ICBA
Independent Community
Bankers of America®

Via Electronic Submission

June 29, 2022

Vincent Tran
International Trade Specialist
International Trade Administration, Department of Commerce
1401 Constitution Avenue, N.W.
Washington, D.C. 20230

RE: Notice and Request for Comment - Docket ITA - 2022-0003 - "Developing a Framework on Competitiveness of Digital Asset Technologies"

Dear Mr. Tran:

The Independent Community Bankers of America® ("ICBA")[1] welcomes the opportunity to provide feedback on the Department of Commerce's ("Commerce") Notice and Request for Comment on Developing a Framework on Competitiveness of Digital Asset Technologies.[2]

ICBA and its members appreciate this as an initial step in continued engagement with the Department of Commerce and other federal agencies and departments tasked with fulfilling President Biden's Executive Order on Ensuring Responsible Development of Digital Assets. Ongoing collaboration and dialogue between community banks and policymakers help

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[1] *The Independent Community Bankers of America® is the nation's voice for community banks with its mission to create and promote an environment where community banks flourish. We are dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best-in-class education, and innovative products and services. With nearly 50,000 locations nationwide, community banks constitute roughly 99 percent of all banks, employ nearly 700,000 Americans and are the only physical banking presence in one in three U.S. counties. Holding nearly $5.9 trillion in assets, over $4.9 trillion in deposits, and more than $3.5 trillion in loans to consumers, small businesses and the agricultural community, community banks channel local deposits into the Main Streets and neighborhoods they serve, spurring job creation, fostering innovation and fueling their customers' dreams in communities throughout America. For more information, visit ICBA's website at www.icba.org.*

[2] International Trade Administration, Department of Commerce, "Developing a Framework on Competitiveness of Digital Assets," Notice posted to the Federal Register on May 19, 2022, https://www.federalregister.gov/documents/2022/05/19/2022-10731/developing-a-framework-on-competitiveness-of-digital-asset-technologies.

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community banks continue to play a leading role in developing the products and services that enable their customers and communities to benefit from advances in financial technology.

Community banks are at the forefront of responsible innovation in financial services as they seek new ways to serve their customers and provide technologies and experiences that support the 21st century economy. Advocates for digital assets, ranging from cryptocurrencies like bitcoin to various tokenized assets, say they can provide new ways to increase speed, efficiency, and transparency in financial services for consumers and businesses. However, ICBA and its members have serious concerns about the potential for disintermediation of traditional financial services by stablecoins and decentralized finance ("DeFi"). Bankers have also expressed alarm at the growing use of cryptocurrencies to facilitate ransomware, money laundering, sanctions evasion, and other criminal activity.

Background

Since the birth of bitcoin, the original cryptocurrency, in 2008, the global market has expanded with the development of thousands of other cryptocurrencies and related products, such as non-fungible tokens ("NFTs"). However, the development of cryptocurrencies and other digital assets has been tempered by frequent and extreme volatility. In November 2021, the cryptocurrency market reached an all-time high of $3 trillion.[3] In the months since, the market has suffered from several high-profile exploits and failures that have contributed to a severe sell-off. As of June 22, the cryptocurrency market is valued at less than $1 trillion, down nearly 67 percent from its peak last year.[4]

A few early adopter banks have started to offer crypto-related products and services, such as custodial services or holding stablecoin issuers' reserve accounts, to meet customer demand. Most community banks, however, are still in the early stages of learning about the underlying technologies, potential use cases and assessing the associated risks. The path forward remains uncertain as policymakers continue to consider potential legislative actions that could impact banks and other digital asset service providers. Bank regulators have also not developed a harmonized regulatory framework that ensures a level playing field.

ICBA Comments

ICBA frequently engages its members to evaluate how community banks are exploring digital assets to address customer needs and learn more about how they think digital assets may impact the future of financial services. The following comments reflect their concerns about the risks of digital assets, their potential benefits, and questions about the lack of regulatory clarity. Bankers encourage the Commerce Department and the Administration to consider the following:

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[3] Macauley Peterson, Blockworks, "Ether All-time High as Total Market Cap Nears $3 Trillion," November 8, 2021, https://blockworks.co/ether-all-time-high-as-total-market-cap-nears-3-trillion/.

[4] See CoinMarketCap.com for overall cryptocurrency market value.

