

# **Bond Case Briefs**

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## **Fitch: Cryptocurrency Poses Risks, Opportunities for US Public Finance**

Fitch Ratings-Chicago/Austin/New York-19 October 2021: A limited number of US public finance issuers are encouraging cryptocurrency (crypto) ventures and exploring the use of crypto as a form of exchange to grow economies and promote efficiencies, but this can expose issuers to a still-evolving economic and regulatory environment, Fitch Ratings says. Public entities have so far typically been recipients of crypto that is converted to cash.

Crypto offers ease and speed of transfer of value, relative to settlement through the conventional US financial system. Because crypto transactions are conducted via distributed ledger technology (DLT), payments can be automatically executed once conditions of the contract recorded on the electronic ledger are met.

However, cryptocurrency can introduce financial and operating risks, particularly as a result of price volatility. The lack of an overarching regulatory framework in the US and other countries contributes to market uncertainty, with changes in regulations potentially affecting value. Increased crypto investment holdings could negatively affect budgets and the ability to pay obligations if there are material price swings. Most municipalities' investment guidelines are typically governed by state statutes, which may allow for crypto investments as regulation develops. In contrast, pension fund investment guidelines are typically at the discretion of the funds' boards or their designees and allow a much broader range of options.

Crypto use will likely require new IT spending, including reinforcing cybersecurity. The rapid rise in the market values of cryptocurrencies, such as Bitcoin, has made them an attractive target for cyber criminals. The nascent global crypto regulatory environment and transaction anonymity contributes to the increased risk of cybercrime and ransomware attacks.

Issuers focused on environmental effects may view the energy-intensive computing power required for the proof-of-work consensus mechanism to validate transactions and mine coins such as bitcoin as detrimental to environmental, social and governance (ESG) goals. Furthermore, social and governance issues may arise from crypto payments or donations from anonymous sources that could create risks for public entities.

Public finance interest in cryptocurrency is not new. Ohio became the first state in 2018 to allow companies to pay taxes in crypto. A third-party processor converted the payment to US dollars, which would then be deposited into a state account. Within a year the program was suspended, with the Ohio State Attorney General citing legal prohibitions against the use of a payment processor to convert cryptocurrency into US dollars for the electronic payment of taxes. Ohio has left the door open to future use.

State and local governments have taken different approaches to crypto, with some cultivating the crypto market by establishing accommodative legal frameworks. Two Texas laws established a working group on blockchain technology and updated the state's Uniform Commercial Code to

recognize crypto. Wyoming passed laws that explicitly exempt virtual currencies from state money transmission laws and permits state-chartered depositories to provide banking services to virtual currency companies. Rhode Island and New York introduced crypto regulations.

Miami accepts donations from CityCoin, a non-profit opensource protocol. CityCoin allows users to mine “MiamiCoins”, which are not affiliated or endorsed by the city. Thirty percent of the contributions submitted by miners is converted to US dollars and transferred to the city. The protocol generated several million for the city since its inception. Miami is not permitted to hold or invest in crypto under current state law.

Not-for-profit healthcare and higher education entities have begun to receive donations in the form of crypto, potentially tapping a new philanthropic base. Many opt to liquidate immediately to avoid the risk of volatility, and crypto remains a small percentage of total giving. Technological infrastructure and a clear policy framework are necessary to accept and process these donations.

#### Related Research:

- [FinTechs, Financial Institutions Balance Risks, Rewards of Crypto \(October 2021\)](#)
- [Digital Assets to Become More Institutionalized in US Financial Sector \(September 2021\)](#)

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