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Stablecoin-on-Creditor Violence

Jeffery Y. Zhang and Peter Zimmerman*

October 1, 2026

Abstract

The GENIUS Act of 2025 rewrites the priority and estate-property rules that govern the failure of a payment stablecoin issuer. It removes an issuer’s required reserves from the bankruptcy estate and grants stablecoin holders a superpriority, capped at any reserve shortfall, over what remains. The commentary so far asks what happens *inside* bankruptcy once an issuer files—whether holders are actually paid and whether the case can be administered. This article identifies a different problem that arises *before* a filing. Because reserve assets leave the estate the moment they back a coin, a distressed firm can issue stablecoins to subordinate its existing creditors, hollow out the value a future administrator would need, and, when the firm is a bank, shift losses onto the deposit insurer and potentially the taxpayer. We call this *stablecoin-on-creditor violence*, drawing an analogy with the phenomenon of creditor-on-creditor violence that began with the 2016 J. Crew dropdown. Unlike in that episode, the stablecoin dropdown is on a statutory footing, meaning it is largely beyond the reach of the doctrines courts use to police its private-law cousins. We show that the subordination is accomplished by the rule carrying reserves out of the estate rather than by the celebrated superpriority. We raise concerns for financial stability: The threat of a dropdown grows with a firm’s holdings of safe assets, meaning that creditors may respond negatively to a firm with a more liquid balance sheet. The harm is gravest when the subordinated creditor is the FDIC or another deposit insurer, because losses can be imposed on the rest of the financial system and the taxpayer. Importantly, the problems we raise do not rely on there being any investor demand for stablecoins. We close with a menu of responses and recommend a layered fix that federal regulators could largely implement on their own.

Keywords: stablecoins; GENIUS Act; bankruptcy priority; liability management exercises; deposit insurance; financial stability.

JEL Classification: G21, G28, G33, K22, K23.

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1. Introduction

A year after the GENIUS Act became law in July 2025,¹ dollar-pegged payment stablecoins have grown into a market of roughly \$300 billion, still dominated by Tether and Circle.² The next cohort of issuers is already visible. Large payment providers have begun minting their own coins, several banks are standing up issuing subsidiaries, and dozens of state-chartered applicants are waiting in the queue.³ In March 2026, the Office of the Comptroller of the Currency opened the rulemaking that will govern much of this activity.⁴ Most public argument about the act has focused on its prudential design (i.e., the one-to-one reserve requirement), the ban on paying interest, and the fear that stablecoins will pull deposits away from community banks.⁵ The feature that may matter most in a crisis has drawn far less attention. Tucked into the act is a rewrite of the priority and estate-property rules that decide what happens when a stablecoin issuer fails.

These new rules accomplish two things. First, they remove an issuer's required reserves from its bankruptcy estate, so that the assets backing outstanding coins sit outside the pool available to ordinary creditors. Second, they give stablecoin holders a claim that, to the extent that reserves fall short, outranks everything else against what remains of the estate, down to the administrator's own fees.⁶ Congress meant to make coins as safe as it possibly could for the people holding them, so that a coin with a nominal value of one dollar retains this value even if the issuer becomes insolvent. The unintended consequences of that generosity are the subject of this article.

¹ Guiding and Establishing National Innovation for U.S. Stablecoins Act of 2025 (GENIUS Act), Pub. L. No. 119-27, 139 Stat. 419 (codified in scattered sections of the U.S. Code, including 12 U.S.C. §§ 5901–5915).

² As of July 25, 2026, total stablecoin market capitalization stood at \$310 billion, with Tether (USDT) and Circle (USDC) together accounting for some 83 percent of outstanding supply. *See Stablecoins Dashboard (2026)*, DEFI LLAMA <https://defillama.com/stablecoins>.

³ PayPal has issued a dollar stablecoin, PYUSD, through Paxos Trust Company since 2023, and Ripple has issued RLUSD through a New York-chartered trust company since 2024. Stripe's Bridge subsidiary issues a coin of its own, USDB, and issues branded coins for other payment firms, including MoneyGram's MGUSD and Deel's DLUSD, both launched in 2026. Fiserv announced its coin in 2025. *See Fiserv Launches New FIUSD Stablecoin for Financial Institutions*, FISERV (June 23, 2025), <https://investors.fiserv.com/news-releases/news-release-details/fiserv-launches-new-fiUSD-stablecoin-financial-institutions>. Western Union's USDPT launched in May 2026, issued by Anchorage Digital Bank, N.A. *See Western Union Launches USDPT on Solana Advancing Regulated Digital Infrastructure for Global Payments*, WESTERN UNION (May 4, 2026), <https://ir.westernunion.com/news/archived-press-releases/press-release-details/2026/Western-Union-Launches-USDPT-on-Solana-Advancing-Regulated-Digital-Infrastructure-for-Global-Payments/default.aspx>. Even the card networks have moved beyond supplying rails. Visa, Mastercard, and American Express are among the more than 140 firms behind Open USD, a consortium coin announced in June 2026 and slated to launch later this year. *See Camila Grigera Naón, Stripe, Visa and Over 140 Other Businesses to Launch Stablecoin to Rival Tether and Circle*, FORTUNE (June 30, 2026), <https://fortune.com/2026/06/30/stripe-visa-stablecoin-rival-ousd-tether-circle/>.

⁴ Office of the Comptroller of the Currency, Notice of Proposed Rulemaking Implementing the GENIUS Act, 91 Fed. Reg. 10202 (Mar. 2, 2026).

⁵ GENIUS Act § 4(a)(1)(A) (one-to-one reserve requirement); *id.* § 4(a)(11) (barring the payment of interest or yield to holders). For the policy debate over these features, see NELLIE LIANG & WILLIAM C. DUDLEY, BROOKINGS HUTCHINS CTR. ON FISCAL & MONETARY POL'Y, NEXT STEPS FOR GENIUS PAYMENT STABLECOINS: WHAT REGULATORS NEED TO DO TO MAKE THEM TRUSTED PAYMENTS AND ENSURE FINANCIAL STABILITY (2026).

⁶ GENIUS Act § 11(e) (adding 11 U.S.C. § 541(b)(11), which excludes required reserves from the estate); *id.* § 11(d) (adding 11 U.S.C. § 507(e), a shortfall-capped superpriority). Section 2 *infra* describes both provisions with care, because the early commentary has at points characterized them imprecisely.

A small set of the literature has begun to probe these provisions, all of which examines what happens *after* an issuer has already filed for bankruptcy. Adam Levitin argues that the superpriority is largely a mirage, because holders will, in practice, sit behind secured lenders, debtor-in-possession financiers, professional carveouts, and setoff claimants, which leaves them roughly fifth in line.⁷ Other commentators worry that pulling reserves out of the estate while raising holders above administrative expenses could make an issuer's bankruptcy impossible to administer, boxing the firm out of Chapter 11 altogether.⁸ Christopher Odinet, Andrea Tosato, and Yesha Yadav document a parallel weakness in private law, showing that the major issuers' terms of service leave most coinholders without privity, without any property interest in the reserves, and with the standing of ordinary unsecured creditors if the issuer fails.⁹

This article asks a different question. What does the new priority structure do to a distressed firm's incentives *before* it files, while managers still control the balance sheet? The answer could be unsettling. Because an issuer's reserves leave the estate the instant they back a coin, a firm that can see insolvency coming may be able to issue stablecoins as a weapon against its own creditors: It can move its best assets beyond their reach, discouraging them from forcing a bankruptcy by hollowing out the value a future administrator would need to run the case. And if the firm is an insured depository institution, it can shunt the resulting losses onto the deposit insurer and, potentially, the taxpayer. We call this maneuver *stablecoin-on-creditor violence*, inspired by the creditor-on-creditor violence that has come to define distressed-debt practice over the past decade.¹⁰

When the retailer J. Crew shifted its most valuable intellectual property into a subsidiary beyond its lenders' reach in 2016, it set off a wave of so-called liability management exercises—specifically, the dropdowns and uptier exchanges through which a borrower mines gaps in its loan

⁷ Adam J. Levitin, *Sorry to Break It to You Geniuses: Under the GENIUS Act the Holders of Stablecoins Actually Have FIFTH Priority in an Issuer Bankruptcy*, CREDIT SLIPS (Dec. 2, 2025), <https://creditslips.org/2025/12/02/sorry-to-break-it-to-you-geniuses-under-the-genius-act-the-holders-of-stablecoins-actually-have-fifth-priority-in-an-issuer-bankruptcy/>.

⁸ See Edwin E. Smith, Penelope L. Christophorou, Stacie Hartman & Alice S. Hrdy, *The Proposed GENIUS Act Raises Concerns Over Insolvency Provisions*, MORGAN LEWIS LAWFLASH (July 2, 2025), <https://www.morganlewis.com/pubs/2025/07/the-proposed-genius-act-raises-concerns-over-insolvency-provisions>; Mark Salzberg, *The GENIUS Act and the Law of Unintended Consequences: Are Stablecoin Issuers Going To Be Boxed Out of Bankruptcy?*, SQUIRE PATTON BOGGS: RESTRUCTURING GLOBALVIEW (Aug. 6, 2025) (arguing that, because legal expenses cannot be paid from reserves and reserves cannot serve as debtor-in-possession collateral, an issuer may be administratively insolvent from the inception of the case).

⁹ Christopher K. Odinet, Andrea Tosato & Yesha Yadav, *The Moneyness of Stablecoins* (forthcoming Yale L.J. 2026). Drawing on the terms of service of Tether and Circle, they show that most holders lack privity with the issuer, hold no property interest in the reserves, and would rank as ordinary unsecured creditors on the issuer's failure, and they independently observe that the shortfall super-priority can leave no one willing to administer the case.

