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A New “Operation Choke Point”? The Quickly Constricting Rules on Crypto Activities for Banks

By Douglas Landy, Glen R. Cuccinello, Leel Sinai and Chante Eliaszadeh*

In this article, the authors review a recent joint statement by federal bank regulators regarding whether banks can continue to provide banking services to the crypto industry, as well as whether they can continue to engage in related activities themselves.

Perhaps responding to criticism that the prior actions and guidance could result in the crypto industry being excluded from the regulated banking system, the Board of Governors of the Federal Reserve System (the Federal Reserve), the Office of the Comptroller of the Currency (the OCC) and the Federal Deposit Insurance Corporation (the FDIC) have issued a “Joint Statement on Liquidity Risks to Banking Organizations Resulting from Crypto-Asset Market Vulnerabilities” (the Joint Liquidity Statement). In the Joint Liquidity Statement, the agencies stated:

The statement reminds banking organizations to apply existing risk management principles; it does not create new risk management principles. [footnote deleted] Banking organizations are neither prohibited nor discouraged from providing banking services to customers of any specific class or type, as permitted by law or regulation. (emphasis added)

Recent actions and guidance by the federal banking regulators, and the recent statement by the White House, against crypto entities have raised the question about whether the banking industry is entering a new “Operation Choke Point,” in which banks are discouraged or precluded from providing banking services to legal cryptocurrency industries.¹ This article reviews what has been issued and whether banks can continue to provide banking services to the crypto industry, as well as whether they can continue to engage in related activities themselves.

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¹ “Operation Choke Point” refers to an initiative by the Department of Justice beginning in 2013 that investigated banks for the business they were doing with firearms manufacturers, payday lenders and certain other legal businesses believed to be at high risk for money laundering and fraud. See Probe Turns Up Heat on Banks, available at https://www.wsj.com/articles/SB10001424127887323838204578654411043000772.
BACKGROUND

After Bitcoin and Ethereum reached their all-time highs in November 2021, the cryptocurrency market entered a downward spiral that continued throughout 2022. That spiral was exacerbated in May 2022 with the collapse of TerraUSD (UST), an ostensibly dollar-pegged “stablecoin” that was intended to maintain its peg algorithmically through arbitrage pressure. UST entered a death spiral to zero that ultimately helped lead to the further collapse of Three Arrows Capital, Voyager Digital, LLC, Celsius Network Limited, and much of the rest of the interconnected market. The most recent blow to hit the crypto markets was the collapse of both Sam Bankman-Fried’s cryptocurrency exchange FTX, and its affiliated hedge fund, Alameda Research, in November 2022. This relentless market collapse hit as traditional financial institutions started engaging in crypto-asset activities, and led to immediate negative effects on banks with exposure to the crypto markets.²

OFFICE OF THE COMPTROLLER OF THE CURRENCY “BUSINESS OF BANKING” LETTERS

Prior to the market collapse in 2022, the OCC released several interpretive letters throughout 2020 and 2021. On July 22, 2020, the OCC issued Interpretive Letter 1170, which authorized national banks to provide certain cryptocurrency custody services on behalf of customers as part of the “business of banking.”³ On September 21, 2020, the OCC issued Interpretive Letter 1172 authorizing national banks to hold cash deposits reserving stablecoin tokens also as part of the “business of banking” as authorized by 12 U.S.C. § 24.⁴ The ability to provide custodial services and to take cash deposits have long been considered core banking activities by the OCC.⁵

