

Federal Reserve Issues Policy Statement Limiting Crypto-Activities of State Member Banks

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The Board of Governors of the Federal Reserve (the “FRB”) issued a [policy statement](#) that interprets Section 9(13) of the Federal Reserve Act to limit state member banks to engage as principal in only activities that are (a) permissible for a national bank or (b) explicitly permissible for state banks under federal law. The activity restrictions apply equally to insured and uninsured state member banks supervised directly by the FRB.

Although this policy statement applies broadly to all activities of state member banks, the policy statement sets forth specific limitations for crypto-asset activities of state member banks:

1. The FRB holds a presumption against allowing state banks to hold crypto-assets as principal.
2. However, the Board has not yet been presented with facts and circumstances that would warrant rebutting its presumption.
3. That being said, nothing in the policy statement would prohibit a state member bank from serving as custodian for crypto-assets if such activities are conducted in a safe and sound manner and in compliance with consumer, anti-money-laundering, and anti-terrorist-financing laws.

The policy statement provides that the FRB would presumptively prohibit state member banks from holding most crypto-assets as principal. Further, the policy statement provides that any state member bank seeking to issue a “dollar token”, *i.e.* a stablecoin, would need to adhere to all the conditions placed on such activity for a national bank, demonstrate, to the satisfaction of FRB supervisors, that the bank has controls in place to conduct the activity in a safe and sound manner, and to receive a Federal Reserve supervisory non-objection before commencing such activity. The FRB reiterated its position first set forth in a [joint statement](#) from January 3, 2023, that issuing tokens on open, public, and/or decentralized networks, or similar systems is highly likely to be inconsistent with safe and sound banking practices. See “[Joint Statement on Crypto-Asset Risks to Banking Organizations’ Will Significantly Impact Cryptocurrency Companies and Their Banking Relationships](#)” on the K&L Gates Fintech Law Watch.

The policy statement does not prohibit a state member bank from providing safekeeping services in a custodial capacity for crypto-assets if such activity is conducted in a safe and sound manner and in compliance with consumer, anti-money laundering, and anti-terrorist financing laws. However, banks

offering custody services for crypto-assets will face a high bar for appropriate conduct and compliance because, with respect to any novel and unprecedented activities such as providing custody of crypto-assets, the FRB has elevated expectations for systems to monitor and control risks and the FRB will expect banks to be able to demonstrate an effective control environment related to such activities.

Concurrent with the issuance of the policy statement, the FRB also announced the denial of the application by Custodia Bank, to become a member of the Federal Reserve System. The FRB denied Custodia's application on grounds that its crypto-focused business model presented significant safety and soundness risks and that Custodia's risk management framework was insufficient to address concerns regarding the heightened risks associated with its proposed crypto activities, including its ability to mitigate money laundering and terrorism financing risks. The denial of Custodia's application is not unexpected and Custodia has also sued the FRB and Federal Reserve Bank of Kansas City related to its application. [See prior Fintech Law Watch coverage regarding Custodia.](#)

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