¹⁰ The phrase is now standard in practice and in the press. See, e.g., Becky Yerak, *Aggrieved Lenders Struggle to Unwind 'Creditor Violence' Deals*, WALL ST. J. (Mar. 9, 2023), <https://www.wsj.com/articles/aggrieved-lenders-struggle-to-unwind-creditor-violence-deals-537f93da>; Matt Wirz, *Coming to a Cash-Strapped Company Near You: Creditor-on-Creditor Violence*, WALL ST. J. (Aug. 19, 2024), <https://www.wsj.com/finance/coming-to-a-cash-strapped-company-near-you-creditor-on-creditor-violence-2dfd4308>; Samuel Antill, Zhaoli Jiang & Neng Wang, *Creditor-on-Creditor Violence and Secured Debt Dynamics* (Nat'l Bureau Econ. Rsch., Working Paper No. 32823, 2024).

documents to subordinate creditors left out of the deal.¹¹ Courts have spent years learning to discipline these transactions through doctrines of good-faith dealing, ratable-treatment and sacred-rights clauses, and equitable subordination.¹²

What makes the stablecoin version more dangerous is its origin. A dropdown engineered through the GENIUS Act does not exploit sloppy drafting that the next credit agreement can tighten. Instead, it draws on a federal statutory entitlement. Because it is a right that Congress has explicitly granted, it sits beyond what equitable doctrine or private ordering can claw back.

Working through the mechanics yields three findings. First, the part of the act that actually powers the maneuver may be unexpected. While most commentary on the act has spotlighted the superpriority, that provision turns out to do limited work, since it bites only when an issuer is already under-reserved. Creditor subordination is instead accomplished through the rule that carries reserves out of the estate to begin with. Because the act confines a permitted issuer to the stablecoin business, a firm with losses elsewhere on its balance sheet must issue new coins through a subsidiary, so the corporate-structure version of the rule is the general case. Second, the threat grows in lockstep with a firm's holdings of reserve-eligible assets such as Treasuries and bank deposits, which are precisely the safe, liquid assets that creditors and supervisors value. As a result, a balance sheet may look safer but be harder to resolve. Third, once the subordinated creditor is the deposit insurer, the transaction operates as an implicit subsidy from the FDIC to bank shareholders. However, this is also where a regulator has the cleanest path to step in.

The remainder of the article delves into this dynamic in four sections. Section 2 maps the act's bankruptcy architecture, including the corporate structures it permits. Section 3 develops the core mechanism. It examines the liability-management playbook, exploring why the statutory version at issue escapes the usual cures. The section then works through a running balance-sheet example and carries that example into the banking system, where the deposit insurer absorbs the loss. Section 4 follows the spillovers and sets out our recommendations. Section 5 concludes.

2. The GENIUS Act's Bankruptcy Architecture

Four features of the act distinguish its treatment of a failed stablecoin issuer from any prior federal priority regime. They are (1) the exclusion of reserves from the estate, (2) a superpriority over what remains, (3) a bar on encumbering reserves, and (4) a set of procedural rules governing the stay, the routing of the case, and the role of the regulator. The early commentary has tended to lead with

¹¹ On the J. Crew dropdown, the Serta uptier, and the broader turn to liability management exercises, see Vincent S.J. Buccola & Greg Nini, *The Loan Market Response to Dropdown and Uptier Transactions*, 53 J. LEGAL STUD. 489 (2024); and Douglas G. Baird, *Three Faces of Creditor-on-Creditor Aggression*, 97 AM. BANKR. L.J. 213 (2023). On the phrase and its limits, see Mark J. Roe & Vasile Rotaru, *Liability Management's Limited Runway*, 136 YALE L.J. (forthcoming 2026).

¹² See, e.g., *In re Serta Simmons Bedding, L.L.C.*, 125 F.4th 555 (5th Cir. 2024) (holding that a non-pro rata uptier was not a permitted "open market purchase" under the credit agreement); *Ocean Trails CLO VII v. MLN TopCo Ltd.*, No. 2024-00169, 2024 WL 5248898 (N.Y. App. Div. Dec. 31, 2024) (upholding an uptier under the plain terms of the documents). Section 3.2 examines these tools and their limits.

the superpriority. We lead with the estate carve-out because that is the provision that does the real work once a firm starts to think strategically.

2.1. Reserves Leave the Estate

Section 11(e) of the act amends section 541(b) of the Bankruptcy Code by adding a new paragraph that excludes an issuer's required payment of stablecoin reserves from the property of the estate.¹³ In an ordinary bankruptcy, section 541 sweeps essentially everything the debtor owns into the estate, which is the common pool that a trustee then marshals and distributes according to the priority rules. The GENIUS Act pulls the reserves out of that pool before the process begins. The assets that back outstanding coins are set aside for holders from the outset, so a trustee never gains control of them.

Even though reserves sit outside the estate, the section 362 automatic stay continues to apply to them, so holders cannot simply seize the assets the moment a petition is filed. Section 11(a) supplies the matching entitlement, giving each holder's claim priority over the issuer and every other claimant with respect to the reserves, shared ratably with other holders.¹⁴ The combined effect is a ring fence. The good assets are reserved for one class and are protected by the stay while the case is pending, such that the rest of the creditor body has no claim on them at all. Everything that follows in this article is a consequence of that fence going up *before* a firm files rather than after.

An exclusion of this kind is unusual, though not wholly without precedent.¹⁵ The reserve carve-out is different in scale, because it can sweep out an issuer's entire base of high-quality assets. It is also different from the tool federal law has traditionally used to favor a class in a failed financial firm. The GENIUS Act does something more aggressive by removing the assets from the common pool rather than merely moving one claimant to the front of the line for them.

2.2. Superpriority, Capped at the Shortfall

Section 11(d) adds a new subsection to section 507 of the Bankruptcy Code. If a holder cannot redeem in full from reserves, the leftover claim jumps to top priority over every other claim against the estate, including the administrative expenses that traditionally come first. Read quickly, this looks like a sweeping superpriority that subordinates the trustee, the tax authorities, and employees alike. But in practice, it is narrower. The priority extends only "to the extent compliance with section 4 of

¹³ 11 U.S.C. § 541(b)(11) (as added by GENIUS Act § 11(e)) excludes "required payment stablecoin reserves under section 4 of the GENIUS Act," while providing that "notwithstanding the exclusion of such reserves from the property of the estate, section 362 of this title shall apply to such reserves."

¹⁴ GENIUS Act § 11(a) (codified at 12 U.S.C. § 5910) gives a holder's claim priority, on a ratable basis with other holders, over the claims of the issuer and every other claimant with respect to required reserves and confirms that a holder is deemed to hold a "claim" for these purposes.

¹⁵ Section 541(b) already excludes discrete categories of property from the estate, such as certain education-savings and pension assets, but those carve-outs are narrow and consumer-protective. The reserve exclusion in the GENIUS Act operates at the scale of an issuer's entire high-quality asset base. Compare the depositor-preference regime of 12 U.S.C. § 1821(d)(11), which reorders priorities within a failed bank's estate without removing assets from it.

the GENIUS Act would have required additional reserves to be maintained.”¹⁶ In other words, the superpriority over the general estate is measured by the reserve deficiency—the gap between the reserves the act demanded and the reserves the issuer held.

This limitation is more significant than it might appear at first glance. Suppose an issuer has maintained full reserves, one dollar of eligible assets for every dollar of coin. There is no deficiency, so there is no superpriority claim against the general estate whatsoever. The holders take their reserves through the carve-out and have nothing further to assert against the loans, receivables, or other assets left behind. The superpriority does real work only when an issuer has run short, whether by breaking the reserve rule or through losses on the reserve assets themselves, as when a spell of Treasury market illiquidity coincides with heavy redemptions. For a firm that plays by the reserve requirement while restructuring its liabilities, the superpriority provision, which has drawn so much commentary, is close to inert.

The point also settles an apparent tension with Adam Levitin, who argues that any holders’ priority is illusory once secured lenders, debtor-in-possession financiers, professional carve-outs, and setoff claims are accounted for. He is right that the superpriority *over the remaining estate* is weak. The subordination we later describe runs through the carve-out in section 11(e), which takes the reserves off the table before any of the section 507 machinery is reached. His weak superpriority and our robust carve-out are two different provisions; the strength of the second does not depend on the first.

The superpriority does, however, bring into relief a separate worry that other commentators have raised. Administrative expenses ordinarily come first in a bankruptcy, because someone has to be paid to run the case.¹⁷ A residual holder claim that outranks even those expenses, arising in a case where the reserves have already been carried off and cannot be borrowed against, is what leads some to fear that a stablecoin bankruptcy for an under-reserved issuer may be impossible to administer. The strategic firm considered by this article takes the opposite approach. Because it keeps full reserves and uses the carve-out, it never triggers the superpriority and never presents the administrative-insolvency problem in the pure form the literature describes. The two failure modes are distinct, and a complete account of the act has to hold both in view.

2.3. Reserves Cannot Be Pledged

The act defines “reserves” as an enumerated collection of high-quality liquid assets, such as short-dated Treasury bills and bank deposits.¹⁸ A separate paragraph provides that required reserves

¹⁶ 11 U.S.C. § 507(e) (as added by GENIUS Act § 11(d)) provides that a residual holder claim “shall have first priority over any other claim, including over any expenses and claims that have priority under that subsection, to the extent compliance with section 4 of the GENIUS Act would have required additional reserves to be maintained.” The concluding limitation is the operative one for our purposes.

¹⁷ Administrative expenses are ordinarily first in line under 11 U.S.C. §§ 503(b), 507(a)(2). The concern in the administrative-insolvency literature is that a residual holder claim under § 507(e), combined with reserves that cannot fund a debtor-in-possession loan, leaves nothing to pay the professionals whose work the case requires.

