

# Lummis-Gillibrand Responsible Financial Innovation Act of 2023

## Section-by-Section Overview

### Title I—Definitions

- **Sec. 101 (Definitions)** One of the most pressing issues in the crypto asset space is the lack of common definitions. This section creates definitions for crypto asset, payment stablecoins, smart contracts, distributed ledger technology and similar important terms.

### Title II—Leading with Consumer Protection

*Key Point: The consumer protection title of Lummis-Gillibrand has nearly doubled since the 2022 version, and includes provisions designed to prevent another FTX, including disclosures, proof of reserves, advertising standards and limits on lending.*

- **Sec. 201 (Sense of Congress)** Provides the sense of Congress on the scope of the existing enforcement powers of the Commodity Futures Trading Commission (CFTC) and Securities and Exchange Commission (SEC).
- **Sec. 202 (Consumer Protection Regulators)** Allocates enforcement authority for new crypto asset consumer protection requirements amongst the CFTC, SEC, banking agencies and a new Customer Protection and Market Integrity Authority.
- **Sec. 203 (Proof of Reserves)** Requires all crypto asset intermediaries to maintain proof of reserves and undergo an annual verification. Gives the Public Company Accounting Oversight Board authority to enforce these provisions.
- **Sec. 204 (Plain Language Customer Agreements)** Specifies that customer agreements must be written in plain language, and that these agreements, and subsequent changes, must be filed in a public database.
- **Sec. 205 (Basic Consumer Protection Standards)** Specifies mandatory notice requirements for customers, specifies allocation of forks and airdrops and requires a mandatory CEO compliance attestation each year regarding compliance.
- **Sec. 206 (Cleaning Up Crypto Asset Lending)** Imposes basic notice and risk management standards for crypto asset lending and bans rehypothecation.
- **Sec. 207 (Settlement Finality)** Requires customer agreements to specify the moment when a transaction is finally settled between an intermediary and a customer as a matter of law.
- **Sec. 208 (Advertising)** Creates advertising standards for crypto asset marketing, including a duty to be fair and balanced, not be misleading and required disclosures, including compensation.
  - Similar to the *Responsible Digital Asset Advertising Act* previously introduced in April 2023 by Senators Lummis and Sinema (S.1357)
- **Sec. 209 (Cybersecurity Standards)** Requires that crypto asset intermediaries report cybersecurity breaches in a timely manner, and requires the

CFTC and SEC, in consultation with other agencies, to develop cybersecurity standards for exchanges, brokers and other intermediaries.

### Title III—Combatting Illicit Finance

*Key Point: Provides focused guidance to Federal agencies to combat use of crypto assets in illicit finance and to support law enforcement.*

- **Sec. 301 (Crypto Asset-Related Violations of the Bank Secrecy Act)** Increases the criminal penalty for a willful violation of the Bank Secrecy Act relating to crypto assets.
- **Sec. 302 (Examination Standards)** Requires the Treasury Department, CFTC and SEC to adopt financial institution examination standards relating to the prevention of money laundering and sanctions evasion.
  - Similar to the *Digital Asset Anti-Money Laundering Act* (S.5267) previously introduced in December 2022 by Senators Warren and Marshall.
- **Sec. 303 (Crypto Asset Kiosks)** Specifies that operators of digital asset kiosks and “ATMs” must maintain accurate addresses with the Financial Crimes Enforcement Network (FinCEN). Requires FinCEN to adopt rules relating to the verification of crypto asset kiosk customer identities.
  - Similar to the *Digital Asset Anti-Money Laundering Act* (S.5267) previously introduced in December 2022 by Senators Warren and Marshall.
- **Sec. 304 (Working Group on Illicit Finance)** Establishes a Financial Technology Working Group composed of the Departments of the Treasury, State, Justice and Homeland Security to make recommendations on illicit finance issues.
  - Similar to the *Financial Technology Protection Act* (S.1340) previously introduced in April 2023 by Senators Budd and Gillibrand.
- **Sec. 305 (Sanctions and Payment Stablecoins)** Requires the Office of Foreign Assets Control to develop guidance articulating the sanctions compliance responsibilities and liabilities of an issuer of payment stablecoins.
- **Sec. 306 (Crypto Asset Mixers and Tumblers)** Requests a report from FinCEN on uses of crypto asset mixers and tumblers and policy recommendations.
- **Sec. 307 (FinCEN Innovation Laboratory)** Establishes an Innovation Laboratory within the Treasury Department’s Financial Crimes Enforcement Network to increase dialogue with the crypto asset and financial technology industry and to enable pilot projects that enhance supervision of financial institutions.

