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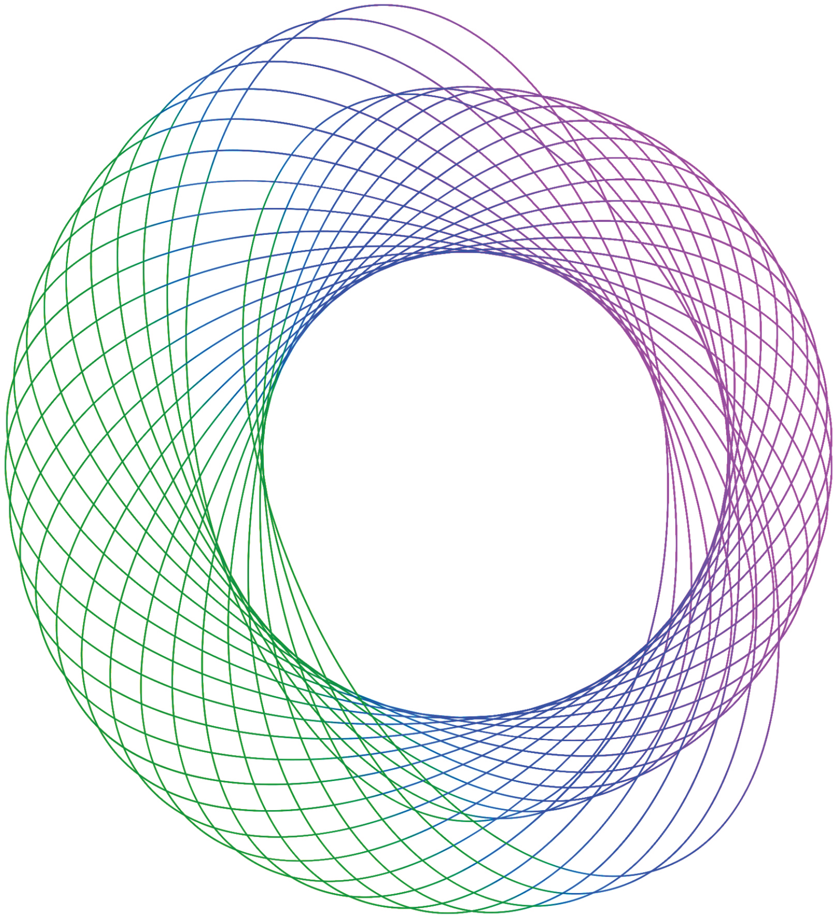


Cryptocurrency notification protocols and readiness

Banks engage in crypto-related activities leaving some regulators behind to pick up the digital pieces

