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Small Business Notes

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In this issue:

Will Cryptocurrencies Ever Make Sense for Small Businesses?

Much of the recent discussion of, and promotion of, cryptocurrencies has moved rapidly to high level discussions of things like tax impact (e.g., the Internal Revenue Service treats cryptocurrency as property for federal tax purposes and so the sale cryptocurrency or its use to obtain goods or services is a taxable event to the user generating a gain or loss) or securities law impact (e.g., the Securities and Exchange Commission considers cryptocurrency tokens to be a security and requires registration for any initial coin offerings; trading platforms that style themselves "exchanges" do not have the level of oversight and regulation of national securities exchanges like the New York Stock Exchange or NASDAQ; the Commodity Futures Trading Commission has determined that cryptocurrency coins and tokens are commodities under the Commodity Exchange Act).

Left out of much of the discussion are the limitations of such currencies that inhibit their use in traditional exchange transactions involving currency as a medium of exchange, unit of account, and store of value.

Cryptocurrencies have an unstable value. They are created privately (as opposed to being created by a central authority with a government mandate to protect stability – as, for example, with the Federal Reserve's open market transaction. These currencies cannot be redeemed, and their value depends on continued acceptance by other parties.

Cryptocurrencies do not have the same scalability as sovereign money: as the velocity of such currencies increase with use and acceptance the need for tremendous computing power to monitor and update the transaction ledger increases. Without that, as is often now the case, congestion can occur requiring queueing of transactions with resultant delay in the payment process.

Cryptocurrencies can result in lack of payment finality as, for example, when there exist two versions of the ledger maintained by two different parties each of whom updates the ledger simultaneously leading to a rollback of transactions in one of the ledgers.

These limitations, at least at present, have sufficient negative impact on buyers' or sellers' sense of cryptocurrencies utility and value to inhibit their use in ordinary exchange transactions.

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