



July 16, 2021

Via Electronic Mail

Mr. James P. Sheesley
Assistant Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street N.W.
Washington, D.C. 20429

Re: Request for Information and Comment on Digital Assets (RIN 3064-ZA25)

Dear Mr. Sheesley:

The Bank Policy Institute¹ and the Consumer Bankers Association² (together, the “Associations”) appreciate the opportunity to comment on the request for information³ issued by the Federal Deposit Insurance Corporation seeking input regarding insured depository institutions’ current and potential activities related to digital assets. Banks⁴ have traditionally been at the forefront of technological innovation, and as more use cases emerge for digital assets,⁵ the Associations’ members are evaluating

¹ The Bank Policy Institute is a nonpartisan public policy, research and advocacy group, representing the nation’s leading banks and their customers. Our members include universal banks, regional banks and the major foreign banks doing business in the United States. Collectively, they employ almost 2 million Americans, make nearly half of the nation’s small business loans, and are an engine for financial innovation and economic growth.

² The Consumer Bankers Association partners with the nation’s leading retail banks to promote sound policy, prepare the next generation of bankers, and finance the dreams of consumers and small businesses. The nation’s largest financial institutions, as well as many regional banks, are CBA corporate members, collectively holding two thirds of the industry’s total assets.

³ Request for Information and Comment on Digital Assets, 86 Fed. Reg. 27,602 (May 21, 2021).

⁴ For purposes of this comment letter, the term “banks” refers to, as the context may require, financial institutions including banks, bank holding companies or the affiliates of such banks and bank holding companies, that are regulated and supervised by the FDIC, the Office of the Comptroller of the Currency (“OCC”) and/or Federal Reserve Board (“Federal Reserve”).

⁵ For the purposes of providing a working definition for this letter only, we use the term “digital assets” to refer to cryptocurrency and other products that employ distributed ledger technologies. The Securities and Exchange Commission has defined a “digital asset” to refer “to an asset that is issued and/or transferred using distributed ledger technology or blockchain technology . . . including, but not limited to, so-called ‘virtual currencies,’ ‘coins,’ and ‘tokens.’” Custody of Digital Asset Securities by Special Purpose Broker Dealers, 86 Fed. Reg. 11,627 (Feb. 26, 2021).

where and how these innovations can be applied in their own businesses to best serve the needs of customers (or potential customers). This letter underscores the importance of bank involvement in the digital assets space, provides an overview of current bank practice and involvement, and addresses two key principles that we believe should guide the FDIC, the OCC and the Federal Reserve (the “federal banking agencies”) in approaching the regulation of digital assets.

I. The Importance of Bank Involvement in Digital Asset Products and Services

Both the public and federal banking agencies benefit from increased involvement by banks in offering digital asset products and services. Banks are already subject to comprehensive and robust risk management, supervision and examination processes, are subject to consumer protection laws and regulations, maintain strong capital buffers, carry deposit insurance, undertake well-developed anti-money laundering (“AML”) practices⁶ and know-your-customer (“KYC”) programs, and have substantial experience with incorporating new technologies into the financial system. Banks have the resources, talent and expertise to implement robust compliance programs, which is especially important with respect to digital assets, which present novel AML risks. To encourage banks to provide digital asset products and services, federal banking agencies should clarify and expand existing supervisory guidance to (1) clearly and unambiguously state that banks are permitted to engage in any activity—regardless of the involvement of digital assets—so long as a bank has the power and authority to provide a particular product or service and continues to operate in a safe and sound manner and (2) develop a regulatory framework for banks to independently apply to the treatment of digital assets.

The sustained growth in digital assets highlights the need for further federal regulatory guidance and the value of increased involvement by banks, which are key components of the domestic and global financial system. The interest in and the use of digital assets by consumers and businesses is here to stay. Accordingly, as with the development of now-traditional financial services and products over the course of the 20th century, federal banking agencies and the institutions they regulate must play an essential part in further developing the norms of transacting in digital assets. Federal banking agencies and banks must also work to manage the potential risks of digital assets, including reducing potential harm to consumers and the wider financial system. Without action by the federal banking agencies to affirm the ability and importance of banks engaging in digital asset activities, consumers will increasingly look to non-bank financial service providers and limited-purpose banking institutions for digital asset products and services, instead of banks.⁷

⁶ For the purposes of this letter, references to AML practices are inclusive of bank compliance with economic sanctions programs administered by the Office of Foreign Assets Control (“OFAC”).

