STATEMENT OF

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NAVIGATING THE DIGITAL PAYMENTS ECOSYSTEM: EXAMINING A FEDERAL FRAMEWORK FOR PAYMENT STABLECOINS AND CONSEQUENCES OF A U.S. CENTRAL BANK DIGITAL CURRENCY

RANDALL D. GUYNN BIOGRAPHY

My name is Randall D. Guynn and I am Chairman of the Financial Institutions Group at Davis Polk & Wardwell LLP, where I have worked since 1986. My practice has focused on advising banks of all sizes on their most critical financial regulatory issues and transactions. During my career, I have played key roles in designing or drafting some of the most important financial regulatory reforms, including Title II of the Dodd-Frank Act, the European Bank Resolution and Recovery Directive, the Hague Securities Convention, the Gramm-Leach-Bliley Act, the European Finality Directive, the 1994 revisions to Article 8 of the Uniform Commercial Code and the 1990 amendments to the Trust Indenture Act. I have also played a leading role in designing the single-point-of-entry (SPOE) recapitalization within resolution strategy, which is widely considered to be the best solution to the too-big-to-fail problem. In recent years, I have advised a large number of financial technology and cryptoasset companies. Among other things, I helped design the proposed Libra/Diem payment stablecoin, most of the features of which are reflected in the proposed STABLE Act. I recently posted a working paper on how the FDIC can avoid a repeat of the disastrously expensive failure of Silicon Valley Bank. I am currently working on a book on the history of private money from Mesopotamia to cryptocurrency and another on the Kirtland Safety Society Anti-Banking Company and other common-law banks in early modern England and on the America frontier. The views I express are my own, and not necessarily those of Davis Polk, any client or any other organization with which I am or have been affiliated.

Introduction

Stablecoins are a modern, digital version of private money. They can be transferred 24/7 on a real time gross basis anywhere around the world. As digitally native payment instruments, they are the most efficient way to pay for a wide variety of cryptoassets on a blockchain. They also have the potential to be an efficient way to transfer remittances across borders and to pay for other goods and services.

If a payment stablecoin issuer has a properly calibrated reserve of liquid assets, capital buffer and no material amount of other liabilities, payment stablecoins should be as safe as insured bank deposits and central bank money. They should also be as safe as the sort of demand deposit liabilities that would have been issued by the 100% reserve banks described in the Program for Monetary Reform developed by some of the most celebrated economists in the 1930s as an alternative to deposit insurance.[1] They should be safer than uninsured deposits held with many commercial banks engaged in maturity or liquidity transformation.[2] Together with other forms of cryptocurrency, stablecoins are the latest version in a long line of various types of private money.

Private money has historically been developed by private actors in response to market demand or predicted market demand for a highly fungible, divisible and durable thing that would facilitate the efficient exchange of a wide variety of goods and services. Voluntary exchange of goods and services increases individual and aggregate well-being by reallocating goods and services to individuals and companies that value them the most.

Private money overcomes the inefficiencies of exchanging goods and services by barter. The inefficiencies of barter are well known and include the lack of a coincidence of wants. For example, if farmer Jones has chickens and farmer Brown has cows, but farmer Jones does not want cows and farmer Brown does not want chickens, no voluntary exchange will take place even if they would both be better off by trading all or some of their animals for other goods or services. If some form of private money is available, however, farmer Brown and farmer Jones can sell some or all of their animals for that private money and use it to buy what they want. Those exchanges will increase their well-being and anyone else's who voluntarily participates in the network of voluntary exchanges on an informed basis.

Earlier forms of private money included shekels of barley, gold or silver bullion, private credit money in the form of book-entries on account books or even clay tablets, bills of exchange, privately minted coins or tokens, cowry shells, salt, tobacco receipts, promissory notes, gold- or silver-backed banknotes, and demand deposit claims against private-sector commercial banks. All of these things are highly fungible, divisible and durable and have been useful forms of private money at one point or another in history. While a substantial portion of the U.S. money supply currently consists of public money in the form of coins, paper dollars and demand deposit claims against the Federal Reserve Banks, the vast majority of the U.S. money supply consists of private money. This includes demand deposit claims against commercial banks, ownership interests in money market funds, short-term trade credit extended by commercial companies, amounts standing to the credit of a person's account with a non-bank payment company, stablecoins and various forms of cryptocurrency.

