

SUPREME COURT OF THE STATE OF NEW YORK

COUNTY OF NEW YORK : CIVIL DIV. : PART 34

-----X
THEO CHINO,

Petitioner, :

- against - : Index No.
: 101880/15

DEPARTMENT OF FINANCIAL SERVICES,
ANTHONY J. ALBANESE, in his Official
Capacity as the Acting Superintendent,

Respondent. :

-----X MOTION

80 Centre Street
New York, New York
October 10, 2017

B E F O R E :

HON. CARMEN VICTORIA ST. GEORGE,
Justice

A P P E A R A N C E S :

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SENIOR COURT REPORTER

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4 THE COURT: Good morning.

5 Off the record.

6 (Discussion off the record.)

7 THE COURT: Appearances for the record.

8 MR. CIRIC: Pierre Ciric, counsel for plaintiff,
9 Theo Chino, Your Honor.

THE COURT: What's your last name?

11 MR. CIRIC: I'm sorry. Cirim, C-I-R-I-C. First
12 name, Pierre.

13 MS. ROACH: Mackenzie Roach.

14 THE COURT: For respondent?

15 MR. CONLEY: Jonathan Conley, assistant attorney
16 general with the New York State Attorney General's Office,
17 for respondent, New York State Department of Financial
18 Services.

19 MS. WRIGHT: Alissa Wright, also with the Attorney
20 General's office for respondent.

21 THE COURT: The Court has before it Sequence One,
22 Article 78 in declaratory judgment petition with cross
23 motion to dismiss by the New York State Department of
24 Financial Services, et al.

25 In addition to that, there was an amended
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1 complaint and Article 78 petition and the op -- for
2 failure to state a claim. That's Sequence 1.

3 Sequence 3 is petitioner's cross motion for
4 limited discovery; pursuant to CPLR 408 to hold the
5 defendant's cross motion in abeyance, and, in the
6 alternative, for leave to serve a sur reply.

7 Have the parties had any meaningful resolution
8 or discussions in an attempt to resolve this matter?

9 MR. CIRIC: In terms of the discovery we've made
10 some attempts. About the discovery, yes, we made attempts,
11 yes.

12 THE COURT: Mr. Ciric, I'll hear you on the
13 petition.

14 MR. CIRIC: Yes.

15 So the first issue I wanted to clarify in terms
16 of the motion to dismiss was the standing question to
17 ensure that all of the questions of the Court can be
18 addressed.

19 At this juncture the standard is that the Court
20 must accept all the fact as alleged in the complaint
21 along with all of the affidavits that were supplied.

22 THE COURT: Okay, hold on a second.

23 Can you shut that air off?

24 COURT OFFICER: In the back?

25 THE COURT: Shut that air conditioner off
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1 (indicating). I can't hear you. And you need to look at
2 me when you're talking to me so that I can understand what
3 you're saying.

4 MR. CIRIC: Okay. I'm sorry.

5 THE COURT: Okay.

6 It is your motion; correct? Respondent's
7 motion?

8 MR. CONLEY: The cross motion --

9 THE COURT: The cross motion.

10 MR. CONLEY: -- to dismiss. Yes, Your Honor.

11 THE COURT: All right. So speak slowly. The
12 reporter moved up so that he can get what you're saying.

13 MR. CIRIC: Sorry. I didn't mean to scream.

14 THE COURT: Go ahead.

15 MR. CIRIC: Okay, so on the standing, the standard
16 is for the Court to look at the face value of the complaint
17 along with all of the affidavits that are submitted.

18 So from the -- on the face of the affidavits
19 we've demonstrated that the plaintiff has standing --

20 THE COURT: Petitioner?

21 MR. CIRIC: The petitioner, I'm sorry. Has
22 standing because he launched a business where he would use
23 Bitcoins in order to allow a bodega to exchange Bitcoins
24 against phonecards or any other items sold by bodegas. He
25 set up computer systems, he set up agreements with bodegas,

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1 he basically made all of the appropriate investments in
2 order to launch his business, which was in fact starting at
3 the time of the Bit license being promulgated in the summer
4 of 2015.

5 He -- before the -- right after the a Bit
6 license was promulgated petitioner filed or submitted an
7 application to DFS in order to obtain a Bit license. The
8 key reason why the petitioner knows that he's subject to
9 the Bit license is that in order for a customer of the
10 bodega to use Bitcoin to make a payment he has to use
11 what's called the QR~Code that was provided to the
12 bodegas. And the QR~Code was not the bodega's QR Code
13 but my client's QR~Code. So that establishes the fact
14 that he was controlling the numbers that make up the
15 Bitcoin algorithm.

16 Because he controlled those numbers he knew that
17 he was subject to the Bit license, which is why he made a
18 submission to or replied to the Bit -- applied to the Bit
19 license.

20 Knowing and realizing the financial --
21 significant financial impact of attempting to comply with
22 the Bit license, within the four-month deadline following
23 the promulgation of the regulation, my client filed
24 pro se a petition -- an initial petition challenging the
25 Bit license. That was in October 2015.

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1 In January 2016 the response from DFS comes back
2 and says, "We don't have enough information to evaluate
3 your application." At that moment my client makes the
4 choice that continuing the application process is futile,
5 A, because the costs were astronomical, B, because he had
6 already had filed a challenge in October and therefore
7 did not pursue the -- the application process and
8 continued to -- to follow all the -- all the steps to
9 continue the challenge.

10 At the same time, in the beginning of 2016 he
11 stopped the business because he knew he was going to be
12 subject to the Bit license and that he just could not
13 comply with --

14 THE COURT: '17. 2017.

15 MR. CIRIC: I'm sorry. No, no, January 2016.

16 THE COURT: Okay.

17 MR. CIRIC: Because the promulgation was in
18 August 2015.

19 THE COURT: Then his license that he filed for was
20 in October --

21 MR. CIRIC: He filed -- he filed in the -- he
22 submits the submission for the Bit license in the summer.

23 THE COURT: October -- you just said October 2016,
24 if I heard you correctly.

25 MR. CIRIC: He files the challenge to the Bit
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1 license in October 2015.

2 THE COURT: Okay.

3 MR. CIRIC: I believe it's the 26th, which was
4 about a week before the four-month expiration. And he gets
5 back the answer from DFS in January of 2016.

