New York County Clerk's Index No. 101880/15
Appellate Division, First Department Case No. 2018-998

Court of Appeals

STATE OF NEW YORK

In the Matter of the Application of
THEO CHINO and CHINO LTD,

Plaintiffs-Petitioners-Appellants,

against

THE NEW YORK DEPARTMENT OF
FINANCIAL SERVICES, et al.,

Defendants-Respondents-Respondents.

MOTION FOR LEAVE TO APPEAL TO THE NEW YORK STATE COURT OF APPEALS

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Date Completed: September 17, 2019

COURT OF APPEALS
STATE OF NEW YORK

THEO CHINO and CHINO LTD,

Plaintiffs-Petitioners-Appellants,

-against-

THE NEW YORK DEPARTMENT OF FINANCIAL SERVICES, et al.,

Defendants-Respondents-Respondents.

NOTICE OF MOTION FOR LEAVE TO APPEAL

Index No. 101880/15

PLEASE TAKE NOTICE that, upon the annexed affirmation of Pierre Ciric, dated September 17, 2019, and all the papers and proceedings had herein, plaintiff-petitioner-appellants Theo Chino and Chino LTD (collectively "Appellants"), will move this Court, at the Courthouse at 20 Eagle Street, Albany, New York, on Monday, October 14, 2019, for an order, pursuant to CPLR 5602(a) and Rule 500.22 of this Court, granting Appellants leave to appeal to this Court from the decision and order of the Appellate Division, First Department, entered April 23, 2019, and for such other and further relief as the Court deems just and proper.

Dated: September 17, 2019
New York, New York

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COURT OF APPEALS
STATE OF NEW YORK

THEO CHINO and CHINO LTD,

Plaintiffs-Petitioners-Appellants,

-against-

THE NEW YORK DEPARTMENT OF FINANCIAL SERVICES, et al.,

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AFFIRMATION IN SUPPORT OF MOTION FOR LEAVE TO APPEAL

Index No. 101880/15

Pierre Ciric, an attorney admitted to practice in the courts of this State, affirms the following to be true, under penalty of perjury:

1. I am the attorney for Plaintiffs-Petitioners-Appellants Theo Chino and Chino LTD (collectively, "Appellants"). I am familiar with the facts and circumstances of this proceeding based upon my review of the files maintained by this office and conversations had with Appellants.

2. This affirmation is submitted in support of Appellants' motion for leave to appeal to this Court from the Decision and Order of the Appellate Division, First Department, entered April 23, 2019 (*see* copy of the Appellate Division Decision and Order, Exhibit A), as well as the Appellate Division, First Department's denial of Appellants' motion for leave to appeal that decision, issued on August 13, 2019, and served on Appellants on August 15, 2019. *See* copy of the Appellate Division, First Department's denial of Appellants' motion for leave to appeal, Exhibit C.

3. In this action, Appellants challenge a regulation issued by Respondent New York Department of Financial Services ("DFS"), the first of its kind in the nation, 23 NYCRR § 200,

et seq. (the "Regulation"), which imposes more than a dozen separate mandates on businesses involved in any way with so-called "virtual currencies," the most well-known of which is Bitcoin.

The Appellate Division Decision

4. On April 23, 2019, the Appellate Division affirmed the order of the Supreme Court, New York County (Carmen Victoria St. George, J.), entered on December 21, 2017, which declared that Appellants failed to exhaust available administrative remedies and to demonstrate an injury-in-fact. *See* copy of the Supreme Court's order, Exhibit B.

5. In its April 23, 2019 decision, the Appellate Division, First Department affirmed, finding that Appellants failed to exhaust administrative remedies, and rejecting the applicability of any of the exceptions to the exhaustion doctrine that this Court has identified, in conflict with this Court's decision in *Watergate II Apts. v Buffalo Sewer Auth.*, 46 NY2d 52 [1978], and the decisions of the Second and Third Departments of the Appellate Division. The court also found that, despite the numerous and burdensome requirements Appellants faced under this licensing regime, they had identified no injury-in-fact and therefore lacked standing to bring this action.

6. This Court should grant leave to appeal the judgment of the Appellate Division, First Department, because this appeal presents novel and important questions of law – particularly the application of the injury-in-fact standing analysis to low-resource technological startup firms – and involves a conflict among Appellate Division departments as well as with the decisions of this Court, and because the decisions below fundamentally conflict with this Court's standing jurisprudence.

Timeliness of the Instant Motion

7. The Supreme Court, New York County, issued its decision dismissing Appellants'

Petition on December 21, 2017. *See* Exhibit B. Appellants were served with notice of entry on January 14, 2018, and timely filed and served a notice of appeal to the Appellate Division, First Department, on February 3, 2018.

8. The Appellate Division, First Department, affirmed the decision of the Supreme Court by an opinion issued April 23, 2019. *See* Exhibit A. Appellants were served with notice of entry on May 10, 2019, and timely sought leave to appeal to this Court from the Appellate Division by motion filed and served on May 31, 2019.

9. The Appellate Division, First Department, denied Appellants' motion for leave to appeal on August 13, 2019. *See* Exhibit C. The Appellate Division's order was served by United States mail by Respondents on August 15, 2019. Thus, this motion is timely since it is made within 35 days of the mailing of the notice of entry.

Jurisdiction of the Court

10. Pursuant to CPLR § 5602(a)(1)(i), this Court has jurisdiction to determine this motion and the proposed appeal because the action originated in the Supreme Court, and the April 23, 2019 order of the Appellate Division is a final disposition of Appellants' initial challenge, which is a hybrid New York Civil Practice Law and Rules ("CPLR") Article 78 proceeding and a declaratory judgment action.

Issues Presented on this Appeal

11. The issues presented in this case are:

a. Whether the Appellate Division erred in refusing to find an injury-in-fact, even where Appellants – a cryptocurrency startup and its founder – established that they were subject to and impacted by the extensive and burdensome requirements of the regulation.

b. Whether the Appellate Division erred in refusing to apply the exceptions to the exhaustion doctrine as stated in *Watergate II* and in affirming the addition of an "irreparable harm" requirement to such exceptions, a new legal creation not found in prior decisions of this Court or any other.

12. These issues were raised both before the Supreme Court (Record on Appeal (R.) 202, R. 203-208, R. 209-217, R. 219-221, R. 271, R. 297-298, R. 300-302, R. 310-311, R. 372-373, R. 375-376, R. 378, Supplemental Record on Appeal (SR.) 394, SR. 398), as well as before the Appellate Division (Br. for Pls.-Pet'rs-Appellants at 11-16, 17-21, Reply Br. for Pls.-Pet'rs-Appellants at 4). Thus, they have been properly preserved for this Court's review.

Promulgation of the BitLicense

13. DFS, of its own initiative, and without the New York State Legislature's mandate or instructions, adopted a regulatory scheme (commonly called the 'BitLicense') to quash the growth of cryptocurrency-based businesses in New York. 23 NYCRR § 200, et seq. The Regulation took effect on June 24, 2015.

14. Under the Regulation, anyone engaging in "virtual currency business activity" was required to obtain a license from DFS's Superintendent. 23 NYCRR § 200.3(a). The first such rule of its kind in the United States, the Regulation created a complex and burdensome set of requirements that applicants and licensees were required to follow in order to simply operate in New York State. *Id.*

15. Specifically, the Regulation imposes upon applicants and licensees a myriad of requirements to which businesses such as Appellants were not previously subject, including: maintaining reserve capital requirements in an amount to be determined by the Superintendent on an individual basis; maintaining a surety bond or trust account in a form and amount to be

determined by the Superintendent on an individual basis; receiving prior government permission to conduct *any* material change in business; receiving prior government permission to undertake *any* mergers, acquisitions, or change in ownership; preserving *all* business records for seven years; permitting intrusive examinations of *any* aspect of the firm's business (including all operations outside New York) at the sole discretion of the Superintendent; establishing an internal anti-money laundering scheme with independent compliance monitoring; and creating a mandatory five-prong cyber-security scheme subject to DFS approval. 23 NYCRR § 200, et. seq.

16. Due to the overwhelming burdens imposed by the Regulation, estimated to cost at least $50,000 to $100,000, nearly every New York cryptocurrency startup company elected to relocate out of state rather than attempt to obtain a BitLicense. *See* R. 33 [citing Daniel Roberts, *Behind the "Exodus" of Bitcoin Startups from New York*, FORTUNE (Aug. 14, 2015)].

Theo Chino and Chino LTD

17. In 2013, prior to the public at large knowing anything about Bitcoin and other cryptocurrencies, Theo Chino ("Theo") started a small business, Chino LTD ("Chino"), to allow more people to use the cryptocurrency Bitcoin in everyday life. R. 44. He wanted New York City bodegas, small grocery stores, and convenience stores to be able to accept Bitcoin as a form of payment for everyday items. R. 45. Theo's entrepreneurial efforts were part of his desire to encourage small businesses to use Bitcoin to ensure that this new technology would reach more consumers. By May 2015, Theo (through Chino) entered into seven contracts with convenience stores in New York and invested significant funds to develop a system infrastructure to achieve his goal. R. 45-46.