¹⁸ GENIUS Act § 4(a)(1)(A)(i)–(viii) (permissible reserves: U.S. coins and currency and balances at a Federal Reserve Bank; deposits at insured depository institutions; Treasury bills, notes, or bonds with 93 days or less to maturity; overnight repurchase and reverse-repurchase agreements collateralized by Treasuries; shares of government money market funds invested solely in the foregoing; other similarly liquid federal assets approved by the primary regulator; and tokenized

may not be pledged, rehypothecated, or reused, whether directly or indirectly, unless they fall under one of a few narrow exceptions for margin, custody, and meeting redemptions.¹⁹ The reserve list and the no-pledge rule are distinct provisions, and it is worth citing them separately.

We note two consequences, both of which we infer from the text. First, reserves cannot be pledged as collateral for debtor-in-possession financing, because the no-pledge rule forecloses exactly that use. A distressed issuer therefore cannot borrow against its best assets to fund a reorganization, and neither can a trustee. Second, because the reserves are not the property of the estate, they should fall outside a surcharge under section 506(c), which lets a trustee recover collateral preservation costs from the collateral itself.²⁰ The reserves are walled off from the mechanisms bankruptcy uses to pay for its own administration.

It is worth dwelling on why the no-pledge rule matters so much. Consider the way that reorganizations are financed. A firm that files for Chapter 11 usually keeps operating on money borrowed after the filing, which a lender advances because it receives a lien or superpriority claim in exchange.²¹ The whole apparatus assumes there are assets to pledge. Strip out the issuer's Treasuries— forbid their use as collateral—and the machinery has nothing to run on. The distressed issuer has not merely rearranged its creditors, it has removed the fuel that a rescue would require, which is a large part of why the ordinary process cannot easily respond.

2.4. The Stay, the Courtroom, and Who Resolves the Firm

Three more provisions round out the bankruptcy architecture. Section 11(c) amends section 362 to add a stay on the redemption of coins from reserves and, alongside it, an expedited track by which holders can obtain relief, with the court directed to use best efforts to enter a final distribution order within 14 days of the required hearing.²² Holders are meant to be paid quickly, which reinforces the sense that the reserves belong to them and not to the estate.

Section 11(g) determines who runs the case. A depository institution is resolved by the FDIC, the NCUA, or a state regulator, in much the same way as for failed banks, credit unions, and thrifts. A subsidiary of a depository institution, or a nonbank issuer, may instead be treated as a debtor under

forms of the same). The FDIC has proposed to clarify that deposits held as reserves are insured to the issuer as a corporate depositor, without pass-through coverage to coinholders, so deposit insurance protects at most \$250,000 of a reserve pool held at any one bank. *See* 91 Fed. Reg. 18534 (Apr. 10, 2026).

¹⁹ GENIUS Act § 4(a)(2) (“Prohibition on Rehypothecation”): required reserves “may not be pledged, rehypothecated, or reused,” directly or indirectly, subject to narrow exceptions for margin on permitted repo, standard custodial obligations, and creating liquidity to meet redemptions.

²⁰ This is our inference, not a term of the act. Because excluded reserves are not the property of the estate, they should fall outside a surcharge under 11 U.S.C. § 506(c), and § 4(a)(2) independently forecloses pledging them to a debtor-in-possession lender. The act itself does not mention § 506(c).

²¹ Debtor-in-possession financing under 11 U.S.C. § 364 typically depends on offering the new lender a priming lien or a superpriority administrative claim. Section 4(a)(2)'s bar on pledging reserves removes the collateral a distressed issuer would otherwise pledge, and the § 507(e) claim sits ahead of any § 364(c) superpriority to the extent of a shortfall.

²² GENIUS Act § 11(c), amending 11 U.S.C. § 362 to add subsection (a)(9) (staying redemption of coins from reserves) and subsection (d)(5) (expedited relief, with the court to use best efforts to enter a final distribution order within 14 days of the required hearing).

Title 11.²³ This distinction turns out to be paramount, as it determines the path that the proceedings continue down. A private administrator can walk away from a case that cannot pay its fees, while a deposit insurer cannot. Section 11(f) adds a further wrinkle by requiring the Comptroller or the state regulator to raise, and to appear and be heard on, any issue in an issuer's Chapter 11, including customer protection.²⁴ A public official is thus already in the room, a fact we return to when we consider responses. Section 2.5 maps the permutations, because which regime governs which level of the group shapes the remedies discussed below.

One definitional point ties the structure to the banking system. Under the act, a bank-affiliated issuer must be an approved subsidiary of an insured depository institution, since the institution itself cannot be a permitted issuer.²⁵ A bank that wants to issue coins does so through a separate entity, funding that entity's reserves by moving assets down from the parent. That intra-group transfer is the hinge of the deposit insurer case. Altogether, the four features build a ring fence around reserve assets that is more protective of one creditor class, and more disruptive of the ordinary rules of distribution, than any modern federal priority statute. The rest of the article asks what a distressed firm does once that fence is available.

2.5. A Map of the Possible Structures

To be clear, the provisions described above do not operate on only one kind of firm. We therefore consider the form of the issuing entity and the form of its parent. An issuer can be an uninsured national trust bank—which is the charter that Anchorage Digital and Paxos hold and toward which much of the industry is converging—or an ordinary corporate entity, such as most fintech issuers. A parent can be an insured depository institution or an ordinary corporation. Crossing the two choices yields the four quadrants of Figure 1, and each quadrant pairs an insolvency regime at the parent with a different one at the issuer.

²³ GENIUS Act § 11(g) (codified at 12 U.S.C. § 5911): a depository institution is resolved by the FDIC, the NCUA, or a state regulator, while a subsidiary of a depository institution or a nonbank issuer “may be considered a debtor under title 11.” To be sure, “depository institution” under section 3 of the Federal Deposit Insurance Act is broader than “insured depository institution,” and only insured institutions are barred from issuing directly. An uninsured national trust bank, a federal branch of a foreign bank, or an uninsured state-chartered depository can itself be a permitted issuer through the federal- or state-qualified routes. Section 11(g)(1) speaks to those entities only imperfectly, because it names the FDIC, the NCUA, and the state regulators but not the Comptroller, whose Part 51 receivership regime currently governs a failed uninsured national bank. *See infra* Section 2.5.

²⁴ GENIUS Act § 11(f), adding 11 U.S.C. § 1109(c): the Comptroller of the Currency or the state payment stablecoin regulator “shall raise, and shall appear and be heard on, any issue, including the protection of customers,” in a Chapter 11 case in which the debtor is a permitted issuer.

²⁵ GENIUS Act § 2(23): a “permitted payment stablecoin issuer” is a subsidiary of an insured depository institution approved under § 5, a federal qualified issuer, or a state qualified issuer. An insured depository institution is not itself on the list and cannot be the issuer.

Figure 1. Insolvency Regimes by Corporate Structure

	Issuer: national trust bank	Issuer: other corporate entity
Parent: insured depository institution	A. Parent in FDIC/NCUA receivership; issuer in OCC receivership	B. Parent in FDIC/NCUA receivership; issuer in bankruptcy court
Parent: other corporate entity	C. Parent in bankruptcy court; issuer in OCC receivership	D. Parent and issuer both in bankruptcy court

Quadrant D is the fully private case, and it worries us most.²⁶ Both estates are administered under the Bankruptcy Code, by judges and trustees with no regulatory mandate, and every issue developed in Section 3—the avoidance clock, the coordination problem, the case nobody will fund—appears there in its purest form. It is also the quadrant where the most lightly supervised issuers sit.

The left-hand column is governed by an unusual framework. An uninsured national trust bank cannot be a debtor under the Bankruptcy Code at all, because it is resolved by a receiver the Comptroller appoints and directs under the National Bank Act. This regime follows the OCC’s Part 51 rules, a framework adopted in 2016 that is essentially untested. The OCC observed when it wrote the rule that it had not appointed a receiver for an uninsured bank since shortly after the FDIC’s creation.²⁷ (The GENIUS Act’s routing provision fits this column imperfectly. Section 11(g)(1) names the FDIC, the NCUA, and the state regulators, but it does not name the Comptroller, even though the national trust bank is the issuer form the market favors. How section 11(g) and Part 51 will mesh is an open question for the implementing rules, which are not yet final.²⁸)

The top row puts a regulator with a mandate at the parent. In particular, the FDIC or NCUA cannot decline the case. These entities bring examination knowledge to the cases they administer and hold avoidance tools of their own. Supervision that no bankruptcy court can provide also operates before any failure arrives. The map also hands creditors an instrument of their own: A lender who cannot stop its borrower from entering the stablecoin business can still bargain over which column the group occupies.

²⁶ We thank Howell Jackson for inspiring this quadrant-by-quadrant analysis. For an early argument that stablecoin issuance belongs inside regulated, administratively resolvable structures, see Howell E. Jackson, Timothy G. Massad & Dan Awrey, *How We Can Regulate Stablecoins Now—Without Congressional Action* (Brookings Hutchins Center on Fiscal & Monetary Pol’y, Working Paper No. 76, 2022).

²⁷ 11 U.S.C. § 109(b) (excluding banks from eligibility as debtors); 12 U.S.C. § 191 (making the FDIC the mandatory receiver only for an insured bank); 12 C.F.R. pt. 51 (OCC receiverships for uninsured national banks, providing a short priority ladder running from receivership expenses to unsecured creditors, subordinated creditors, and shareholders).

²⁸ GENIUS Act § 20 (the act takes effect on the earlier of 18 months after enactment, that is, January 18, 2027, or 120 days after the primary federal payment stablecoin regulators issue final implementing regulations). As of this writing, the agencies have issued only proposed rules.