6 THE COURT: '17.

7 MR. CIRIC: January 2016, Your Honor.

8 THE COURT: Okay.

9 MR. CIRIC: At that time he just stops the
10 business. So -- and this -- and the back and forth in
11 terms of the challenge happens at that time from
12 October 2015 to today.

13 So, from a standing perspective, we supplied all
14 the papers establishing -- all the evidence establishing
15 that, A, he had the business in place, B, he was the one
16 controlling the Bitcoin -- what's called the Bitcoin key
17 to simplify the technical jargon, and therefore he knew
18 he was subject to the Bit license.

19 So, from the record, either if you look at just
20 his affidavit that establishes all of the facts, and also
21 we've augmented the affidavit from the petitioner with
22 additional evidence, including the agreements with the
23 bodegas, including an example of a transaction that went
24 through the system and the picture of the QR code that's
25 being used in the bodegas.

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1 So we have -- you know, normally the affidavit
2 should suffice, but we've augmented the affidavit with
3 more evidence that explains it, because it's not a
4 straight forward technology obviously as to all of the
5 facts that support standing.

6 Those facts have not been countered or
7 conflicted or opposed by the government with counter
8 facts. The only thing that the government has said is,
9 "Well, that's not sufficient to support standing because,
10 you know, you could have done something else or your
11 business could have failed for other reasons."

12 No, the affidavit states, "I stopped the
13 business because I couldn't comply with the Bit license."

14 And, normally, at this stage of a motion to
15 dismiss, that should suffice.

16 THE COURT: I'll hear you.

17 MR. CONLEY: As opposing counsel has noted, as the
18 petitioner is bringing this hybrid Article 78 proceeding
19 and challenging the validity of a regulation that was
20 promulgated by the New York State Department of Financial
21 Services in the summer of 2015 which regulates certain
22 business activity involving virtual currencies. We have
23 cross moved to dismiss that petition on three main grounds.

24 All of the petitioner's claims fail for three
25 reasons:

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1 First, the petitioner does not have standing to
2 bring this litigation because he's not alleged any
3 nonspeculative facts demonstrating that the regulation
4 has caused him a concrete injury of fact.

5 Second, the Department of Financial Services
6 acted within the scope of its regulatory authority in --
7 under the Financial Services Law when it promulgated the
8 challenged regulation in the summer of 2015, because the
9 legislature expressly conferred upon the Department the
10 authority to regulate new financial products and services
11 as well as the providers of those products and services.

12 And, third, the petitioner has failed to meet
13 his heavy burden of showing that the regulation is
14 unreasonable and unsupported by any evidence.

15 Opposing counsel was discussing the issue of
16 standing. The petitioner's do not have standing in this
17 proceeding for a simple reason: Nothing in -- in the
18 petition demonstrates that the regulation has harmed or
19 is likely to harm the petitioner. The petitioner alleges
20 that he is the owner of a business called Chino, Limited.
21 At the time the regulation -- after the regulation was
22 promulgated the petitioner submitted an application with
23 the Department for a license to engage in virtual
24 currency business activity. At the time this license was
25 pending the petitioner commenced this litigation.

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1 The -- In January of 2016 the Department of
2 Financial Services notified the petitioner by letter that
3 because of the exceptionally limited amount of
4 information it had been provided in the application that
5 they could not process it without more, which could not
6 have come -- could not have been a surprise to the
7 petitioner because there was literally no information in
8 the application about Chino, Limited, the proposed
9 business activity of Chino, Limited. The application is
10 mainly filled with, "I will not disclose" and "Not
11 applicable." And at the time that he received this
12 letter notifying him that there was not enough
13 information to process the application he did not follow
14 up with the Department, he did not provide the Department
15 more information, he did not choose to get clarification
16 about the letter or to submit an application on behalf of
17 the other business that he alleges owning. Instead, at
18 that time he shut down the business and alleges that the
19 resulting financial losses constitute an injury in fact
20 that should confer standing. But that is not enough
21 to -- for standing under New York law. Because he closed
22 the business and the resulting financial losses of that
23 were the petitioner's decision. The Department never
24 told the -- denied the petitioner a license and never
25 told him to close down his businesses. Instead, the

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1 petitioner is trying to get standing based on speculation
2 of how the regulation might have impacted his business
3 down the road. And that is not sufficient to confer
4 standing. That's a type of -- broad nondescript
5 allegations of anticipatory harm is not enough to
6 establish an injury in fact, and for that reason the
7 petitioner doesn't have standing here.

8 THE COURT: Okay.

9 The petitioner only addressed one of the three
10 points that you've raised. I didn't hear anything from
11 the petitioner regarding the scope of the
12 superintendent's abilities to regulate this financial
13 product and services, nor did I hear anything regarding
14 the unreasonable or unsupported nature of this by any
15 evidence or any argument regarding arbitrary and
16 capricious. I have your papers on it and I'm going to
17 give you an opportunity.

18 I have a question for the respondent: In the
19 letter or in the notification in January 2016 apparently
20 letting the petitioner know that you do not have enough
21 information provided to you to confer upon him a license,
22 is the Department not in effect essentially denying him a
23 license at that point?

24 MR. CONLEY: No, Your Honor. If -- The letter
25 explained that there -- due to the exceptionally limited
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1 amount of information they were not able to process the
2 application to ascertain whether his business even needed a
3 license, whether he was engaging in activity that required
4 a license, and, so, without more the Department could not
5 come to a decision one way or the other. And the letter
6 makes that abundantly clear.

7 The application and the letter both annexed to
8 that affidavit of Mr. Chino, I believe as Exhibits 7
9 and 9, somewhere in that range, the -- it makes it, one,
10 exceptionally clear why the Department could not have
11 come to a determination about this business; and, two,
12 that it was not -- it says explicitly that it's not
13 making a decision about the license one way or the other,
14 just it needs -- there needs to be more information about
15 what type of virtual currency business activity the
16 applicant sees the business potentially engaging in, the
17 proposed volume of business. There's just a litany of
18 information lacking.

19 THE COURT: Is this type of letter a form letter
20 of sorts that's sent to other people in similar
21 circumstances or was this a letter created specifically for
22 Bitcoin for first time ever written?

