law. Instead, under UCC Section 8-102(a)(14)(ii) it includes any “person . . . that in the ordinary course of its business maintains securities accounts for others and is acting in that capacity.” Likewise, the definition of “securities account” is not confined to an account at a bank or broker or other person regulated under banking or securities law. Instead, under UCC Section 8-501(a) it includes any “account to which a financial asset is or may be credited in accordance with an agreement under which the person maintaining the account undertakes the treat the person for whom the account is maintained as entitled to exercise the rights that comprise the financial asset.”

Similarly, the definition of “financial asset” is not confined to what UCC Article 8 or other laws define as a “security.” Instead, under UCC Section 8-102(a)(9)(iii) it includes “any property that is held by a securities intermediary for another person in a securities account if the securities intermediary has expressly agreed with the other person that the property is to be treated as a financial asset under [Article 8].” As Official Comment 9 to UCC Section 8-102 states: “The term financial asset is defined to include not only securities but also a broader category of obligations, shares, participations, and interests.” For a decision in which a bank certificate of deposit was treated as a financial asset credited to a securities account, see *Monticello Banking Co. v. Flener (In re Alexander)*, 429 B.R. 876 (Bankr. W.D. Ky. 2010), *aff’d*, 2011 WL 9961118 (6th Cir. 2011).

b. UCC Article 8 “Opt-in.” A licensee or registrant in the business of maintaining control of virtual currencies for users may expressly agree with the users that virtual currency of which the licensee or registrant has control for the users will be treated as “financial assets” credited to the users’ “securities accounts” under UCC Article 8. Article 8 does not

dictate what form the express agreement might take, but it would certainly permit the express agreement to be contained in the account agreement between the licensee or registrant and a user. Article 8, Part 5 sets limits on provisions in the agreement, as are described in subsection c of this Official Comment, *infra*.

c. Application of UCC Article 8, Part 5 Duties. If the licensee or registrant expressly agrees with users to treat virtual currency of which the licensee or registrant has control for the users as financial assets credited to the users' securities accounts, then the licensee or registrant has the following Part 5 Duties relevant for a virtual currency and enforceable by the users by private right of action:

- *The duty to maintain sufficient financial assets to satisfy all security entitlements to the financial assets.* UCC Section 8-504(a).

The licensee or registrant would need to maintain control of sufficient virtual currency of each type to satisfy all entitlements of the users to virtual currency of that type.

- *The duty to comply with the entitlement holder's entitlement orders to transfer or redeem a financial asset.* UCC Section 8-507.

The licensee or registrant would need to comply with a user's instructions to transfer virtual currency of which the licensee or registrant has control for the user to another person, as and when, for example, the user wishes to exchange the virtual currency for goods, services, fiat currency, or any other type of virtual currency.

- *The duty to change the entitlement holder's security entitlement to another form of holding for which the entitlement holder is eligible, or to deliver out a financial asset, at the request of the entitlement holder.* UCC Section 8-508.

The licensee or registrant would need to comply with a user's instructions to transfer virtual currency of which the licensee or registrant has control for the user to another licensee or registrant for the account of the user, or to another eligible account of the user.

The Part 5 Duties are not controversial. They should be consistent with a user's expectations of the licensee's or registrant's performance with respect to the user's virtual currency.

d. Protection of Licensee or Registrant. If licensee or registrant transfers virtual currency as instructed by the user, the licensee or registrant cannot be held liable to an adverse claimant to the virtual currency for the transfer except as otherwise specified in UCC Section 8-115, including, pursuant to UCC Section 8-115(2), if the licensee or registrant acted in collusion with the wrongdoer in violating the rights of the adverse claimant.

e. Claims of Creditors of Licensee or Registrant. When the licensee or registrant expressly agrees with users to treat virtual currency of which the licensee or registrant has control for the users as financial assets credited to the users' securities accounts, then the

virtual currency is generally not subject to the claims of creditors of the securities intermediary, to the extent necessary for the licensee or registrant to satisfy all security entitlements with respect to the virtual currency. *See* Official Comment 2.c above. Accordingly, virtual currency of which a licensee or registrant has control for a user would generally not be subject to claims of creditors of the licensee or registrant.