18. Chino filed an application for a BitLicense under the Regulation on August 7, 2015. R. 46-47. Realizing, through the application process, the incredible burdens of this

Regulation, as well as DFS's overreach to create law outside of the Legislature's mandate, and while his application was pending, Theo and Chino filed a pro se verified complaint and petition on October 16, 2015, under CPLR Article 78, and within the appropriate four-month statute of limitations. R. 47. They claimed that the challenged Regulation (i) violated the separation of powers doctrine; (ii) was arbitrary and capricious; (iii) was preempted by federal law; and (iv) contained disclosure requirements that violated the First Amendments to the United States Constitution and New York Constitution. R. 48-58.

19. After this filing, Chino's application was returned without further processing on January 4, 2016.[1] R. 47.

20. The appeal before the Appellate Division and this motion for leave to appeal now before this Court are limited to the issues of standing and exhaustion of administrative remedies.[2]

Leave to Appeal Should be Granted Because the Decision Below Fundamentally Conflicts with this Court's Standing Jurisprudence

21. Leave to appeal should be granted because this case raises a significant legal issue as to whether the Appellate Division has sharply reversed this Court's continuing expansion of standing jurisprudence so as to find that even a company faced with financial extinction lacks standing to challenge the regulation that is the direct cause of such ruin.

22. Whether in the Article 78 or the declaratory judgment contexts, this Court has shown a consistent concern for ensuring that its standing doctrine is flexible and consistent with

[1] Theo Chino later hired counsel and filed an amended verified complaint and petition through counsel on May 26, 2017.

[2] The issue of whether Appellants' cross-motion for limited discovery (filed on August 2, 2017, and denied as moot in the decision dated December 21, 2017) was warranted was also addressed below. However, this issue was not the focus of the appeal, but was brought up to preserve the request should the Supreme Court's decisions on standing and exhaustion be overturned.

the public policy goal of ensuring reasonable access to the court system. A two-prong test allows courts to evaluate a petitioner's standing to challenge a governmental agency's actions. A petitioner need only show: (1) that there is "injury in fact," meaning petitioner will actually be harmed by the administrative action; and (2) that the interest the petitioner asserts falls "within the zone of interests or concerns sought to be promoted or protected by the statutory provision under which the agency has acted." *NY State Assn. of Nurse Anesthetists v Novello*, 2 NY3d 207, 211 [2004]; *Dairylea Coop., Inc. v Walkley*, 38 NY2d 6, 9 [1975].

23. The touchstone of the standing doctrine has been a requirement that the petitioner has "suffered an injury in fact, distinct from that of the general public." *Novello*, 2 NY3d at 211-12; *Transactive Corp. v NY State Dept. of Social Servs.*, 92 NY2d 579, 587 [1998] (emphasis added). In a declaratory judgment context, this Court has similarly held that the plaintiff must show "special damages distinct from that suffered by the public at large," and it is shown that personal or property rights will be directly and specifically affected. *Abrams v NY City Tr. Auth.*, 48 AD2d 69, 70 [1st Dept 1975], *aff'd*, 39 NY2d 990 [1976].

24. Furthermore, a petitioner does not have to prove actual and present harm, rather, he or she needs only demonstrate that "it is reasonably certain that the harm will occur if the challenged action is permitted to continue." *Police Benevolent Assn. of NY State Troopers, Inc. v Div. of NY State Police*, 29 AD3d 68, 70 [3rd Dept 2006] [citing *Socy. of Plastics Indus. v County of Suffolk*, 77 NY2d 761, 776 [1991]]. Moreover, a petitioner is not required to describe injury "with specific quantification." *NY Propane Gas Assn. v NY State Dept. of State*, 17 AD3d 915, 916 [3rd Dept 2005].

25. The purpose of this test is to determine whether a party should have access to the court system, and is not to assess the specific merits of a petitioner's claim. *Socy. of Plastics*

Indus., 77 NY2d at 769.

26. Over time, this Court has continually expanded the concept of standing, noting that "[t]he increasing pervasiveness of administrative influence on daily life ... necessitates a concomitant broadening of the category of persons entitled to judicial determination" and that "[a] fundamental tenant of our system of remedies is that when a government agency seeks to act in a manner adversely affecting a party, judicial review of that action may be had." *Dairylea*, 38 NY2d at 10; *see also Sun-Brite Car Wash, Inc. v Bd. of Zoning & Appeals*, 69 NY2d 406, 413 [1987]. In fact, this Court specifically warned that standing principles, "which are in the end matters of policy, should not be heavy-handed." *Sun-Brite Car Wash*, 69 NY2d at 413.

27. This Court has maintained a continuous effort to cautiously expand the standing doctrine, even finding that "proof of special damage or in-fact injury is not required in every instance to establish that the value or enjoyment of one's property is adversely affected". *Id.* [citing *Douglaston Civic Asso. v Galvin*, 36 NY2d 1 [1974]]; *Little Joseph Realty, Inc. v Babylon*, 41 NY2d 738 [1977]; *Douglaston Civic Asso.*, 36 NY2d at 6. Indeed, "an allegation of close proximity alone may give rise to an inference of damage or injury that enables a nearby owner to challenge a zoning board decision without proof of actual injury." *Sun-Brite Car Wash*, 69 NY2d at 414.

28. In all of these contexts, the standing requirement is satisfied when, once a form of special damage can be demonstrated which is distinct from that suffered by the public at large, "personal or property rights will be directly and specifically affected." *Abrams*, 48 AD2d at 71 [emphasis added]. Therefore, the standing requirement is satisfied as long as the petitioner shows that the challenged regulation has an actual or potential impact on his or her personal or property rights. In this Court's standing jurisprudence, no petitioner is required to quantify with precision

the nature and value of his or her actual or potential injuries.

29. Given the historical development of the standing doctrine and the trend toward preserving access to the courts, particularly for plaintiffs who are affected in a manner distinct from the general public, the First Department's finding that Appellants lacked standing because they could not point to any harm they suffered under the Regulation is absurd. Chino – a one-man operation – went overnight from being subject only to generally-applicable business laws to being under the thumb of the first-in-the-nation regulatory scheme requiring compliance with a dozen new mandates at an estimated cost of $50,000 to $100,000, far more than the entirety of its annual revenues. R. 33.

30. In the present case, Appellants satisfied the evidentiary burden provided by this Court's existing jurisprudence. Appellants established that they took many affirmative steps to establish the business, such as signing contracts with convenience stores and investing significant funds into system infrastructure. R. 44-46. In fact, the business was fully operational at the time of the Regulation's promulgation, and at the time the initial action was filed, on October 16, 2015. R. 44-47. Appellants would have been required to take significant and costly compliance measures to either comply with the Regulation or to continue the application process. The record demonstrates that the resources needed to comply with the Regulation would be overwhelming for Appellants' small business. The license application cost is a non-refundable $5,000 fee, with some companies reporting they have spent $50,000-$100,000 to comply with the Regulation. R. 33. *See also* 23 NYCRR § 200.5.

31. Furthermore, Appellants have shown that they are subject to the Regulation. The record below shows the challenged Regulation applies to Appellants because, in processing Bitcoin for the retail stores, Appellants have custody of the Bitcoin key transferred by customers

to pay for retail items. R. 255-56. That custody of the Bitcoin key, as well as the exchange services performed on behalf of the retail stores, triggers a number of provisions from the Regulation. 23 NYCRR § 200.2(q)(2)-(q)(4). A licensee also must have someone "qualified" to handle monitoring compliance with the Regulation, day-to-day compliance with DFS's anti-money laundering program, and a "Chief Information Security Officer responsible for overseeing and implementing… cyber security program and enforcing its cyber security policy." 23 NYCRR § 200.7, § 200.15(c)(3), and § 200.16(c) and (g). Hiring a Chief Information Security Officer would have represented an overwhelming cost for Appellants. 23 NYCRR § 200.12(c).

32. Therefore, based on the record below, Appellants have raised more than an amorphous allegation of potential future injury. Appellants have asserted a concrete interest in the matter that Respondents are attempting to regulate and doing so without the Legislature's mandate. Appellants have more than a tangential stake in the litigation because they have established that they are directly affected by the Regulation and face a concrete injury within the zone of interests protected by the procedural statutes.

33. Furthermore, this Court's existing standing doctrine does not require proof that the challenged action was the exclusive threat affecting a petitioner's personal or property rights. For instance, the courts never asked, <u>for standing purposes</u>, the property owners to prove that the challenged zoning regulation was the sole reason for a drop in real estate values. *Sun-Brite Car Wash, Inc.*, 69 NY2d 406 at 413. With its decision in the case at hand, the Appellate Division demanded just that from Appellants, by stating that Appellants failed to prove that the Regulation was the sole reason their business encountered difficulties or that Appellants decided to stop further marketing efforts after they received the January 6, 2016 letter from Respondents seeking additional information. *Chino v NY Dept. of Fin. Servs.*, 171 AD3d 610, 610 [1st Dept

2019].