⁷ Non-bank financial service providers and limited-purpose banking institutions have been early providers of digital asset products and services. Many products and services offered by limited-purpose banking institutions resemble traditional bank products and activities, including custodial services, payment services and activity akin to deposit-taking. States have established regulatory frameworks supporting non-bank financial services providers’ offering of these products. For example, the New York State Department of Financial Services (“NYDFS”) has been issuing licenses related to virtual currency business activities, known as BitLicenses, since 2015 pursuant to its virtual currency regulations under the New York Financial Services Law. The NYDFS has also granted limited-purpose trust company charters under the New York Banking Law, giving such entities state authority to act as qualified custodians and exchanges for digital assets. Similarly, in 2019, the State of Wyoming created Special Purpose Depository

Fractured regulation ultimately harms consumers. The continued state-by-state regulation of digital assets undermines long-standing goals of federal banking policy, as state-by-state regulation invites regulatory arbitrage, and states may be incentivized to attract digital asset providers through a regulatory “race to the bottom.”⁸ While the number and scope of non-banks and limited-purpose banking institutions offering digital asset products and services has increased, such entities are not necessarily subject to comprehensive and robust supervision and examination or consumer protection regimes, may have thin capital requirements and may not have sufficient resources to cover operational and other losses.⁹ Further, some non-banks offer digital asset products that bear similarities to bank products—like interest bearing accounts—even though such products lack FDIC insurance.¹⁰

The ability of non-banks and limited purpose banking institutions to offer digital asset banking products outside the federal banking regulatory framework undercuts carefully crafted measures to prevent financial instability. Though digital assets may be new, the potential harms to the financial sector are not: volatility, a lack of stable sources of capital and the potential for significant losses to consumers. Indeed, the founding rationale of federal deposit insurance, paired with supervision, was aimed at minimizing such risks. Consumers may also increasingly seek out decentralized finance (“DeFi”) products and services from non-bank providers, degrading, to some extent, the concept of financial intermediation.¹¹ Though banks will continue to perform the essential role of financial intermediation in the overwhelming majority of contexts, DeFi may erode the need for central financial intermediaries with respect to digital asset products and services, thus decreasing the safety-net that would otherwise be available to consumers of such products.¹²

Institution (“SPDI”) charters, Wyo. Stat. § 13-12-101, *et seq.*, authorizing the chartering of institutions focused on digital assets.

⁸ The Icelandic Financial Crisis presents an illustrative example of the perils of a lack of sufficient regulatory oversight. *See generally* Benediktsdóttir, Eggertsson and Þórarinnsson, *The rise, the fall, and the resurrection of Iceland*, National Bureau of Economic Research (Nov. 2017).

⁹ *See, e.g.*, BPI, *Beware the Kraken* (Oct. 21, 2020), <https://bpi.com/beware-the-kraken/>; BPI, *Why a Wyoming Charter is No Hail Mary for the Anti-Fractional Banking Team* (Nov. 9, 2020), <https://bpi.com/why-a-wyoming-charter-is-no-hail-mary-for-the-anti-fractional-banking-team/>.

¹⁰ Consumers may view such products as equally safe as traditional, FDIC-insured bank deposit accounts. One exchange advertises one such account to customers who are “looking for a dollar-based experience that’s more like an interest-bearing savings account . . .” *See* Coinbase, *How to earn crypto rewards*, <https://www.coinbase.com/learn/tips-and-tutorials/how-to-earn-crypto-rewards>; Gemini, *What is Gemini Earn?*, <https://support.gemini.com/hc/en-us/articles/360055836212-What-is-Gemini-Earn->.

¹¹ Decentralized finance seeks to offer financial products directly on the blockchain, using decentralized smart contracts. *See* Campbell, Ramachandran and Santoro, *DeFi and the Future of Finance* at 22 (Apr. 5, 2021), <https://ssrn.com/abstract=3711777>.

