



President Biden's EO: Its meaning and next steps

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Link to the Executive Order:

<https://www.whitehouse.gov/briefing-room/presidential-actions/2022/03/09/executive-order-on-ensuring-responsible-development-of-digital-assets/>



President Biden's EO: Its meaning and next steps (1/3)

Over the past few years, the convergence of traditional, centralized finance (CeFi) with digital assets and decentralized finance (DeFi) has increasingly become evident. While the innovations underlying Bitcoin, digital assets and DeFi have been around for well over a decade, its real-life applications and their penetration into the financial services sector have grown exponentially over the past few years. As of today, USD 300 B¹ of digital assets traded on a daily basis over 300 crypto exchanges globally.¹ 9 countries have launched their CBDC², and 15 are in the Pilot stage, and many more are in the development or research stage.²

We talk about convergence because in fact, traditional players of the financial services sectors are increasingly investigating, experimenting and even delving into digital assets, offering services that were previously only available through non-traditional players. Whereas, the crypto ecosystem is increasingly seeking to work with regulatory bodies to help define the regulatory framework and diversify into non-crypto product offering.

On March 9th, 2022, the White House issued the Executive Order (EO) on Ensuring Responsible Development of Digital Assets. The content of the 13 pages EO, unsurprisingly overall well received by the crypto industry, reinforces the importance of striking a balance between innovation and regulation. To achieve its purpose of greater financial inclusion, to be a sustainable innovation, in all its meanings, and to act as a trusted alternative to complement existing infrastructures and services, digital assets and their underlying and complementary infrastructures must combine with the adequate level of governance. The EO acknowledges that the path towards mainstream adoption of digital assets requires a clear regulatory framework, and it sets out a timeline to do just that.

However, the importance of the EO and associated Presidential actions also lies in its acknowledgement that digital assets are intrinsically financial innovations, innovations that are already part of the economy, not something in the distant future. And the adequate answer to innovation is not simply to ban it, nor to blindly accept it. Rather, it lies, at least from a governmental standpoint, in ensuring that the technological blinspots or weak points are mitigated through adequate regulation, strong governance models, transparency and information sharing. Moreover, the EO further shows that the knowledge gap is closing, recognizing that the crypto industry has moved beyond the discovery phase. The administration understands what are digital assets, the infrastructure construct and their potential use cases; at least partially.

The following two pages of this document summarize some of the potential implications for the different players of the digital asset ecosystem we might anticipate.

Figure 1 summarizes briefly the six (6) key policy objectives of the US with respect to digital assets, comprised of: a) Consumer and Investor Protection; b) Financial Stability and Systemic Risk Mitigation; c) Illicit Finance and National Security Risks; d) US Leadership in the Global Financial System; e) Financial Inclusion; and f) Responsible Innovation.

Figure 2 summarizes key dates and milestones for the Policy and Actions outlined in the EO.

Table 1 presents the key elements of the various reports as outlined in the EO.

Sources: 1. CoinMarketCap (2022); 2. Atlantic Council map (2022); Executive Order (2022)

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Below we summarize some of the potential implications for the different players of the digital asset ecosystem we might anticipate:

1. **Digital assets issuers:** Digital Asset issuers include broadly miners and firms that issue tokens or coins. Although some have already begun the journey, they will likely need to evolve their business model towards a more sustainable one - notably the environmental - such that they mitigate their carbon footprint to a level deemed appropriate. With the emphasis of the EO on protection, notably that of consumers, there will likely be expectations around ensuring digital asset issuers set up the appropriate security features along with a governance structure that minimizes the likelihood of security breaches and downtime, but also the impact in case of such events.
2. **Crypto exchanges:** Crypto exchanges will likely need to ensure their KYC/AML process, and governance and policies in place for the monitoring of illicit activities are adequate and compliant with the standards that will be set by the US's strategy. As consumer protection is emphasized, exchanges could well be responsible for providing sufficient information on the assets and their risks, but also on the different types of wallets and their associated risks, given the central role they play in the ecosystem. Similarly exchanges that facilitate connection with a DeFi platform are likely to have to inform their user base of the associated risks, if they are not already doing so. It is important to note that a public discussion is still underway on how to regulate digital asset custody in Australia where industry experts are being asked to answer questions and provide feedback on Crypto asset secondary service providers: Licensing and custody requirements.
3. **Custodians:** Crypto exchanges may likely need to offer non-custodial wallets to their customers with the option to store their assets in these wallets. Exchanges may be required to custody their assets with a third-party independent Qualified custodian. These hypothesized measures lower the security breach risk of assets held in an exchange. As users are made more aware of the risks of holding assets in a crypto exchange, they may prefer to hold their assets with a custodian or self-custody their assets. Increased competition between existing custodians to obtain a qualified status may be observed.
4. **Wallet providers:** We can see a case for wallet providers that are independent to play a role in limiting the risks for the consumers. Standards could be established to provide adequate information on the different types of wallets and associated level of security and ensure that wallets are either intuitive or come with the right level of instructions and support to minimize the risk of potential loss of digital assets.
5. **CBDC solution providers:** There will be a need to study the potential benefits and risks of Central Bank Digital Currency (CBDC). It will be important to evaluate the potential relationship between a CBDC and private-sector administrated digital assets, but also its implication on the current financial system and democracy. The EO called for a full report on CBDC issuance within the next 180 days, but clearly the research and development efforts on CBDC are of the highest urgency for the U.S. Government. It is important to note that a public discussion is still underway where industry experts are being asked to answer questions and provide feedback on CBDC pro's and con's.

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More generally, the outcome of the EO is expected to be greater regulation, but also clarity of the regulation for the industry. This clarity and the requirements stemming from the various regulations that will result from this concerted effort are likely to lead to increased competition, notably from traditional financial services players, and increased if not mainstream adoption by consumers and enterprises; that is, if regulation is set to ensure people have the tools to make informed decisions about digital assets, wallets, etc.

The efforts for greater harmonization of the regulation globally will also be key to financial stability and the more generalized trust in digital assets and the value they embody. Since geolocalisation on a blockchain is not currently available, will this result in the creation of a blacklist of countries where global players would be expected not to offer their platform for trading digital assets? We are too early to say, but next year will be packed with actions and proposals that will greatly influence the future of crypto.

Figure 1. High level summary of the EO principal objectives

a. Consumer and Investor Protection

Sufficient and adequate safeguards ought to be in place, while promoting responsible development of digital assets. Customers and investors should be able to make informed decisions, informed of key risks and potential impacts. Businesses should have the necessary infrastructure, controls, and governance structure to maintain privacy and protect against arbitrary or unlawful surveillance.

b. Financial Stability and Systemic Risk Mitigation

Current regulations, supervision and regulatory approach must evolve to reflect the economic and financial risks relevant to digital assets, reflecting the new and unique uses and functions of digital assets.

c. Illicit Finance and National Security Risks

The use of digital assets to circumvent US and foreign financial sanctions regimes and other tools and authorities may pose significant illicit finance risk, such as money laundering, cybercrime and ransomware, narcotics and human trafficking, and terrorism and proliferation financing, and as such pose national security risks. The US must ensure cybersecurity and AML/CFT regulation, oversight, law enforcement action or other authorities are adequate and sufficient to mitigate these risks in a global context.

d. US Leadership in the Global Financial System

It is in the US' economic interest to be at the forefront of responsible development of payment innovations and digital assets, including in setting the standards that promote: democratic values, the rule of law, privacy, the protection of consumers, investors, and businesses, and interoperability with digital platforms, legacy architecture, and international payment systems.

e. Financial Inclusion

Given that an estimated 22% of Americans are either unbanked or underbanked, the US has a strong interest in promoting access to safe and affordable financial services equitably, for all Americans, through responsible financial innovation.

f. Responsible Innovation and Climate Risk

It is in the US's interest to ensure that the digital asset ecosystem and technologies are developed, designed and implemented with privacy and security in their architecture, integration of features and controls defending against illicit exploitation, and that reduces negative climate impacts and environmental pollution.



