

RISK INSIGHTS

Cryptocurrency is a digital currency that operates independently of traditional banking networks. It is based on blockchain technology, which is a decentralized and immutable ledger system that uses cryptography to ensure secure transactions. There are many different types of cryptocurrency, but the largest by market capitalization is bitcoin. Despite its intangible form, cryptocurrency functions similarly to physical cash across various countries and governments. This currency has grown in popularity over the past decade, with many businesses embracing it in the processes of selling goods or services online and accepting payments from customers. Utilizing this currency can provide several benefits for businesses, yet the unique and evolving nature of the cryptocurrency market also poses considerable risks. That's why it's crucial for businesses to have a clear understanding of the cryptocurrency risk landscape and best practices for minimizing potential threats. This article weighs the pros and cons of accepting cryptocurrency for businesses and outlines related risk management practices.

Accepting cryptocurrency can benefit businesses in a variety of ways, including the following:

- **Reduced transaction fees**—Businesses are generally required to pay the associated transaction fees when using traditional payment processors to sell goods and services to their customers. While some processors implement fees as high as 4% per transaction (potentially even more for international transactions), cryptocurrency-related transaction fees are often much lower, with some bitcoin exchanges offering fees below 1%. This can generate significant cost savings for businesses over time.
- **Expedited transactions**—In addition to reducing transaction fees, accepting cryptocurrency can allow businesses to expedite their transaction processes. Unlike traditional payment methods, cryptocurrency isn't attached to a country of origin or national bank and doesn't involve intermediaries, therefore eliminating the risk of related delays. Through the use of blockchain technology, cryptocurrency transactions can be processed smoothly and swiftly, usually in a matter of minutes. This, in turn, can help businesses improve their cash flow management practices, particularly as it pertains to international transactions.
- **Extended customer reach**—Since cryptocurrency isn't limited by geographical borders, businesses that accept this currency can easily connect with customers throughout the world without any concerns regarding cross-border restrictions or conversion costs. Such widespread international accessibility gives businesses the opportunity to substantially expand their customer bases and tap into new markets. Furthermore, accepting cryptocurrency can help businesses enhance their digital footprints and foster a more innovative and forward-thinking brand, thus attracting tech-savvy customers who favor virtual transactions.
- **Minimized fraud exposures**—When a customer makes a payment using cryptocurrency, it's permanent. Once the payment is processed, it cannot be reversed or undone. For businesses that accept cryptocurrency, this can help prevent chargebacks and related fraud concerns. Additionally, blockchain technology makes all the difference in creating a secure digital environment for cryptocurrency transactions to take place. This technology establishes advanced security measures to safeguard the funds and sensitive information being processed amid cryptocurrency transactions, limiting the likelihood of data breaches and other cyberattacks.

Although accepting cryptocurrency can prove beneficial to businesses, it also comes with a range of risks, such as the following:

- **Market volatility**—While the value of cryptocurrency isn't impacted by national inflation issues, it's still considered a highly volatile market that can experience frequent and drastic price fluctuations. According to data from financial,

software and media company Bloomberg, bitcoin has experienced four market drawdowns that have exceeded 50% since 2014, three of which affected the market for several years afterward. This means that businesses that accept cryptocurrency could be increasingly vulnerable to financial instability and lost revenue if the value of such currency drops suddenly following large transactions.