¹² The concept of financial intermediation is a foundation of the existing regulatory framework of banks and financial markets. As DeFi seeks to be decentralized, there may be no entity party to a DeFi transaction that would have a responsibility for ongoing compliance with applicable law or maintaining infrastructure stability in a particular DeFi marketplace. As a result, for example, there would be no clear application of disclosure requirements under securities law, examination or supervision requirements under banking law, or the application of other pertinent laws, regulations and requirements, such as broker-dealer registration or complying with AML or KYC requirements. Regarding infrastructure stability, DeFi marketplaces automatically process transactions, which could result in cascading losses if adequate protections are not put in place. *See* Iron Finance’s Titan Token Falls to Near Zero in DeFi Panic Selling,

Providing both an overarching principles-based approach and a clear analytical framework for digital asset products and services offered by banks would encourage the introduction of digital asset products and services by banks, which are subject to the highest levels of regulatory scrutiny, and would support the development of new risk management best practices. We believe promoting the development of digital asset markets and technology in the United States in the years to come is the approach best suited to maintain the United States' central role in the global financial system.

II. Current Bank Practice and the Development of Services Related to Digital Assets

Digital assets present potential benefits to banks, from reducing inefficiencies in traditional financial activities to allowing banks to offer innovative products and services to meet consumer demand. Despite concerns as to the current lack of regulatory guidance in some contexts, banks are beginning to offer digital asset management and custodial services, both in order to meet consumer demand for these services, and because of promising regulatory guidance from the OCC recognizing the existing authority of banks to provide custodial services.¹³ Beyond custodial services, and in response to the FDIC's questions concerning potential and current use cases, banks are also beginning to evaluate, among other digital asset products and services, the following:

- offering digital asset investment products to clients;
- support for trading digital assets (including cryptocurrency assets)—in both an agent or principal capacity, including derivatives, structured notes and exchange traded products referencing digital assets;
- payment systems and mobile payments platforms that support digital asset transactions;
- the settlement of obligations using digital assets, including in the use of delivery-versus-payment (“DvP”) and payment-versus-payment (“PvP”) securities settlement methods;
- the issuance of cryptocurrency as a credit or debit card reward;
- using digital assets on private, permissioned blockchain networks to improve internal operations; and
- lending involving digital assets, including accepting digital assets as collateral.

There is a clear market need for banking services relating to digital assets: consumer demand and growth in digital assets, including funds investing in such assets, continue and the size of the digital assets industry is significant. Fifteen percent of U.S. consumers own cryptocurrency, and a recent survey suggests that a majority of them would like banks to offer more digital asset products and services.¹⁴ Banks have seen demand for the use of distributed ledger technology to optimize settlement times and

Coindesk (June 17, 2021), <https://www.coindesk.com/iron-finance-defi-titan-iron-price-drop>. Allowing banks greater regulatory clarity in order to explore or participate in the DeFi space, to the extent possible, may lessen some of these concerns.

¹³ See, e.g., Authority of a National Bank to Provide Cryptocurrency Custody Services for Customers, OCC Interpretive Letter #1170 (July 2020) (providing that national banks have the authority to perform safekeeping and custody services for digital assets).

¹⁴ Ron Shevlin, *The Coming Bank-Bitcoin Boom*, FORBES (Apr. 19, 2021), <https://www.forbes.com/sites/ronshevlin/2021/04/19/the-coming-bank-bitcoin-boom-americans-want-cryptocurrency-from-their-banks/?sh=c94d1c249086>.

increase the liquidity of assets. There is also client demand for banks to provide prime brokerage, margin finance and cross-border payment services in digital assets.

Beyond the potential benefits of digital assets, the use of distributed ledger technology carries potential benefits in its own right, which may include:

- reduced needs for data reconciliation and confirmation of trade details between front and back offices post-trade;
- reduced operational inefficiencies, including with respect to cross-border payments;
- improved end-to-end processing speeds, data transfer and availability of funds;
- increased efficiency in capital allocation, thereby reducing funding costs and improving balance sheet, treasury, liquidity and collateral management;
- enhanced compliance, auditability, traceability and transparency abilities according to the nature of certain distributed ledger technology networks;
- reduced post-trade settlement risk by enabling the use of less intraday unsecured credit, including reducing the reliance on intermediaries; and
- the ability to deploy smart contracts to automatically manage specific actions related to a particular asset or transaction.

