



Digital Assets Banking and Capital Markets Regulatory Digest: January 2024

Center for
**Regulatory
Strategy**
US

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1. Introduction

The discourse surrounding digital assets and their applications has undergone significant developments. After the failure of several digital asset entities, there has been an increased readiness among policymakers and regulatory authorities to tackle the unresolved issues prevalent within the sector. In spite of the ambiguity within the current system, progress continues to be made toward regulatory clarity. As other jurisdictions implement comprehensive rules for digital assets, US policymakers are increasingly feeling pressure to respond to maintain US competitiveness. In the absence of federal legislation, many states are developing their own rules and licensing frameworks. As a result of these and other forces in the space, a few themes are expected to drive the US policy environment in 2024, including:

- **Enforcement intensifies:** In line with our previous digest issues' forecasts, regulatory bodies have intensified enforcement actions aimed at businesses operating in the digital asset sector, with a particular focus on crypto exchanges. We expect this trend of rigorous enforcement continuing into the foreseeable future, given the increasing recognition of digital assets and their impact on the financial landscape.
- **Market infrastructure under-developed, but evolving:** Compared to the traditional financial market, the digital asset space lacks much of the needed market infrastructure for widespread institutional and retail adoption. A promising development is the Securities and Exchange Commission's (SEC) recent approval of the first spot bitcoin exchange-traded fund (ETF), which may serve as a significant milestone towards improving liquidity within the market. We expect the digital asset market infrastructure to continue to mature and evolve in the years ahead.
- **Banks continue to be discouraged from engaging in digital assets:** In recent years, regulators have attempted to limit the connection points between the traditional financial system and digital asset ecosystem. International standard-setting bodies have proposed stringent capital treatment measures for digital assets, while federal banking regulators have instituted non-objection processes and special supervisory programs for banks engaging in novel activities. As such, it is expected that these regulatory measures will continue to dissuade banks from engaging in digital assets, thereby creating a gap that nonbank financial companies (NBFCs) may potentially fill.
- **Accounting and tax treatment remains in focus:** Regulatory and professional bodies have made efforts in recent months to provide clarity on the accounting and tax treatment of digital assets. However, some of these developments, such as SAB 121, have been criticized by some market participants as burdensome and discouraging, while others, such as the Department of Treasury's proposed regulations for transaction tax reporting, continue to receive extensive engagement from the market. We expect attention to focus on areas such as interpretation of key terms, classification, and user privacy.

We have identified certain regulatory developments and will unpack some of their implications within five policy focus areas:

1. **Classification and reporting of digital assets:** While the reporting framework for digital assets is becoming clearer, disputes over the classification of specific assets continue as both regulators and the industry remain litigious. We expect a broad shift to tokenization of a range of assets, which is raising a new set of regulatory questions on the underlying technology.
2. **Regulating crypto exchanges:** Exchanges face increased regulatory pressures that extend beyond the established asset classification debate and could test their business model.
3. **Stablecoin issuance:** The regulatory treatment of stablecoins appears more muddled than ever. The President's Working Group Report on Stablecoins recommended a bank regulatory framework, yet recent enforcement actions by the Securities and Exchange Commission have further complicated the regulatory approach. Several legislative approaches are being discussed.
4. **Path to a US CBDC:** Initiatives to modernize the financial system through a US central bank digital currency (CBDC) are still at early stages. However, there remains significant political resistance to the idea.
5. **Tokenization of real-world assets:** As industry participants continue to explore the development of tokenization, regulators and policymakers continue to study the technology's implications, balancing innovation, investor and consumer protection, and financial stability.

2. Policy primer mark-to-market

In our policy primer, we outlined two distinct paths that US regulatory policy could potentially take: with legislation or without legislation. Since there has not been federal legislation clarifying the regulatory framework for digital assets, the recent developments are more consistent with our predictions for the regulatory environment to develop in a diffused pattern without legislation, such as through state and agency action including guidance, reports, and enforcement actions.