34. Furthermore, in its decision, the Appellate Division incorrectly relied on *Cherry v Koch*, 126 AD2d 346 [2nd Dept 1987], which involved the denial of standing to a prostitute and a patron of prostitutes to challenge the constitutionality of a criminal code provision declaring illegal private commercial sex between consenting adults.

35. In *Cherry*, the petitioners lacked standing because they were not involved in any prostitution activity at the time they filed their declaratory judgment action, and even for several years prior to that date. *Id.* at 352. In the present case, Appellants have demonstrated that they were operating a cryptocurrency business and were subject to the challenged Regulation at the time they filed the action. Contrary to the petitioners in *Cherry*, Appellants had standing because they showed that they were subject to the Regulation and demonstrated a special damage which is distinct from that suffered by the public at large. Appellants are quite far from mere bystanders finding the challenged government action "personally offensive." *Id.*

36. With its present decision, the Appellate Division has significantly restricted this Court's standing doctrine by demanding that Appellants prove, <u>for standing purposes</u>, that the Regulation was not just impacting Appellants' business, but that it was the sole reason Appellants stopped their marketing efforts to the exclusion of all other factors. Through this change, the Appellate Division has improperly imported a significant evidentiary burden, reserved for the damages stage of litigation, into the standing analysis. The issue raised by this motion is not whether such a significant doctrinal shift is to be supported or rejected by this Court, but whether the Appellate Division has the power, alone, to modify this Court's doctrine. We argue that it lacks such power, and consequently urge this Court to grant this motion.

Leave to Appeal Should Be Granted Because the Appellate Division Decision Would Erect an "Impenetrable Barrier to Judicial Review" of Respondents' Unlawful Actions

37. One of the most significant concerns in this Court's standing doctrine is "to prevent the erection of an impenetrable barrier to judicial review of unlawful official action." *Abrams*, 39 NY2d at 992.

38. Allowing the Appellate Division's decision to stand would have the effect of insulating the Regulation from a timely procedural challenge. This result would be contrary to the public interest. *See Matter of Assn. for a Better Long Is., Inc. v NY State Dept. of Envtl. Conservation*, 23 NY3d 1, 8 [2014] [observing that "[g]iven the compressed four-month statute of limitations (*see* State Administrative Procedure Act 202 § [8]), we would be erecting an 'impenetrable barrier' to any review of this facet of the administrative action."].

39. Here, Appellants had only four months following the Regulation's promulgation to challenge it under CPLR Article 78. At the time the Regulation was promulgated, only technology firms interested in starting a business involving cryptocurrency were subject to the Regulation. The vast majority of the smaller startup companies impacted by the Regulation decided to immediately move out of New York State rather than seek to comply with the Regulation's byzantine requirements. R. 40-42. The companies that fled New York would have encountered significant legal hurdles to establish standing to challenge the Regulation upon its promulgation since, at the expiration of the four-month statute of limitations, they would have lost the necessary jurisdictional nexus with New York to challenge the Regulation. No other small startup company beside Appellants' applied for a license because it was cost-prohibitive. R. 139, R. 33, R. 44. Furthermore, Appellants are the only small startup company that decided to stay in New York because the business owner could not afford to move out of state. R. 46. Therefore, Appellants, who stayed in the jurisdiction, are uniquely positioned to challenge the Regulation because they are the only ones that could satisfy the standing requirements by

remaining in New York.

40. If Appellants do not have standing in this case, then no one can have standing, thus "erecting an 'impenetrable barrier' to any review of this facet of the administrative action." *Abrams*, 39 NY2d at 992. This outcome would have profound implications on the due process and constitutional rights of these entities, as well as the ability of the court system to adjudicate the Regulation's lawfulness, which is particularly important in this vital and emerging area of new technology.

41. Finally, succeeding in a business plan is not necessary to show standing. Even had Appellants failed to turn a profit absent the Regulation, it is enough for standing purposes to show that the challenged action negatively impacted them. *Abrams*, 48 AD2d at 70; *see also Credico v NY State Bd. of Elections*, 2013 U.S. Dist. LEXIS 109737 [EDNY June 19, 2013] ["[I]t is not necessary for the purpose of establishing standing that plaintiffs show that Mr. Credico might have won the election or achieved a specific number of additional votes…."].

42. Whether or not Appellants' business, if allowed to continue operations, would have succeeded does not belong in a standing analysis. Thus, the lower courts' discussion of "self-inflicted injury" is beside the point. *Chino v NY Dept. of Fin. Servs.*, 171 AD3d 610, 610 [1st Dept 2019]. All Appellants needed to demonstrate was that the Regulation negatively affected them in a way distinct from the general public. *Novello*, 2 NY3d at 211-12; *Transactive Corp.*, 92 NY2d at 587.

Leave to Appeal Should be Granted Because Respondents' Regulatory Overreach into the Cryptocurrency/Blockchain Industry is an Issue of Public Importance.

43. This case, involving the first attempt by any state to regulate cryptocurrency businesses, has been the subject of intense attention from the industry, and other states have been watching its evolution to determine whether they should adopt statutes similar to the Regulation.

On March 25, 2019, the Uniform Law Commission ("ULC") withdrew its model act titled the Uniform Regulation of Virtual-Currencies Businesses Act ("URVCBA"), after backlash from the industry and other states vehemently opposition to ULC's approach. NAT'L CONFERENCE OF COMM'RS ON UNIF. STATE LAWS, UNIFORM REGULATION OF VIRTUAL-CURRENCIES BUSINESSES ACT (2017), https://www.uniformlaws.org/HigherLogic/System/DownloadDocumentFile.ashx?DocumentFileKey=ef45a10b-ac62-ad3d-2f42-588d7eac3e40&forceDialog=0. The URVCBA was finalized in 2017 essentially using the Regulation as a template, requiring an entity to apply for a license and be approved after a thorough review of its policies, procedures, and background. To date, no state has adopted URVCBA's approach, based on the New York framework. Clearly, the regulatory approach to cryptocurrencies is the subject of an important debate, not only in New York but also throughout the country and many states have clearly signaled their opposition to New York's framework. Caitlin Long, *Seismic News About State Virtual Currency Laws: ULC Urges States to Withdraw Model Act* (Mar. 25, 2019), https://www.forbes.com/sites/caitlinlong/2019/03/25/seismic-news-about-state-virtual-currency-laws-ulc-urges-states-to-withdraw-model-act/#2cc2c3625fda.

44. Even in New York, the virtual currency industry has been the subject of continued interest. New York Assembly Bill A08783 was signed into law on December 21, 2018. 2018 N.Y. ALS 456, 2018 N.Y. Laws 456, 2018 N.Y. Ch. 456, 2017 N.Y. AB 8783. This law established a "digital currency task force" to provide the governor and the legislature with information on the potential effects of the widespread implementation of digital currencies on financial markets in the state. It marks the Legislature's first foray into investigating the uses of virtual currencies in the state. The enactment of New York Assembly Bill A08783 not only

indicates that DFS lacks the broad power to regulate virtual currencies as it has claimed since 2015 but also shows that the development of the blockchain technology and cryptocurrency-based businesses is becoming a major topic of public debate within the general population and within the New York Legislature.

45. Before the enactment of Assembly Bill A08783, the New York Senate held a roundtable discussion on cryptocurrency in February 2018 to gain insight into cryptocurrency, its marketplace, and the impact of the Regulation. Every participant to the roundtable called by the Senate expressed significant opposition to the Regulation. Stan Higgins, *New York Lawmakers Open to Revisiting the BitLicense,* COINDESK (Feb. 23, 2018), https://www.coindesk.com/bitcoin-crypto-ny-lawmaker-pledges-make-bitlicense-something-works.

46. The level of public importance around the regulatory approaches to blockchain technology and cryptocurrency businesses is similarly illustrated by multiple hearings held in the U.S. Congress over the past two years. *See e.g.* Exploring the Cryptocurrency and Blockchain Ecosystem Before the S. Comm. on Banking, Housing, and Urban Affairs, 115th Cong. (2017). Further, multiple bills have been introduced involving cryptocurrency: (1) To amend the Internal Revenue Code of 1986 to exclude from gross income de minimis gains from certain sales or exchanges of virtual currency, and for other purposes, H.R. 3708, 115th Cong. (2017); (2) Section 12 of Combating Money Laundering, Terrorist Financing and Counterfeiting Act of 2017, S. 1241, 115th Cong. (2017); and (3) Section 1409 of SECURE Act of 2017, S. 2192, 115th Cong. (2017). The regulatory approaches around this critical technology represent an important issue of great public concern, not only in New York but also across the country.