Nonetheless, we recognize that there remain legitimate challenges related to digital asset products and services. Banks acknowledge that AML practices have not yet been fully developed with respect to certain digital asset transactions, and appreciate that regulators note the varying degrees of AML risk associated with different types of digital asset services.¹⁵ The potential for banks to provide a solution to these challenges is evidenced by a proposed rulemaking by the Financial Crimes Enforcement Network (“FinCEN”). That proposal acknowledges, to the extent wallets are hosted by a regulated financial institution,¹⁶ that AML concerns are lessened as “financial institutions are subject to certain [Bank Secrecy Act] regulatory obligations when providing [Convertible Virtual Currency]-related services, including services involving hosted wallets.”¹⁷ We continue, and we encourage regulators to continue, to consider whether evolving diligence practices related to non-custodial wallet use, such as through an on-chain analytics-based AML review, can assist in narrowing or erasing the gap between custodial and non-custodial wallet use. Additionally, broadly speaking, banks have sought to address AML risks in nascent digital asset-related operations and will continue to do so through due diligence, risk management and supervisory dialogue. For instance, AML risks may be mitigated through a robust KYC process for blockchain users on a permission-based blockchain, as well as the use of blockchain

¹⁵ See Requirements for Certain Transactions Involving Convertible Virtual Currency or Digital Assets, 85 Fed. Reg. 83,840 (Dec. 23, 2020) (seeking comments on a proposal to require banks and money service businesses to submit reports, keep records and verify the identity of customers in relation to transactions in convertible virtual currency or digital assets with legal tender status held in unhosted wallets or held in wallets hosted in a jurisdiction identified by FinCEN).

¹⁶ A “hosted wallet” is an “account-based software program for storing cryptographic keys controlled by an identifiable third party,” which may be a bank or other licensed money services business. Authority to Hold Stablecoin Reserves, OCC Interpretive Letter #1172 at 1, n.3 (Sept. 2020). “Hosted wallets” are contrasted with “unhosted wallets,” where “the individual owner of a cryptocurrency maintains control of the cryptographic keys for accessing the underlying cryptocurrency.” *Id.* at 1, n.3.

¹⁷ Requirements for Certain Transactions Involving Convertible Virtual Currency or Digital Assets, 85 Fed. Reg. 83,840, 83,842 (Dec. 23, 2020)

technology that allows banks to identify and analyze the entire transaction history preceding a given transaction.¹⁸

Other challenges remain, including with respect to cybersecurity, integrating operations with legacy banking systems¹⁹ and appropriately delineating the responsibilities of certain participants on the blockchain. We do not believe these challenges are insurmountable, however; banks have a long history of addressing and managing similar risks throughout their operations and will continue to do so through due diligence, governance and risk management, disclosure and supervisory dialogue.²⁰ Given the existing challenges, banks have welcomed steps towards regulatory clarity with respect to the use of digital assets, including the consensus as to the ability of banks to act as custodians for digital assets²¹ and to participate in independent node verification networks.²²

To further address the development of the regulatory framework for banks' participation in the market for digital assets products and services, we suggest that two overarching principles, outlined below, inform any future regulations and guidance with respect to digital assets undertaken by the FDIC and other federal banking agencies.

III. Federal Banking Agencies Should Adopt a Consistent "General Permissibility" Approach for Activities Involving Digital Assets so long as Banks Continue to Operate in a Safe and Sound Manner

We urge the federal banking agencies to clearly and uniformly state that core activities associated with the business of banking and banks' incidental powers apply to activities regardless of the technology involved, and that banks have general authority to engage in digital asset activities—

¹⁸ Many of the most significant regulatory concerns associated with digital assets, particularly those related to AML and KYC compliance, arise at the exchange of fiat currency to cryptocurrency and vice versa (the "on/off ramps"). Participating in regulated on/off ramps could allow banks to apply KYC and AML compliance expertise to mitigate such risks, and banks may even assist in increasing consumer awareness of risks related to digital assets, including by informing consumers on the unique economic characteristics of digital assets and their treatment under tax law.

¹⁹ *See Statement on Crypto-Assets*, Basel Committee on Banking Supervision (Mar. 13, 2019), https://www.bis.org/publ/bcbs_n121.htm (stating that crypto-assets present operational risk (including fraud and cyber risks) and legal and reputational risks, among others). The establishment of and participation in "permissioned blockchains," whereby banks may act as known validators on the blockchain to ensure that transactions on the blockchain are valid, and the users on the blockchain have been appropriately identified, may mitigate certain risks.

²⁰ *See Statement on Crypto-Assets*, Basel Committee on Banking Supervision (Mar. 13, 2019), https://www.bis.org/publ/bcbs_n121.htm. *See also Guidance for a Risk-Based Approach, Virtual Assets and Virtual Asset Service Providers*, Financial Action Task Force (June 2019), available at <https://www.fatf-gafi.org/media/fatf/documents/recommendations/RBA-VA-VASPs.pdf>.