Topic	Previous outlook	What's changed
Classification and reporting of digital assets	International regulators are looking to provide a unified, harmonized regulatory environment for crypto and digital assets.	Efforts to classify and regulate digital assets remain a focus around the industry. In the absence of federal legislation, individual states (notably, New York and California) are implementing their own reporting and licensing structures.
Regulating exchanges	Enforcement actions against exchanges continue to cascade down in recent months, impacting small and large exchanges alike. This pressure will continue unless and until regulatory clarity is provided regarding the role of these exchanges, such as with Coinbase's petition to the SEC.	Legislators and regulators have continued to increase scrutiny and enforcement of exchanges in recent months, with an increasing focus on decentralized finance (DeFi). Recent proposed legislation would further regulate exchanges, as well as new proposed regulations on brokers and exchanges from the US Department of Treasury and the Internal Revenue Service (IRS).
Stablecoin issuance	The regulatory environment surrounding stablecoins has inched closer and closer to clarity in recent months and could become more well established if current bills are turned into law.	The fate of stablecoins in the United States will likely be closely tied to bills that have been proposed earlier this year. In the meantime, agencies are examining the risks that stablecoins could present in the market.
Path to a US CBDC	Development and issuance of a CBDC or other similar digital dollar project continues to become increasingly political and controversial, which could delay any major development progress. That being said, there still has not been any official decision on the pursuit of a CBDC.	Issuance of a CBDC has becoming an increasingly political issue in recent months, with new bills being introduced to slow or even stop research and development of such an instrument. However, there has still not been a firm decision on the pursuit of a CBDC in the United States.
Tokenization of real-world assets	As industry participants continue to explore the development of tokenization, regulators and policymakers continue to study the technology's implications, balancing innovation, investor and consumer protection, and financial stability.	

3. Classification, reporting, and registration

3.1 Federal Reserve SR 23-7: Creation of Novel Activities Supervision Program

SR 23-7: Creation of Novel Activities Supervision Program ¹	
Authority: Board of Governors of the Federal Reserve System (FRB)	Date: August 2023
Key summary points	Implications
<ul style="list-style-type: none">• To better enhance the supervision of risks associated with innovation, the FRB has established a new program, the Novel Activities Supervision Program, to monitor and examine activities conducted by supervised banking organizations.• The program will focus on four pillars:<ol style="list-style-type: none">1. Complex, technology-driven partnerships with non-banks to provide banking services (e.g., banking-as-a-service).2. Crypto-asset related activities (e.g., custody, lending, issuance).3. Projects that use distributed ledger technology (DLT) with the potential for significant impact on the financial system.4. Concentrated provision of banking services to crypto asset-related entities and fintech companies.• The Program is not a new supervisory portfolio but will instead work within existing supervisory portfolios and alongside existing supervisory teams.• The Federal Reserve will notify banking organizations in writing when their novel activities will be examined under the program, and this list will be updated periodically.	<ul style="list-style-type: none">• The Federal Reserve's Novel Activities Supervision Program signals increased scrutiny on novel activities in crypto assets, DLT, and tech-driven partnerships.• Institutions engaged in any of the Program's four pillars will need to prepare for greater supervisory scrutiny and be able to demonstrate that governance and risk management controls are appropriately tailored to the unique risks of these activities.• Notable is the Program's fourth pillar which focuses on traditional banking services to crypto asset-related entities and fintech companies, suggesting that heightened scrutiny will be applied based on client type as well.• Expect significant supervisory attention for the firms that are engaged in activities subject to this scope, supervisory impacts will be akin to larger bank supervisory practices. Exam activities will likely commence shortly.

Additional material: Deloitte, "[Federal Reserve Board establishes Novel Activities Supervision Program](#)," August 2023.