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1. Digital assets present numerous significant threats, including financial crimes and risks for financial stability.
2. Stablecoins currently exist in an unregulated space with several non-bank entities performing critical intermediary functions. Community bankers believe it is essential to bring stablecoins within the federal banking regulatory perimeter to address these risks and explore the potential use of stablecoins for responsible innovation within the payments sector.
3. Federal banking and markets regulators should collaborate on a comprehensive regulatory framework for digital assets. Responsible innovation requires policymakers to establish clear regulatory guidelines.
4. Community banks play a vital role in providing access to financial services and payments innovation. Community banks support the development of FedNow^{SM}, a new instant payment system, as well as efforts to bring unbanked citizens within the banking system.
5. Community bankers are opposed to the United States issuing a digital dollar, or Central Bank Digital Currency (CBDC). The risks far outweigh the uncertain and unproven benefits cited by CBDC advocates. A CBDC threatens to disintermediate community banks, thus raising the risk of serious economic consequences.

Risks of Digital Assets

ICBA and its members have serious concerns about the risks posed by cryptocurrency to privacy, consumer protections, and financial stability. The recent market volatility has heightened these concerns and highlighted the need for policymakers to work together to ensure that turmoil in the cryptocurrency markets does not spread into the wider financial system.

Cryptocurrencies are frequently used by bad actors to facilitate money laundering, terrorist financing, and other financial crimes. Although some proponents point to studies that seem to indicate relatively low amounts of illicit cryptocurrency activity, the Financial Action Task Force ("FATF") has repeatedly raised concerns about the methodologies employed by blockchain analytics companies and cautioned that their research has significant gaps.[5] A FATF report released last July noted that blockchain analyses are limited to "identified illicit transactions which the companies are able to identify" and "does not generally include [Money Laundering]/[Terrorist Financing] activity where virtual assets are being used to launder proceeds of crime that originate in fiat currency."[6] Therefore, these information gaps indicate that criminal activity associated with cryptoassets likely remains underreported. Policymakers should be mindful of these deficiencies as they work towards building a regulatory and legal framework that recognizes and addresses the myriad risks presented by bad actors in this space.

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[5] Chainalysis' *Crypto Crime Trends for 2022* claims illicit activity only accounts for 0.15% of total cryptocurrency transaction volume.
[6] FATF (2021), Second 12-month Review Virtual Assets and VASPs, FATF, Paris, France, www.fatf-gafi.org/publications/fatfrecommendations/documents/second-12-month-review-virtual-assetsvasps.html.

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ICBA has grave concerns about the potential for unregulated cryptocurrency entities to disintermediate community banks and undermine their ability to provide funding to support local economic activity, growth, and development. Bankers have expressed alarm about the growing number of deposits flowing out of the banking system into unregulated cryptocurrency platforms. This burgeoning world of shadow banking presents serious risks to financial stability if crypto market turmoil spills over onto Main Street. The risk for contagion is real, and ICBA urges policymakers to act now to prevent crises in the crypto markets from harming the wider financial system.

Another serious risk is the growing fragmentation of the digital asset ecosystem. There are now almost twenty thousand cryptocurrencies in circulation, with several major stablecoins issued across multiple blockchains. In a recent speech, Acting Comptroller of the Currency Michael Hsu identified the lack of interoperability within and across major blockchains as one of the largest hurdles to wider adoption.[7] Currently, one of the primary ways to address such deficiencies involves the use of so-called "cross-chain bridges" that allow users to exchange digital assets across blockchains. Unfortunately, these systems are often targeted by bad actors, as evidenced by the Axie Infinity hack earlier this year that resulted in over $600 million in stolen assets.[8]

The Bank for International Settlements has also raised concerns about the fragmented state of cryptocurrency. In a new report, BIS researchers said "…fragmentation of the crypto universe raises serious questions as to the suitability of crypto as money." The fundamental flaw, the BIS contends, is that "the more users flock to one blockchain system, the worse is the congestion and the higher are the transaction fees, opening the door to the entry of newer rivals who may cut corners on security in favour of higher capacity."[9]

Stablecoins

Bankers have expressed uncertainty about the possible roles for new payment mechanisms, including stablecoins. Bankers are concerned that the current state of stablecoin development creates more risks as unregulated non-bank crypto entities develop stablecoin products and services, thus contributing to the growth of a shadow banking world. ICBA is concerned that nonbank stablecoin issuers may disintermediate community banks, reducing deposits in the banking system and restricting access to credit in local communities. Regulators around the world have also voiced concerns about the growing risks associated with unregulated stablecoins. As noted in a new report by the Bank for International Settlements, stablecoins are flawed because they "must import their credibility from sovereign fiat currencies, but they

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[7] Office of the Comptroller of the Currency, Acting Comptroller of the Currency Michael J. Hsu, Remarks Before the Institute of International Economic Law at Georgetown University Law Center, "Thoughts on Stablecoin Architecture," April 8, 2022, https://www.occ.treas.gov/news-issuances/speeches/2022/pub-speech-2022-37.pdf

[8] Prashant Jha, Cointelegraph, "The Aftermath of the Axie Infinity's $650M Ronin Bridge Hack," April 12, 2022, https://cointelegraph.com/news/the-aftermath-of-axie-infinity-s-650m-ronin-bridge-hack.