²¹ *See Authority of a National Bank to Provide Cryptocurrency Custody Services for Customers*, OCC Interpretive Letter #1170 (July 2020).

²² *See Authority to Use Independent Node Verification Networks and Stablecoins for Payment Activities*, OCC Interpretive Letter #1174 (Jan. 2021). Nodes are broken down into two main types: full nodes and lightweight nodes. Full nodes act as servers on a blockchain, maintain consensus and verify transactions. Lightweight nodes do not store the entire blockchain and instead broadcast transactions for processing. *See Josh Evans, Blockchain Nodes: An In-Depth Guide*, NODES.COM (Sept. 22, 2020), <https://nodes.com/>.

without regard to the characterization of the particular digital asset in question—so long as such activities fall within core or incidental banking activities.²³ Federal banking agencies do not need to issue incremental guidance as to whether a new product or service involving digital assets falls under a permissible banking activity, unless the facts and circumstances present novel or difficult legal interpretive challenges.²⁴ For instance, maintaining a record of bank dollar deposits on a distributed ledger is in no way different from maintaining any other record of deposit from a permissibility standpoint. This regulatory approach will be particularly beneficial as the use cases for digital assets have increased and continue to increase.

The view that the authority of banks to provide digital asset products and services should be evaluated on the basis of the nature of the products or services provided by the bank, regardless of the technology involved, has been recognized in part by the OCC. In Interpretive Letter No. 1170, the OCC determined that banks' offering of cryptocurrency custody services "falls within . . . longstanding authorities to engage in safekeeping and custody activities" and that custodial services are "among the most fundamental and basic services provided by banks."²⁵ The interpretive letter also noted that national banks providing services related to the safekeeping and custody of digital assets are the functional equivalent of providing such services for physical assets.²⁶ In other words, a bank should be able to perform custodial services for assets, whether recorded on paper, on a mainframe operated at an onsite or offsite data center, or on a distributed ledger, as custody of digital assets, from a legal perspective, does not meaningfully differ from the custody of traditional assets. The framework articulated by the OCC with respect to custodial services should be adopted by the FDIC and the Federal

²³ Pursuant to the National Bank Act, a national bank shall have the power to exercise "*all such incidental powers as shall be necessary to carry on the business of banking*; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes . . ." 12 U.S.C. § 24 (emphasis added). FDIC-insured state banks may not generally engage as principal in activity that is not permissible for a national bank. See 12 U.S.C. § 1831a(a)(1).

²⁴ The recent consultative document from the Basel Committee on Banking Supervision notes that "the prudential framework should apply the concept of 'technology neutrality' and not be designed in a way to explicitly advocate or discourage the use of specific technologies related to cryptoassets." Basel Committee on Banking Supervision, *Consultative Document: Prudential treatment of cryptoasset exposures* at 3-4 (June 2021), <https://www.bis.org/bcbs/publ/d519.pdf>. The technology-neutral approach argued for by the Basel Committee on Banking Supervision is consistent with the approach the OCC has taken in regard to digital assets for custody services, and is generally consistent with the principles-based approach that this letter advocates for. See *Authority of a National Bank to Provide Cryptocurrency Custody Services for Customers*, OCC Interpretive Letter #1170 at 10 (July 2020) ("The OCC generally has not prohibited banks from providing custody services for any particular type of asset . . .").

²⁵ *Authority of a National Bank to Provide Cryptocurrency Custody Services for Customers*, OCC Interpretive Letter #1170 at 6-7 (July 2020). State regulators have taken a similar approach. The Texas Department of Banking recently issued an industry notice affirming the authority of Texas state-chartered banks to provide customers with virtual currency custody services and stating that such authority already exists under Texas law. Industry Notice 2021-03: Authority of Texas State-Chartered Banks to Provide Virtual Currency Custody Services to Customers, Texas Department of Banking (June 10, 2021), <https://www.dob.texas.gov/sites/default/files/files/news/IndustryNotices/in2021-03.pdf>.

²⁶ See *Authority of a National Bank to Provide Cryptocurrency Custody Services for Customers*, OCC Interpretive Letter #1170 at 8 (July 2020).