3.2 Digital Asset Anti-Money Laundering Act of 2023

Digital Asset Anti-Money Laundering Act of 2023 ²	
Authority: US Senate	Date: August 5, 2023
Key summary points	Implications
<ul style="list-style-type: none"> • Expands Bank Secrecy Act (BSA) obligations, including know your customer (KYC) requirements to crypto-related companies, including digital wallet providers, miners, and other network participants involved in validating, securing, or facilitating digital asset transactions. • Closes a significant loophole related to “unhosted” digital wallets which allowed individuals to bypass anti-money laundering and sanctions tests. • Mandates that banks and money service businesses verify customer and counterparty identities, maintain records, and submit reports for specific digital asset transactions involving unhosted wallets or wallets hosted in non BSA-compliant jurisdictions. • Mandates Financial Crimes Enforcement Network (FinCEN) to finalize rules for financial institutions on managing the risks associated with handling, using, or transacting with assets anonymized through digital asset mixers and other anonymity-enhancing technologies. • Enhance enforcement of BSA compliance by instructing the Treasury Department to establish an anti-money laundering (AML)/countering the financing of terrorism (CFT) compliance examination and review process for digital asset participants. • Broaden rules concerning the reporting of foreign bank accounts to include digital assets. 	<ul style="list-style-type: none"> • The Act was reintroduced by a bipartisan group of senators led by Senators Elizabeth Warren (MA-D) and Roger Marshall (KS-R) after having been originally introduced in 117th Congress. • The reintroduction of the Act with bipartisan support suggests growing concern among legislators of crypto-AML risks and potential new momentum for federal legislation. • This Act follows a growing international movement to address money laundering concerns in the cryptocurrency industry with countries such as Japan, South Korea, and India already having taken similar steps.

3.3 FDIC Risk Review: Crypto Asset Risk

FDIC Risk Review: Crypto Asset Risk ³	
Authority: Federal Deposit Insurance Corporation (FDIC)	Date: October 18, 2023
Key summary points	Implications
<ul style="list-style-type: none">• The Office of the Inspector General (OIG) of the FDIC released a report on the FDIC’s strategies for managing risks associated with crypto assets.• The OIG made two recommendations to the FDIC:<ol style="list-style-type: none">1. Establish a plan with timeframes for assessing risks pertaining to crypto-related activities; and2. Update and clarify the supervisory feedback process related to its review of supervised institutions’ crypto-related activities.• The report pointed out that the FDIC has not yet completed a risk assessment to determine whether it can sufficiently address crypto asset-related risks through actions such as issuing guidance to supervised institutions.• The OIG also warned that a lack of review process could create a perception that the supervisory body is not being supportive of institutions currently engaging or planning to engage with crypto.• The FDIC has agreed with the report’s recommendations and plans to complete corrective actions for these recommendations by the end of January 2024.	<ul style="list-style-type: none">• The report’s findings validate many industry concerns that the FDIC has lacked sufficient feedback for supervised institutions, which has resulted in a state of uncertainty for market participants.• The FDIC agreed with the report’s findings and committed to completing corrective actions by the end of January 2024, suggesting the agency may soon provide additional guidance for digital asset activities and address existing gaps in the current regulatory framework.

3.4 California Digital Financial Assets Law

California Digital Financial Assets Law ⁴	
Authority: State of California	Date: October 2023
Key summary points	Implications
<ul style="list-style-type: none"> California enacted the Digital Financial Assets Law (DFAL), which will create a comprehensive licensing framework for digital asset businesses in the state under the supervision of the Department of Financial Protection and Innovation (DFPI). The law defines “digital financial asset” to mean “a digital representation of value that is used as a medium of exchange, unit of account, or store of value, and that is not legal tender, whether or not denominated as legal tender” and excludes reward points, game platform values, and SEC-registered securities. DFAL exempts banks, California and federal trust companies, and certain other narrow categories of persons, and allows DFPI to issue a “conditional license” to applicants holding a “BitLicense” from the New York State Department of Financial Services (NYDFS). The law takes effect July 1, 2025. 	<ul style="list-style-type: none"> DFAL is a significant step towards regulatory clarity for blockchain and digital asset firms, which have, until now, operated in a relatively unregulated manner in California. While the federal government has yet to enact any significant legislation for digital assets, the DFAL contributes to a growing trend of states establishing stand-alone regulatory frameworks for digital assets, including New York and Illinois. Given the size and influence of the California economy and the current absence of comprehensive federal law and regulation addressing digital assets, DFAL will likely have a significant impact on the digital asset industry and direction for any future regulatory developments.
Additional material: Deloitte, “California passes digital asset regulatory framework,” January 2024.	

