Statement for the Record

On behalf of the

American Bankers Association

before the

Committee on Banking, Housing, and Urban Affairs

June 30, 2020

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The American Bankers Association[1] (ABA) appreciates the opportunity to submit a statement for the record for the hearing titled "The Digitization of Money and Payments."

America's banks support the goal of providing inclusive financial services that can help our country recover from the Novel Coronavirus (COVID-19) pandemic. Banks have played a critical role in delivering much needed stimulus and are supporting their customers and communities affected by the pandemic.

However, we have serious concerns that proposals to assign every American one or more "FedAccounts" backed by novel "digital dollars" will not help achieve this goal and would instead introduce unintended consequences that could undermine our economic recovery and threaten the stability of the banking system without contributing meaningfully to economic inclusion.

While we are strongly in support of electronifying payments, that technology is already in use today and we are in the midst of revolutionary growth in access to a growing number of options. Consumers and merchants value *choices*, from cash to mobile payments, and displacing those choices with a so-called digital dollar would be a costly solution in search of a non-existant problem. For those consumers and merchants left behind, such as those who prefer cash, the costs of this experiment would be high.

We are in the strongest possible agreement with the intent of these proposals – improving the speed and accessibility of mainstream electronic payments options. There are exciting developments on those fronts and we urge the committee to join with us in promoting the growth these options which are coming into the marketplace as we speak. That is a faster and surer solution than reinventing our currency and turning the Federal Reserve from the lender of last resort to the default banker for the majority of Americans.

[1] The ABA is the voice of the nation's $18.7 trillion banking industry, which is comprised of small, midsized, regional and large financial institutions. Together, these institutions employ more than 2 million people, safeguard $14.6 trillion in deposits and extend more than $10.5 trillion in loans.

A disruptive federalization of the banking system introduces serious risks to monetary policy, financial stability, credit availability, and financial inclusion. There is important work already underway to ensure all Americans have access to both basic and innovative banking services including real-time payments. Congress can best support pandemic relief efforts and future rounds of stimulus payments by supporting these initiatives.

Though Central Bank Digital Currency (CBDC) pilot programs are underway in China, the European Union, and elsewhere with the goal of eliminating cash, our own central bank has wisely declined to be pressured into premature action or participate in an arms race with nations that have vastly different economic and monetary systems than the United States.[2] Those central banks operating pilots (e.g. Peoples Bank of China) operate under far more plenary mandates than than the focused mission given to the Federal Reserve by Congress. It is important that this debate not be driven by fear of America "missing out" on CBDC. We would hardly be alone: several of the largest developed nations have passed on pursuing the CBDC project. In fact, given our advanced payments sytems, there is little compelling reason to believe that any vague benefits would outweigh the clear costs. The potential cost to inclusion that would come with the displacement of cash is an area that requires particularly thoughtful study.

Banks Have Been a Critical Delivery Mechanism for COVID Relief

As the coronavirus continues to impact communities across the country, America's banks have stepped up to assist individual and business customers affected by the pandemic, as well as the communities they serve. Banks have developed numerous programs to help their customers and acted as a critical delivery mechanism for government stimulus programs designed to help those impacted by this health crisis.

Banks are helping consumers access their Economic Impact Payments.

Digital tools have been a key factor in the unprecedented speed and efficiency of the Economic Impact Payments (EIP) program, and many of these innovations, including remote account opening, remote check deposit, and real-time payments continue to evolve to ensure a more inclusive, accessible, and secure banking ecosystem. Banks have worked hard to ensure the safe and secure delivery of $512 billion in EIPs to more than 159 million Americans under the CARES Act. More than 80 million EIP recipients received their payment electronically on the first day of the program.[3]

This is significantly more efficient than past stimulus payments. It took Treasury just two months to deliver the 159 million payments. The last time a similar effort was undertaken in 2009 it took over two months to deliver 800,000 payments. The majority of the payments this year were made electronically with 120 million delivered by direct deposit and 4 million in the form of a prepaid card.

ABA encouraged Treasury to maximize the use of electronic payments by leveraging all existing government data sources to identify eligible recipients with deposit account information on file and by creating a web portal to allow individuals not in those systems to upload their direct deposit information and promoted

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[2] https://www.economist.com/finance-and-economics/2020/04/23/china-aims-to-launch-the-worlds-first-official-digital-currency

[3] https://home.treasury.gov/news/press-releases/sm1025

that portal once it was established. We also worked with the FDIC and others to promote remote account opening offerings, including those that could be funded initially with an EIP.

Banks are also working to help check recipients access their EIPs. They are creating "safe" and socially distant ways to cash checks. In addition, a number of banks have committed to cash stimulus checks for noncustomers for free.