However, if (a) the licensee or registrant has granted to the creditor a security interest in the virtual currency, and the creditor has “control” of the virtual currency as defined in UCC Section 8-106(d), then the claim of the secured creditor has priority over the claims of the users (to the detriment of the users if the securities intermediary has not complied with its duty to maintain sufficient virtual currency, see Official Comment 4.c above). UCC Section 8-511(b). As explained in Official Comment 6, under subsection 4(a)(3)(D) of this act (unlike under Article 8 alone), a user’s consent to the licensee’s or registrant’s grant of the security interest is ineffective.

f. Choice of Law. If an express agreement to opt in to UCC Article 8 is contained in an agreement, presumably the account agreement between the licensee or registrant and the user, then, in order for a court in a Uniform Commercial Code jurisdiction to apply the substantive commercial law rules of Article 8 to the virtual currency held in the account, the law governing the account agreement must be that of a Uniform Commercial Code jurisdiction, or the agreement must provide for a Uniform Commercial Code jurisdiction to be the “securities intermediary’s jurisdiction” (UCC Sections 8-110(b), (e)(1) and (2)) and for all of the issues in Article 2(1) of the Hague Securities Convention to be governed by the law of a Uniform Commercial Code jurisdiction. Hague Securities Convention, Art. 4(1). Subsections 4(a)(1), (2) and (5) of this act ensure that, when the UCC Article 8 opt in provisions are contained in an agreement (whether the agreement is actual or deemed under subsection 4(b) of this act, see Official Comment 6), the choice-of-law rules of UCC Article 8 and, assuming that the qualifying office test is met, the Hague Securities Convention (when applicable) will point to the law of a particular Uniform Commercial Code jurisdiction so that the substantive commercial law rules of UCC Article 8 will apply. These subsections thus prevent a licensee or registrant from avoiding the commercial law rules of UCC Article 8.

Under Section 5 of this act, the licensee or registrant must maintain a qualifying office in the United States to make certain that the Article 8 protections are effective after applying the choice-of-law rules of the Hague Securities Convention.

5. Problems in Practice Addressed by the UCC Article 8 Opt-in. When the licensee or registrant expressly agrees (or, under subsection 4(b) of this act, is deemed to agree) with users to treat virtual currency over which the licensee or registrant has control for the users as financial assets credited to the users’ securities accounts, then several problems that exist under secured transactions law without giving effect to this act will be addressed. It is intended that addressing these problems will facilitate the greater availability of credit or lower its costs for a user who wishes to offer the user’s virtual-currency account and the virtual currency credited to the user’s account maintained with the licensee or registrant as collateral for a loan or other obligation and will otherwise facilitate the utility of virtual currency as a medium of exchange.

a. Security Interests. One problem concerns the method of perfection and the priority of a security interest that the user might grant in the user's virtual-currency account. Absent the licensee or registrant expressly agreeing with the user to treat virtual currency as a "financial asset" credited to the user's securities account, a user's entitlement to virtual currency maintained for the user by the licensee or registrant would be classified under UCC Article 9 as a "general intangible" pursuant to UCC Section 9-102(a)(42) (but not necessarily be "payment intangibles" under UCC Section 9-102(a)(61)). The filing of a financing statement would be the sole method for the secured party to perfect its security interest in the "general intangible," i.e., the user's virtual-currency account under UCC Section 9-310. The priority of competing security interests in the virtual-currency account would be determined in favor of the first secured party to file or perfect its security interest. UCC Section 9-322(a)(1).

By contrast, if the licensee or registrant expressly agrees with users to treat virtual currency over which the licensee or registrant has control for the users as "financial assets" credited to the users' securities accounts, a user's virtual-currency account would be classified as "investment property" under UCC Article 9. UCC Section 9-102(a)(49) defines "investment property" to include a "security entitlement" and a "securities account." The method of perfection of a security interest in the user's virtual-currency account as "investment property" would be either the filing of a financing statement or the secured party obtaining control of the investment property. UCC Sections 9-312(a) and 9-314(a). A secured party that obtains control would have priority over a secured party that perfects by filing, even if the perfection by filing was earlier in time than the perfection by obtaining control. UCC Section 9-328(a).

It is preferable as a policy matter for the perfection and priority scheme for investment property rather than general intangibles to apply to the virtual-currency account. The policy rationale is analogous to that for the perfection and priority of security interests in investment property generally. A secured party taking a security interest in investment property and relying on that collateral in extending credit should demonstrate that reliance by taking the steps to obtain control. If the secured party takes those steps, its security interest is entitled to priority over a secured party who had perfected its security interest merely by the filing of a financing statement and who, presumably by not taking the steps to obtain control, was not substantially relying on the investment property in extending credit.

