



## Applying the BSA/AML Framework to Virtual Currencies and Digital Assets:

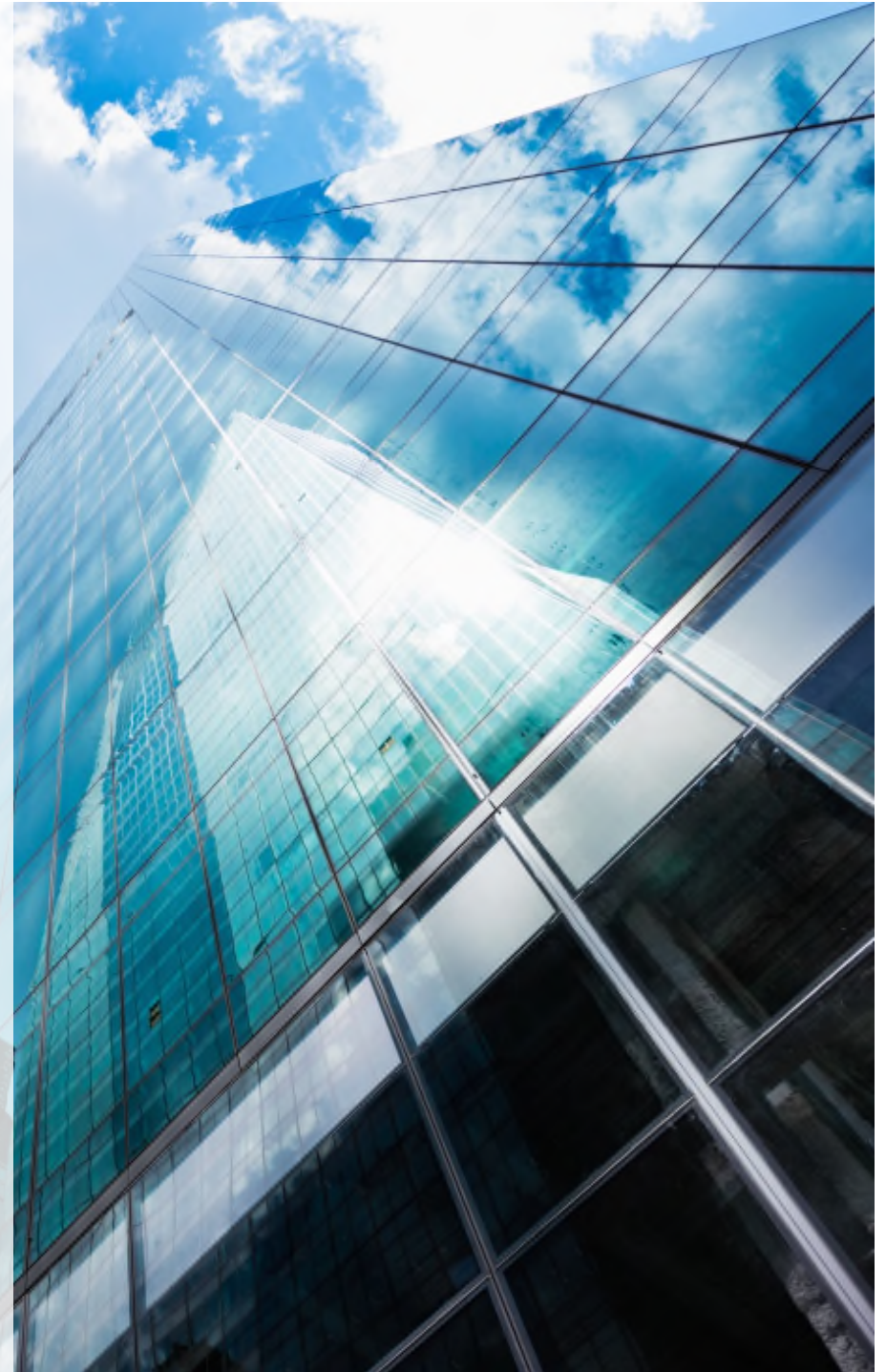
*Summary and Implications of FinCEN's Proposed  
Reporting and Recordkeeping Rule*

Presentation to the Federal Reserve Bank of New York  
Financial Markets Lawyers Group

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# Topics



1. Key Takeaways

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2. Background and Context

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3. Summary; Compliance Requirements

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4. Select Interpretive Issues

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5. Procedural Uncertainty; Current Status