23 MR. CONLEY: This letter was written directly to
24 Mr. Chino regarding his application. The Department takes
25 each application letter it receives for a license for
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1 virtual currency business activity on a case-by-case basis.
2 And it -- because there was no information to really go off
3 of, really, except for the address to send the letter to,
4 they were addressing it -- it was not a form letter that
5 was sent to -- that is sent to all applicants.

6 THE COURT: Okay.

7 Let me hear you, petitioner, regarding the
8 respondent's contention first with respect to their point
9 that, number one, your client did nothing to attempt to
10 resolve the issue, which was the Department's concern was
11 that they couldn't make a decision whether or not you
12 even needed a license because your client did not produce
13 enough information and they're saying that your client
14 did nothing to follow up on that.

15 And, secondly, let me hear your response to
16 their position that -- and the case law that they've
17 cited in New York that anticipatory harm is not going to
18 qualify you in this --

19 MR. CIRIC: Okay. So --

20 THE COURT: -- to establish your injury in fact.

21 MR. CIRIC: Thank you, Your Honor.

22 Okay, so on the client that did nothing part,
23 because this is a facial challenge and not an as applied
24 challenge, the client -- my client -- the client started
25 pro se. We came in the case, in fact, in late 2016. But

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1 we believe that the client is still justified in what he
2 did because there is no -- this is not a situation where
3 there is an administrative exhaustion requirement.
4 That's not in the statute, that's not in the writing. So
5 the question is if he actually suffered injury in fact,
6 which is, in fact, supported by facts in the complaint.
7 I mean, you cannot do more -- you know, this is not
8 speculation to have distributed QR codes to bodegas in
9 order to initiate processing. This is not speculative,
10 this is --

11 THE COURT: He closed down his business, though,
12 without completing the application.

13 MR. CIRIC: Yes, right.

14 THE COURT: And their position is, "You could have
15 come to us, you could have asked us questions, you could
16 have followed up on the content of the letter, you could
17 have I picked up the phone and spoken to somebody and said
18 'Hey, I started this business, I have a lot invested in it,
19 I project that it's going to yield profit in the future.
20 What is it that you need, Department, from me, so that I
21 can fulfill my obligations and comply?'"

22 MR. CIRIC: Okay. So first part to this is the --
23 for the petitioner the question was not "How much stack of
24 information do I need to supply." On the face of the
25 regulation and the fact that dozens of businesses left

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1 New York after the regulation was promulgated, the -- my
2 client was a small business owner, knew on the face of the
3 regulation that the cost to comply was prohibitive. It's
4 not just the \$5,000 to initiate or to pay as a filing fee,
5 it's also all of the requirements involving computer
6 supports, cyber security and et cetera, that --

7 THE COURT: And what? What's the point? The
8 superintendent -- the Department of Financial Services is
9 who we entrust to come up with these regulations. They are
10 the ones with the expertise, the exceeded knowledge to be
11 able to come up with whatever they have as regulations for
12 people so people don't just, you know, come out of the
13 blue, start up companies and think that they don't have to
14 face any regulations.

15 MR. CIRIC: Right. Okay.

16 So, on the first part, the -- on the nonresponse
17 standpoint, the case that drives this is Police
18 Benevolent, which is --

19 THE COURT: Police Benevolent?

20 MR. CIRIC: Association of New York State
21 Troopers, 29 A.D.3d 68. Under that case the threat of the
22 police officers to be arrested because of mis-compliance on
23 some other prior facts was sufficient to confer standing;
24 they didn't need going to jail in order for the standing to
25 be recognized by the Court. You don't need to -- if the

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1 harm is very likely but you're not in the jail yet, that
2 suffices to confer standing.

3 THE COURT: That is what you believe the standard
4 is, "Very likely"? That's your belief?

5 MR. CIRIC: Okay, he's got the injury --

6 THE COURT: Give me a case that says that.

7 MR. CIRIC: Okay.

8 THE COURT: Give me a First Department or a Court
9 of Appeals case that says that the standard of law is "Very
10 likely," if you are very likely to suffer a harm that
11 suffices for the requirement.

12 MR. CIRIC: Okay. Police Benevolent is Third
13 Department, Your Honor. So that -- that's -- there's
14 another case, which is Dairy--- which is Dairylee
15 Cooperative.

16 THE COURT: "Theory"? T-H-E-O-R-Y?

17 MR. CIRIC: Dairylee, Incorporated, 38 NY2d 6, the
18 year is 1975, Court of Appeals.

19 So this is zone of interest case that says a
20 competitor that is not directly impacted by the
21 regulation but suffers from this regulation imposed by an
22 agency that imposed certain -- granted, in fact, certain
23 licensing to milk dealers has standing.

24 So there is case law that says -- okay, our
25 theory is the injury has already occurred, vis-a-vis the
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1 client, vis-a-vis my client because, A, the business was
2 there. It's not like he had a pipe dream in a garage. I
3 mean, his business was launched, going, number one.

4 Number two, he knew, and on the face of the
5 affidavit he says, "I know that I'm subject to the Bit
6 license, because under the technology I own the key of
7 Bitcoin once the customer triggers the transaction." So
8 he had to go to a Bit license.

9 Then you apply Police Benevolent. And Police
10 Benevolent says he can go -- he's subject to the police
11 power of the government. I don't know what you plan to
12 do to people that did not comply, but he is subject to
13 the police power of the government because the government
14 said, "If you're not licensed you cannot run a Bitcoin
15 business."

16 So from the moment that the -- from the moment
17 that the Bit license was promulgated he understood,
18 vis-a-vis the cost of compliance, that it was impossible
19 for him to face, that either he had to shut down or --
20 well, that was his only option. I mean, what am I going
21 to do, spend tens of thousands of dollars when I -- the
22 volume of business is not going to justify it?

23 So our position is he had standing at the time
24 he filed the challenge in October 2015 because on the
25 face of the affidavit he's -- You know, my client is not,

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1 you know, the guy around the street, he has expertise in
2 Bitcoin, he's a programmer, if he tells his attorney, "I
3 was subject to the Bit license because I own the Bitcoin
4 numbers once they're transacted from the customer to me
5 in order for them to settle the transactions with the
6 bodega," that's -- that's at face value what I'm -- what
7 I'm believing. So, from that standpoint, we have the
8 evidence in front of the Court to establish standing.

