Regulatory Alert

Regulatory Insights

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GENIUS Act: New York Payment Stablecoin Proposed Rule

KPMG Regulatory Insights:

The name of the game is "alignment" as New York DFS reaffirms its U.S dollar-backed payment stablecoin framework and proposes a new framework intended to:

- *Align with the federal regulatory framework under the GENIUS Act, including in areas of BSA/AML/CFT, sanctions compliance, certifications, and prohibited activities.*
- *Be at the forefront of state efforts to align new and existing requirements for payment stablecoin issuers with the federal prudential regulations.*

The New York State Department of Financial Services (DFS) has issued a proposed rule that would establish requirements for "authorized payment stablecoin issuers" (hereinafter "APSI") as defined by DFS pursuant to the GENIUS Act (Guiding and Establishing National Innovation for U.S. Stablecoins Act). The proposal would build on DFS's prior guidance for U.S. dollar-backed stablecoins and add provisions intended to align the New York framework with the federal regulatory framework of the GENIUS Act.

The proposed rule would address requirements including:

- Scope and definitions
- Issuer authorization
- Reserves and redemption requirements
- Capital and operational backstops
- Compliance and operational controls, including BSA/AML/CFT
- Information technology and security
- Supervision and recordkeeping

DFS proposes the rule would become effective upon the effective date of the GENIUS Act. Consistent with the GENIUS Act, the DFS proposes transition provisions that would, in general, require an APSI with a total consolidated outstanding payment stablecoin issuance of more than $10 billion to transition to the federal regulatory framework under the joint supervision of the DFS and the appropriate federal regulatory agency (i.e., for an APSI that is a state chartered depository institution, the primary federal regulator of that state-chartered depository institution; for other APSI, the OCC).

Scope and Definitions

DFS would align its payment stablecoin framework with the federal stablecoin framework with terms defined accordingly, including:

- **"APSI:"** A person approved by DFS to issue one or more payment stablecoins.
- **"Limited purpose trust company:"** A New York-chartered trust company that does not receive deposits from the general public and has been exempted from generally applicable deposit-taking trust company requirements.
- **Reserve asset:** An asset maintained by an APSI that is a type permitted by the GENIUS Act.

Issuer Authorization

Issuer authorization requirements would address who may issue payment stablecoins and the conditions attached to DFS approval, including:

Topic	Requirement
Eligible applicants	Limited purpose trust companies, applicants for limited purpose trust company charters, and other entity types as determined by DFS may apply for approval to issue one or more payment stablecoins. Non-financial public companies, and their wholly or majority owned subsidiaries or affiliates, would be ineligible to apply, except as permitted under the GENIUS Act.
Application review	Applications would need to be submitted in writing using the form and materials required by DFS. Applications would need to demonstrate financial capacity to meet APSI requirements, acceptable officer and director backgrounds, qualified and reliable leadership and ownership, and readiness to meet DFS stablecoin requirements. DFS would approve applications that satisfy the approval standards, and denied applicants could reapply.
Existing issuers and brands	Existing DFS-approved payment stablecoin issuers need not obtain a second approval to issue the-approved payment stablecoins. However, existing DFS-approved issuers would need to comply with the new requirements within 12 months after the effective date, except for the separate compliance-certification timing. Prior DFS approval would be required before issuing a distinguishable payment stablecoin brand.
Prohibited activities	APSIs would be prohibited from engaging in any activity prohibited by or otherwise inconsistent with the GENIUS Act, including: — Rehypothecation. — Tying arrangements. — Certain marketing practices, including the use of deceptive names and/or claims. — Misrepresentation of insured status. — Paying interest or yield to holder of the stablecoin.
Officers and directors	— Individuals with specified felony convictions could not serve as officers or directors of APSIs.

Reserve and Redemption Requirements

Reserve requirements would address how the assets backing payment stablecoins must be maintained and verified for DFS oversight; redemption requirements would address holder access to redemption and the circumstances that may affect redemption timing, as follows:

Topic	Requirement
Reserve Requirements	
Custody	Reserve assets would be required to be maintained with an eligible financial institution other than the APSI, with DFS approval required to hold reserves at an eligible financial institution that is not an insured depository institution.
Segregation by brand	APSIs with more than one distinguishable payment stablecoin brand would be required to maintain separately identifiable reserves and segregated reserve pools unless DFS approves commingling.
Composition and concentration	Reserve assets would be limited to authorized asset types and managed under applicable diversification and concentration expectations.

