

Central Bank Digital Currency: Significant Risks Must Preclude Adoption

The Independent Community Bankers of America, representing community banks across the nation with nearly 50,000 locations, appreciates the opportunity to provide this statement for the record for today’s hearing titled: “Digital Dollar Dilemma: The Implications of a Central Bank Digital Currency and Private Sector Alternatives.”

ICBA believes that clear and significant risks would be derived from the adoption of a CBDC and few if any clearly defined benefits. For the reasons set forth in this statement, ICBA strongly opposes the creation of a U.S. CBDC and urges Congress to oppose this unprecedented and transformative step as well. The policy goals identified in support of a CBDC would best be addressed through alternatives that are readily available in the market today such as FedNow. Similarly, community bankers also believe a wholesale CBDC, a potential form of digital currency limited to financial institutions, is unnecessary given the increasing adoption of instant payment solutions.

Last year, ICBA filed a [comment letter with the Federal Reserve Board of Governors](#) on its public consultation paper, “Money and Payments: The U.S. Dollar in the Age of Digital Transformation,” which solicits views from stakeholders on the risks and benefits of a potential U.S. CBDC. The views summarized in this statement are set forth more comprehensively in our comment letter and reflect extensive consultations with community bankers serving rural, suburban, and urban markets in all regions of the United States.

Disintermediation of Community Bank Deposits

The Federal Reserve defines a CBDC as “a digital liability of a central bank that is widely available to the general public.” Under the “intermediated” model contemplated by the Federal Reserve, “the private sector would offer accounts or digital wallets to facilitate the management of CBDC holdings and payments. Potential intermediaries could include commercial banks and regulated nonbank financial service providers and would operate in an open market for CBDC services.”¹

Bank deposits are a liability of the issuing bank and reside on its balance sheet. As such, deposits serve as a source of bank lending. By contrast, as a liability of the Federal Reserve, a CBDC, even one that is “intermediated,” would not be available to support bank lending. A CBDC would position the Federal Reserve as a direct, advantaged competitor for bank deposits. The Federal Reserve concedes that a CBDC “substitution effect could reduce the aggregate amount of deposits in the banking system, which could in turn increase bank funding expenses, and reduce credit availability or raise credit costs for households and businesses.” In other words, a CBDC could create an outflow of deposits

¹ Board of Governors of the Federal Reserve System, Research & Analysis, “Money and Payments: The U.S. Dollar in the Age of Digital Transformation” (January 2022), available at: <https://www.federalreserve.gov/publications/files/money-and-payments-20220120.pdf>.

from community banks with a direct and adverse impact on credit availability. The risk of this scenario would be accentuated in a financial crisis. Because a CBDC would not have credit or liquidity risk, depositors might “run on the bank” and transfer their balances to CBDC wallets. The digital nature of CBDC would allow these transfers to occur with unprecedented speed, triggering a chain reaction of events that could lead to bank failures. The rapid outflow of deposits following the failure of Silicon Valley Bank in March offers a preview of what could occur on much broader scale.

ICBA strongly objects to any policy change that would disrupt credit availability needed to support consumer spending, home purchasing, business working capital, investment, and hiring. The impact would be especially felt in rural and agricultural communities which are primarily served by community banks. Community banks are small business lending specialists responsible for approximately 60 percent of small business loans. Any policy change that would disrupt community bank deposit availability and the lending that depends on it is an unacceptable risk for communities across America and the economy.

A CBDC Would Be Costly for Community Banks

In the intermediated model, banks would provide a CBDC “wallet” for customers, but CBDC would not fund loans or otherwise serve as a source of bank revenues. Nevertheless, banks would remain saddled with the identity verification, customer service, know your customer (KYC), anti-money laundering (AML), sanctions screening and other compliance burdens associated with maintaining CBDC wallets.

Holding CBDC would create a net cost for community banks, which already operate on narrow margins. Today, deposit compliance and operating costs are effectively supported by loan interest revenues and non-interest income. Community banks would also be required to make significant new technology investments in order to provide CBDC wallet services. Banks would have to offset these new costs by charging significant fees.

The Federal Reserve proposal envisions banks in competition with regulated nonbank financial service providers in an open market for CBDC wallets. This could introduce regulatory arbitrage risk and unfairly advantage these nonbank providers if they are not regulated as stringently as banks.

A CBDC Would Risk a Consumer Privacy Backlash

A CBDC would require a public record of all transactions conducted in CBDC to be maintained by the central bank. ICBA believes that consumers would be strongly resistant to using a digital asset that undermines their financial privacy. For this reason, a CBDC would not be an effective means of drawing more Americans into the banking system – a benefit proponents claim for the proposal. Surveys of unbanked households consistently show that financial privacy is a primary reason they choose not to use the banking system.