3. The Mechanism: A Stablecoin Dropdown

3.1. The Liability Management Playbook, and Why a Statutory Version Is Different

A liability management exercise is an out-of-court restructuring in which a borrower uses the flexibility in its own debt documents to improve some creditors' position at the expense of others. The canonical example is the dropdown. In 2016, the retailer J. Crew moved its most valuable intellectual property into a subsidiary that its existing lenders could not reach, then borrowed fresh money against those assets, leaving the original lenders structurally subordinated to the new debt. The Serta Simmons uptier of 2020 achieved a similar result by a different route; a majority of lenders agree to elevate their own loans above those of the holdouts. A decade of hardball recapitalizations has followed, to the point that practitioners now speak openly of creditor-on-creditor violence.²⁹

A body of scholarship traces how these transactions reshape the secured-debt market, how creditor groups organize to attack or defend against them, and how an uneasy truce has begun to form as lenders learn to cooperate through carve-out arrangements rather than fight every deal to the finish.³⁰ The throughline of this literature is that the maneuvers are a product of the documents. These exploits exist because credit agreements left room for them. They are contested by reading those agreements closely and recede as the agreements are rewritten.

The law has been catching up. Courts police these transactions through the implied covenant of good faith, through ratable-treatment and sacred-rights clauses in credit agreements, and through the equitable-subordination power in section 510(c) of the Bankruptcy Code.³¹ There is evidence that the market itself adapts by demanding higher compensation or changes to contractual terms.³² The lesson of this body of work is that contractual maneuvers invite contractual and equitable answers. Better drafting, sharper covenants, and a willingness by courts to consider substance over form can and do blunt the next transaction.³³

²⁹ Buccola & Nini, *supra* note 11, find that loans originated after Serta became far more likely to block uptier transactions, while the frequency of dropdown-susceptible loans changed little after J. Crew, suggesting markets can price and contract around some of these maneuvers more readily than others.

³⁰ On the secured-debt dynamics and the emerging détente among creditor groups, see Antill, Jiang & Wang, *supra* note 10; Brett Seaton, *The Carveout Co-Op: A Truce in the Lender Wars*, WHARTON INITIATIVE ON FIN. POL'Y & REG. (May 16, 2025), <https://wffi.wharton.upenn.edu/blog/carveout-co-op/>. Sell-side research anticipated the continuation of these transactions. See BARCLAYS CREDIT RESEARCH, LME: TRADING THROUGH PRISONER'S DILEMMAS (2024); Sergio Padilla, *Barclays: Creditor-on-Creditor Violence to Continue*, PRIVATE DEBT INVESTOR (Aug. 8, 2024), <https://www.pei-privatecredit.com/barclays-creditor-on-creditor-violence-to-continue/>.

³¹ Compare *In re Serta Simmons Bedding, L.L.C.*, 125 F.4th 555 (5th Cir. 2024) (striking down an uptier), with *Ocean Trails CLO VII v. MLN TopCo Ltd.*, No. 2024-00169, 2024 WL 5248898 (N.Y. App. Div. Dec. 31, 2024) (upholding one). The divergence underscores how much turns on the language of the particular documents.

³² Baird, *supra* note 11; see also Yerak, *supra* note 10; Wirz, *supra* note 10 (documenting the growth of creditor-on-creditor aggression since 2020).

³³ On the courts' evolving treatment, see the litigation surrounding Serta Simmons and Mitel and the debate over implied covenants, ratable-treatment clauses, and equitable subordination under 11 U.S.C. § 510(c). Our point is comparative:

A stablecoin dropdown is different in kind because its authority comes from Congress. When a firm moves Treasuries into an issuing subsidiary and the reserves leave the estate, it is not exploiting a gap a lender forgot to close: It is exercising a right the GENIUS Act confers in express terms. Equitable subordination struggles against a clear federal entitlement, because sacred-rights clauses in existing credit agreements do not bind a priority that Congress, rather than the borrower, has created. And a challenge to the transfer as a fraudulent conveyance runs into the awkward fact that the recipient is a vehicle the act itself authorizes and encourages. The doctrines that discipline the private-law versions of this maneuver have little purchase here—exactly why the *ex ante* conduct we describe deserves more attention than the existing literature has given it.

There is an argument that contractual dropdowns may be beneficial to society, because they allow for flexible state-contingent renegotiation of debt contracts and avoid potentially costly bankruptcy proceedings.³⁴ But, for a stablecoin dropdown, the ability to renegotiate is much more limited, because the statute restricts the form of the contract and hands much of the bargaining power to the borrower. Thus, to the extent that contractual dropdowns improve social welfare, it is not clear that this argument can be extended to statutory stablecoin dropdowns.

3.2. Why the Usual Cures Fail

The claim that a statutory dropdown resists the ordinary remedies deserves to be tested against the four specific tools a subordinated creditor would reach for. The first three lose much of their force when the priority in question comes from an act of Congress rather than from a contract, while the fourth survives on paper, but is blunted instead by timing.

The first tool is a challenge under a fraudulent transfer doctrine. A creditor watching good assets leave the estate would ordinarily attack the transfer under section 548 of the Bankruptcy Code or its state-law analogues, arguing either that the debtor acted with actual intent to hinder or delay creditors or that it gave up the assets for less than reasonably equivalent value while insolvent.³⁵ Both theories struggle in this context.

The issuer that moves Treasuries into a subsidiary and issues coins receives the cash proceeds of the coin sale in return, then uses that cash to retire debt at par. On the face of the ledger, the estate has exchanged one asset for another of equal book value, which makes the reasonably-equivalent-value theory awkward to run. The actual-intent theory fares better in principle, and precision matters here. Federal law often protects the destination of a transfer without immunizing the transfer itself. For example, an eve-of-bankruptcy conversion of nonexempt assets into a protected retirement

These tools operate on contract language and debtor conduct and accordingly have less purchase on an express federal entitlement.

³⁴ See Antill, Jiang & Wang, *supra* note 10.

³⁵ See 11 U.S.C. § 548 (avoidance of fraudulent transfers, on either an actual-intent or a constructive theory requiring a transfer for less than reasonably equivalent value while insolvent) and the Uniform Voidable Transactions Act as adopted in the states. Transfers to insiders within the extended reach-back period, and transfers lacking a legitimate business purpose, remain the most exposed.

account remains avoidable on proof of intent to hinder or delay,³⁶ and the same logic applies to a transfer into a statutorily protected reserve. What shields the coin dropdown is proof rather than doctrine. The issuance looks routine, and since Congress has supplied a legitimate business purpose to recite, a court must tease intent out of a transaction the statute encourages on its face.

The second tool is equitable subordination. A court may, under section 510(c), subordinate a claim whose holder engaged in inequitable conduct that harmed other creditors; this is the inquiry associated with *Mobile Steel*.³⁷ The coins in our example, though, are held by ordinary purchasers who have done nothing wrong. The priority they enjoy was not engineered by the purchasers for their own benefit but was handed to them by statute. Asking a court to subordinate a claim that Congress placed first, on the ground that the issuer behaved badly in creating it, is asking equity to override an express statutory command.

The third tool is contractual. Lenders have for years written sacred-rights and ratable-treatment clauses into their credit agreements for the very purpose of blocking dropdowns and uptiers.³⁸ Those clauses bind the borrower. But they cannot bind a priority created by federal statute. A promise that no lender will be subordinated without its consent may hand the aggrieved creditor a breach claim against the issuer, but the breach claim does nothing to unwind the coin holders' statutory position, and if the issuer is insolvent, the breach claim against them is worth very little. The market's habitual answer to the last maneuver, tighter drafting in the next deal, cannot uphold a right that never came from a deal in the first place.

The fourth tool is preference law, which stands on different footing because the act does nothing to disturb it. The par repayment at the center of the swap is a transfer to creditors on account of antecedent debt, made while the firm is insolvent, which leaves them far better off than a liquidation would have. That is the textbook example of voidable preference under section 547(b).³⁹ Indeed, the voidable transfer is the repayment to the favored creditors; the recovery runs against them or the value they received, down to the coins themselves. The reserves are never touched, so the act's protection of the reserves is beside the point. The act alters none of the elements implicated by this area of law. If a petition arrives within 90 days of the repayment (or within a year where the favored creditors are insiders), the trustee avoids the payment and recovers the cash from them, regardless of what has

³⁶ Cf. 11 U.S.C. § 727(a)(2) (denying a discharge for transfers made with intent to hinder, delay, or defraud); *id.* § 522(o) (reducing a homestead exemption by amounts attributable to such conversions). The protection federal law gives the destination of a transfer does not determine whether the transfer into it was fraudulent.

³⁷ 11 U.S.C. § 510(c); *see In re Mobile Steel Co.*, 563 F.2d 692 (5th Cir. 1977) (subordination requires inequitable conduct that injured creditors or conferred an unfair advantage). Equitable subordination is remedial and claimant-specific, and courts have been reluctant to deploy it against priorities fixed by statute.

³⁸ Buccola & Nini, *supra* note 11 (documenting the sharp rise in anti-uptier protections in loans originated after *Serta*); *see also* Seaton, *supra* note 30.

³⁹ 11 U.S.C. § 547(b); *see also id.* § 550(a) (recovery from the initial transferee wherever the value has since traveled); § 502(h) (revival of the avoided claim); § 549 (avoidance of unauthorized transfers made during the gap period of an involuntary case); § 303(i) (sanctions for a failed involuntary petition). The repayment fits no § 547(c) defense, being neither a contemporaneous exchange for new value nor a payment in the ordinary course.

since happened to the coins; the avoided claims simply revive. The recovery also refills the estate, which blunts the administrator-starving problem developed below.

The maneuver is safe only once the preference window has closed, and because the act's own monthly disclosures will reveal an unusual issuance within weeks, the window is no dead letter. What protects the firm in practice is coordination. A dispersed creditor body must recognize a routine-looking issuance as the opening move of a dropdown, then organize an involuntary petition—which carries sanctions if it fails—all before the clock runs. The going-concern shield described below does much of that work for the firm, since every month of induced forbearance runs the clock in its favor.

