By Email Submission to Comments@fdic.gov

July 15, 2021

Mr. James P. Sheesley
Assistant Executive Secretary
Attention: Comments-RIN 3064-ZA25
Federal Deposit Insurance Corporation
550 17th Street N.W.
Washington, DC 20429
U.S.A.

Re: Federal Deposit Insurance Corporation (FDIC) Request for Information and Comment on Digital Assets (RIN 3064-ZA25).

Dear Mr. Sheesley:

The Wall Street Blockchain Alliance (the "WSBA") appreciates the opportunity to provide the views of our member-based organization for the Federal Deposit Insurance Corporation (FDIC) Request for Information and Comment (RIN 3064-ZA25) regarding insured depository institutions' ("IDIs") current and potential activities related to digital assets.

The WSBA is an industry leading non-profit trade association based in New York City. Our mission is to guide and promote the comprehensive adoption of blockchain technology and digital assets across global markets in a manner that complies with all relevant laws and regulations. The WSBA is structured into Working Groups that, in turn, coordinate the collaboration of leaders across industries and professions to fulfill the WSBA's mission.

Introduction

The WSBA, as a matter of policy, supports the equitable regulation and monitoring of financial markets and financial market participants. The WSBA membership encompasses a wide variety of organizations and roles, including banks, broker-dealers, investment firms, law firms, accountants, compliance officers and more, all of whom are deeply familiar with and appreciative of the importance of protective laws and regulations.

Given this variety of industries and professionals within the WSBA, we would like to share our responses to the Request for Comment Questions posed in the FDIC published statement. We will limit our response to a small number of those questions which we believe the team at the WSBA is qualified to address. These comments are our own, in our personal capacity, and do not necessarily reflect the views of any member or partner of the WSBA, nor the WSBA Board of Directors.

Request for Comment Questions

Questions Regarding Current and Potential Use Cases

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 IDIs are engaged in or exploring?

   We believe that the broad categories described in the Request for Comment (technology solutions, asset-based activities, liability-based activities, and custodial activities) fairly cover the extensive innovations developing in global financial markets due to the advent of blockchain and digital asset technologies. That said, we believe it is important to recognize the pace of development in digital assets and related activities is accelerating within all the noted categories. For example, the asset-based activities category should consider the proliferation of new investments and collateral facilities being developed, as well as, for example, the growth of non-fungible tokens ("NFTs"). NFTs are units of data stored on a blockchain which verifies that a digital asset is unique and not interchangeable. There is a growing ability for market participants in the decentralized finance ("DeFi") space to use these instruments, including NFT's representing ownership of physical assets like art, as collateral for loans. In addition, the growing appetite in the market for interest payments on "staked" or deposited digital assets is worthy of consideration. This market, now approximately $9 billion in value, is estimated to grow to $40 billion by 2025.[1]

Questions Regarding Risk and Compliance Management

[1] https://www.businessinsider.com/cryptocurrency-investing-coinbase-jpmorgan-9-billion-opportunity-crypto-staking-ethereum-2021-7

4. To what extent are IDIs' existing risk and compliance management frameworks designed to identify, measure, monitor, and control risks associated with the various digital asset use cases? Do some use cases more easily align with existing risk and compliance management frameworks compared to others? Do, or would, some use cases result in IDIs developing entirely new or materially different risk and compliance management frameworks?

   In our discussions within the industry as well as among members, there is a notable focus on making sure that any digital asset activities conform with all existing risk and compliance management frameworks. For example, all market participants that we speak with have robust AML/KYC and BSA reporting in place. In addition, there is a growing stable of technology tools to enable robust reporting to identify, measure, monitor and control any risks associated with digital asset use. This also applies to some of the powerful forensic tools available to IDI's and other market participants for tracking digital asset flows and transactions.[2] That said, we believe that it is important to note some of the challenges associated with DeFi, or unhosted wallets for example, which allow for significant activity without many of the intermediary functions necessary for some risk and compliance functions. To the extent these market segments touch on IDIs in some way (including conversions to fiat currency), there will be a need for greater diligence. While we do not believe that this will necessitate IDIs developing entirely new or materially different risk and compliance management frameworks, it may require evolution of these frameworks to interoperate with new technology platforms and solutions

5. What unique or particular risks are challenging to measure, monitor, and control for the various digital asset use cases? What unique controls or processes are or could be implemented to address such risks?