³ OCC Interpretive Letter No. 1170 (July 22, 2020), available at https://www.occ.gov/topics/charters-and-licensing/interpretations-and-actions/2020/int1170.pdf. The OCC considers the following factors when determining whether an activity is part of the business of banking, including: (i) whether the activity is the functional equivalent to, or a logical outgrowth of, a recognized banking activity; (ii) whether the activity strengthens the bank by benefiting its clients or its business; (iii) whether the activity involves risks similar in nature to those already assumed by banks; and (iv) whether the activity is authorized for State-chartered banks. 12 CFR 7.1000(d).
⁵ 12 CFR 5.20(e)(1)(i) (providing that the OCC may charter “a special purpose bank” that either “limits its activities to fiduciary activities” or engages in (at least one of) (i) receiving
National banks are also authorized to engage in other activities “incidental to the business of banking” if it is convenient or useful to an activity that is specifically authorized for national banks or to an activity that is otherwise part of the business of banking. The OCC issued Interpretive Letter 1174 on January 4, 2021, which found that national banks may act as nodes on an independent node verification network (i.e., distributed ledger) to verify customer payments, and may engage in certain stablecoin activities to facilitate payment transactions on a distributed ledger.

More recently, the OCC began to back away from its prior approvals of crypto-asset activities for national banks. It issued Interpretive Letter 1179 on November 18, 2021, which stated that while the activities described in Interpretive Letters 1170, 1172 and 1174 remained legally permissible for national banks, such legal permissibility also included a requirement that any national bank must first demonstrate, to the satisfaction of its regional OCC supervisory office, that it has controls in place to conduct the activity in a safe and sound manner, a so-called “pre-approval” requirement.

The OCC’s more cautious approach faced an immediate test on January 18, 2022, when the OCC conditionally approved Social Finance Inc.’s (SoFi) application to create SoFi Bank, N.A. (SoFi Bank) through the acquisition of Golden Pacific Bank, N.A. on the condition “that the resulting bank will not engage in any crypto-asset activities or services” without the prior approval from the OCC. SoFi Bank’s parent company, SoFi Technologies, Inc.’s application

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6 In determining whether an activity is convenient or useful to such activities, the OCC considers the following factors: (i) whether the activity facilitates the production or delivery of a bank’s products or services, enhances the bank’s ability to sell or market its products or services, or improves the effectiveness or efficiency of the bank’s operations, in light of risks presented, innovations, strategies, techniques and new technologies for producing and delivering financial products and services; and (ii) whether the activity enables the bank to use capacity acquired for its banking operations or otherwise avoid economic loss or waste. 12 C.F.R. § 7.1000(d)(1)(i)-(ii).


9 Office of the Comptroller of the Currency, OCC Conditionally Approves SoFi Bank, National Association, News Release 2022-4 (January 18, 2022). We do not know what “crypto-asset activities or services” SoFi applied to begin or maintain; however, this condition may be a statement by the OCC that the crypto-asset activities or services factually covered are impermissible for a national bank as not being part of the business of banking or incidental thereto. It could also be a statement, pursuant to Interpretive Letter 1179, that SoFi had not
to the Federal Reserve to become a bank holding company was granted around
the same time, and in the approval letter the Federal Reserve Bank of San
Francisco (FRBSF) stated that the crypto-asset activities engaged in by SoFi’s
non-bank, digital-asset-focused subsidiary, SoFi Digital Assets, could be re-
tained for a period of two years (with the possibility of three additional one-year
extensions) pursuant to Section 4(a)(2) of the Bank Holding Company Act of
1956, as amended (the BHC Act).10 Put another way, the FRBSF found that
the crypto-asset activities engaged in indirectly by SoFi Technologies, Inc. were
not financial in nature, incidental to a financial activity, or complementary to
a financial activity, and therefore were impermissible activities under Section 4
of the BHCA, and could only be engaged in under a temporary authority
available to newly formed bank holding companies for a limited period of
time.11

On October 28, 2022, the OCC approved the merger of New York
Community Bank and Flagstar Bank, N.A., with Flagstar Bank as the resulting
institution. One condition of approval imposed by the OCC was that Flagstar
refrain from increasing and divest from its interest in the USDF Consortium –
a group of nine banks that aims to further the adoption and interoperability of
tokenized fiat deposits on blockchain – and Hash holdings (the native token of
the Provenance Blockchain), unless the OCC finds that they are permissible for
national banks.12 In essence, this commitment imposes the pre-approval
requirement of Interpretative Letter 1179 to any crypto-activities or services in
which the new Flagstar may wish to engage.

shown to the OCC’s satisfaction that it could engage in such activities or services in a safe and
sound manner.

