Whither the Biden Administration Finreg Agenda?

At the beginning of the year, we observed that "we do not think the agencies will be able to address fully" all items on the financial regulatory agenda. We also noted that "regulatory approaches to cryptoassets will be front and center in 2022". With the first quarter behind us, we remain of the same view.

Indeed, the banking agencies seem to have spent several months waiting for Senate-confirmed leadership to be in place before moving forward in earnest on many policy issues. Yet, the Federal Reserve Board ("FRB") remains without a Vice Chair for Supervision[1] and Senator Sherrod Brown, Chair of the Senate Banking Committee, has said that he sees no need to confirm leadership at the Office of the Comptroller of the Currency ("OCC") or the Federal Deposit Insurance Corporation ("FDIC").[2] As a result, there is limited time remaining to make progress on the regulatory agenda and, therefore, the number of issues to be tackled is likely to be fewer.

For this reason, regulatory approaches to cryptoassets are likely to take a significant portion of available policymaking bandwidth for the remainder of the year. For stablecoins, which have received a particularly large amount of attention from Congress and other policymakers, we believe policymakers on both sides of the aisle are increasingly showing public indications of a willingness to find common ground on good policy, compromise and get something done. Therefore, stablecoin legislation has a chance of becoming law in 2022. Such a law should provide banks and nonbanks alike with clearer rules of the road, which, in turn, should help accelerate innovation and competition. And, ultimately, the "future of money" also should become meaningfully clearer.

Below we review important developments from early 2022, and provide thoughts what to expect over the mid-year period.

Early 2022 Developments

- Several legislative proposals have been put forward for the regulation of stablecoins (see our summary of the proposals here). These follow the November 2021 recommendations made by the President's Working Group ("PWG") on Financial Markets for Congress to pass legislation requiring stablecoin issuers to be insured depository institutions and to provide federal authorities with oversight over custodial wallet providers and other key participants in stablecoin arrangements (see our prior analysis here).

- Notably, one of the legislative proposals was put forward by Senator Pat Toomey, Ranking Member of the Banking Committee (see our summary of his proposal here). In releasing the proposal, Senator Toomey said he has been in discussions with the Biden administration and he believes "there is a possibility of bipartisan consensus".[3] We agree. There are a variety of issues that the legislation likely would address, but none seem insurmountable to us from a policy—as opposed to political—perspective.

- The FRB appears to be preparing for such an outcome too. For example, in February
    - Governor Lael Brainard said that the FRB is experimenting "with stablecoin interoperability and testing of retail payments across multiple distributed payment ledger systems".
    - The Financial Stability Oversight Council ("FSOC") released minutes from a December 2021 meeting in which an FRB staffer said "the agencies would develop a regulatory and supervisory framework for banking organizations' participation in stablecoin arrangements".

[1] On Friday, April 15, 2022, President Biden announced his intent to nominate Michael Barr for the role.

[2] "With Marty at FDIC, with Michael at OCC, I think that we can move forward without full-time directors or confirmed directors". Virtual Press Conference (Jan. 18, 2022). *See also* Brendan Pedersen, *White House in no hurry to confirm key bank regulators*, American Banker (April 11, 2022), available here.

[3] https://subscriber.politicopro.com/article/2022/04/toomey-proposes-occ-oversight-of-stablecoin-00023533

• In January, the FRB released a paper to examine the pros and cons of a potential U.S. central bank digital currency ("CBDC") (see our summary here). The paper invited public comment by May 20, 2022. The paper was open ended and, in our view, shows that the FRB is looking for clear direction from the executive and legislative branches and is leaving the agency open for a wide range of outcomes.

• On March 1, 2022, the FRB invited public comment on a supplement to its prior proposal regarding the process and standards it uses to evaluate requests for access to the Federal Reserve's payment system. Of note, the supplemental proposal would provide an easier way for institutions without deposit insurance (such as a state chartered, special purpose institution) to access the Federal Reserve's payment systems by having their parent companies agree to be regulated by the FRB through commitments (essentially a contract) with the FRB. The supplement, however, did not describe the substance of those commitments in any detail.