3.5 GAO Report on Applicability of the Congressional Review Act to SAB No. 121

GAO Report on Applicability of the Congressional Review Act to Staff Accounting Bulletin No. 121 ⁵	
Authority: Government Accountability Office (GAO)	Date: October 31, 2023
Key summary points	Implications
<ul style="list-style-type: none">• The US Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin No. 121 (Bulletin) on March 31, 2022.• This Bulletin serves as a report and provides interpretive guidance on how covered entities should account for and disclose their custodial obligations for safeguarding crypto assets held for platform users.• The SEC did not submit a report on the Bulletin to Congress or the Comptroller General under the Congressional Review Act (CRA).• The CRA mandates that before a rule can take effect, it needs to be reported to both the House of Representatives and the Senate, as well as the Comptroller General. It also outlines procedures for congressional review, allowing Congress to disapprove rules.• The CRA adopts the definition of a rule under the Administrative Procedure Act (APA) but excludes certain categories of rules.• The Bulletin qualifies as a rule under CRA as it meets the APA definition of a rule, and no exceptions apply.• Consequently, the Bulletin should have been submitted to Congress according to the requirements of the CRA.	<ul style="list-style-type: none">• Providing interpretive guidance on custodial obligations for crypto assets held for platform users, the Bulletin aims to standardize reporting practices in the crypto space.• Mention of the CRA and its procedures for congressional review highlights legislative checks and balances, emphasizing transparency and accountability in rulemaking.• The Bulletin qualifies as a rule under CRA, subjecting even interpretive guidance to congressional scrutiny, revealing the substantial regulatory impact of such guidance.• The Bulletin's guidance directly impacts covered entities, influencing how they report custodial obligations for crypto assets, potentially necessitating changes in operational practices.• Non-compliance with the CRA may attract congressional scrutiny, influencing the SEC's relationship with Congress and potentially affecting future rulemaking.

3.6 Financial Accounting Standards Board: Accounting Standards Update

Financial Accounting Standards Board: Accounting Standards Update ⁶	
Authority: Financial Accounting Standards Board (FASB)	Date: December 2023
Key summary points	Implications
<ul style="list-style-type: none"> • FASB issued the Accounting Standards Update (ASU) to enhance accounting and disclosure of certain crypto assets. • Amendments in the ASU require measuring crypto assets at fair value each reporting period, with changes recorded in net income. • Disclosure requirements include significant holdings, contractual sale restrictions, and changes during the reporting period. • The ASU applies to assets meeting specific criteria such as being intangible, blockchain-based, secured through cryptography, and not issued by the reporting entity. • Non-fungible tokens (NFTs), stablecoins, and other issuer-created tokens are excluded from this update • Effective for all entities for fiscal years beginning after December 15, 2024, with early adoption permitted. 	<ul style="list-style-type: none"> • FASB's new accounting standards will likely lead to more volatility in net income for companies that directly hold crypt assets, as previous accounting practices only allowed recording the lows. • The amendments aim to offer more relevant information to investors, requiring disclosure of significant holdings and contractual restrictions. • Industry response has been largely positive, with many market participants emphasizing the importance of standardization for investor confidence.

3.7 Financial Stability Oversight Council: Annual Report 2023

Financial Stability Oversight Council: Annual Report 2023 ⁷	
Authority: Financial Stability Oversight Council (FSOC)	Date: December 2023
Key summary points	Implications
<ul style="list-style-type: none">• FSOC unanimously approved its 2023 annual report, focusing on reviewing financial market developments, identifying emerging threats, and making recommendations for US financial stability.• The report highlights the resilience of the U.S. financial system, touching on several notable topics, including banking and financial intermediation, artificial intelligence, climate change-related financial risk, and digital assets.• According to the report, digital assets pose financial stability vulnerabilities due to several factors, including:<ul style="list-style-type: none">• The industry’s high use of leverage;• The level of interconnectedness among digital assets,• Operational risks;• Risks surrounding runs on crypto asset platforms and digital assets;• Token ownership concentration;• Cybersecurity risks; and• The proliferation of platforms acting outside of or out of compliance with applicable laws and regulations.• As a result of these and other vulnerabilities, the Council urged enforcement of existing rules and legislation for stablecoins and non-security crypto assets.	<ul style="list-style-type: none">• The recommendation to enforce existing laws remain unchanged from last year’s report, underscoring the slow pace of legislation and regulation regarding digital assets.• The report could encourage lawmakers to move more quickly on various bills currently being considered by Congress.<ul style="list-style-type: none">• This includes a pair of bills that seek to address some of the challenges mentioned in the report, including H.R. 4763, the Financial Innovation and Technology for the 21st Century Act, and H.R. 1747, the Blockchain Regulatory Certainty Act.