ABA agrees, however, that improvements can be made to deliver even more payments electronically and to move those electronic payments even more quickly by leveraging existing real-time payments and other capabilities. We have committed to working closely with the Department of Treasury to consider these changes for future rounds of stimulus payments.[4] In addition, ABA has worked with other banking trade associations and with consumer and public interest groups to seek legal clarity that stimulus payments are critical economic relief and should not be subject to garnishment.[5]

Banks have been central to delivery of Paycheck Protection Program funds.

Banks have also played a central role in delivering the Paycheck Protection Program (PPP) loans designed to give businesses the resources to keep their workforce employed through the pandemic. As of June 8, the PPP has delivered 4.5 million loans worth $512 billion at an average size of $113,000.

Banks' presence in their community and their strong balance sheets enabled them to quickly move to get these funds where they were most needed. In the first round of the program, banks accounted for 93.7% of all PPP loans. While full cumulative data is not yet available, banks account for 81.7% of loans made by institutions under $1 billion.[6]

One factor that contributed to banks' swift response is their balance sheet driven model. While market-funded lenders had to wait for new funding facilities, many banks were able to leverage their deposit funding to begin funding loans right away. If digital dollar proposals were successfully implemented, they would severely limit the kind of deposits that made this swift action possible.

Banks are working with their customers.

In addition to their role in delivering government stimulus, banks have provided unprecedented assistance to customers affected by the pandemic. The relief, which varies by institution and depends on a customer's individual circumstances, includes (but is not limited to):

- Offering hardship programs
- Waiving certain fees
- Deferring loan payments
- Providing temporary credit lines

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[4] May 13, 2020, Joint Trade Association letter to Treasury Fiscal Assistant Secretary David Lebryk.

[5] May 26, 2020, Press Release, Consumer, Banking Groups Applaud Bill to Exempt Economic Impact Payments From Garnishment,

[6] https://www.nber.org/papers/w27095

- Modifying loans
- Helping customers use mobile and digital banking platforms
- Alerting customers to scams related to the coronavirus
- Offering “safe” banking services by expanding drive-through and ATM operations
- Establishing “Golden Hours” when at risk individuals such as seniors can bank in a branch with less risk of exposure to the virus

Implementation of a digital dollar would not help deliver COVID aid.

The implementation of a digital dollar cannot be accomplished by flipping a switch and would take far too long to have any impact on the COVID recovery. Before the Federal Reserve could unveil a digital dollar, they would have to carefully consider the implications to the monetary and banking systems and build the infrastructure and expertise to operate a consumer-facing bank.

The Monetary Control Act and the Federal Reserve’s longstanding policy regarding the provision of payments services requires the Federal Reserve to meet three criteria when considering offering a new service. The basic requirements are:

1. Full recovery of costs over the long run.
2. The service will provide a clear public benefit.
3. The service should be one that other providers alone can’t be expected to provide with reasonable scope, effectiveness, and equity.

Banks are Committed to Financial Inclusion; Digital Dollar Proposals Would Undermine those Efforts

A foundational goal of digital dollar proposals (and similar proposals like postal banking) are to promote financial inclusion and to give more Americans access to fast payments. America’s banks are committed to promoting financial inclusion. Access to banking services provides people with a means to save for their future and economic opportunity that is critical to promoting social equality. This is an important and urgent goal; however, by taking too narrow a view of the problem, digital dollar proposals risk undermining these efforts.

ABA and its member banks are leveraging new digital tools to bring more Americans into the banking system.

Digital dollar proposals focus solely on the question of access to a deposit account. While it is true that deposit accounts are often the first step towards inclusion, 95% of U.S. households already have access to a bank account or prepaid card account.[7]

[7] 2017 (most recent) FDIC National Survey of Unbanked and Underbanked Households. which shows that 93.5 percent of households have a checking or savings account (page 2) and an additional 26.9 percent of the unbanked have a

The U.S. rate of inclusion positions the U.S. as a global leader in financial inclusion, but it is not good enough, and there is work to be done. Banks are committed to continued investments to ensure all Americans have access to the banking system.

Today, unbanked customers have numerous options to open bank accounts. ABA has worked collaboratively with the FDIC and BankOn[8] to publish a list[9] of banks where consumers can open an account entirely online, with no need for a customer to visit a branch. Many of these accounts can be opened with a zero balance and funded entirely by an EIP.

Through BankOn and other efforts, free and low-cost bank accounts are widely available at banks of all sizes. BankOn sets account standards that provide a benchmark for safe, affordable accounts at mainstream financial institutions, setting consumers on a path toward financial inclusion. Today, these accounts are available at over 24,000 branches across the United States.

Digital dollar proposals would do little to improve on these programs or address the true reasons that consumers don't have accounts today. The top three cited reasons cited for not having a bank account include "don't have enough money to keep in account" (52%), "don't trust banks" (30.2%), and "avoiding bank gives more privacy" (28%). [10]

The benefits of a long-term banking relationship go well beyond a deposit account.