Insured deposit threshold	APSIs with an outstanding issuance value of $25 billion or more would be required to maintain a specified portion (proposed to be a minimum of 0.5 percent) of reserve assets in insured deposits or insured shares at an insured depository institution.
Reporting and certifications	APSIs would be required to provide DFS with reserve reporting and certification materials, including monthly reserve composition reports for each distinguishable brand, monthly CEO/CFO certifications regarding report accuracy, and registered public accounting firm attestations of management's assertion of information disclosed in the previous monthly report.
Shortfalls	Reserve deficiencies would trigger: — Same-day DFS notice. — Issuance restrictions until compliance is restored. — Possible compliance plans. — Liquidation or redemption if a shortfall continues for 15 consecutive business days absent a DFS extension.
Annual attestations	Annual registered public accounting firm attestations would be required for management assertions concerning internal controls, structure, and procedures for compliance with the reserve reporting requirement.
Redemption Requirements	
Public disclosure	APSIs would be required to obtain DFS approval for, and publicly disclose, their redemption policy, which at a minimum must include the: — Timeframe for redeeming payment stablecoins. — Limits on timely redemption. — Scenarios for extending the redemption period. — Instructions for how holders may redeem. — Minimum number of payment stablecoins to be redeemed provided the number is one or more payment stablecoins.
Timeliness	Payment stablecoin redemption would be required to occur within two business days after the redemption request.
Limitations or extensions	Discretionary limitations on timely redemption may be imposed only by the applicable federal regulator or DFS. DFS could extend timely redemption if it determines that the issuer poses a threat to safety and soundness or financial stability, or if an extension is otherwise in the public interest.

Capital and Operational Backstops

Capital and operational backstop requirements would address issuer-level resources needed to support operations separately from reserve assets, including:

Topic	Requirement
Capital requirements	Capital requirements, including tier 1 capital, would be expected to be commensurate with the level and nature of risks facing the APSI, including off-balance sheet risks, and sufficient to ensure ongoing operations. DFS may establish additional capital thresholds or metrics, including additional types of capital or risk-based capital requirements.
Capital adequacy process	APSIs would need a process for assessing overall capital adequacy and a strategy for sustaining appropriate capital.
Operational backstop	APSIs would be required to maintain an operational backstop of liquid identifiable assets to meet short-term liquidity needs, stabilize operations after a business disruption and continue or resume normal operations.
DFS revisions	DFS may revise an APSI’s capital requirement or operational backstop based on a change to the issuer’s business model or risk profile, or if DFS determines that a change is needed for safety and soundness. DFS would provide written notice of any revision.
Shortfalls	Capital or backstop deficiencies at the end of a quarter would trigger new-issuance restrictions, and after two consecutive deficient quarters, would trigger liquidation of reserve assets, redemption of outstanding stablecoins without fees, and prohibition of new issuance.

Compliance and Operational Controls, including BSA/AML/CFT

Compliance and operational standards would address financial-crime controls, management accountability, audit, and risk management across APSI operations, including:

Topic	Requirement
BSA/AML/CFT and sanctions compliance	APSIs would be required to comply with applicable Bank Secrecy Act (BSA), anti-money laundering (AML) and combatting the financing of terrorism (CFT) requirements as well as sanctions.
Compliance certifications	An APSI would be required to certify annually that it has implemented BSA/AML/CFT and economic sanctions compliance programs that are reasonably designed to prevent illicit activity. Failure to timely file a certification may result in revocation of the issuer’s authorization.
Internal controls and information systems	Internal controls and information systems would be required to support effective risk management based on the size and complexity of the APSI and the nature, scope and risk of its activities.
Internal audit system	Internal audit or independent review systems appropriate for the size and complexity of the APSI and the nature, scope and risk of its activities would be required to provide for: — Independent testing of controls and information systems. — Verification of published information available to customers. — Verification of required reserve calculations. — Verification of regulatory filings. — Documentation of findings and corrective actions. — Review of remediation for identified deficiencies. — Audit committee or board review.

Operational standards	APSIs would need processes addressing operational standards such as interest rate exposure, "prudent asset growth", processes to evaluate and monitor earnings, liquidity/concentration risk management, and consumer protection compliance.

Information Technology and Security

Technology, cybersecurity, and customer-information requirements would address issuer systems, nonpublic information, and customer-notice obligations, including:

Topic	Requirement
Cybersecurity requirements	APSIs would be required to comply with DFS cybersecurity requirements applicable to Class A companies, without otherwise available exemptions, and additional requirements designed to produce outcomes at least as stringent and protective as federal standards.
Customer and nonpublic information	Nonpublic information would include information provided by a customer to obtain a financial product or service, transaction-related customer information, and other customer information obtained in connection with financial products or services.
Customer notice	Customer notice would be required when unauthorized access to nonpublic customer information has resulted or will result in misuse, and when affected customers cannot be identified but misuse is reasonably possible. Notice would be required to be provided as soon as possible and without unreasonable delay.

Supervision and Recordkeeping

Supervisory and post-authorization requirements would address DFS oversight and APSI obligations that continue after authorization, including:

Topic	Requirement
Examinations	APSIs would be examined at least annually, though DFS may examine APSIs at any time when, in the judgement of DFS it is necessary or advisable.
Supervisory access	When requested, APSIs would be required to provide DFS full and immediate access to personnel; books, records, documents, and other information; and facilities used by the issuer or its affiliates.
Records, reports, audits	APSIs would be required to: — Maintain records retention policies. — Provide DFS with periodical or special reports, as required by DFS. — Submit audited financial statements (for APSIs with outstanding issuance values above $50 billion that are not subject to Securities Exchange Act reporting requirements).
Insolvency, custody, and information sharing	Provisions related to insolvency, custody, and information-sharing treatment would align with the relevant GENIUS Act provisions.

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