## Title IV—Responsible Commodities Regulation

*Key Point: Would comprehensively prevent the FTX bankruptcy from reoccurring, through strong custody requirements, affiliate supervision, change of control approval, function separation and mandatory registration, alongside managing the risks and opportunities of decentralized finance.*

- **Sec. 401 (Definitions)** Adds “crypto asset” and “crypto asset exchange” to definitions contained in the Commodity Exchange Act.
- **Sec. 402 (Conforming Amendments)** Implements this title.
- **Sec. 403 (CFTC Jurisdiction)** Grants the CFTC spot market jurisdiction over all fungible crypto assets which are not securities in addition to the agency’s current jurisdiction over leveraged transactions. Permits futures commission merchants to conduct crypto asset activities and provides strong custody and customer protection requirements.
- **Sec. 404 (Registration of Crypto Asset Exchanges)** Creates a robust registration framework for crypto asset exchanges to register with the CFTC to conduct trading activities. Establishes core principles, rulemaking, custody, customer protection, prevention of market manipulation, information-sharing and preemption standards. Establishes risk management standards for crypto asset exchanges to conduct trading activities with decentralized crypto asset exchanges and requires the CFTC to authorize change of control applications for exchanges.
- **Sec. 405 (Affiliate Supervision)** Grants the CFTC authority to designate material affiliates of exchanges, and to conduct limited supervision of affiliates.
- **Secs. 406, 407 (Conforming Amendments)** Implements this title.
- **Sec. 408 (Bankruptcy Treatment of Crypto assets)** Creates needed legal clarity for investors, creditors, crypto asset exchanges and other financial institutions about the treatment of crypto assets in bankruptcy.
- **Sec. 409 (Payment Stablecoins)** Provides that a payment stablecoin issued by a depository institution (bank/credit union) is neither a commodity, nor a security.
- **Sec. 410 (Financial Institutions Definition)** Establishes crypto asset exchanges as ‘financial institutions’ under the Bank Secrecy Act.
- **Sec. 411 (CFTC Regulatory Costs)** Permits the CFTC to impose a user fee on crypto asset exchanges to cover increased costs to the agency, under strict conditions.

## Title V—Responsible Securities Regulation

*Key Point: Codifies the existing Howey test, as interpreted by the Federal courts over the last eighty years.*

- **Sec. 501 (Legal Clarity for Commodities and Securities)** Makes a clear distinction between crypto assets that are commodities or securities by examining the rights or powers conveyed to the consumer, giving crypto asset companies the ability to determine what their regulatory obligations will be and giving regulators

the clarity they need to enforce existing commodities and securities laws, bringing crypto assets into the regulatory perimeter from the current vacuum. Lummis-Gillibrand accomplishes this by codifying existing precedents under the *Howey* test that an ancillary asset (defined below) provided to a purchaser under an investment contract is not inherently a security.

- Crypto assets which are not fully decentralized, and which benefit from entrepreneurial and managerial efforts that determine the value of the assets, but do not represent securities because they are not debt or equity or do not create rights to profits, liquidation preferences or other financial interests in a business entity (“ancillary assets”), will be required to furnish disclosures with the SEC twice a year. Ancillary assets in compliance with these disclosure requirements are presumed to be a commodity.
  - Lummis-Gillibrand strengthens our existing laws by requiring tailored disclosures relating to ancillary assets, ensuring consumers have the information they need to make informed financial decisions.
  - This section balances investor protection, the need to provide information to the marketplace and legal certainty for innovators.
  - Establishes a procedure for a court to rebut the presumption that an ancillary asset is a commodity.
- **Sec. 502 (Satisfactory Control Location)** Resolves a long-standing issue with SEC custody requirements. Provides that the requirement to maintain a satisfactory control location under SEC Rules (17 C.F.R. § 240.15c3-3), with respect to a crypto asset that is a security, may be fulfilled by protecting the asset with commercially reasonable cybersecurity practices for a private key.

