

## THE ASSOCIATION OF GLOBAL CUSTODIANS

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COUNSEL AND SECRETARIAT TO THE ASSOCIATION:  
BAKER & MCKENZIE LLP  
GLOBAL  
ATT: ROBIN TRUESDALE  
815 CONNECTICUT AVENUE, N.W.  
WASHINGTON, D.C. 20006  
TEL: 202 452 7000  
FAX: 202 452 7074  
WWW.THEAGC.COM

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Via Electronic Submission at [www.bis.org/bcbs/commentupload.htm](http://www.bis.org/bcbs/commentupload.htm)

Basel Committee on Banking Supervision  
Bank for International Settlements  
CH-4002 – Basel  
Switzerland

RE: Consultative Document, Second consultation on the prudential treatment of cryptoasset exposures (Issued 30 June 2022)

Ladies and Gentlemen:

The Association of Global Custodians<sup>1</sup> (AGC) appreciates the opportunity to comment on the *Second consultation on the prudential treatment of cryptoasset exposures* (Second Consultation), published by the Basel Committee on Banking Supervision (the “Committee”) on 30 June 2022. We note that many of our members have participated in joint banking industry responses to the Second Consultation. This submission is intended to address aspects of the Second Consultation that are particularly important to our custody bank members as well as the overall stability of the financial system.

As the Committee notes, the cryptoasset market has developed rapidly over a short period of time. We agree that such rapid growth may raise financial stability concerns and we appreciate the Committee’s efforts to design a prudential framework of minimum standard that is simple and that is based on the core principles of “same risk, same activity, same treatment” and “technology neutrality”.

To develop such a framework, we recommend the following changes to the Second Consultation:

1. The proposed definition of “exposure” in section SCO60.4 should be revised to eliminate the reference to ‘non-fiduciary custody activities’ since such an approach would inappropriately have the effect of redefining the existing capital framework for assets held in custody.

Custody banks are the primary providers of essential custodial and fiduciary services, a role that is widely understood by the market and by the regulatory community as providing important benefits

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<sup>1</sup> Established in 1996, the Association of Global Custodians (AGC) is an informal group of 12 global financial institutions that provide securities safekeeping services and asset-servicing functions primarily to institutional clients worldwide. As a non-partisan advocacy organization, the AGC represents members’ common interests on regulatory and market structure matters through comment letters, white papers and interaction with legislative and regulatory authorities and financial industry organizations around the globe.

for the safety of client assets and the stability of the financial system. The risks that result from the provision of custody services today by banks are appropriately managed through a combination of stringent risk-management expectations, robust supervisory oversight and the application of a capital charge for operational risk. Our members do not believe that it's appropriate for the Committee to use the Second Consultation to redefine the current understanding of the term 'exposure' to include assets held in custody, a designation that would seem to implicate the imposition of an infrastructure risk add-on, the Group 2 exposure limit and various other provisions.

Assets held in custody by banks are not the property of the bank and are segregated at all times from the bank's own assets. For example, in the US, according to the Uniform Commercial Code, assets under custody are bankruptcy remote and cannot be used to satisfy the claims of the custodian's creditors. For these reasons, assets under custody are not treated as exposures of the bank and are therefore not subject to the application of risk factors outside of the framework for operational risk capital. Any deviation from this standard would serve to inappropriately limit the role of custody banks in the provision of safekeeping services for cryptoassets in a manner that would undermine the stability of the financial markets.

2. The Committee should clarify that the proposed Group 2 exposure limit does not apply to assets held in custody, as such an outcome would prevent custody banks from safeguarding Group 2 cryptoassets.

Custody banks specialize in the provision of safekeeping and asset administration services for their clients and can provide cost-effective services largely because of the economies of scale they can achieve. The proposed Group 2 exposure limit, if applied to assets held in custody, would preclude custody banks from supporting their client's evolving investment needs, as it would be economically unviable for custody banks to do so at such a small scale. Additionally, the application of an exposure limit for Group 2 assets would be fundamentally at odds with the well-established understanding that assets held in custody are not the property of the custodian and therefore do not create risks to the custody banks that require the application of risk metrics outside of the existing framework for operational risk.

3. The proposed infrastructure risk add-on for Group 1 cryptoassets should be eliminated as it is unnecessary to ensure the proper deployment by banks of new technology and may hinder responsible innovation using DLT by custody banks

Custody banks have long recognized the benefits that distributed ledger technology (DLT) and other related innovations can bring to core post-trade processes, including enhanced efficiencies, greater market transparency and reduced risk. Existing prudential regulation and supervision of banks covers the development and use of various technologies, which are subject to stringent risk management standards and consistent monitoring throughout their lifecycle. The Committee appears to recognize this in Section 60.130 of the Draft Standards where detailed expectations are laid out for the management of 'cryptoasset technology risk'. The proposed infrastructure risk add-on is therefore unnecessary and may discourage custody banks from responsibly developing and implementing new technologies for key financial market processes due to the material cost this add-on would impose on banks.

The proposed add-on is also not technology neutral, and it could serve to limit a bank's design of its internal books and recordkeeping systems in a manner that would be unsuitable. As such, the scope of the cryptoasset exposure framework should be further clarified to ensure that it does not have unintended consequences. The Committee should clarify that the use of DLT for settlement or recordkeeping purposes - including internally developed, private, permissioned

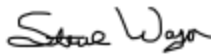
blockchain systems— should not by itself subject the related asset to the crypto asset exposure framework because such activities generally do not create a new asset that is distinct from the underlying asset or increase the risk or liquidity profile of the underlying assets.

Furthermore, the infrastructure risk add on for Group 1 cryptoassets could negatively impact the ability of custody banks to participate in efforts of regulated financial market infrastructure, such as the Depository Trust & Clearing Corporation (DTCC) or the Australian Securities Exchange (ASX), to deploy DLT based systems in support of clearing and settlement functionalities.

Thank you for the opportunity to comment on the Second Consultation from the perspective of our custody banks members. While the AGC supports the Committee's goal of establishing simple and technology neutral minimum standards for the prudential treatment of cryptoasset exposures, we believe that several components of the intended framework will have the practical effect of limiting the ability of custody banks to participate in the crypto-asset market in a way that could undermine responsible innovation and the overall stability of the financial markets.

We welcome further engagement with the Committee on this important subject.

Sincerely,

A handwritten signature in black ink that reads "Steven Wager". The signature is written in a cursive, slightly slanted style.

Steven Wager  
Chair, Americas Focus Committee  
Association of Global Custodians