

September 20, 2022

## **Client Update: California advances new Digital Financial Assets Law**

### Client Updates

## California Advances New Digital Financial Assets Law

At the end of August 2022, the California State Assembly and the state Senate passed [the Digital Financial Assets Law](#) ("**Law**" or "**Bill**"). The recently passed Bill sets a regulatory framework for crypto companies wishing to operate in the State of California and conduct business with its residents.

The Bill is still subject to the signature of the Governor of California, and following such signature is expected to come into force on January 1<sup>st</sup> 2025.

Under the framework of the new Law, a person will be prohibited from engaging in digital financial asset business activity or holding itself out as being able to engage in such activity, with or on behalf of a resident of California, unless such person meets all the requirements set out in the Law including the newly obligation of being licensed with the Department of Financial Protection and Innovation ("**Department**").

The Law authorizes the Department to conduct examinations of licensees and to take enforcement measures against a licensee or a person that is not a licensee but is engaging in digital financial asset business activity materially violating the Law, a rule adopted or an order issued under the Law, or of other laws of the State of California that applies to such activities, with, or on behalf of, a resident. In addition, the Law prescribes civil penalties for violations of its provisions.

A digital financial asset is defined in the Law as a "**digital representation of value that is used as a medium of exchange, unit of account, or store of value, and that is not legal tender, whether or not denominated in legal tender.**" The definition has some exemptions, for instance, it does not include certain types of virtual coins used solely within a gaming platform.

The Law also includes extensive definition of digital financial asset business activity: (a) Exchange, transfer, storage or engagement in digital financial asset administration, whether directly or through an agreement with a digital financial asset control services vendor; (b) Holding electronic precious metals or electronic certificates representing interests in precious metals on behalf of another person or issuing shares or electronic certificates representing interests in precious metals; (c) Exchanging one or more digital representations of value used within one or more online games, game platforms, or family of games for

either of the following:

- (1) A digital financial asset offered by or on behalf of the same publisher from which the original digital representation of value was received.
- (2) Legal tender or bank or credit union credit outside the online game, game platform, or family of games offered by or on behalf of the same publisher from which the original digital representation of value was received.

The Law also sets several rules in connection to stablecoins, which [as we previously updated](#), have been getting attention from various regulators. Stablecoins are defined as "a digital financial asset that is denominated in United States dollars or pegged to the United States dollar or denominated in or pegged to another national or state currency and is issued with a fixed nominal redemption value with the intent of establishing a reasonable expectation or belief among the general public that the instrument will retain a nominal redemption value that is so stable as to render the nominal redemption effectively fixed."

The Law clearly states that until January 1<sup>st</sup> 2028, the exchange, transfer, storage or engagement in digital financial asset administration with regard to stablecoins, whether directly or through an agreement with a digital financial asset control services vendor - is prohibited, unless the following combined conditions are answered:

- (a) The issuer of the stablecoin is licensed accordingly or is a bank.
- (b) The issuer of the stablecoin at all times owns eligible securities having an aggregate market value of not less than the aggregate amount of all of its outstanding stablecoins issued or sold in the US.

The Law is expected to play a significant role in the shaping of the crypto policy in California and will surely affect crypto companies operating in the state or conducting business with its residents. It is therefore important for such companies to start preparing for taking appropriate steps to comply with the expected regulatory framework.

Please feel free to contact us with any questions that you have on this matter.

\*This client update is designed to provide general information only, is not a full or complete analysis of the matters presented, and may not be relied upon as legal advice

## Key Contacts



**Timor Belan**  
Partner



**Avital Haitovich**  
Senior Associate