Reserve, and further, should be applied more broadly to other permissible bank activities recognized to be part of the business of banking or the incidental powers of banks.²⁷

The federal banking agencies should also clearly delineate between the ability of a bank to engage in activity and the separate obligation of banks to operate in a safe and sound manner. The concept of permissibility, which requires an analysis of banking powers, is distinct from an analysis of whether a bank operates in a safe and sound manner and engages in sound risk management practices. Offering digital asset products and services, as with the introduction of many other banking products or services, is primarily a question of adequate risk management. Banks should be permitted to provide permissible banking services so long as banks adopt sound risk management practices that are effectively tailored to the level and type of risk inherent in the activity or service being provided, and so long as banks comply with all other applicable laws, including those relating to AML requirements.²⁸ In the case of digital assets—as with any other technological development—banks will determine whether adoption of new digital asset products and services, or incorporation of new digital asset technology into their businesses, is consistent with all regulatory obligations relating to operating in a safe and sound manner.

We believe that banks are well equipped to adapt their existing risk and compliance management frameworks to manage the unique risks posed by digital assets.²⁹ A framework that recognizes the general authority of banks to provide products and services involving digital assets, so long as such activities fall within a recognized banking activity and do not prevent banks from operating in a safe and sound manner, would allow banks to innovate while protecting consumers, provide customers with in-demand products and services, and limit risk to the financial system.

Similarly, federal banking agencies should acknowledge that there are many different types of digital assets with different structures and risk profiles.³⁰ Distributed ledger technology—at its base, a system for recording transactions—may be used to record the ownership of a traditional asset, such as real property, debt or conventional securities. Depending on their structure, digital assets that are

²⁷ Despite the broad statements in the OCC's letter relating to custody, subsequent interpretive letters, relating to holding stablecoin reserves and operating validation nodes, revert to a more asset-specific approach. *See generally* Authority to Hold Stablecoin Reserves, OCC Interpretive Letter #1172 (Sept. 2020) (addressing the authority of banks to hold deposits with respect to stablecoin reserves only); OCC Chief Counsel's Interpretation on National Bank and Federal Savings Association Authority to Use Independent Node Verification Networks and Stablecoins for Payment Activities, OCC Interpretive Letter #1174 (Jan. 2021) (addressing the permissibility of payment-related activities with respect to stablecoins only).

²⁸ *See* Authority of a National Bank to Provide Cryptocurrency Custody Services for Customers, OCC Interpretive Letter #1170 at 10 (July 2020) (noting that the due diligence process for new custodial services should involve a review of compliance with anti-money laundering rules); Authority to Hold Stablecoin Reserves, OCC Interpretive Letter #1172 at 3 (Sept. 2020) (“[N]ational banks may provide permissible banking services to any lawful business they choose, including cryptocurrency businesses, so long as they effectively manage the risks and comply with applicable law, including those relating to the BSA and anti-money laundering.”).

²⁹ Further, with respect to banks subject to ongoing federal banking supervision, supervisory teams receive information on proposed bank activities and are able to provide direct input, lessening the need for more formal case-by-case safety and soundness determinations.

³⁰ This may be of particular importance in the context of resolution planning, where a bank must identify and value digital assets held.

representations of traditional assets may more or less bear the same risk profile of the underlying asset. Other types of digital assets, such as stablecoins (depending on their structure), may also roughly track the risk profile of the underlying asset into which the stablecoin is convertible, recognizing that there may exist additional risk relating to the creditworthiness of the stablecoin issuer or the safeguarding and management of the underlying assets. These digital assets may be contrasted with cryptocurrencies that expose holders to high levels of volatility when compared to traditional, retail financial products. Though banks should determine whether the adoption of new digital asset products or services complies with operating in a safe and sound manner, it is possible that representations of traditional assets, or certain types of stablecoins, may be more readily adapted to existing bank risk management practices.

IV. Federal Banking Agencies Should Adopt a Framework for Banks to Categorize Digital Assets to Determine a Bank's Ability to Act as a Principal or Intermediary in Activities Involving Digital Assets

Digital assets have a wide range of financial, functional and other characteristics. As a result, they have been subject to overlapping—and at times conflicting—regulatory categorizations. Digital assets, depending on their features and the purpose of the categorization exercise, have been considered virtual currency, securities, commodities or a combination of these by federal banking agencies, FinCEN, the SEC, the CFTC and courts. As a result, different digital assets are subject to varying federal banking regulations and guidance, in addition to regulations and guidance promulgated by non-banking agencies.