47. This technology is an area of further public interest, especially because the technology industry is promoted by New York State as an increasingly important component of its economy. *See The New York City Tech Ecosystem*, HR&A ADVISORS (Mar. 2014), https://www.hraadvisors.com/wp-content/uploads/2014/03/NYC_Tech_Ecosystem_032614_WEB.pdf; Brian Forde, *How to Prevent New York from Becoming the Bitcoin Backwater of the U.S.*, MEDIUM (May 12, 2015), https://medium.com/mit-media-lab-digital-currency-initiative/how-to-prevent-new-york-from-becoming-the-bitcoin-backwater-of-the-u-s-931505a54560. Startup entities are essential to technological innovation and growth, and in 2015, New York City was recognized as being one of the top startup ecosystems in the world. Richard Florida, *The World's Leading Startup Cities*, CITYLAB (July 27, 2015), https://www.citylab.com/life/2015/07/the-worlds-leading-startup-cities/399623/; Emily Edwards, *Financial Technology Startups Are Bringing Underbanked Into the Economy*, MEDIUM (May 16. 2016), https://medium.com/village-capital/financial-technology-startups-are-bringing-the-underbanked-into-the-economy-24978561b9ea. However, the Regulation has transformed this once welcoming New York landscape into an inhospitable environment for digital currency-related startups. Daniel Roberts, *Behind the "Exodus" of Bitcoin Startups from New York*, FORTUNE (Aug. 14, 2015), http://fortune.com/2015/08/14/bitcoin-startups-leave-new-york-bitlicense/.

48. Permitting the Court of Appeals to review Appellants' access to the courts will allow this Court to weigh in on an issue of great public importance to New York's tech startups and will avoid a significant detrimental precedent for both the administrative exhaustion rules and the injury analysis as applied to startup entities.

49. As this technology continues to grow more popular and more startup entities attempt to create new business opportunities in this field, the application of the Regulation, as well as issues of standing and exhaustion, to this dynamic industry will be an ever-growing area of public interest. Furthermore, it is without question that other states will be watching New York's approach as they continue to consider their own regulatory approaches to this technology.

Leave to Appeal Should be Granted Because Adapting the Standing Doctrine to Startups Involved in new Technology is a Novel Issue

50. Although standing is not a new area of law, the question of how the current laws apply to new technology has become of critical importance and is a new issue in today's economy. "As technology has developed, old assumptions and guideposts are ever challenged, providing doctrinal puzzles we must solve…. The old rules of thumb are deteriorating as useful metrics…." *People v Diaz*, 33 NY3d 92, 114-15 [2019] [Wilson, J., dissenting]. Prior assumptions about standing and its application to businesses involving cryptocurrency are a prime example of the Court of Appeals needing to solve a puzzle where old assumptions and guideposts are challenged.

51. Moreover, Appellants' business was fully operational at the time of the Regulation's promulgation, and at the time the initial action was filed, on October 16, 2015. The standing analysis must be applied as of the date of the complaint's filing, October 16, 2015, and not at the time Appellants stopped their business activities. *See, e.g., Wells Fargo Bank, N.A. v Jones*, 139 AD3d 520, 523 [1st Dept 2016] (standing determined "at the time the action was commenced").

52. The record demonstrated that the standing test was satisfied at the time of the filing of the action and that Appellants have made significant investments to launch their business plans. The record also establishes that Appellants were not able to reap the benefits of

their investments because of the Regulation. Appellants filed their action on October 16, 2015, before they decided to stop their business activities on January 4, 2016. Therefore, Appellants must have an opportunity to seek the Court of Appeals' views as to how the standing test applies in this type of new technology environment.

53. The Court of Appeals should be provided with an opportunity to determine when a startup business that has taken affirmative steps and expended significant resources can satisfy the standing analysis. Declining to provide an opportunity for the Court of Appeals to review the standing analysis as to startup environments would have profound implications and a severe impact on new technology sectors, where market participants effectively would be denied the opportunity to challenge new regulations where doing so would require expending prohibitively large sums.

Leave to Appeal Should Be Granted Because the Appellate Division Erred in Refusing to Apply This Court's Holding in *Watergate II*

54. Leave to appeal should be granted because this case raises a significant legal issue as to whether and when litigants are exempted from exhausting administrative remedies if they qualify for specific exceptions established by this Court in *Watergate II.*

55. "It is well established that a person aggrieved by the action of a government agency is generally required to exhaust the available administrative remedies before seeking judicial review of the agency's action." *Bankers Trust Corp. v New York City*, 750 NYS2d 29, 34 [1st Dept 2002] [citations omitted]. "The exhaustion rule, however, is not an inflexible one." *Watergate II Apts.*, 46 NY2d at 57. This Court outlined four specific circumstances when the exhaustion rule did not apply to a petitioner: (1) when an agency's action is challenged as unconstitutional; or (2) when an agency's action is wholly beyond its grant of power; or (3) when resorting to an administrative remedy would be futile; or (4) when pursuit of an administrative

remedy would cause irreparable injury. *Id*.

56. A petitioner need only establish one exception to the exhaustion rule to permit a direct challenge to an agency action. Based on the record below, Appellants have amply demonstrated that they qualify for multiple exceptions to the exhaustion rule.

57. First, Appellants are exempt from the exhaustion rule because challenged Respondents' action in promulgating the Regulation as being "wholly beyond its grant of power" and the Legislature has not empowered DFS to regulate new technologies beyond traditional financial products and services. *See* FSL § 104(a)(2). R. 48. This claim alone is plainly sufficient to excuse a failure to exhaust. *See Bankers Trust Corp.*, 750 NYS2d at 34. Indeed, Respondents admitted that they promulgated the Regulation on their own volition and without statutory direction from the New York State Legislature. R. 209-218, R. 146. Appellants' allegations that the Regulation is an ultra vires exercise of administrative power excuses any failure to exhaust administrative remedies. *See Watergate II Apts*, 46 NY2d at 57.

58. Second, Appellants are exempt from the exhaustion rule because they sufficiently allege that the Regulation is unconstitutional. R. 254-255; R. 54-58. The Regulation contains disclosure requirements that violate commercial speech rights under the First Amendments to the United States Constitution and the New York Constitution, allowing them to forgo compliance with the exhaustion rule. R. 54-58.

59. Third, Appellants are exempt from the exhaustion rule because pursuit of an administrative remedy would cause irreparable harm to them. When a petitioner challenges a regulation for being inconsistent with the governing statutes and, therefore, irrational, arbitrary and capricious, the petitioner is governed by the four-month statute of limitations applicable to Article 78 proceedings. *NY City Health & Hosps. Corp. v Bane*, 621 NYS2d 539, 543-544 [1st

Dept 1995]; *see also* CPLR § 217. As pled in their Complaint, it became obvious to Appellants that pursuing the application process would be overwhelmingly burdensome. R. 47. Therefore, Appellants had no other option but to file a combined Article 78 and declaratory judgment action within four months of the Regulation's final promulgation, which Appellants in fact purposefully and scrupulously did. R. 26. The final version of the Regulation was published in the New York State Register on June 24, 2015, with an effective date of June 24, 2015. R. 138. Appellants commenced this action on October 16, 2015, within the four-month period for challenging the promulgation of a regulation. R. 26. If Appellants had waited for a "final decision" on the application, Appellants would have lost their right to file a challenge to the Regulation because they did not get an initial response about their application until after the four-month statute of limitations had expired and because it was overwhelmingly burdensome to pursue that application process. R. 46-47.

60. Allowing the decision below to stand will effectively overturn this Court's exceptions to the exhaustion doctrine as explained in *Watergate II*. The Appellate Division's decision actually leads to an absurd economic result. Under its reasoning, any startup company involved in virtual currency business that would have wished to challenge the Regulation (either Appellants, who applied for a license, or those that left New York because they decided not to apply for a license) would be forced to endure a burdensome and expensive application process just for the chance to challenge the ultra vires nature of the Regulation. Daniel Roberts, *Behind the "Exodus" of Bitcoin Startups from New York*, FORTUNE (Aug. 14, 2015) (noting that the true costs of applying for a license under the Regulation are between $50,000 and $100,000). Under the Appellate Division's decision, attempting to comply with the prohibitive cost of challenging the ultra vires nature of a regulation would effectively eliminate the legal right of a

startup business to challenge the Regulation, rendering the *Watergate II* exceptions useless.

61. To accommodate further technological developments or new economic conditions, this Court specifically noted that the exhaustion rule is not an inflexible one. *Watergate II Apts.*, 46 NY2d at 57. The *Watergate II* decision was issued over forty years before the invention of Bitcoin. Therefore, this case raises a significantly important question as to how this rule should apply in the context of modern startups facing new regulations.