10 SoFi Technologies announced that its application to become a bank holding company was
approved by the Federal Reserve on January 18, 2022. SoFi RECEIVES REGULATORY APPROVAL TO
BECOME A NATIONAL BANK (Jan. 18, 2022), available at https://www.sec.gov/Archives/edgar/data/
1818874/000181887422000004/exhibit991_8-k1182022.htm.

11 We do not know exactly what those activities are. The Federal Reserve refused repeated
FOIA requests to release that information, stating that the responsive information contains
“nonpublic proprietary information (e.g., information related to SoFi’s business strategies and
internal financial information).” This information, the Federal Reserve found, is subject to
withholding and was withheld pursuant to exemption 4 of the FOIA, 5 U.S.C. § 552(b)(4). In
addition, the Federal Reserve determined that the information should be withheld because it is
“reasonably foreseeable that disclosure would harm an interest protected by an exemption
described in subsection (b) of the FOIA, 5 U.S.C. § 552(b).” SoFi does list certain crypto-asset
activities and services provided on its website. See Buy Cryptocurrency: Trade Bitcoin, Ethereum
+28 Coins | SoFi (accessed on February 21, 2023), available at https://www.sofi.com/invest/buy-
cryptocurrency/.

JOINT STATEMENT BY THE FEDERAL BANK REGULATORY AGENCIES

On January 21, 2023, the Federal Reserve, the FDIC, and the OCC (collectively, the Agencies) issued an Interagency Statement on “Crypto-Asset Risks to Banking Organizations” (the Interagency Statement). The Interagency Statement highlighted the Agencies’ concerns about risks to the banking institutions in light of the volatility experienced in the crypto-asset markets over the past year. The risks identified in the Interagency Statement include, among other things, legal uncertainties related to custody practices, redemptions, and ownership rights, safety and soundness, fraud and misrepresentation, contagion, and stablecoin run risk. The Agencies also cited heightened risks associated with open, public, and/or decentralized networks, or similar systems, including, but not limited to, the lack of governance mechanisms establishing oversight of the system; the absence of contracts or standards to clearly establish roles, responsibilities, and liabilities; and vulnerabilities related to cyber-attacks, outages, lost or trapped assets, and illicit finance.

The Interagency Statement appears to signal the adoption of a more consistent approach among the federal bank regulators to concerns about safety and soundness requirements for new crypto-asset activities and whether such

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14 Certain state bank regulatory agencies have also expressed concern in regards to risks associated with stablecoin arrangements. For example, on March 13, 2023, in an action against a stablecoin from a U.S.-issuer, the New York Department of Financial Services (NYDFS) ordered Paxos Trust Company (Paxos), a limited purpose trust company under the supervision of the NYDFS, to cease minting Paxos-issued BUSD as a result of several unresolved issues related to Paxos’ oversight of its relationship with Binance through Paxos-issued BUSD. In response, on February 13, 2023, Paxos notified customers of its intent to end its relationship with Binance for BUSD. See N.Y. Dep’t of Fin. Servs., NOTICE REGARDING PAXOS-ISSUED BUSD (Feb. 13, 2023), available at https://www.dfs.ny.gov/consumers/alerts/Paxos_and_Binance.