4. Regulating exchanges

4.1 Proposed Regulations on Reporting by Brokers for Sales or Exchanges of Digital Assets

Proposed Regulations on Reporting by Brokers for Sales or Exchanges of Digital Assets ⁸	
Authority: Internal Revenue Service (IRS)	Date: August 25, 2023
Key summary points	Implications
<ul style="list-style-type: none"> • The proposal establishes a new Form 1099-DA for digital asset trading platforms, payment processors, and hosted wallet providers. • The proposed regulation, set to become effective January 1, 2025, outlines gain/loss computation rules, basis determination rules, and backup withholding rules for digital asset sale and exchange transactions. • Real estate reporting persons, including title companies and mortgage lenders, are treated as brokers for digital asset dispositions and must include the fair market value of digital assets paid in real estate transactions on Form 1099-S. 	<ul style="list-style-type: none"> • The proposal is focused on preventing tax evasion through digital assets, with an emphasis on third-party reporting to improve compliance and provide transparency into the activities of high-income individuals • The regulations indicate a proactive approach by the IRS to address potential tax evasion through digital assets, showcasing a commitment to maintaining tax integrity within the evolving landscape of digital assets. • The emphasis on transparency through third-party reporting aligns with broader efforts to prevent the misuse of digital assets for hiding taxable income.

4.2 Commodity Futures Trading Commission: Bitnomial Approval

Commodity Futures Trading Commission: Bitnomial Approval ⁹	
Authority: Commodity Futures Trading Commission (CFTC)	Date: December 2023
Key summary points	Implications
<ul style="list-style-type: none"> • In a divided vote, the CFTC recently approved Bitnomial's application to launch a regulated clearinghouse, allowing the company to run a derivative clearing organization. • The CFTC also proposed new rules on cybersecurity and protecting clearinghouse members' funds on the same day as Bitnomial's approval. • Bitnomial's CEO, Luke Hoersten, said in a statement that he sees this approval as indicative of the future of the industry, describing it as being at the forefront of change. 	<ul style="list-style-type: none"> • This is the first time the CFTC has allowed a vertically integrated market structure, marking a shift in the regulatory landscape. • The approval is expected to set a precedent for others seeking similar arrangements, potentially altering the CFTC's market structure. • The divide over Bitnomial reflects ongoing tensions among Washington regulators regarding how to regulate the growing digital asset market within existing rules.

5. Path to a US CBDC

5.1 CBDC Anti-Surveillance State Act

CBDC Anti-Surveillance State Act ¹⁰	
Authority: US House of Representatives	Date: September 12, 2023
Key summary points	Implications
<ul style="list-style-type: none">• On Sept. 12, 2023, Rep. Tom Emmer and 49 co-sponsors reintroduced the “CBDC Anti-Surveillance State Act” in the US House of Representatives in an effort “to protect Americans’ financial privacy.”• The bill was introduced in response to privacy concerns among several legislators related to a potential CBDC The bill was first proposed in January 2022 and formally introduced to Congress in February 2023.• The legislation aims to limit the Federal Reserve from minting a programmable digital dollar.• The bill prevents the FRB from issuing a CBDC to individuals, blocking it from becoming a retail bank collecting personal financial data.• The bill also restricts the central bank from using any CBDC to implement monetary policy.• This follows other anti-CBDC proposals in recent months, including the “Digital Dollar Pilot Prevention Act” bill¹¹ as controversy continues to mount surrounding the possibility of a digital dollar project.	<ul style="list-style-type: none">• The bill further restricts the central bank from using any CBDC to implement monetary policy, potentially limiting the scope of CBDC influence on economic tools.• This legislation is part of a broader trend of anti-CBDC regulation in recent months, exemplified by the previously introduced “Digital Dollar Pilot Prevention Act” bill. The controversy surrounding the potential launch of a digital dollar project has sparked increased regulatory scrutiny.• The reintroduction of the CBDC Anti-Surveillance State Act reflects ongoing concerns about privacy infringement and surveillance associated with the development and implementation of CBDCs.• The bill's focus on limiting the Federal Reserve’s authority in issuing a CBDC underscores apprehensions about the potential impact on individual financial privacy and the broader financial system.• The legislative response aligns with a growing sentiment that regulatory frameworks must be established to balance the potential benefits of CBDCs with privacy and surveillance risks.

