

The Responsible Financial Innovation Act – A Bullet Point Summary

June 10, 2022

Key Points:

- On June 7, 2022, Senators Cynthia Lummis (R-WY) and Kirsten Gillibrand (D-NY) released long-awaited legislation addressing the regulatory and tax treatment of digital assets. Their *Responsible Financial Innovation Act* seeks to create a comprehensive regulatory framework for digital assets, and it does so in a crypto-friendly manner, in contrast to a generally crypto-skeptical Administration and regulators.
- This legislation would largely settle the existing dispute between the Securities and Exchange Commission (SEC) and the Commodity Futures Trading Commission (CFTC) over cryptocurrency jurisdiction, with deference being given to the CFTC.
- On the tax front, the bill would require the Internal Revenue Service (IRS) to issue regulations clarifying long-standing issues in the digital asset industry, eliminate capital gains taxes through a *de minimis* exclusion for cryptocurrencies used to buy up to \$200 of goods and services per transaction, and allow crypto miners to defer income taxes on digital assets earned while mining or staking until they dispose of the assets.
- Overall, the bill should be viewed as an opening volley in the debate over crypto's future regulatory landscape. While it has little chance of advancing this late in an election year, it will serve as a marker and jumping off point for negotiations in the next Congress.

The proposed legislation is long and detailed. In an effort to make the salient points accessible to business and finance professionals, we have prepared the following bullet-point summary:

Taxation of Digital Assets (Title II)

- Requires regulations providing for information returns on virtual currency transactions while implementing a *de minimis* rule to exclude gains or losses from cryptocurrency transactions (i.e., under \$200) from gross income calculations, beginning in 2023. (Sec. 201)

Contact Information

If you have any questions
concerning this alert,
please contact:

Brendan M. Dunn

Partner

bdunn@akingump.com

Washington, D.C.

+1 202.887.4230

Zachary M. Rudisill

Partner

zrudisill@akingump.com

Washington, D.C.

+1 202.887.4225

Eric C. Ettore

Policy Advisor

eettore@akingump.com

Washington, D.C.

+1 202.887.4235

Joshua A. Gohlke

Public Policy Specialist

jgohlke@akingump.com

Washington, D.C.

+1 202.416.5183

- Requires brokers to file returns and furnish certain information with respect to transactions involving digital assets that are classified as covered securities, beginning in 2026. (Sec. 202)
- Adds digital asset exchanges to the Internal Revenue Code (IRC) as an item separate from commodities and securities brokers and exchanges. (Sec. 203)
- Defines decentralized autonomous organizations (“DAOs”) using smart contracts to effectuate collective action as business entities that are not disregarded entities. (Sec. 204)
- Requires guidance to be published by the Treasury on: the classification of forks, airdrops and similar subsidiary value as taxable; merchant acceptance of digital assets and the tax treatment of payments and receipts; treatment of digital asset mining and staking, including mining and staking rewards; allowance of charitable contributions of digital assets greater than \$5,000 and which are traded on established financial markets; and characterization of payment stablecoins. (Sec. 206)
- Requires the Comptroller General to conduct a study and publish a report on retirement investing in digital assets, including potential benefits to diversification, appropriate asset allocations, consumer education and financial literacy, risks and potential legal and operational barriers. (Sec. 207)
- Clarifies that income related to digital asset mining or staking activities shall not be included in gross income calculations until the taxable year of disposition of the assets produced. (Sec. 208)

Securities Innovation (Title III)

- Defines “ancillary assets” as intangible, fungible – “digital” – assets offered or sold in connection with the purchase or sale of a security constituting an investment contract, as defined by the SEC’s **Howey Test**, and that do not provide the holder of the asset with debt or equity rights, liquidation rights of the issuer, the right to profits from the issuer, or any other financial interest in the issuing entity. (Sec. 301)
 - Requires issuers of ancillary assets who offer or sell assets with an aggregate value greater than \$5 million in a 180-day period, or whose issued assets are traded publicly at an average daily aggregate value greater than \$5 million in a 180-day period, to file semiannual public disclosures with the SEC that include basic corporate information regarding the issuer and information relating to the issued ancillary assets, including technical details. (Sec. 301)
 - Clarifies that, if the issuer of ancillary assets makes the appropriate disclosures with the SEC, those assets are presumed to be commodities and the issuers will be regulated as such, unless a court issues an order finding that there is not substantial basis for the asset to be a commodity. (Sec. 301)
- Allows issuers of ancillary assets which have become completely decentralized – not connected with the purchase or sale of a security constituting an investment contract – to file a certification with the SEC to cease disclosures; allows the SEC to deny certifications by majority vote if the certification is not supported by substantial evidence, and allows such certifications to be refiled after 180 days. (Sec. 302)
- Requires the SEC to issue guidance, within 180 days of enactment of the legislation, providing that the requirement to designate a satisfactory control

location for a digital asset may be satisfied with commercially reasonable cybersecurity practices to maintain control of sufficient private key material to transfer control of the digital assets. (Sec. 303)