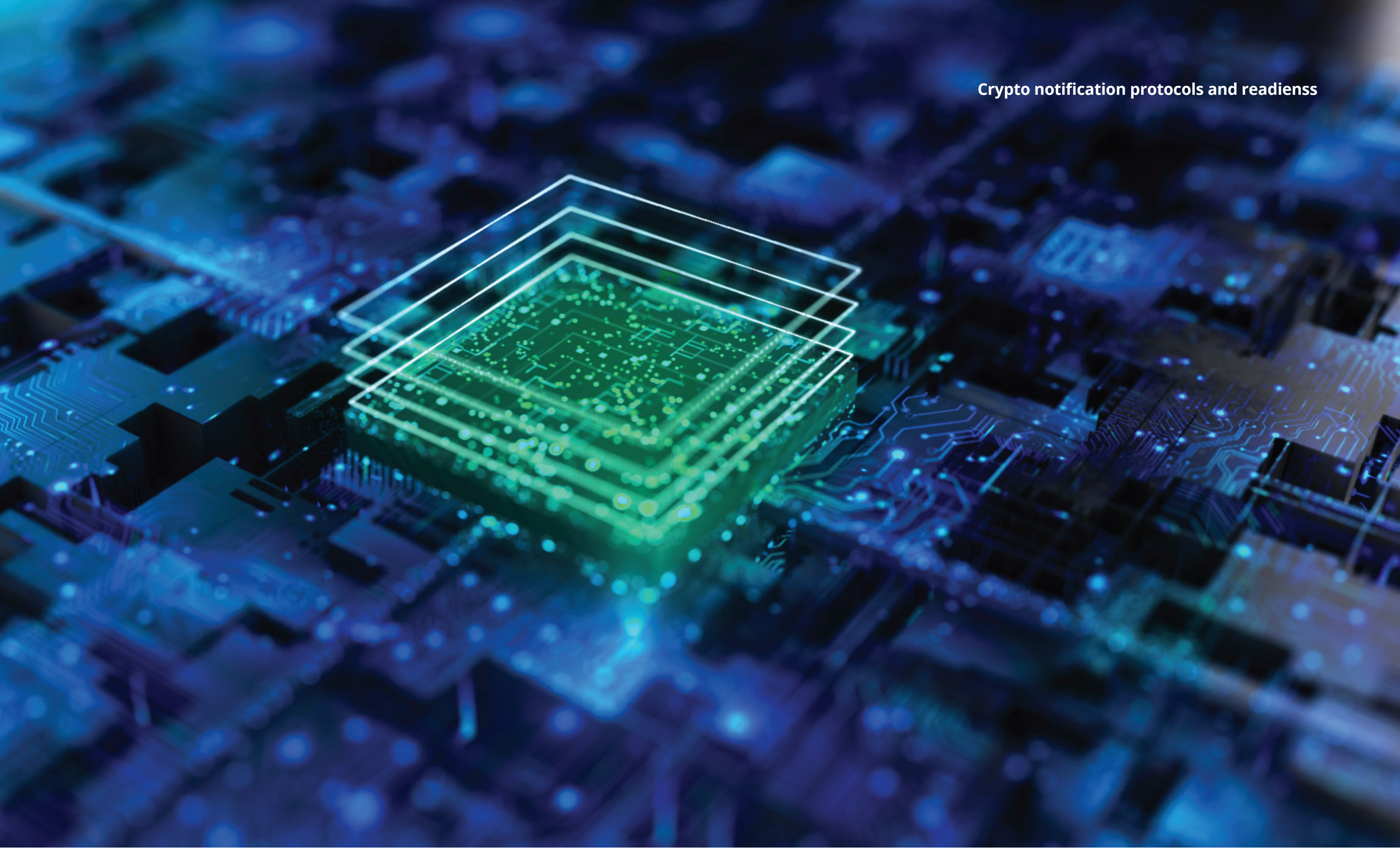
April 11, 2022

A comparison of Federal Deposit Insurance Corporation (FDIC) and Office of the Comptroller of the Currency (OCC) cryptocurrency notification protocols for supervised banks

In recent remarks, Secretary of the Treasury, Janet L. Yellen, mentioned federal financial regulators having existing authorities to regulate risks presented by technological innovation (including crypto and digital assets).[1] These remarks align with federal banking regulators' common goal of safety and sound operation of banks. In the interim, the federal financial regulators have supervisory and enforcement authority that can be used until comprehensive digital assets legislation is set forth by Congress and a formalized interagency supervisory framework is implemented.

As seen with the OCC's November 2021 Interpretive Letter, 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,[2] and the FDIC's recent Financial Institution Letter, Notification of Engaging in Crypto-Related Activities,[3] regulators are trying to wrap their arms around cryptocurrency activities that banks are conducting as well as those included in future plans. In establishing notification protocols, regulators are using their existing toolkits to better understand and supervise banks that assume risks associated with cryptocurrency activities.

	FEDERAL BANKING REGULATOR	
NOTIFICATION DESCRIPTION	**FDIC**	**OCC**
Publication date (Publication type)	• April 7, 2022 (Financial Institution Letter)	• November 18, 2021 (Interpretive Letter)
Notification timing	• Pre-notification *or* • Post-notification	• Pre-notification only
Notification recipient	• Regional director *and* • State banking regulator	• Supervisory office
Internal review areas	• Safety and soundness[4] • Financial stability • Consumer protection	• Risk management systems and controls • Risk measurement systems • Other supervisory considerations relevant to the proposal
Risk considerations	• Credit • Liquidity • Market • Pricing • Operational • Systemic • Consumer protection	• Operational • Liquidity • Strategic • Compliance
Requirements of review	• Demonstrate the ability to conduct activities in a safe and sound manner	• Demonstrate establishment of an appropriate risk management and measurement process for the proposed activities
Requests for additional information	• On a case-by-case basis	• Not specifically covered
Notification response	• Supervisory feedback	• Objection or non-objection