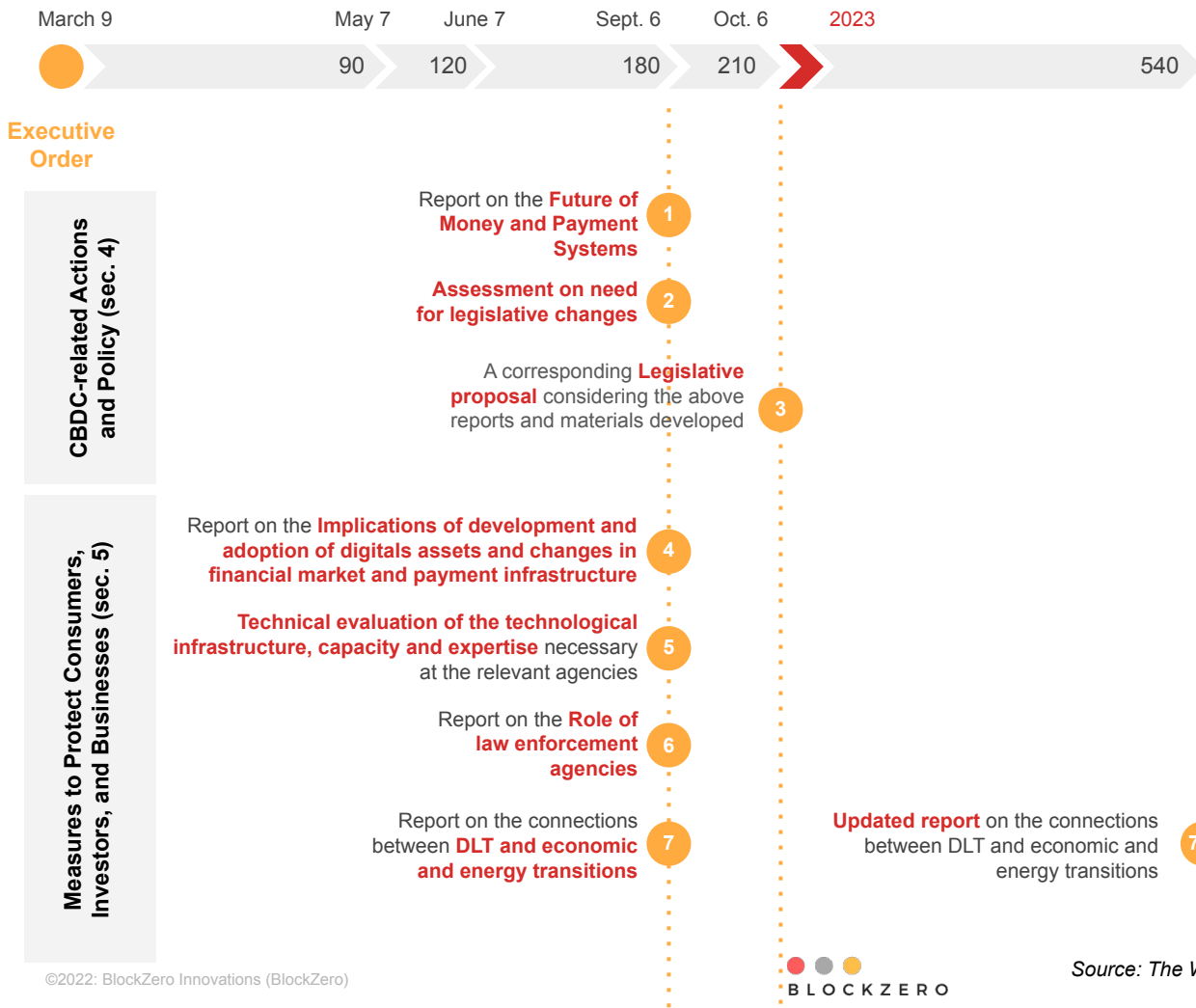


Figure 2. Mapping of the various reports and actions presented in the EO





Actions to Promote Fin. Stability, Mitigate Syst. Risk, and Strengthen Market Integrity (sec. 6)

Report outlining **Recommendations to address financial stability risks and regulatory gaps**

8

Supplemental annexes to the Strategy offering additional views on illicit finance risks posed by digital assets.

