August 8, 2022

Via Electronic Submission

Natalia Li
Deputy Director, Office of Financial Institutions Policy
U.S. Department of the Treasury
Office of Financial Institutions Policy
1500 Pennsylvania Avenue, NW
Washington, DC 20220

RE: Request for Comment – TREAS-DO-2022-0014-0001 – "Ensuring Responsible Development of Digital Assets"

Dear Ms. Li:

The Independent Community Bankers of America ("ICBA")[1] welcomes the opportunity to provide feedback on the U.S. Treasury Department's ("Treasury") Request for Comment on Ensuring Responsible Development of Digital Assets (the "Request").

ICBA and its members appreciate Treasury's engagement with the banking industry and American public to fulfill the directives outlined in President Biden's Executive Order on Ensuring Responsible Development of Digital Assets. Community banks play a leading role in developing the products and services that enable their customers and communities to benefit from advances in financial technology, so we welcome the opportunity to engage with policymakers to assess the potential benefits and risks of the growing digital asset market.

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

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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 century economy. Advocates for digital assets - ranging from cryptocurrencies like bitcoin to various tokenized assets - represent that they can provide new ways to increase speed, efficiency, and transparency in financial services for consumers and businesses. However, we are alarmed by the growing use of cryptocurrencies to facilitate ransomware, money laundering, sanctions evasion, and other criminal activity. Additionally, ICBA has serious concerns about the potential for disintermediation of traditional financial services by stablecoins and decentralized finance ("DeFi") - a result which could negatively impact and disrupt the nation's financial system as a whole.

Executive Summary

ICBA has closely monitored significant events in the crypto markets this year, especially the catastrophic failure of the algorithmic stablecoin TerraUSD. Community bankers are increasingly alarmed by the risks presented by digital assets, including scams, misrepresentations to consumers, and a growing potential for these digital assets to threaten the financial stability of the traditional banking sector. ICBA worked with its members to solicit feedback for this response, and we have identified the following as the most critical areas for the Treasury Department to consider as it weighs the future of digital assets and financial services:

- Broader use of cryptocurrency, without accompanying regulation or oversight, allows financial crimes and threats to national security to proliferate. Therefore, protecting national security and implementing anti-crime measures should be primary drivers of cryptocurrency policymaking and regulation.

- ICBA and its members support cross-agency collaboration to establish a clear regulatory framework for digital assets.

- Nonbank stablecoin issuers and unregulated cryptocurrency entities may disintermediate community banks, reducing deposits in the banking system, and restricting access to credit in local communities. To that end, ICBA believes that stablecoin issuance should be limited to insured depository institutions to address serious risks to financial stability, consumer protection, and national security.

- ICBA implores the banking regulators to continue the work they started with the Crypto-Asset Policy Sprint Initiative and communicate clear guidelines on how community banks can safely and permissibly offer crypto products and services to meet customer needs.

- 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.

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Suite 900
Washington, DC 20036

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518 Lincoln Road
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- ICBA calls upon regulators to move swiftly on a comprehensive framework that will address the shadow banking activities of unregulated platforms to protect the financial system.

- If the Administration believes that stablecoins or other digital assets will serve as a cornerstone for the digital economy, then community banks need clear guidance to develop safe and innovative solutions to meet their customers' needs.

- ICBA urges Treasury to give appropriate weight to our staunch opposition to a Central Bank Digital Currency ("CBDC").

- A CBDC would not yield benefits more effectively than alternative methods in the market today. Creating a CBDC would introduce risks without providing benefits to households, businesses, and the overall economy.

ICBA and its members welcome the opportunity to share our perspectives with Treasury and look forward to further engagement with the Administration as it considers the future of digital assets.

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.[2] 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, 2022, the cryptocurrency market was valued at less than $1 trillion, down nearly 67 percent from its peak last year.[3]

A few early adopter banks have started to offer crypto-related products and services, such as custodial services or holding stablecoin issuers' reserve accounts, in order to meet customer demand. Most community banks, however, are still evaluating and assessing underlying technologies, potential use cases, associated risks, and resulting regulatory responses. 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.

