

Enhanced Regulation of Digital Assets Will Promote Responsible Innovation

The Independent Community Bankers of America, representing community banks across the nation with nearly 50,000 locations, appreciates the opportunity to provide this statement for the record for today's hearing titled: "Digital Assets and the Future of Finance: Understanding the Challenges and Benefits of Financial Innovation in the United States."

We appreciate the Committee's examination of fundamental issues related to the surge in digital assets and are pleased to share the community bank perspective. To ensure that innovation is undertaken safely, ICBA advocates for a comprehensive, coordinated regulatory approach for the reasons described below.

Community Banks and Cryptocurrency

Wider adoption of cryptocurrency is altering global digital commerce and the global financial system. Community banks keep pace with innovation to remain viable, relevant and continue to serve their communities. Numerous financial service providers and financial technology companies now offer consumers and businesses access to cryptocurrency-related activities, such as investments, lending, and custodial services. Although cryptocurrencies are still not widely used for payments, some community banks are beginning to explore offering cryptocurrency services to meet customer demand. They want to ensure they can do so safely. Several crypto companies are developing solutions to enable crypto payments for consumers and businesses.

ICBA is working with community bankers to educate their staffs on cryptocurrencies, follow market and regulatory developments, and evaluate their bank's exposure to cryptocurrency through customer activities. Community bank involvement, as regulated financial institutions, will help mitigate risks presented by cryptocurrencies, provided it can be done under a rigorous and thoughtful regulatory framework.

Community banks have a strong interest in ensuring that cryptocurrencies do not create systemic, investor, or consumer risk. As described below, ICBA is concerned with cryptocurrency's potential impact on privacy, money laundering, terrorist financing, fraud, consumer protection, and financial stability.

Risks Presented by Cryptocurrencies

Risks presented by cryptocurrencies include:

- Due to limited regulation and oversight, consumers and investors that use or hold cryptocurrency are exposed to significant risks, including highly volatile fluctuations in value.
 - Cryptocurrencies have a long history of being used for criminal and illicit activity, undermining law enforcement. Criminals frequently use cryptocurrencies to launder funds, hijack computer systems with malware to surreptitiously mine cryptocurrency, and use cryptocurrencies to facilitate payments for illegal goods and services. Anonymity-enhanced cryptocurrencies, or cryptocurrencies designed to evade scrutiny and cloak users in greater secrecy, are utilized by fraudsters around the world for a variety of criminal actions.
 - Private stablecoins, including those backed by fiat currencies, can pose other threats, including eroding monetary authority, threatening financial stability, and risking community bank disintermediation.

Policy Recommendations

ICBA encourages policymakers to harmonize regulations to ensure strong, clear, and consistent oversight of cryptocurrency service providers.

- Any regulatory regime applied to cryptocurrency should be comparable to the same regulations applicable to traditional, functionally similar payments products and services offered by the banking system.
- The scope of regulation should include capital adequacy and reserves; activity restrictions; due diligence; information security and privacy; business resiliency; ownership and control of data; anti-money laundering and anti-terrorist financing; reporting and maintenance of books and records; consumer protections; safeguarding customer information; vendor and third-party management; and ongoing examination.
- A more comprehensive, coordinated regulatory approach by banking and market regulators, including the Securities and Exchange Commission and the Commodity Futures Trading Commission, could help address risks, dispel confusion in the marketplace, and prompt more community banks to explore digital asset products and services to address customer needs. Cryptocurrency companies are not subject to comprehensive consolidated supervision, which allows for risks to multiply and creates an unequal playing field with banks.
- The harmonization of regulations will not only address risk—the additional clarity can level the playing field and create opportunities for more community banks to consider offering crypto products and services. Without such information, many banks may choose not to engage in cryptocurrency or other digital asset activities.
- Collaboration can also help to ensure that the development of digital assets will not harm the integrity of the U.S. financial system by disintermediating community banks. Without harmonization among all the banking regulators, community banks that are not regulated by the OCC may find they are at a competitive disadvantage relative to their OCC-regulated peers and non-bank cryptocurrency companies.

Special-Purpose Bank Charters

ICBA strongly opposes granting special-purpose bank charters to cryptocurrency companies that do not fully meet the requirements of federally insured chartered banks. These novel charters for non-banks firms raise a number of regulatory concerns—such as violation of the long-standing principle of the separation of banking and commerce, lack of application of traditional banking statutes and regulations governing safety and soundness and consumer protection, and the potential introduction of systemic risk into the payments system.

Stablecoins

Stablecoins are digital assets that are issued and transferred using distributed ledger technologies and are purported to maintain a stable value relative to a national currency or other reference asset or assets. Many of the concerns expressed above with regard to cryptocurrencies also apply to stablecoins, which could disintermediate national payment systems and even monetary policy.

The President’s Working Group on Financial Markets (PWG) report on digital assets rightly reflects ICBA concerns about the potentially harmful and rapidly accelerating risks to consumers, the financial system, and the economy of continued, rapid stablecoin growth. In addition, the November 2021 Financial Stability Report of the Board of Governors of the Federal Reserve, quoted below, identifies the following risks associated with stablecoins:

- “Certain stablecoins, including the largest ones, promise to be redeemable at any time at a stable value in U.S. dollars but are, in part, backed by assets that may lose value or become illiquid. **If the assets backing a stablecoin fall in value, the issuer may not be able to meet redemptions at the promised stable value.**
- “Accordingly, these stablecoins have structural vulnerabilities similar to (...) certain money market funds and are susceptible to runs.
- “These vulnerabilities may be exacerbated by a lack of transparency and governance standards regarding the assets backing stablecoins. **The potential use of stablecoins in payments and their capacity to grow can also pose risks to payment and financial systems.”**

Stablecoin Policy Recommendations

ICBA’s policy recommendations on stablecoins are broadly similar to our cryptocurrency policy recommendations.

Regulatory collaboration on a comprehensive approach would prevent the rise of a shadow banking system filled with unregulated platforms that pose risks to consumers, the financial system, and U.S. national security. Enhanced regulation of stablecoin arrangements is critical. Whether classified as securities, commodities, or demand deposits, stablecoins must be brought within the regulatory perimeter. Appropriate federal oversight is needed to close regulatory gaps regardless of how these digital assets are classified by policy makers. The regulatory framework should address risks posed by any entity within a stablecoin arrangement that participates in the creation, transfer, or storage of stablecoins. Unregulated entities should not be permitted to issue stablecoins.

A consistent federal regulatory framework for stablecoins should balance their benefits and risks and preserve the separation of banking and commerce.

Closing

ICBA and community bankers look forward to continuing to work with policymakers to balance the benefits of innovation in digital assets with their safety and soundness risks.

Thank you for your consideration of the community bank perspective.