[9] Bank for International Settlements, BIS Annual Economic Report, "III. The Future Monetary System," June 21, 2022, https://www.bis.org/publ/arpdf/ar2022e3.htm.

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benefit neither from the regulatory requirements and protections of bank deposits and e-money, nor from the central bank as a lender of last resort."[10]

If stablecoins can introduce efficiencies or support new payment products, then the best way to realize that potential for responsible innovation of stablecoins is within the regulated banking system. This view is supported by Acting Comptroller of the Currency Michael Hsu who recently said a "banking approach would be more effective," especially one with a "tailored set of bank regulatory and supervisory requirements [that] could balance stability with efficiency."[11] To that end, ICBA supports the President's Working Group's determination that stablecoin issuance should be limited to insured depository institutions to address serious risks to financial stability, consumer protection, and national security. Additionally, ICBA urges policymakers to prevent unregulated entities from issuing stablecoins and maintain the separation of banking and commerce to prevent Big Tech firms from quickly scaling and monopolizing the stablecoin marketplace.

Regulatory Harmonization and Clarity

ICBA and its members support cross-agency collaboration to establish a clear regulatory framework for digital assets. Currently, community banks have a limited ability to offer digital asset products and services. Recent guidance from the Office of the Comptroller of the Currency (OCC) and the Federal Deposit Insurance Corporation (FDIC) requires banks to seek approval from their regulator prior to engaging in any crypto-related activities.[12] The interagency effort between the Federal Reserve, OCC, and FDIC has not yet resulted in any joint effort to produce additional guidance on specific activities, such as cryptoasset custody or stablecoin issuance.[13]

Regulators should apply a consistent approach to all entities engaged in similar digital asset products and services to support a level field for competition and ensure appropriate robust protections for consumers. A more comprehensive and coordinated approach from all prudential regulators can help to dispel confusion in the marketplace and may prompt more community banks to explore digital asset products and services to address customer needs.

The lack of a clear and comprehensive regulatory framework can have a chilling effect on innovation, leading to inaction or speculation among banks about prudent courses of action. Responsible innovation in financial services requires clear guardrails so that banks know which activities are permissible, how products and systems should operate while mitigating risks. Without such information, many banks may choose not to engage in cryptocurrency or other digital asset activities.

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[10] Ibid.
[11] Acting Comptroller Michael Hsu, "Thoughts on Stablecoin Architecture".
[12] See OCC Interpretive Letter 1179 and FDIC Notification of Engaging in Crypto-Related Activities.
[13] The three agencies announced in November 2022 that they intended to work together on guidance related to several specific crypto-related activities.

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Enabling Access to Bank Accounts

ICBA and its members appreciate the Commerce Department's acknowledgment of the recent FDIC survey that shows nearly 95 percent of all American families have access to a bank account.[14] ICBA and its members firmly believe that access to a bank account is key to financial success, and we support ongoing efforts to reach un/underbanked populations through programs such as the FDIC's #GetBanked initiative.

A bank account provides much more to consumers than the convenience of electronic payments—it also offers a safe and trusted place to deposit money. The recent troubles of crypto lending platforms and the resulting loss of users' assets highlights the safety and value provided by the regulated banking system. Unregulated crypto lenders and decentralized finance protocols cannot offer consumers the same level of protection and trust. The lack of regulation, combined with extreme market volatility, smart contract flaws and criminal activity, present consumers with heightened and unacceptable risks.

Community Banks and Payments Innovation

Community banks are subject to a robust regulatory framework and prudential oversight that balances responsible innovation with safety and soundness protections for consumers and businesses. Community banks recognize the important role of faster payments in payments modernization and support key initiatives to deliver safe and fast payment experiences.

Community banks are vital participants in the ACH Network, which launched Same Day ACH in 2016. Same Day ACH enables community banks to provide consumers and businesses with a faster and cost-effective payment option. Last year, usage of Same Day ACH increased 74 percent to reach a new high of 603.8 million transactions valued at $943.7 billion.[15] Same Day ACH is poised to continue its rapid growth as more businesses and community banks bring more efficiency and speed to use cases such as bill pay, payment for gig economy workers, and faster payroll payments.

