

Focus on Fintech

Welcome to Wilson Sonsini's *Focus on Fintech* newsletter. This quarterly newsletter provides ongoing analysis and commentary on regulatory developments impacting the fintech industry.

The third quarter of 2022 has been a busy one in the fintech space. In this issue of *Focus on Fintech*, we discuss various regulatory developments related to banking and payments programs, including an update on the anticipated launch of FedNow, regulatory concerns related to “buy now pay later” programs and banking-as-a-service in connection with bank-fintech partnerships, expanded access to the Federal Reserve Bank accounts and services, and the FDIC’s concerns with misleading statements. We also discuss FinCEN’s final regulations on beneficial ownership reporting requirements and their effects, as well as the increased regulatory scrutiny on blockchain and crypto assets by the CFTC, OFAC, the SEC, and the White House. Finally, we wrap up this edition with state-level updates in the digital asset space and an overview of new agency-level departments that have been created to address the unique challenges posed by digital assets.

Regulatory Developments Related to Innovative Banking and Payments Programs

Anticipated Launch of FedNow

The Federal Reserve Board (FRB) [announced](#) that its much-anticipated real-time payments system, FedNow,

will launch between May and July of 2023. FedNow will be open to depository institutions of any size, allowing financial institutions nationwide to provide consumers and businesses with the ability to send and receive instant payments. The FRB hopes that FedNow will enable greater adoption of real-time payments among smaller depository institutions, with the goal of reaching communities nationwide. Notably, in a [recent speech](#), FRB Governor Michelle Bowman acknowledged that the introduction of FedNow may lessen the need for the creation of a central bank digital currency.



institutions to hold money at the Federal Reserve as well as transfer it directly to other account holders. Under the new guidelines, institutions with federal deposit insurance would be subject to a more streamlined level of review, while institutions engaging in novel activities, or activities for which regulators are still developing appropriate regulatory frameworks, such as crypto asset-related activities, would undergo a more extensive review.

Concerns Related to “Buy Now Pay Later” Programs

The Consumer Financial Protection Bureau (CFPB) published a [report](#) on

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Potential Master Account Access for Non-Traditional Financial Institutions

The FRB recently issued its final [Guidelines for Evaluating Account and Services Requests](#), potentially paving the way for state-chartered crypto bank entities and other fintech institutions to access master accounts. Generally, master accounts are only available to banks that are members of the Federal Reserve System and allow member

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the buy now, pay later (BNPL) industry, finding that the BNPL industry has experienced rapid growth from 2019 to 2021. While BNPL products have several benefits, the CFPB found that BNPL firms are not providing the same rights and protections provided by credit card companies. In his [prepared remarks](#) on the release of the report, Director Chopra noted a number of next steps that he has asked the CFPB staff to take. These steps include: (i) identifying interpretive guidance or rules to issue to ensure that BNPL providers adhere to protections consistent with those provided by credit card companies; (ii) identifying data surveillance practices that need to be limited and regulated; (iii) developing options on how consumer reporting agencies can develop appropriate and accurate credit reporting practices; and (iv) ensuring that BNPL providers are subject to supervisory examinations. The BNPL industry can expect increased scrutiny and regulatory oversight.

Misleading Assurances of FDIC Insurance

The Federal Deposit Insurance Company (FDIC) released a [Fact Sheet](#) and an [Advisory](#) to clarify that the FDIC does not insure assets issued by non-

bank entities, including crypto asset companies. The Advisory warns insured banks that partner with non-bank institutions to monitor the non-banks and manage the risk from such third-party relationships.

