



July 16, 2021

Via Electronic Submission: Comments@fdic.gov

James P. Sheesley
Assistant Executive Secretary
Attention: Comments-RIN 3064-ZA25
Federal Deposit Insurance Corporation
550 17th Street N.W.
Washington, D.C. 20429

**Re: Coinbase Response to FDIC “Request for Information and Comment on Digital Assets”
(RIN 3064-ZA25)**

Dear Mr. Sheesley:

This comment is submitted on behalf of Coinbase in response to the Federal Deposit Insurance Corporation’s “Request for Information and Comment on Digital Assets,” issued on May 17, 2021 (hereinafter, the “RFI”).¹

Coinbase was founded in 2012 as a consumer platform that makes it easy to purchase, sell, and transact in digital assets. Our business was founded on the premise that the digital asset economy—and the open, global network upon which it is built—creates unprecedented opportunities to accelerate financial services innovation and enhance consumer access throughout the global financial system. In the ensuing years, we have witnessed and participated in the tremendous growth of digital assets and decentralized networks. The concurrent explosion of entrepreneurial activity has led to the emergence of myriad applications for global remittance, foreign exchange and payments, the creation of fiat-backed stablecoins, tokenized securities, and other emerging financial technologies. Today the market capitalization of digital assets exceeds \$1 trillion, not including the significant research and development value and thousands of jobs created by growing technology businesses like Coinbase that operate in this sector.

Over the past nine years Coinbase has created a secure and regulated part of the emerging infrastructure of the digital asset economy. We have worked closely with regulators, law enforcement, banks, and technologists to create a safe and trusted environment in which consumers and institutional investors can access and trade digital assets. In the course of the tremendous growth of our U.S. business, we know that banks and bank regulators play a key role in the digital asset economy: digital asset businesses use existing bank payments infrastructure to process clients’ fiat currency payments in relation to the purchase and sale of digital assets; institutional investors increasingly rely on banks (or trust banks) to provide digital asset custodial services; these custodial banks may play an important role in the growth of trading in tokenized securities and other derivative products that are being built upon blockchain technology. Further, as consumers and institutions continue to demand sophisticated and

¹ “Request for Information and Comment on Digital Assets,” 86 Fed. Reg. 27602 (May 21, 2021).

familiar financial products—like credit and interest-like returns on custodial assets—we anticipate that the Federal Deposit Insurance Corporation (“FDIC” or “Corporation”), its fellow banking regulators, and state and federal banks themselves will be increasingly relevant to the continued maturation of the digital asset economy emerging in the United States.

We have said before—and we continue to believe—that regulators’ investment in this sector has the significant potential to enable Internet-like growth and returns that will yield tremendous benefits to the U.S. economy and enhance U.S. consumers’ access to fair and transparent financial products for years to come. As the leading, regulated digital asset business in the United States, we are pleased to share our perspective with the FDIC.

I. Coinbase

Coinbase Global, Inc. is registered with the SEC as a public company listed on Nasdaq with a market capitalization exceeding \$45 billion. Through our primary operating company, Coinbase, Inc., and affiliates (collectively, “Coinbase”), we operate one of the largest digital asset exchange platforms in the world. By the close of 2020, we supported over 43 million users across more than 100 countries who traded over \$450 billion in digital assets on our platform and entrusted us to secure over \$90 billion of their assets. Our more than 2,000 employees—mostly based in the U.S.—are devoted to creating safe and reliable digital asset services that our clients expect.

With an early focus on regulatory requirements, Coinbase has set the standard for legal compliance in the digital asset industry. Coinbase was among the first regulated digital asset exchanges in the United States, and today our activities are regulated under various state regulatory regimes, including money transmission regulation, bespoke virtual currency regulation, and bank and trust company laws in New York, and are subject to federal oversight, including by the Department of the Treasury’s Financial Crimes Enforcement Network Bureau (“FinCEN”), the Securities and Exchange Commission and the Commodity Futures Trading Commission. Coinbase has participated in the development of investigative methods employed by a myriad of state, federal, and international law enforcement agencies to identify and pursue illicit use of digital asset technologies, and we have been twice recognized by FinCEN for providing essential intelligence to law enforcement authorities. In 2019, we received the Private/Public Partnership award from Homeland Security Investigations for our contribution to major law enforcement investigations. We have a robust AML/BSA program, and we are one of only two digital asset members of the Department of the Treasury’s Bank Secrecy Act Advisory Group.