15 On February 16, 2023, the Office of Inspector General (OIG) of the FDIC issued its annual assessment of the “Top Management and Performance Challenges Facing the” FDIC. Among those challenges, the OIG identified “Supervising Risks Posed by Digital Assets.” According to OIG, FDIC data, as of January 2023, shows that the FDIC was aware that 136 insured banks had ongoing or planned crypto asset-related activities. For example, these banks have arrangements with third parties that allow bank customers to buy and sell crypto assets. Banks also provide account deposit services, custody services, and lending to crypto asset exchanges. Banks’ interactions with crypto assets present risks for the FDIC in supervising banks and resolving failed institutions. Top Management and Performance Challenges Facing the Federal Deposit Insurance Corporation, available at https://www fdicoig.gov/sites/default/files/reports/2023-02/TMPC%20Final%202-16-23_0.pdf?source=govdelivery&utm_medium=email&utm_source=govdelivery.
considerations are or are not separate from the question of legal permissibility.\textsuperscript{16} As evidenced in the policy statement it issued on January 27, 2023 (described below) and Supervision and Regulation Letter 22-6 (SR 22-6),\textsuperscript{17} the Federal Reserve seems to distinguish between legal permissibility (whether an activity is authorized as a legal matter) from permissibility for the particular bank in question (which also requires the bank’s regulator to approve or provide non-objection in light of, among other things, the bank’s internal control framework and ability to engage in such activity in a safe and sound manner). The Federal Reserve identified safety and soundness, consumer protection, financial stability, and legal permissibility as separate items of concern in its consideration of banks’ proposed crypto-asset activities. In contrast, the OCC’s actions and statements in this area, as evidenced in precedents such as OCC Interpretive Letter 1179,\textsuperscript{18} indicate that the OCC takes the position that whether or not an activity can properly be considered to be part of the business of banking necessarily also involves a consideration of whether the activity can be conducted at all in a safe and sound manner. The FDIC similarly highlights safety and soundness, consumer protection, and financial stability implications of crypto-asset activities in its Financial Institution Letter on Notification of Engaging in Crypto-Related Activities (FIL-16-2022).\textsuperscript{19}

We note that the focus on safety and soundness as a requirement for an activity to be permissible, as it appears in the Policy Statement, the Joint

\textsuperscript{16} In his recent remarks at the Global Interdependence Center Conference: Digital Money, Decentralized Finance, and the Puzzle of Crypto, La Jolla, California, Federal Reserve Governor Christopher J. Waller stated, “While I don’t care if people take on risky investments or engage in risky business ventures, banks and other financial intermediaries must engage in any activity they do in a safe and sound manner. I’m supportive of prudent innovation in the financial system, while at the same time concerned about banks engaging in activities that present a heightened risk of fraud and scams, legal uncertainties, and the prevalence of inaccurate and misleading financial disclosures. As with any customer in any industry, a bank engaging with crypto customers would have to be very clear about the customers’ business models, risk-management systems, and corporate governance structures to ensure that the bank is not left holding the bag if there is a crypto meltdown. And banks considering engaging in crypto-asset-related activities face a critical task to meet the “know your customer” and “anti-money laundering” requirements, which they in no way are allowed to ignore. So far, spillovers to other parts of the financial system from the stress in the crypto industry have been minimal.” Governor Waller’s remarks are available at https://www.federalreserve.gov/newsevents/speech/waller20230210a.htm.

\textsuperscript{17} https://www.federalreserve.gov/supervisionreg/srletters/SR2206.htm.


Statement, and the Agencies’ guidance noted above, clearly arises in the context of, and has been motivated by, market-related and bad actor events that have occurred recently in the crypto space. The principles reflected in such guidance are nonetheless not specifically limited to crypto-asset activities, but rather would seem to be relevant, at least in theory, to all types of new activities by banking institutions. If the Agencies are indeed taking that broader approach, it would make for a substantial departure from the traditional approach of the Agencies in dealing with proposals by banking institutions to conduct previously unapproved activities, which have focused to a substantial extent on issues of legal permissibility.

The Policy Statement refers to “crypto-assets” as digital assets (such as BTC and ETH) issued using distributed ledger technology and cryptographic techniques. The Federal Reserve did not include in this category assets represented on a blockchain that are more appropriately categorized within a recognized, traditional asset class (such as properly registered securities that are issued, stored, or transferred through a regulated clearing agency) but reserved the right to treat such assets as “crypto-assets” if using distributed ledger technology and cryptographic techniques changes the risks of that traditional asset.