In addition, following Voyager Digital, LLC's (Voyager's) bankruptcy filing, the FDIC and the FRB issued a [joint letter](#) demanding that Voyager cease and desist from making false and misleading statements regarding its FDIC deposit insurance status and take immediate action to correct any such prior statements. The letter alleged that Voyager had previously made various statements suggesting that Voyager is FDIC-insured and that Voyager customers would receive protection in the form of FDIC insurance coverage. Voyager holds a deposit account at Metropolitan Commercial Bank for the benefit of its customers who make USD deposits; however, customers who invested through Voyager's crypto asset platform do not receive the benefit of FDIC insurance coverage because Voyager is not insured by the FDIC. Following the joint letter, the FDIC sent similar cease-and-desist [letters](#) to five additional crypto asset companies.

In light of this, crypto asset companies should consider whether any marketing statements about FDIC insurance coverage may be misleading to customers, and banks that partner with crypto asset companies should ensure that their non-bank partners are not making misleading statements regarding FDIC insurance to their customers.

Potential Movement Toward Regulating Banking-as-a-Service

In his [remarks](#) at the TCH + BPI Annual Conference, Acting Comptroller of the Currency Michael J. Hsu highlighted the growth of "banking-as-a-service." Among other things, Comptroller Hsu focused on bank-fintech partnerships, which he characterized as a "complex set of arrangements," with financial services being compartmentalized and offered by non-bank entities. Comptroller Hsu stated that the Office of the Comptroller of the Currency (OCC) is working to mitigate the risk by developing a process to "subdivide bank-fintech arrangements into cohorts with similar safety and soundness risk profiles and attributes." Comptroller Hsu also noted that the OCC continues to work with other regulators to avoid regulatory arbitrage.

FinCEN Issues Final Beneficial Ownership Regulations Imposing Federal Filing Requirements

On September 30, 2022, the Treasury's Financial Crimes Enforcement Network (FinCEN) published its final regulations on [Beneficial Ownership Information \(BOI\) Reporting Requirements](#). The regulations impose federal filing requirements on domestic and foreign "reporting companies," which generally include legal entities created or registered via a state (or tribal) filing. Please review our recent alert, "[Final Regulations on Beneficial Ownership Will](#)



[Require 'Tens of Millions' of Legal Entities to File Reports,](#)" to learn more about the new requirements that become effective January 1, 2024.

FinCEN [estimated](#) that "[t]he number of legal entities already in existence in the United States that may need to report information on themselves, their beneficial owners, and their formation or registration agents pursuant to the [Corporate Transparency Act] is in the tens of millions," *plus* more than two million new entities each year.

Increased Regulatory Scrutiny of Blockchain and Crypto Assets



White House Releases Framework for Digital Assets

The White House [released](#) a Fact Sheet on the “Comprehensive Framework for Responsible Development of Digital Assets.” The Framework follows President Biden’s [Executive Order on Ensuring Responsible Development of Digital Assets](#) (Digital Assets Executive Order), issued in March of this year. The Fact Sheet highlights the reports that have been submitted pursuant to the Digital Assets Executive Order and outlines additional steps that the Biden administration plans to take. These steps include: (i) encouraging regulators to aggressively pursue investigations and enforcement actions against unlawful practices; (ii) encouraging the Consumer Financial Protection Bureau and the Federal Trade Commission to monitor consumer complaints of unfair, deceptive, or abusive practices; (iii) encouraging agencies to issue rules and guidance to address risks; and (iv) leading efforts to help the public understand the risks involved with digital assets.

In addition, the Fact Sheet outlines plans to improve payment systems through efforts such as the development of FedNow (discussed above), the creation of a regulatory framework for federal

non-bank payment providers, and the prioritization of improvements to streamline efficiency of cross-border payments systems. The Fact Sheet also discusses ongoing efforts between the Federal Reserve and other government offices to research the benefits and consequences of a U.S. Central Bank Digital Currency (CBDC), which could potentially provide an alternative to currently existing stablecoins and would have increased consumer protections such as increased cybersecurity and safeguards for sensitive data.

Treasury Publishes Three Reports Required by the Digital Assets Executive Order and a Request for Comment

Following up on the Digital Assets Executive Order, [the Treasury published](#) three reports on September 16, 2022: (i) [The Future of Money and Payments](#); (ii) [Implications for Consumers, Investors, and Businesses](#); and (iii) [Action Plan to Address Illicit Financing Risks of Digital Assets](#).