- Mandates that the SEC complete, within 18 months of enactment of the legislation, the multi-year study of the Commission with respect to the modernization of the rules of the Commission relating to customer protection and custody of securities, digital assets and client funds. (Sec. 304)

Commodities Innovation (Title IV)

- Grants the CFTC exclusive jurisdiction over retail digital asset transactions over any agreement, contract or transaction involving a contract of sale of a digital asset – as specified in the *Digital Commodity Exchange Act* ([H.R.7614](#)) – that are not categorized as securities, including ancillary assets. (Sec. 403)
 - Permits future commission merchants to hold customers' money, assets and property in a manner to minimize the customer's risk of loss or unreasonable delay in an effort to synchronize consumer protection requirements, and restricts futures commission merchants from acting as a counterparty in digital asset transactions. (Sec. 403)
- Allows any trading facility that offers or seeks to offer a market in digital assets to become designated as a digital asset exchange and register with the CFTC and to make any digital asset not susceptible to manipulation available for trading. (Sec. 404)
 - Authorizes the CFTC to make, promulgate and enforce additional rules governing margined, leveraged or financed transactions. (Sec. 404)
 - Restricts digital asset exchanges from offering any derivative products for sale; sets rules for compliance which will be regulated by a digital asset exchange, including terms and conditions of the trades traded or processed through the exchange. (Sec. 404)
 - Promotes core principles in information-sharing and preemption standards; Requires that digital asset exchanges maintain records of all activities relating to the business for a period of five years and report to the CFTC. (Sec. 404)
- Provides that a payment stablecoin issued by a depository institution, a bank or credit union, is neither a commodity nor a security. (Sec. 408)

Consumer Protection (Title V)

- Requires that issuers of digital asset services ensure that the scope of permissible transactions is clearly disclosed in a customer agreement, as well as source code changes to digital assets prior to implementation of updates, information on the segregation of digital assets, how customer assets would be treated during bankruptcy or insolvency and applicable fees. (Sec. 501)
- Directs digital asset service providers and customers, at the initiation of a contractual relationship, to agree on the source code version used for each digital asset and treatment of each asset under the law, including securities and commodities laws applicable to transactions. (Sec. 502)
- Requires digital asset service providers and customers to agree on the terms of settlement finality for all transactions, including the conditions under which digital

assets may be deemed fully transferred, the exact moment of transfer, and the discharge of any obligations upon transfer of a digital asset. (Sec. 503)

- Clarifies that individuals are under no obligation to use an intermediary for the safekeeping of digital assets that are legally owned or possessed and controlled. (Sec. 505)

Payments Innovation (Title VI)

- Mandates that all issuers of payment stablecoins maintain high-quality liquid assets equaling 100 percent of the face value of all liabilities of the issuer on issued stablecoins, including insured depository institutions. (Sec. 601)
 - Clarifies that high-quality liquid assets include United States currency, demand deposits at a depository institution, balances held at a Federal Reserve Bank, foreign withdrawable reserves, securities or related reserve repurchase agreements issued by or with unconditionally guaranteed payment by the Department of the Treasury with an original maturity of one year or less, or other high-quality liquid assets determined to be consistent with safe and sound banking practices by an appropriate Federal banking agency or State bank supervisor. (Sec. 601)
 - Requires monthly disclosures by stablecoin issuers describing the assets backing their issued stablecoins, the value of these assets and the number of outstanding payment stablecoins; Requires that stablecoin issuers obtain permission from appropriate Federal agencies or State supervisors prior to issuance of stablecoins and include a tailored recovery and resolution plan; Requires that stablecoin issuers redeem outstanding payment stablecoins with legal currency upon a customer's demand. (Sec. 601)
 - Requires that Federal banking agencies adopt rules to implement the requirements in this section. (Sec. 601)
- Directs that the Treasury, within 120 days of enactment of the legislation, adopt final guidance clarifying sanctions compliance responsibilities and liability of a payment stablecoin issuer with respect to downstream transactions using issued stablecoins. (Sec. 602)
- Requires that, within 60 days of enactment of the legislation, the Office of Management and Budget, in consultation with the Administrator of General Services, the Director of the Cybersecurity and Infrastructure Security Agency, the Director of National Intelligence and the Secretary of Defense, develop standards and guidelines for executive agencies which require adequate security measures for use of the Chinese digital yuan on government information technology devices. (Sec. 603)
- Obligates the person or entity with a controlling interest in a payment stablecoin issuer submit annual audited financial statements and provide a description of all affiliated or parent entities; Prohibits commercial firms from holding a controlling interest in a payment stablecoin issuer. (Sec. 605)
- Establishes an Innovation Laboratory at the Financial Crimes Enforcement Network (FinCEN) to promote regulatory dialogue, data sharing between FinCEN and financial companies, and an assessment of potential changes in law, rules or policies to facilitate appropriate supervision of financial technology. (Sec. 607)