9 The Police Benevolent case explains why he
10 doesn't have to, you know, go through all of the hoops,
11 because he already filed a challenge in October 2015, so
12 at that point there is no administrative exhaustion
13 requirement in this. He didn't have to wait for a
14 determination at some point in time because it's a facial
15 challenge as to the -- the fact that my client claims
16 that the government does not have the expertise and does
17 not have the power under the Financial Services Law to
18 actually regulate the coin.

19 THE COURT: What is the basis of that statement --

20 MR. CIRIC: Okay.

21 THE COURT: -- that you just made?

22 MR. CIRIC: Yes.

23 THE COURT: Do you not agree that Bitcoin is a
24 financial product? Yes or no?

25 MR. CIRIC: Okay. Okay. Our theory from the
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beginning of the first paper to the last page is that
Bitcoin is not a financial product or service under the
statutory framework passed in 2011. Yes.

THE COURT: Is Bitcoin a financial product? Yes
or no?

MR. CIRIC: No. Absolutely not.

During the first piece of evidence during the
hearing that was organized by DFS to -- as a prelude to
promulgating the regulation, evidence was entered in the
record as to whether Bitcoin should be regulated, why and
how. The only entry in the record -- written entry in
the record is from a professor at Boston University
called Mr. Williams...

I forgot his first name. Mr. Williams. It's in
the record.

...that essentially writes down black and white,
and he's the only one who writes something down, that
says this is not a currency, this is not money, this is
basically a commodity because of its highly volatile
price, it does not have characteristics of something that
has -- that holds a store value, so this thing is
basically no different than gold or no different than
oranges to speculate upon."

So, from that standpoint, the first evidence is
that during that hearing the only thing on the record is

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1 something that says it's not a financial product or
2 service. So right here and there that's the first item.

3 There is all sorts of other decisions around the
4 country and authority that is in the record that
5 establishes that other states and other courts agree with
6 that finding. Texas, Kansas, the -- two states. Okay?

7 THE COURT: This is New York.

8 MR. CIRIC: I understand.

9 THE COURT: That's the only relevant thing.

10 MR. CIRIC: I understand, Your Honor.

11 THE COURT: Okay.

12 MR. CIRIC: Another court in Florida decided the
13 same thing.

14 So there is no authority in -- or no -- there is
15 a lot of debate, obviously, these days as to what Bitcoin
16 is, what its characteristics is, so the fact that there
17 is uncertainty as to what it is does not confer
18 automatically authority into an agency that actually
19 wants to regulate Bitcoin.

20 In fact, the examples of the other states, from
21 the perspective that they can be admitted, is the fact
22 that other states have introduced legislation and not
23 regulation in order to regulate Bitcoin. So --

24 THE COURT: Backtrack a second for me to the whole
25 premise. Your client Chino's reaching out to these
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1 bodegas.

2 MR. CIRIC: Yes.

3 THE COURT: For what?

4 MR. CIRIC: Okay.

5 So he starts, what he wants to do is encourage
6 the user of Bitcoin at the retail level. So he starts by
7 trying to develop commercial relationships with the
8 bodegas. In order to do this he says, "I'm going to
9 first enter a contract with you to distribute
10 phonecards." You know, the old phone cards where you --

11 THE COURT: Yes.

12 MR. CIRIC: Okay.

13 So he starts with that in order to establish
14 stable customer relationships with the bodegas.

15 THE COURT: Okay. Stop there.

16 MR. CIRIC: Yes.

17 THE COURT: The whole point is to encourage
18 Bitcoin at a retail level; correct?

19 MR. CIRIC: Yes, yes.

20 THE COURT: Okay.

21 And he was going to do this through the use of
22 these phonecards --

23 MR. CIRIC: Yes.

24 THE COURT: -- correct? Okay.

25 How does that mean that Bitcoin does not hold
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1 store value?

2 MR. CIRIC: Okay. So the calling card thing or
3 the phone card thing is not within -- it's not key to the
4 actual transaction. The only thing that the calling card
5 was --

6 THE COURT: It's value, sir. It's value. You're
7 the one that stood up on this record and said that, you
8 know, part of the reason that there is this debate about
9 whether or not Bitcoin is a financial product and your
10 position from inception, from start to finish to today, is
11 that it is not a financial product, that, you know, has to
12 be equated to money. And your specific words that you used
13 on the record here before this Court was that it does not
14 hold store value.

15 MR. CIRIC: Right.

16 THE COURT: I'm trying to make sense of that
17 statement in relation to what active measures your client
18 actually took to reach out to these bodegas for the purpose
19 of encouraging them to gain retail level with respect to
20 these phone cards. That was the in that he used.

21 MR. CIRIC: Right.

22 So, number one, the calling card is not used to
23 trigger a Bitcoin transaction. The calling card -- I'm
24 sorry, phonecard is only used to initiate some
25 relationship with the bodegas. Once that relationship --

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1 THE COURT: How is that not value?

2 MR. CIRIC: Because that's not where the Bitcoin
3 transaction applies. The Bitcoin transaction is for the
4 client to come in and then pay for -- for the customer, the
5 end user customer to come in and pay for -- for everything
6 he wants. Whether it's with a calling card or whether it's
7 a gallon of milk or whether it's a piece of bread. So he's
8 going to present all that he purchases to the bodega and
9 pay with Bitcoin.

10 THE COURT: How is that not value?

11 MR. CIRIC: That's -- that's a bartering unit,
12 Your Honor. That's not -- that's value, but that's not
13 sufficient to make it money, number one. And, number two,
14 that is not --

15 THE COURT: Says who? Says you? Says --

16 MR. CIRIC: Says the statute, Your Honor.

17 THE COURT: Where?

18 MR. CIRIC: Section --

19 THE COURT: Pull that section of the statute --

20 MR. CIRIC: Sure. Absolutely.

21 THE COURT: -- or any case law which supports your
22 position.

23 (Brief pause.)

24 (Mr. Ciric handing to the Court and defense
25 counsel.)

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1 MR. CIRIC: Okay, so, number one, is the speech
2 from --

3 THE COURT: You're giving me a speech as
4 authority? You're kidding, right?

5 MR. CIRIC: No, no, no. I'm... Let me just
6 switch you to the definition financial product or service.
7 It's the fourth page. Page Number 4.