The Future of Money and Payments report discusses the development of a U.S. CBDC and presents four recommendations: “(i) advance work on a possible U.S. CBDC; (ii) encourage use of instant payment systems to support a more competitive, efficient, and inclusive U.S. payment landscape; (iii) establish a federal framework for payments regulation to protect users and the financial system, while supporting responsible innovations in payments; and (iv) prioritize efforts to improve cross-border payments, both to enhance payment system efficiency and protect national security.”

The Implications for Consumers, Investors, and Businesses report discusses various crypto asset and

activity use cases, and the associated risks. This report presents three recommendations: (i) federal regulatory and law enforcement agencies should monitor the crypto asset sector for unlawful activity and pursue investigations and/or enforcement actions to protect consumers, investors, and markets; (ii) continue to use existing authority and regulatory powers to address current and emerging risks; and (iii) the U.S. authorities should work with the Financial Literacy and Education Commission to ensure participants have access to trustworthy information on crypto assets.

The Action Plan to Address Illicit Financing Risks of Digital Assets report addresses the use of virtual assets for money laundering, proliferation financing, and terrorist financing. The report details seven priority actions: (i) monitoring emerging risks; (ii) improving global AML/CFT regulation and enforcement; (iii) updating Bank Secrecy Act (BSA) regulations; (iv) strengthening AML/CFT supervision of virtual asset activities; (v) holding illicit actors accountable; (vi) engaging with the private sector as it relates to existing obligations and illicit financing risks related to digital assets; and (vii) supporting U.S. leadership in financial and payments technology.

On September 20, 2022, the Treasury filed a [Request for Comment](#) (RFC) on the illicit finance and national security risks posed by digital assets in response to the Digital Assets Executive Order. The Treasury’s RFC primarily poses questions, the answers of which are intended to give the Treasury insight into the public’s view on the emerging digital asset risks, and issues or actions the Treasury may take to mitigate those risks. Importantly, the Treasury defines

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“digital asset” and “virtual asset.” The term “digital asset” refers to “all CBDCs, regardless of the technology used, and to other representations of value, financial assets and instruments, or claims that are used to make payments or investments, or to transmit or exchange funds or the equivalent thereof, that are issued or represented in digital form through the use of distributed ledger technology.” The term “virtual asset” refers to “a subset of digital assets that does not include CBDCs or representations of other financial assets, such as digitized representations of existing securities or deposits.” The comment period closes on November 3, 2022.

CFTC Announces First Enforcement Against a “DAO,” Characterizing the DAO as an Unincorporated Association

In the first action of its type against a “Decentralized Autonomous Organization,” or DAO, the Commodity Futures Trading Commission (CFTC) [announced](#) that it settled charges against bZeroX, LLC, the entity responsible for the decentralized finance protocol, bZx, and its founders (Respondents), and simultaneously filed an enforcement action against bZeroX, LLC’s successor DAO, Ooki DAO for illegally offering leveraged and margined retail commodity transactions in crypto assets.

In its complaint, the CFTC claims that crypto assets such as ETH, DAI, and others traded on the bZx protocol are “commodities” under the Commodities Exchange Act. Notably, the complaint characterizes Ooki DAO as an “unincorporated association” whose members (i.e., voting governance token holders) are liable for the DAO’s actions. CFTC Commissioner Summer Mersinger [issued](#) a dissent, disagreeing with the Commission’s approach of determining liability for DAO token holders based on their participation in governance voting. The CFTC served a copy of the complaint

on Ooki DAO through the DAO’s website and through a chatbot. Such service was subsequently [upheld](#) by the U.S. District Court for the Northern District of California.

Based on the CFTC’s complaint, clients both creating DAOs and participating in the governance of DAOs through governance tokens should consider the potential legal ramifications.

