To:	Members of the Committee on Financial Services
From:	Financial Services Committee Majority Staff
Date:	May 15, 2023
Re:	Subcommittee on Digital Assets, Financial Technology, and Inclusion Hearing: "Putting the "Stable" in "Stablecoins:" How Legislation Will Help Stablecoins Achieve Their Promise."

On Thursday, May 18, 2023, at 9:00 a.m. the Committee on Financial Services Subcommittee on Digital Assets, Financial Technology, and Inclusion will hold a hearing titled "Putting the "Stable" in "Stablecoins:" How Legislation Will Help Stablecoins Achieve Their Promise." Testifying at the hearing will be:

- **Fennie Wang**, Founder and CEO, Humanity Cash
- **Matt Homer**, Managing Member, The Department of XYZ and former Executive Deputy Superintendent of Research and Innovation, New York Department of Financial Services (NYDFS)
- **David Portilla**, Partner, Davis Polk & Wardwell LLP
- **Robert Morgan**, CEO, USDF Consortium
- **Delicia Reynolds Hand,** Director, Financial Fairness, Consumer Reports

Evolution of Stablecoins

Stablecoins are a class of digital assets designed to offer price stability by being pegged to another asset's value. The most popular stablecoins are currently pegged to the U.S. dollar. Stablecoins, as the name implies, are intended to be less volatile than other digital assets and sufficiently stable to enable them to be used in a similar manner to currency.

There are different types of stablecoins that are identifiable based on their underlying collateral structures. They include fiat-collateralized stablecoins, crypto-collateralized stablecoins, commodity-collateralized stablecoins, and non-collateralized stablecoins.[1] Fiat-collateralized coins are pegged to a fiat currency, and crypto-collateralized stablecoins are backed by other digital assets. Commodity-backed stablecoins are collateralized using physical assets like metals, oil, or real estate. Non-collateralized stablecoins, or algorithmic stablecoins, use a working, autonomous mechanism to maintain a stable price.[2]

<u>Overview of the Stablecoin Market</u>

Today, there are more than two hundred different types of stablecoins, collectively worth more

---

[1] *See* Cryptopedia Staff, *The Global Stablecoin Ecosystem*, *Cryptopedia* (Mar. 8, 2022) *available at* https://www.gemini.com/cryptopedia/what-are-stablecoins-list-global-ecosystem.
[2] *Id.*

than $130 billion. The most popular stablecoin is Tether (USDT) with a $82.5 billion market capitalization, followed by USD Coin (USDC) with a $30.1 billion market capitalization, and Binance Coin (BUSD) with a $5.7 billion market capitalization.

President's Working Group on Financial Markets, FDIC, and OCC Report on Stablecoins

On November 1, 2021, the President's Working Group on Financial Markets (PWG) - which includes the Chairman of the Board of Governors of the Federal Reserve System, the Chairman of the Securities and Exchange Commission (SEC), and the Chairman of the Commodity Futures Trading Commission (CFTC) - in consultation with the OCC and the FDIC, released a report on stablecoins. The report contained several recommendations, including a proposed federal regulatory framework to address existing and potential risks of stablecoins.[3] The report identified several potential risks, including vulnerability of payment systems, systemic risks to the U.S. financial system, and economic concentration of power. The PWG recommended that Congress act promptly to enact legislation to ensure that payment stablecoins are subject to a federal prudential regulatory framework. Specifically, the PWG recommended that Congress pass a law requiring stablecoins to be issued only by insured depository institutions (IDIs).

Benefits of Stablecoins

As the PWG report notes, "stablecoins are primarily used in the United States to facilitate trading, lending, or borrowing of other digital assets, predominantly on or through digital asset trading platforms."[4] Because stablecoins serve as an on- and off-ramp and provide protection for individuals during market volatility, they allow individuals to enter and exit the digital asset market without the need to convert their assets back to a fiat currency. If issued under a clear regulatory framework, stablecoins could help provide more efficient retail payments. Stablecoins could be a source of healthy competition in the payments sector and help reach a wider range of consumers.[5] Moreover, stablecoins have the potential to improve the sending and receiving of remittances.