6. Tokenization of real-world assets

6.1 Securities and Exchange Commission Approves First Bitcoin Spot ETFs

Securities and Exchange Commission Approves First Bitcoin Spot ETFs ¹²	
Authority: Securities and Exchange Commission (SEC)	Date: January 10, 2024
Key summary points	Implications
<ul style="list-style-type: none"> On Jan. 10, 2024, the SEC approved the first bitcoin spot ETFs, more than 10 years after the first bitcoin spot ETF application was submitted in 2013. The approval of the bitcoin spot ETFs comes after the agency declined to appeal an August 2023 ruling by the US District of Columbia Court of Appeals that held the SEC acted "arbitrary and capricious" when it rejected a prior bitcoin spot application. The Court found the proposed bitcoin spot ETF was "materially similar" to SEC-approved bitcoin futures ETFs that trade on the Chicago Mercantile Exchange (CME). The SEC found a high correlation between the CME bitcoin futures market and spot prices, suggesting that any fraudulent or manipulative activities affecting spot bitcoin prices would likely impact CME bitcoin futures prices as well. Therefore, the SEC concluded that the market surveillance-sharing agreement between the CME and spot exchanges could effectively address its concerns about fraud and market manipulation. The newly approved ETFs (11 in total) are now trading on three major exchanges: NYSE Arca, Nasdaq Stock Market, and Cboe BZX Exchange. 	<ul style="list-style-type: none"> Given the technical requirements to store and safely maintain digital assets, the approval of bitcoin spot ETFs may encourage more adoption of digital assets by retail and institutional investors. Compared to existing digital asset futures ETFs, a bitcoin spot ETF may lower costs for investors as spot ETFs will not have rollover costs associated with futures contracts. Market participant responses have been overwhelmingly positive. Given the significant milestone and investor appetite, more digital asset spot ETF applications may follow, potentially offering investors with a wider range of means to invest in digital assets and increased competition.

