Statement for the Record

On Behalf of the

American Bankers Association

Before the

Committee on Banking, Housing, and Urban Affairs

U.S. Senate

December 14, 2021

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Chairman Brown, Ranking Member Toomey, and distinguished Members of the Committee, the American Bankers Association (**ABA**)[1] appreciates the opportunity to submit a statement for the record for the hearing titled "Stablecoins: How Do They Work, How Are They Used, and What Are Their Risks?" The topic of today's hearing is an important one.

The origins of cryptocurrency were driven by the desire to build a "trustless" financial system, where parties can transact directly with each other without the need for a trusted third party. It is ironic, therefore, that as interest in cryptocurrencies and other digital assets such as stablecoins continues to grow, consumers engaging with digital assets most often seek out trusted financial institutions to act as financial intermediaries.[2] ***ABA believes that customers who choose to access digital asset markets, including stablecoins, will be best served when they can do so through fully regulated banks where they are afforded robust consumer protection.*** To accommodate this customer demand, banks are actively evaluating ways to safely and responsibly allow their customers to buy, hold, and sell digital assets through their existing banking relationships, as well as become involved in stablecoin arrangements. We have encouraged regulators to clarify that such digital asset activities are generally permissible for banks when conducted in a safe and sound manner, notwithstanding the novel technology involved.[3]

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[1] *The ABA is the voice of the nation's $23.3 trillion banking industry, which is composed of small, regional and large banks that together employ more than 2 million people, safeguard $19.2 trillion in deposits and extend $11 trillion in loans.*

[2] *See, e.g.*, NYDIG, *Survey: Bitcoin + Banking* (Jan. 2021), https://assets-global.website-files.com/614e11536f66309636c98688/616db2743df0d03cf3824093_NYDIG-Survey-Bitcoin-Banking.pdf.

[3] *See* ABA Comment Letter on FDIC RFI on Digital Assets (July 15, 2021), https://www.aba.com/advocacy/policy-analysis/aba-comment-letter-on-fdic-rfi-on-digital-assets; *see also* OCC Interpretive Letter No. 1179, Chief Counsel's Interpretation Clarifying: (1) Authority of a Bank to Engage in Certain Cryptocurrency Activities; and (2) Authority of the OCC to Charter a National Trust Bank (Nov. 18, 2021), https://www.occ.gov/topics/charters-and-licensing/interpretations-and-actions/2021/int1179.pdfhttps://www.occ.gov/topics/charters-and-licensing/interpretations-and-actions/2020/int1172.pdf.

Recently, the President's Working Group on Financial Markets, together with the FDIC and OCC, released a report on stablecoins that are pegged or linked to the value of fiat currencies (**Report**).[4] Given the risks these products pose to consumers, the payments system, and the broader financial system, the Report recommends that Congress act promptly to enact legislation to ensure that stablecoin arrangements are subject to a consistent and comprehensive federal prudential regulatory framework. The Report also identifies certain interim measures detailing how financial and banking regulators can address stablecoin risks falling within their respective jurisdiction. In addition, in the absence of Congressional action, the Report recommends that the Financial Stability Oversite Council (**FSOC**) consider steps to address the risks outlined in the Report. ***ABA agrees that action is urgently needed to address the gaps in the federal regulation of the stablecoin market and supports many of the Report's recommendations.***

Stablecoins, unlike other financial instruments, are not subject to a consistent, comprehensive set of regulatory standards that mitigate the risks they pose to consumers and the financial system. The lack of regulation is particularly concerning as the rapidly evolving uses of stablecoins is fueling significant market growth. To date, stablecoins have primarily been used to facilitate digital asset trading and lending activities, but increasingly they are being used as a means of payment for real-world goods and services (*e.g.*, Facebook/Meta's new digital wallet using stablecoins, called "Novi Wallet").

While enthusiasts claim that stablecoins have the potential to support faster and more efficient payments options, real-time payments facilitated through the regulated banking system are fast becoming a reality. Stablecoins, which are designed to circumvent this established regulatory architecture, pose a number of unmitigated risks including harm to consumers, the potential for stablecoin runs, and payment system risks, the latter of which could spill over into the broader financial system. The possibility that some stablecoins may rapidly scale, particularly as affiliates of commercial entities, also raises additional issues related to the concentration of economic power.

Existing regulation of stablecoin arrangements is neither comprehensive nor sufficient. The Securities and Exchange Commission (**SEC**) and the Commodity Futures Trading Commission (**CFTC**) exercise jurisdiction over certain aspects of stablecoin activity, but not all, particularly if the stablecoins are not securities. Some states subject virtual currencies, including stablecoins, to money transmission laws, but other states are undecided in their approaches. While these state laws are often aimed at a range of policy goals, including consumer protection and prevention of payment instrument default, they are not consistently applied and lack rigorous supervision and enforcement. This has resulted in a patchwork of guidance at a state and federal level

[4] President's Working Group on Financial Markets, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency, *Report on Stablecoins* (Nov. 2021), https://home.treasury.gov/system/files/136/StableCoinReport_Nov1_508.pdf.

that fails to ensure that all stablecoin arrangements are subject to appropriate prudential oversight on a consistent and comprehensive basis and that consumer financial protection laws are rigorously enforced.[5] This is particularly troubling in the case of stablecoins that may pose systemic significance.