II. Engagement Beyond the RFI

We applaud the FDIC’s continued efforts to embrace innovations in financial services, including through initiatives like FDITECH and the appointment of a Chief Innovation Officer. We view the RFI as a prudent and important step in the direction of supporting insured depository institutions’ explorations of the innovation and financial inclusion made available by digital asset products. At the same time, we recognize that the topics addressed by the RFI—digital asset products and, more generally, distributed ledger technology—are rapidly evolving topics with breadth and complexity that outstrips any single discussion. Bearing this in mind, we offer this comment letter to begin what we hope will be an ongoing dialogue with FDIC staff about the digital asset economy and distributed ledger technology.

The FDIC has a strong history of partnering with industry experts, particularly to explore far-reaching topics. An excellent recent example of this would be the FDIC’s Advisory Committee on Community Banking’s Subcommittee on Supervision Modernization, which brought together thought leaders from banks, leading law firms, fintechs and universities for the purpose of evaluating changes to FDIC supervision that might beneficially impact banks and their communities throughout the country. Coinbase respectfully submits that the Corporation’s exploration of digital asset products and distributed ledger technology also is a far-reaching conversation that could be worthy of a similarly structured advisory committee to facilitate an ongoing dialogue. Throughout our letter we have identified specific topics where we believe our expertise and perspective would add value to the FDIC’s consideration of the issues raised in the RFI; there are others, as well. We believe our industry would both welcome and benefit from engagement with FDIC staff on these and other topics, in whatever form or format appropriate.

III. Responses to Specific RFI Questions

RFI Question 1: In addition to the broad categories of digital assets and related activities described above, are there any additional or alternative categories or subcategories that insured depository institutions are engaged in or exploring?

By operating our core exchange business we have insight into the rapidly growing demands for digital assets and the evolving nature of related activities in the crypto economy. Coinbase gains insight from the safekeeping of customer digital assets through our regulated custodial entity, Coinbase Custody Trust Company, LLC (“Coinbase Custody”), a New York state-chartered limited purpose trust company that was established in October 2018 under the New York Banking Law. Finally, we are informed by our strong and continually expanding relationships with banks and other financial institutions, including several insured depository institutions (“IDIs”).

While Coinbase is not itself an IDI, our broad experience indicates that digital-asset use cases for IDIs may encompass such diverse activities as traditional fiat banking, digital asset custodial services, validation of digital asset transactions, issuance of digital assets, governance of certain blockchains, digital asset payments, remittances, and fiat lending, as well as eventually digital asset banking.

Consistent with our strong history of working closely with regulators, we would be happy to help FDIC staff build familiarity with these and other activities in the digital asset economy, especially as new applications of distributed ledger technology continue to develop.

RFI Question 8: Please identify any potential benefits, and any unique risks, of particular digital asset product offerings or services to IDI customers.

General Benefits and Risks of Digital Assets and Distributed Ledger Technology.

- (a) *Enhanced Transparency.* One of the benefits of digital asset technology is that distributed ledgers are simultaneously hosted across multiple systems with no central authority. Recording transactions requires consensus in accordance with the distributed ledger’s technology: either a computationally intensive cryptographic problem (*i.e.*, “proof of work”) or validation by the community of digital asset owners (*i.e.*, “proof of stake”). The distributed nature of this validation process and the accessibility of the ledger

provide enhanced transparency as well as a readily accessible means of auditing past transactions in the digital asset.

