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Remarks at the IIB Annual Washington Conference
"Trust and Global Banking: Lessons for Crypto"
March 6, 2023

Thank you for inviting me to the 2023 Institute of International Bankers (IIB) Annual Washington Conference. It is a pleasure and an honor to be here.

I would like to speak today about what it takes to build and maintain trust in global banking and what lessons this may hold for crypto. In particular, I believe there are strong parallels between FTX and the Bank of Credit and Commerce International – better known in bank regulatory circles as BCCI – which failed in 1991 and led to significant changes in how global banks are supervised.

Let me start by highlighting key features of the trust architecture for global banking that has been constructed over the past several decades. That will lead to a discussion of BCCI, parallels to FTX, and lessons for crypto.

Trust in Global Banking

Banking is global, while bank regulation and supervision are local. This creates challenges for bank regulators located in different jurisdictions tasked with ensuring the safety and soundness of different parts of global banks.

There are two key risks. First, there is the risk of an unlevel playing field – where rules differ by jurisdiction – which can enable regulatory arbitrage by banks and drive races to the bottom by local authorities.

Second, there is the risk of regulators having limited visibility into and influence over global banks – what one might call "supervisability" risk. Host and home regulators, having differing lines of sight and authorities into different entities within a global bank, may

struggle to see the true risk profile of the enterprise and may be limited in their abilities to address gaps.

The risk of an unlevel playing field can be mitigated by *coordination* among home and host authorities, while the supervisability risk of global banks can only be solved through *collaboration*.

Take capital requirements, for instance. The Basel Committee on Banking Supervision (BCBS) was founded in 1974 as a forum for regulatory coordination among its member countries on banking matters. In response to the debt crisis of the early 1980s, which exposed concerns about the capital ratios of international banks, the BCBS formulated the first Basel accord, now known as Basel I. The BCBS member states came to a shared goal of leveling the playing field with regard to risk-based capital and agreed to the objectives laid out in Basel I. Each member jurisdiction then took actions broadly consistent with those objectives to adopt and implement the capital standards in its national system.

In 2004, in order to update the capital framework in line with advances in bank risk measurement and management practices, the BCBS issued a revised capital framework, known as Basel II. Then, in 2011, in response to weaknesses and inefficiencies laid bare by the financial crisis, the BCBS issued a set of reforms collectively known as Basel III.

In each instance, the BCBS members recommitted to the shared goal of maintaining a level playing field, and the federal banking agencies determined that it was appropriate to implement regulatory capital requirements in the United States that were broadly consistent with the BCBS framework, including the Basel III final rule in 2013.

More recently, the BCBS updated and published revisions to the Basel III framework in 2017. I want to reconfirm today that the OCC remains fully committed to implementing enhanced regulatory capital requirements that align with the final set of Basel III standards as soon as possible. Our unwavering resolve is reflected in the September 2022 statement

reaffirming our collective commitment to Basel III.[1] The implementation of these standards for large banking organizations will strengthen the resilience of the domestic banking system and is a priority for the OCC.

Of course, in the meantime, risks continue to evolve. The BCBS recently developed prudential standards for crypto-asset exposures. The minimum capital and liquidity standards that have been developed are designed to ensure that banks maintain resiliency to risks associated with crypto-asset exposures. The rapid progress by the Basel Committee paves the way for a more consistent international approach to this new asset type and should help level the playing field. In December, along with the other members of the Global Heads of Supervision, I endorsed the final Basel standard for crypto-assets.

In contrast to regulatory standards, the supervisability of global banks cannot be achieved effectively through mere coordination among authorities. This was learned the hard way with the failure of BCCI in 1991 (which most IIB members will be familiar with, but is worth recounting).

In July 1991, immediately prior to its closure, BCCI had assets of $23 billion and 380 offices in over 72 countries. In the United States, BCCI owned four banks, operating in seven states and the District of Columbia. Scattered throughout the world, BCCI had a complex web of subsidiaries, affiliates, branches, and other entities. While BCCI was subject to a variety of local host regulations, there was no lead regulator with responsibility for the enterprise in its entirety. This meant that the supervision of BCCI was highly fractured, and no single supervisor had a clear picture of BCCI's consolidated activities.

To make matters worse, BCCI's parent holding company was not subject to supervision in the jurisdiction in which it was chartered, enabling the bank to engage in

[1] OCC News Release 2022-109, "Agencies Reaffirm Commitment to Basel III Standards."

interaffiliate transactions that facilitated money laundering and obfuscated its true financial condition for years.

Despite these challenges, there was suspicion among at least some regulators of significant underlying problems. Several key authorities collaborated to successfully close BCCI in a coordinated fashion in July 1991.

