The Surety & Fidelity Association of America

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December 29, 2014

Via Electronic Mail

Lonnie Christopher
Rule Coordinator
Office of Commissioner of Banks
4309 Mail Service Center
Raleigh, NC 27699-4309

Re: Proposed Rules
North Carolina Administrative Code
Subchapter F-Licensees
Money Transmitter Act

Dear Mr. Christopher:

The Surety & Fidelity Association of America ("SFAA") is a non-profit corporation whose member companies collectively write the majority of surety and fidelity bonds in the United States. SFAA is a licensed rating or advisory organization in all states and is designated by state insurance departments as a statistical agent for the reporting of fidelity and surety experience. The vast majority of bonds that secure licensing and regulatory obligations are provided by SFAA members. We have had an opportunity to review the captioned revised regulations for licensees under the Money Transmitters Act ("Act"). The revisions clarify the applicable regulations so that they pertain to virtual currency transmitters. As you know, N.C. Gen. Stat. 53-208.8 requires that licensees furnish a surety bond "to secure the faithful performance of the obligations of the licensee with respect to the receipt, handling, transmission, and payment of money or monetary value in connection with the sale and issuance of payment instruments, stored value, or transmission of money." We recommend that the regulations should clarify that the bond provides security with respect to exposures related strictly to the money transmission activity, whether traditional or virtual currency involved. The bond should not extend to the risks unique to virtual currency and cannot be quantified or underwritten.

Virtual currency presents additional risks to those presented by the transmission of traditional currency. For example, the value of virtual currency can fluctuate wildly on a daily basis. For example, between March 2013 and March 2014, the value of the virtual currency

Bitcoin fluctuated between $100 and $1200.[1] In addition, virtual currencies present other risks that are not present when dealing with currencies that are regulated by a central bank. Some of these additional risks are:

- Virtual currency is subject to minimal regulation.
- Virtual currency exchanges and e-wallets are susceptible to cyber-attacks.
- Virtual currency accounts are not insured by the Federal Deposit Insurance Corporation (FDIC), which insures bank deposits up to $250,000.
- Users in virtual currency will be highly reliant upon unregulated exchanges that may lack appropriate internal controls and may be more susceptible to fraud and theft than regulated financial institutions.
- Users will have to rely upon the strength of their own computer security systems, as well as security systems provided by third parties, to protect their e-wallets from theft.

These are not exposures contemplated in a traditional transmission transaction and they expand the surety's risk.

Further, the exposures in virtual currency transactions are difficult to quantify and identify, thereby creating ambiguities as to bond coverage. It is questionable whether the exposures noted above involve the "performance of the obligations of the licensee with respect to the receipt, handling, transmission, and payment of money or monetary value." Moreover, it could be difficult to determine a simple matter of whether a "loss" has occurred under a bond. For example, assume a money transmitter sent 10 Bitcoins from a customer's wallet to a third party. Before the transmission, the value of the Bitcoins was $100. Due to wild fluctuations in values, the value after the transmission is $30. Is there a loss under the bond? The regulations should be more specific regarding what "performance of obligations" means, specifically with respect to transactions involving virtual currency.

The scope of the surety bond obligations affects the availability of the bond. If the obligation that the surety is securing (as stated in the condition of the bond) is clear, well-defined, and capable of being underwritten, then availability should not be affected negatively. We thank you for your consideration. We would be happy to discuss our guidance further with you in order to develop a workable bond requirement that provides meaningful coverage to the Commissioner and is reasonably available in the market.

Sincerely,

Robert J. Duke

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[1] California Department of Business Oversight, "What You Should Know About Virtual Currencies" (http://www.dbo.ca.gov/Consumers/Advisories/Virtual_Currencies_0414.pdf).