9

(90 days)*

Coordinated Action plan based on the Strategy's conclusions for mitigating digital illicit finance and national security risks.

10

(120 days)*

Update on rulemakings to address digital asset illicit finance risks. Consultation with relevant agencies, evaluation opportunities to mitigate these risks through regulation

11

(120 days)**

Figure 2. Mapping of the various reports and actions presented in the EO (cont'd)

* # Days relative to date of submission to the Congress of the National Strategy for Combating Terrorist and Other Illicit Finance (not specified)

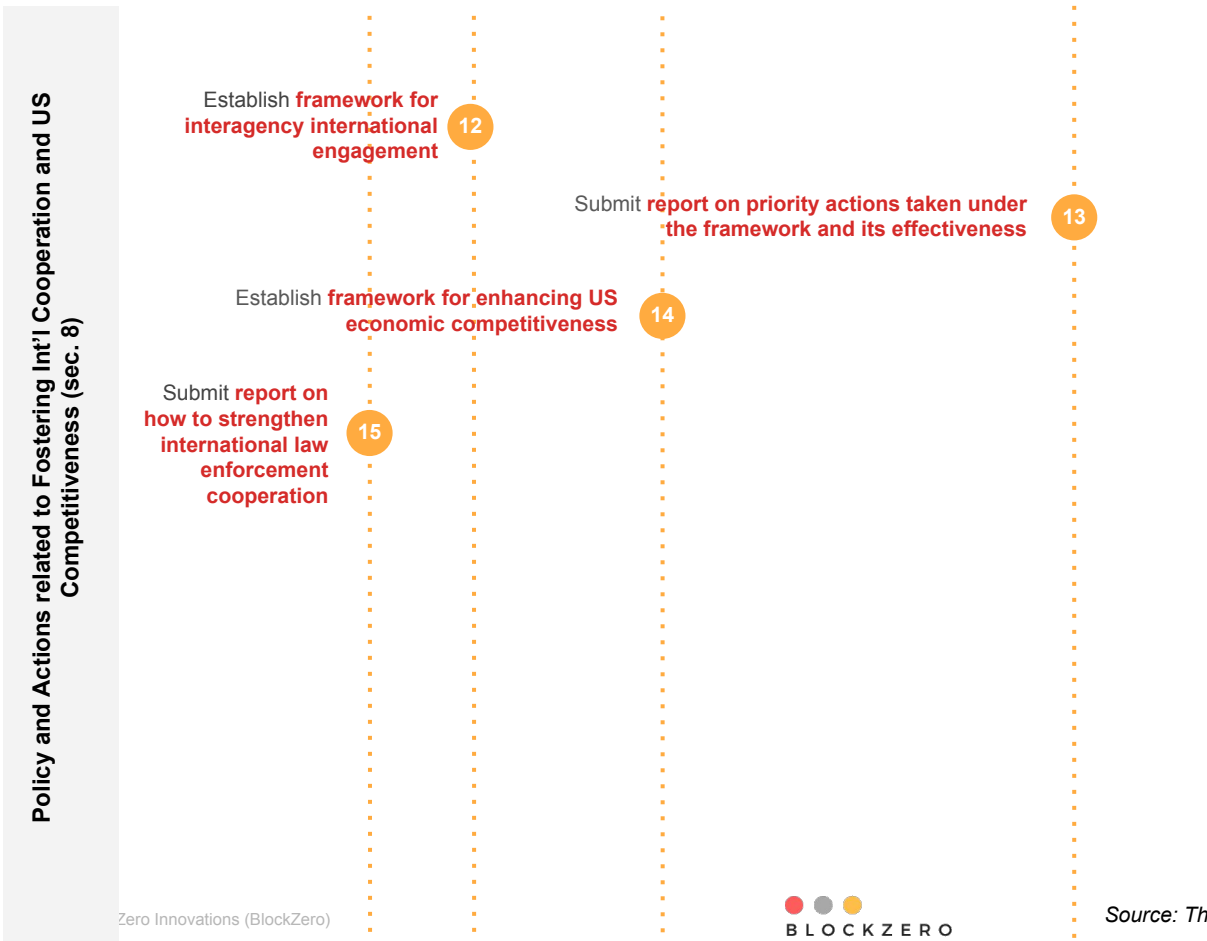
** # Days following completion of the assessments on the three key risks: Money laundering, national terrorist financing, and national proliferation financing; and the updated National Strategy