SEC Enforcement Developments Related to Crypto Assets

The SEC continues to bring enforcement actions against unregistered offerings of crypto assets. For recent examples, see the [settled proceeding](#) against Bloom Protocol, LLC; the [complaint](#) against Dragonchain Inc.; a [cease-and-desist order](#) against Sparkster Ltd. and its CEO, as well as [charges](#) against crypto influencer Ian Balina for promoting SPRK tokens; and [charges](#) against The Hydrogen Technology Corporation.

In a [speech](#) at the Practicing Law Institute’s SEC Speaks conference and during recent [testimony](#) before the Senate Committee on Banking and Urban Affairs, SEC Chairman Gary Gensler noted that there is a “fair amount of non-compliance” in the crypto asset industry and re-affirmed that most crypto assets are securities. Chairman Gensler also urged market participants to talk to the SEC and highlighted the handful of crypto security token offerings that have registered under the securities laws (Wilson Sonsini was involved in the [first two token offerings under Regulation A](#)).

Notably:

- In its complaint against Ian Balina, the SEC alleged that the transactions took place in the United States because the U.S.-based investors sent their ETH contributions from within the United States and these contributions were validated by a

network of nodes on the Ethereum blockchain, which are clustered more densely in the U.S. than in any other country.

- The Hydrogen complaint alleges that the airdrops were part of the plan of public distribution, offer, and sale of the securities.
- Of the actions listed above, only the charges against The Hydrogen Technology Corporation involved fraud.

Additionally, the SEC brought its first [insider trading action](#) involving crypto assets, charging a former Coinbase product manager, his brother, and his friend. Woven into the complaint was the SEC’s conclusion (and accompanying analysis) that at least nine of the 25 crypto assets involved are securities.

Given the SEC’s stated goal of registration and enforcement of crypto asset securities, we expect to see more enforcement in the coming months.

Senate Democrat Calls for the SEC to Issue Crypto Asset Regulations

In a [letter](#) to SEC Chairman Gary Gensler, U.S. Senator John Hickenlooper (D-Colo.) urged the SEC to issue regulations for crypto asset securities through the standard regulatory process. Senator Hickenlooper is one of the first Democratic senators to criticize the SEC’s approach to crypto assets.

Federal Reserve Board Issues Warnings to Banks Considering Crypto-Related Activities

The FRB issued a [supervisory letter](#) for FRB-supervised banking organizations engaging in crypto asset-related activities. The supervisory letter states that prior to engaging in any crypto asset-related activity, supervised banks must assess the legality of such activities and determine whether any filings are required under applicable federal or

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state laws. Additionally, a supervised bank must “notify its lead supervisory point of contact at the Federal Reserve prior to engaging in any crypto-asset-related activity.” The supervisory letter also emphasizes that supervised organizations should have adequate systems and controls in place to ensure that crypto asset-related activities are conducted in a safe and sound manner. Though the supervisory letter does not directly address the legal permissibility

of specific crypto activities, it signals the FRB’s acknowledgement that supervised organizations are dealing with crypto assets, which may be a step toward regulation and supervision of those activities.

Office of Foreign Assets Control’s First Smart Contracts Sanctions

The Treasury’s Office of Foreign Assets Control (OFAC) issued its [first smart](#)

[contracts sanction](#) and added Tornado Cash (Tornado), a virtual currency mixer, to the Specially Designated Nationals list on August 8, 2022. In its announcement of the sanctions against Tornado, OFAC stated that mixers should generally be considered “high-risk” until they have “appropriate controls in place” to mitigate money laundering concerns.