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## Three Key Takeaways

1. FinCEN's **December 2020 proposed rule** imposing compliance, reporting and recordkeeping requirements on banks and money services businesses ("MSBs") engaged in certain transactions involving convertible virtual currency ("CVC") (e.g., Bitcoin, Ethereum) and digital assets with legal tender status ("LDTA") **faces an uncertain future.**
2. Although reportedly a high priority of the former Trump administration, the proposed rule met **significant resistance from the digital asset industry.**
  - Treasury Secretary Janet Yellen has indicated general support, but questions remain about how (and when) the ultimate regulations will be formulated
  - Designee for a key open position remains to be named: Treasury Undersecretary for Terrorism and Financial Intelligence
3. As proposed, the rule would place **stringent requirements on U.S. banks and MSBs** in respect of transactions in CVC and digital assets – **generally beyond those adopted to date in other jurisdictions.**

# Background and Context

- **May 2019:** FinCEN issues guidance on application of the BSA/AML framework to various types of CVC and business models.
- **June 2019:** Financial Action Task Force (“FATF”) issues recommendations on global standards for regulation of transactions in virtual assets or involving virtual asset service providers (“VASPs”), including reporting and recordkeeping requirements.
- **October 2020:** FinCEN and the Federal Reserve issue proposed rule applying existing information and recordkeeping requirements for fund transfers and other transmittals (the so-called “Travel Rule”) to transactions involving CVC and digital assets.
- **December 18, 2020:** FinCEN announces proposed rule applying compliance obligations to banks and MSBs for transactions involving CVC/LTDA to or from “unhosted” and other designated wallets.
- **December 23, 2020:** Initial publication in the Federal Register.
- **January 1, 2021:** Congress enacts sweeping AML legislation with various provisions relating to CVC and digital assets.
- **January 28, 2021:** Extension of comment period to March 29, 2021.



**DEPARTMENT OF THE TREASURY**  
**Financial Crimes Enforcement Network**

**31 CFR Parts 1010, 1020, and 1022**  
**RIN 1506-AB47**

**Requirements for Certain Transactions  
Involving Convertible Virtual Currency  
or Digital Assets**

**AGENCY:** Financial Crimes Enforcement Network (“FinCEN”), Treasury.

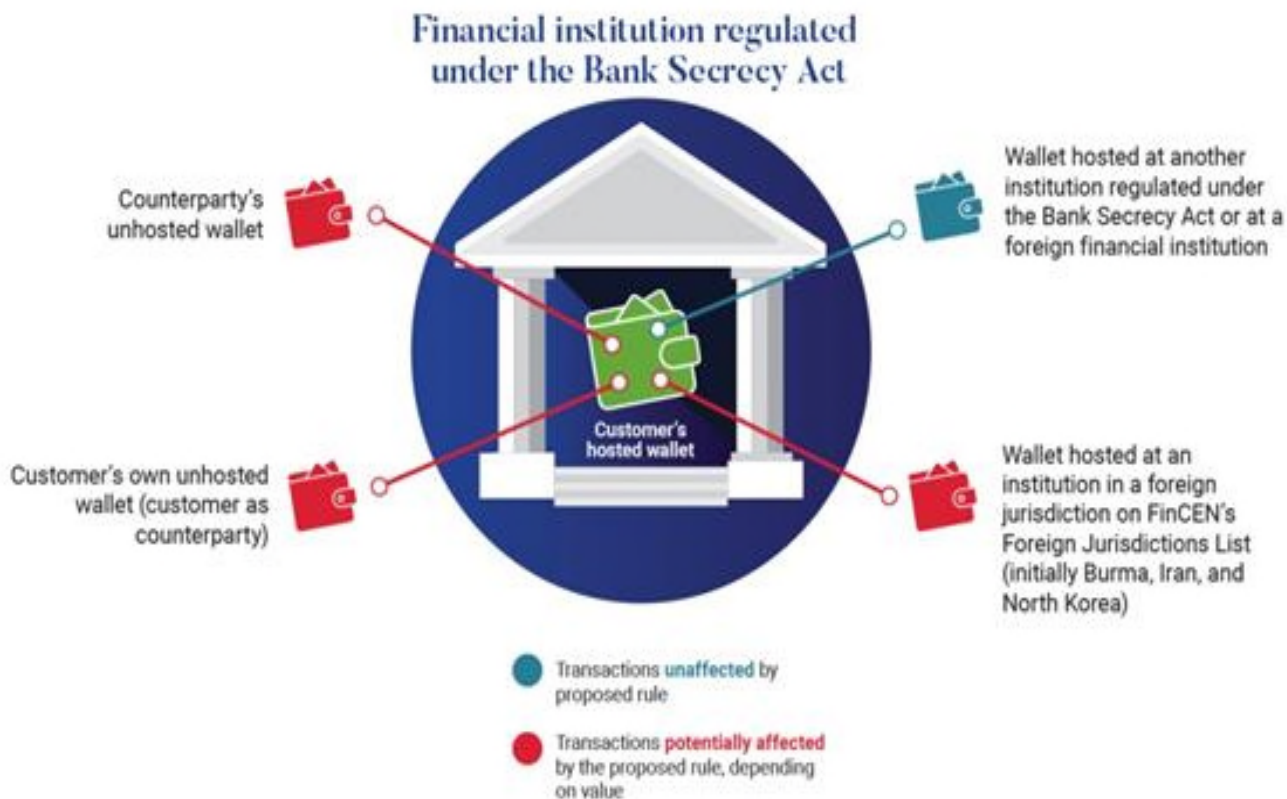
**ACTION:** Notice of proposed rulemaking.