By focusing solely on Americans without access to an account, digital dollar proposals ignore the 18.7% of U.S. households that are considered underbanked. These households have an account at an insured institution but also have had to rely on financial products or services outside of the banking system like payday lenders.

Not only do current digital dollar proposals not address this serious issue, they will likely exacerbate it. Philadelphia Fed Research referenced above found that these proposals would create a "deposit monopoly" that would "attract deposits away from the commercial banking sector." This has the effect of reducing the funds on banks' balance sheets that is available to lend which would reduce access to credit.[11]

Innovation in banking has the strongest potential to drive inclusion.

ABA believes that responsible innovation in financial services will continue to benefit customers as it has throughout the history of banking and has the potential to drive financial inclusion. New technologies have been shown to make it possible to extend credit to many more borrowers.

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prepaid account (page 7). Prepaid accounts generally offer the same features and functions of as checking accounts though they do not permit overdrafts.

[8] Bank On platform supports local coalition and financial institution efforts to connect consumers to safe, affordable banks accounts and worked to develop Bank On National Accounts standards.

[9] https://www.aba.com/banking-topics/payments/economic-impact-payments/banks-offering-online-account-opening?utm_source=fdic&utm_medium=referral&utm_campaign=covid&utm_content=fdiclink

[10] https://economicinclusion.gov/downloads/2017_FDIC_Unbanked_HH_Survey_Report.pdf

[11] https://www.philadelphiafed.org/-/media/research-and-data/publications/working-papers/2020/wp20-19.pdf

Digital technology has put a bank branch into a consumer's pocket. This makes banking more convenient but also more accessible. The scalable nature of these technologies mean that it is cheaper today to extend financial services to more people. Recent examples include:

- Mobile banking that can give people without easy access to physical branches access to a full suite of banking services;
- New underwriting technologies like cashflow lending that allow banks to evaluate the creditworthiness of those with little to no credit history;
- Automated underwriting that lowers the cost of underwriting individual loans making it possible to profitably extend smaller loans; and
- AI and other technologies that have created easy-to-use and intuitive interfaces that make technology more accessible.

Fast, Electronic Payments are Already a Reality

The U.S. dollar is already largely digital today. While digital dollar proposals claim to speed up payments, they ignore the strong progress that has been made to modernize and digitize payments. Today, consumers and businesses have the option to pay with credit or debit cards, payments applications like Zelle or Venmo, and via automated clearinghouse (ACH).

Efforts to modernize and speed up our payments system have been underway for some time and are already being implemented. The Federal Reserve's 2017 Faster Payments Task Force examined the entirety of the payment system and its experts, including consumer groups, recommended faster networks – not a new currency. As a result of these efforts, the Federal Reserve is building out an instant payments solution called FedNow.

Industry has been driving these improvements as well. The Real-Time Payments (RTP) Network is a brand-new instant payment system that represents an advancement equivalent to moving from dial-up to broadband in terms of speed and features. ABA was a strong advocate for using this capability as part of the EIP program to speed electronic payments to those with bank accounts or even prepaid cards.

Together, RTP, FedNow, and faster ACH systems are forming a web of super-fast, low-cost or free digital payment options that will make waiting for days a thing of the past.

Proponents of digital dollar proposals claim that we must radically change the underpinnings of our currency to compete with China and maintain the dollar's status as the world's reserve currency. These claims ignore the strong progress that has been made to modernize payments in recent years. In fact, the dollar's status as the world's preferred reserve currency is based largely on its stability. Changing its underpinnings would distract the deliberate progress that is being made to modernize U.S. payments, but also risks undermining that stability.

Implementing digital dollar proposals would be a distraction that creates delays in deploying many payments improvements, and derail some entirely. Even the newest systems would have to be reworked and the Fed's resources would be diverted from developing and deploying FedNow, an urgent priority.

Given the significant investments in digital payments and the strong progress that has been made, there is little role for a digital dollar. Governor Brainard came to the same conclusion in her evaluation of CBDC noting:

> There is no compelling demonstrated need for a Fed-issued digital currency. Most consumers and businesses in the U.S. already make retail payments electronically using debit and credit cards, payment applications, and the automated clearinghouse network. Moreover, people are finding easy ways to make digital payments directly to other people through a variety of mobile apps. New private-sector real-time payments solutions are beginning to gain acceptance in the United States. And the Faster Payments Task Force has laid out a roadmap embraced by a variety of stakeholders for a fast, ubiquitous, and secure payments system to be in place in the United States in the next few years. In short, a multiplicity of mechanisms are likely to be available for American consumers to make payments electronically in real time. As such, it is not obvious what additional value a Fed-issued digital currency would provide over and above these options.[12]

Digital Dollar Proposals Have Wide-Ranging Implications that Would Undermine Recovery and Limit Future Economic Growth

The implementation of digital dollar proposals has serious implications for the transmission of monetary policy and would fundamentally reshape our banking system. While the goals of these proposals are narrow, they have wide-ranging unintended consequences that undermine these goals and would do more harm than good.