State Digital Asset Developments

Amendment to the Uniform Commercial Code to Provide Rules for Emerging Technologies Approved by the American Law Institute and Uniform Law Commission

The American Law Institute and Uniform Law Commission have approved the Committee on the Uniform Commercial Code (UCC) and Emerging Technology’s [draft amendments](#) to the UCC (the Amendments). Now that the Amendments have been approved by both bodies, they will go to the state legislatures for adoption. Among other changes, the Amendments introduce a new article, Article 12, which provides rules for transactions involving certain types of digital assets, categorizing them as “controllable electronic records.” Under the Amendments, security interests in certain controllable electronic records may be perfected by filing or obtaining control over such asset (with perfection by control having priority). Additionally, Article 12 allows a good-faith purchaser for value who obtains control of a controllable electronic record to benefit from the “take-free” rule. The scope of Article 12 intentionally excludes certain



digital assets that are already dealt with elsewhere in the UCC. While the amendments make a number of changes, another notable update is the revision of the definition of “money” to carve out cryptocurrencies that are subsequently designated as legal tender by a government. The Amendments create a new definition of “electronic money” and the Amendments provide that electronic money is able to be perfected by control.

Certain states have already adopted interim versions of the Amendments

and are expected to further amend the enacted amendments to adopt the final language. Notably, Wyoming has taken a different path, passing an amendment with broad reach that diverges from the ULC/ALI Amendment. Parties to transactions should be aware of the Amendments and especially whether the state governing their transactions has enacted or plans to enact the Amendments (either in their current form or with changes), and adjust accordingly.

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State Digital Asset Developments *(Continued from page 5)*

Connecticut Department of Banking Issues Advisory on Money Transmission Related to Crypto Assets

On July 20, 2022, the Connecticut Department of Banking issued an [advisory](#) on money transmission related to crypto assets. Connecticut opined that “[money transmission] [l]icensure may be required of persons that engage in virtual currency transactions to the extent they take possession or control of virtual currency belonging to another person, or transmit

or receive virtual currency for another person.” If crypto asset companies take possession or control of crypto assets, or transmit or receive crypto assets on behalf of another person, then they are required to be licensed as money transmitters in Connecticut.

California Governor Vetoes California Digital Financial Assets Law

California Governor Gavin Newsom [vetoed AB-2269](#), a bill that would have established the California Digital

Financial Assets Law, requiring licensure and regulating entities engaged in “digital financial asset business activity.” In his letter to the members of the California State Assembly, Governor Newsom said the bill was premature and that the state needs a more flexible approach. Previously, Governor Newsom issued [Executive Order N-9-22](#), which called on the state to create a regulatory framework for blockchain and crypto asset companies.

New Fintech and Crypto Asset Agency Offices and Departments

CFTC Announces Office of Technology and Innovation

The CFTC [announced](#) a new Office of Technology Innovation. The office, formerly the LabCFTC, will bolster the CFTC’s fintech efforts and will report directly to the Chairman’s office. CFTC Chairman Rostin Behnam noted that he has “asked the staff to be proactive in considering the extent to which [CFTC] authority can be leveraged to bring these novel products into the regulatory fold to ensure important protections for customers and market integrity provided by CFTC regulation[.]”

SEC Announces Addition of Office of Crypto Assets to Division of Corporation Finance’s Disclosure Review Program

The SEC [announced](#) plans to add an Office of Crypto Assets to the Division of Corporation Finance’s Disclosure Review Program. The Office of Crypto Assets will enable the Division of Corporation Finance to focus its resources on the filing review issues unique to crypto assets.

Department of Justice (DOJ) Launches Digital Asset Coordinator Network

The DOJ’s Criminal Division [launched](#) a new Digital Asset Coordinator Network composed of designated federal prosecutors from U.S. Attorneys’ Offices nationwide and the department’s litigating components. The designated prosecutors will “act as their office’s subject-matter expert on digital assets, serving as a first-line source of information and guidance about legal and technical matters related to these technologies.”