None of this leaves a determined litigant helpless. A transfer executed on the eve of a filing, in favor of insiders, at a moment of obvious insolvency may still be vulnerable, especially as the regulator's statutory appearance right supplies a public objector with a seat at the table. But the doctrines that have slowly tamed the private-law dropdown were built to police the language of contracts and the conduct of debtors; they have far less to hold on to when the subordination is delivered by statute. This point of comparison is why the *ex ante* problem cannot be left—as the contractual analogy might tempt one to leave it—to litigation and the next round of covenants.

3.3. A Distressed Issuer

Consider a firm with the stylized balance sheet shown in Table 1. On a book basis it holds \$100 of assets, comprising \$75 in Treasury bills and \$25 in loans, funded by \$95 of debt and \$5 of equity. The loans have soured and are really worth only \$15. Once that loss is recognized, the firm is insolvent, its assets worth \$90 against liabilities of \$95. But for the moment only management knows about these impaired assets. Assume management wants to protect a favored subset of creditors—perhaps insiders or a lender whose continued support it needs—by maximizing what those creditors recover. Importantly, because the act confines a permitted issuer to the stablecoin business, a firm carrying impaired loans cannot issue coins itself, so the maneuver that follows runs through an issuing subsidiary, whatever the firm's charter.

Table 1. Distressed Balance Sheet

Assets	Liabilities
Treasury bills 75 (75)	Debt 95 (90)
Loans 25 (15)	Equity 5 (0)

Note: The first number in each cell gives the book value of each item. The second number in parentheses gives its economic value, that is, the value after recognizing the impairments on the loans.

3.4. The Debt-for-Stablecoin Swap

The firm now performs a dropdown using stablecoins. It moves the Treasury bills into a stablecoin-issuing subsidiary, has that subsidiary issue \$75 of stablecoins backed one-for-one by the bills, sells the coins to the favored creditors, and uses the \$75 in cash proceeds to pay down \$75 of the old debt. Tables 2a and 2b show where things stand afterward. The subsidiary holds the Treasuries against the coins it has issued. The parent has swapped \$75 of debt for the coin sale and is left with the impaired loans and \$20 of remaining debt.

Two features of the swap deserve emphasis. First, the favored creditors take part willingly, because the coins hand them a claim on the Treasuries worth far more than the impaired debt they surrender, so management can present the deal as a favor, free from coercion. Second, the transaction looks routine. From the outside, it is an ordinary issuance of a fully backed stablecoin—the very activity the act was written to promote—which lets the subordination hide in plain sight until the assets are already beyond reach. A remaining creditor who wanted to object would have to recognize a routine-looking issuance as the opening move of a dropdown, and to do so in time to act.

Table 2a. Issuing Subsidiary After the Dropdown

Assets	Liabilities
Treasury bills 75 (75)	Stablecoins 75 (75)

Table 2b. Parent Firm After the Dropdown

Assets	Liabilities
Treasury bills 0 (0)	Debt 20 (15)
Loans 25 (15)	Equity 5 (0)

Note: The first number in each cell gives the book value of each item. The second number in parentheses gives its economic value, that is, the value after recognizing the impairments on the loans.

3.5. Subordinating the General Creditors

The favored creditors now hold coins with a superior claim on the good assets. The left-behind creditors hold \$20 of debt backed only by loans worth \$15, so they absorb the entire \$5 loss. Compare the recoveries. Before the dropdown, every creditor shared a pool worth \$90 against claims of \$95, a loss of about 5.3 percent spread evenly across the group. After the dropdown, the favored creditors are made whole through their coins, and the remaining creditors face a loss of \$5 on \$20, or 25 percent. Management has chosen who bears the loss; while the losers can still force the firm into bankruptcy, by then their claims are worth a fifth less than they were the day before. This is the ordinary economics of a dropdown, reached here through the Bankruptcy Code rather than through a hole in an indenture.

It is worth being precise about which provision did the damage. The coins here are fully reserved, \$75 of Treasuries behind \$75 of coins, so there is no reserve shortfall and the section 507 superpriority never comes into play. The corporate structure is doing real work to subordinate the remaining creditors: Because the firm's losses sit in its loan book, it cannot be the issuer itself under the act's activities limitation.⁴⁰ Instead, the Treasuries leave the parent's estate by an ordinary intercompany transfer, the same structural subordination that powered J. Crew. The carve-out's

⁴⁰ GENIUS Act § 4(a)(7) confines a permitted issuer to issuing and redeeming payment stablecoins, managing the related reserves, providing custody, and activities that directly support them. A firm with an operating business therefore cannot be its own issuer. The same requirement is why the traditional distinction between a dropdown and an uptier dissolves here: Even an uptier, which classically requires no separate vehicle, would have to run through an issuing subsidiary. A standalone issuer—that is, one in the coin business and nothing else—would feel the exclusion directly, since the moment its Treasuries backed coins, they would leave its own estate under 11 U.S.C. § 541(b)(11). It is hard to see how such an issuer accumulates losses on the scale of our example, short of legal liability, operational failure, or losses on the reserve assets themselves, so we treat the corporate group as the general case.

contribution is quieter but no less essential. It guarantees that the coins pay in full even in the case of the subsidiary's own failure, ahead of the subsidiary's administrative expenses; that credibility is why the favored creditors accept coins at par rather than demanding a discount. Together with the no-pledge rule, it keeps the subsidiary permanently clean, so the dropped assets can never be borrowed against the way J. Crew's intellectual property was. And because the exclusion attaches to the reserves themselves rather than to any particular debtor's estate, it holds even if a court substantively consolidates the subsidiary with its parent, foreclosing the remedy that ordinarily polices structural subordination.⁴¹ The superpriority contributed nothing. The estate exclusion, by making the structure credible and consolidation-proof, did all of it.

Of note, the same transaction affects a second target: namely, the financing of any future case. Suppose that running a Chapter 7 or Chapter 11 case for this firm, when considering the payments for the trustee's work, counsel, and any other professionals an administration requires,⁴² would cost \$18 in fees and expenses.⁴³ Before the dropdown, the estate worth \$90 could absorb that cost and still return meaningful value to creditors. After the dropdown, the parent's estate is just the loans, worth \$15. (The subsidiary, if it ever filed, would have a case and an estate of its own; the shortfall here afflicts the parent.) In this scenario, there is no longer enough value to pay for the case's own administration, and the ring-fenced Treasuries cannot fund debtor-in-possession financing that might have bridged the gap, because they sit in a separate entity. Section 4(a)(2) would bar pledging them even in the subsidiary's own case.

The result is that nobody has an incentive to bring a case. A Chapter 7 trustee assigned the case must serve, but no trustee funds a deficit, and professionals asked to spend \$18 to recover \$15 would be working at a guaranteed loss that nothing in the estate can make up.⁴⁴ The remaining creditors could in principle fund the shortfall themselves, paying \$3 out of pocket for the privilege of a bankruptcy that returns them nothing, but no rational creditor would do so; indeed, no rational creditor would file the petition in the first place. The practical effect is that the firm becomes unresolvable through the ordinary process. The threat that the bankruptcy system represents—that the law will impose discipline on management—loses its force when management can discreetly make the system too expensive to invoke.

⁴¹ On the standards for substantive consolidation, see *In re Owens Corning*, 419 F.3d 195 (3d Cir. 2005). Because 11 U.S.C. § 541(b)(11) excludes required reserves from whatever estate they would otherwise enter, consolidating the issuing subsidiary into its parent's case would not return them to the common pool.

⁴² We use “administrator” in a loose, generic sense throughout: whoever runs and staffs an insolvency proceeding, meaning the trustee or debtor in possession and the retained professionals in a U.S. bankruptcy case, or the receiver in a bank resolution. No reference to the formal administrator of U.K. insolvency practice is intended.

⁴³ Samuel Antill, *Are Bankruptcy Professional Fees Excessively High?*, 37 REV. FIN. STUD. (2024). Table 2 suggests that our assumed ratio of expenses to liquidation value of 20 percent, \$18 on a \$90 estate, sits between the 75th and 90th percentiles of historic Chapter 7 cases, high but not unrealistically so.

⁴⁴ No-asset cases are routine in consumer Chapter 7 practice, where trustees serve for nominal compensation. The corporate problem is different in kind because a contested liquidation or reorganization needs funded professionals, and, unlike the deposit insurer, no private party is obliged to supply the funding.

3.6. The Going-Concern Shield

Management need not even carry out the dropdown to capture much of its value, as the threat is often enough. Return to the balance sheet in Table 1. Imagine that some creditors suspect there are unrecognized losses and are considering petitioning for bankruptcy. In response, management approaches a group of creditors holding \$20 of debt and explains, credibly, that it is prepared to subordinate them through a stablecoin dropdown exactly as described. Those creditors now face a choice: They can force the firm into bankruptcy today and, once the dropdown is executed or once the administrator problem bites, recover almost nothing, short of funding the uncertain avoidance litigation described in Section 3.2, or they can agree to write down \$5 of their claim, forbear, and let the firm continue in the hope that the loans recover. Faced with those options, rational creditors forbear. Forbearance also runs the preference clock described in Section 3.2, so the longer the threat holds, the safer the dropdown becomes to execute.

This forbearance may shake out in one of two ways. On one hand, it can avert a costly and value-destroying bankruptcy, which is sometimes exactly what a temporarily illiquid but fundamentally sound firm needs. On the other, it lets an insolvent firm continue under the same management and shareholders long after the point at which it should have been restructured or wound down. The act thus hands distressed firms a tool for keeping zombies alive, financed by creditors who forbear because the alternative is worse. Whether the net effect is benign depends on the firm, but the option to extend a doomed firm's life at creditors' expense is now written into federal law.⁴⁵

It is fair to ask which firms would actually reach for this. A large bank under close and continuous supervision may hesitate, wary that examiners will notice an unusual transfer, and mindful of the reputational cost of being seen to game a public backstop. A more lightly supervised issuer, such as a fintech or a state-chartered entity operating near the edge of the framework, faces fewer of those checks and is the likelier first mover. In the framework of Figure 1, the danger concentrates in quadrant D, where no banking regulator stands behind either level of the structure.