- (b) *Increased Resiliency*. By design, distributed ledgers are simultaneously and redundantly hosted across multiple systems, and as a result are highly resistant to corruption. Attacks would be extraordinarily computationally and resource intensive; system failures are significantly less likely.
- (c) *Disintermediated Processing*. Another benefit of digital assets is that participants can maintain their own addresses or accounts on the distributed ledger, enabling their transactions (e.g., payments or remittances) to be processed by the ledger protocol directly between participants' accounts, rather than relying on intermediation. This processing model could improve settlement certainty, reduce processing times and minimize systems demands on centralized entities.
- (d) *Lower Settlement Risk*. Digital assets, distributed ledger technology, and smart contracts can be designed to permit the automatic execution of digital asset transactions only if necessary conditions are met (e.g., release of collateral upon repayment of a loan). This enables real-time processing, which in turn reduces settlement risk.
- (e) *Continuous Operation*. Digital assets and distributed ledgers are in continuous operation, allowing transactions to be processed and validated 24 hours a day, 365 days a year.
- (f) *Immutability/Irreversibility*. With the resiliency built into the technology from its immutability and decentralization, loss via hack or transfer-in-error may be irreversible, as there is no built-in mechanism for corrections (absent reverting the blockchain to a prior moment in time). As discussed in our response to RFI Question 12 (below), this is particularly relevant to custodial activities. However, IDIs' current risk management frameworks may have useful constructs for analyzing and mitigating these and other broadly similar technology risks.²
- (g) *Protocol-Related Risk*. In addition, digital assets carry novel protocol-related risks beyond the perimeter of financial institutions. These derive from the programming of the digital assets themselves (e.g., smart-contract risk, where design flaws or implementation bugs cause unexpected behavior). These risks, however, are consistent with the cybersecurity and data privacy risks IDIs already manage.³
- (h) *AML/CTF Risk*. The typical risks for digital asset remittances, money laundering and terrorist financing, are mitigated by banks' compliance with their AML obligations under the Bank Secrecy Act. However, news coverage surrounding cryptocurrencies may

² The risks posed by digital assets can be understood similarly to the cybersecurity risks to which IDIs are already broadly subject. As stated in the Corporation's January 2020 joint statement with the OCC, supervised financial institutions are already mandated to follow cybersecurity risk management principles, which apply equally to digital assets.

³ See e.g., FIL-44-2008, Guidance For Managing Third-Party Risk (Jun. 6, 2008), FIL-68-2016, FFIEC Cybersecurity Assessment Tool (Oct. 18, 2016).

overstate cryptocurrencies' role in illicit activities according to a recent report by the Financial Action Task Force.⁴ Coinbase agrees that ongoing monitoring is appropriate, but notes that IDIs are already well-positioned to manage such risks (*e.g.*, using blockchain analytics).⁵

As discussed in the responses to the RFI questions below, Coinbase believes it may be appropriate for the FDIC to recognize and address the unique benefits and risks of digital asset products and distributed ledger technology in supervisory guidance.

RFI Question 10: Are there any unique aspects of digital asset activities that the FDIC should take into account from a supervisory perspective?

In general, we believe that IDIs' willingness to develop and offer digital asset products or employ distributed ledger technology will be influenced by the clarity of the FDIC's supervisory guidance for such activities. In that context, we encourage the FDIC to consider the unique benefits and risks of current or potential IDI digital asset activities, some of which are highlighted in our responses to RFI Questions 8 and 12.

RFI Question 11: Are there any areas in which the FDIC should clarify or expand existing supervisory guidance to address digital asset activities?

While Coinbase is not itself subject to FDIC supervisory guidance, we nonetheless believe there are certain areas in which clarification or expansion of current guidance could not only accelerate IDIs' basic utilization of digital assets and distributed ledger technologies, but could also facilitate supervisory and law enforcement activity. We highlight two such areas. First, as discussed in our response to RFI Question 8, transactions validated on a distributed ledger are viewable by all participants as a tamper-resistant electronic record. This has inherent recordkeeping benefits. IDIs and regulators may wish to clarify scenarios and circumstances in which the FDIC could accept distributed ledger information as evidence under current regulations. Second, basic BSA/AML/CFT processes may be enhanced by distributed ledger technology. For example, distributed ledgers could be used to improve existing know-your-customer and customer due diligence efforts by capturing and encoding client-specific information, strengthening IDIs' real-time monitoring of financial transactions and enabling bank regulators and law enforcement to better detect and prosecute illegal activity.

⁴ See 12-Month Review of the Revised FATF Standards on Virtual Assets and Virtual Asset Service Providers, *Financial Action Task Force* (June 2020), available at: <http://www.fatf-gafi.org/media/fatf/documents/recommendations/12-Month-Review-Revised-FATF-Standards-Virtual-Assets-VASPS.pdf>; see also *The 2020 State of Crypto Crime*, Chainalysis, p. 5 (January 2020) available at <https://go.chainalysis.com/rs/503-FAP-074/images/2020-Crypto-Crime-Report.pdf> (reaching similar conclusions).

⁵ Separately, the Funds Travel Rule presents unique challenges for digital asset transmissions; however, Coinbase is leading development of an industry-wide solution to meet compliance requirements.

RFI Question 12: In what ways, if any, does custody of digital assets differ from custody of traditional assets?

