One Mission. Community Banks.

January 29, 2024

Basel Committee on Banking Supervision
Bank of International Settlements
Centralbahnplatz 2
4051 Basel
Switzerland

Re: Consultative Document: Disclosure of Cryptoasset Exposures

Dear Sir or Madam:

The Independent Community Bankers of America ("ICBA")[1] appreciates the opportunity to comment on the consultative document titled "Disclosure of Cryptoasset Exposures". The Basel Committee is using this document to describe a standardized set of disclosures that can form a framework for the presentation of bank cryptoasset exposures. Through the publication of a standardized set of disclosures, the Basel Committee is hopeful that banks will present exposures consistently across the spectrum of reporting institutions. The documented framework includes qualitative disclosures on bank activities related to cryptoassets as well as quantitative disclosures on exposures by type, capital requirements, accounting classifications, and liquidity requirements.

ICBA supports the work of the Basel Committee to create a framework of cryptoasset disclosures that thoroughly covers the critical elements needed for full disclosure of the bank's exposure and explains how such exposure impacts the financial statements of the organization. Because cryptocurrency exposures have not yet found wide entry into the banking system in highly developed countries, ICBA expects that this framework will need to evolve as the creation of financial instruments with crypto-like attributes gains traction over time.

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[1] The Independent Community Bankers of America® creates and promotes an environment where community banks flourish. ICBA is dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best-in-class education, and high-quality 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.

The Document

This consultative document sets forth a standardized set of disclosure templates for bank crypto exposures in an effort to promote a consistent framework across institutions. The proposed disclosure framework centers around qualitative disclosures on a bank's cryptocurrency activities and three separate quantitative tabular disclosures detailing the exposures, associated capital requirements, liquidity requirements, and accounting classifications. In addition, banks will need to disclose the sources of information used in their assessments of cryptocurrency exposures in the populated data sets. Note that the document calls for semiannual disclosures for the tables, which would normally be presented on a quarterly basis for U.S. financial statement and bank reporting preparers.

Qualitative disclosures on a bank's cryptocurrency activities are proposed to be disclosed annually with a focus on the business activities related to the exposure including assets owned directly, trading in customer accounts, equity investments in related activities like exchanges and venture funds, and any cryptocurrency contracts issued by the bank. Banks will need to discuss their role in a cryptocurrency arrangement and state when they act as intermediary. If a bank has a commitment to redeem or otherwise purchase a cryptocurrency asset, that commitment should be described. Banks would describe the risk profile of their cryptocurrency exposures, including the potential impact of credit risk, market risk, and operational risk with their associated risk mitigation strategies and monitoring techniques. Banks would also explain their most significant current risk and most significant emerging risk with regard to their current cryptocurrency activities and how these risks are currently being mitigated.

Capital Disclosures. Banks would present cryptocurrency exposures in a tabular format with their associated capital requirements. Exposures would be grouped by the Basel classification type (Group 1a, 1b, and 2) and show total exposure, credit exposure, and risk weighting in the calculation of risk-weighted assets. Market risk exposure would be disclosed separately for long positions and short positions. Separate notation would be made for those cryptoassets held in custody for customers. Banks would also present a narrative discussion of significant changes over the reporting period and the cause of such changes. Significant policies used to manage operational risk would also be disclosed.

Accounting Disclosures. Banks would present cryptocurrency exposures in a tabular format based on accounting classification for assets and liabilities. Exposures would be listed by those measured at fair value with unrealized gains and losses flowing through the income statement, those measured at fair value with unrealized gains and losses flowing through other comprehensive income, and those measured at amortized cost. Banks would include a narrative with the table explaining significant changes over the reporting period and the source of the changes.

Liquidity Disclosures. Banks would present cryptocurrency exposures in a tabular format based on their liquidity risk. Exposures would be listed by Basel classification type with further delineation of those group 1a tokenized assets that meet the definition of a high-quality liquid asset (HQLA), tokenized claim on a bank, or other tokenized claim. Exposures would be separated by derivative assets and liabilities versus assets and liabilities that are not derivatives. For applicable banks, the liquidity impact of the crypto exposures on the liquidity capital ratio and net stable funding ratio would be disclosed with their associated haircuts and ratio impacts on available stable funding versus required stable funding.

