

Federal Reserve Eliminates 'Reputational Risk' Criterion in Bank Oversight: A Potential Turning Point for Crypto Firms

The U.S. Federal Reserve has announced a significant policy change: it will no longer instruct bank supervisors to consider “reputational risk” as part of their oversight of financial institutions. This move addresses longstanding concerns that the ambiguous concept was used disproportionately to restrict banking services to cryptocurrency and technology companies.

Following the collapse of several crypto-friendly banks in 2023, including Signature Bank and Silvergate, more than 30 technology and crypto firms found themselves effectively cut off from essential banking services, a phenomenon critics labeled Operation Chokepoint 2.0. Many industry stakeholders argued that reputational risk was wielded as a vague justification to “debank” these firms despite their compliance with laws and regulations.

In its recent statement, the Federal Reserve Board confirmed it is reviewing supervisory materials to remove references to reputational risk, replacing them with more precise assessments focused on financial risk. The Fed also plans to train examiners accordingly and coordinate with other federal regulatory agencies to ensure consistent implementation.

The policy shift has been met with cautious optimism by cryptocurrency advocates. Senator Cynthia Lummis described the prior use of reputational risk policies as having “assassinated American Bitcoin and digital asset businesses,” framing the Fed’s announcement as a positive, though incomplete, step forward. Rob Nichols, president and CEO of the American Bankers Association, welcomed the change as enhancing transparency and fairness in bank supervision, emphasizing the importance of decisions grounded in prudent risk management rather than subjective regulatory perspectives.

However, some experts caution that eliminating reputational risk from the supervisory framework could reduce regulators’ ability to identify non-financial risks that may affect a bank’s long-term stability such as ethical concerns, social trust, or association with illicit activities. Karen Petroski, a scholar of financial ethics, noted that reputational risk served as a proxy for broader societal considerations that extend beyond purely financial metrics.

The Federal Reserve clarified that while it will no longer require supervisors to factor reputational risk into oversight, banks remain responsible for maintaining comprehensive risk management programs compliant with all applicable laws and regulations. Moreover, banks retain the discretion to consider reputational risk internally within their own risk frameworks.

For the cryptocurrency sector, this policy adjustment may signal an opportunity to re-establish and expand banking relationships within the United States, potentially reversing some of the access challenges experienced in recent years. Yet, the industry’s future will

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likely depend on its ability to demonstrate robust compliance and build trust with both regulators and financial institutions.

In summary, the Fed's removal of reputational risk as a supervisory consideration marks a notable shift toward clearer, more objective regulatory standards. While it may open doors for innovation and growth in crypto and technology sectors, it also places renewed emphasis on these firms' responsibility to uphold transparency and sound risk management in an evolving financial landscape.