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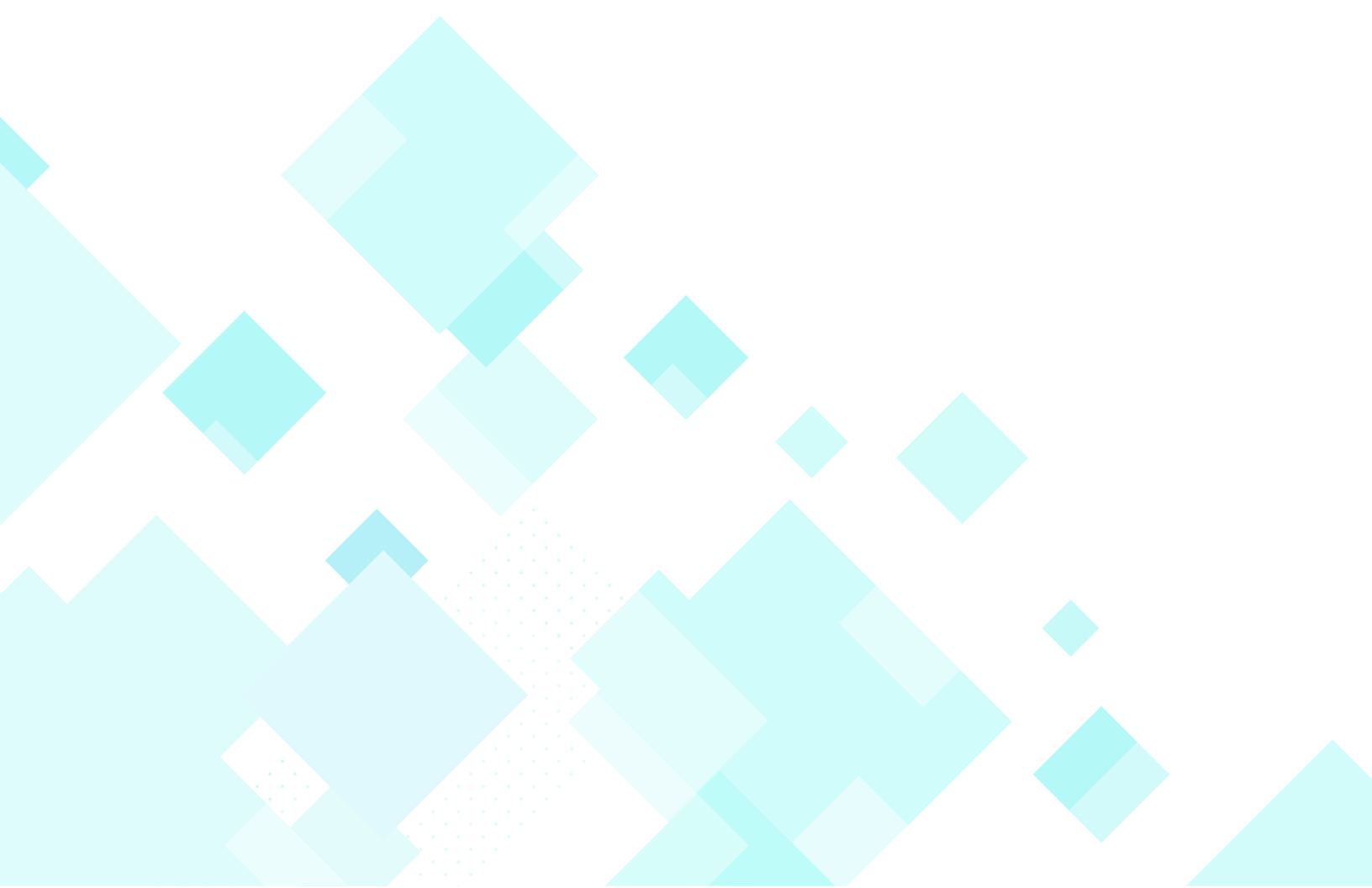
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Endnotes

¹ Board of Governors of the Federal Reserve System, "[SR 23-7: Creation of Novel Activities Supervision Program](#)," August 8, 2023.

² US Senate, "[Digital Anti Money Laundering Act of 2023](#)," August 2023.

³ Federal Deposit Insurance Corporation (FDIC), Office of Inspector General, "[FDIC Strategies Related to Crypto-Asset Risks](#)," October 18 2023.

⁴ State of California, [California Digital Financial Assets Law](#), October 16, 2023.

⁵ Government Accountability Office, "[Securities and Exchange Commission—Applicability of the Congressional Review Act to Staff Accounting Bulletin No. 121](#)," October 31, 2023.

⁶ Financial Accounting Standards Board, [Accounting Standards Update: Intangibles – Goodwill and Other – Crypto Assets](#), No. 2023-08, December 2023.

⁷ Financial Stability Oversight Council, [Annual Report 2023](#), December 2023.

⁸ Internal Revenue Service, "[Gross Proceeds and Basis Reporting by Brokers and Determination of Amount Realized and Basis for Digital Asset Transactions](#)," August 29, 2023.

⁹ Commodities Futures Trading Commission, "[CFTC Approves Two Proposals and a DCO Application](#)," December 18, 2023.

¹⁰ US House of Representatives, [CBDC Anti-Surveillance State Act](#), 118th Cong., reintroduced September 12, 2023.

¹¹ US House of Representatives, [Digital Dollar Pilot Prevention Act](#), 118th Cong., introduced May 25, 2023.

¹² Securities and Exchange Commission, "[Order Granting Accelerated Approval of Proposed Rule Changes, as Modified by Amendments Thereto, to List and Trade Bitcoin-Based Commodity-Based Trust Shares and Trust Units](#)," January 10, 2023.

Center for Regulatory Strategy US

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