In addition to concerns about granting the federal government visibility into consumer transactions, a CBDC would create an irresistible target for criminal hackers and rogue states. A CBDC would depend on the Federal Reserve to serve as a hub, validating all transactions between CBDC wallets. A breach of the Federal Reserve’s cybersecurity could disrupt or misdirect countless transactions, inflicting financial harm on consumers and damaging the credibility of the CBDC and potentially the dollar as well.

FedNowSM Is a More Viable Solution

The supposed benefits claimed for a CBDC do not withstand scrutiny. As noted above, it is an implausible means of reaching the unbanked. ICBA’s comment letter to the Federal Reserve argues against other supposed benefits, such as supporting the global dominance of the dollar. We address here the claim that a CBDC is needed to modernize the U.S. payments system.

CBDC proponents argue that more competition is needed in the payments system. There is a wealth of evidence that demonstrates the U.S. has a diverse and highly competitive payments system today, with significant consumer choice. Safe, efficient Federal Reserve and private-sector interbank payment systems exist now that offer increased transaction speed and reduced costs. The FedNow service, which launched this year, will enable financial institutions of all sizes to provide safe and efficient instant payment services in real time and around the clock. FedNow will provide many of the benefits of alternative payments rails without the risk and will accomplish many of the stated goals of a CBDC. It is worth clarifying here that FedNow is not CBDC. A misinformation campaign is attempting to confuse the public by conflating the two.

In public comments addressing unequal access to the financial system, Nellie Liang, Treasury Undersecretary for Domestic Finance, said that FedNow “will be low cost to users. Because FedNow relies on the banking system, there already are safeguards for consumers and businesses.”² With the introduction of FedNow instant payment services, increased Same Day ACH adoption, and The Clearing House’s introduction of Real Time Payments (RTP®), Americans are enjoying faster transactions clearance and can expect further innovations to be built upon these rails. ICBA urges policymakers to give FedNow a chance to succeed in advancing payments modernization. The launch of a CBDC, if adopted, will be many years away. A decision at this time to establish a U.S. CBDC would be premature. FedNow must be given a chance to work and be evaluated in the market before a CBDC is considered. Additionally, CBDC must not be viewed as an alternative to privately issued cryptocurrency. Nor should cryptocurrency be viewed as a substitute for a CBDC. There is no binary choice between the two. A CBDC will neither compete cryptocurrency out of existence nor solve the regulatory challenges and systemic risks presented by privately issued cryptocurrency arrangements, including stablecoins.

² <https://home.treasury.gov/news/press-releases/jy0673>

The Role of Congress

The Federal Reserve promised in its report not to move forward “without clear support from the executive branch and from Congress, ideally in the form of a specific authorizing law.” Federal legislation would be required to establish the roles and responsibilities of the various stakeholders—including the Treasury Department, Federal Reserve, and the private sector. Congress would need to exercise its authority to preclude any actions that would disrupt the stability of the economy and inject safety and soundness risks to the financial system. Congress must not be sidelined in a policy choice with such far reaching, and potentially damaging, significance.

Support for Legislation Before This Committee

In light of our strong objections to a U.S. CBDC, ICBA is pleased to support the following bills under consideration by this committee:

- H.R. 3402, the Power of the Mint Act (Auchincloss/Hill): Prohibits the Board of Governors of the Federal Reserve and the Secretary of the Treasury from issuing a Central Bank Digital Currency without congressional authorization. As noted above, the far-reaching impact of a potential CBDC warrants Congressional authorization.
- The CBDC Anti-Surveillance State Act (Emmer): Prohibits a Federal Reserve Bank from offering products or services directly to individuals, maintaining individual accounts, or issuing a CBDC to individuals. It would also prohibit the Federal Reserve and the Federal Open Market Committee from using a CBDC to implement monetary policy. This bill would prohibit both FedAccounts and a direct-to-consumer CBDC. In addition to competing directly with checking and savings accounts offered by community banks, both FedAccounts and consumer CBDC accounts raise serious privacy concerns, as they could potentially be used by the government to track and control consumer financial transactions.

These bills effectively address some of the concerns identified in this statement. ICBA thanks Representatives Hill, Auchincloss, and Emmer for introducing them.

Closing

Thank you for convening today’s hearing to highlight the significant stakes in any creation of a CBDC. ICBA urges the members of this committee to carefully consider ICBA’s objections to a CBDC as expressed in this statement and more fully in our [recent comment letter to the Federal Reserve](#).