CHAMBER
OF PROGRESS

August 5, 2022

Sandra Navarro
Department of Financial Protection and Innovation
2101 Arena Boulevard
Sacramento, CA 95834

Dear Ms. Navarro,

On behalf of Chamber of Progress, a tech industry association working to ensure that all Americans benefit from technological leaps, I appreciate the chance to submit comments on Crypto Asset-Related Financial Products And Services Under The California Consumer Financial Protection Law. Responses are provided below:

Regulatory Priorities

1. What steps should the DFPI take to better protect consumers from scams and frauds associated with crypto asset-related financial products and services?

The DFPI could establish a crypto-related complaint line and buyer beware website to collect data on the specific types of cryptocurrency fraud consumers are experiencing. When gathering data on fraud, the DFPI should identify the relation of cryptocurrency to the fraud– for example, is it a pump and dump scheme around a coin? Or does the cryptocurrency serve as a medium for payment in common schemes like romance scams and tech support fraud? The data collection could include key demographic information to pinpoint groups frequently targeted by these scams. The data collection will aim to identify the most common crypto-related scams, and the DFPI can publish this information online monthly. The DFPI could also publish an annual report on the crypto fraud data, listing the cryptocurrencies and decentralized finance (DeFi) products that have attempted to defraud Californians.

2. What steps should the DFPI take to improve consumer education and outreach for crypto asset-related financial products and services?

The DFPI could establish a public-private partnership with crypto industry leaders, academics and non-profit associations to develop a 'Crypto Hub' – an online website providing consumers with educational tools on cryptocurrency. To promote equity, all educational tools provided should be free and easily accessible to Californians. The DFPI could improve consumer education in underserved communities by distributing information from the Crypto Hub to local municipalities and hosting events promoting financial literacy at community centers, libraries, senior centers, churches and community colleges. To connect with digitally adept consumers, the DFPI can create a social media toolkit with informative videos and posts about cryptocurrencies and other digital assets to mitigate misinformation from nefarious sources. The DFPI could create advertisements and commercials promoting digital literacy and partner with sports teams, retail outlets and video games to connect with a variety of consumers.

Additionally, the DFPI could create an interagency task force on digital asset financial education, similar to the US Department of Treasury's Financial Literacy Education Commission (FLEC). FLEC recently formed a subgroup on digital asset financial education, which plans to develop trustworthy and educational materials to help consumers make informed decisions about digital assets. DFPI could use this information at the Federal level to initially provide materials to educate Californians.

3. What steps should the DFPI take to better ensure consumer protection in the offering and provision of crypto asset-related financial products and services?

The DFPI should establish a regulatory 'sandbox' for crypto companies with innovative financial products and services. In a sandbox, companies launch cutting-edge products and services initially with test users that have a low level of risk of losing money, and later with a larger test group that is well informed of the potential risks involved. There are a handful of states establishing innovative spaces for crypto companies to test new products on a small set of consumers without fear of enforcement from regulators and lawmakers. Governments in the US and around the world are using these sandboxes to develop a collaborative approach with companies, regulators and in some cases, consumers. The sandbox can provide the DFPI with information to develop best practices and policy recommendations for crypto regulation. With supportive regulatory oversight, companies can suggest recommendations to keep predatory practices at bay, which will benefit the CA consumer.

4. What steps should the DFPI take to better ensure investor protection in the offering and provision of crypto asset-related financial products and services?

The DFPI can ensure investor protection and promote market integrity by strengthening disclosure requirements around crypto companies issuing digital assets directly. To ensure better investor protection, the DFPI should mandate that crypto companies operating in California must explicitly say on their website that their products and services are not FDIC insured and may not be recovered in the event of a run or extreme market fluctuation. This disclosure could either be a popup on the landing page of a company's website, a notice at the top of the webpage or a checkbox acknowledging the product is not FDIC-insured, and assets may not be recovered. In the proposed regulatory sandbox model, the DFPI could conduct regular risk assessments with crypto companies to identify areas of concern and establish control measures and procedures that will protect companies and investors alike.

5. What steps should the DFPI take to better ensure financial stability in the market from risks posed in the offering and provision of crypto asset-related financial products and services?

Over the years, the crypto markets lost stability due to hacking, currency runs, and usage bans of crypto in certain countries. The 2022 market volatility was due to the collapse of an algorithmic stablecoin that was heavily invested by other crypto companies, causing runs on the currency and other decentralized finance platforms. To prevent another stablecoin collapse, DFPI should institute additional oversight on algorithmic stablecoins and limit its usage until they have been thoroughly vetted through the regulatory sandbox process.

