DREHER TOMKIES LLP

ALERT

FOR CLIENTS AND FRIENDS OF DREHER TOMKIES LLP

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MAJOR CENTRAL BANKS SHOW INTEREST IN CENTRAL BANK DIGITAL CURRENCY DEVELOPMENT

On January 21, 2020, the central banks of Canada, the United Kingdom, Japan, European Union, Sweden and Switzerland announced that they were creating a group with the Bank of International Settlements to jointly research central bank digital currencies ("CBDC"). According to a press release issued by the Bank of England, the group will (i) assess CBDC use cases, (ii) assess economic, functional and technical design choices, including cross-border interoperability, and (iii) share knowledge on emerging technologies.

On January 16, 2020, the former chair of the Commodity Futures Trading Commission ("CFTC"), Christopher Giancarlo, announced a partnership with Accenture to create the non-profit "Digital Dollar Project" to advance exploration of a United States CBDC. The press release states that the purpose of the Digital Dollar Project is to encourage research and public discussion on potential advantages of a digital dollar, convene private sector though leaders and actors and propose possible models to support the public sector. The Digital Dollar Project will develop a framework for potential, practical steps that can be taken to establish a dollar CBDC.

In November 2019, the Chairman of the Board of Governors of the Federal Reserve System ("Federal Reserve") wrote a letter in response to U.S. Representative French Hill, regarding the Federal Reserve's views on the development of a CBDC. The letter states that the Federal Reserve is not currently developing a CBDC, but the Federal Reserve is monitoring the developments of the central banks that are actively exploring CBDC options. The letter states that the Federal Reserve believes that many of the challenges that CBDC hope to address do not apply to the U.S. context, including disuse of physical cash, narrow reaching or highly concentrated banking sectors or poorly developed payment infrastructure.

On February 5, 2020, Federal Reserve Governor Lael Brainard stated in a speech that given the dollar's important role, it is essential that the Federal Reserve remain on the frontier of research and policy development regarding CBDC. In her speech, Governor Brainard said that the Federal Reserve must determine whether CBDC would offer important benefits to the United States. Some of the issues that need addressed include whether a new form of digital central bank liability might improve the payment system, taking into account the innovation offered by the private sector and whether adding a new form of central bank liability would reduce operational vulnerabilities from a safety and resilience perspective.

The Federal Reserve may not be focused on developing a CBDC, but in her speech, Governor Brainard noted that the Federal Reserve understands that it is vital to invest in real-time retail payments infrastructure with national reach. She stated that the Federal Reserve is building its first new payments rail in more than 40 years, the FedNow Service, to facilitate end-to-end faster payment services, increase competition and ensure equitable and ubiquitous access to banks of all seizes nationwide.

The rise of interest in CBDC likely arises from the growth of public interest in cryptocurrencies. A CBDC is different from private digital token initiatives (*i.e.*, cryptocurrencies), as a CBDC is issued by a central bank and subject to the control and stability mechanisms of the issuing central bank. To date, the United States does not have an overarching framework for regulatory private cryptocurrencies. The Financial Crimes Enforcement Network ("FinCEN"), Securities and Exchange Commission ("SEC") and the Department of the Treasury have all released guidance on how each agency views certain aspects of cryptocurrency. *See* our prior ALERTS of May 13, 2019 and March 28, 2018.

In December 2019, U.S. Congressman Paul Gosar presented a draft bill titled the Crypto-Currency Act of 2020. The draft bill aims at bringing regulatory clarity to the cryptocurrency industry. The draft bill defines three types of crypto-assets:

- Crypto-commodity: Crypto-commodities are economic goods or services that (i) have full or substantial fungibility, (ii) the markets treat with no regard as to who produced the goods or services and (iii) rest on blockchain or decentralized cryptographic ledger. The draft bill delegates the CFTC as the sole government agency with the authority to regulate crypto-commodities.
- Crypto-currency: Crypto-currencies are representations of United States currency or synthetic derivatives resting on a blockchain or decentralized cryptographic ledger, including (i) such representations or synthetic derivatives that are reserve-backed digital assets that are fully collateralized in a

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correspondent banking account, such as stable coins, and (ii) synthetic derivatives that are determined by decentralized oracles or smart contracts and collateralized by crypto-commodities, other crypto-currencies or crypto-securities. The draft bill delegates the Secretary of the Treasury, acting through the FinCEN, as the sole government agency with the authority to regulate crypto-currencies (other than synthetic stablecoins).

- Crypto-security: Crypto-securities are all debt, equity and derivative instruments that rest on a blockchain or decentralized cryptographic ledger. The draft bill excludes from the definition of crypto-currencies a synthetic derivative that (i) is operated as, and is registered with the Department of the Treasury as, a money services business and (ii) is operated in compliance with all applicable requirements of the Bank Secrecy Act and all other Federal anti-money laundering, anti-terrorism and screening requirements of the Office of Foreign Assets Control and FinCEN. The draft bill delegates the SEC as the sole government agency with the authority to regulate -securities and synthetic stablecoins. The draft bill defines synthetic stablecoins as a digital asset, other than a reserve-backed stablecoin, that (i) is stabilized against the value of a currency or other asset and (ii) rests on a blockchain or decentralized cryptographic ledger.

If enacted, the draft bill will provide regulatory clarity for those financial institutions and persons involved in virtual currency transactions.

As other major central banks research and develop CBDC, there is question as to whether the U.S. dollar could fall behind a state-sponsored stablecoin of another country. As major central banks develop and implement CBDC, a well-defined technology framework will emerge that private digital token initiatives can implement. We will continue to monitor and report on the development of CBDC and regulation of cryptocurrencies. ❑

✧ *Mike Tomkies & Lindsay Valentine*