Once a particular form of private money has become widely accepted as a payment instrument for goods and services in a community or economy, public authorities have often reinforced its desirability among market participants by allowing taxpayers to use it to pay taxes, using it to buy armies and navies, and declaring it to be legal tender for public and private debts. Public authorities have also minted their own coins, issued gold- or silver-backed promissory notes, fiat currency or other forms of public money that have competed with private money. A central bank digital currency (CBDC) would be a new, digital form of public money that would compete with private money, including payment stablecoins.

People have been free during most of human history to innovate in the creation of private money without government interference, including any requirement to obtain government permission to do so.[3] In modern times, governments have attempted to assert control over the production and circulation of private money with limited success. Among other methods, they have granted monopolies to certain entities, imposed excise taxes on certain forms of private money or prohibited companies from issuing certain forms of private money without a government license or charter to do so.

For example, the English Parliament incorporated the Bank of England in 1694. The Bank immediately started issuing promissory notes designed to circulate as paper money (banknotes) alongside banknotes previously circulated by various goldsmith banks starting in about 1650. Both the Bank of England and the goldsmith banks issued their banknotes pursuant to a natural or common-law right to do so, without any need to obtain any express government approval, license or charter. To protect the Bank of England against competition after 1708, however, Parliament prohibited any entity other than the Bank of England to issue promissory notes that circulated as paper money.[4] But that prohibition was limited by its terms to the territory of England and for all practical purposes to the city of London. It also contained an exemption for virtually all of the goldsmith, private, country, joint stock and other common-law banks that existed or were formed over the next two centuries. Those common-law banks continued to issue banknotes alongside the Bank of England until the early 20th century.[5]

After the Civil War, the U.S. federal government attempted to drive state-chartered banks out of business by imposing a 10% excise tax on their banknotes, but not on the banknotes issued by national banks chartered under the new National Bank Act.[6] The state-chartered banks survived despite this attack on one of their core functions by persuading their customers that payment orders in the form of checks were just as useful as banknotes to pay for goods and services. The excise tax on their banknotes was never extended to the checks used by customers to buy goods and services by ordering their banks to debit specified amounts from their deposit accounts and credit those amounts to the deposit accounts of their sellers.

Finally, Section 21 of the Glass-Steagall Act makes it a crime for anyone to willfully engage in the business of issuing demand deposit liabilities that can be transferred by checks without first obtaining a government license or charter to do so.[7] Although ownership interests in money market funds (MMFs) are economically similar to bank deposits, the U.S. Department of Justice issued an opinion in 1979 that ownership interests in MMFs are not deposits for purposes of Section 21.[8] Nonbank payment companies allow customers to maintain credit balances that can be used to pay for goods and services without issuing demand deposit liabilities that are prohibited by Section 21. Finally, nonbank payment stablecoin issuers allow customers to

purchase and use stablecoins to pay for goods and services including other cryptoassets without issuing demand deposit liabilities prohibited by Section 21.

The STABLE Act

Today we are faced with a new form of private money—payment stablecoins. Legislation like the STABLE Act seeks to bring payment stablecoins inside the regulatory perimeter just as earlier forms of private money have been brought inside that regulatory perimeter.

Licensing Requirements

The STABLE Act would require payment stablecoin issuers to obtain a state or federal license to issue payment stablecoins. It would prohibit anyone from issuing payment stablecoins for use by any person in the United States without first obtaining such a license.