Hackers stealing digital assets is another contributor to market instability. Since digital assets are not protected by FDIC insurance, consumers are unable to recoup their losses in the event of a breach. To ensure financial stability for California consumers, DFPI must promote innovation for crypto companies developing cybersecurity products on the blockchain, and maintain market integrity by enforcing Know Your Customer (KYC) and anti-money laundering

(AML) regulations, along with creating safeguards against hackers. These regulations will reduce the amount of users and hackers committing cybercrime, and consumers will be more comfortable using digital assets without fear of losing everything.

6. **What steps should the DFPI take to address climate risks posed in the offering and provision of crypto asset-related financial products and services?**

The DFPI should work with CalEPA to develop a study around the environmental effects of cryptocurrency mining and its potential impact on climate change. The DFPI should encourage crypto mining companies to innovate sustainably by promoting the use of renewable energy. Similar to Amazon's data centers, crypto mining has intentionally gravitated towards becoming more energy-conscious, as consumers and investors are interested in supporting companies that align with their eco-friendly values. As a result, crypto mining companies are competing with one another to be more environmentally sustainable, which causes mining to become cheaper, with cleaner energy sources.

7. How should the DFPI strive to harmonize its regulatory approach to crypto asset-related financial products and services with federal authorities?

California is looked to as a leader in the US when generating policy, and it should lead in developing a fair and unbiased approach to crypto regulation. The DFPI should break away from the SEC's approach of regulation by enforcement and work closely with industry to create a regulatory framework that stimulates competition and protects consumers. Through the sandbox and proposed CALicense introduced in CA AB 2269, California has a prime opportunity to lead and provide federal authorities with valuable information and data to help them develop the appropriate framework for the industry.

8. In developing a comprehensive regulatory approach to crypto asset-related financial products and services, how should the DFPI work with other state financial regulators to promote a common approach that increases the reach of DFPI's consumer protection efforts and reduces unnecessary burdens, if any, on companies seeking to operate nationwide?

To gather information from other state financial regulators, the DFPI should create a roundtable with top regulators identifying upcoming risks and challenges to the crypto ecosystem. In 2018, the North American Securities Administrators Association (NASAA) organized a group of regulators from different states across the country that researched initial coin offerings (ICOs) and cryptocurrency investment products in violation of individual states' laws. DFPI could do something similar with a group of states to identify bad actors in the crypto industry and coordinate enforcement actions. Finally, states are introducing money transmitter licensing or depository institution charters as a means to regulate crypto companies. This piecemeal approach is a stopgap now until the Federal government creates a nation-wide framework. California should lead by creating a universal digital asset license application through a year-long working group process with states invited to participate. The DFPI should develop a reciprocity agreement with these other states, which gives companies portability for conducting business in other jurisdictions with similar compliance requirements to California.

9. **How can the DFPI make California the most desirable home state for responsible companies when developing guidance and, as appropriate, regulatory clarity and supervision of persons involved in the offering and provision of crypto asset-related financial products and services in California?**

Feasible and reasonable regulations are needed to keep and attract competitive companies in the state, and robust compliance procedures will weed out bad actors. The DFPI can establish California as a regulatory leader by regularly working with industry to understand the crypto ecosystem, its challenges and opportunities for innovation. By creating an advisory council with industry leaders, the DFPI can hold regular meetings to learn more about the trajectory of the industry. The DFPI could also establish a Blockchain Chamber of Commerce for all crypto companies operating in California. This will bring a fragmented industry together and allow the DFPI to receive additional feedback from industry on regulatory proposals. Through California-based industry groups, the DFPI could also gather information and recommend programs that reward California-based crypto companies for creating environmentally conscious innovative products and services. By only rewarding California companies, this could inspire crypto companies to establish headquarters in the state.

10. How should the DFPI ensure that California values of inclusive innovation and equity-focused consumer protection are core components of crypto asset-related financial products and services as it develops guidance and, as appropriate, regulatory clarity supervision of those persons involved in the offering and provision of crypto asset- related financial products and services in California?

Financial equity begins with consumer education. The 2022 Black Investor Survey showed that Black investors are more than twice as likely to trust social media as an information source on investing than White investors. Consumers are increasingly being exposed to scams and misinformation littered throughout social media platforms, and the DFPI must share factual information to potential investors of color through multiple outreach campaigns. The DFPI sharing information on social media and through other forums will provide consumers of color with a trusted source, and a forum for questions and comments. The DFPI could create a subdivision for Financial Inclusion and Equity that collects cryptocurrency usage data in un- and under-banked populations, provides educational outreach in communities of color and advocates for the needs of marginalized populations.

Sincerely,

Janay Eyo
Director, Financial Policy
Chamber of Progress