Select Publications

The Banker Article

[Stablecoins: the regulatory void left by US authorities](#)

October 27, 2022

Wilson Sonsini Alert

[Final Regulations on Beneficial Ownership Will Require “Tens of Millions” of Legal Entities to File Reports](#)

October 4, 2022

Wilson Sonsini Alert

[SEC-Proposed Amendments Regarding ESG Disclosures: Considerations for Fintech-Oriented Investment Advisers](#)

September 20, 2022

Wilson Sonsini Alert

[Money Services Businesses Penalized for Failure to Adopt Robust Anti-Money Laundering Practices](#)

August 18, 2022

Law360 Article

[Are Securities Laws Appropriate To Protect Crypto Markets?](#)

August 16, 2022

Wilson Sonsini Alert

[UK Financial Services Consumer Regulation Reset: The “Consumer Duty”](#)

August 8, 2022

Bylined Article

[Reading the Not-So-Subtle Tea Leaves: What the SEC is Likely to Do Next in Crypto, and How Crypto Participants Should Prepare](#)

July 26, 2022

Wilson Sonsini Alert

[SEC Charges Former Coinbase Employee with Insider Trading in Crypto Assets – the First SEC Enforcement Action Against a Crypto Exchange Employee](#)

July 22, 2022

Wilson Sonsini Alert

[SEC Proposes Changes to the Definition of “Exchange” under the Securities Exchange Act](#)

July 19, 2022

Wilson Sonsini Alert

[SEC Proposes Changes to the Definitions of “Dealer” and “Government Securities Dealer” Under the Securities Exchange Act](#)

July 19, 2022

Wilson Sonsini Alert

[European Regulatory Overhaul for Crypto Firms on the Horizon](#)

July 18, 2022

Wilson Sonsini Client Advisory

[Headed to the Metaverse? Be “The One” to Minimize Money Laundering Risk](#)

July 14, 2022

Recent Fintech Practice Highlights

Amy Caiazza recognized as a 2022 Cryptocurrency/Blockchain/Fintech Trailblazer

Washington, D.C., partner and Fintech and Financial Services practice group leader [Amy Caiazza](#) was named a [2022 Cryptocurrency/Blockchain/Fintech Trailblazer](#) by *The National Law Journal*. The publication focused on Amy’s early work with her client AngelList, as well as her work with companies building new products using blockchain, artificial intelligence, data scraping, and other tech.

Wilson Sonsini at TechCrunch

On Thursday, November 17, Wilson Sonsini will be hosting a panel on legal issues associated with crypto and Web3 at the TechCrunch Miami conference. The discussion will include topics such as regulatory risk, structuring financings, and protecting IP. Wilson Sonsini panelists include Washington, D.C., Fintech and Financial Services partner and practice group leader [Amy Caiazza](#); Washington, D.C., Fintech and Financial Services partner [Neel Maitra](#); Washington, D.C., Technology Transactions partner [Scott McKinney](#); and Palo Alto Emerging Companies Of Counsel [Jonathan Chan](#).

Wilson Sonsini at FinTech R:Evolution

On Thursday, October 20, London Corporate partner [Josh Kaplan](#) joined a panel titled “Fintech internationalization: lost in translation” at the FinTech R:Evolution conference.

The following attorneys have editorial oversight of Wilson Sonsini's *Focus on Fintech*. They would like to take this opportunity to thank all of the contributors to this edition, including Tanner Long, Eric Quang, and Bridget Grier.



Rob Rosenblum
(202) 973-8808
rosenblum@wsgr.com



Amy Caiazza
(202) 973-8887
acaiazza@wsgr.com



Neel Maitra
(202) 973-8827
nmaitra@wsgr.com



Josh Kaplan
44-20-39634069
jkaplan@wsgr.com



Stephen Heifetz
(202) 973-8802
sheifetz@wsgr.com



Mara Alioto
(415) 947-2185
malioto@wsgr.com



Troy Jenkins
(202) 920-8732
tjenkins@wsgr.com



Chris Hurn
44-20-39634061
churn@wsgr.com

WILSON SONSINI

650 Page Mill Road, Palo Alto, California 94304-1050 | Phone 650-493-9300 | Fax 650-493-6811 | www.wsgr.com

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