

New York Financial Regulator Publishes Stablecoin Guidance

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There have been a number of developments swirling around stablecoins in the past month, including, earlier this week, the recent introduction in the U.S. Senate of a [bill](#) (the “Responsible Financial Innovation Act”) that would put in place a regulatory framework for digital assets and enact certain requirements and consumer protections surrounding stablecoins. The topic of stablecoins’ utility and risk has been in the headlines and on the minds of both legislators and state and federal financial regulators. In a timely move, the New York Department of Financial Services (NYDFS), [released](#) its “[Guidance on the Issuance of U.S. Dollar-Backed Stablecoins](#)” meant to set foundational criteria for USD-backed stablecoins issued by DFS-regulated entities on the issues of redeemability, assets reserves and attestations about such reserves. The NYDFS is the first state regulator to release such guidance. With the fate of Congressional action on stablecoins this year uncertain (and equally uncertain whether federal agencies or banking regulators will step in to offer certain guardrails), it will likely be left to the states (and the industry itself) to establish certain baselines that offer consumer protection and stability without harming innovation. Given NYDFS’s experience in the virtual currency space and its prominence, its latest guidance may be influential to other regulators around the country.

Stablecoins are digital assets designed to maintain a stable value by pegging the digital asset to a national currency or another reference asset (i.e., a commodity like gold or silver). Using reference assets to stabilize price, stablecoins seek to become a less-volatile payment mechanism to bitcoin and other cryptocurrencies, and have also been used to facilitate trading and lending of other digital assets in many decentralized finance (DeFi) transactions. Algorithmic stablecoins, on the other hand, typically use an algorithm or smart contract to manage the supply of tokens and guide their value to a reference asset (e.g., U.S. dollar); such stablecoins generally do not attempt to achieve value by holding fiat reserves that approach a value in a 1:1 relationship with the value of the stablecoin. Proponents note that a well-designed stablecoin can enable faster and more efficient payment options for a host of customers; however, regulators, like the federal Financial Stability Oversight Council, have [previously cautioned that such digital assets present potential systemic risk due to stablecoins' lack of consistent risk-management standards and their operational complexity.](#)

NYDFS is no stranger to regulating the virtual currency industry. In 2015, it released its final [“BitLicense” rules](#), becoming the first state to promulgate a [comprehensive framework for regulating virtual currency-related businesses](#). Since 2018 NYDFS has also imposed requirements and controls on the stablecoins issued by its regulated entities. As noted in the guidance, the agency carefully reviews a company’s product offerings (including any stablecoin-related products) when evaluating a BitLicense application, and going forward, BitLicensees and New York State limited purpose trust companies that engage in virtual currency business activity must obtain DFS’s written approval before introducing a materially new product, service, or activity (including issuance of stablecoins).

Specifically, NYDFS released this guidance to “emphasize certain requirements that will generally apply to stablecoins backed by the U.S. dollar that are issued under DFS oversight.” [For further insight, see an [interview with NYDFS Superintendent Adrienne Harris](#) about the new stablecoin guidance]. The principal issues covered in the guidance are backing and redeemability, assets reserve requirements and attestations concerning the backing of such reserves:

- **Backing and Redeemability:** Under the guidance, a stablecoin must be “fully backed” by a reserve of assets (as opposed to algorithmic stablecoins not fully

backed by fiat reserves), such that the “market value of the Reserve is at least equal to the nominal value of all outstanding units of the stablecoin as of the end of each business day.” It goes on to state that the stablecoin issuer must adopt “clear, conspicuous redemption policies, approved in advance by DFS in writing,” that allow holders a right to redeem stablecoin tokens from the issuer (as opposed to through a third party) “in a timely fashion at par for the U.S. dollar,” less applicable fees. The guidance includes model language for customer terms, including a definition of redemption and what “timely” means under normal and extraordinary circumstances.

- **Reserves:** The guidance requires reserve assets to be segregated from the proprietary tokens of the issuer and held in a chartered institution. It also requires the reserve to consist of only certain types of assets, including cash held in U.S. deposit accounts, U.S. Treasury bills maturing within three months and certain other listed Treasuries. Notably, the guidance does not list commercial paper among allowable reserve holdings.
- **Attestation:** The guidance requires, among other things, that the reserve be subject to an examination of management’s assertions at least monthly by an independent Certified Public Accountant (“CPA”) applying the attestation standards of the American Institute of Certified Public Accountants (“AICPA”), and also submit an annual attestation report to NYDFS.

As a final aside, the guidance states that the above items are not the sole regulatory requirements placed on the issuance of stablecoins and that NYDFS will look to a range of other risks before authorizing a regulated virtual currency entity to issue a stablecoin, including risks related to cybersecurity and network design and AML compliance, among others. Also, NYDFS notes that the guidance does not apply to USD-backed stablecoins listed, but not issued, by DFS-regulated exchanges.

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