How a digital asset is categorized from a legal perspective may lead to differing compliance obligations. With respect to many traditional banking products, the classification of the underlying digital asset would not be relevant to its regulatory treatment. For example, the permissibility of custodial services, in general, would not depend on the type of asset being held for safekeeping. However, the classification of a digital asset is of particular importance where a bank desires to act as a principal or as an intermediary to a transaction. Such activities include direct investment in digital assets by banks, market-making activity and the issuance of digital assets. For example, were a digital asset considered a commodity by the Federal Reserve, a bank may be permitted to act as a principal in, or invest in companies engaged in, a limited set of related activities under the Federal Reserve's regulations;³¹ if the CFTC also views the digital asset as a commodity, the company would be required to comply with relevant requirements under the Commodities Exchange Act depending on the nature of the transaction involving the digital asset. Similarly, digital assets that are considered securities by the FDIC and bought or sold on behalf of bank clients would be subject to the FDIC's securities recordkeeping requirements³² and, if held on a principal basis, would be subject to further regulatory limitations on dealing in, underwriting, and buying or selling securities. Digital assets that are considered securities by the SEC would also be subject to additional offer and sale requirements under the Securities Act.³³

³¹ See 12 U.S.C. § 1843(k)(1)(B).

³² See 12 C.F.R. § 344.4.

³³ See, e.g., 15 U.S.C. § 77e. The SEC and CFTC have taken disparate approaches to determining whether a digital asset is a security or commodity, respectively. The SEC has taken a case-by-case approach: SEC staff has noted that “[w]hether a particular digital asset . . . is a security under the federal securities laws is inherently a facts and circumstances determination[, which] requires a careful analysis of the nature of the instrument, including the rights it purports to convey, and how it is offered and sold.” SEC FinHub Staff, *SEC FinHub Staff Statement on OCC Interpretation*, SEC (Sept. 21, 2020),

The federal banking agencies, seeking to harmonize with other regulators, including the SEC and CFTC, should jointly develop an analytical framework to assist banks in assessing whether a digital asset should be considered a security, commodity, virtual currency or a combination thereof for purposes of federal banking law.³⁴ Where the classification by the SEC or CFTC of a digital asset as a security or commodity is clear, banks should be able to rely on that determination, except in instances where federal banking agencies explicitly make a determination that such digital asset should be treated differently for bank regulatory purposes. For instance, certain cryptocurrencies may warrant classification as cash equivalents due to their usage by customers, as opposed to being considered a security or commodity.³⁵ If there is no consensus among regulators as to a digital asset's classification, a process should be established whereby banks may seek an expedited "non-objection" from regulators as to certain treatment. Even without immediately issuing a classification of digital assets, banks would benefit from the federal banking agencies indicating whether they will take a unified, as opposed to an independent, approach to classification.

A digital asset system of classification should include general indicia for each regulatory class of digital asset, based on its structure and utilization in the market.³⁶ Banks would be able to use an interagency categorical framework to make independent determinations as to the required regulatory treatment of a given digital asset in light of the proposed activity undertaken by the consumer and bank. In light of the fact that the development of any such classification framework may take time, banks will continue to make independent judgments as to the appropriate regulatory treatment of digital assets.

<https://www.sec.gov/news/public-statement/sec-finhub-statement-occ-interpretation>. On the other hand, the CFTC has taken the view that all virtual currencies are commodities subject to anti-fraud and anti-manipulation provisions of the Commodity Exchange Act. *See* Retail Commodity Transactions Involving Certain Digital Assets, 85 Fed. Reg. 37,734 (June 24, 2020). The differing approaches taken by the SEC and the CFTC are driven in part by the differences in the statutes, regulations and case law that govern the regulation of securities and commodities.

³⁴ To date, the approach of the federal banking agencies is unclear with respect to their potential treatment of digital assets: though none have provided a systematic classification of digital assets, it is also true that federal banking agencies have not refrained entirely from categorizing digital assets. *See, e.g.,* Authority of a National Bank to Provide Cryptocurrency Custody Services for Customers, OCC Interpretive Letter #1170 at 1 n.3 (Jul. 2020) (defining cryptocurrencies both as a medium of exchange created and stored electronically and as digital assets not broadly used as currencies); Threshold for the Requirement to Collect, Retain, and Transmit Information on Funds Transfers that Begin or End Outside the United States, and Clarification of the Requirement to Collect, Retain, and Transmit Information on Transactions Involving Convertible Virtual Currencies and Digital Assets with Legal Tender Status, 85 Fed. Reg. 68,005, 68,006 (Oct. 27, 2020) (the Federal Reserve and FinCEN defining a "convertible virtual currency" as "a medium of exchange (such as cryptocurrency) that either has an equivalent value as currency, or acts as a substitute for currency, but lacks legal tender status").