State Regulatory Framework

Each state has a different regulatory framework for stablecoins. Generally, states have concluded that stablecoin issuers are engaged in money transmission activities and require issuers to obtain a license submitting to periodic examinations and take certain actions to safeguard consumers.[6] Most state money transmitter statutes were not drafted to address digital asset businesses. The

---

[3] President's Working Group on Financial Markets Releases Report and Recommendations on Stablecoins (Nov. 1, 2021), *available at* https://home.treasury.gov/news/press-releases/jy0454.
[4] *See* President's Working Group on Financial Markets Releases Report and Recommendations on Stablecoins, *supra* note 3.
[5] *Reflections on Stablecoins and Payments Innovations Governor Christopher J. Waller*, Federal Reserve Board of Governors, *available at* https://www.federalreserve.gov/newsevents/speech/waller20211117a.htm.
[6] American Bar Association, *50-state survey of virtual currency regulation* (Oct. 8, 2020), *available at* https://www.americanbar.org/content/dam/aba/administrative/business_law/buslaw/committees/CL620000pub/digital_assets.pdf.

state regulatory framework imposes significant costs on market participants, who must work with each state regulator to satisfy each state's regulatory requirements.[7]

Federal Regulatory Framework

Stablecoins and activities involving stablecoins may fall under the jurisdiction of several regulators depending on the composition of stablecoin reserve assets and the range of activities in which a user engages.[8] Today, the SEC regulates digital assets if deemed a security and the CFTC oversees virtual currencies used in a derivatives contract and enforces against fraud or manipulation involving a virtual currency.[9] Aspects of certain stablecoin related activities may also implicate additional state and federal regulators, including the Board of Governors of the Federal Reserve System, the OCC, the FDIC, and the Financial Crimes Enforcement Network.

Legislation Attached to This Hearing

H.R. ____, To provide for the regulation of payment stablecoins, and for other purposes (Chairman McHenry) – The discussion draft defines payment stablecoins and requires such stablecoins to be issued by an issuer who has been approved by their primary federal regulator or a state regulator. The bill subjects payment stablecoins to standards for reserves, redemption, disclosure, and risk management. The bill also provides clarity for insured depository institutions seeking to provide digital asset-related services.

H.R. ____, To provide requirements for payment stablecoin issuers, research on a digital dollar, and for other purposes (Ranking Member Waters)

The discussion draft provides a legal definition for "payment stablecoins" and requires payment stablecoin issuers to be approved by the Federal Reserve or another Federal banking regulator and, if applicable, their state regulator. Specifically, payment stablecoins may be issued by either a qualified bank subsidiary or a nonbank financial company. Issuers would be subject to standards for reserves, capital, liquidity, redemption, disclosure, risk management, financial crimes compliance, and robust prudential oversight. The draft bill also provides clarity relating to tokenized deposits. The discussion draft includes customer protections related to trading platforms, requires custodial service providers (i.e., "wallets") to maintain segregation of customer assets, and prohibits commingling of customer assets with the assets of the platform or provider. The draft bill includes a two-year moratorium on algorithmic stablecoins.

The draft bill also maintains the separation of banking and commerce, restricting Facebook, Wal-Mart, or other large commercial retailers from issuing their own stablecoins. The discussion draft includes important diversity and inclusion requirements, including with respect to certain data

---

[7] *Id.*

[8] American Bar Association, *Digital and Digitized Assets: Federal and State Jurisdictional Issues* (Dec. 2020), *available at* https://www.americanbar.org/content/dam/aba/administrative/business_law/buslaw/committees/CL620000pub/digital_assets.pdf.

[9] CFTC Commissioner Dawn Stump, *Digital Assets: Clarifying CFTC Regulatory Authority & the Fallacy of the Question, "Is it a Commodity or a Security?"* (Aug. 23, 2021), *available at* https://www.cftc.gov/media/6306/DigitalAssetsAuthorityInfographic_CommStump082321/download.

reporting. The draft bill preserves existing authorities the SEC, CFPB, and other agencies may have that are applicable to these entities and activities. The draft bill also requires the Federal Reserve to conduct a study on a central bank digital currency.