On March 9, 2022, President Biden signed an Executive Order with the goal of "outlining the first ever, whole-of-government approach to addressing the risks and harnessing the potential

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[2] 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/.
[3] See CoinMarketCap.com for overall cryptocurrency market value.

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benefits of digital assets and their underlying technology."[4] In the past few months, the government has published several requests for comment to gather public feedback on a range of topics detailed within the Executive Order. However, interests in the digital assets extend beyond the White House to other branches of the United States government. The House and Senate have both held several hearings on the impacts of cryptocurrency, and lawmakers have advanced multiple proposals to address growing risks within the sector. Members of Congress have also examined the possible creation of a CBDC, or a digital version of the dollar—a development that would have disastrous effects on community banks and the populations they serve.

ICBA and its members recognize the significance of these debates, and we have devoted considerable time and resources to studying the technologies to consider the potential benefits and risks. ICBA has been an active participant in policymaker debates on Capitol Hill, as demonstrated by ICBA's recent letter to the House Financial Services Committee that expressed community bankers' concerns about potential stablecoin legislation.[5] ICBA has also provided statements to Congress urging lawmakers to oppose the creation of a CBDC.[6]

ICBA Comments

Through its extensive community bank network, ICBA frequently engages its members to evaluate how community banks are exploring digital assets to address customer needs and learn more about how digital assets may impact the future of financial services. The following comments reflect their concerns about the risks of digital assets, potential benefits, and questions the lack of regulatory clarity:

1. Digital assets present numerous significant threats, including financial crimes and risks to financial stability. Many blockchain systems are also plagued by slow and inefficient transaction processing, and they experience frequent disruptions and outages.

2. Stablecoins currently exist in an unregulated space with several nonbank 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.

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[4] President Joseph R. Biden, Jr., Press Statement, "Fact Sheet: President Biden to Sign Executive Order on Ensuring Responsible Development of Digital Assets" (March 9, 2022), https://www.whitehouse.gov/briefing-room/statements-releases/2022/03/09/fact-sheet-president-biden-to-sign-executive-order-on-ensuring-responsible-innovation-in-digital-assets/.

[5] Independent Community Bankers of America, Letter to the House Committee on Financial Services ,"Re: Community Bank Perspective on Stablecoin Legislation" (July 22, 2022), https://www.icba.org/docs/default-source/icba/advocacy-documents/letters-to-congress/letter-on-stablecoin-legislation.

[6] Independent Community Bankers of America, Statement submitted to United States Senate, "Central Bank Digital Currency: Significant Risks Must Preclude Adoption," (May 26, 2022), https://www. icba.org/docs/default-source/icba/advocacy-documents/testimony/hearing-statement-on-central-bank-digital-currency.pdf.

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3. Federal banking and market regulators should collaborate on a comprehensive regulatory framework for digital assets. Responsible innovation requires policymakers to establish clear regulatory guidelines with input from the industry.

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 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.

Threats to Financial Stability and Significant Operational Risks

ICBA and its members have serious concerns about the risks posed by cryptocurrency to privacy, consumer protection, 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.

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 destabilizing the broader financial system.

Cryptoization, or the substitution of national monetary and payment systems by cryptocurrencies, has been repeatedly highlighted as a growing concern by organizations like the International Monetary Fund ("IMF"). The IMF warns that cryptoization can undermine national fiscal policies because cryptocurrencies "can facilitate tax evasion, and seigniorage revenue may also decline due to the shrinking role of central bank money in the economy."[7] If cryptocurrency becomes more widely adopted as an alternative to the United States dollar and the regulated payment system, community banks will suffer significant harm as depositors move assets from bank accounts onto crypto exchanges. The loss of deposits would have an immediate impact on community banks' ability to provide credit within their communities. The resulting loss of credit access to consumers and small businesses in communities across the country will inevitably lead to broader and far more damaging economic consequences. ICBA and its members call on

[7] International Monetary Fund, 2021, *Global Financial Stability Report—COVID-19, Crypto, and Climate: Navigating Challenging Transitions* (Washington, DC, October 2021), 52, https://www.imf.org/en/Publications/GFSR/Issues/2021/10/12/global-financial-stability-report-october-2021.