³⁵ Relatedly, the OCC has recognized that "[f]inancial instruments, intangible assets or rights, and indices are not physical commodities." OCC Bulletin 2015-35, n. 3 (Aug. 4, 2015). Digital assets that constitute financial instruments, or that represent intangible assets or rights should also not be classified as physical commodities.

³⁶ The SEC Staff has provided a framework to assist individuals in assessing whether a particular digital asset is an "investment contract" and thus a security. *See* SEC, *Framework for "Investment Contract" Analysis of Digital Assets* (Apr. 3, 2019), <https://www.sec.gov/corpfin/framework-investment-contract-analysis-digital-assets>.

However, the creation of a formalized taxonomy would assist banks in doing so, especially as the range and complexity of digital assets, and related products and services, increase. A consistent interagency approach among federal banking agencies would both provide clarity and deter forum-shopping by regulated entities. Furthermore, in developing any analytical framework, the federal banking agencies should be aware of the approach taken by international regulators, including by the Basel Committee on Banking Supervision, and should generally seek to harmonize guidance among domestic and international regulators.³⁷ We support the FDIC, OCC and Federal Reserve, consulting as appropriate with other agencies such as the SEC and CFTC, in establishing an interagency policy team to examine digital assets and their regulation, and developing a framework for classifying digital assets should be one of its priorities.³⁸

The development of a taxonomy will likely not provide answers in all circumstances, given the wide range of ways in which any particular digital asset may be used and the complexity of some types of digital assets. For instance, a cryptocurrency (itself potentially a security, commodity, virtual currency or combination thereof) may be the means of exchange underlying a smart financial contract, which may in turn be classified as a security, debt instrument or derivative.³⁹ Accordingly, we urge federal banking agencies to recognize that whether a digital asset clearly falls within the bounds of a taxonomy may not be the only determinant of whether any particular activity is permitted and, as noted in Section III above, the permissibility of an activity involving digital assets should be determinable based on the role that a bank or an affiliate performs in a transaction.

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³⁷ Basel Committee on Banking Supervision, *Consultative Document: Prudential treatment of cryptoasset exposures* (June 2021), <https://www.bis.org/bcbs/publ/d519.pdf>.

³⁸ Apart from the Basel Committee proposing a crypto-asset taxonomy for the purpose of informing credit and market risk requirements, the Global Financial Markets Association (“GFMA”) has also recognized a need for identifying different classes of crypto-assets. *See, e.g.*, Global Financial Markets Association, *Consultation Response: Basel Committee on Banking Supervision – Designing a Prudential Treatment for Crypto-Assets* (Mar. 2020), [gfma-bcbs-prudential-crypto-assets-final-consolidated-version-20200427.pdf](https://www.gfma.org/wp-content/uploads/2020/04/gfma-bcbs-prudential-crypto-assets-final-consolidated-version-20200427.pdf) (proposing a taxonomy of crypto-assets to assist in identifying and mitigating prudential risks); Global Financial Markets Association, *Consultation Response: Financial Stability Board – Addressing the regulatory, supervisory and oversight challenges raised by “global stablecoin” arrangements* (July 2020), [gfma-response-fsb-cp-global-stablecoins.pdf](https://www.gfma.org/wp-content/uploads/2020/07/gfma-response-fsb-cp-global-stablecoins.pdf) (arguing for the development of a crypto-asset taxonomy to assign appropriate regulatory treatment to such assets).

³⁹ *See generally* Campbell, Ramachandran and Santoro, *DeFi and the Future of Finance* (Apr. 5, 2021), <https://ssrn.com/abstract=3711777> (describing various applications of blockchain-based smart contracts).

The Associations appreciate the opportunity to comment on the FDIC's request for information. If you have any questions, please contact Dafina Stewart by phone at (202) 589-2424 or by email at dafina.stewart@bpi.com or André B. Cotten by phone at (202) 552-6360 or acotten@consumerbankers.com.

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