October 19, 2021

The Honorable Janet Yellen
Secretary of the Treasury
1500 Pennsylvania Avenue NW
Washington, DC 20220

Dear Secretary Yellen:

We write to share our alarm regarding recent reporting in the Wall Street Journal indicating that the Treasury Department and President Biden’s Working Group on Financial Markets (PWG) are considering recommending that Congress create special bank charters as the preferred approach to the regulation of stablecoins.¹ For the reasons stated below, we think this approach is dangerous. Instead, we urge Treasury and the PWG to (1) clarify and confirm the authorities that federal regulatory agencies already have to regulate stablecoins, and (2) call on those agencies to act swiftly to exercise their authorities now. Unless federal regulators take prompt and effective action to deal with stablecoins, there is a grave danger that the $120 billion dollar stablecoin market will pose severe operational and systemic threats to our financial system.

Despite widespread claims by the cryptocurrency industry touting the potential for stablecoins to be used as payment instruments for goods and services in the real economy, substantial evidence indicates that stablecoins are not being used to expand financial inclusion or conduct daily transactions in the real economy. Instead, stablecoins are primarily used as a specialized payment mechanism for speculating in various types of cryptocurrencies, including decentralized tokens. As data from DeFi Pulse shows, the growth in stablecoins has closely followed the growth in the open interest of decentralized tokens.² It has also been well documented that the anonymity that stablecoins provide to buyers is integral to the appeal of stablecoins, as their anonymity helps to facilitate evasion of tax laws, terrorist sanctions, and anti-money laundering laws.³

In addition, there is growing evidence that the largest stablecoin company, Tether, which reportedly has issued $69 billion of stablecoins, does not back those stablecoins with 1-to-1 fiat money reserves. A recent enforcement action by the Commodity Futures Trading Commission (CFTC) determined that the lack of 1-to-1 fiat money reserves for Tether stablecoins⁴ could lead holders to lose money when they try to redeem their holdings. Recent reporting by Bloomberg shows that many Tether stablecoins are backed by very risky short-term loans to large Chinese real estate companies.⁵ Worse still, although Tether claims to hold $30 billion of commercial

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paper, many participants in the tightly knit commercial paper market have not seen transactions from Tether, despite the fact that, if its reserve attestations are true, it would be the world’s seventh largest holder of commercial paper. There are also reputational concerns for the Treasury Department should it provide a perception of legitimacy and an avenue for access to the federal banking safety net to a firm like Tether, which is reportedly under investigation by the Department of Justice (DOJ).

Various legal precedents support the view that stablecoins are subject to the federal securities laws and therefore to regulation by the Securities and Exchange Commission (SEC). In SEC v. U.S. Reservation Bank & Trust (USRBT) for example, the courts ruled that deposit-like products offered by USRBT were in fact securities based on a combination of widespread marketing to profit-driven investors and a lack of investor protection such as the guarantee provided by FDIC deposit insurance to depositors in FDIC-insured banks.

Similarly, in the case of the SEC v. Stanford International Bank, where Stanford International Bank was involved in the sale of foreign certificates of deposit (CDs), the district court held that the SEC had authority to regulate those CDs as securities. The court ruled that a combination of features, including the buyers’ profit motives, direct solicitation to investors, and the speculative status of Stanford’s unbacked financial instruments meant that the CDs issued by Stanford were in fact securities.

Current law also provides the DOJ with authority to investigate whether non-regulated financial institutions such as Tether, which offer stablecoins with purportedly “stable” values, are illegally accepting “deposits” under Section 21(a)(2) of 12 U.S.C. 378. This authority should be exercised, not ignored or undermined.

There is no reason to believe that Congress is on a path towards passage of legislation authorizing a new type of bank charter for stablecoin issuers that would include the public protections and accountability – including FDIC deposit insurance and regulation of corporate owners of banks under the Bank Holding Company Act – necessary to protect consumers and ensure the stability of our financial system. Advocates for the financial industry calling on Treasury to defer to Congress are doing so precisely because they want the financial industry to be able to shape its own “regulation-lite” environment and enjoy bank-like powers and privileges without bank-like protections and responsibilities.

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Given the concerns about the risky reserves backing many stablecoins and the serious hazards presented by weak non-bank charters, we urge the Treasury and President’s Working Group against referring the challenges presented by stablecoins to Congress. Instead, we ask the Treasury and the PWG to clarify and confirm how the federal regulators should use their existing authorities and coordinate their efforts to protect investors, the financial system, and the broader economy from the very severe dangers posed by stablecoins.

Furthermore, we urge the Treasury and the PWG to use this opportunity to design a whole-of-government approach to improving our current payment system to be more inclusive and less costly by lowering transaction fees and shortening settlement periods. The fast growth of unregulated stablecoins highlights why implementing FedNOW\textsuperscript{12} and building a central bank digital currency should be top priorities for regulators.

We appreciate your attention to this matter. If you have any follow up questions, please do not hesitate to reach out to Andrew Park (andrew@ourfinancialsecurity.org) and Renita Marcellin (renita@ourfinancialsecurity.org)