- **Regulatory uncertainty**—The cryptocurrency market remains largely unregulated because it is still a relatively new entrant to the global economy. However, government agencies and organizations such as the U.S. Securities and Exchange Commission and the Federal Deposit Insurance Corporation are currently in the process of developing cryptocurrency standards and related legislation for businesses. As the legal landscape surrounding cryptocurrency continues to evolve, businesses that accept this currency will have to prepare for sudden regulatory changes and adjust their operations accordingly. Failure to do so could result in costly noncompliance fines and other penalties.
- **Security issues**—Blockchain technology can help ensure safe transaction processes for businesses that accept cryptocurrency, but the storage of this currency still carries elevated security exposures. After all, cryptocurrency is considered highly attractive to cybercriminals, making businesses that utilize this currency more likely to encounter hacking attempts, phishing scams and ransomware threats. Without ample security measures to protect their digital wallets, these businesses could experience large-scale financial losses, operational disruptions and diminished profitability. In fact, the latest Crypto Crime Report from software company Chainalysis revealed that hackers and other cybercriminals stole \$2.2 billion in cryptocurrency funds in 2023 alone.
- **Technical barriers**—Even though the use of cryptocurrency has steadily grown in recent years, widespread adoption will take time. Until then, businesses could face technical challenges when adjusting their operations and overall digital infrastructures to accept cryptocurrency and may even require additional assistance from software experts to properly set up and manage related transactions. What's more, customers who are inexperienced with digital wallets might initially struggle to use cryptocurrency. In some cases, customers could be wary of using this currency altogether; they may assume that it's tied to high-risk activities and investments (e.g., cybercrime, money laundering, terrorism financing and other illegal transactions). As such, businesses that utilize cryptocurrency may have to spend time and resources educating customers on the proper usage of this currency and combatting any negative perceptions or risk potential reputational fallout.

Fortunately, there are several strategies that businesses can leverage to reduce the risks associated with accepting cryptocurrency. Here are some best practices for businesses to consider:

- **Conduct a risk assessment.** First and foremost, businesses should identify the specific risks stemming from accepting cryptocurrency and document how these concerns could affect their IT infrastructures, sales processes, finances and reputations. Key risks to consider include the overall volatility and popularity of the type of cryptocurrency being accepted, possible cybersecurity threats and applicable legislation. From there, businesses can better determine necessary operational changes and safeguards.
- **Establish secure payment systems.** To properly protect cryptocurrency funds and minimize digital wallet losses, businesses should establish secure payment policies and procedures. This may include setting up secure and encrypted cryptocurrency payment gateways; requiring the use of two-factor authentication for all transactions; leveraging multi-signature digital wallets; implementing advanced security software; and utilizing patching systems to address any vulnerabilities in this software, making updates as needed.
- **Maintain diversified assets.** Apart from adopting secure payment policies and procedures, it's essential for businesses to ensure the safe storage of their cryptocurrency funds. This entails spreading out digital assets across different platforms to prevent hackers and other cybercriminals from accessing large sums of money upon infiltrating a single access point. To better distribute and diversify their assets, businesses should also avoid storing the entirety of their cryptocurrency funds on exchanges; rather, they should consider leveraging multiple offline wallets for long-term storage.
- **Ensure continuous monitoring.** Businesses should utilize advanced technology solutions to monitor all cryptocurrency transactions in real time. Doing so can ensure prompt detection and remediation of any suspicious activities or other security issues. Businesses should also conduct regular security audits and penetration tests to identify any remaining failures or vulnerabilities among cryptocurrency-related operations, making adjustments whenever necessary.
- **Develop an incident response plan.** Even with proper safeguards in place, security incidents involving cryptocurrency may still occur (e.g., data breaches, ransomware attacks and stolen funds). With this in mind, it's imperative for businesses to develop incident response plans that outline timely resolution steps to take amid various cryptocurrency-related scenarios. These plans should also be communicated to all applicable parties and routinely evaluated through stress tests, simulations and tabletop exercises to ensure their effectiveness and identify any ongoing security gaps.
- **Comply with the Anti-money Laundering (AML) rules, Know Your Customer (KYC) requirements and new laws.** To maintain regulatory compliance in today's evolving legal landscape, businesses should work with trusted cryptocurrency payment providers that adhere to all applicable standards and consult legal counsel to monitor upcoming legislative changes. Businesses should also uphold compliance with existing federal laws regarding safe financial practices, including the AML rules and KYC requirements.

As cryptocurrency continues to rise in popularity, a growing number of businesses may consider utilizing it. By carefully assessing the pros and cons of accepting this currency and implementing effective risk management techniques, businesses can be better equipped to maintain successful operations and limit potential losses. Contact us today for more risk management guidance.

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