Through our experience with Coinbase Custody, we understand how custody of digital assets differs from traditional assets. A simple description of digital asset custodial services—the transfer in (deposit) or transfer out (withdrawal) of certain supported digital assets by institutional clients into custodial accounts established on the books and records of the custodian on behalf of the client—does not capture the technical complexity of the activity. Facilitating deposits and withdrawals requires specific processes for encryption (*i.e.*, key generation), secure storage and decryption. The processes that Coinbase has implemented are designed to protect private keys from being used to make an unauthorized or accidental transfer of a digital asset and to protect private keys from being corrupted, lost or destroyed. We believe it is important that digital asset custodians support their core custodial functions with a body of operational processes that are carefully documented in policies and procedures and subject to effective internal governance and controls. Coinbase would welcome the opportunity to provide further technical support to FDIC on how these key differences between custodial services for digital versus traditional assets should inform the Corporation’s supervisory guidance or future proposals concerning IDI custody of digital assets.

RFI Question 14: Are there any steps the FDIC should consider to ensure customers can distinguish between uninsured digital asset products on the one hand, and insured deposits on the other?

Coinbase supports the efforts of the FDIC to ensure that consumers are appropriately made aware of the availability, or lack of availability, of deposit insurance, which is critical to stability in the U.S. banking system. However, we believe existing conventions for distinguishing between FDIC insured deposits and other IDI products can be readily applied to digital asset products without additional regulation.

RFI Question 15: Are there distinctions or similarities between fiat-backed stablecoins and stored value products where the underlying funds are held at IDIs and for which pass-through deposit insurance may be available?

Yes, there are similarities in that fiat-backed stablecoins also operate as a store of value. With respect to pass-through FDIC deposit insurance, prepaid bank cards have benefited from the clarity of the Corporation’s 2008 General Counsel’s Opinion.⁶ As described in that opinion, to the extent funds underlying stored value cards are held at IDIs, they will be treated as “deposits,” and therefore cardholders will be eligible for pass-through deposit insurance if the FDIC’s standard recordkeeping requirements have been satisfied. Yet, for reasons we would welcome the opportunity to discuss, fiat-backed stablecoins appear less likely to be structured such that pass-through deposit insurance would be reasonably available to owners under these standards.

While not yet a strong detraction from adoption and usage of fiat-backed stablecoin products,⁷ adoption and usage continue to grow. The Corporation may wish to consider the applicability of

⁶ General Counsel's Opinion 8, 74 Fed. Reg. 67155 (Nov. 13, 2008).

⁷ For a table of “Top Stablecoin Tokens by Market Capitalization,” see <https://coinmarketcap.com/view/stablecoin/>.

pass-through deposit insurance to fiat-back stablecoin holders in the future, and we are happy to assist FDIC staff as needed.

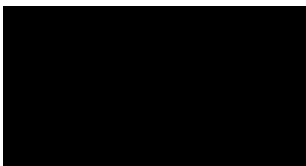
RFI Question 16: If the FDIC were to encounter any of the digital assets use cases in the resolution process or in a receivership capacity, what complexities might be encountered in valuing, marketing, transferring, operating, or resolving the digital asset activity? What actions should be considered to overcome the complexities?

Whether in the resolution process, a receivership capacity, or otherwise, predicting what challenges or benefits FDIC staff might face in valuing, marketing, transferring, operating, or resolving IDIs' digital-asset activities depends largely on the specific digital asset or assets at issue. Cryptocurrencies are numerous and diverse, reflecting material asset-by-asset differences (*e.g.*, from market size and activity, to liquidity profile, to underlying protocol). With respect to the ease of valuation and tradability, we recognize broad potential advantages to digital assets. These become especially pronounced in the case of prevalent coins such as BTC and ETH, which together make up approximately ~63% of the entire market for digital assets, which has a total market cap of \$1.3 trillion. With high liquidity, their demand has proven resilient in the face of sector-wide volatility. Even as a class, digital assets are more quickly, more reliably, and more securely transferable, with ownership and transaction histories that are readily traceable to each IDI customer.

IV. Conclusion

Our nine-year experience as a leading digital asset platform has shown that customers are eager to discover financial services that are faster, cheaper and more accessible, and return greater benefits than those available through conventional products and legacy technology. Although digital assets do not immediately solve every problem, they create a platform upon which entrepreneurs can innovate financial technologies faster than ever before. We look forward to being part of the ongoing dialogue as the FDIC continues to become expert in digital assets and distributed ledger technology.

Sincerely,



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