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policymakers to remember the vital role that community banks played in the distribution of the Small Business Administration's Paycheck Protection Program ("SBA's PPP")—community banks' rapid response and knowledge of their communities proved to be the lifeline for small businesses as the federal government sought to buoy the nation's economy at the start of the pandemic.

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. The Bank for International Settlements ("BIS") has 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."[8] 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 favor of higher capacity."[9]

The threat of network congestion, and other operational failures that disrupt blockchains, is a real concern today. In May, the Solana and Ethereum blockchains were disrupted after bots generated an excessive amount of network activity as they tried to create and sell non-fungible tokens.[10] The Solana network suffered an eight-hour outage and average Ethereum transactions fees soared to an all-time high of $200 per transaction.[11] More recently, the Celo blockchain, which is home to three different stablecoins, was offline for nearly an entire day before validators updated their software.[12] Hours-long outages and volatile, unpredictable fees are significant hurdles to adoption that policymakers should consider as they weigh the benefits and risks of digital assets.

In a recent speech, Acting Comptroller of the Currency Michael Hsu also identified the lack of interoperability within and across major blockchains as one of the largest hurdles to wider adoption.[13] Currently, one of the primary ways to address the lack of interoperability involves the use of so-called "cross-chain bridges" that allow users to exchange digital assets across blockchains. Unfortunately, these systems are repeatedly targeted by bad actors, as evidenced by

[8] Bank for International Settlements, *BIS Annual Economic Report*, "III. The Future Monetary System" (June 21, 2022), https://www.bis.org/publ/arpdf/ar2022e3.htm.
[9] Ibid.
[10] Macauley Peterson, *Blockworks*, "NFT Buying Frenzies Disrupt Solana and Ethereum Blockchains" (May 2, 2022), https://blockworks.co/solana-and-ethereum-suffer-weekend-disruptions-thanks-to-nft-mints/.
[11] "NFT Buying Frenzies Disrupt Solana and Ethereum Blockchains"; BitInfoCharts, Ethereum Avg. Transaction Fee historical chart, accessed August 1, 2022, https://bitinfocharts.com/comparison/ethereum-transactionfees.html#3m
[12] Felix Ng, *Cointelegraph*, "Celo network back online after almost 24-hour outage" (July 15, 2022), https://cointelegraph.com/news/celo-network-back-online-after-almost-24-hour-outage.
[13] 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/.

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P.O. Box 267
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the Axie Infinity hack earlier this year that resulted in over $600 million in stolen assets.[14] If cryptocurrencies and stablecoins are to play a role in the future of payments, policymakers must give consideration to these interoperability challenges and work with a broad set of stakeholders, including community banks, to evaluate potential solutions.

Financial Crime and Digital Assets

Broader use of cryptocurrencies has expanded the Bank Secrecy Act/Anti-Money Laundering ("BSA/AML") and other financial crime risk, including money laundering and terror financing threats. Further, cyber vulnerabilities create opportunities for adversaries to use digital assets to advance efforts that may threaten national security and harm American businesses. For example, the Axie Infinity attack, like many others before it, was attributed to North Korean hackers known as the Lazarus Group.[15] Although the federal government has targeted some crypto platforms that aid North Korean cybercriminals, such as the Office of Foreign Assets Control's ("OFAC") sanctioning of Blender.io, North Korea remains undeterred in their efforts to use cryptocurrency to evade sanctions to seek funding for the Kim regime and its weapons programs.[16] In June 2022, the Lazarus Group conducted another significant heist with an attack against Horizon Bridge that yielded $100 million in ether, USD Coin, Dai, and other assets.[17] All these attacks suggest that adversarial nation-states will continue to circumvent traditional financial systems through the use of cryptocurrencies or other digital assets. Therefore, it is critical for policymakers to consider the potential for cryptocurrencies to jeopardize national security.