8 THE COURT: Page 4 of -- I don't have a Page 4.
9 My starts with Page 5 of 219 on the top right hand corner.

10 MR. CIRIC: I'm sorry, it's the definition which
11 is the fourth physical page of the package.

12 Those are the definitions from the Financial
13 Services Bureau, Your Honor. It says a financial product
14 or service is -- essentially under 2A, either -- the
15 first part of A, "Any financial product or financial
16 service offered or provided by any person that's already
17 regulated by the banking law or the insurance law."

18 So that's Part 1. Okay? That's not here what
19 the statutory authority is, because in 2011 Bitcoin did
20 not -- was not already regulated by insurance law or
21 banking law. So it's the second part, which is --

22 THE COURT: That's not what it says. You are
23 misreading what it says. "Any financial product or
24 financial service offered or provided by any person
25 regulated or required to be regulated."

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1 MR. CIRIC: Right. Okay. So you either fall
2 under that first bucket or the second bucket. But in order
3 for that to happen you must have characteristics of a
4 financial product or service. And the question is -- the
5 fact that, Your Honor, at the second page of the packet you
6 have -- which actually is the introduction or the
7 legislative findings from the statute -- from the
8 legislation that was passed in 2011, it said the
9 regulation -- the Section F, if Your Honor -- on the second
10 page of the package. No, no, no, I'm sorry. Right. Okay.
11 So turn to the second page. Right. And I think it's
12 yellow.

13 It says that in the legislative findings it's to
14 provide for the regulation of new financial service or
15 products. Well, that's an undefined term, Your Honor.
16 It's basically not a definition of a financial product or
17 service. Financial product or service is defined and is
18 defined in a limited fashion. So under -- essentially --

19 THE COURT: Look at your under your Page 4
20 Definition 2B, "Financial Products or Service."

21 MR. CIRIC: Right. It's defined limitedly because
22 "Financial Product or Service" essentially will not be a
23 series of things, which is essentially credit to consumers.
24 But the key is when the statute was passed and "Financial
25 Product or Service" was -- was defined it was, A, defined

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1 in a limited fashion, and, number two, there was an
2 exception also for either something that is regulated under
3 the exclusive jurisdiction of a federal agency or something
4 that's preempted by federal law. Our theory is it's also
5 preempted by federal law because only the consumer -- the
6 CPB, the Consumer Protection Bureau, has authority to
7 define the terms.

8 THE COURT: Okay. Let's --

9 MR. CIRIC: If it's not regulated by another
10 agency, which is one of the other exceptions in the
11 statute.

12 THE COURT: Let's move on --

13 MR. CIRIC: Yes.

14 THE COURT: -- to the position that they have
15 acted within the scope of regulating new financial products
16 and services.

17 MR. CIRIC: I'm sorry, Your Honor, I'm --

18 THE COURT: Your adversary's position was that
19 they're opposing on three grounds: One, that you don't
20 have standing; two, that you acted within the scope of
21 regulating this new financial product; and, three, that you
22 have failed to meet the -- that high standard of
23 unreasonable and unsupported by any evidence.

24 MR. CIRIC: Okay.

25 So if you take aside for a moment the
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1 statutory --

2 THE COURT: The standing issue.

3 MR. CIRIC: The standing issue and the statutory
4 issue, the regulation is unreasonable for a number of
5 reasons. First is the compliance costs are enormous.
6 There's no provisions for a small business -- there is
7 nothing that allows a small business to --

8 THE COURT: Where do you have grounds to suggest
9 that that is unreasonable and unsupported?

10 MR. CIRIC: There was, in fact, discussion --

11 THE COURT: Where is -- Is there a financial
12 number that you lean on? In other words, once it passes X
13 dollars it becomes unreasonable?

14 MR. CIRIC: Okay. There was, in fact, after the
15 hearing in 2014 that DFS organized in order to talk about
16 Bitcoin there was, in fact, discussions about accommodating
17 some kind of small business waiver. And, in fact, there
18 were discussions as to what the thresholds will be. So it
19 was an issue that was in the record at the time that was
20 unresolved. So it's not -- I mean, the regulators were
21 aware that there was this issue of, you know, if Goldman
22 Sacks is running a Bitcoin exchange it's one thing, but if
23 a whole bunch of other small business owners are not going
24 to be able to necessarily comply with it. So this is part
25 of the record that the defendants or the government

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1 actually was -- had created.

2 So that was your first question. What was
3 your -- I'm sorry, I forgot your second question. Oh,
4 the -- right, okay, arbitrary and capricious.

5 So that's the first issue. The second issue is
6 besides the compliant costs, that it's essentially one
7 size fits all when it deals with record--- recordkeeping
8 requirements, money laundering requirements, along with
9 all of the reporting requirements. There is in the
10 record a recognition by the regulator that the regulator
11 created requirements that were above and beyond the
12 requirements for existing financial institutions and
13 money transmitters. It's in the record along the lines
14 of things such as longer record retaining periods, a --
15 systematic reporting of SARs, which is the suspicious
16 activity reports, under any circumstance when money
17 transmitters only provided for situations where they
18 actually have suspicions. And the third example that was
19 in the record was, um, something that will -- there are
20 requirements above and beyond what's being done on money
21 transmitters, which, in fact, was recognized and
22 acknowledged by the -- by the regulators.

23 Oh, capital requirements as well. The capital
24 requirements piece is essentially a provision that says
25 whatever the regulator is going to decide. When you deal

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1 with capital requirements on financial institutions
2 either you set them -- you have to quantify them. So you
3 basically are saying as a percent of assets for a bank,
4 or, when you're dealing with a money transmitter business
5 you deal with -- you express them in the form of X amount
6 of dollars in reserves or X amount of -- you know,
7 \$50,000 of cash set up in a line of credit.

8 So they're quantifiable in order for the
9 business owner to know what to shoot for. Here the
10 capital requirements is whatever the regulator is going
11 to say.

12 THE COURT: I'll hear you. Any reply?

13 MR. CONLEY: Yes, Your Honor.

14 Just quickly, to go back to the standing issue.
15 The opposing counsel argues that this is a facial
16 challenge. And while the petitioner does attempt to
17 bring a facial challenge to this regulation there is
18 still a requirement that he himself has been injured by
19 the regulation. And it's an injury in fact, it's not an
20 injury based on hypotheticals.