• On March 9, 2022, President Biden signed an executive order ("EO") on ensuring responsible development of digital assets. The EO is wide-ranging, and requires the federal government to study legal, national security and other policy and technology-related issues with respect to a potential U.S. CBDC and cryptoassets more broadly. See here for our timeline of reports required under the EO. We view the EO as a sign that the administration would like to take more control over the policy debate regarding a CBDC and cryptoassets more broadly, particularly because of the intersection of this issue with national security and international financial system leadership.

• The FDIC released guidance requesting that FDIC-supervised institutions provide the agency notice prior to engaging in "crypto-related" activities. The guidance follows similar guidance issued by the OCC at the end of 2021 (see our prior analysis here).

• These issues also remain at the fore at the international level. For example, on March 31, 2022, the Financial Stability Board issued its "work programme" for 2022. The agenda includes "harnessing the benefits of digital innovation while containing its risks".

Mid-Year Outlook

Over the next several months, we will be watching the following points.

• As noted, from a policy perspective, we see a real possibility for bi-partisan agreement on stablecoin legislation. We anticipate further proposals and hearings from Capitol Hill. We will be watching the tone at any hearings closely to see if bi-partisan agreement appears in reach. We think key issues to watch (and which could become sticking points) are: whether state-only level regulation for stablecoin issuers remains an option; whether and the extent to which nonbank stablecoin issuers would be provided access to the federal safety net, including availability of "deposit" insurance for stablecoins and access to the discount window for stablecoin issuers; whether stablecoin issuers would be provided access to the Federal Reserve's payment system; the extent to which stablecoin issuers may be affiliated with commercial companies; limits on transactions between a stablecoin issuer and its affiliates; and the insolvency regime applicable to stablecoins and their issuers.

• We also continue to watch whether the FSOC will take public-facing steps regarding stablecoin regulation. The PWG recommended that, in the absence of legislation, the FSOC should use its authorities to designate systemically important payment, clearing and settlement activities. If the tone from Capitol Hill remains as productive as it has been to date on this issue, we suspect the FSOC will feel less compelled to take public-facing steps.

• Regarding cryptoassets more broadly, the federal banking agencies said at the end of 2021 that they would address a variety of issues in 2022. We think standards associated with providing custody of cryptoassets may be one of the first issues to be addressed, along with market making and other client facilitation activities.

- The Basel Committee on Banking Supervision ("BCBS") has said that it anticipates issuing a second consultation on the regulatory capital treatment of cryptoasset exposures. We will be watching to see if this consultation reflects meaningful changes from the June 2021 consultation (see our prior analysis here), which "would create material impediments to regulated bank participation in cryptoasset markets" according to a group of trade associations. The substance and tenor of the forthcoming consultation may well be a leading indicator of whether regulators from many jurisdictions can agree to take a balanced approach to bank participation in cryptoasset markets.

- We will be watching to see whether the FRB finalizes its proposed guidelines for evaluating the process and standards it uses to evaluate requests for access to the Federal Reserve's payment system. Perhaps more importantly, we will be watching to see if the Federal Reserve provides payment system access to any special-purpose, uninsured institution, particularly one with a cryptoasset-focused business model. If so, the terms upon which payment system access is granted could indicate how the FRB believes nonbank stablecoin issuers should be treated.

With such a full agenda, the administration, lawmakers and the agencies will need to prioritize and ask themselves, "Whither the Biden administration financial regulatory agenda?". In our minds, it would be a significant (and achievable) accomplishment if we go into the late summer and fall with a clear path to comprehensive stablecoin regulation and some indication of how cryptoassets more broadly will be treated in the banking sector. That accomplishment would set necessary groundwork for future debates about a U.S. CBDC, the future of money and further regulation of cryptoassets. And, correspondingly, policymakers could decide that it would be worth the trade for issues like merger review standards (see a comment letter on the topic we submitted here), prescriptive regulation or guidance regarding climate-related risks (see our overview here) or even Basel III endgame to take a backseat temporarily.