Frequently Asked Questions (FAQs) on Virtual Currencies

What is a Virtual Currency?

- A virtual currency (VC) is a type of digital "currency" created by a community of online users, is stored in electronic wallets (e-wallets), and generally transacted online.
- It is not issued or guaranteed by central banks or government authorities.
- VCs may be transferred within the community of users. It may be used to buy virtual items (e.g. games, apps) or real goods from online shops/merchants willing to receive the VC as payment. In this sense, VCs are used as a medium of exchange.
- VCs may also be exchanged to/from actual cash (fiat money) through people/companies that are part of the community of users.

How does VC differ from Cryptocurrency?

VC is a general term that covers different types depending on business model – centralized (e.g. one entity/individual issues the VC); decentralized (e.g. no central repository or administrator but several entities/individuals maintain the VC); convertible (e.g. the VCs can be exchanged to fiat currency and vice versa); or cryptocurrencies.

Cryptocurrency is a type of VC that uses cryptography – a method of storing and transmitting data in unreadable form so that only the intended receivers can read and process it. This allows cryptocurrency transactions to be carried out in a decentralized manner by a group of users.

The first and most popular cryptocurrency to date is "Bitcoin", introduced in 2009.

How does Bitcoin work?

Below is a simplified narration of how Bitcoin works:

1. A user sets up a Bitcoin wallet onto a personal computer or mobile device. The wallet's software interfaces with wallets of other Bitcoin users.
2. The user loads funds into the Bitcoin wallet. This can be done by:
    - Purchasing from a Bitcoin exchange, trading platform or directly from another person using Bitcoin;
    - Transferring Bitcoin to/from other Bitcoin users as payment for goods and services; and
    - Awarding of Bitcoin for performing validation of Bitcoin transactions. An example is "mining" wherein a person who successfully validates a Bitcoin transaction is rewarded with corresponding Bitcoins.
3. Once Bitcoins are in the wallet, the user can initiate a Bitcoin transaction.
4. Upon initiation of the transaction, Bitcoin miners confirm and validate the transaction. The validation process involves solving certain math problems using "private key", "public key" and transaction message to address double-spending and ensure authenticity of the Bitcoin holder. A "public key" is a sequence of

letters/numbers that everyone in the Bitcoin community can see. A "private key" is another set of letters/numbers that is kept secret between/among the transactors.

5. Once validated, the transaction is effected and posted in the public ledger called the "blockchain", also known as "digital ledger technology".

How does VC differ from Fiat Currency and E-Money?

VC is distinct from fiat currency or real currency – the coins and paper money minted and printed by the central bank of a country; designated and circulated as legal tender in the country; and used and accepted as a medium of exchange in the country. Fiat currency is fully backed by the government of a country, and is acceptable as payment for public and private debts.

VC is also distinct from e-money, which is a digital representation of fiat currency. E-money is convertible to fiat currency in licensed e-money issuers or e-money agents. It is used to electronically transfer monetary value that is equivalent to, or similarly denominated as fiat currency. Like fiat currency, e-money is legal tender.

What are the potential benefits of VCs?

From a consumer standpoint, VCs may provide benefits in the following areas:

- ***Remittances and wire transfers***

  The Philippines is one of the countries receiving high levels of remittances from overseas. Many Filipinos either receive remittances from abroad, or send remittances to relatives and loved ones within the Philippines. Increasing number of Filipinos shop online, pay for goods/services online, or transfer funds via digital means. Such remittances and transfers – when facilitated using cryptocurrencies or VCs through licensed VC Exchanges – are relatively more convenient, faster and cheaper compared to traditional remittance and payment schemes. In this case, the average Filipino stands to benefit. The entry of VC Exchanges also enhances competition in the remittance and payments market, which can result in lower transaction costs and improved services.

- ***Electronic payments***

  As a digital value or asset, VCs are easier to use as payment for goods and services that are offered online. This can support the growing e-commerce industry in the Philippines. It can also support the use of social media, mobile technologies and other innovative platforms as delivery channels for financial services.

- ***Financial inclusion***

  VCs also have potential to expand financial inclusion. VCs may be used to facilitate and expand financial services for low-income Filipinos and those living in far-flung areas where traditional financial service providers like banks are unable to reach.

This may be possible and profitable, given the cost-efficiency of VC transactions as well as Filipinos' tendency to adopt digital platforms and mobile technology.

What are the risks involved in using VCs?