62. In addition, the Appellate Division's decision creates a glaring conflict between the First, Second, and Third Departments regarding the application of the exceptions to the exhaustion rule. Both the Second and Third Departments follow the Court of Appeals' pronouncement that exhaustion is not required where "an agency's action is challenged as either unconstitutional or wholly beyond its grant of power." *Watergate II Apts.*, 46 NY2d at 57; *see Kindlon v County of Rensselaer*, 158 AD2d 178, 180 [3d Dept 1990]; *Hamptons Hosp. & Med. Ctr., Inc. v Moore*, 74 AD2d 30, 33-34 [2d Dept 1980], *mod.*, 52 NY2d 88 [1981]. Yet, with its decision rejecting Appellants' challenge, the First Department split with the other departments in applying the *Watergate II* rule, requiring petitioners to go back through an administrative application process even where the petition specifically alleges ultra vires acts. *See Community Sch. Bd. Nine v Crew*, 224 AD2d 8, 13 [1st Dept 1996]. Further demonstrating the First Department's divergence with other departments, this Court affirmed, in the instant action, the Supreme Court's patently incorrect addition of an irreparable harm requirement to the ultra vires exception. *See Chino v NY Dept. of Fin. Servs.*, 58 Misc 3d 1203(A) [Sup Ct, NY County 2017] ["Moreover, even if an ultra vires or unconstitutional action were at issue, petitioner has not shown that DFS has caused it irreparable harm."].

Conclusion

63. For all of the foregoing reasons, and for the reasons set forth in Appellants' main and reply briefs filed in the Appellate Division, this Court should grant Appellants leave to appeal to this Court from the Decision and Order of the Appellate Division, First Department, dated April 23, 2019.

Dated: September 17, 2019
New York, New York

Pierre Ciric
THE CIRIC LAW FIRM, PLLC
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New York, NY 10009
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Tel: (212) 260-6090
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Attorney for Plaintiffs-Petitioners-Appellants

EXHIBIT “A”

Renwick, J.P., Gische, Webber, Singh, JJ.

9076 Theo Chino, et al., Index 101880/15
Plaintiffs-Petitioners-Appellants,

-against-

The New York Department of Financial Services, et al.,
Defendants-Respondents-Respondents.

The Ciric Law Firm, PLLC, New York (Pierre Ciric of counsel), for appellants.

Letitia James, Attorney General, New York (Eric R. Haren of counsel), for respondents.

Judgment, Supreme Court, New York County (Carmen Victoria St. George, J.), entered on or about December 21, 2017, granting respondents' motion to dismiss the proceeding, and denying petitioners' motion seeking discovery, unanimously affirmed, without costs.

This action arises from petitioners' application for a license pursuant to 23 NYCRR § 200.3(c)(2), pertaining to virtual currency. DFS neither approved nor rejected the application because the information petitioners provided was so sparse that no determination could be made, including whether the business activity plaintiffs were seeking to engage in required licensing under the challenged regulation. Petitioners never sought to provide the missing information; nor did they ever pay the

required licensing fee. Petitioners neither exhausted their administrative remedies, nor demonstrated applicability of one of the exceptions to the doctrine of exhaustion (*see Watergate II Apts. v Buffalo Sewer Auth.*, 46 NY2d 52, 57 [1978]; *Sohn v Calderon*, 78 NY2d 755, 767 [1991]; *Martinez 2001 v New York City Campaign Fin. Bd.*, 36 AD3d 544, 548-549 [1st Dept 2007]). As for their direct constitutional claims, the motion court correctly determined that petitioners lack standing, as they failed to show some actual or threatened injury to a protected interest by reason of the operation of an unconstitutional feature of the regulation at issue (*Cherry v Koch*, 126 AD2d 346, 351 [2d Dept 1987], *lv denied* 70 NY2d 603 [1987]). Indeed, any injury suffered by petitioners was self-created, by abandonment of the licensing process after submission of an incomplete application. Their motion seeking discovery was properly denied as moot.

We have considered petitioners' remaining contentions and find them unavailing.

THIS CONSTITUTES THE DECISION AND ORDER
OF THE SUPREME COURT, APPELLATE DIVISION, FIRST DEPARTMENT.

ENTERED: APRIL 23, 2019

CLERK

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EXHIBIT “B”

STATE OF NEW YORK
OFFICE OF THE ATTORNEY GENERAL

LETITIA JAMES
ATTORNEY GENERAL

BARBARA D. UNDERWOOD
SOLICITOR GENERAL
DIVISION OF APPEALS & OPINIONS

August 15, 2019

Pierre Ciric, Esq.
The Ciric Law Firm, PLLC
17A Stuyvesant Oval
New York, NY 10009

Re: *Chino, et al. v. NYS Dept. of Financial Services, et al.*, No. 181880/15

Dear Mr. Ciric:

Please take notice that the enclosed is a true and correct copy of the Decision and Order on Motion entered on August 13, 2019 by the Office of the Clerk of the Appellate Division, First Department in *Chino, et al. v. NYS Dept. of Financial Services, et al.*, No. 181880/15.

Please be advised that service of a cover letter together with an order or judgment constitutes service of that order or judgment with notice of entry. *Norstar Bank of Upstate N.Y. v. Office Control Sys., Inc.*, 78 N.Y.2d 1110 (1991).

Sincerely,

Eric R. Haren
Special Counsel to the Solicitor General
212-416-8804

Encl.

At a Term of the Appellate Division of the Supreme Court held in and for the First Judicial Department in the County of New York on August 13, 2019.

PRESENT: Hon. Dianne T. Renwick, Justice Presiding,
Judith J. Gische
Troy K. Webber
Anil C. Singh, Justices.

Theo Chino, et al.,
Plaintiffs-Petitioners-Appellants,

-against-

M-2829
Index No. 101880/15

The New York Department of Financial Services, et al.,
Defendants-Respondents-Respondents.

Plaintiffs-petitioners-appellants having moved for leave to appeal to the Court of Appeals from the decision and order of this Court, entered on April 23, 2019 (Appeal No. 9076),

Now, upon reading and filing the papers with respect to the motion, and due deliberation having been had thereon,

It is ordered that the motion is denied.

ENTERED:

CLERK

EXHIBIT “C”

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

Theo Chino and Chino LTD,

Plaintiffs-Petitioners,

- against -

The New York State Department of Financial Services and Maria T. Vullo, in her official capacity as Superintendent of the New York State Department of Financial Services,

Defendants-Respondents.

Notice of Entry

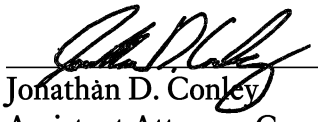
Index No. 101880/2015

PLEASE TAKE NOTICE that the enclosed is a true copy of a court order and decision in the above-captioned matter, dated December 21, 2017, and duly entered in the office of the Clerk of the Supreme Court of the State of New York, County of New York, on December 27, 2017.

Dated: New York, New York
January 14, 2018

Respectfully submitted,

ERIC T. SCHNEIDERMAN
Attorney General of the
State of New York
Counsel for Defendants-Respondents



Jonathan D. Conley
Assistant Attorney General
120 Broadway, 24th floor
New York, New York 10271
Tel.: (212) 416-8108

SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: HON. CARMEN VICTORIA ST. GEORGE J.S.C.
Justice

PART 34

Index Number : 101880/2015
CHINO, THEO
vs
DEPARTMENT OF FINANCIAL
Sequence Number : ~~003~~ 001
COMPEL

INDEX NO. _____
MOTION DATE _____
MOTION SEQ. NO. _____

The following papers, numbered 1 to _____, were read on this motion to/for _____

Notice of Motion/Order to Show Cause — Affidavits — Exhibits	No(s). 3; 12-13
Answering Affidavits — Exhibits Cross-Motion + Reply	No(s). 14-19; 33-34
Replying Affidavits	No(s). 20-23

Upon the foregoing papers, it is ordered that ~~this motion is~~ the cross-motion to dismiss is granted and the case is dismissed pursuant to the accompanying decision. The Clerk is directed to enter judgment accordingly.

