Financial Services Management

National-Bank Digital-Currency Powers

Cite

OCC Interpretive Letter 1174: Federal-Charter Stablecoin Power:
OCC Chief Counsel's Interpretation on National Bank and Federal Savings Association Authority to Use Independent Node Verification Networks and Stablecoins for Payment Activities

Recommended Distribution

Recommended distribution: Fintech, Payment Services, Corporate Planning, Corporate Development, Risk Management, Legal, Government Relations

Website

https://www.occ.gov/news-issuances/news-releases/2021/nr-occ-2021-2a.pdf

Impact Assessment

- If sustained, the new OCC interpretation allows a wide range of national-bank digital payment services that may speed innovation, develop alternative payment channels, and increase stablecoin use.
- However, numerous risks highlighted by the PWG and FSB are not addressed.
- Most immediately, this action may thus support internal, permission-based stablecoin payment networks, not open-access operations.

Overview

This interpretive letter (IL) follows an OCC advance notice of proposed rulemaking that suggested a notice-and-comment process before the agency made substantive changes to the digital-currency powers of federally-chartered banks.[1] Nonetheless, the OCC has now authorized broad payment activities in stablecoins, doing so based on an earlier action authorizing national banks to hold stablecoin reserves[2] without the restrictions recommended by global regulators[3] or the still more stringent ones demanded by the President's Working Group on Financial Markets (PWG)[4] addressing matters such as how 1:1 reserving can actually assure sufficient fiat currency is available on demand to back stablecoin.

[1] See **DIGITAL5**, *Financial Services Management*, June 9, 2020.

[2] See **CRYPTO15**, *Financial Services Management*, September 28, 2020.

[3] See **CRYPTO14**, *Financial Services Management*, April 23, 2020.

[4] See *Client Report* **CRYPTO16**, December 28, 2020.

Impact

This OCC interpretation details many possible uses for stablecoins (e.g., cross-border remittances), arguing that it is a natural continuation of national-bank powers for the OCC now to authorize stablecoin-related payment services. The OCC has indeed previously stated that any activity a national bank may offer in analog or physical form may be offered electronically.[5] Indeed, this IL is so emphatic about the appropriateness of bank stablecoin activities that it cites banking in Ancient Mesopotamia to emphasize the traditional value of bank payment services.

However, the OCC's rationale regarding longstanding bank payment powers appears more relevant to authorizing bank participation in independent Node Verification Networks (INVNs) than also to the associated stablecoin authorization also granted in this IL. While banks have long served as central portals for payment-system payors and payees, they have not created the coin on which transactions are consummated since the mid-19th century. If banks create stablecoins for external use, they would in fact be creating a new form of money much as Facebook has proposed to do with Libra, now called Diem. As emphasized most recently by the PWG's report and repeated late last year by global finance ministers and central bankers, any such non-fiat currency poses monetary policy, financial stability, and economic-equality issues along with the safety-and-soundness ones addressed to some degree in this IL.

Even so, it is possible that facilitating stablecoin activities by national banks and FSAs will indeed improve payment-system efficiency. Several GSIBs have developed stablecoin products through internal, permission-based digital-ledger technology (DLT) and other programs under the more diverse Independent Node Verification Systems (INVNs) covered by this letter are also in the works. An additional rationale for these stablecoin payment powers cited by the OCC is the need for faster payments. Acting Comptroller Brooks has strongly advocated private payment options, doing so in sharp contrast to the Federal Reserve's plans to dominate "instant" U.S. payments.[6]

Despite lengthy discussions about the advantages of stablecoins, the OCC is at pains to state that this IL does not mean that the agency endorses any specific products; indeed, it argues that banks must consider both INVNs and stablecoins to ensure their continuing payment-system relevance. However, the agency also describes an array of benefits it believes adhere only to INVNs such as being a decentralized network without a single point of failure. In contrast, the Financial Stability Board has raised many concerns about decentralized financial services.[7] The agency also asserts that INVN consensus requirements may also make them more trusted than the current system, with stablecoins adding fiat-currency stability to the overall process. However, such consensus mechanisms have not protected virtual currencies from numerous fraud, security, and other challenges; stablecoins thus would need to be very, very stable for trust to be consistently rewarded.

5 See **CHARTER27**, *Financial Services Management*, December 2, 2020.

6 See **PAYMENT16**, *Financial Services Management*, August 7, 2019.

7 See *Client Report*, **FINTECH24**, June 17, 2019.

What's Next

The OCC released this letter on January 4. It does not cross the many political boundaries over which Acting Comptroller Brooks has stepped in recent months.[8] However, the risks involved are such and the contradictions to PWG statements so pronounced that the Biden Administration's Comptroller may well reverse or modify it over time.

Analysis

The thrust of this IL concludes that a bank may validate, store, and record payments transactions by serving as a node on an INVN. In addition, a bank may use INVNs and related stablecoins to carry out other permissible payment activities, conducting these activities in a manner consistent with applicable law and safe and sound banking practices. The bank may issue the stablecoin or facilitate payments via an INVN for other stablecoin issuers.

Citing the PWG, the OCC specifies that a bank's compliance capabilities must include transaction-participant identification and verification, including with regard to unhosted wallets and systems to safeguard reserve assets, including a 1:1 ratio and loss-absorption capability. However, it is unclear how a bank acting only as the neutral provider of payment services described in the IL with regard to permissible INVN payment transactions for third parties could ensure adequate reserves unless the bank also acted as custodian (a power separately authorized for national banks by the OCC[9]).

Like the PWG, the OCC observes that some stablecoins may be securities under U.S. law. If they are, then a bank issuer is obligated to comply with applicable SEC requirements; it is unclear if the bank would need to ensure compliance if it acts only as a node on an INVN. To the extent the bank needs to buy and sell stablecoins to honor its INVN obligations, then bank could instead be considered the holder of the stablecoin and thus akin to an investor when stablecoins are purchased, but it conversely could be an issuer as it sells the stablecoin, raising securities-law concerns.

Banks engaging in INVN or stablecoin activities must conduct a legal analysis and ensure not only that they meet the safety-and-soundness requirements noted above, but also have appropriate operational- and compliance-risk management capability. Banks are thus advised to consult with their OCC supervisor before embarking on these activities.

---

8 See for example: **ESG3**, *Financial Services Management*, December 1, 2020.

9 See **CRYPTO15**, *Financial Services Management*, September 28, 2020.

Federal Financial Analytics, Inc.
2101 L Street, N.W., Suite 300, Washington, D.C. 20037
Phone: (202) 589-0880
E-mail: info@fedfin.com Website: www.fedfin.com