While VCs and the digital ledger technology that powers VCs have potential to facilitate delivery of legitimate financial services such as remittances and payments, there are inherent risks:

- ***Prices change quickly***

  The value of VCs is solely driven by supply and demand (i.e. its value increases as more people want to get the VC, and decreases when there are unpleasant incidents or negative news involving VCs). Because of speculations in the VC market, prices are unstable and change quickly over time. Users trading, investing and/or accepting VCs bear the risk of loss. There is no legal protection available for VC users in such cases.

- ***Potential for unlawful use***

  VC transactions have high degree of anonymity. The creators, senders and receivers can easily and effectively transact without knowing each other's real identities. The pseudo-anonymous and online nature of VCs make them attractive to fraudsters, scammers and people intending to do unlawful activities (e.g., money laundering/ terrorist financing). Legitimate VC users may be affected in case law enforcers clamp down on certain VC Exchanges.

- ***Prone to theft or loss***

  Just like any type of asset that is available online, VCs may be subject to hacking or theft, virus infection, and other cyber threats. Users may inadvertently lose their private keys that are used to secure the VC wallet. VC holders must adopt sound security practices and other safety measures to protect their VC accounts.

- ***VC transactions are immediate and irreversible***

  In case of fraudulent, unauthorized or erroneous transactions, VC holders may find it difficult to reverse said transactions. VC holders will be unable to file complaints or seek recourse since there is no central authority or issuer that backs or guarantees VCs.

- ***VC holdings are not insured***

  In the Philippines, VCs are not considered as deposits. In case VC Exchanges fold up or stop operating, VC holders cannot claim deposit insurance from the Philippine Deposit Insurance Corporation (PDIC).

What is the BSP regulatory approach to VCs?

Consistent with the Bangko Sentral ng Pilipinas (BSP) approach to innovation, the BSP has adopted a balanced approach to VCs by allowing the market to develop and subsequently issuing responsive regulations, as follows:

- **Warning Advisory on Virtual Currencies dated 06 March 2014**

  When VCs were starting to grow in the Philippine market, the BSP issued an advisory in 2014. It informed the public of the features, benefits and attendant risks when dealing with VCs.

  This advisory can be accessed at:
  http://www.bsp.gov.ph/publications/media.asp?id=3377

- **BSP Circular No. 944 dated 06 February 2017**

  Following the rise in the use of VCs for payments and remittances in the Philippines, the BSP established a formal regulatory framework for VC Exchanges – Circular No. 944 dated 6 February 2017. VC Exchanges are companies or businesses engaged in changing VCs into fiat currency (and vice versa). The act of converting VCs into Philippine money can facilitate payments and remittances. Circular 944 requires VC Exchanges to register with the BSP as remittance and transfer companies. They are also required to put in place adequate safeguards to address the risks associated with VCs. These include control measures to counter money laundering/ terrorist financing (ML/TF), technology risk management systems, and consumer protection mechanisms.

  BPS Circular 944 can be accessed at:
  http://www.bsp.gov.ph/downloads/regulations/attachments/2017/c944.pdf

  The list of BSP registered remittance and transfer companies with VC Exchange Service can be accessed at:
  http://www.bsp.gov.ph/banking/directories.asp

- **Advisory on the Use of Virtual Currencies dated 29 December 2017**

  The BSP recently issued another public advisory in response to certain unscrupulous fraudsters/groups that try to entice consumers to "invest" in Bitcoins or VCs packaged as an Initial Coin Offering (ICO). The advisory warns consumers to be cautious in dealing with VCs, only maintain VCs sufficient to meet their transactional requirements, and adopt sound security measures to protect their VC accounts. The advisory also reiterates that BSP does not endorse VCs as a currency or an investment instrument due to its highly-speculative and risky nature.

  The BSP highly encourages existing and prospective VC users to deal only with BSP-registered VC Exchanges. The BSP also cautions the public to be vigilant about VC related transactions and investments in view of potential risks.

This advisory can be accessed at:
http://www.bsp.gov.ph/publications/media.asp?id=4575

Is it good to invest in VCs?

Because of price volatility, VC holders may incur significant losses when trading or investing in VCs. While VCs were not initially designed to be used as an investment product, some traders/people speculate on VCs which adds to the price volatility. As in any other type of investment, prospective VC investors should know and fully understand VCs and cryptocurrencies before speculating or investing in such a product. The public is advised not to blindly follow the crowd, adopt herd mentality, or engage in speculative transactions. The public should exercise extreme caution at all times when dealing with VC products and transactions in general.