

# Alert

## FDIC Issues Letter on Crypto-Related Activities

April 13, 2022

On April 7, 2022, the Federal Deposit Insurance Corporation (“FDIC”) released a Financial Institution Letter (the “Letter”)<sup>1</sup> in order to address FDIC-supervised institutions (“Covered Entities”) that are intending to engage or are already engaging in crypto-related activities.<sup>2</sup> The Letter requested that any Covered Entities seeking to engage in crypto-related activities notify the FDIC and provide all necessary information to the FDIC that would allow the agency to confer with the Covered Entity regarding related risks.<sup>3</sup> In addition, the FDIC requested prompt notifications from Covered Entities already conducting crypto-related activities.<sup>4</sup> The Letter also encouraged Covered Entities to notify their relevant state regulators, in addition to the FDIC.<sup>5</sup>

### Risks Posed by Crypto-Related Activities

As support for the issuance of the Letter, the FDIC discussed the following safety and soundness, financial stability, and consumer protection risks that crypto-related activities pose.

#### *Safety and Soundness*

According to the Letter, safety and soundness concerns are implicated by the “new, heightened, or unique credit, liquidity, market, pricing, and operational risks” associated with crypto-related activities.<sup>6</sup> Examples included: (i) issues with validating and confirming ownership; (ii) anti-money laundering and countering terrorist financing implications due to “reported instances of crypto assets being used for illicit activities;” (iii) information technology and security risks; (iv) credit risk exposure linked to measuring, among other factors, asset quality and counterparty risk; (v) market risks due to pricing and valuation difficulties; and (vi) liquidity risk exposure given the volatility of crypto assets.<sup>7</sup>

#### *Financial Stability*

The Letter also asserted that crypto-related activities could pose systemic risks to the financial system. Systemic risks could result from the “interconnected nature of certain crypto-related activities” as well

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<sup>1</sup> *FIL-16-2022: Notification and Supervisory Feedback Procedures for FDIC-Supervised Institutions Engaging in Crypto-Related Activities*, FDIC (April 7, 2022) (the “Letter”), available [here](#).

<sup>2</sup> In the context of the Letter, the term “crypto-asset” generally referred to “any digital asset implemented using cryptographic techniques.” *See id.* In addition, the term “crypto-related activities . . . includes acting as crypto-asset custodians; maintaining stablecoin reserves; issuing crypto and other digital assets; acting as market makers or exchange or redemption agents; participating in blockchain-and distributed ledger-based settlement or payment systems, including performing node functions; as well as related activities such as finder activities and lending.” *See id.* However, the Letter also noted that “given the changing nature of this area, other activities may emerge that fall within” the Letter’s scope. *See id.*

<sup>3</sup> *See id.*

<sup>4</sup> *See id.*

<sup>5</sup> *See id.*

<sup>6</sup> *See id.*

<sup>7</sup> *See id.*

as through the structure of crypto assets.<sup>8</sup> The Letter pointed to the risk of “runs” on the financial assets which back crypto assets or crypto-related activities, creating a “self-reinforcing cycle of redemptions and fire sales of financial assets” which could cause market disruptions.<sup>9</sup> The FDIC also highlighted how operational failures involving crypto-related activities or crypto assets could destabilize Covered Entities engaging in crypto-related activities.

### *Consumer Protection*

The FDIC expressed concerns about the risks that crypto-related activities could pose to consumers. In particular, the Letter emphasized that consumer confusion could occur regarding crypto-related services offered by Covered Entities. The FDIC also mentioned that Covered Entities could struggle in effectively applying consumer protection requirements (*e.g.*, laws regarding unfair or deceptive acts or practices) to crypto-related activities.<sup>10</sup>

### **Notifying the FDIC**

The Letter stated that Covered Entities should promptly notify the appropriate FDIC Regional Director prior to conducting, or if already conducting, crypto-related activity. This initial notice should describe the crypto-related activities in detail, along with the Covered Entities proposed timeline for conducting the crypto-related activities. The FDIC will then ask the Covered Entity to provide all information necessary to allow the FDIC to evaluate the safety and soundness, financial stability, and consumer protection risks associated with the crypto-related activity. After its review, the FDIC will provide feedback to the Covered Entity.

### **Legal Implications**

In the Letter, the FDIC also highlighted that crypto-related activities can magnify risk to the Covered Entity, to consumers, and even to the Deposit Insurance Fund. As such, the FDIC expects Covered Entities to have the capacity to “demonstrate their ability to conduct crypto-related activities in a safe and sound manner.”<sup>11</sup>

Schulte Roth & Zabel’s lawyers are available to assist you in addressing any questions you may have regarding these developments. Please contact the Schulte Roth & Zabel lawyer with whom you usually work or any of the following lawyers:

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<sup>8</sup> *See id.*

<sup>9</sup> *See id.*

<sup>10</sup> *See id.*

<sup>11</sup> *See id.*

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