Accordingly, ABA supports appropriate regulatory and legislative actions to provide a comprehensive federal regulatory framework for stablecoins. While Congressional action is pending, we encourage regulatory agencies to use their existing authorities to identify and address the risks of stablecoin arrangements, as well as FSOC to engage in a determination of whether certain activities conducted within a stablecoin arrangement are, or are likely to become, systemically important payment, clearing, and/or settlement activities.

In connection with this, ABA wishes to emphasize that any regulatory or Congressional action should:

- Provide a clear and comprehensive definition of "stablecoin" that avoids creating loopholes or permitting regulatory arbitrage and that clearly differentiates stablecoins from other types of digital assets. This would also ensure the regulatory treatment of stablecoins is appropriately calibrated to their risks;
- Recognize that stablecoin arrangements pose *both* systemic risks *and* consumer and investor protection concerns, making it critical to regulate not just the issuers of stablecoins, but also other participants in the stablecoin ecosystem, including custodial wallet providers and parties engaged in the business of stablecoin trading and/or brokerage;
- Encourage banking and financial regulators to collaborate on and coordinate a comprehensive approach to prevent the rise of unregulated (or under-regulated) stablecoin issuers and platforms that could pose risks to consumers, investors, the financial system, and the general economy; and
- Provide consistent treatment of banks and non-banks that engage in similar stablecoin activity to prevent regulatory arbitrage and ensure all customers are protected equally.

* * *

[5] Accepting and transmitting activity denominated in stablecoins does make a person a money transmitter under the Bank Secrecy Act (**BSA**). As a result, administrators of stablecoins, and potentially other participants in stablecoin arrangements, are required to register as money transmitter businesses (**MSBs**) with the Financial Crimes Enforcement Network (**FinCEN**) and become subject to AML and sanctions requirements. However, FinCEN has delegated its supervisory authority to a variety of different entities.

<table>
<tr><th colspan="2">ABA Assessment of Legislative Recommendations in the PWG Report</th></tr>
<tr><th>Legislative Recommendations</th><th>ABA Assessment</th></tr>
<tr><td>Stablecoin Runs: Require stablecoin issuers to be insured depository institutions, subject to appropriate supervision and regulation at the depository institution and the holding company level, and require them to be subject to standards and regulations aimed at managing liquidity risk.</td><td>ABA supports this recommendation.

A key risk related to the use of stablecoins is the possibility for loss of value. Stablecoins’ design sets them up as a store of value that can be used as an alternative to bank deposits. In order to protect stablecoin users and prevent stablecoin runs it is critical to maintain trust in the value of a stablecoin. The PWG report identifies the following factors that could undermine this confidence:

(1) use of reserve assets that could fall in price or become illiquid;
(2) a failure to appropriately safeguard reserve assets;
(3) a lack of clarity regarding the redemption rights of stablecoin holders; and
(4) operational risks related to cybersecurity and the collecting, storing, and safeguarding of data.

Banking regulation is designed to address exactly these risks and requiring stablecoin issuers to be insured depository institutions is the most effective way to address risks to stablecoin users and guard against stablecoin runs. This would provide for supervision on a consolidated basis; prudential standards; and, potentially, access to appropriate components of the federal safety net.

Furthermore, insured depository institutions, which include both state and federally chartered banks and savings associations, have deposits that are covered, subject to legal limits, by deposit insurance, and have access to emergency liquidity and Federal Reserve services, unlike stablecoin issuers that are not insured depository institutions.</td></tr>
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Payment System Risk: Require custodial wallet providers to be subject to appropriate federal oversight. Provide the federal supervisor of a stablecoin issuer with the authority to require any entity that performs activities that are critical to the functioning of the stablecoin arrangement to meet appropriate risk-management standards.	ABA supports these recommendations. Custodial wallet providers play a key role in the stablecoin ecosystem and should be subject to appropriate federal oversight to address payment system risk. This should include, among other things, requirements for clear and complete disclosures and protections against fraud, manipulation, and related risks, as well as appropriate risk management standards. Oversight at the federal level is critical because there is a patchwork of guidance at the state and federal level that fails to ensure that all stablecoin arrangements are subject to appropriate prudential oversight on a consistent and comprehensive basis and that consumer financial protection laws are rigorously enforced, and that the entities issuing stablecoins are subject to rigorous supervision and enforcement.
Systemic Risk and Concentration: Require stablecoin issuers to comply with activities restrictions that limit affiliation with commercial entities. Supervisors should have authority to implement standards to promote interoperability among stablecoins. In addition, Congress may wish to consider other standards for custodial wallet providers, such as limits on affiliation with commercial entities or on use of users' transaction data.	ABA supports imposing activities restrictions that limit the affiliation of stablecoin issuers with commercial entities to prevent the concentration of economic power and address additional concerns about systemic risk. Interoperability among stablecoins and between stablecoins and other payment instruments is critical in order not to disrupt existing payments systems. Appropriate restrictions that limit affiliation of custodial wallet providers with commercial entities and the use of users' transaction data will help to prevent concentration of economic power.