One Mission. Community Banks.

December 11, 2025

Interest on Reserve Balances: The Community Bank Perspective

The Independent Community Bankers of America (ICBA),[1] 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 on the Federal Reserve's policy of paying interest on reserve balances (IORB) to financial institutions that maintain balances at the Federal Reserve. We welcome the opportunity to clarify the importance of IORB to our nation's conduct of monetary policy and smoothly functioning credit markets on which our economy depends. ICBA appreciates the Senate's recent, strong bipartisan vote to reject elimination of IORB by a margin of 14 to 83. We hope that this hearing will dispel misunderstandings concerning IORB—including the mistaken argument that IORB "costs" taxpayers and that its elimination would "save" taxpayer dollars.

This statement will describe the IORB program, its importance to effective monetary policy and to community banks and the broader financial system, and the disruption and interest rate spikes that would result from the program's elimination.

Banks keep reserves at the Federal Reserve to facilitate payments and create liquidity

Many banks including community banks keep reserves at the Federal Reserve to settle payments, such as Automated Clearing House (ACH) transfers, wire payments, credit card settlements, and check clearing. As the safest and most liquid asset available to banks, reserves held at the Federal Reserve also help banks meet regulatory liquidity requirements. Reserves are also a reliable source of operational liquidity to meet unanticipated customer deposit withdrawals. Readily available liquidity is essential to the safety and soundness of the banking system.

Congress created IORB to modernize monetary policy

Congress created IORB in 2006 legislation for the purpose of modernizing monetary policy. Initially, payment of IORB was to begin in 2011. However, in 2008, Congress advanced the IORB start date in direct response to the global financial crisis and the need to stabilize banks. Bank liquidity, supported by IORB, played a critical role in containing and resolving that crisis.

Before IORB, banks earned no interest on reserves held at the Federal Reserve and therefore held only enough to meet regulatory minimums. Reserves held at the Federal Reserve were effectively a "tax" on banks, a lost opportunity to earn income on these funds.

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[1] The Independent Community Bankers of America® has one mission: to create and promote an environment where community banks flourish. We power the potential of the nation's community banks through effective advocacy, education, and innovation. As local and trusted sources of credit, America's community banks leverage their relationship-based business model and innovative offerings to channel deposits into the neighborhoods they serve, creating jobs, fostering economic prosperity, and fueling their customers' financial goals and dreams.

Bank reserves are invested by the Federal Reserve and earn income

Reserves held at the Federal Reserve do not sit idle but are invested in Treasury and agency securities, and the interest earned by the Federal Reserve on these securities is used to pay IORB. Over time, the Federal Reserve collects more than enough interest on Treasury securities to pay IORB and remits net income to the Treasury Department after covering expenses and capital.

In 2022, the Federal Reserve began raising interest rates to fight inflation. As a result, the Federal Reserve's net income turned negative temporarily. This is an unusual circumstance that will be reversed in the near term as the Federal Reserve cuts interest rates. Since 2010, the Federal Reserve has remitted nearly $850 billion to Treasury.

IORB is critical to the effective conduct of modern monetary policy

As noted above, Congress created IORB to modernize monetary policy, with a dual mandate of promoting maximum employment and stable prices. IORB has proved effective for that purpose. Before IORB, monetary policy was conducted by adjusting reserve requirements, forcing borrowing and lending among banks to meet minimum reserve requirements that were then in effect. This intra-bank borrowing determined the Federal Funds Rate, the interest rate targeted by the Federal Open Market Committee (FOMC) of the Federal Reserve. This cumbersome and imprecise means of conducting monetary policy was later replaced by the IORB.

IORB has simplified monetary policy. The FOMC sets IORB directly, thereby creating a floor interest rate to be earned by banks. No bank would lend in the Federal Funds market for less than it could earn in the IORB. Setting the IORB directly allows the FOMC to effectively also set the Federal Funds Rate. Using IORB, the Fed calibrates the Federal Funds Rate to economic conditions in pursuit of its dual mandate.

Repeal of the IORB would be highly disruptive to monetary policy, forcing a reversion to the old, less effective system and rupturing confidence in global credit markets.

IORB does not cost taxpayers

As noted above, reserves held at the Federal Reserve are used to purchase securities, primarily Treasury securities. Interest earned on these securities is used to pay IORB, and over time the Fed earns more in interest, funded by reserves, than it pays in IORB.

It would be a mistake to focus only on the cost of IORB, ignoring the income generated by reserve-funded investments, and conclude that IORB costs taxpayers. If IORB were eliminated, banks would withdraw their reserves from the Fed, and most of those funds would be invested in Treasury securities directly. The government would still pay interest to banks. Elimination of IORB would not save taxpayer dollars.

Elimination of IORB would spike interest rates across maturities and slow economic growth

If banks could no longer earn IORB, they would abruptly withdraw reserves from the Federal Reserve. The Federal Reserve would fund these withdrawals by selling its securities portfolio, and fire sales would spike interest rates across maturities. Higher interest rates would raise borrowing costs for Treasury, more than erasing any "savings" achieved by not paying IORB, as well as for households and businesses across the entire economy. Elimination of IORB would slow economic growth and widen the federal budget deficit.

Thank you for the opportunity to provide this statement for the record. We expect that this hearing will educate the public about the true value of IORB policy and the importance of preserving it.