3.7. The Deposit-Insurer Case

If the mechanism is troubling when the disadvantaged creditor is a hedge fund or a trade lender, it is even more troubling when the creditor is a federal deposit insurer; this is where the stakes of the article are highest. Suppose the firm in the running example is an insured bank. It fails and is resolved not by a private administrator who can decline the assignment but by the FDIC, which is legally obliged to resolve a failed insured institution whether or not the estate can pay for it.⁴⁶

⁴⁵ Antill, Jiang & Wang, *supra* note 10 (showing that the net welfare effect can be positive where firms and creditors renegotiate efficiently after observing the state of the world).

⁴⁶ Federal Deposit Insurance Act § 11(d), 12 U.S.C. § 1821(d); for credit unions, see 12 U.S.C. § 1787.

Run the numbers with a resolution cost of \$33, higher than a private administrator's because deposit-insurance resolutions are more expensive to conduct.⁴⁷ The estate is worth \$15 after the dropdown. The FDIC recovers that \$15 and absorbs \$18 of loss, and the remaining creditors are wiped out. That shortfall falls on the Deposit Insurance Fund, whoever the remaining creditors are. If they are insured depositors, the fund must make them whole as well. Either way, the fund is replenished by assessments on other banks or, if it runs short, by borrowing from the Treasury. The recent precedent is the special assessment the FDIC levied on the banking industry after the 2023 failures, a reminder that resolution losses are mutualized across banks and, in the tail, across taxpayers.⁴⁸

Now recall that a bank cannot itself be the issuer and must use an approved subsidiary. If we take a consolidated view of the banking group, funding that subsidiary's reserves means transferring Treasuries (or other reserve assets) down from the parent bank. Those Treasuries would otherwise have been available to the FDIC in resolution. Moving them into the issuing subsidiary subordinates the deposit insurer, the Federal Home Loan Banks, and any uninsured depositors, in favor of whoever holds the coins. The transaction operates as an implicit subsidy running from the deposit insurer to the bank's shareholders, drawn upon at the worst possible moment and paid, in the end, by other banks and perhaps the public. Because a public resolver cannot walk away, the administrator-starving problem does not make the case disappear here. It converts, instead, into a transfer of losses onto the insurance fund. That is the variant the responses in Section 4 are chiefly designed to address.

Importantly, a failed insured bank is resolved under the Federal Deposit Insurance Act rather than the Bankruptcy Code, so section 547 and its 90-day clock never apply. The receiver is not helpless: If the failed entity is a national bank, a statute as old as the charter itself, section 91 of the National Bank Act makes "utterly null and void" any transfer or payment made after an act of insolvency, or in contemplation of it, with a view to preferring one creditor over another. Moreover, the Supreme Court has read the provision without a fixed lookback window and without any requirement that the recipient knew what the bank intended.⁴⁹

⁴⁷ Rosalind L. Bennett & Haluk Unal, *Understanding the Components of Bank Failure Resolution Costs*, 24 FIN. MKTS. INSTITUTIONS & INSTRUMENTS 349 (2015) (finding an average discounted resolution cost of 33.18 percent of assets for FDIC resolutions between 1986 and 2007).

⁴⁸ The FDIC recovered part of the cost of resolving Silicon Valley Bank and Signature Bank in 2023 through a special assessment on other insured institutions, a recent illustration of how resolution losses are mutualized across the banking system. See *Special Assessment Pursuant to Systemic Risk Determination*, FDIC (Apr. 17, 2026), <https://www.fdic.gov/deposit-insurance-assessments/special-assessment-pursuant-systemic-risk-determination>. For evidence that systemic banking crises have resulted in costs to taxpayers, see BAIRD WEBEL & MARC LABONTE, CONG. RSCH. SERV., R43413, COSTS OF GOVERNMENT INTERVENTIONS IN RESPONSE TO THE FINANCIAL CRISIS: A RETROSPECTIVE (2018), <https://www.congress.gov/crs-product/R43413>.

⁴⁹ 12 U.S.C. § 91 (derived from the National Bank Act of 1864); *National Security Bank v. Butler*, 129 U.S. 223 (1889) (holding that the bank's preferential purpose suffices, so the recipient's knowledge is unnecessary); *Mechanics Universal Joint Co. v. Culhane*, 299 U.S. 51 (1936) (recovering an insider's eve-of-failure withdrawal, while cautioning that ordinary-course payments to depositors are not recoverable merely because the bank proves insolvent). The FDIC as receiver also holds a fraudulent-transfer power, 12 U.S.C. § 1821(d)(17), reaching transfers by institution-affiliated parties and debtors of the institution made within five years with actual intent to hinder, delay, or defraud. For state-chartered banks, preference recovery depends on state receivership law. We thank Howell Jackson for pressing us on these authorities.

However, the receiver must prove that the bank acted with a view to prefer, where section 547 asks only for elements no explanation can rebut. The Court has cautioned that ordinary-course payments to depositors are not recoverable merely because the bank turned out to be insolvent. A GENIUS-blessed dropdown could survive a purpose test. The transaction is the very activity the statute invites, every step comes with a legitimate account of itself, and the preferential design must be teased out of conduct that looks like compliance. Thus, the gravest variant of the maneuver is the hardest to unwind after the fact (for reasons of proof rather than any absence of power) and still argues for stopping the transaction before it starts.

The subordination also stacks on top of preferences the law already grants. In a bank failure, a Federal Home Loan Bank has a superior lien, so the deposit insurer is often not first in line even before any coins are issued.⁵⁰ A stablecoin dropdown pushes the insurer further back still, layering a fresh carve-out over an estate that was already encumbered. Now consider that the numbers in the stylized example, though small, are meant to be read as proportions. Scale them to a mid-sized bank with tens of billions in reserve-eligible assets, and the amount a group could move beyond the insurer's reach, at the moment the insurer can least afford it, is not a rounding error. The uncomfortable feature of the deposit insurer case is thus that the maneuver is most damaging exactly where the balance sheets are largest and the public backstop is deepest, even if close supervision makes it least likely to be attempted there. Low-probability, high-severity risks are the ones prudential regulation exists to manage. A maneuver that transfers losses to the insurance fund at the worst moment is squarely of that kind.

4. Consequences and Responses

The harm to a single subordinated creditor is a matter of fair dealing and corporate governance. It would justify concern on those grounds alone. What moves the problem from a governance question to a regulatory one is that the maneuver has consequences beyond the parties to any single transaction. We examine those spillovers first, because they make the case for intervention, then turn to what a regulator might do when confronted with these problems.

4.1. Spillovers

Start with the most counterintuitive consequence. The threat we have described grows with a firm's holdings of the very assets the act—and prudential liquidity regulation more generally—treats as safe.⁵¹ Only Treasuries, deposits at insured institutions, and their close cousins can back stablecoins.

⁵⁰ The Federal Home Loan Banks already enjoy a statutory lien that primes other creditors, including the FDIC, in a member's failure. Stacking a stablecoin carve-out atop that regime compounds the subordination of the deposit insurer on a consolidated view of the group. *See* 12 U.S.C. § 1430(e). On the Federal Home Loan Banks as a standing, collateralized source of government-backed liquidity whose claims shift losses to the insurer and other creditors, see Kathryn Judge, *Three Discount Windows*, 99 CORNELL L. REV. 795 (2014).

⁵¹ For example, the liquidity coverage ratio requires covered banking organizations to hold high-quality liquid assets against projected 30-day net cash outflows. *See* 12 C.F.R. pt. 249. Among other things, banks may also hold high-quality liquid assets to meet the net stable funding ratio, to reduce risk-based capital requirements, to have collateral eligible to be placed

Therefore, only a firm holding those assets can perform a coin dropdown, and the larger its stock of those safe assets, the more it can move beyond creditors' reach. A balance sheet that looks safer by the usual measures is, for this purpose, more dangerous, because it is precisely the safe assets that can be spirited into the ring fence. While the conventional intuition is that liquid, high-quality balance sheets are more stable, the relationship runs backward here.

There is a related perversity in how a firm might try to reassure its creditors. The most credible way to promise that one will never perform a coin dropdown is to hold few assets capable of backing coins. A firm taking that route would deliberately shift out of Treasuries and deposits and into lower-quality, less liquid holdings—worsening its own resilience in order to signal restraint. A rule meant to promote safe assets can thus push some firms away from them and can leave a firm less able to raise liquidity in a hurry when it most needs to.

The effect on funding costs cuts in two directions depending on who ultimately bears the loss. In situations where a private administrator would run an ensuing bankruptcy, wary creditors see the dropdown coming and demand more compensation up front for the risk of being subordinated. Once management can hand-pick winners, creditors must price the risk of being a loser, and the general cost of credit to permitted issuers rises. A firm that cannot bind itself against a future dropdown pays for that inability in its cost of capital, even if it never intends to use the tool, a standard commitment problem.⁵² Where a public resolver stands behind the firm, the sign can flip. Creditors who believe that losses will fall on the deposit insurer rather than on them demand less compensation, which channels funding toward insured institutions that can play this game and encourages them to lever up. The compression is partial, because a creditor enjoys the subsidy only if she ends up among the favored, so she discounts it by the odds of being chosen, and both forces operate at once. In the first case, the act taxes honest firms; in the second, it can subsidize risk.

Two further consequences deserve a mention. First, the going-concern shield keeps insolvent firms alive past the point of efficient resolution, adding to the stock of zombie firms whose continued operation ties up resources and depresses healthier competitors. At the same time, the ability to choose which creditors are made whole erodes the *pari passu* norm (the expectation that similarly situated creditors are treated alike), which underpins a great deal of ordinary lending. Each channel above also operates most powerfully when a firm is already close to failure, so the act's side effects arrive at exactly the moment when a bad situation is easiest to make worse.