Additionally, cryptocurrencies are frequently used by bad actors to facilitate money laundering, terrorist financing, and other financial crimes. American citizens are regularly targeted by scammers and cybercriminals who use cryptocurrency as their preferred method for ransomware or other scam related payments, such as romance scams or fraudulent investment schemes. In June, the Federal Trade Commission ("FTC") revealed that almost 46,000 Americans have lost nearly $1 billion to cryptocurrency scams since the start of 2021.[18] The FTC said that nearly $600 million was lost to crypto investment scams and romance scams claimed another $185 million.[19] The FTC found that Millennials reported the most fraud losses; however, elder

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[14] 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.
[15] Aaron Schaffer, "North Korean hackers linked to $620 million Axie Infinity crypto heist," Washington Post, April 14, 2022. https://www.washingtonpost.com/technology/2022/04/14/us-links-axie-crypto-heist-north-korea/ (accessed July 20, 2022).
[16] United States Department of the Treasury, Press Release, "U.S. Treasury Issues First-Ever Sanctions on a Virtual Currency Mixer, Targets DPRK Cyber Threats" (May 6, 2022), https://home.treasury.gov/news/press-releases/jy0768.
[17] Carly Page, *TechCrunch*, "North Korean Lazarus hackers linked to $100M Harmony bridge theft" (June 30, 2022), https://techcrunch.com/2022/06/30/north-korea-lazarus-harmony-theft.
[18] Lesley Fair, Federal Trade Commission, "Reported crypto scam losses since 2021 top $1 billion, says FTC Data Spotlight" (June 3, 2022), https://www.ftc.gov/business-guidance/blog/2022/06/reported-crypto-scam-losses-2021-top-1-billion-says-ftc-data-spotlight
[19] Ibid.

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Americans suffered the highest median losses, with those aged 70-79 seeing losses climb as high as $11,708.[20]

These attacks and scams, combined with the laundering of digital assets through decentralized exchanges and mixers, notably Tornado Cash, continue to complicate law enforcement's efforts to stop cybercriminals and recover users' stolen assets. Mixers are centralized or decentralized services "that attempt to obfuscate the source or owner of particular units of cryptocurrency by mixing the cryptocurrency of several users prior to delivery of the units to their ultimate destination."[21] While mixers are designed to provide privacy in cryptocurrency transactions, they are used by cybercriminals to conceal the source of funds and, in turn, willfully disregard BSA/AML requirements governing financial transactions. New research by Chainalysis shows the use of mixers has reached new heights this year, with the 30-day moving average value of assets received by mixers climbing to a peak of nearly $52 million in April.[22] Bad actors are driving this increase as Chainalysis noted that "nearly 10% of all funds sent from illicit addresses are sent to mixers — no other service type cracked a 0.3% mixer sending share."[23] The Financial Crimes Enforcement Network ("FinCEN") established, in 2019, guidance that mixers are money transmitters subject to Bank Secrecy Act ("BSA") reporting obligations, yet mixers flagrantly ignore these legal and regulatory requirements.[24] In fact, Chainalysis said it is not "aware of any mixers currently following rules related to the BSA's 'Know Your Customer' processes, source of funds checks, and other basic customer identification and due diligence regulations that [Money Service Businesses] are subject to in most jurisdictions."[25] These challenges should not be underestimated as policymakers consider the future of digital assets. Community banks are responsible actors that work with regulators and law enforcement to investigate and mitigate financial crimes. If digital assets are going to play a role in the future financial system, then all participants must be held to the same high standards and work to curtail the ability of bad actors to scam consumers and commit other financial crimes.

<u>Regulatory Harmonization and Clarity</u>

ICBA and its members support cross-agency collaboration to establish a clear regulatory framework for digital assets. 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.[26]

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[20] Ibid.
[21] United States Department of Justice, *Report of the Attorney General's Cyber Digital Task Force: Cryptocurrency Enforcement Framework* (October 2020), https://www.justice.gov/archives/ag/page/file/1326061/download.
[22] Chainalysis, "Crypto Mixer Usage Reaches All-time Highs in 2022 With Nation State Actors and Cybercriminals Contributing Significant Volume" (July 14, 2022), https://blog.chainalysis.com/reports/cryptocurrency-mixers/.
[23] Ibid.
[24] Financial Crimes Enforcement Network, FinCEN Guidance FIN-2019-G001, "Application of FinCEN's Regulations to Certain Business Models Involving Convertible Virtual Currencies" (May 9, 2019), https://www.fincen.gov/sites/default/files/2019-05/FinCEN%20Guidance%20CVC%20FINAL%20508.pdf.
[25] Chainalysis, "Crypto Mixer Usage Reaches All-time High."
[26] See OCC Interpretive Letter 1179 and FDIC Notification of Engaging in Crypto-Related Activities.