Actions to Limit Illicit Finance and Associated National Security Risks (sec. 7)





Figure 2. Mapping of the various reports and actions presented in the EO (cont'd)



Zero Innovations (BlockZero)



Source: *The White House Briefing Room, Executive Order (2022)*



Table 1. Summary of the identified reports presented in the EO

CBDC-related Actions and Policy (sec. 4)

- 1 Report on the **Future of Money and Payment Systems****
The Secretary of the Treasury (in Consultation with other identified parties) to submit a report on the future of money and payment systems, incl. the conditions that drive broad adoption of digital assets; the extent to which technological innovation may influence these outcomes; and the implications for the US financial system, the modernization of and changes to payment systems, economic growth, financial inclusion and national security.
- 2 Assessment on need for legislative changes**
The Attorney General (in consultation with Secretary of the Treasury and Chairman of the Federal Reserve) to submit through the APNSA and APEP an assessment of whether legislative changes would be necessary to issue a US CBDC.
- 3 A corresponding Legislative proposal**
The Attorney General (in consultation with Secretary of the Treasury and Chairman of the Federal Reserve) to provide through the APNSA and APEP a corresponding legislative proposal considering previous report by Secretary of Treasury and any other materials developed by the Chairman of the Federal Reserve.

Measures to Protect Consumers, Investors, and Businesses (sec.5)

- 4 Report on the **Implications of development and adoption of digital assets and changes in financial market and payment infrastructure****
Secretary of the Treasury (in Consultation with other identified parties) to submit a report or section of report on implications of developments and adoption of digital assets and changes in financial market and payment system infrastructures for US consumers, investors, businesses, and for equitable economic growth; address conditions that would drive mass adoption, risks and opportunities of such growth for US, incl. Focus on how technological innovation may impact these efforts, with an eye toward those most vulnerable to disparate impacts; incl. Recommendations, incl. Potential regulatory and legislative actions, and support expanding access to safe and affordable financial services.
- 5 Technical evaluation of the **technological infrastructure, capacity and expertise necessary** at the relevant agencies**
The Director of Office of Science and Technology Policy and Chief Technology Officer of the US (in consultation with other identified parties) to submit technical evaluation of the technological infrastructure, capacity and expertise that would be necessary at relevant agencies to facilitate and support the introduction of a CBDC should one be proposed; evaluate technical risks of the various designs, incl. quantum computing; any reflections or recommendations on how the inclusion of digital assets in Federal processes may affect the work of the US Government and the provision of Government services, incl. risks and benefits to cybersecurity, customer experience and social safety net programs.
- 6 Report on the Role of law enforcement agencies**
The Attorney General (in consultation with other identified parties) to submit a report on the role of law enforcement agencies in detecting, investigating and prosecuting criminal activity related to Digital Assets, and include recommendations on regulatory or legislative actions.



Table 1. Summary of the identified reports presented in the EO (cont'd)

**Measures to Protect
(sec.5) - cont.'d**

- 7** Report on the connections between **DLT and economic and energy transitions**

The Director of the Office of Science and Technology Policy (in consultation with other identified parties) to submit a report on the connections between distributed ledger technology (DLT) and short-, medium-, and long-term economic and **energy transitions**; the potential for these technologies to **impede or advance efforts to tackle climate change in the US and abroad; and their impact on the environment**. Consensus mechanisms impact on energy usage, incl. mitigating measures or alternative mechanisms and design tradeoffs are to be assessed.
- 7.1** Update of the Report on the connections between **DLT and economic and energy transitions**

The report shall be updated, including to address any knowledge gaps identified in such report, within 1 year of submitting the original report (7).