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

Dated: 12/21/2017

_____, J.S.C.
HON. CARMEN VICTORIA ST. GEORGE

1. CHECK ONE: ..... ☒ CASE DISPOSED ☐ NON-FINAL DISPOSITION
2. CHECK AS APPROPRIATE: .....MOTION IS: ☒ GRANTED (cross-motion) ☐ DENIED ☐ GRANTED IN PART ☐ OTHER
3. CHECK IF APPROPRIATE: ..... ☐ SETTLE ORDER ☐ SUBMIT ORDER
☐ DO NOT POST ☐ FIDUCIARY APPOINTMENT ☐ REFERENCE

SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY: IAS PART 34

----------X

THEO CHINO and CHINO LTD,

Plaintiffs-Petitioners,

-against-

THE NEW YORK DEPARTMENT OF FINANCIAL SERVICES and MARIA T. VULLO, in her official Capacity as the Superintendent of the New York Department of Financial Services,

Respondents,

----------X

Index No. 101880/2015

Decision, Order and Judgment

Motion Sequence No. 001

CARMEN VICTORIA ST. GEORGE, J.S.C.:

In this Article 78 proceeding, motion sequence number 001, plaintiffs-petitioners Theo Chino and Chino Ltd (collectively, petitioner) seek the following relief against defendants-respondents The New York Department of Financial Services and Maria T. Vullo, in her capacity as the Superintendent of the Department (collectively, respondent): a) an order enjoining and permanently restraining DFS from enforcing Title 23, Chapter 1, Part 200 of the New York Codes, Rules, and Regulations (NYCRR), which went into effect on June 24, 2015; b) a declaration that Part 200, which regulates virtual currency, violates the separation-of-powers doctrine in that it delegates to DFS the authority to promulgate the regulation; c) an order enjoining and restraining implementation of the regulation on the ground that it is arbitrary and capricious; d) an order enjoining and restraining implementation on the ground that federal law preempts the regulation; e) an order setting aside the regulation as being made in violation of law; f) a declaration that DFS exceeded its jurisdiction; g) a declaration that the law is preempted; and h) granting Chino

monetary relief, attorney's fees, costs, and interest. DFS makes a pre-answer motion to dismiss on the bases that 1) petitioner lacks standing to challenge the legislation, 2) the challenged regulation is not arbitrary and capricious, and 3) federal law does not preempt the regulation. Separately, as motion sequence number 003, Chino moves to compel limited discovery and to hold DFS's cross-motion to dismiss in abeyance pending the completion of that discovery.[1] For the reasons below, the Court grants the cross-motion to dismiss the petition and denies the motion for limited discovery as moot.

BACKGROUND

Bitcoin is an electronically based and mathematically created currency, or cryptocurrency, which was invented by Satoshi Nakamoto,[2] following the publication of Satoshi Nakamoto's essay titled "Bitcoin: A Peer-to-Peer Electronic Cash System" (https://bitcoin.org/bitcoin.pdf). Bitcoins are released into cyberspace according to a mathematically predetermined system. Under the current protocol, bitcoin circulation will be capped at 21 million. A peer-to-peer user network regulates bitcoin, eliminating central entities such as banks. In addition, to ensure the legitimacy of transactions, individuals or entities called "miners" identify and verify the bitcoins used in the transactions. Miners block groups of these verified transactions together in "blockchains," recording the blockchains online on a shared public ledger. According to *Mastering Bitcoin: Unlocking Digital Cryptocurrencies* (Andreas M. Antonopoulos [2014] [avail at http://chimera.labs.oreilly.com/books/1234000001802/ch01.html]), to which petitioner cites for various principles, the formulas and algorithms "form the basis of a digital money ecosystem" that

[1] Chino refers to this as a "cross-motion," but it is a separately filed motion. The Court also has before it pleadings and documents filed by Chino prior to his retention of counsel, but they are not relevant to the resolution of the cross-motion

[2] Nakamoto is a pseudonym, and the actual identity of the author remains unknown.

can "do just about anything that can be done with conventional currencies, including buy and sell goods, send money to people or organizations, or extend credit" (*Id.*, Chapter 1, Introduction: What is Bitcoin?).

According to respondents, the State legislature merged the State's banking and insurance departments, creating DFS, in 2011 in reaction to the 2008 financial crisis. The Financial Services Law (FSL) empowers DFS to regulate and supervise specified financial products and services as well as those who provide them. Among other things, DFS used this power to create a regulation governing virtual money businesses (Title 23, Chapter 1, Part 200 of the NYCRR [the regulation]). The regulation went into effect on June 24, 2015.

The regulation defines virtual currency broadly, and includes all digital units of exchange that:

> (1) have a centralized repository or administrator;
> (2) are decentralized and have no centralized repository or administrator; or
> (3) may be created or obtained by computing or manufacturing effort. Virtual currency shall not be construed to include any of the following:
> (i) digital units that:
> *(a)* are used solely within online gaming platforms;
> *(b)* have no market or application outside of those gaming platforms;
> *(c)* cannot be converted into, or redeemed for, Fiat Currency[3] or Virtual Currency; and
> (ii) may or may not be redeemable for real-world goods, services, discounts, or purchases; digital units that can be redeemed for goods, services, discounts, or purchases as part of a customer affinity or rewards program with the issuer and/or other designated merchants or can be redeemed for digital units in another customer affinity or rewards program; or
> (iii) digital units used as part of Prepaid Cards.

[3] Fiat Currency includes any currency that is recognized by the government as legal tender but is not backed by a physical commodity such as gold.

(Regulations of the Superintendent of Financial Services: Virtual Currency [23 NYCRR] § 200.1 [p]).

Virtual currency business activity includes the following conduct involving New York or a resident of New York:

> (1) receiving Virtual Currency for Transmission or Transmitting Virtual Currency, except where the transaction is undertaken for non-financial purposes and does not involve the transfer of more than a nominal amount of virtual currency;
> (2) storing, holding, or maintaining custody or control of Virtual Currency on behalf of others;
> (3) buying and selling Virtual Currency as a customer business;
> (4) performing Exchange Services as a customer business; or
> (5) controlling, administering, or issuing a Virtual Currency.

(*Id.*, at § q).

In addition, pursuant to 23 NYCRR § 200.3 (a), anyone engaged in virtual currency business activity must first obtain a license. The following section, 23 NYCRR § 200.4 (a), states that the application, which must be accompanied by a $5,000 fee (*see* 23 NYCRR § 200.5), must include:

> (1) the exact name of the applicant, including any doing business as name . . .;
> (2) a list of all the applicant's Affiliates and an organization chart illustrating [their] relationship [to] the applicant . . .;
> (3) a list of . . . each individual applicant and each director . . . including such individual's name, physical and mailing addresses, and information and documentation regarding such individual's personal history, experience, and qualification, which shall be accompanied by a form of authority, executed by such individual, to release information to the Department;
> (4) a background report prepared by an independent investigatory agency acceptable to the superintendent for each individual applicant, and each Principal Officer, Principal Stockholder, and Principal Beneficiary of the applicant, as applicable;

(5) for each individual applicant . . . and for all individuals to be employed by the applicant who have access to any customer funds, whether denominated in Fiat Currency or Virtual Currency:
(i) a set of completed fingerprints. . . for submission to the State Division of Criminal Justice Services and the Federal Bureau of Investigation;
(ii) if applicable, . . . processing fees [prescribed by the Superintendent] . . .; and
(iii) two portrait-style photographs of the individuals . . .;
(6) an organization chart of the applicant and its management structure . . .;
(7) a current financial statement for the applicant and each Principal Officer, Principal Stockholder, and Principal Beneficiary of the applicant, as applicable, and a projected balance sheeting and income statement for the following year of the applicant's operation;
(8) a description of the proposed, current, and historical business of the applicant . . .;
(9) details of all banking arrangements;
(10) all written policies and procedures required . . .;
(11) an affidavit describing any pending or threatened [actions or proceedings of any kind]
(12) verification from the New York State Department of Taxation and Finance that the applicant is compliant with all . . . tax obligations . . .;
(13). . . a copy of any insurance policies maintained for the benefit of the applicant, its directors or officers, or its customers;
(14) an explanation of the methodology used to calculate the value of Virtual Currency in Fiat Currency; and
(15) such other additional information as the superintendent may require.

A verification that the applicant has complied with the above requirements is considered part of the application (*see id.*, § 200.4 [b]). The Superintendent is required to rule on applications

within 90 days from the date on which the filing is "deemed by the superintendent to be complete" (*See id.*, § 200.6 [b]). The remaining provisions regulate the approved virtual currency business, requiring mandatory compliance with anti-money laundering rules, the maintenance of adequate books and records and the obligation to allow the Superintendent to inspect such records, minimum capitalization requirements, and the obligation to protect its customers' assets in several enumerated respects (*See generally* 23 NYCRR §§ 200.7-200.22).

According to petitioner, many of the requirements for virtual currency businesses do not exist in the rules applicable to "fiat currency transmitters" (Amended Verified Complaint and Article 78 Petition [Petition], ¶ 52]. These include the requirement that it maintain records of anti-money laundering programs for seven, as opposed to five, years; the requirement that it provide the identity and physical address of parties to transactions; and the requirement to report all transactions with an aggregate amount of more than $10,000. Petitioner claims that Superintendent Benjamin Lawsky, who held the position before the current Superintendent Maria T. Vullo, acknowledged that his goal was not in response to a pressing need and instead was intended to create a working model for regulated banks and insurance companies.[4]

FACTS

On November 19, 2013, petitioner, a New York resident, incorporated Chino LTD (LTD) in Delaware. With the corporation, petitioner intended to set up a business in New York that was to install Bitcoin processing services in bodegas in New York State. He applied to conduct business in New York under Business Corporation Law § 1304, as an out-of-state corporation. In addition, in March 2014, he hired an employee to sell the LTD's services. On December 31, 2014, he co-founded Conglomerate Business Consultants, Inc. (CBC), which was incorporated in New York,

[4] For the purposes of this order, the Court need not address the accuracy of this statement.

and which purchased phone minutes and created phone calling cards the bodegas also could sell using LTD's bitcoin processing services. Petitioner submits copies of his tax returns showing that LTD lost $4,367 in 2013, $59, 667 in 2015, and $30,588 in 2016. He alleges these losses are attributable to start-up costs including computer equipment, as well as marketing and other ongoing costs.