## Title VI—Customer Protection and Market Integrity Authority

*Key Point: This title is similar to the Responsible Self-Regulation Act previously introduced by Senator Lummis in December 2022.*

- **Sec. 601 (Market Integrity Authority Creation)** Authorizes the SEC and CFTC to charter customer protection and market integrity authorities to supervise crypto asset intermediaries and to enforce the law.
- **Sec. 602 (Registration Procedure)** Establishes a registration procedure for market integrity authorities with the SEC and CFTC, and provides rulemaking standards.
- **Sec. 603 (Supervision of Crypto Asset Intermediaries)** Creates tough supervisory and regulatory standards for crypto asset intermediary operations.

## Title VII – Responsible Payments Regulation

*Key Point: All payment stablecoin issuers are required to become state- or Federally-chartered depository institutions under this title, with mandatory Federal supervision for state issuers.*

- **Sec. 701 (Issuance of Payment Stablecoins)** Lummis-Gillibrand requires all issuers of payment stablecoins to become depository institutions supervised by a federal/state regulator and to: (1) maintain high-quality liquid assets valued at 100% of the face value of all outstanding payment stablecoins; (2) provide public disclosures on the assets backing the stablecoin and their value; and (3) have the ability to redeem all outstanding payment stablecoin at par in legal tender.
- **Sec. 702 (Algorithmic Stablecoin Classification)** Provides that endogenously referenced crypto assets (“algorithmic stablecoins”) are hybrid instruments for the purposes of the Commodity Exchange Act, and that these instruments are prohibited from using the term “stablecoin.”
- **Sec. 703 (Certificate of Authority to Commence Banking)** Alongside the state charter option, provides that the Office of the Comptroller of the Currency may charter a National Bank Association for the exclusive purpose of issuing a payment stablecoin, and establishes permissible activities, tailored capital requirements, community contribution requirements and a recovery and resolution plan.
- **Sec. 704 (Tailored Holding Company Supervision)** Establishes tailored holding company supervision for depository institutions operating under section 701 or a substantially similar State law, which are exclusively engaged in issuing a payment stablecoin or in custodial or trust activities.
- **Sec. 705 (Codifying the Law of Custody)** For the first time, codifies in one place the law of custodial services for financial institutions relating to legal status, balance sheet treatment, segregation and documentation.
- **Sec. 706 (Implementation Rules Relating to Payment Stablecoins)** Ensures that existing stablecoin issuers and new entrants into the market have an adequate opportunity to compete with existing banks and credit unions for the issuance of payment stablecoins.
- **Sec. 707 (Reduction of Risk in Depository Institutions)** Requires the Federal Reserve Board of Governors to study how distributed ledger technology (DLT) may be used to reduce risk in depository institutions, including through reduced settlement/ operational risk and capital requirements.
- **Sec. 708 (Application Review Timelines)** Prohibits the Federal banking agencies from delaying applicability of a requirement under existing law (12 U.S.C. 4807) to render a decision on all applications within 1 year by requiring that additional information be provided to the agency. Clarifies that the existing 1 year requirement is applicable to the Federal Reserve banks.
- **Sec. 709 (Technical and Conforming Amendments)** Implements this title.

## Title VIII—Responsible Taxation of Crypto Assets

*Key Point: Sections 804, 805 and 806 were included in the Treasury Department’s 2023 Green Book Proposal recommending changes to the tax code.*

- **Sec. 801 (De Minimis Exclusion)** Provides a *de minimis* exclusion of up to \$200 per transaction from a taxpayer’s gross income for use of crypto assets for payment for goods and services, under specified conditions.
- **Sec. 802 (Broker Clarification)** Clarifies the definition of ‘broker’ for the purposes of the Infrastructure Investment and Jobs Act’s new reporting requirement on crypto assets, delaying the implementation date to January 1, 2025.
  - Similar to the *Keep Innovation in America Act* (H.R. 1414) previously introduced by Rep. Patrick McHenry in March 2023.
- **Sec. 803 (Sources of Income)** Extends the current safe harbors for securities and commodities trading activity made by non-United States persons who use a United States financial institution to conduct crypto asset trading activities under specified conditions, including that the non-United States person does not have an office in the United States.
- **Sec. 804 (Crypto Asset Lending)** Establishes that crypto asset lending agreements are not generally taxable events, in the same way that securities lending transactions are not today.
- **Sec. 805 (Wash Sales)** Specifies that taxpayers cannot claim a deduction relating to a loss incurred in a crypto asset sale—similar to existing wash provisions for securities.
- **Sec. 806 (Mark to Market)** Requires crypto asset intermediaries to mark their crypto assets to market for accounting purposes at year end.
- **Sec. 807 (Forks, Airdrops and Subsidiary Value)** Provides that the IRS must not recognize crypto assets provided to a taxpayer through a fork or airdrop as gross income until the taxpayer exercises control over the asset.
- **Sec. 808 (Crypto Asset Mining and Staking)** Declares that crypto assets obtained from mining or staking activities do not form part of a taxpayer’s gross income until the disposition of those assets.
- **Sec. 809 (Charitable Contributions)** Provides that a qualified appraisal of crypto assets are not required as a condition of a charitable contribution.