Digital dollar proposals threaten the retail banking model.

The successful implementation of digital dollar proposals would have serious implications for retail banking that reach well beyond payments. In effect, these accounts will serve as an advantaged competitor to retail bank deposits that will move money off bank balance sheets where it can be lent back into the economy and into accounts at the Federal Reserve. Every digital dollar held at the Fed instead of a full-service bank will reduce the amount of real dollars available for real Americans to borrow and drive the economy.

While depositors at FDIC insured banks have never lost a penny of an insured deposit, it is hard to compete with a government agency that prints that money. Philadelphia Federal Reserve research found that depositors value this and will, in equilibrium, choose to hold their funds at the Federal Reserve instead of at retail banks, establishing the Federal Reserve as a “deposit monopolist.”

Unlike retail banks, the Federal Reserve is not prepared to make loans to consumers and businesses. As deposits migrate from bank balance sheets to the Federal Reserve, it will severely restrict the availability of the capital that fuels economic growth.

Federal Reserve Chairman Jerome Powell recognized this in his comments made to this committee. When asked about the various digital dollar proposals, he responded,

> “We can only offer bank accounts to our reserve banks through depository institutions, not people. I think that would be a very dramatic change in the landscape of banking and I would worry about what would happen to the rest of our private system of banking because an awful lot of people would opt to

[12] https://www.federalreserve.gov/newsevents/speech/files/brainard20180515a.pdf

> keep their money at the Fed and then who would do the lending? It could hurt our intermediation process."[13]

In times of economic hardship, banks' balance sheet driven model is even more important. Banks' balance sheets and strong capital position allow them to make long-term investments and continue lending throughout a downturn, just when it is needed most.

A digital currency also creates a risk to financial stability. In times of economic stress, depositors are likely to prefer holding their money at the Federal Reserve. This creates a risk of bank runs that would undermine financial stability.

Federal Reserve is not positioned to be a retail bank.

The Federal Reserve has neither the authority nor experience to operate a consumer-facing bank. The banking industry has a long track record of serving customers. To do this, America's banks employ more than 2 million people. Today the Federal Reserve System has about 20,000 employees. Building a nationwide consumer-facing bank would require a substantial investment in staff, expertise, processes and infrastructure.

Governor Brainard details some operational challenges that this would entail,

> "First, there are serious technical and operational challenges that would need to be overcome, such as the risk of creating a global target for cyberattacks or a ready means of money laundering. For starters, with regard to money laundering risks, unless there is the technological capability for effective identity authentication, a central bank digital currency would provide no improvement over physical notes and could be worse than current noncash funds transfer systems, especially for a digital currency that could circulate worldwide. In addition, putting a central bank currency in digital form could make it a very attractive target for cyberattacks by giving threat actors a prominent platform on which to focus their efforts. Any implementation would need to adequately deal with a variety of cyber threats--especially for a reserve currency like the U.S. dollar." [14]

A central bank digital currency implicates societal values and privacy.

By making a quasi-governmental body into the nation's near-monopoly provider of currency, bank accounts, and payment services, the Federal Reserve would quickly become politicized as the central control point for monitoring and potentially denying transactions. For controversial but locally regulated purchases such as cannabis and firearms, a central bank digital currency would entangle the Federal Reserve as a national arbiter of social issues. The right of people to transact outside the view of the central bank is a cherished civil liberty that is preserved and protected by the due process of a competitive private banking sector.

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[13] Federal Reserve Chairman Jerome Powell comments in response to questions on digital dollar proposals at the June 17th, 2020 hearing of the Committee on Banking, Housing, and Urban Affairs of the U.S. Senate.

[14] https://www.federalreserve.gov/newsevents/speech/files/brainard20180515a.pdf

Conclusion

As our nation faces a pandemic, it is only natural that we look to technology for innovative solutions to address the new problems that we face today. The rapid convergence of banking and technology is quickly changing the financial services market in ways that are making financial services cheaper and more widely available and accessible.

Digital dollar proposals are well-intentioned but ineffective responses to the challenges identified by supporters. They look to provide more efficient COVID relief but would take far too long to implement to have any meaningful effect. They look to promote financial inclusion but take a narrow view of the problem and would ultimately undermine it. They seek to speed up payments while ignoring the cross-industry efforts that are already underway and delivering for consumers.

Ultimately these proposals fall short on their promise and introduce serious unintended consequences that would undermine our recovery and future economic growth.