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Accordingly, regulators should apply a consistent approach to all entities engaged in similar digital asset products and services to support a consistent approach for competition and ensure appropriate robust protections for consumers.

The lack of a clear and comprehensive regulatory framework can have a chilling effect on innovation, leading to inaction or speculation among banks unclear about regulatory treatment around a new product or service. Responsible innovation in financial services requires clear guardrails so that banks know which activities are permissible as well as how products and systems should operate while mitigating risks, including those to BSA/AML compliance, vendor management, and liquidity, among others. Without such information, many banks may choose not to engage in cryptocurrency or other digital asset activities.

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 nonbank 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 voiced similar concerns about the growing risks associated with unregulated stablecoins. As noted in a new report by BIS, stablecoins are flawed because they "must import their credibility from sovereign fiat currencies, but they 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."[27]

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."[28]

To that end, ICBA continues to support 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. Limiting stablecoin issuance to insured depository institutions will ensure that stablecoins are subject to the established banking

[27] Bank for International Settlements, "III. The future monetary system."
[28] Acting Comptroller Michael Hsu, "Thoughts on Stablecoin Architecture."

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regulatory framework, complete with robust consumer protections and regulations that support safety and soundness throughout the financial system.

However, community banks need a clear path to pursue innovation responsibly. In the past several months, both the OCC and the FDIC have issued bulletins indicating that banks must receive regulator-approval prior to engaging in any crypto-related activities, including stablecoins.[29] These actions are not in concert with statements issued by the Board of Governors of the Federal Reserve (the "Board"), OCC, and FDIC that indicated the agencies would release additional guidance on stablecoin issuance and distribution in 2022. As we approach almost nine months without any new guidance, we implore the banking regulators to continue the work they started with the Crypto-Asset Policy Sprint Initiative and communicate clear guidelines on how community banks can offer crypto products and services to meet customer needs.[30]

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. Providing a path for nonbanks to issue stablecoins, without applying the same rigorous regulation that banks follow to support the integrity and safety of financial system, will only lead to an unlevel playing field that will introduce new risks and raise concerns about potential harm to consumers and investors.

Access to Bank Accounts Improves Financial Inclusion

According to the most recent FDIC survey, nearly 95 percent of all American families have access to a bank account.[31] 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.

However, ICBA and its members also recognize that financial inclusion is much more than simply opening a bank account or facilitating payments—financial inclusion means going the extra mile to help customers establish and maintain financial well-being. Community banks in areas with large immigrant populations demonstrate this commitment to their communities by maintaining staff who are fluent in multiple languages, using alternative forms of identification to meet "Know Your Customer" requirements, or using alternative data when assessing

[29] The OCC's Interpretive Letter #1179 and the FDIC's FIL-16-2022 both affirmed that community banks could pursue crypto products and services, as long as they notified their regulator and received supervisory approval. However, several community banks have reported that they difficulty receiving clear answers to their questions.
[30] The Federal Reserve, OCC, and FDIC published a joint statement in November 2021 to mark the end of their Crypto-Asset Policy Sprint Initiative. The statement said that the regulatory agencies would "provide greater clarity" on several crypto-related activities, including stablecoin issuance and distribution.
[31] Federal Deposit Insurance Corporation, "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.

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creditworthiness. As an example, one community bank in Massachusetts developed language and citizenship courses to help meet their needs of their customers.[32]

It is this level of commitment, care, and attention to customers and the wider community that is not easily replicated or reproduced by crypto platforms. Community banks are the foundation of their communities' economic activities, and these connections will continue to have meaning even as the digital economy expands and new opportunities develop. We encourage policymakers to consider the vital role of community banks as they debate the future of digital assets—Main Street still matters in the 21st century economy.