Some banks have explored offering tokenized dollar products and services. Although permitted, banks are required to seek pre-approval or non-objection from the Agencies, as applicable and noted above. Pertinent to the provision of such products and services has been the question of whether FDIC insurance applies to tokenized dollars as so-called “pass-through insurance,” and a number of other interpretive questions for which there is no definitive interpretive guidance.

FEDERAL RESERVE POLICY STATEMENT AND RELATED MEMBER BANK APPLICATION DENIAL

In an effort to align the permissibility of crypto activities for all member banks of the Federal Reserve System (the FRS), which includes all national banks and state member banks), Federal Reserve issued a policy statement under Section 9(13) of the Federal Reserve Act (FRA) limiting permissible state member bank activities (the Policy Statement) while simultaneously announcing the denial of Custodia Bank, Inc.’s (Custodia) application for membership to the FRS.²⁰ The Policy Statement exercised the Federal Reserve’s discretionary

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authority under FRA Section 9(13) to limit the activities of insured and uninsured state member banks to those permissible for national banks. The authority to engage in permissible activities under Section 9(13) also must be exercised consistent with Section 24 of the Federal Deposit Insurance Act (the FDIA), which prohibits all insured state banks from principally engaging in activities not permissible for national banks unless authorized by federal statute or the FDIC. Section 24 of the FDIA does not apply to uninsured state banks.

The Policy Statement sets forth a rebuttable presumption prohibiting state member banks from engaging in activities impermissible for national banks unless authorized by federal statute or FDIC regulation, whether or not such activity is permissible under applicable state law. That presumption may be rebutted only if (1) there is a “clear and compelling” reason justifying the “deviation in regulatory treatment among federally supervised banks,” and (2) the state member bank has “robust” risk management plans for the proposed activity that is in accordance “with principles of safe and sound banking.” While the Policy Statement is much broader in application to crypto-asset-related activities, the Federal Reserve addressed state member bank inquiries into “crypto-asset-related activities” and concluded that the rebuttable presumption would apply to state member banks seeking to either hold crypto-assets as principal or issue dollar-denominated tokens.

CUSTODIA APPLICATIONS DENIED

Custodia is an uninsured special purpose depository institution chartered under Wyoming banking law, focused on providing digital asset banking, custody, and payment solutions. On October 29, 2020, Custodia applied to the Federal Reserve Bank of Kansas City (FRBKC) for a Federal Reserve “master account” that would give Custodia access to the Federal Reserve’s account services, including its electronic payments system. In August 2021, Custodia also applied to the Federal Reserve for membership in the FRS, which (if accepted) would subject Custodia to oversight and regulation by the Federal Reserve as an uninsured state member bank.

For almost two years, Custodia’s master account and Federal Reserve membership applications went undecided. Consequently, on June 7, 2022, Custodia filed suit against the Federal Reserve and the FRBKC (collectively, the FR Defendants) in the United States District Court of Wyoming for their alleged unreasonable delays in processing Custodia’s applications. On Novem-

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ber 11, 2022, U.S. District Judge Skavdahl partially granted and partially denied the FR Defendants’ motion to dismiss, leaving intact Custodia’s Administrative Procedure Act, mandamus, due process, and declaratory judgment claims. Judge Skavdahl dismissed Custodia’s alternative claims for relief in the event its applications were denied as non-justiciable on ripeness grounds because the applications had not yet been decided.