The risk of dropdown makes firms more subject to runs. When short-term creditors, especially uninsured depositors, come to understand that a distressed issuer can subordinate them without warning, the rational response is to run at the first sign of trouble rather than wait to be picked as a loser. Even worse, a faster run is a more destabilizing one. Moreover, as we have shown, creditors

at the Federal Reserve's discount window and other liquidity facilities, and to be able to meet margin calls on derivative transactions.

⁵² The commitment problem is standard in the pricing of subordination risk. A firm that cannot bind itself against a future dropdown must compensate creditors *ex ante* for the option it retains, which raises its cost of capital even if it never exercises the option.

may be more concerned about firms that hold *more* liquid assets on their balance sheets. As a result, such firms may actually become more vulnerable to a run, contrary to standard banking theory.⁵³ This state of affairs could lead to perverse incentives. For example, a firm close to insolvency may seek to reduce its asset liquidity in order to reassure creditors about the risk of a stablecoin dropdown, even though doing so worsens the consequences of a run if it does occur. Furthermore, the consequences do not stay inside a single firm because runs at one depository institution may cause fire sales of eligible reserve assets and make depositors at others more prone to flight. The resolution of one bank through a special assessment on the others already shows how a single failure is shared across the system. A tool designed to be used quietly by one firm thus raises the temperature for the whole class.

There are also consequences for the fiscal picture. Supporters of the act have argued that stablecoin growth will create a large, stable source of demand for short-dated Treasuries that lower the government's funding costs.⁵⁴ Even granting that claim, the analysis here identifies an offsetting cost. The same Treasury holdings that generate the demand also raise the expected cost of resolving failed issuers, which lands on the public balance sheet at the exact moment when the banking system is under stress. A benefit measured in basis points on Treasury issuance must be set against a contingent liability that materializes in bad states of the world, when public money may be scarcest.

Finally, we observe that none of these consequences depend on stablecoins being used as money. Even if there is zero monetary demand for stablecoins, a firm can still carry out a dropdown and place stablecoins with creditors that it wishes to make senior. This distinguishes our concerns from those expressed elsewhere in the literature, which typically assume that there is some demand to hold stablecoins for monetary purposes.

4.2. Responses

A workable response should meet three conditions. It should preserve the act's central promise that coins are safe for the people holding them—the no-questions-asked quality that lets a stablecoin function as money.⁵⁵ It should protect existing creditors, and above all the deposit insurer, from being unexpectedly subordinated. And it should be capable of implementation by regulators under existing authority wherever possible, since a fix that requires Congress to reopen the act is a fix that may never arrive.⁵⁶ We canvass several options against those criteria before recommending a combination.

⁵³ Douglas W. Diamond & Philip H. Dybvig, *Bank Runs, Deposit Insurance, and Liquidity*, 91 J. POL. ECON. 401 (1983). In the classic model, banks with more liquid assets are less vulnerable to runs. That logic can break down when creditors fear being subordinated by a stablecoin dropdown.

⁵⁴ Cf. Secretary Bessent's contention (2025) that GENIUS Act reserve demand will support the market for short-dated Treasuries. See also Nellie Liang & Brent Neiman, *Stablecoins After GENIUS: Private Money, Public Debt, and the Global Dollar*, in *THE AMERICAN ECONOMY IN A NEW ERA* (Melissa S. Kearney & Luke Pardue eds., 2026).

⁵⁵ Gary B. Gorton & Jeffery Y. Zhang, *Taming Wildcat Stablecoins*, 90 U. CHI. L. REV. 909 (2023).

⁵⁶ For a complementary regulatory agenda under the act, trained on making payment stablecoins trusted money rather than on strategic issuance, see LIANG & DUDLEY, *supra* note 5.

4.2.1. Policies to Regulate New Stablecoin Issuance

Our first group of policies places constraints on a firm's ability to issue new stablecoins and sell them externally. These aim to blunt the ability of the firm to perform a dropdown quickly upon learning of upcoming distress and make the maneuver more visible to stakeholders, such as creditors and supervisors.

A *lockup* requires newly issued coins to be held by the issuer for a period, say, a year, before they can be transferred to outside holders. An *entry restriction* is a weaker cousin, barring a newly chartered issuing entity from issuing externally for its first year. Both throw sand in the gears; though both can be dulled by a firm that sets up its issuer and stockpiles capacity well in advance, to do so would send its own signal to stakeholders.

A third option prohibits debt-for-coin swaps outright, barring issuance of coins to existing creditors of the issuer or its affiliates. Although this option is easily evaded, because a creditor can be repaid in cash and then buy freshly issued coins a moment later, it does raise the cost and the visibility of the maneuver.

4.2.2. Policies to Regulate the Transfer of Value to a Stablecoin Issuer

A fourth option constrains the intra-group transfer that makes the bank case possible. Full-value compensation is the natural first leg, requiring an issuing subsidiary to pay its parent in cash or other high-quality assets when the parent funds its reserves. Even compensation in the form of equity in the issuer can deliver value for the parent's creditors, though only to the extent that the issuer holds more than it owes. Standing alone, though, this option does not reach the transaction described in Section 3 above, where the parent received full value in cash then stripped the estate through the repayment of favored creditors at par. The constraint therefore needs a second leg restricting what a troubled parent may do with the proceeds, barring distributions and debt repayments funded by coin issuance while the parent's condition is impaired. The combined effect is to prevent valuable assets from being moved beyond the reach of the parent's creditors.

Banking law already has a template in the form of its brokered deposit rules, which cut off a funding channel Congress judged too dangerous for banks that are less than well capitalized.⁵⁷ A parallel rule keyed to the parent's capital category would be familiar to supervisors and administrable with tools they already use. Resolution planning supplies a second template. The largest banking groups already maintain prepositioned resources and legally binding secured support agreements, built so that intra-group transfers in distress are pre-committed, collateralized, and defensible against later challenge.⁵⁸ An analogous instrument for stablecoin groups, adopted as a condition of approval, would bind the parent and the issuing entity in advance to full-value compensation and to limits on

⁵⁷ 12 U.S.C. § 1831f; 12 C.F.R. § 337.6 (barring banks that are less than well capitalized from accepting brokered deposits).

⁵⁸ Resolution plans are required by 12 U.S.C. § 5365(d) and implemented at 12 C.F.R. parts 243 and 381. On prepositioning and secured support agreements, see Final Guidance for the 2019 and Subsequent Resolution Plan Submissions by the Eight Largest, Complex U.S. Banking Organizations, 84 Fed. Reg. 1438 (Feb. 4, 2019). We thank Michael Hsu for the suggestion.

distressed-period distributions, converting this option from an after-the-fact rule into a standing contract a receiver can enforce.

Notably, this option may also be less reliant on the passage of new law than one might think, at least where the parent is an insured bank. Sections 23A and 23B of the Federal Reserve Act, implemented by the Board of Governors' Regulation W, cap a bank's covered transactions—including extensions of credit, investments in securities, and purchases of assets—with any one affiliate at 10 percent of the bank's capital. It also caps covered transactions with all affiliates together at 20 percent, require credit exposures to an affiliate to be fully collateralized, and require that sales of assets between a bank and its affiliates occur on market terms.⁵⁹ A bank's own operating subsidiary is treated as part of the bank rather than as an affiliate, so transfers into an issuing subsidiary the bank controls fall outside the regime entirely.⁶⁰ The Board may determine, by regulation or order, that a particular subsidiary should not be excluded from the definition; as a result, it could make that determination for stablecoin-issuing subsidiaries as a class.⁶¹ That single definitional choice would cap the scale of reserve funding at a fraction of the bank's capital, force full-value compensation whenever the parent sells Treasuries down to the issuer, and collateralize any credit the bank extends to it. Much of this option, in other words, waits on a determination by the Federal Reserve Board of Governors.

The agencies' implementing proposals of the GENIUS Act sharpen our point. Each agency has proposed a standard requiring an issuer's transactions with insiders and affiliates to be non-detrimental and conducted on market terms. But the standards guard the issuer rather than the parent's estate, diverging on the one channel we have emphasized. The OCC's version contains no exception for the parent, and the NCUA defines insiders to include a parent company; meanwhile, the FDIC's version expressly excludes transactions with the parent bank.⁶² The agency whose insurance fund bears the loss in our gravest case is, for now, the one that has exempted the parent-to-issuer leg. And none of the three proposals reach for quantitative limits, collateral requirements, or pre-committed support agreements, so the tools canvassed above remain on the table.

⁵⁹ 12 U.S.C. § 371c(a)(1)(A)–(B) (capping the aggregate amount of covered transactions at 10 percent of capital stock and surplus for any one affiliate and 20 percent for all affiliates); *id.* § 371c(b)(7) (defining covered transactions to include extensions of credit to an affiliate, investments in its securities, and purchases of its assets); *id.* § 371c(c)(1) (requiring collateral of 100 to 130 percent of the exposure, depending on collateral type, for credit transactions); 12 U.S.C. § 371c-1(a)(1) (requiring terms substantially the same as, or at least as favorable to the bank as, those prevailing for comparable transactions with nonaffiliates); 12 C.F.R. §§ 223.11–223.14, 223.51. Sections 23A and 23B apply of their own force to member banks and are extended to insured nonmember banks by 12 U.S.C. § 1828(j).

⁶⁰ 12 U.S.C. § 371c(b)(2)(A) (excluding from the definition of affiliate any company, other than a bank, that is a subsidiary of the bank); 12 C.F.R. § 223.2(b). The exclusion does not extend to financial subsidiaries, which are deemed affiliates of the bank. 12 U.S.C. § 371c(e)(1)–(2).

⁶¹ 12 U.S.C. § 371c(b)(1)(E) (authorizing the Board, by regulation or order, to treat as an affiliate any company whose relationship with the bank could cause covered transactions to work to the bank's detriment); *id.* § 371c(b)(2)(A) (making the operating-subsidiary exclusion expressly subject to such a determination). The Board's general rulemaking and exemptive authority, *id.* § 371c(f), cuts in the opposite direction and would need to be exercised with care.

