



New York Attorney General Launches Inquiry into Cryptocurrency Exchanges

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On April 17, 2018, New York Attorney General Eric T. Schneiderman (the “NY AG”) launched the “Virtual Markets Integrity Initiative” (the “Initiative”), a fact-finding inquiry into the policies and practices of platforms used by consumers to trade virtual currencies like bitcoin and ether.

As part of a broader effort to protect cryptocurrency consumers, the Attorney General’s office sent letters to thirteen major virtual currency trading platforms requesting key information on their operations, internal controls, and safeguards to protect consumer assets.

In his Inquiry letters, the NY AG acknowledges that a balance must be struck between protecting consumers without stifling new, innovative solutions to consumer needs, wants, or demands. Accordingly, the Initiative seeks to increase transparency and accountability as it relates to the platforms consumers rely on to trade virtual currency, offering consumers better disclosure pertaining to volatility and risk, and to better inform enforcement agencies, to avoid overly-broad regulatory restrictions in the future.

Ensuring that enforcement agencies, investors, and consumers have the information they need to understand the practices and the risks on these platforms is critical, given recent news reports of trading outages, consumers having difficulty accessing their funds, funds being lost due to cyber-attacks, and the potential for market manipulation. Often, the platforms lack the basic market protections of traditional investing platforms. Moreover, the extent of disclosures to customers about trading rules, internal controls, and other basic practices varies from platform-to-platform, making it difficult for consumers to evaluate the actual risks of trading on a particular platform.

The Initiative stems from the NY AG’s duty to protect consumers and ensure the fairness and integrity of the financial markets. Before

trading on a new platform, sophisticated investors routinely demand robust disclosures, allowing them to assess the platform's operations and the adequacy of its policies and internal controls. The questionnaire delivered to the virtual currency platforms asks for similar information so that average investors can better understand the risks and protections.

The questionnaires ask the platforms to disclose information falling within six major topic areas, including:

- Ownership and Control (including disclosing beneficial owners of more than 5% of the platform)
- Basic Operation and Fees (all jurisdictions where consumers live, lists of all currencies transacted, and fees)
- Trading Policies and Procedures (how trading works, use of trading bots)
- Outages and Other Suspensions of Trading (outage history and remedial procedures)
- Internal Controls (i.e. preventing insider trading activities)
- Privacy and Money Laundering (AML/KYC procedures and safeguards)
- Protection Against Risks to Consumer Funds (capital accounts or insurance policies), and
- Written Materials (such as platform terms and conditions, NY BitLicense applications, and cyber policies/procedures).
- The NY AG's full questionnaire is [available here](#).

The Investor Protection Bureau of the Office of the NY AG sent letters to the following virtual currency trading platforms:

- Coinbase, Inc. (GDAX)
- Gemini Trust Company
- bitFlyer USA, Inc.
- iFinex Inc. (Bitfinex)
- Bitstamp USA Inc.
- Payward, Inc. (Kraken)
- Bittrex, Inc.

- Circle Internet Financial Limited (Poloniex LLC)
- Binance Limited
- Elite Way Developments LLP (Tidex.com)
- Gate Technology Incorporated (Gate.io)
- itBit Trust Company
- Huobi Global Limited (Huobi.Pro).

The full text of the letters sent to the trading platforms is copied below.

We write on behalf of the New York State Office of the Attorney General (“OAG”) to request the participation of [company] in OAG’s Virtual Markets Integrity Initiative, which seeks to protect the interests of New York residents who trade virtual currency and related investment products.[1] OAG is asking major virtual currency trading platforms (often referred to as “exchanges”) to respond to a questionnaire addressing key aspects of their operations, including their fee structure, their internal controls, and the measures they take to safeguard funds in customer accounts.[2] Through this Initiative, OAG seeks to increase transparency and accountability in the virtual currency marketplace—and better inform the actions of enforcement agencies, investors, and consumers in this space.

As you know, bitcoin, ether, and other virtual currencies have captured the imagination of millions of people worldwide. Representing a technological advance, a medium of exchange, and an investment opportunity all at once, virtual currencies are inspiring innovators, entrepreneurs, and investors—and are fueling an increasingly diverse ecosystem of companies and applications. But virtual currency is also a highly speculative sector, featuring significant volatility, instability, and risk. Moreover, published reports indicate the sector has attracted fraudsters, market manipulators, and thieves. As the State’s chief law enforcement agency, OAG is responsible for protecting consumers and investors from these bad actors and ensuring the fairness and integrity of New York’s financial markets.[3] See, e.g., N.Y. Exec. Law § 63(12); N.Y. Gen. Bus. Law § 349; N.Y. Gen. Bus. Law § 352.

As with other emerging sectors, the challenge with virtual currency is to prevent fraud and other abuses, safeguard market integrity, and protect individual investors—without stifling legitimate market activity or innovation. OAG’s Virtual Markets Integrity Initiative seeks to advance these objectives by promoting meaningful transparency, accountability, and the opportunity for government agencies, consumer advocates, and investors to compare the policies, procedures, and protections of virtual currency platforms. Sophisticated investors routinely require privately-owned trading venues on which they are considering trading to furnish robust disclosures about their operations, policies, and internal controls so that they can evaluate the risks of trading on a given platform. The enclosed questionnaire asks [company] to supply similar information, for the benefit of not only professional investors and financial firms, but all consumers who may trade virtual currency on platforms, so that they better understand their operations and the associated risks.

The topics set forth in our questionnaire address fundamental aspects of your operations or issues that have already attracted significant public attention. Indeed, many may be covered in your web disclosures or regulatory filings. They range from your platform’s basic trading rules, to the policies and safeguards you have implemented to prevent conflicts of interest, fraud, and illegality; address the operation of bots; and protection of customer assets from theft and other risks. We will review and assess your responses, compare them with those of other platforms, and disclose certain information in a publicly accessible format.[4] As part of this disclosure, we will identify any platforms that decline to provide meaningfully complete responses.

We kindly ask that you provide detailed and clear responses for each topic, as well as a contact from whom we can seek supplemental information, as necessary. Please complete the enclosed questionnaire and return your responses to our attention no later than May 1, 2018. In the event you have any questions or concerns, please do not hesitate to reach out to us.

Sincerely,

Simon G. Brandler, Senior Advisor & Special Counsel

*John D. Castiglione, Asst. Attorney General, Investor Protection
Bureau*

[1] As used here and in the enclosed questionnaire, “Virtual Currency” and other terms have the same meanings as set forth in 23 NYCRR § 200.2 (Definitions).

[2] We are aware that certain trading platforms have formal rules barring access in New York and may not have a license to engage in virtual currency business activity in New York. Among other topics, we are asking platforms to describe their measures for restricting trading from prohibited jurisdictions.

[3] This role is separate from, but complementary to, that of New York State’s Department of Financial Services, which established a first-in-the-nation licensing protocol that requires virtual currency trading platforms and other firms engaged in virtual currency business activities to receive approval to operate and follow certain regulatory requirements.

[4] You may designate and request confidential treatment for the portion of any response that contains a valid trade secret or may otherwise be exempt from disclosure under New York’s Freedom of Information Law. N.Y. Pub. Off. Law §§ 87(2)(a)–(d).

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