On January 27, 2023, FRBKC issued Custodia a letter denying its master account application and the FR Defendants promptly filed a new motion to dismiss the remaining claims (which sought prompt decisions on the applications by the FR Defendants) as moot in light of the FRBKC decision. On the same day, the Federal Reserve announced its denial of Custodia’s application to become a member of the Federal Reserve System, citing that Custodia’s application, as submitted, was inconsistent with the required factors under the law. As noted in the Federal Reserve’s Press Release, Custodia “proposed to engage in novel and untested crypto activities that include issuing a crypto asset on open, public and/or decentralized networks,” a business model about which the Federal Reserve is particularly concerned, as the Federal Reserve and the other agencies made clear in the Interagency Statement. Specifically, the Federal Reserve stated that Custodia’s crypto activities are “highly likely to be inconsistent with safe and sound banking practices,” and that Custodia’s “risk management framework was insufficient to address concerns regarding the heightened risks associated with its proposed crypto activities, including its ability to mitigate money laundering and terrorism financing risks.”

SUMMARY OF THE WHITE HOUSE STATEMENT

On January 27, 2023 – the same day as the Policy Statement and the Federal Reserve’s denial of Custodia – the White House’s National Economic Council (the Administration) released “The Administration’s Roadmap to Mitigate Cryptocurrencies’ Risks” (the Administration Announcement). The Administration Announcement emphasized the need to effectively regulate crypto-assets to protect investors, hold bad actors accountable, and – in explicit reference to the May 2022 “so-called stablecoin” collapse – prevent turmoil in the cryptocurrency sector from spreading to the broader financial system.

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The Administration Announcement is chiefly concerned with crypto-asset entities “ignoring” financial regulations, failing to institute “basic” risk controls, and engaging in fraudulent and misleading behavior. To that end, the Administration highlighted increased government and regulatory enforcement efforts and the issuance of necessary guidance. The Administration encouraged regulators to continue their efforts to clarify regulatory ambiguity and limit financial institutions’ exposure to the risks of cryptocurrencies.

The Administration noted that additional efforts are needed and unveiled its plan to release digital assets research and development priorities – priorities the Administration contends will help the technologies powering cryptocurrencies protect consumers “by default.” The Administration further called for Congressional action to expand regulators’ powers to prevent the misuse of customer assets, strengthen crypto-asset company disclosure requirements, and provide more severe penalties for violations of illicit-finance rules. The Administration concluded by warning against Congressional action that could “greenlight” mainstream financial institutions, such as pension funds, to “dive headlong into cryptocurrency markets.”

THE JOINT LIQUIDITY STATEMENT

On February 23, 2023, the Agencies issued the Joint Liquidity Statement. The Agencies notes that “certain sources of funding from crypto-asset-related entities may pose heightened liquidity risks to banking organizations due to the unpredictability of the scale and timing of deposit inflows and outflows, including, for example:

• Deposits placed by a crypto-asset-related entity that are for the benefit of the crypto-asset-related entity’s customers (end customers). The stability of such deposits may be driven by the behavior of the end customer or crypto-asset sector dynamics, and not solely by the crypto-asset-related entity itself, which is the banking organization’s direct counterparty. The stability of the deposits may be influenced by, for example, periods of stress, market volatility, and related vulnerabilities in the crypto-asset sector, which may or may not be specific to the crypto-asset-related entity. Such deposits can be susceptible to large and rapid inflows as well as outflows, when end customers react to crypto-asset-sector-related market events, media reports, and uncertainty.

• Deposits that constitute stablecoin-related reserves. The stability of

such deposits may be linked to demand for stablecoins, the confidence of stablecoin holders in the stablecoin arrangement, and the stablecoin issuer’s reserve management practices. Such deposits can be susceptible to large and rapid outflows stemming from, for example, unanticipated stablecoin redemptions or dislocations in crypto-asset markets.

The Agencies then reminded banking organizations that such risks are subject to all applicable risk management and reporting requirements, and all applicable laws and regulation, including those covering brokered deposits.26

THE PATH AHEAD

The Agencies’ actions, complemented by the Administration’s continuous research and statements on the risks of crypto-asset business activities for banking institutions, leave a trail of indications as to what the banking industry is likely to see in the year ahead. Such actions denote an effort by the Agencies to consolidate their regulatory posture with regard to such activities in the absence of legislative direction. As a result of such efforts, banks are faced with a limited set of crypto-asset activities in which they may engage, most of which are subject to pre-approval or non-objection by the Agencies.