As the Court noted above (*see supra*, at p 3), the regulations governing virtual currency businesses became effective on June 24, 2015.[5] Petitioner applied for a Virtual Currency Business license on behalf of LTD on August 7, 2015. Petitioner annexes a copy of the application as Exhibit IX to his petition. He provided the name but not the address of LTD. He did not provide an authorization as required by 23 NYCRR § 200.3 (a) (3); instead, he wrote on the form that he did not authorize the release of information. He filled out some but not all financial information on the form requested, and he indicated that he had no insurance and kept no financial or accounting books. For his background report certification, he wrote: "[Could] not obtain in time." He filled out a personal information form but he refused to disclose his employment history for the last fifteen years, and he did not provide the names and addresses of past employers. He did not disclose whether he was employed by, performed services for, or had business connections with any agency or authority of the State of New York, or any institutions subject to DFS supervision. He stated he had no financial interest in any agency or authority in New York or any other state. He provided none of the required references. He stated that his high school, college, and professional or technical school information was not applicable. He refused to disclose his social

[5] In advance of the regulation's effective date, between November 2014 and June 2015, petitioner filed several Freedom of Information Law requests, hoping to clarify DFS' "process for framing the Regulation" (Petition, ¶ 62). According to the petition, DFS did not provide any information, stating the material either did not exist or was exempt from disclosure.

security number. Along with his application, he submitted a handwritten letter which requested a waiver of the $5,000 application fee based on his characterization of the size of the business, its budget, and its financial status.[6]

Petitioner initiated this proceeding, pro se, on October 16, 2015, before he received any response from DFS; he states that he did so because he realized "he would be required to incur expenses beyond his means to comply with the burdensome compliance costs under the Regulation" (Petition, ¶ 91). On January 4, 2016, DFS returned his August 7, 2015 application without processing it. The letter states that DFS could not evaluate the application because it contained "extremely limited" information and, among other things, did not describe the business in which LTD was or would be engaged and did not specify in what respect, if any, the business involved virtual currency (DFS Jan. 4, 2016 letter [Exh. XI to Petition]). The letter explained that because of this DFS could not determine whether LTD was a virtual currency business subject to the regulations. Petitioner states that CDC discontinued its bitcoin processing services at that time but LTD continued as a nonoperating business. He states LTD lost $53,053 in 2016 because of its inability to provide bitcoin services. He provides tax returns for LTD for 2016 as well as for 2013-15 to substantiate his allegation that LTD lost money during these years.

The Ciric Law Firm, PLLC, appeared on behalf of petitioner on October 31, 2016. On May 26, 2017, the parties stipulated to convert the proceeding to e-filing. Accordingly, all papers submitted on or after that date are e-filed. Petitioner amended the action/proceeding around that time, and submitted a supplement summons on August 10, 2017. Respondent filed its notice of cross-motion and supporting papers on August 15, 2017.[7] The matter was argued before this Court

[6] The petition refers to this as a request for a fee waiver under Banking Law § 18-a (6) (a).
[7] Respondents previously had cross-moved in response to the original pleadings.

FILED: NEW YORK COUNTY CLERK 12/27/2017 11:35 AM INDEX NO. 101880/2015
NYSCEF DOC. NO. 39 RECEIVED NYSCEF: 12/27/2017

on October 10, 2017, and the parties were directed to order and provide copies of the transcript, which they did the following week.

ARGUMENTS REGARDING STANDING

In their cross-motion, respondents first argue the threshold issue of standing. They point to the January 2016 letter of DFS, which not only stated that it could not determine whether LTD was engaged in a virtual currency business activity but that, by returning the application, DFS did not "offer any opinion as to whether. . . any business activity of the Company requires or would require licensing by New York" (DFS Jan. 4, 2016 letter [Exh. XI to Petition]). The letter provided petitioner with contact information for the Supervising Bank Examiner for DFS' Capital Markets Division. Respondents state that after he received the letter, petitioner did not supplement the application, did not submit a new application for CBC, and did not contact the Supervising Bank Examiner or anyone else at DFS with questions. Instead, he treated the letter as a de facto denial of his application and shut down CBC.

Based on the facts in the petition and on the January 4, 2016 letter, respondents argue, petitioner has not shown standing. They note that petitioner has the burden to establish standing (*Society of the Plastics Indus., Inc. v County of Suffolk*, 77 NY2d 761, 769 [1991]) and that without standing, this matter is not justiciable (*Roberts v Health & Hosp. Corp.*, 87 AD3d 311 [1st Dept 2011]). The party must demonstrate an injury in fact – which, in turn, requires a showing of actual harm due to the administrative action (*N.Y. State Assoc. of Nurse Anesthetists v Novello*, 2 NY3d 207, 214-15 [2004] [Novello]). Actual harm, by definition, cannot be conjectural or ephemeral, and cannot be based on a general harm but must be specific to the individual or entity asserting the claim (*Id.*). Absent such a showing, the Court of Appeals has stated, the lawsuit is "little more than an attempt to legislate through the courts" (*Rudder v Pataki*, 93 NY2d 273, 280 [1999]).

According to respondents, petitioner's failure lies in his inability to demonstrate that he has suffered an injury in fact. He has not shown that he has or is likely to sustain a cognizable injury due to the regulation, they argue, because he submitted an incomplete license application which made adequate review impossible, he began his lawsuit before DFS responded to his application, and he did not attempt to pursue his application when DFS stated he had provided insufficient information to them and they could not evaluate his application. Petitioner cannot assert standing, respondents argue, before DFS even determined whether an application was required. Instead of proceeding with the application process, respondents state, petitioner "charted a decidedly different course by preemptively halting the operations of CBC and Chino LTD and commencing this litigation" (Mem. of Law in Support of Defendants'-Respondents' Cross-Motion to Dismiss the Amended Verified Complaint and Article 78 Petition [Respondents' Mem. in Support], at p 12). Petitioner's decision to shut down his businesses does not confer standing, respondents argue, because petitioner based his decision "on the speculative assumption that their operations *might* be impacted by the Regulation" (*Id.* [emphasis in original]).

Furthermore, respondents argue that LTD's tax returns do not show any causal connection between the regulation and petitioner or LTD's financial losses, because the returns were for 2013 through 2015, and the regulation did not go into effect until the second half of the last of these three years. Thus, LTD's losses of $4,367 in 2013 and $59,667 in 2014 were entirely unrelated to the regulation. The losses of $30,588 in 2015 partly occurred prior to the effective date of the regulation and partly were due to litigation expenses. As for LTD's loss of $53,053 in 2016, respondents note that this purportedly was partly due to litigation expenses, partly because LTD remained an active business and retained its equipment operational in case it prevails in this lawsuit, and partly due to interest on the loan he used to establish his business. Respondents argue

that "these losses plainly arise from [petitioner's] decision to challenge the legality of the Regulation before determining whether it even applied to his businesses, and cannot be plausibly attributed to the Regulation going into effect" (*Id.*).

In opposition, petitioner contends that he has standing. He reiterates the arguments he set forth originally in support of his proceeding. He states that he commenced the petition/action before he received a determination from DFS because he could not afford the regulatory costs of running a virtual currency business, and that he did not respond to the January 4, 2016 letter he received from DFS "because I had already commenced this action in October 2015 and I knew this action could invalidate the Regulation. Therefore, I concluded that it was futile for me and for my business to continue the application process at this stage" (Theo Chino Aff. in Support of Opposition to Cross-Motion [Chino Aff.], at ¶ 16). He states that the January 4, 2016 "response from the Department" forced him "to abandon my Bitcoin processing business because my application *was not approved*" (*Id.*, at ¶ 15 [emphasis supplied]). Petitioner further states that respondents have not submitted documentary evidence which refutes his statement of facts. Therefore, he states, the Court must accept his asserted facts as to standing as true and rule in his favor on this threshold issue. He states that he satisfies the two-pronged test the Court of Appeals set forth in *Novello* (2 NY3d at 211). He states that the closure of his businesses demonstrates his actual harm because "it is reasonably certain that the harm will occur if the challenged action is permitted to continue" (*Police Benevolent Ass'n of N.Y. State Troopers, Inc. v Division of N.Y. State Police*, 29 AD3d 68, 70 [3rd Dept 2006] [Police Benevolent Ass'n]). Citing *New York Propane Gas Ass'n v N.Y. State Dep't of State* (17 AD3d 915, 916 [3rd Dept 2005]), he argues that he need not quantify his loss with particularity. Furthermore, he asserts, the drastic increase in LTD's financial losses following the implementation of the regulations and its accompanying

application process establishes a causal connection, and that his realization that the cost of compliance with the regulation would be prohibitive is causally connected to his decision to shutter his business. He states that he did not shut his business voluntarily but was compelled to do so by the burdens of the application process and the anticipated burden of compliance. He suggests that it was unnecessary for DFS to determine that his business qualified as a virtual currency business under the regulation because he, an expert in the field, knew that LTD was subject to the regulation.