Crypto Platforms May Engage in Risky Activities

A bank account with a local community bank 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 do not offer consumers the same level of protection and trust offered by community banks. The lack of regulation, combined with extreme market volatility, smart contract flaws and criminal activity, present consumers with heightened and unacceptable risks. In the past few weeks, several crypto platforms unexpectedly limited withdrawals and other user activity, leaving untold numbers of consumers unable to access their assets. In some cases, these platforms even marketed themselves as alternatives to regulated financial institutions.[33] Many failed crypto platforms are now moving through the bankruptcy process, but customers are still uncertain as to whether they will ever regain access to their digital assets.

The clear and present danger of crypto shadow banks has been laid bare before the public and policymakers by the latest crypto market turmoil. Although the volatility has not yet spread into the traditional financial system, ICBA and its members remain concerned that the next crypto collapse may spill over onto Main Street. ICBA and its members call upon regulators to move swiftly on a comprehensive framework that will address the shadow banking activities of these unregulated platforms to protect the financial system.

Community banks have a track record of safeguarding customer assets, so community banks can play a significant role in the growing digital economy. If the Administration believes that stablecoins, or other digital assets, will serve as a cornerstone for the digital economy, then community banks need clear guidance to develop safe and innovative solutions to meet their customers' needs.

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[32] Independent Community Bankers of America, *Financial Inclusion Report* (September 2021), https://www.icba.org/docs/default-source/icba/advocacy-documents/reports/financial-inclusion-report.pdf
[33] Voyager Digital is currently under investigation by the Federal Deposit Insurance Corporation for issuing statements that led customers to believe that user assets were subject to deposit insurance.

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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.[34] 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 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.

ICBA Opposes Creation of a U.S. CBDC

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

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[34] 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.

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

SAUK CENTRE, MN
518 Lincoln Road
P.O. Box 267
Sauk Centre, MN 56378

866-843-4222
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ensure the U.S. payments and monetary system remains modern and competitive, creating a CBDC would introduce risks and additional costs without providing benefits to households, businesses, and the overall economy.

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."[35]

ICBA urges Treasury 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 SBA's PPP 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 Treasury 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, 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 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

[35] 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.

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

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518 Lincoln Road
P.O. Box 267
Sauk Centre, MN 56378

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Liang, Undersecretary for Domestic Finance at the Treasury Department, discussed additional means of addressing unequal access to the financial system, including FedNow.[36]

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 the compliance burdens of numerous requirements, including identity-verification, customer service, Know Your Customer (KYC), Anti-Money Laundering (AML), privacy protections, sanctions screening with no clearly identified revenue stream to compensate banks for these services. Because the Federal Reserve has proposed that banks would compete with regulated nonbanks in an open market, community banks would be at risk of losing customers to wallets offered by less regulated companies.

A CBDC Will Impede the Formation of Banking Relationships and Harm Small Businesses

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 to 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 and ultimately help their customers. Community banks may have additional costs and hurdles when offering CBDC wallets than 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

[36] 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.

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

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518 Lincoln Road
P.O. Box 267
Sauk Centre, MN 56378

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customer service as community banks, the long-term unintended consequences 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, "[d]espite 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, "[c]ommunity 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."[37] While we appreciate the Chairman's commitment to a continued dialogue, we do not believe that the authority for the Federal Reserve to issue a CBDC exists under current law. ICBA also urges Congress to consider the many risks and concerns raised above and not authorize the creation of CBDC.

Conclusion

ICBA and its members appreciate the opportunity to comment on the Treasury's Request. We believe that any federal regulatory framework for digital assets must protect the nation's financial system from unsound risks and criminal activity, must protect consumers from misrepresentations and must preserve the separation of banking and commerce. We look forward to working with the Treasury on developing policies that will enable community banks, and their

[37] "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).

WASHINGTON, DC
1615 L Street NW
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Washington, DC 20036

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518 Lincoln Road
P.O. Box 267
Sauk Centre, MN 56378

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customers to benefit from advances in financial technology without sacrificing the health of the broader economy. 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