A secured party that extends credit in reliance on the virtual-currency account as collateral would generally want its security interest to be senior and would generally take the necessary steps to obtain control as that term is defined in UCC Sections 8-106(d) and 9-106(a). However, absent investment property treatment of the virtual-currency account, control would not be a permitted method of perfection or a basis for having priority. The secured party would need to bargain with any other secured party who had already filed a financing statement covering general intangibles, and who presumably is not relying to any substantial extent on the virtual-currency account as collateral, to obtain a release or subordination of the other secured party's security interest. There would seem to be no policy justification for the filed secured party to be entitled to the priority benefit and negotiating leverage over the later secured party who relies on the account, merely because the filed secured party has, without that reliance, taken a general security interest in the user's "general intangibles."

For a secured party to take control of a virtual-currency account for purposes of Article 9, some new techniques may need to be developed. Unless the licensee or registrant is itself the secured party, or the virtual currency is credited to an account of the secured party at another licensee or registrant, the licensee or registrant would need to enter into a control agreement by which it agrees to follow instructions from the secured party to transfer the virtual currency without further consent by the user. *See* UCC Sections 8-106(d), (g) and 9-106(a). Such an agreement may require a mechanism for the user confidentially to inform the secured party of the user's private key, or for the secured party to have its own private key, to the virtual-currency account.

b. “Negotiability” of Virtual Currency. Another problem concerns the rights of transferees of virtual currency. If a secured party's security interest in a virtual-currency account is perfected as a general intangible, then any transfer of the virtual currency by the user out of the account will be subject to the secured party's security interest unless the secured party had authorized the transfer free of the security interest. *See* UCC Section 9-315(a)(1). This would undermine the certainty of virtual currency transactions, because there is no rule under Article 9 that otherwise cuts off a security interest in a virtual-currency account perfected as a general intangible as there is under UCC Section 9-332(b) for a transfer of funds from a deposit account. A secured party of the transferee, thinking of extending credit against the virtual currency credited to the account, would be subject to a security interest in favor of a prior transferor's secured party.

However, if the licensee or registrant expressly agrees with users to treat virtual currency over which the licensee or registrant has control for the users as financial assets credited to the users' securities accounts, then the adverse claim cut-off rule of Article 8 would apply. Under that rule, when a transferee acquires for value a “security entitlement” in the transferred virtual currency resulting from a credit of the virtual currency to the transferee's account at its licensee or registrant, the transferee will have acquired its interest in the virtual currency free of any “adverse claims” of which the transferee did not have notice. Specifically, UCC Section 8-502 provides that “[A]n action based on an adverse claim to a financial asset, whether framed in conversion, replevin, constructive trust, equitable lien, or other theory, may not be asserted against a person who acquires a security entitlement under UCC Section 8-501 for value and without notice of the adverse claim.”

An “adverse claim” is defined in UCC Section 8-102(a)(1) as “a claim that a claimant has a property interest in a financial asset and that it is a violation of the rights of the claimant” for the transferee to acquire a security entitlement to the financial asset. Notice of an adverse claim under UCC Section 8-105 means generally that the transferee either knows of the adverse claim (which means actual knowledge, *see* UCC Section 1-202(b)) or has acted with willful blindness to avoid knowing of it. Notice of an adverse claim also can arise if the transferee had a statutory or regulatory duty to investigate the existence of an adverse claim and an investigation would have revealed the adverse claim, *see* UCC Section 8-105(a)(3).

The mere fact that the transferee suspects or even knows that its transferor may have granted a security interest in the transferor's virtual-currency account at its licensee or registrant does not put the transferee on notice of an adverse claim to the virtual currency. Often, the

secured party will have authorized the transfer of the virtual currency free of the security interest. For a transferee to have notice of the adverse claim, the transferee must know, or have been willfully blind in avoiding knowing, that the acquisition by the transferee of a security entitlement to the transferred virtual currency violates the rights of the adverse claimant.