⁶² Compare Proposed 12 C.F.R. § 15.13(a)(6), 91 Fed. Reg. 10202 (Mar. 2, 2026) (OCC; no exception for the parent), and Proposed 12 C.F.R. § 706.204(a)(6), 91 Fed. Reg. 28956 (May 18, 2026) (NCUA; defining insiders to include a parent company), with Proposed 12 C.F.R. § 350.6(a)(5), 91 Fed. Reg. 18534 (Apr. 10, 2026) (FDIC; excepting transactions with “the parent IDI of which it is a subsidiary”). A market-terms rule would not have stopped the transaction in Section 3 in any event, because the parent receives full value in cash.

4.2.3. Prudential Supervision

There are two entry points for prudential supervisors: regulation of the issuing entity and, if relevant, regulation of the parent. We suggest a capital requirement for the issuer, a tool the act already instructs regulators to design.⁶³ A minimum equity requirement shrinks every dropdown mechanically, because a subsidiary holding \$75 of Treasuries (in our example above) would be able to place less than \$75 of stablecoins. In addition, we propose that a minimum amount of this equity must be retained by the parent and not sold externally. This keeps the parent's creditors exposed to the good assets, because the parent's equity claim on a solvent, overcollateralized issuer has real value that stays in the estate. Of note, in pending proposals, the OCC would impose fixed and tailored capital requirements on issuers, with consequences keyed to condition, so that an issuer failing to meet the requirements would be barred from net new issuance; persistent failure would force an orderly wind-down of the coin.⁶⁴ However, no proposal yet requires the parent to retain the equity slice rather than sell it.

The GENIUS Act stipulates that regulators play an important role in approving the establishment of new permitted payment stablecoin issuers (PPSIs).⁶⁵ This approval process provides an opportunity to impose our suggested policies. For example, regulators could require any new PPSI to impose lockup periods and fully compensate the parent for any assets transferred.

Depending on the corporate form of the parent, it may have its own supervisor, especially if it is an insured depository institution. Thus, our final policy option relies on prudential examination of the parent, asking regulatory agencies to police strategic transfers through ordinary examination. Supervision has the virtue of being available now; its main drawback is that it bites only before the transfer, since, once the high-quality assets are in the ring fence, the act makes them very hard to recover.

One specific example in the case of banks is whether the issuer's assets should be included in calculating the liquidity coverage ratio (LCR) for the consolidated entity. In their pending implementing proposals, the OCC and FDIC have asked precisely this question, down to whether the parent should instead carry a small outflow add-on for the possibility that it supports the issuer, and whether the same treatment applies to the net stable funding ratio.⁶⁶ Our answer is that assets against

⁶³ GENIUS Act § 4(a)(4) (directing the primary federal payment stablecoin regulators, and state regulators for state-qualified issuers, to establish capital, liquidity, and risk-management requirements tailored to issuers' business models).

⁶⁴ *See* 91 Fed. Reg. 10202 (Mar. 2, 2026) (proposing fixed minimum and tailored capital requirements and an operational backstop for permitted issuers, with suspension of net new issuance on breach and orderly redemption on persistent breach).

⁶⁵ 12 U.S.C. § 5904.

⁶⁶ Office of the Comptroller of the Currency, Notice of Proposed Rulemaking Implementing the GENIUS Act, 91 Fed. Reg. 10202 (Mar. 2, 2026), Question 87; FDIC, GENIUS Act Requirements and Standards for FDIC-Supervised Permitted Payment Stablecoin Issuers and Insured Depository Institutions, 91 Fed. Reg. 18534 (Apr. 10, 2026), Question 59. Both ask whether the LCR and NSFR rules should be amended so that depository institutions cannot count high-quality liquid assets held by issuer subsidiaries, whether the subsidiary's activities should be excluded entirely, and whether a limited outflow of 1, 5, or 10 percent of outstanding issuance should apply instead.

which the issuer has issued stablecoins should not count toward either ratio at the parent.⁶⁷ This paradigm would have the benefit of limiting the transfer of high-quality assets away from the parent in a dropdown.

4.2.4. Policy Recommendations

Our recommendation is to layer three of these options rather than to hunt for a single cure. Combine the constraint on intra-group transfers, implemented through pre-committed support agreements; the issuer capital requirement, which shrinks every dropdown mechanically and limits risk transfer; and a regulator-administered version of the lockup, which slows opportunistic issuance across the board. The deposit insurer variant is the most consequential form of the problem, but it is also the most reachable, because each of these measures lie within the banking agencies' existing authority.

To be sure, none of these measures is costless. A lockup delays the point at which a new issuer can put its coins to work, which is a real burden on an honest entrant and represents a drag on competition in a market the act was meant to open. A transfer constraint adds friction to intra-group funding that banking groups may use for entirely legitimate reasons. The capital requirement traps equity that an honest group would rather deploy elsewhere inside the issuing entity. We think these costs are modest when weighed against the harm they head off. Furthermore, each can be fine-tuned—for example, a shorter lockup or a threshold below which transfers are unconstrained—so that the friction falls mainly on the transactions that raise concern. The alternative, waiting for a failure to reveal the gap and then legislating in the aftermath, is the more expensive course.

One other measure stands apart, which we would single out for legislative rather than regulatory attention. Placing the deposit insurer on an equal footing with—or even senior to—stablecoin holders for the recovery of resolution costs in the consolidated group is the first-best answer to the gravest case, because it neutralizes the incentive at its source instead of merely raising the cost of acting on it. No amount of supervisory diligence fully substitutes for a solution that goes to the source. It requires reopening the act, which is why we do not hinge our recommendations on this point, but it belongs on the agenda whenever the statute is next revisited. Noting that the best and most effective solution would come from the legislature also carries a lesson for future governments considering this exact situation. Other jurisdictions are now drafting their own stablecoin regimes with the advantage of a blank page; they would be wise to seat the public insurer level with holders from the start, sparing themselves the retrofit the United States now faces.

A final word on timing. The act instructs the banking agencies to study the insolvency of stablecoin issuers and to report within three years. That study is the natural vehicle for several of the measures above.⁶⁸ The study's framing, though, is trained on whether holders are paid and whether

⁶⁷ In our view the answer follows from existing law, because eligible assets must be unencumbered and assets held at a consolidated subsidiary count only to the extent of the subsidiary's own outflows plus what is freely transferable. *See* 12 C.F.R. §§ 249.3, 249.22(b). Regulators should be explicit to avoid any doubt.

⁶⁸ GENIUS Act § 11(h) directs the primary federal payment stablecoin regulators to study the potential insolvency proceedings of permitted issuers, including existing gaps in the bankruptcy laws, and to report within three years. The study is framed around holder payout and orderly administration, not the ex ante conduct this article addresses.

cases can be administered, the two ex post questions the existing literature has already raised. The final rules the agencies must now write are another channel, but they have not yet asked about the transfer channel this article identifies.⁶⁹ If the study is to be useful, it should be widened to take in the ex ante conduct described here, because the cheapest moment to close this gap is before the first strategic issuance rather than after it.

5. Conclusion

Criticism of the GENIUS Act's bankruptcy provisions has so far run along two axes. One camp doubts that stablecoin holders will always be paid, ranking them well below the secured lenders and financiers who come first in a real case. Another doubts that a failed issuer can be administered at all, given reserves that cannot fund a reorganization and a superpriority that sits above the trustee's fees. Both camps are looking inside the bankruptcy, at the wreckage after a firm has filed.

This article has added a third axis, one that runs both before and outside bankruptcy. Moreover, it applies even when there is no demand for stablecoins from investors. A distressed issuer, or a parent that controls one, can use the act of issuing coins as a weapon against its own creditors, moving its best assets beyond their reach, deterring them from forcing a filing, and draining the value a future administrator would need to resolve the estate. The tool works because reserves leave the estate the instant they back a coin, and it works whether or not the celebrated superpriority is worth anything. The gravest version arrives when the subordinated creditor is the deposit insurer, implicating the public along with it. The paradox is that the danger grows with the very holdings of safe assets that much of the edifice of post-2008 prudential regulation was written to encourage.

There is a lesson here that extends far beyond stablecoins. Each time Congress grants one class of claimant a hard statutory priority in the name of making its claims safe, it creates an incentive for a distressed firm to route value toward that class and away from everyone else. The safer the favored claim is made, the more valuable it becomes as a destination for a firm's best assets on the way out the door. Depositor preference, the Federal Home Loan Banks' lien, and now the stablecoin carve-out all share this shape. The safe harbors that lift derivatives counterparties out of the automatic stay drew the same criticism a decade ago, for the same reason.⁷⁰ Designing a priority for the class one wants to protect is only half the task. The other half is anticipating how a firm in trouble will use that priority against the classes left behind, which is the half the GENIUS Act skipped.

Thus, we recommend holding the issuing entity to a real capital requirement; binding parent and issuer in advance to full-value compensation through the support agreements that resolution planning has normalized; confirming that ring-fenced reserves count toward no one else's liquidity; and slowing opportunistic issuance with a lockup a regulator can administer.

⁶⁹ See 91 Fed. Reg. 10202, Question 207 (asking whether the OCC should adopt rules implementing the act's insolvency provisions and whether issuers should be required to prepare resolution plans); *id.* at Question 87; 91 Fed. Reg. 18534, Questions 30, 33, 59 (bankruptcy-remote structuring and liquidity treatment).

⁷⁰ See Patrick Bolton & Martin Oehmke, *Should Derivatives Be Privileged in Bankruptcy?*, 70 J. FIN. 2353 (2015); Mark J. Roe, *The Derivatives Market's Payment Priorities as Financial Crisis Accelerator*, 63 STAN. L. REV. 539 (2011).