   Some particular risks that may be challenging to measure, monitor, and control for the various digital asset use cases could include but not be limited to: the opaque nature of some digital asset markets; potential discrepancies in the level of operational integrity, security and regulatory compliance of some venues or participants in the digital asset markets; challenges associated with unhosted wallets, which allow for value exchange without the need for a banking intermediary; challenges associated

[2] https://blockchaingroup.io and https://www.chainalysis.com are good examples.

with valuation of digital assets, as many lack a clear valuation methodology, which may impact measurement and control criteria as well as cause financial reporting and taxation difficulties. To address such risks, we would suggest that, in addition to the forensic and reporting tools we cited earlier, IDIs dedicate time and resource to knowledge development within the organization to create and evolve unique digital asset controls or processes, which can be done in coordination with existing IDI technology and control frameworks, and the multitude of digital asset vendor products now in market to facilitate such controls.

6. What unique benefits to operations do IDIs consider as they analyze various digital asset use cases?

IDIs should consider the transparent and auditable nature of digital asset transactions on blockchain as a definite benefit to operations. While there are certainly risks that need to be assessed, the ability to leverage the structural benefits of blockchain based digital assets, including auditability, speedier settlement, improved security, reduced costs, and immutability of data are clear benefits that should be part of any IDI's consideration of digital asset use cases.

Questions Regarding Supervision and Activities

7. Are there any unique aspects of digital asset activities that the FDIC should take into account from a supervisory perspective?

The financial technology innovations that the FDIC might wish to classify as "digital assets," even within the proposed categories, may not be effectively accounted for under current regulatory schema and as noted above, may requires some form of evolution or innovation. In large part this is due to the concept of financial risk around which much of FDIC policy revolves. Many digital assets showcase their varied, flexible, and decentralized nature, but these features generate difficulty in appraising the risk of those assets.

We believe that it would be an unhelpful response to denote all digital assets, or all digital assets of a given category, using the same standards of quality under the FDIC's Examination Policy, for example.[3] Since digital assets classified within the same

[3] See "Risk Management Manual of Examination Policies," Sec. 3-1, https://www.fdic.gov/regulations/safety/manual/section3-1.pdf

proposed category may vary so intensely, any one asset could easily be rated or appraised at a level which inaccurately represents its true risk. This perspective aligns with our earlier comments about the rapid pace of innovation in the digital asset space as well.

Consider an example with cryptocurrencies: "Nectar" versus "Ether." The FDIC categorizations as enumerated in its RFI would dub both these cryptocurrencies, "asset-based activities." On the one hand, Nectar is a cryptocurrency used to reward participants in cybersecurity initiatives run by the firm Polyswarm[4]. Polyswarm maintains tight control over the production and dispersal of Nectar with the intention of keeping its price as stable as possible.

On the other hand, Ether is designed to enable smart contracts to operate on the associated "Ethereum" blockchain[5]. Ethereum is one of the most commonly used means of smart-contracting on the planet--to the extent that it is emblematic of blockchain technology as a whole. Ether's central role in fueling this technology causes it to experience price swings as market sentiment fluctuates in reaction to the constant, rapid stream of negative and positive developments in the blockchain industry.

Both of these cryptocurrencies would be identified under the FDIC's proposed categories as "asset-based activities," and while factors such as their respective price stability may be comfortably assessed through existing quality standards, others will prove more difficult. For example, while Nectar's stability may be viewed as a plus for quality at-face, what of the fact that such stability is dependent upon a single company's management of the asset? Although Ether experiences short-term fluctuation, would its long-term reflection of blockchain market trends--and hence, relative predictability--boost its rating? How should a history of abrupt developments that affect the industry long-term, like China's recent threat to ban cryptocurrency mining, affect the quality rating of either asset?[6]

In answering these questions, and myriad others now or yet to come, the FDIC will potentially need to take stances on unsettled matters of debate. Current and new standards of assessment should evolve to account for the unique and novel elements

[4] https://polyswarm.io
[5] https://ethereum.org/en/what-is-ethereum/
[6] https://www.reuters.com/technology/chinas-ban-forces-some-bitcoin-miners-flee-overseas-others-sell-out-2021-06-25/

of all digital assets. A failure to carefully consider the features of each technology could stifle its growth and cut short its potential in the banking sector and beyond.

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Thank you for your consideration and for the opportunity to submit this response regarding the FDIC Request for Information and Comment on Digital Assets (RIN 3064-ZA25). On behalf of the Board of Directors and Members of the Wall Street Blockchain Alliance, we look forward to your thoughts and feedback. We would also welcome the opportunity to respond to any questions or comments in a more substantive manner, should that prove useful to the FDIC.

Respectfully Submitted,

Ron Quaranta - Chairman and Chief Executive Officer, *Wall Street Blockchain Alliance*

Alice Albl - Legal Working Group Associate, *Wall Street Blockchain Alliance*