The FDIC's letter sends a clear sign that some FDIC-supervised banks have already started to conduct cryptocurrency activities without obtaining the agency's sign-off. Those banks would need to provide retroactive notice of their activities to the FDIC and follow the assessment protocol. The FDIC gives no indication that it is planning to "approve" cryptocurrency activities, rather it seems that it will likely respond with firm-specific supervisory expectations based on the nature of the activities.

In contrast, the OCC's process requires prior notification of a bank's intent to conduct cryptocurrency activities and for banks to refrain from conducting any such activities until receiving the OCC's non-objection. Once a bank receives notice of non-objection from the OCC, the subject activities are folded into the bank's normal supervisory process and the bank is expected to have adequate risk management policies, procedures, limits, and controls similar to what is in place for other banking products. OCC banks that have received non-objection for cryptocurrency activities should continue forward with prudent risk management processes and monitor for future agency notifications on this topic.

Both agencies highlight several risks that may be heightened in the presence of cryptocurrency activities at banks; however, the risk types themselves are not novel. The way that banks may need to identify, measure, monitor, and mitigate risks resulting from cryptocurrency activities will likely vary from established risk management tactics used for more traditional products. However, neither agency provides detail on potential risk management practices for banks or how they intend to consider these risks within the parameters of existing bank supervisory frameworks.

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Preparing for the way forward

FDIC- and OCC-supervised firms that are interested in conducting cryptocurrency activities should prepare in the following ways:

- Understand the activities of interest and how they may present specific (e.g., credit, liquidity, market) and unique risks to your organization, the banking system, or US financial stability, as applicable.
- Determine how existing or future systems will be able to effectively identify, measure, monitor, and mitigate risks presented by cryptocurrency activities.
- Depending on the materiality of the cryptocurrency initiative, draft a full business plan with supporting financials (to include a view on controls and policies).
- Clarify the change management process across skills.
- Conduct a skillset review across the three lines of defense, within impacted business lines, and throughout the risk/compliance and internal audit functions. Determine how management and staff are positioned and if they have the necessary skillsets.
- Leverage existing new product approval processes. Decide how cryptocurrency activities will be subject to new product governance processes in relation to strategic initiatives.
- Engage the board and C-suite. Initiate corporate governance and business oversight processes for cryptocurrency activities. Provide the necessary training to confirm that board members and senior management have the requisite skills and abilities to review and challenge management.
- Solidify the linkage between strategy, strategic initiatives, and governance for potential business activities. Review the impact of cryptocurrency activities on the bank's risk appetite and strategic goals.
- Develop and implement a regulatory engagement plan.
- Develop a plan to communicate risks to consumers via disclosures and other means for customer-facing activities.[5]
- Perform a risk assessment focusing on digital assets and cryptocurrency products and services. Design risk identification and management methods for inclusion in related policies and procedures.

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Endnotes

1 U.S. Department of the Treasury, “Remarks from Secretary of the Treasury Janet L. Yellen on Digital Assets,” April 7, 2022.

2 Office of the Comptroller of the Currency (OCC), “OCC Clarifies Bank Authority to Engage in Certain Cryptocurrency Activities and Authority of OCC to Charter National Trust Banks,” news release2021-121, November 23, 2021.

3 Federal Deposit Insurance Corporation (FDIC), “FDIC: FIL-16-2022: Notification of Engaging in Crypto-Related Activities,” April 7, 2022.

4 FDIC, “FDIC Law, Regulations, Related Acts – Federal Deposit Insurance Act,” accessed April 7, 2022.

5 In our previous publication, “So you want to be a crypto bank,” we discuss details on how banks and fintech companies can participate in crypto “banking” and other activities tied to cryptocurrencies.