ICBA believes that real-time "instant" payments will help businesses and consumers access payments products and services that meet the needs of the 21st century economy. The implementation and ubiquitous adoption of instant payment systems will strengthen the U.S. economy by providing a platform for continued innovation and economic growth, and will facilitate America's global competitiveness. Community banks are actively supporting the development of a new instant payment system called FedNow, expected to launch next year. FedNow will enable payments to clear and settle in mere seconds. ICBA applauds the

[14] FDIC, "FDIC Survey Shows 95 Percent of U.S. Households Were Banked in 2019," October 19, 2020, https://www.fdic.gov/news/press-releases/2020/pr20113.html.
[15] Nacha, "ACH Network Sees 29.1 Billion Payments in 2021, Led By Major Gains in B2B and Same Day ACH," February 3, 2022, https://www.nacha.org/news/ach-network-sees-291-billion-payments-2021-led-major-gains-b2b-and-same-day-ach#:~:text=The%20modern%20ACH%20Network%20experienced,new%20figures%20from%20Nacha%20show.

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development of FedNow as a crucial milestone for payments transformation, by providing the nation with a modern, safe, and effective financial system. By bringing FedNow to market, the Federal Reserve: 1) provides financial institutions an infrastructure option for clearing and settling faster payments; 2) ensures access and choice for all financial institutions; 3) serves as a backbone to ensure settlement continuity in the event of disruption in the private sector; and 4) encourages competition and innovation. ICBA encourages its members to develop strategies to adopt FedNow to bring the benefits of this new technology to consumers and businesses.

<u>ICBA Opposes Creation of a U.S. Central Bank Digital Currency</u>

In January 2022, the Federal Reserve Board issued a consultation paper, "Money and Payments: The U.S. Dollar in the Age of Digital Transformation," to initiate public dialog on the benefits and risks of creating a U.S. CBDC. Based on thorough analysis of the proposal and feedback from a broad cross section of ICBA members, we conclude a CBDC would not yield benefits more effectively than alternative methods in the market today. While we support efforts to ensure the U.S. payments and monetary system remains modern and competitive, creating a CBDC would introduce risks without providing benefits to households, businesses, and the overall economy that exceed the costs and risks.

ICBA opposes the creation of a CBDC because it will introduce significant privacy and cybersecurity risks into the nation's monetary system and disrupt the stability of America's banking system. A CBDC could threaten the health of the U.S. financial system by destabilizing existing banking and payments systems that are the backbone of our economy and markets. As a digital liability of the Federal Reserve, a CBDC will cannibalize bank deposits, reduce credit availability, and raise costs for households and businesses. According to the Federal Reserve, "the substitution effect could reduce the aggregate amount of deposits in the banking system, which could in turn increase bank funding expenses, and reduce credit availability or raise credit costs for households and businesses."[16]

ICBA urges the Commerce Department to consider the spillover effect that a CBDC would have on community banks and the customers that rely on these institutions as a financial lifeline. As an example, ICBA points to the outsized role community banks played in implementing the Small Business Administration's Paycheck Protection Program where community banks generated over 60 percent of the loans to struggling small businesses due to the pandemic. Because of the critical role that community banks play in the banking system and as small business lenders, as well as their unique understanding of the needs of their communities, we urge Commerce to give appropriate weight to their staunch opposition to a CBDC.

During a time of financial crisis, the risk to bank deposits posed by a CBDC could be dramatic. Because a CBDC is a liability of the central bank and would not have credit or liquidity risk,

[16] Board of Governors of the Federal Reserve System, Research & Analysis, "Money and Payments: The U.S. Dollar in the Age of Digital Transformation" (January 2022), available at: https://www.federalreserve.gov/publications/files/money-and-payments-20220120.pdf.

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there is a risk that, during times of financial stress, depositors would "run on the bank" and transfer their balances to CBDC wallets. Like a traditional bank run, this may lead to forced liquidations, which could plunge financial markets and the economy into a collapse. It could also lead to losses for the FDIC if forced liquidations lead to bank failures.

