

# Capital Treatment of Tokenized Securities FAQs

## Introduction

There has been increasing interest in representing ownership rights in securities using distributed ledger technology (DLT). Such securities are often referred to as “tokenized securities.”<sup>1</sup> This document provides answers to several frequently asked questions concerning the capital treatment of tokenized securities that, under applicable law, confer legal rights identical to those of the non-tokenized form of the security (“eligible tokenized securities”).<sup>2</sup>

## Questions

*What is the capital treatment for eligible tokenized securities?*

- The capital rule for banking organizations implemented by the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, and the Federal Deposit Insurance Corporation (together, the federal banking agencies) is technology neutral. The technologies used to issue and transact in a security do not generally impact its capital treatment.
- Accordingly, an eligible tokenized security should be treated in the same manner as the non-tokenized form of the security would be treated under the capital rule. Similarly, a derivative that references an eligible tokenized security should be treated for capital purposes as a derivative that references the non-tokenized form of the security.
- As with any exposure, banking organizations holding tokenized securities must apply sound risk management practices and comply with applicable regulations.<sup>3</sup>

*Would a tokenized security qualify as financial collateral for purposes of the capital rule?*

- The technologies used to confer legal rights to a security do not impact its ability to meet the definition of “financial collateral” in the capital rule. A banking organization should evaluate the tokenized security according to the definition of

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<sup>1</sup> The process of representing an asset on DLT is often referred to as “tokenization.” Tokenization of securities generally takes one of two forms. In some cases, the token is used to represent an interest in a security that has been issued using traditional processes, such as a central securities depository. In other cases, an issuer may issue the security directly on DLT. This document uses the term “tokenized security” to refer to both types of arrangements.

<sup>2</sup> Tokenized securities that do not confer legal rights identical to those of the non-tokenized form of the security, including legal ownership rights, are outside the scope of this document.

<sup>3</sup> See, e.g., 12 CFR part 1 (national banks), 12 CFR 160 (federal savings associations), 208.21 (state member banks), and part 362 (state non-member banks) for tokenized securities purchased under that authority; or 12 CFR part 32 and part 252, subpart H for tokenized securities purchased as extensions of credit.

“financial collateral” in the capital rule.<sup>4</sup> An eligible tokenized security that satisfies the definition of “financial collateral” would qualify as financial collateral for purposes of the capital rule and may be recognized by the banking organization as a credit risk mitigant if all the other relevant requirements in the capital rule are met.<sup>5</sup> As financial collateral, an eligible tokenized security would be subject to the same haircuts applicable to the non-tokenized form of the security.

*Would the capital treatment of tokenized securities depend on whether the tokens are issued on permissioned or permissionless blockchains?*

- No, the capital rule does not provide a different treatment based on the use of permissioned or permissionless blockchains.

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<sup>4</sup> For example, the banking organization must have a perfected, first-priority security interest or, outside of the United States, the legal equivalent thereof (with the exception of cash on deposit; and notwithstanding the prior security interest of any custodial agent or any priority security interest granted to a CCP in connection with collateral posted to that CCP) in order for the tokenized security to qualify as financial collateral under the capital rule. 12 CFR 3.2 (OCC), 217.2 (Board), and 324.2 (FDIC).

<sup>5</sup> 12 CFR 3.37, 3.132 (OCC); 217.37, 217.132 (Board); and 324.37, 324.132 (FDIC).