6. Additional User Protections. This section contains several other user protections based on UCC Article 8.

a. Standard of Licensee or Registrant Performance of Part 5 Duties. Article 8 provides a good deal of flexibility for the securities intermediary and the entitlement holder to agree to standards for the performance by the securities intermediary of its Part 5 Duties. Subsection 4(a)(3) of this act provides, however, that the licensee or registrant may not, through its form of agreement or otherwise, cause itself to be subject to a lower standard than if there had been no agreement at all. The subsection thereby establishes a “floor” to the standard-setting that Article 8 alone would otherwise allow. At a minimum, under this act, the licensee or registrant must act in respect of its Part 5 Duties with “due care in accordance with reasonable commercial standards,” which is the default standard under Article 8. *See* UCC Sections 8-504(c)(2), 8-505(a)(2), 8-506(2), 8-507(a)(2) and 8-508(2).

b. Security Interest Granted by Licensee or Registrant in User’s Virtual Currency. Article 8 permits a user to consent to the licensee or registrant granting a security interest in virtual currency of which the licensee or registrant has control for the user. UCC Section 8-504(b). UCC Article 9 provides to the licensee or registrant the right to grant such a security interest absent the licensee’s or registrant’s agreement with the user to the contrary. UCC Section 9-207(c)(3).

In this act, by contrast, Subsection 4(a)(3)(D) requires that the licensee or registrant affirmatively agree with the user that the licensee or registrant will not grant such a security interest. This addresses the concern that, without a user’s informed assent, a licensee’s or registrant’s standard form agreement would otherwise permit the licensee or registrant to grant a security interest, for the licensee’s or registrant’s own account, in any virtual currency of which the licensee or registrant has control for the user, or that the licensee or registrant would do so if the agreement were silent on the issue.

Subsection 4(a)(3)(D) does not prohibit (a) the user from granting a security interest to a licensee or registrant in virtual currency of which the licensee or registrant has control for the user, to secure payment either of customary amounts owing to the licensee or registrant by the user or of any credit extended by the licensee or registrant to the user, or (b) the licensee or resident from enforcing such a security interest granted by the user following the user’s default.

The subsection also does not prohibit the user from granting a security interest in the virtual currency to a third party. If such a grant is made the licensee or registrant is not obligated to assume any duties to the third party. *See, e.g.*, UCC Section 8-106(g) (securities intermediary is not obligated to enter into control agreement).

If a licensee or registrant violates the restriction in subsection 4(a)(3)(D), that violation would constitute a violation of the URVCBA, subjecting the licensee or registrant to enforcement action that the user could pursue under Section 407 of the URVCBA in addition to the user's rights under UCC Article 8 or other law. However, subsection 4(a)(3)(D) does not disturb the protections afforded to an innocent secured party or downstream "purchaser" relying on the adverse claims cut-off rules of Part 5 of Article 8 explained above.

c. Failure to Opt In. In addition, subsection 4(b) of this act provides that if, whether through inadvertence or otherwise, the licensee or registrant and the user fail to opt in to Article 8 by an actual agreement, their respective rights and obligations will be determined as if the opt in had occurred. Thus, a user is assured that the user will have the protections of Article 8 even if there is no actual agreement between the licensee or registrant and the user, or the agreement does not include the required opt in provisions.

d. No Waiver Permitted. In light of the regulatory purpose of the subsection 4(a) agreement and of the deemed subsection 4(b) agreement, any purported waiver or amendment of the requirements imposed by this section that would not have passed muster under this act in the first instance is ineffective as between the licensee or registrant and the user under subsection 4(c). The prohibition on waiver applies not only at the time of the original agreement between the licensee or registrant and the user, but also through the course of the relationship between the licensee or registrant and the user.

SECTION 5. QUALIFYING OFFICE UNDER HAGUE SECURITIES

CONVENTION.

(a) A licensee or registrant shall maintain in a state an office that complies with the second sentence of Article 4(1) of the Hague Securities Convention.

(b) The effect of this section may not be varied by agreement.

Official Comment

The Hague Securities Convention provides that the governing law of an account agreement effectively points to the law of a Uniform Commercial Code jurisdiction only if the intermediary maintains a qualifying office in any state of the United States at the time of the agreement. Hague Securities Convention, Art. 4(1).