**Actions to Promote
Fin. Stability...(sec. 6)**

- 8** Report outlining **Recommendations to address financial stability risks and regulatory gaps**

The Secretary of the Treasury with the Financial Stability Oversight Council (FSOC) will convene and produce a report that outlines recommendations to address the risks related to specific financial stability risks and regulatory gaps previously identified, including any proposals for additional or adjusted regulation and supervision as well as for new legislation.

**Actions to Limit Illicit Fin. &
ass. National Security Risks
(sec. 7)**

- 9** **Supplemental annexes to the Strategy** offering additional views on illicit finance risks posed by digital assets

The Secretary of Treasury and other Secretaries listed as well as heads of other relevant agencies may submit supplemental annexes to the National Strategy for Combating Terrorist and Other Illicit Financing offering additional views on illicit finance risks posed by digital assets.
(within 90 days of submission to the Congress of the Strategy)
- 10** **Coordinated Action plan** based on the Strategy's conclusions for mitigating digital illicit finance and national security risks

The Secretary of Treasury (in consultation with identified parties) to develop a coordinated action plan on the National Strategy for Combating Terrorist and Other Illicit Financing's conclusions for mitigating the digital asset-related illicit finance and national security risks addressed in the updated strategy. It should address the role of law enforcement and measures to increase financial services providers' compliance with AML/CFT obligations related to digital assets.
(within 120 days of submission to the Congress of the Strategy)



Table 1. Summary of the identified reports presented in the EO (cont'd)

Actions to Limit Illicit
Fin..(sec. 7)

11 Update on rulemakings to address digital asset illicit finance risks. Consultation with relevant agencies...

The Secretary of Treasury is to notify the relevant agencies on any pending, proposed, or prospective rulemakings to address digital asset illicit finance risk. The Secretary shall consult with and consider the perspectives of relevant agencies in evaluating opportunities to mitigate such risks through regulation.
(within 120 days from completion of these reports: National Money Laundering Risk Assessment; National Terrorist Financing Risk Assessment; National Proliferation Financing Risk Assessment; updated National Strategy for Combating Terrorist and Other Illicit Financing)

Policy and Actions related to Fostering Int'l Cooperation
and US Competitiveness (sec. 8)

12 Establish **framework for interagency international engagement**

The Secretary of Treasury (in consultation with identified parties) to establish a framework for interagency international engagement with foreign counterparts and in international fora to adapt, update and enhance adoption of global principles and standards for how digital assets are used and transaction, and to promote development of digital asset and CBDC technologies consistent with the US values and legal requirements.

Key elements of the framework incl.: specific and prioritized line of efforts and coordinated messaging; interagency engagement and activities with foreign partners (e.g. compliance); and whole of gov. Efforts to promote international principles, standards and best practices.

13 Submit **report on priority actions taken under the framework and its effectiveness**

The Secretary of Treasury (in consultation with identified parties) to submit a report on priority actions taken under the framework and its effectiveness.

14 Establish **framework for enhancing US economic competitiveness**

The Secretary of Commerce (in consultation with identified parties) to establish a framework for enhancing United States economic competitiveness in, and leveraging of, digital asset technologies.

15 Submit **report on how to strengthen international law enforcement cooperation**

The Attorney General (in consultation with identified parties) to submit a report on how to strengthen international law enforcement cooperation for detecting, investigating and prosecuting criminal activity related to digital assets.



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About BlockZero:

BlockZero is a boutique consulting firm specializing in the evolution of the financial infrastructure through digital assets, digital currency, stablecoins and Central Bank Digital Currency (CBDC).

BlockZero advises global financial institutions, central banks and financial technology companies in the exploration, experimentation, technical implementation and rolling out of digital asset-based infrastructure.

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