21 The New York State Court of Appeals has defined
22 an injury in fact to mean that the plaintiff will
23 actually be harmed by the administrative action.

24 The plaintiff is basing -- the petitioner is
25 basing his standing argument on a self-professed

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1 expertise in the field of virtual currencies, but
2 speculation on how a law is -- or a regulation may or may
3 not be enforced in the future is far too attenuated to
4 confer standing to someone to challenge your regulation.

5 Shifting to --

6 THE COURT: I don't think he said that. He's
7 basing his challenge that he was harmed -- well, obviously
8 he gives these cases that he cites to, but he says he
9 basically had to shut down the business and he incurred
10 losses as a result of that. How are those losses not
11 injuries in fact to that particular petitioner?

12 MR. CONLEY: Your Honor, they may be an injury to
13 the particular petitioner, but they are not connected in
14 any way to the actual regulation. It's based on the
15 petitioner's understanding of how the regulation might have
16 impacted his business in the future. The Department never
17 advised him to shut down his business. That was the
18 petitioner's decision based on his understanding of what
19 could potentially happen under the regulation in the
20 future. And that -- that type of speculation is -- is not
21 enough to establish that an administrative act has actually
22 caused harm that would be considered an injury in fact.

23 THE COURT: So it's the Department's position that
24 the petitioner would have had to have waited for the
25 Department to specifically say, "Shut down your business,

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1 you're not getting a license"?

2 MR. CONLEY: The -- the petitioner would have
3 needed to have incurred an injury because of the
4 regulation. Whether that be that he was denied an
5 application or that he was granted an application but felt
6 that the compliance costs were too high and the resulting
7 financial losses were an injury, to then challenge the
8 aspects of the regulation he objected to. But what he --
9 or -- yes, that the Department in some way compelled him to
10 shut down the business.

11 THE COURT: So what you're saying on behalf of the
12 respondent is that there would have had to be an
13 affirmative act on behalf of the Department to trigger his
14 standing. In other words, the Department would have had to
15 flatout deny him the license or grant him the license but
16 make it feasibly impossible for him to continue. And,
17 therefore, by that act on behalf of the Department it would
18 have triggered his ability to then proceed forward.

19 MR. CONLEY: Not -- not exactly, Your Honor.
20 The -- the Department's position is that he -- the
21 petitioner is trying to get standing in this case with
22 these facts by litigating a decision that had never been
23 rendered in the first place.

24 THE COURT: Well, because he's trying to say,
25 "Listen, why do I have to wait to suffer the brunt in full
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1 force of this injury? You're going to deny me regardless,
2 so let me go ahead and proceed this way."

3 I mean, are you telling me that he would have
4 had to have waited for the Department to flatout say,
5 "You're denied a license" or "You're granted a license,
6 but these are the things that you needed to do"?

7 MR. CONLEY: He --

8 THE COURT: In other words, what the Department
9 did instead was it gave him -- they sent him a letter, a
10 correspondence that invited him to converse more or to
11 have, you know, a further discussion as to what things he
12 could do.

13 MR. CONLEY: The -- the Department sent a letter
14 saying that it was impossible based on the information
15 provided the Department, it was in the dark, it has no idea
16 what Chino, Limited is and whether there would need to be a
17 license.

18 And the petitioner would need to show some kind
19 of injury that resulted from the regulation. And there
20 is -- there is no connection to the injury that they are
21 pointing to here.

22 THE COURT: How is him not shutting down this
23 business a direct response to a challenge to the regulation
24 itself?

25 MR. CONLEY: Because any individual could shut
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1 down a business and then blame it on some law or
2 regulation. There needs to be some kind of cause and
3 effect, some type of connection between the harm you're
4 professing to have suffered and the law or regulation that
5 you're challenging.

6 THE COURT: Are you suggesting that he just
7 randomly decided to shut down the business just because?

8 MR. CONLEY: It appears that the petitioner would
9 prefer to challenge the validity of the regulation in court
10 based on his impressions of how the regulation might have
11 impacted him in the future.

12 THE COURT: Okay.

13 Do you have anything to add or respond, a brief
14 reply with respect to the other issues that were raised?

15 MR. CONLEY: Yes, Your Honor.

16 Just briefly on the point of the Department's
17 authority under the Financial Services Law: The
18 Department was created in the aftermath of the 2008
19 financial crisis and in -- through the enactment of the
20 Financial Services Law. And in enacting the Financial
21 Services Law the legislature tasked the -- this newly
22 formed department with the enforcement of the Banking
23 Insurance and Financial Services Laws and provided a
24 broad grant of authority to regulate new financial
25 services and products and to ensure the continued safety

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1 and soundness of the banking financial insurance
2 industries.

3 The petitioner and virtual currency business
4 activity clearly fits within this. The petitioner's
5 cramped reading of the Financial Services Law ignores the
6 broad consumer protection mandate that's clear on the
7 face of the statute. The virtual currency business
8 activity that is regulated under this regulation is
9 clearly a financial product or service. It's essentially
10 a digital form of money, a medium of exchange that acts
11 as a denominator of value and it can be used to conduct
12 financial transactions, such as buying and selling goods
13 and services.

14 The petitioner maintains and tries to draw a
15 distinction arguing that virtual currency business
16 activity cannot be a financial product or service because
17 it does not involve fiat currencies.

18 THE COURT: It doesn't -- it doesn't have to -- I
19 would remind petitioner that a financial product does not
20 have to be a dollar or money. I mean, how -- I'm still
21 stuck on virtual currency is a digital form of money. Is
22 it not?

23 MR. CIRIC: Okay. Are you asking --

24 THE COURT: We will go back. Go ahead.

25 MR. CONLEY: Okay.

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1 Yes, Your Honor, in certain uses it is.

2 And, to be clear, the regulation does not seek
3 to regulate blockchain technology in the abstract or to
4 regulate just virtual currencies, it's regulating virtual
5 currency business activity, that is virtual currencies
6 which are defined in the statute as any digital unit that
7 is used a medium of exchange or a digitally stored form
8 of value. And it is regulating the financial use of this
9 for those providing financial services and products to
10 New York residents and consumers.

