**Cryptocurrency as Collateral in Financing**

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Bitcoin’s rise in popularity has disrupted many areas of commercial law. Agencies and industries have spent the last few years trying to classify cryptocurrencies using current formalities, which has proven difficult given the unique characteristics of cryptocurrencies[[1]](#footnote-1) and the growing distinction between coins and tokens. Classification under the Uniform Commercial Code (UCC) is no different. The uncertainty around UCC classification is an issue for secured lenders who need to ensure that any security interest in cryptocurrency is properly perfected. Without judicial clarification or formal changes to the UCC, the appropriate classification of cryptocurrencies under the UCC for perfection purposes is at best a question of informed speculation.

Although commentators argue that cryptocurrencies likely fall under the UCC’s catchall category of “general intangible,”[[2]](#footnote-2) not all cryptocurrencies serve the same function. The underlying function and origination of the cryptocurrency is what distinguishes coins from tokens. But there is no bright line, and many cryptocurrencies can incorporate characteristics of both. Coins are generally used as a method of exchange, created from their own native blockchain and given as a reward or payment for the recipient’s services.[[3]](#footnote-3) Utility tokens, however, are created on existing blockchains and are often distributed through initial coin offerings (ICOs) as a means for raising capital.[[4]](#footnote-4) Tokens “are designed for, and have, a clear and intended use” apart from simply serving as a unit of value.[[5]](#footnote-5) For example, a token can convey or evidence voting or participation rights in an organization or grant the owner access to certain application features.[[6]](#footnote-6)

Whether cryptocurrency functions solely as a method of exchange or participation in an issuer of property can have a huge impact on its classification under the UCC. Because Bitcoin rose in popularity as a unit of value, the initial instinct is to classify cryptocurrencies as “money,” which is defined in the UCC as “a medium of exchange currently authorized or adopted by a domestic or foreign government.”[[7]](#footnote-7) However, because no government has authorized or adopted any cryptocurrency, it is difficult to argue that it should be treated as “money” for UCC classification purposes. Further, cryptocurrencies are not represented by a physical, tangible object, so perfection by possession as required under UCC § 9-312 is not practically possible.

Within the confines of Article 9 of the UCC, the most logical classification category is the catchall “general intangibles,” which includes any personal property that does not fall into any of the specifically enumerated categories.[[8]](#footnote-8) Further, classification as a general intangible means that a security interest in cryptocurrency will continue even if the cryptocurrency is sold, exchanged or otherwise disposed of, and will attach to any identifiable proceeds of the cryptocurrency.[[9]](#footnote-9) This classification provides some assurance to secured lenders because perfection is easily obtained through filing a financing statement, and the security interest will survive even if the cryptocurrency is transferred to multiple third parties. Such classification, however, raises issues. Because the nature of most cryptocurrencies involves anonymity in ownership, enforcing a security interest in cryptocurrency that has been transferred is practically impossible.[[10]](#footnote-10) Commentators have also argued that classifying cryptocurrencies as general intangibles has negative implications on their utility as a method of payment because of limited negotiability.[[11]](#footnote-11)

The growing distinction between coins and tokens also begs the question of whether cryptocurrencies can fall under one UCC classification or should be classified based on their use or purpose. This is particularly relevant for tokens or cryptocurrencies that are generated through ICOs and represent a participatory interest in a business enterprise. Article 8 of the UCC contains another classification that may be better suited for these types of tokens. Namely, a “Security” under UCC § 8-102(15) is a “share, participation, or other interest in an issuer” that is of a class or series of shares, is certificated or uncertificated, and is either traded on a securities exchange or market or is a “medium for investment” that expressly states that it is a “security” under Article 8.[[12]](#footnote-12) The initial problem with defining cryptocurrencies as a security is that traditional coins, such as Bitcoin, do not have an “issuer” creating the coin.[[13]](#footnote-13) But with tokens, the company holding the ICO generally *issues* a token to investors as a means of raising capital or achieving its corporate goals.

The next steps required for perfection depend on the token’s characteristics. Section 9-313(a) permits perfection of “certificated securities” by “taking delivery.”[[14]](#footnote-14) Delivery occurs when a person (either directly or through a third-party “securities intermediary”[[15]](#footnote-15)) “acquires possession of the security certificate.”[[16]](#footnote-16) Alternatively, and for uncertificated securities, perfection is obtained through control,[[17]](#footnote-17) a process that depends on whether a securities intermediary is involved. Because effective “control” over a token may require access to or possession of the relevant encryption key to access the token, if a token is treated as an uncertificated security, then unique issues are raised to ensure that the secured party will have control over the token.