## Title IX – Responsible Interagency Coordination

*Key Point: Promotes a whole-of-government approach to crypto assets and financial innovation.*

- **Sec. 901 (Interpretive Guidance from Federal Financial Regulators)** Requires Federal financial regulators to provide interpretive guidance on a matter within the jurisdiction of the regulator within 6 months of a request.

- **Sec. 902 (State Money Transmission Laws and Crypto assets)** Similar to the approach of the SAFE Mortgage Licensing Act of 2008 (12 U.S.C. 5107), requires state bank supervisors to adopt substantially uniform standards relating to the treatment of crypto assets under money transmission laws within 2 years.
- **Sec. 903 (Federal-State Financial Regulator Information Sharing)** Establishes rules for the privacy and confidentiality of information shared between State and Federal financial regulators.
- **Sec. 904 (Analysis of Energy Consumption in Crypto Asset Markets)** Directs the Energy Information Administration, in consultation with the CFTC and SEC, to conduct a study analyzing topics around energy consumption.
- **Sec. 905 (Analysis of Energy Consumption by Distributed Ledger Technology)** Requires the National Institute of Standards and Technology and the National Academy of the Sciences to conduct an evidence-based study on energy consumption by proof of work and proof of stake technologies and to provide best practices to reduce energy consumption.
- **Sec. 906 (Applications of Distributed Ledger Technology in Energy)** Requires the Energy Department to conduct a study on potential applications for distributed ledger technology in the energy industry.
- **Sec. 907 (Government Employees)** Permits Federal Government employees to own a *de minimis* amount of crypto assets under Federal ethics standards for the purposes of building familiarity with this asset class and technology.
- **Sec. 908 (Advisory Committee on Financial Innovation)** Lummis-Gillibrand establishes an Advisory Committee on Financial Innovation with the goal of studying and reporting to regulators on the evolving crypto asset market so that regulations can be adapted and updated as the industry and regulatory needs change.

## Title X—Equipping Agencies to Protect Consumers and Promote Responsible Financial Innovation

*Key Point: Lummis-Gillibrand provides over \$1.4 billion dollars over five years in new resources to Federal agencies, and is fully paid for.*

- **Sec. 1001 (Executive Office of the President)** Provides a \$25 million appropriation over five years to the Office of Science and Technology Policy and National Economic Council to hire staff specializing in crypto asset, distributed ledger technology, artificial intelligence and other financial technology issues.
- **Sec. 1002 (FinCEN)** Provides a \$150 million appropriation over five years to FinCEN for the purposes of preventing money laundering in the crypto asset space and implementing this Act.
- **Sec. 1003 (CFTC)** Provides a \$500 million appropriation over five years to implement this Act and supervise crypto asset intermediaries, conditioned on the

chartering of at least one Customer Protection and Market Integrity Authority in concert with the SEC..

- **Sec. 1004 (SEC)** Provides a \$500 million appropriation over five years to implement this Act and supervise crypto asset intermediaries. Not permitted to be used for enforcement purposes, and conditioned on the chartering of at least one Customer Protection and Market Integrity Authority in concert with the CFTC. Establishes an Office of Financial Innovation at the SEC.
- **Sec. 1005 (Federal Trade Commission)** Provides \$150 million appropriation over five years to the Federal Trade Commission for conducting consumer education and enforcement relating to crypto assets.
- **Sec. 1006 (Advisory Committee on Financial Innovation)** Provides a \$12.5 million dollar appropriation to fund the operations of the Committee for five years.