11 The -- the petitioner's myopic interpretation of
12 what financial products and services involves and it must
13 involve fiat currency has -- finds no support in fact or
14 law and it defies common sense.

15 THE COURT: Okay, let me just hear you briefly on
16 the federal preemption argument.

17 MR. CONLEY: The federal preemption argument.

18 The federal preemption argument is wholly
19 without merit, Your Honor. The petitioner is arguing
20 that the regulation is preempted by the Dodd Frank Act.
21 But the Dodd Frank Act was enacted to preserve consumer
22 protection laws, not to preempt them. And it says so
23 explicitly in the texts of the statute, providing that,
24 "Nothing in this provision shall exempt a person from
25 complying with state law."

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1 In enacting Dodd Frank congress specifically
2 preserved the state's authority to enact and enforce laws
3 that grant consumers greater protections than those
4 provided by Dodd Frank itself. There's just nothing in
5 Dodd Frank that evinces a congressional intent to preempt
6 state consumer protection laws. And this has been --
7 it's been explicitly recognized by the Consumer
8 Protection Finance Bureau that Dodd Frank will not
9 supplant consumers in the financial marketplace. This
10 CFPB, the Consumer Finance Protection Bureau has
11 actually, like, worked with states, including the
12 Department of Financial Services, to protect consumers
13 and investigate wrongdoing, by bringing enforcement
14 actions to halt the harmful conduct that is in violation
15 of state and federal law. There's nothing in the text of
16 the statute to support some type of explicit or implied
17 preemption argument.

18 THE COURT: Anything further?

19 MR. CIRIC: Sure.

20 If I may provide just three pieces of
21 information for the Court: On the arbitrary and
22 capricious part of things, the record displays that the
23 certain blockchain technologies that are not Bitcoin
24 could actually be reached by the regulation. There are
25 certain products or certain technologies where you

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1 actually use blockchain in order to develop or to make
2 certain aspects which could actually be covered by the
3 regulation. There's two examples.

4 (To Ms. Roach) If you could just tell me what
5 the index number is or...

6 It's actually in the -- I'm sorry, it's in the
7 affirmation for the motion to dismiss, Section 37,
8 Footnote 57, there is two technology names, one called
9 Uprov and the other called Ascribe. Ascribe is an
10 electronic copy of digital art. If you actually -- you
11 actually --

12 THE COURT: Why is any of that relevant to the
13 arbitrary and capricious standard?

14 MR. CIRIC: Because the regulation -- the
15 regulation could include those type of technologies,
16 because it says anything of value that travels essentially
17 on the blockchain train, to make it simple. Okay, so if
18 you picture blockchain like a train and if you put little
19 wagons and if you have essentially electronic versions of
20 print art or digital art, that technically is also a store
21 value, because that's what people are trying to sell them
22 for. So technically the regulation that is so overbroad
23 is, in fact, cover -- could technically cover those.

24 The second technology called Uprov is electronic
25 copies of photos and videos. If there is a transaction

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1 associated to those, the item that travels on the
2 blockchain train, you could actually make an argument
3 that this -- that the regulation covers those type of
4 products. So if you say store value it could be
5 anything. So basically our argument is that it's too
6 broad. That's the first issue.

7 On the second issue is the statute, 1042(a) is
8 not defined in broad terms. The government wants it to
9 be broad to capture everything and anything. The statute
10 doesn't say that. The statute is limited in nature,
11 that's the key I want -- I want the Court to just take
12 away from the point of the petitioner.

13 On Dodd Frank: If I may just -- and I apologize
14 for the enumeration [sic] of the papers -- in the
15 packet that I gave you there is at the end a page that is
16 actually Page Number 4.

17 THE COURT: I didn't see this in your moving
18 papers or your responsive papers.

19 MR. CIRIC: Actually they're in the -- they're
20 cited. Yeah, they're cited.

21 THE COURT: This seems to be a compilation of
22 various --

23 MR. CIRIC: I'm sorry, Your Honor --

24 THE COURT: -- definitions.

25 MR. CIRIC: -- I wasn't sure where you were going
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1 to go.

2 THE COURT: This here you handed up to me is
3 not -- in its current form you've given to me is not an
4 exhibit to anything. Is it in separates?

5 MR. CIRIC: Well, we cite -- actually both
6 sides -- both sides cite a statute. It's the Dodd Frank
7 section that essentially refers to the power of the CPB
8 over financial products and services. So the only thing we
9 want to attract the attention of the Court on is something
10 called 15--- it's actually Sub Part 1511, which is on
11 Page 4 of -- Numbered 4 -- Okay? -- I -- I don't know which
12 page it is, the physical page, but if you look at the
13 bottom of Page Number 4, and if you see right before, "B,
14 Rules of Construction, Section 11," the little "11..." I'm
15 sorry.

16 (Brief pause.)

17 MR. CIRIC: And the Number 11 says, "Such other
18 financial product or service as may be defined by the
19 Bureau and by regulation for purposes of this title, if the
20 bureau finds such financial products or services..." All
21 sorts of conditions.

22 So Dodd Frank said it's the CBP that defines,
23 Consumer Protection Bureau. I agree with the
24 government -- we agree with the government that states
25 have complete power to develop legislation for consumer

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1 protection. Once a product -- once a financial product
2 or service is defined the CBP controls that. After that
3 control takes place the government can do whatever it
4 wants, absolutely. But, in terms of the definition, a
5 state doesn't have the power to just come up and say that
6 an art -- you know an art gallery or a dealer in oranges
7 is subject to a regulation.

8 THE COURT: Okay. That's the argument on the
9 Article 78 and declaratory judgment, petitioner, with the
10 cross motions.

11 With respect to Sequence Number 3, the motion to
12 compel --

13 MR. CIRIC: Yes.

14 THE COURT: -- there were papers that were filed
15 just a few days ago. So this Court --

16 MR. CIRIC: Okay.

17 THE COURT: Go ahead.

18 MR. CIRIC: Okay.

19 In terms of the bottom line, Your Honor, the
20 Court -- the case law extensively supports the ability
21 for a Court within an Article 78 challenge to order,
22 under CPLR 408, a limited discovery order, if, in fact,
23 the discovery is helping the Court to determine
24 information directly relating to the cause of action.