Petitioner also claims standing with respect to his claim for declaratory relief. Relying on *Plaza Health Clubs, Inc. v New York* (76 AD2d 509 [1st Dept 1980] [finding no standing because plaintiffs contended they did not engage in any business activities proscribed by the statute]) for the proposition that the possible threat to his business activity is sufficient to confer standing with respect to this claim. The reasonable certainty of future harm, he states, is enough (*Police Benevolent Ass'n*, 29 AD3d at 70 [finding that standing existed because, due to the petitioners' violations of court orders and the court's warning that they would be held in contempt for their alleged misconduct, the asserted harm was more than speculative]).

In reply, respondents reiterate their earlier arguments. They emphasize that petitioner did not complete the application process or allow DFS to reach a final determination. They contend that petitioner's entire argument rests on the fallacy that DFS' January 4, 2016 letter constitutes a denial of petitioner's application. They challenge petitioner's proximate cause argument because petitioner stopped operating his business before DFS even determined that a license and the accompanying compliance requirements applied. DFS also did not order LTD to cease its operations, respondents point out. Moreover, they contend that petitioner's statement that compliance with the regulation would be unduly burdensome is a speculative allegation regarding anticipatory harm.

DISCUSSION

After careful consideration, the Court concludes that petitioner has no right to commence an Article 78 proceeding and lacks standing to challenge the underlying regulation.

I. Petition

Petitioner did not complete LTD's application, and did not respond to DFS' January 2016 letter which notified him of his failure to do so. Petitioner acknowledges that he abandoned the application process because of the pendency of this hybrid action/proceeding challenging the regulation (Chino Aff. in Opp. To Cross-Motion, at ¶ 16). CPLR § 7803 provides a petitioner with a means to challenge "whether a determination was made in violation of lawful procedure, was affected by an error of law or was arbitrary and capricious or an abuse of discretion" (CPLR § 7808 [3]). Moreover, "one who objects to the acts of an administrative agency must exhaust available administrative remedies before being permitted to litigate in a court of law" (*DiBlasio v Novello*, 28 AD3d 339, 341 [1st Dept 2006] [citations and internal quotation marks omitted]). Courts cannot "interject themselves into ongoing administrative proceedings until final resolution of those proceedings before the agency" (*Id.*). In the proceeding at hand, DFS did not reach a final decision. Indeed, it did not reach any decision. Accordingly, there is nothing for this Court to review.

The Court notes that an exception exists to the exhaustion requirement when the action "is challenged as either unconstitutional or wholly beyond its grant of power, when resort to an administrative remedy would be futile or when its pursuit would cause irreparable injury" (*Martinez 2001 v New York City Campaign Finance Bd.*, 36 AD3d 544, 548 [1st Dept 2007]). The exception does not apply in this instance. Again, petitioner's failure to complete his application precludes him from raising this argument. Because of his failure, the agency did not take any action

– constitutional or otherwise, and neither within nor exceeding its grant of power. The DFS letter stating more information was necessary is not an action or decision within the meaning of the governing law. Instead, it is the legislation itself that petitioner challenges here. Any irreparable injury petitioner alleges is a result of the underlying law and not of any agency action.

Moreover, even if an ultra vires or unconstitutional action were at issue, petitioner has not shown that DFS has caused it irreparable harm. LTD's tax returns show three-and-a-half years of losses prior to the initiation of this action, and show comparable losses in 2014 – prior to the existence of the regulation – due to ongoing operation expenses. Petitioner attributes the 2016 losses to ongoing operation expenses and litigation costs resulting from this proceeding. Petitioner only shows one sale dated January 4, 2016 with a $279.41 invoice to support his contention regarding lost profits. Petitioner has not shown DFS would have determined the business was subject to the regulation. Although LTD appears to have engaged in a virtual currency business and petitioner claims that it was such a business, DFS never had the opportunity to evaluate the issue because petitioner did not provide it with most of the information it sought and the application obstructed DFS' efforts to obtain further information about him or LTD.

Similarly, petitioner's application for mandamus relief under Article 78 must fail. To the extent that he brings an Article 78 proceeding it is based on a challenge to DFS' action. Here, the purported action relates to petitioner's virtual currency business certification application. Not only did he fail to complete his application, but he does not seek an order mandating the granting of the license. Instead, he challenges the underlying regulation. Article 78 is not the proper vehicle for a challenge to the constitutionality of a regulation (*Westhampton Beach Assoc., LLC v Village of Westhampton Beach*, 151 AD3d 793 [2nd Dept 2017]).

II. Action

Next, the Court examines the question of whether petitioner has standing to challenge the constitutionality of the regulation. This presents a much closer issue than that of his Article 78 proceeding. To establish standing, a plaintiff must show injury in fact, which, "[a]s the term itself implies, . . . must be more than conjectural" (*Quast v Westchester County Bd. of Elections*, 155 AD3d 674, 674 [2nd Dept 2017]). In addition, the plaintiff must establish that he or she falls within the zone of interest which the regulation impacts (*See id.*). Moreover, "personal disagreement and speculative financial loss are insufficient to confer standing" (*Roulan v County of Onandaga*, 21 NY3d 902, 905 [2013] [rejecting plaintiff's standing argument that he sustained financial harm because challenged plan caused him to be assigned fewer criminal cases]; *see New York State Psychiatric Assoc., Inc. v Mills*, 29 AD3d 1058, 1059 [3rd Dept 2006] [asserted financial harm to psychiatrists was speculative]). The issue of standing, when applicable, must be considered at the outset of the litigation (*Society of Plastics Indus. v County of Suffolk*, 77 NY2d 761, 769 [1991]). If there is no standing, a court cannot issue a declaration as to the validity of a regulation (*See Roulan*, 21 NY3d at 905).

In the proper circumstances, the argument that a regulation imposes "an unacceptable burden" on an individual or business is sufficient to establish standing (*See Doe v Axelrod*, 136 AD2nd 410 [1st Dept 1988] [concerning regulations on pharmaceutical and medical professions that allegedly interfered with ability to provide medical case, invaded patients' privacy, and violated interstate commerce clause]). If, for example, this matter involved the issue of organizational standing, or, as in *Doe v Axelrod*, a large coalition of business owners who showed harm to their business under the regulation, or an individual or business that could show the probability of financial harm, there might be a strong argument in favor of standing. Here,

however, petitioner did not apply for certification,[8] and has not shown sufficient economic loss. Any argument as to the $5,000 application fee was waived because petitioner did not pay the fee or pursue the application. His economic loss argument is otherwise insufficient because LTD has never made a profit and petitioner showed proof of only one $279.41 sale. Moreover, its losses in 2016, once petitioner thought LTD was subject to the regulation, are not inconsistent with LTD's prior financial history.

III. Motion for Limited Discovery

Petitioner's motion for limited discovery is denied as moot. The discovery petitioner requested included depositions of Nobel Prize-winning New York Times columnist Paul Krugman and former DFS chair Benjamin Lawsky, and any documentary evidence relevant to respondents' conclusion that bitcoin is a financial product or service within the meaning of the regulation. None of the proposed discovery relates to the standing issue. Moreover, the Court notes that even if it had reached the issue of whether bitcoin should be governed by the regulation, it would have concluded that this discovery was unwarranted. It was not necessary to depose Paul Krugman and Benjamin Lasky, or to examine the entire history behind DFS' determination that bitcoin is a financial product governed by the regulation. Instead, the issue is the impact of the regulation on petitioner and other virtual currency businesses, and the discovery he seeks is not relevant to that issue. Petitioner has not provided – or argued that he attempted to provide – any pertinent evidence supporting this critical contention.

[8] The application form he submits here, with so much of the critical information absent and without allowing for further examination by DFS, cannot be considered an application, especially when petitioner abandoned his attempt to obtain certification prior to his receipt of the DFS January 2016 letter.

CONCLUSION

For the reasons above, the Court need not reach the other issues. Accordingly, it is

ORDERED that the cross-motion to dismiss which is part of motion sequence number 001 is granted and therefore the petition, also part of motion sequence number 001, is dismissed; and it is further

ORDERED that motion sequence number 003, which seeks limited pre-joinder discovery, is denied as moot.

Dated: 12/21, 2017

ENTER:

CARMEN VICTORIA ST. GEORGE, J.S.C.

HON. CARMEN VICTORIA ST. GEORGE
J.S.C.