The supervisability risks revealed by the rise of BCCI led to significant enhancements in supervisory collaboration over internationally active banks. Through the BCBS, bank supervisory authorities developed standardized criteria for the establishment of bank branches or subsidiaries by foreign banks and strengthened the relationships between home and host country supervisors. Supervisory colleges created in the wake of BCCI's failure enhanced the sharing of prudential information on firms with cross-border operations and deepened collaboration across jurisdictions. Today, supervisory colleges, along with crisis management groups, play a vital role in the supervision of global systemically important banks (GSIBs).

In response to the BCCI failure, the U.S. Congress passed the Foreign Bank Supervision Enhancement Act (FBSEA), which prohibited entry of *any* foreign bank into the U.S. unless it was subject to comprehensive, consolidated supervision by a home country agency. In short, to do business in the U.S., foreign banks needed to have a lead regulator with visibility and authority over the entirety of the bank's global activities. FBSEA also authorized the examination of foreign banking organization (FBO) branches and established the requirement that any foreign bank operating in the U.S. grant the federal banking agencies supervisory access to necessary information. Foreign jurisdictions enacted similar legislation, effectively "leveling up" by requiring comprehensive, consolidated supervision for *all* internationally active banking groups.

The BCCI story is interesting from multiple angles, but is especially salient, I believe, for those looking for a path forward on crypto.

Lessons for Crypto Advocates and Policymakers

One of the underlying premises of crypto is that cryptography can be a viable replacement for trust in the traditional banking system – or, at least, cryptography and distributed ledgers may enable an alternative to the traditional banking and finance model.

Satoshi Nakamoto's bitcoin white paper is elegant in its arguments. Crypto in practice, however, has proven to be extraordinarily messy and complex. Nakamoto's vision of peer-to-peer payments never took hold and has been virtually nonexistent. Rather, crypto has served primarily as an alternative asset class and the dominant activity has been trading. In addition, the activities of many key participants in the markets lack transparency.

Intermediaries are required for crypto to operate at any scale. The events of the past year have shown that trust in those intermediaries can be quickly lost, large numbers of individuals can be hurt, and knock-on effects to the traditional financial system can result.

The rise and fall of FTX is especially noteworthy. While the details of FTX's failure continue to unfold and not all of the facts have yet been revealed, there are striking similarities between BCCI and FTX.

Both faced fragmented supervision by a combination of state, federal, and foreign authorities. Both lacked a lead or "home" regulator with authority and responsibility for developing a consolidated and holistic view of the firms. Both operated across jurisdictions where there was no established framework for regulators to share information on the firms' operations and risk controls. Both used multiple auditors to ensure that no one could have a holistic view of their firms.

As a result, BCCI and FTX were able to carry out and obfuscate fraudulent activity and operate with a stunning lack of basic risk management and internal controls for an extended period of time, despite being "regulated." By seemingly being everywhere and structuring entities in multiple jurisdictions, they were effectively nowhere and were able to evade meaningful regulation.

The analogy isn't perfect, of course. BCCI was a bank. FTX was a crypto exchange. So the actions needed to fix the problem in the crypto arena will have to take place outside of bank regulatory channels. Fortunately, international bodies like the Financial Stability Board, International Monetary Fund, and CPMI/IOSCO have recognized the need for a comprehensive global supervisory and regulatory framework for crypto participants, and can perhaps look to the BCCI experience as a model.[2]

Until that is done, crypto firms with subsidiaries and operations in multiple jurisdictions will be able to arbitrage local regulations and potentially play shell games using inter-affiliate transactions to obfuscate and mask their true risk profiles.

To be clear, not all global crypto players will do this. But we won't be able to know which players are trustworthy and which aren't until a credible third party, like a consolidated home country supervisor, can meaningfully oversee them.

Currently, no crypto platforms are subject to consolidated supervision. Not one.

Conclusion

Trust is a fragile thing. It is hard to earn, and easy to lose. Building trust and maintaining it take time and effort.

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[2] Financial Stability Board, *Regulation, Supervision and Oversight of Crypto-Asset Activities and Markets: Consultative document* (fsb.org); "IMF Executive Board Discusses Elements of Effective Policies for Crypto Assets"; Committee on Payments and Market Infrastructure and Board of the International Organization of Securities Commissions, *Application of the Principles for Financial Market Infrastructures to Stablecoin Arrangements* (iosco.org); OR03/22, "IOSCO Crypto-Asset Roadmap for 2022-2023" (iosco.org).

As international bankers, you know that this time and effort are worth it. Global trust can enrich communities, facilitate activities, and enable economic opportunities that previously would have been out of reach.

The flip side of that coin, however, warrants equal attention. Regulatory coordination and supervisory collaboration can help mitigate the risks of losing that trust. We have learned this the hard way in banking. I believe it contains useful lessons for crypto.

Thank you.