25 The reason we are asking for the expert is that
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1 since everybody and anybody disagrees on what Bitcoin is
2 these days, the issue or the request of the petitioner is
3 to say, Your Honor, get an expert in order to help you
4 analyze what the economic nature of Bitcoin is.

5 THE COURT: My question to you is if these papers
6 that were filed on October 2nd -- these were E-filed
7 papers?

8 MR. CIRIC: They were E-filed papers. The papers
9 supporting the limited discovery request were filed in
10 September -- were E-filed in September and I think it's the
11 paper copies that we delivered to you last week, yes. The
12 courtesy copies, I'm sorry.

13 THE COURT: The petitioner on this cross motion
14 for limited discovery seeks to hold the defendants -- the
15 respondent's cross motion in abeyance, or, in the
16 alternative, for leave to serve a sur reply. Let me hear
17 you. Are you prepared to orally argue on this motion?

18 MR. CONLEY: Yes, Your Honor.

19 THE COURT: Okay.

20 Let me hear you.

21 MR. CIRIC: Yes. So the bottom line is if the
22 Court orders -- there is ample authority for a Court to get
23 an expert to determine critical information related to the
24 cause of action. There is ample authority to have the
25 court get an expert to help the Court analyze information

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1 that is critical to or directly related to the cause of
2 action. That's the Farkas case which I refer to.

3 So under that rule what we basically argue is in
4 order to get the expert -- any economic expert that can
5 speak to the nature of -- the economic nature of Bitcoin
6 is critical in order for -- for the Court to make the
7 determination of whether or not Bitcoin is a financial
8 product or service. That's number one.

9 Under those types of situations abeyance has
10 been provided in situations where -- of the motion to
11 dismiss that was filed by the other side is accommodated
12 for the purpose of making that determination. So we have
13 a couple of...

14 (Mr. Ciric and Ms. Roach confer.)

15 THE COURT: Your opposition...?

16 MR. CONLEY: Your Honor, on the discovery issue,
17 the petitioner's motion for limited discovery is
18 inappropriate for multiple reasons. Setting aside the
19 particulars of the discovery that is actually being sought
20 as a procedural matter, discovery is presumptively improper
21 in Article 78 proceedings. And under the CPLR an automatic
22 stay is put in place when a party files a dispositive
23 motion to dismiss under CPLR 3211.

24 So, here, to direct discovery, the moving party,
25 the petitioner, would have to demonstrate an ample need

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1 for the requested discovery that was both material and
2 necessary to the claims being raised.

3 The claims being raised here are that the
4 Department of Financial Services exceeded the scope of
5 its regulatory authority in promulgating challenge
6 regulation and that that -- and that the regulation,
7 certain aspects of its scope and design are arbitrary and
8 capricious.

9 In other words, the petitioner is raising pure
10 questions of law that this Court can fully and fairly
11 review by looking at the challenged regulation itself,
12 the enabling legislation, the Financial Services Law and
13 applicable precedent.

14 Yet the petitioner is seeking a wide range of
15 irrelevant information, including an order from the Court
16 compelling Paul Krugman, the Nobel Prize winning
17 economist and New York Times columnist, to testify on the
18 economic nature of Bitcoin; an order compelling the
19 Department to produce an assortment of emails and other
20 written documentation that was internally circulated over
21 a three-year period; and an order directing the former
22 superintendent, the head of the Department of Financial
23 Services, to attend a deposition to be deposed on his
24 internal thought processes leading up to the promulgation
25 of the regulation.

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1 These requests are facially improper and
2 inappropriate, Your Honor. And it's a quintessential
3 example of a party seeking permission to go on a fishing
4 expedition and find something of possible relevance that
5 could salvage their claims. And the petitioner's request
6 here should be denied.

7 THE COURT: Do you have any objection to them --
8 their request for a sur reply? I believe that was an
9 outstanding request, although maybe you resolved that.

10 MR. CIRIC: The sur reply was coming from the
11 prior -- from the paper record prior to the filing
12 conversion, Your Honor.

13 THE COURT: Okay. So that is a nonissue at this
14 point.

15 MR. CIRIC: Correct.

16 THE COURT: Okay.

17 Anything to add?

18 MR. CIRIC: On the -- on the discovery piece, on
19 the ample need situation, under -- By the way, limited
20 discovery is routinely granted. Okay? This is not a
21 situation where -- even in governmental cases or in -- it's
22 exceptional. It's -- it's not every day, but it's not
23 just, you know, supremely rare. So the key is if --

24 THE COURT: What's your response to the fact that
25 discovery is stayed because of the filing of the motion?

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1 MR. CIRIC: Okay, the discovery, in terms of the
2 expert, is critical to what Bitcoin is. In order to
3 resolve the motion to dismiss that's a critical threshold
4 question. In order for that critical threshold question to
5 be addressed you first -- if you get the expert you have to
6 basically stop the rest of the train. That's our request.

7 THE COURT: Anything further?

8 MR. CONLEY: Not -- No, Your Honor.

9 THE COURT: Okay.

10 This Court has fully heard the parties with
11 respect to Sequence Number 1 and Sequence Number 3
12 regarding Theo Chino against the New York State
13 Department of Financial Services, et al, under Index
14 Number 101880 of 2015.

15 The Court reserves decision. We will put this
16 on for a future date for a decision.

17 Off the record.

18 (Discussion off the record.)

19 THE COURT: Back on the record.

20 The parties have agreed to order the transcript
21 of today's proceeding for this Court's consideration in
22 full of these motions. The parties are directed to order
23 the minutes of this proceeding within the next five days.
24 It does not have to be done expedited, but it needs to be
25 done within the next five days and provided to the Court

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1 upon receipt.

2 The Court will review the minutes, as well as
3 obviously all the written submitted material with respect
4 to these decisions, and the case will be next on for
5 January 11, at 2:15 p.m. for a decision.

6 Thank you.

7 MR. CIRIC: Thank you very much, Your Honor.

8 MR. CONLEY: Thank you.

9 (Whereupon, the above-captioned proceedings
10 were concluded.)

11 oo
12 (It is hereby certified that the
13 foregoing is a true and accurate
14 transcript of the proceedings.
15 (
16 _____
17 ROBERT PORTAS, RPR, CRR
18 Senior Court Reporter
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