A national bank may provide cryptocurrency custody activities under Interpretive Letter 1170, which the OCC described as “taking possession of the cryptographic access keys to that unit of cryptocurrency.”27 As stipulated in Interpretive Letter 1179, a bank may engage in such cryptocurrency custody activities if it is able to demonstrate, to the satisfaction of its supervisory office, that it has controls in place to conduct the activity in a safe and sound manner. As noted in Interpretive Letter 1179, a bank already engaged in such activity as of the date of publication of Interpretive Letter 1179 does not need to obtain supervisory non-objection.28

Other activities, such as operation of a closed-loop network or token transfer system, issuance of stablecoins or tokenized deposits, holding cash deposits as reserves for issued stablecoins, and holding crypto-assets as principal, present their own regulatory hurdles, all of which must be conducted in a safe and sound manner and in compliance with consumer, anti-money-laundering, and anti-terrorist-financing laws.29 The standards by which banks may satisfy these

26 See 12 CFR 337.6.
29 Federal Reserve Policy Statement on Section 9(13) of the Federal Reserve Act (Jan. 27,
requirements remain unclear and ill described by the Agencies, which therefore leaves the Agencies near full discretion to approve or disapprove pre-approval requests for almost any reason.

Banks are likely prohibited, for the time being, from engaging in crypto-asset activities on “open, public and/or decentralized networks,” as opposed to those networks that are closed, permissioned, and centralized. The Agencies have shown a clear aversion to permitting banks to engage in such open, public and/or decentralized network. Consistent with the Agencies’ concern for safety and soundness considerations, and permissibility more generally, the Agencies appear to prefer for banks, to the extent they wish to engage in crypto-asset activities, to operate on blockchain networks that may be more easily observed, maintained, and managed, taking into account prominent risks such as fraud and manipulation, illicit financial transactions, runs on the market, hacking and contagion.

Under OCC Interpretive Letter 1174, national banks may act as nodes on an independent node verification network (i.e., distributed ledger) to verify customer payments, and may engage in certain stablecoin activities to facilitate payment transactions on a distributed ledger. The OCC acknowledged that certain stablecoins may be backed by U.S. dollars, while others “may be more complex, backed by commodities, cryptocurrencies, or other assets but with values that are pegged to a fiat currency or managed by algorithm.”\(^\text{30}\) It should be noted, however, that Interpretive Letter 1174 discussed its view regarding the ability of national banks to engage in stablecoin issuance within the context of a dollar-backed product. As noted by the OCC, “[j]ust as banks may buy and sell [electronically stored value] as a means of converting the [electronically stored value] into dollars (and vice versa) to complete customer payment transactions, banks may buy, sell, and issue stablecoin to facilitate payments.”\(^\text{31}\) In this regard, the OCC appears to have permitted, subject to supervisory non-objection under Interpretive Letter 1179, the issuance of stablecoins that are dollar-backed tokens.\(^\text{32}\) The OCC did not make explicit its view as to the issuance of “more complex” stablecoins referenced above.

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31 OCC Interpretive Letter No. 1174 (Jan. 4, 2021) at 7.

32 Neither the OCC nor the Federal Reserve defined what it considered to be the difference between a stablecoin pegged to U.S. dollars and a tokenized dollar deposit. In practical terms one can consider the market difference to be that a stablecoin is an instrument issued by a non-bank that is an obligation reserved (stated to be collateralized) by U.S. dollars and other short-term
In the Policy Statement, the Federal Reserve stated the view that a state member bank seeking to issue what it referred to as a “dollar token” (but, importantly, did not distinguish from the term “stablecoin” referred to in Interpretive Letter 1174) would be required to “adhere to all the conditions the OCC has placed on national banks with respect to such activity, including demonstrating, to the satisfaction of Federal Reserve supervisors, that the bank has controls in place to conduct the activity in a safe and sound manner, and receiving a supervisory nonobjection before commencing such activity.”