This section accordingly requires that the licensee or registrant maintain such an office. This requirement prevents the choice-of-law provisions of the agreement between the licensee or registrant and the user that otherwise point to the law of a Uniform Commercial Code jurisdiction from failing to be effective. The qualifying office need not be located in the enacting state or in the state designated in the agreement. The test under the Hague Securities Convention requires only that the qualifying office be located in the United States. Hague Securities Convention, Art. 12(1)(b). Moreover, this section and the Hague Securities Convention require

only that the office in question be located in a jurisdiction in the United States, which need not be a Uniform Commercial Code jurisdiction, so that an office located, for example, in a U.S. territory or insular possession that has not enacted the UCC may qualify. Because many providers that may be subject to the URVCBA will be online businesses, and many will be start-up businesses, the single office in the United States requirement in the Hague Securities Convention is a sensible approach and is sufficient to preserve the applicability of Article 8.

The activities that constitute a qualifying office are minimal and may take any of a variety of forms, e.g., effecting transactions from the office, monitoring entries to virtual-currency accounts from the office, administering payments relating to virtual-currency accounts from the office, or otherwise being engaged in a regular activity of maintaining virtual-currency accounts from the office. Hague Securities Convention, Art. 4(1)(a). The test may also be met if the office is “identified by an account number, bank code, or other specific means of identification as maintaining securities accounts” in the United States. Hague Securities Convention, Art. 4(1)(b). Moreover, there is no requirement that the test apply to the virtual currency of which the licensee or registrant has control for the user, so long as the test is met for any virtual-currency accounts of which the licensee or registrant has control for any users.

Under Section 6 of this act, a failure to maintain an office in a jurisdiction in the United States is a regulatory violation of the URVCBA.

SECTION 6. EFFECT OF FAILURE TO COMPLY WITH [ACT]. Failure to comply with this [act] is a violation of the Uniform Regulation of Virtual-Currency Businesses Act.

Official Comment

This act provides more certainty for all parties on the commercial law rules for virtual currency over which the licensee or registrant has “control,” as that term is defined in the URVCBA. For this reason, it is important that URVCBA and this act be enacted by any state that seeks to provide the complex of prudential regulation and commercial-transaction certainty that the combination of both acts provides.

SECTION 7. NO INFERENCE AS TO CHARACTERIZATION UNDER OTHER STATUTE OR RULE. Treatment of virtual currency as a financial asset credited to a securities account under this [act] and Article 8 does not determine the characterization or treatment of the virtual currency under any other statute or rule.

Official Comment

This act has the limited objective of subjecting virtual-currency transactions governed by the URVCBA to the commercial law rules of UCC Article 8. It codifies the Part 5 Duties of a licensee or registrant with respect to users, and addresses the commercial law problems referred to in Official Comment 5 to Section 4 of this act.

Because of the limited purpose of this act, the treatment under this act and Article 8 of virtual currency as a financial asset credited to a securities account should not determine the characterization or treatment of the virtual currency for purposes of other laws, such as laws dealing with the regulation of securities or commodities.

SECTION 8. SUPPLEMENTARY LAW. Unless displaced by the particular provisions of this [act], the principles of law and equity supplement this [act].

SECTION 9. UNIFORMITY OF APPLICATION AND CONSTRUCTION. In applying and construing this uniform act, consideration must be given to the need to promote uniformity of the law with respect to its subject matter among states that enact it.

SECTION 10. RELATION TO ELECTRONIC SIGNATURES IN GLOBAL AND NATIONAL COMMERCE ACT. This [act] modifies, limits, or supersedes the Electronic Signatures in Global and National Commerce Act, 15 U.S.C. Section 7001, et seq., but does not modify, limit, or supersede Section 101(c) of that act, 15 U.S.C. Section 7001(c), or authorize electronic delivery of any of the notices described in Section 103(b) of that act, 15 U.S.C. Section 7003(b)).

[SECTION 11. SEVERABILITY CLAUSE. If any provision of this [act] or its application to any person or circumstance is held invalid, the invalidity does not affect other provisions or application of this [act] which can be given effect without the invalid provision or application, and to this end the provisions of this [act] are severable.]

Legislative Note: Include this section only if this state lacks a general severability statute or a decision by the highest court of this state stating a general rule of severability.

SECTION 12. REPEALS; CONFORMING AMENDMENTS.

(a)

(b)

Legislative Note: The Uniform Regulation of Virtual-Currency Businesses Act should be amended to repeal Section 502 of that act and to change references to Section 502 to references to this act. Any provision of this state's money transmission statute that may apply to virtual currency should be amended or repealed.

SECTION 13. EFFECTIVE DATE. This [act] takes effect

Legislative Note: The effective date of this act should not be before the effective date of the Uniform Regulation of Virtual-Currency Businesses Act.