**SUMMARY:** FinCEN is issuing this notice of proposed rulemaking to seek public comments on a proposal to require banks and money service businesses (“MSBs”) to submit reports, keep records, and verify the identity of customers in relation to transactions involving convertible virtual currency

# Summary of Proposed Rule

## Covered FIs and Transactions

|                        |  |
|------------------------|--|
| Financial institutions | <ul style="list-style-type: none"><li>▪ Banks and money service businesses only</li></ul>                  |
| Transactions involving | <ul style="list-style-type: none"><li>▪ “Unhosted wallets”</li><li>▪ “Otherwise covered wallets”</li></ul> |



Source of graphic:  
<https://www.jdsupra.com/legalnews/proposed-rules-for-transactions-with-3375455/>

# Specific Compliance Requirements

| Bank/MSB Obligation under Proposed Rule:                                   | Transactions to or from Unhosted and “Otherwise Covered” Wallets |                                     |
|--|--|-------------------------------------|
|  | Tx > \$3,000   | Tx > \$10,000*                      |
| - Verify customer’s identity   | <input checked="" type="checkbox"/>                              | <input checked="" type="checkbox"/> |
| - Collect, at least, name and physical address of each <u>counterparty</u> | <input checked="" type="checkbox"/>                              | <input checked="" type="checkbox"/> |
| - Retain records on transaction and <u>counterparty</u>                    | <input checked="" type="checkbox"/>                              | <input checked="" type="checkbox"/> |
| - File CTR-like reports  | <input type="checkbox"/>   | <input checked="" type="checkbox"/> |

\* Multiple transactions by or on behalf of any person during a single business day must be aggregated to determine whether >\$10,000 threshold is met.

- **Key term is not defined:** “Unhosted wallet.”
- **Competitive disadvantage for regulated banks and MSBs?**
  - Concern that rule may drive CVC/LTDA transactions into the unregulated peer-to-peer (“P2P”) space or offshore, frustrating the policy objectives and limiting law enforcement value
- **Is compliance possible?** Currently no reliable methods or technology for:
  - Determining whether a customer’s off-exchange wallet is hosted or unhosted
  - Obtaining identifying information from counterparties (*i.e.*, non-customers) given nature of CVC/LTDA instruments
- **Differential treatment of CVC/LTDA relative to transactions in fiat currency and funds transfers.**
  - Requirements for CVC transactions exceeding \$3,000 are comparable to CTR rules for cash transactions exceeding \$10,000
  - Counterparty verification is not required for any other transaction types
  - Exemptions arguably narrower than analogous CTR exemptions

- FinCEN originally took a position that the proposed rule was **not subject to notice-and-comment rulemaking** because it involves a “foreign affairs function” of the federal government and, therefore, exempt from the Administrative Procedure Act (“APA”).
  - Agency nevertheless invited comments
    - » 7,500 comments submitted during original, truncated comment period
  - Unclear whether current Treasury leadership will also assert an APA exemption
    - » January 20, 2021: Biden Administration issued Regulatory Freeze Memo pausing pending rulemakings
    - » January 26, 2021: FinCEN extends comment period to **March 29, 2021** without addressing APA issues
  - Various industry participants, including one of the largest cryptocurrency exchanges, Coinbase, have threatened litigation
- With the status so uncertain, and so many interpretive issues remaining open, some have speculated that FinCEN will re-propose a rule, and that it may differ substantially from the original proposal
  - There has been no official indication that FinCEN is considering this course



# Additional Questions?

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