



Federal Reserve Board establishes Novel Activities Supervision Program as well as a nonobjection requirement for state member banks engaging with dollar tokens



## Letters clarify supervisory expectations

On August 8, 2023, the Board of Governors of the Federal Reserve System (FRB) issued two Supervision and Regulation letters (SR): (1) SR 23-7 regarding the creation of the Novel Activities Supervision Program and (2) SR 23-8 regarding a supervisory nonobjection process for state member banks wanting to engage in certain activities involving tokens denominated in national currencies.<sup>1</sup> Both letters clarify supervisory expectations and practices for banks under the FRB's remit.

The letters reflect a keen focus on the potential risk exposures facing FRB supervised banking organizations from:

- Partnerships with nonbanks to provide banking services (e.g., Banking as a Service [BaaS]).
- Business models concentrated in supporting digital asset or fintech businesses.
- Applications of distributed ledger technology (DLT).
- Crypto-asset-related activities.
- Dollar token activities (e.g., issuing, holding, transacting).

## Key takeaways

### • The letters align FRB policy with prior moves by other regulators:

1. The creation of the novel activities supervision program mirrors approaches being taken by other regulators—including the Office of the Comptroller of the Currency (OCC), New York State Department of Financial Services (NYDFS), Commodity Futures Trading Commission (CFTC), and Financial Industry Regulatory Authority (FINRA)—that concentrate resources with expertise in emerging technology.
2. The SR 23-8 nonobjection process formally aligns FRB policy for state member banks with the OCC nonobjection requirement for national banks seeking to engage in specified stablecoin or dollar token bank activities.

- **SR 23-7 defines the scope of “novel activities” beyond crypto-assets.** While SR 23-7 reflects continued supervisory concerns regarding the risks presented by crypto-assets, the Novel Activities Supervision Program will also cover banking

organizations in partnerships with nonbanks to provide banking services, with business models concentrated in supporting digital asset or fintech businesses, engaging in crypto-asset-related activities, or—more generally—deploying DLT/blockchain technology.

- **SR 23-7 could make it more difficult for FRB-supervised banking organizations to engage with any application of DLT,** as this “novel activity” will be subject to greater scrutiny.

While reflecting continued supervisory concerns and greater scrutiny of the identified activities, the new supervision program should serve to further augment FRB knowledge of and familiarity with technological and marketplace developments, and the relative risks and benefits they present.

### *SR 23-7: Creation of Novel Activities Supervision Program<sup>2</sup>*

SR 23-7 establishes the Novel Activities Supervision Program (the Program), which concentrates supervision resources with expertise in DLT and other emerging technologies into a single workstream that will complement existing supervisory teams. Per the announcement, the Program will be risk-based and “the level and intensity of supervision will vary based on the level of engagement in novel activities.” The stated goal of the Program is to help ensure innovations improve access to and delivery of financial services, while also safeguarding bank customers, banking organizations, and financial stability.<sup>3</sup>

The Program will focus on the following scenarios:

- Complex, technology-driven partnerships with nonbanks to provide banking services, including “partnerships” with nonbanks using application programming interfaces (APIs) that “provide automated access to the bank’s infrastructure”
- Crypto-asset-related activities, including custody, crypto-collateralized lending, crypto-asset trade facilitation, and stablecoin or dollar token issuance
- Projects that use DLT with the potential for significant impact on the financial system, examples of which include issuance of dollar tokens and tokenization of securities or other assets
- Concentrated provision of banking services (e.g., deposits, payments, lending) to crypto-asset-related entities and fintech companies

The FRB will notify any banking organizations that will be subject to examination through the Program and will “routinely monitor supervised banking organizations that are exploring novel activities.” Supervised entities engaging in novel activities will not be moved to a new or separate supervisory portfolio. Rather, the Program will work alongside the banking organization’s existing supervisors. Stated goals of the Program include enhancing the FRB’s ability to understand novel activities and their manifestation of risk, and enhancing the supervision of risks associated with banks engaging in these activities, while “allow[ing] for innovations that improve access to and delivery of financial services.”<sup>4</sup>

### *SR 23-8: Supervisory Nonobjection Process for State Member Banks Seeking to Engage in Certain Activities Involving Dollar Tokens<sup>5</sup>*

SR 23-8 details the supervisory nonobjection process for state member banks that seek to engage in “activities involving tokens denominated in national currencies and issued using DLT or similar technologies to facilitate payments,” which the FRB refers to as “dollar tokens.” SR 23-8 explicitly aligns FRB policy with 2021 OCC Interpretive Letters 1174 and 1179, which require the OCC to advance nonobjection before a national bank can offer a stablecoin.<sup>6</sup>

A state member bank must notify the FRB of its intention to engage in dollar token activities and obtain a written notification of supervisory nonobjection, before engaging in the activity (including for testing purposes). FRB supervisory staff will seek to understand the bank’s control framework. The bank will then be subject to heightened monitoring under the Novel Activities Supervision Program.

As stated in SR 23-8, a state member bank must demonstrate that it has appropriate risk management practices for the proposed activities. Supervisory staff will focus on risks for dollar tokens as identified in its earlier 2023 Policy Statement, including operational, cyber, liquidity, illicit finance, and consumer compliance risks.<sup>7</sup> This will include risks as they relate to the DLT network.

With respect to novel cryptocurrency activities, the FRB, OCC, and Federal Deposit Insurance Corporation (FDIC) issued earlier this year a joint statement on crypto-asset risks to banking organizations, reinforcing their views on the importance of safeguarding banks and consumers.<sup>8</sup> Additionally, in 2022, the Consumer Financial Protection Bureau published a summary and analysis of consumer complaint data relating to potential consumer harm from such activities.<sup>9</sup> See also our prior point of view on this matter, [“Banking regulators reinforce wall for bank involvement in crypto-assets.”](#)<sup>10</sup>





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# Endnotes

01. Federal Reserve Board of Governors (FRB), "[SR 23-7: Creation of Novel Activities Supervision Program](#)," August 8, 2023; FRB, "[SR 23-8 / CA 23-5: Supervisory Nonobjection Process for State Member Banks Seeking to Engage in Certain Activities Involving Dollar Tokens](#)," August 8, 2023.
02. FRB, "[SR 23-7](#)."
03. With respect to novel cryptocurrency activities, FRB, Office of the Comptroller of the Currency (OCC), and Federal Deposit Insurance Corporation (FDIC) recently issued a joint statement on crypto-asset risks to banking organizations (January 3, 2023), reinforcing their views on the importance of safeguarding banks and consumers. See Deloitte, "[Banking regulators reinforce wall for bank involvement in crypto-assets](#)," 2022.
04. Ibid.
05. FRB, "[SR 23-8](#)."
06. OCC, "[Interpretive Letter 1174: OCC Chief Counsel's Interpretation on National Bank and Federal Savings Association Authority to Use Independent Node Verification Networks and Stablecoins for Payment Activities](#)," January 4, 2021; OCC, "[Interpretive Letter 1179: Chief Counsel's Interpretation Clarifying: \(1\) Authority of a Bank to Engage in Certain Cryptocurrency Activities; and \(2\) Authority of the OCC to Charter a National Trust Bank](#)," November 8, 2021.
07. FRB, FDIC, and OCC, "[Agencies issue joint statement on crypto-asset risks to banking organizations](#)," press release, January 3, 2023.
08. Ibid.
09. Consumer Financial Protection Bureau (CFPB), "[Complaint Bulletin: An analysis of consumer complaints related to crypto-assets](#)," November 10, 2022.
10. Deloitte, "[Banking regulators reinforce wall for bank involvement in crypto-assets](#)."



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