Banking Innovation (Title VII)

- Requires the Federal Reserve, within 180 days of the enactment of the legislation, to complete a study on the manner in which distributed ledger technology may reduce risk for depository institution and submit a report to all relevant Congressional Committees. (Sec. 701)
- Recognizes that final settlement of transactions reduces risk in the financial system and that digital assets settle with finality in seconds or minutes in contrast with traditional financial transactions. (Sec. 702)
 - Recognizes that it is appropriate for Congress to reaffirm its existing statutory intent to ensure that all depository institutions may access services under the Federal Reserve Act “on an equitable basis, and to do so in an atmosphere of competitive fairness.” (Sec. 702)
- Requires the Federal Reserve, within two years of enactment of the legislation, to assume responsibility for issuing routing transit numbers to depository institutions for all purposes relating to the clearing of transactions. (Sec. 703)
- Directs the Federal Financial Institutions Examination Council, within 18 months of the enactment of the legislation and in coordination with FinCEN, to publish final guidance and examiner handbooks for depository institutions on anti-money laundering, customer identification, beneficial ownership, sanctions compliance, custody, fiduciary and capital markets activities, information technology standards, payment system risk and consumer protection relating to digital assets. (Sec. 705)
 - Requires the SEC and CFTC, within 18 months of the enactment of the legislation and in coordination with FinCEN, to publish final guidance and examiner handbooks on digital asset intermediaries regarding the same topics. (Sec. 705)

Interagency Coordination (Title VIII)

- Requires, within 180 days, Federal financial regulators to provide individualized interpretive guidance with respect to application of a statute, rule or policy under the financial regulators’ jurisdiction. (Sec. 801)
- Permits a financial company operating in an existing state financial technology sandbox to do business across state lines upon approval of the appropriate State and Federal regulator, under strict consumer protection and activities restrictions. (Sec. 802)
 - Requires State and Federal financial regulators to jointly issue a decision for applications from financial companies to do business across state lines. (Sec. 802)
 - Allows State regulators to opt out of consumer education and financial literacy requirements. (Sec. 802)
- Directs the States, through the Conference of State Bank Supervisors and the Money Transmission Regulators Association, to ensure uniform treatment of digital assets under state money transmission laws within two years after the enactment of this Act. (Sec. 803)

- If compliance is not met by a State, the Consumer Financial Protection Bureau shall adopt rules applicable to that State to assure it achieves uniform standards across all states. (Sec. 803)
- Establishes rules for privacy and confidentiality for information shared between State and Federal financial regulators. (Sec. 804)
- Requires the Secretary of Treasury, within one year of enactment of this Act and in consultation with the CFTC and SEC, to analyze the market position of decentralized finance technologies with respect to digital assets and submit the study to relevant congressional committees. (Sec. 805)
- Directs the Federal Energy Regulatory Commission (FERC) to analyze energy consumption for mining and staking of digital transactions each year. Subsequently requires that FERC analyze the effect of consumption on energy prices, baseload power levels, and how renewable energy sources could provide potential benefits to the process. (Sec. 806)
- Authorizes the CFTC and SEC, in consultation with digital asset intermediaries and the digital asset industry, to conduct a study on self-regulation in the digital asset markets and to develop a proposal for the establishment registered digital asset associations. (Sec. 807)
- Requires the CFTC and SEC, in consultation with the Secretary of the Treasury, to develop comprehensive, principles-based guidance relation to cybersecurity for digital asset intermediaries around topics such as internal governance, security operations, risk identification and mitigation, assurance and testing. (Sec. 808)
- Establishes an Advisory Committee on Financial Innovation with the distinct goals of studying and reporting to regulators on the evolving digital asset market so that regulations can be updated and adapted as the industry and regulatory needs change. (Sec. 809)
 - The Committee is to be composed of members in the financial technology industry; experts in consumer protection, financial literacy and inclusion; a Federal Reserve Board member, a state regulator and commissioners of the CFTC and SEC. (Sec. 809)

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