It remains unclear that a government-sponsored cryptocurrency will ever be able to achieve the potential benefits of payments modernization or increased financial inclusion. Advocates of a CBDC say that it could promote financial inclusion by allowing low-income individuals to transfer money or receive payments digitally, without having to pay the fees associated with a traditional deposit account or for remittances. In our view, it seems incredibly unlikely that that a technologically complex, government-issued cryptocurrency, which will likely depend on fee-based private wallets, is the best way to reach the underbanked. In public comments, Nellie Liang, Undersecretary for Domestic Finance at the Treasury Department, discussed additional means of addressing unequal access to the financial system, including FedNow.[17]

Critically, a CBDC would also alter the roles and responsibilities of the private sector and the central bank in an unprecedented way. ICBA is adamantly opposed to a direct-to-consumer model. Even with an intermediated model as proposed in the consultation paper, community banks will be harmed by a CBDC. Banks would be saddled with all of the identity-verification, customer service, Know Your Customer (KYC), Anti-Money Laundering (AML), privacy protections, sanctions screening and other compliance burdens with no clearly identified revenue stream to compensate banks for these services. Because the Federal Reserve has proposed that banks would compete with regulated non-banks in an open market, community banks would be at risk of losing customers to wallets offered by less regulated companies.

<u>A CBDC Will Impede the Formation of Banking Relationships and Harm Small Businesses</u>

The core of the community bank business model is relationship banking. Community banks provide more than simply access to payments rails and credit. Community bankers work with their customers – both retail and small business – and help them manage their finances and make informed financial decisions. This guidance can range from teaching a retail customer how to balance their checkbook, to guiding a family through the process of applying for a first mortgage, to helping a small or midsized business apply for government guaranteed loans and other forms of more complicated financing that suit their individual business needs. In other words, relationship banking is more than simply taking deposits and extending credit, it is about creating mutually beneficial trust by acting as an educator and advisor to customers.

For most customers, the banking relationship begins with opening a deposit account. If the creation of a CBDC disintermediates this step, it could upend the ability of community banks to form this relationship with their customers. Community banks may not be able to offer CBDC

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[17] Nellie Liang, U.S. Department of the Treasury, "Remarks by Under Secretary for Domestic Finance Nellie Liang to the National Association for Business Economics" (March 22, 2022), available at: https://home.treasury.gov/news/press-releases/jy0673.

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wallets as cheaply or conveniently as larger-scale, less-regulated financial technology providers. Because CBDC wallet balances will not be able to be lent against, some community banks will likely choose not to offer CBDC wallets at all because the business case is not sustainable.

If a CBDC nips this relationship formation in the bud, it will have effects that harm the customer's financial health in the long term. For example, if a customer chooses to transact entirely through a CBDC wallet, that customer will not build a credit history. A community banker could advise them that, by using a bank-issued credit card and paying off the balances in a timely way, they will be able to improve their credit score in a way that will reduce the cost of borrowing for major purchases such as a home or business loan. If customers are forced to rely on large-scale, online providers of CBDC wallets that do not offer the same level of high-touch customer service as community banks, the end result could be a decline in financial literacy and an increase in customers making adverse financial decisions due to a lack of guidance.

The lack of relationship building may also lead to lower levels of small business formation. According to the FDIC, "Despite holding only 15 percent of total industry loans in 2019, community banks held 36 percent of the banking industry's small business loans. Community banks focus on building relationships with small business owners and tend to make loans that require more interaction with the borrower." According to the same study, in rural areas, "Community banks are an important source of financing for U.S. agriculture, funding roughly 31 percent of farm sector debt in 2019, with half of that total financed by community-bank agricultural specialists … Community-bank agricultural specialists have shown a strong commitment to lending to farmers through the peaks and valleys of cycles in the agricultural sector." If potential small business owners or farmers never walk through the door of a community bank to open a deposit account, they will lose a potential financial partner who could help them navigate the challenges of business formation or adverse economic cycles.

Congressional Authority Required for a U.S. CBDC

ICBA strongly urges policymakers not to proceed with creation of a CBDC without explicit statutory authorization and oversight from Congress. In testimony before the Senate Banking Committee, Chairman Jerome Powell said that before proceeding to develop a CBDC the Federal Reserve would "want very broad support in society and in Congress and ideally that would take the form of authorizing legislation as opposed to a very careful reading of ambiguous law."[18] While we appreciate the Chairman's commitment to a continued dialogue, we do not believe that the authority to issue a CBDC exists under current law.

[18] "The Semiannual Monetary Report to the Congress," United States Senate Committee on Banking, Housing, and Urban Affairs (July 15, 2021) (Testimony of the Hon. J. Powell).

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Conclusion

ICBA and its members appreciate the opportunity to comment on the Notice and Request for Comment on Developing a Framework on Competitiveness of Digital Asset Technologies and look forward to continued dialogue to ensure that all community banks continue to play a leading role in developing the products and services that enable their customers and communities to benefit from advances in financial technology. If you have questions or require additional information about ICBA's statements, please contact me at (202) 821-4427 or by email at Brian.Laverdure@icba.org.

Sincerely,

/s/

Brian Laverdure, AAP
Vice President, Payments and Technology Policy