In addition to the qualitative and tabular disclosure framework described above, the Basel Committee describes potential additional qualitative disclosures that could be added to provide detail on the four classification conditions needed for a cryptocurrency exposure to be included in Group 1, which includes tokenized traditional assets and certain stablecoins. Classification condition 1 disclosures would include a description of the stabilization mechanisms used. Classification condition 2 disclosures would include guarantee provisions, redemption rights, and availability of public information used to ensure accuracy. Classification condition 3 would include key network risks, risk governance and control policies surrounding the mechanical aspects of the crypto exposure, and the key provisions of the network like node management and network validation. Classification condition 4 would include discussion of regulator jurisdictions, supervisors, and any lack of regulation. The discussion would cover redemptions of assets and liabilities, transfers, storage, settlement, and the handling of reserve assets.

ICBA's Comments

ICBA appreciates the work of the Basel Committee to provide an initial regulatory framework on bank cryptocurrency exposures, and the publication of this consultative document as a furthering of that effort. The Committee has clearly designed both a qualitative and quantitative disclosure matrix that captures the key regulatory and accounting concerns of prudential supervisors as they prepare to examine institutions that add cryptocurrency exposures in permitted jurisdictions. ICBA believes that the work of the Basel Committee in the cryptocurrency sphere of influence is especially challenging since the asset class is rapidly changing as new entrants appear every day, introducing products and services that produce new risks for banks to consider as they navigate present and future customer demand for these financial instruments. Integration of crypto exposures into the audited financial statements of banking organizations and the regulatory capital ratios of their subsidiary banks presents a whole host of dynamic risk profiles that will need to be thoroughly vetted by standard setters and regulators to ensure that banks are properly capturing financial, operational, liquidity, and other risks. Through the publication of this document, the Basel Committee has successfully crafted a good starting point for the discussion.

One concern that community banks often identify is the potential for different regulated entities within a jurisdiction or on a cross-jurisdictional basis to reach different conclusions about cryptocurrency exposures that are popular in a specific region of the globe. Banks, bank customers, bank regulators, and sovereign governments might apply different haircuts to certain cryptocurrency exposures that originate from a specific country or tokenize a specific physical asset on an inconsistent basis either across regulators or regulated institutions. For example, in one country the tokenization of residential real estate mortgage loans for distribution on a blockchain ledger might be looked upon favorably as an innovative method to increase demand and liquidity for cryptoassets with yield potential. That country's prudential bank regulator may assign a favorable risk weight to such an exposure. The same exposure could be more harshly criticized in another country's prudential regulator either based on the credit, liquidity, or transactional risk associated with the cryptoasset or the blockchain where the crypto asset is transacted. Such a risk could quickly become unmanageable due to the ease with which a cryptocurrency project can be launched, gain traction, and achieve sufficient liquidity to be acquired by a bank. Smaller institutions like community banks lack the resources and expertise needed to thoroughly evaluate the contractual terms of the project, it's underlying cryptographic characteristics, scripted code, developers and investors, etc. when a new project is launched. ICBA suspects that the Basel Committee will need to work with prudential regulators to develop a mechanism for all market participants and their supervisors to quickly gain the needed parameters of the exposure's key risks.

ICBA notes that increasingly some cryptocurrency exposures are controlled by exchanges or other market makers that either specialize in providing liquidity for a cryptocurrency product or have a vested interest in the success of a cryptoasset. Amid the current regulatory uncertainty in the United States, the purchase, sale, transfer, and origination of cryptoassets has been placed in the hands of a few large organizations that control the ability for a project to achieve the needed liquidity for a U.S. bank to take a position. If uncertainty continues, banks will need to place a high degree of reliance on these third-party participants, many if not all being unregulated entities, to ensure operational and liquidity risk compliance. ICBA recommends that the Basel Committee study this phenomenon and its impact on banking organizations across the countries that are most likely to participate in cryptocurrency transactions. For example, the Basel Committee should consider whether concentration risk exists within a country's cryptocurrency liquidity providers and how an increase in price volatility could hypothetically limit the ability of a bank to transact at quoted market prices. The Basel Committee may conclude that the resulting price discovery exercise that a bank must undergo when price volatility reaches excessive levels warrants enhanced disclosures. Further, ICBA would like to see the Basel Committee assess the impact of banking organizations of different sizes to practically participate in cryptocurrency markets knowing that concentration risk among market makers could develop into a real concern.

ICBA appreciates the opportunity to provide comments on this consultative document and hopes that the Basel Committee will consider our observations. If you have any questions or would like additional information, please do not hesitate to contact me at james.kendrick@icba.org.

Sincerely,

/s/

James Kendrick
First Vice President, Accounting & Capital Policy