The Federal Reserve specified, however, that tokens issued on open, public, and/or decentralized networks, or similar systems, are highly likely to be inconsistent with safe and sound banking practices because they raise concerns related to operational, cybersecurity, and run risks, and may also present significant illicit finance risks. Accordingly, banks appear free to pursue supervisory nonobjection for the purpose of issuing dollar-backed tokens on closed-loop, permissioned blockchain networks, such as those established on an intra-bank or inter-bank (e.g., as part of a consortium) basis.

The Agencies appear to be unwilling to permit banks to hold crypto-assets such as bitcoin and ether, as principal, in the near term. The Policy Statement notes that, “[t]o date, the OCC has not made a determination addressing the permissibility of a national bank holding cryptoassets as principal, other than ‘stablecoins’ to facilitate payments subject to the conditions of OCC Interpretive Letter 1179.” In this regard, the Federal Reserve noted that it would “presumptively prohibit state member banks from engaging in such activity under section 9(13) of the Act.” The FDIC is further bound by the restriction that “an insured State bank may not engage as principal in any type of activity that is not permissible for a national bank – (A) unless the [FDIC] has highly liquid instruments; while a tokenized dollar is an instrument issued by a bank that is a tokenized version of a related dollar deposit, is not backed by specific reserves or collateral (other than the issuer bank’s general cash reserves and other liquidity requirements) and does not itself carry independent value outside of the value of the underlying deposit.


34 Yet, see the conditions placed by the OCC on Flagstar. OCC Conditional Approval Letter No. 1299 (Oct. 27, 2022).

35 See OCC Interpretive Letter No. 1174 (Jan. 4, 2021); OCC Interpretive Letter No. 1179 (Nov. 18, 2021); this statement appears to overlook the SoFi approval letter described above.

determined that the activity would pose no significant risk to the Deposit Insurance Fund.” As noted in the Interagency Statement, “[b]ased on the A[gentures’ current understanding and experience to date, the A[gentures believe that issuing or holding as principal crypto-assets that are issued, stored, or transferred on an open, public, and/or decentralized network, or similar system is highly likely to be inconsistent with safe and sound banking practices.”

Although the OCC’s major interpretive actions involving crypto-asset activities that are discussed above have identified only a small number of specific crypto-asset activities as being permissible for national banks, certain OCC conditional approvals for national banks or federal branches in formation suggest that traditional bank financial intermediation functions such as acting as broker or agent for customers in connection with trading in financial instruments may also be permissible for national banks in connection with crypto-assets. Trading activities conducted by a bank as broker or agent for a customer would not expose the bank to principal risk or various of the other types of risks that would arise if a bank were to trade in or hold crypto-assets as principal or engage in financial intermediation activities in a principal capacity, such as acting as a dealer or a market maker, rather than in a brokerage or agency capacity. At a minimum, however, a national bank would presumably need to demonstrate to the satisfaction of the OCC that the bank has controls in place to conduct the crypto-asset brokerage or agency trading activities in a safe and sound manner, consistent with OCC Interpretive Letter 1179. As noted in the OCC’s conditional approval for a federal branch of foreign bank Adyen N.V., which provides that “[t]he [b]ranch shall not engage in any crypto-asset related activities (including but not limited to holding crypto assets on balance sheets or in a custodial or fiduciary capacity, accepting crypto assets as collateral, making markets or other financial intermediation in crypto assets, or trading crypto assets, including acting as agent) unless specifically authorized to do so by the OCC.” A state member bank would similarly be required under the Policy Statement to demonstrate an effective internal control framework for any such brokerage or agency trading activities for crypto-assets, as well as to comply with any terms, conditions or limitations imposed on such activities by the OCC in the case of national banks.