**Tuesday, November 2, 2021**

# FedFin Assessment: The Near-Term Stablecoin Regulatory Agenda

**Client Report: CRYPTO21**

## Executive Summary

As noted yesterday, the President's Working Group on Financial Markets (PWG) was joined by the OCC and FDIC yesterday issuing a report calling for prompt Congressional action to regulate stablecoins and, even in its absence, also for fast action by federal regulators and the FSOC. In part because it poses the largest regulatory void, the most worrisome of the risks the report details arises from the role stablecoins may play in the payment system and resulting threats to systemic stability and competition. Issues germane to digital-asset trading (defined to include lending and related activities) are described but largely left to regulators; SEC Chairman Gensler has made it clear (see *Client Report* **INVESTOR19**) that he intends to act and the CFTC-chair nominee has done the same. The report also notes that, while limited to stablecoins, the Administration and agencies are working on many other initiatives on cryptography and digital-ledger technology. As might be expected, no reference is made to a rumored executive order from President Biden laying out a tough whole-of-government stand in these arenas. This report forecasts near-term regulatory action by relevant federal agencies.

## Analysis

This report does not summarize the factual description of stablecoin nor the detailed explanation of various risks; we note that this should be referenced by clients looking for insight into the PWG's views on DLT and related DeFi considerations not specific to stablecoin. Based on the analyses in the report and its discussion of existing regulatory authority, we forecast the following near-term actions:

- clarification in the inter-agency final rule on third-party vendors (see FSM Report **VENDOR9**) that bank interfaces with stablecoin issuers, wallets, or related entities are within the full scope of this rule's consumer-protection and prudential requirements;

- an express third-party relationship approach for custodial digital wallets to govern consumer protection, safety and soundness, privacy, and – to the extent possible under current law – commercial affiliations;

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- no action by the FDIC to authorize ILC charters for stablecoin related ventures outside a bank holding company;

- no further action by the OCC to authorize special-purpose crypto charters, with the agency likely to go beyond the letter of the stablecoin report also to stand firm against any crypto charter outside a national bank or FSB in a Fed-regulated holding company;

- extensive new standards from the CFPB per Director Chopra's statement when the report was issued;

- continuing SEC enforcement actions applying the scope of securities law to stablecoins;

- a similar approach once the CFTC has a confirmed chairman;

- FinCEN rules expressly governing stablecoins and custodial wallets to the extent current or pending standards for convertible digital currencies do not suffice;

- additional OFAC attention to and possible enforcement actions to ensure sanctions compliance; and

- systemic designation for large-scale stablecoin entities (see below).

The report also calls for Congressional action on matters such as a consolidated prudential framework governed by the Fed for payment-stablecoin entities, a federal backstop, express reserve-asset requirements, a special resolution framework, and additional rules for custodial wallets. We think the odds of enactment in this Congress are low absent a scandal, crisis, or major new offering from a tech-platform company. The report is unclear as to whether the FSOC should await Congressional action or proceed more quickly to designate stablecoin activities as systemic financial-market utilities for purposes of top-down Fed, SEC, or CFTC regulation. It seems likely that FSOC will wait a while to give Congress some time and allow functional regulators to act as promised. However, we expect the systemic-designation process to begin in mid-2022, if not before.

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