Cryptocurrency technology continues its rapid evolution, and the development and use of coins and tokens has followed suit. For lenders seeking to perfect collateral interests in cryptocurrency assets, the safest bet is to consider those assets general intangibles. However, lenders should be particularly prudent in cases where cryptocurrency assets make up the majority of the facility’s collateral, or where the cryptocurrency has characteristics that may fall within the token category. In such cases, determining how to properly perfect a security interest requires further investigation into the tokens themselves and a determination of how to gain control over them.

1. The term “cryptocurrency” is used through this article to refer to all currencies deriving from a blockchain protocol, whether considered a token, coin or otherwise. [↑](#footnote-ref-1)
2. *See* George K Fogg,“The UCC and Bitcoins – Solution to Existing Fatal Flaw,” *Bloomberg BNA* (April 14, 2015), *available at* www.perkinscoie.com/en/news-insights/the-ucc-and-bitcoins-solution-to-existing-fatal-flaw.html. S*ee also* Jean L. Schroder, “Bitcoin and the Uniform Commercial Code,” 24 *U. Miami Bus. L. Rev.* 1, 10 (2016), *available at* repository.law.miami.edu/umblr/vol24/iss3/ (citing Fogg, *supra* note 2); Bob Lawless, “Is UCC Article 9 the Achilles Heel of Bitcoin?,” Credit Slips (Mar. 10, 2014), *available at* www.creditslips.org/creditslips/2014/03/isucc-article-9-the-achilles-heel-of-bitcoin.html#more. [↑](#footnote-ref-2)
3. *See generally* Ray King, “Token vs. Coin: What’s the Difference?,” Bitdegree, *available at* www.bitdegree.org/tutorials/token-vs-coin/ (last updated Nov. 9, 2018) (providing examples and explanations of the difference between coins and tokens). [↑](#footnote-ref-3)
4. *See id*. [↑](#footnote-ref-4)
5. Douglas Pepe, “Are Blockchain Utility Tokens Securities?,” *Law360* (July 24, 2018), *available at* www.law360.com/articles/1066435/are-blockchain-utility-tokens-securities-. [↑](#footnote-ref-5)
6. King, “Token vs. Coin,” *supra* note 3 (referencing Musicoin as an example that gives its holders access to certain features on the Musicoin Platform, such as streaming music). *But see* Dean Seal, “SEC Hasn’t Shown Crypto Tokens Are Securities, Judge Says,” *Law360* (Nov. 27, 2018), *available at* [www.law360.com/articles/1105406/sec-hasn-t-shown-crypto-tokens-are-securities-judge-says](https://www.law360.com/articles/1105406/sec-hasn-t-shown-crypto-tokens-are-securities-judge-says) (discussing a recent case in which a federal judge found that the SEC had not demonstrated that a token offered through an ICO was a “security”). [↑](#footnote-ref-6)
7. U.C.C. § 1-201(a)(24) (2010). [↑](#footnote-ref-7)
8. U.C.C. § 9-102(a)(43) (2010). [↑](#footnote-ref-8)
9. U.C.C. § 9-315(a) (2010). [↑](#footnote-ref-9)
10. *See, e.g.,* *Schroeder*, *supra* note 2, at 30-43 (arguing that if Bitcoin falls under “general intangibles” category, the negative implications arise because security interest continues). [↑](#footnote-ref-10)
11. *See* *Schroeder*, *supra* note 2, at 41 (arguing that proceeds security interest in bitcoins limits their negotiability and utility as a currency or payment system); *Fogg, supra note* 2, at 3 (arguing that if bitcoins are considered general intangibles, the continuing security interest despite transfer will prohibit Bitcoin’s evolution beyond the novelty stage). [↑](#footnote-ref-11)
12. U.C.C. § 8-102(15) (2010). [↑](#footnote-ref-12)
13. Bitcoins are created through a mining process and given as a reward for providing the computational power necessary to create “blocks” on the blockchain. *See also* Lawless, *supra* note 2 (arguing that Bitcoin does not fall within the definition of “security” for lack of an “issuer”). [↑](#footnote-ref-13)
14. U.C.C. § 9-313(a) (2010). [↑](#footnote-ref-14)
15. “Securities intermediary” is defined as a “clearing corporation” or a third party that “in the ordinary course of its business maintains securities accounts for others and is acting in that capacity.” U.C.C. § 8-102(a)(14) (2010). [↑](#footnote-ref-15)
16. U.C.C. § 8-301(a) (2010). [↑](#footnote-ref-16)
17. U.C.C. § 9-314(a) (2010). [↑](#footnote-ref-17)