Reserve Requirements

Section 4(a)(1) of the STABLE Act would require licensed or "permitted" payment stablecoin issuers to maintain a reserve of high quality liquid assets equal to at least 100% of their stablecoin liabilities. The assets that would qualify as high quality and liquid are listed in Section 4(a)(1). Together with a properly calibrated capital requirement and activities restrictions, this 100% reserve requirement should make payment stablecoins as safe as insured bank deposits or even central bank money, including any potential central bank digital currency, or "CBDC". These features will reduce any run risk against a payment stablecoin issuer to a negligible or even infinitesimal amount.[9]

For example, suppose that a payment stablecoin issuer's reserve consisted exclusively of U.S. Treasury securities with an original maturity of 93 days or less as required by the current version of the STABLE Act. Assume that the issuer laddered those Treasury securities consistent with sound risk management so that the portfolio had an average duration of one month. Such a portfolio would be virtually immune from interest-rate and credit risk, unlike the bond portfolio of, say, Silicon Valley Bank (SVB), which had an average duration of more than six years at the time of its failure. For every 1% increase in interest rates, the market value of SVB's bond portfolio dropped by more than 6%.[10] For every 1% decrease in interest rates, the market value of SVB's portfolio would have risen by more than 6%.[11]

In the case of a portfolio of U.S. Treasury securities with an average duration of only one month, every 1% change in interest rates would only change the market value of the portfolio up or down by 0.08%. Assuming the issuer had a capital buffer calibrated to reflect the negligible interest-rate and credit risk of its reserve as required by Section 4(a)(4) of the STABLE Act and was not permitted to incur any material liabilities other than its stablecoin liabilities, it should be able to liquidate its reserve immediately at a haircut to face value of only 0.08% and use the proceeds to immediately redeem all of its outstanding stablecoins. This is fundamentally different from the failure of SVB where the FDIC spent $22 billion of the Deposit Insurance Fund to bail out uninsured depositors and then imposed special assessments of $22 billion on the surviving banks (and ultimately their shareholders, management and customers depending on the elasticity of demand) to pay for it.[12]

Although the assets permitted to be included in the required reserve need to be limited to sufficiently safe and liquid assets, the current list of qualifying assets is too restrictive. The STABLE Act should permit all short-term U.S. government securities, meaning those with an original maturity of less than one year, to be included in the required reserve. At a minimum, the 93-day requirement should be extended to 26 weeks (6 months). In addition, the STABLE Act should be amended to give the Federal Reserve the limited discretionary authority to designate additional assets as permitted reserve assets if they are sufficiently safe and liquid. Those changes might increase the average duration of the portfolio of reserve assets from one month to a range between three and six months. That would mean that the market value of the reserve portfolio might vary by 0.25% to 0.5% instead of only 0.08% for every 1% change in general interest rates. But that modest amount of additional interest rate risk could easily be addressed by a modest increase in the capital buffer required by Section 4(a)(4) of the STABLE Act.

Capital Requirements

Section 4(a)(4) of the STABLE Act would require the relevant payment stablecoin regulators to impose capital requirements on permitted payment stablecoin issuers. Capital requirements should protect stablecoin holders against any loss arising from any interest-rate or credit risk that might exist in the reserve portfolio despite the safe and highly liquid nature of the assets that would qualify as permitted reserve assets. The STABLE Act provides that the Collins Amendment in Section 171 of the Dodd-Frank Act would not apply to payment stablecoin issuers or their parent holding companies on a consolidated basis. The Collins Amendment imposed minimum leverage capital requirements on insured depository institutions (IDIs) and their parent depository institution holding companies on a consolidated basis. The Collins Amendment might make sense in the context of IDIs engaged in maturity or liquidity transformation. But because the STABLE Act would prohibit permitted payment stablecoin issuers from engaging in maturity or liquidity transformation, a minimum leverage capital requirement would be inappropriate. A permitted payment stablecoin issuer should be subject only to risk-based capital requirements. Moreover, any risk-based capital requirement should be calibrated to reflect the risk profile of the permitted payment stablecoin issuer's reserve and other assets, which would be different and much less risky than the assets of a bank engaged in maturity or liquidity transformation.

Activities Restrictions

Section 4(a)(6) of the STABLE Act would prohibit a permitted payment stablecoin issuer from engaging in any activities other than those specified in that subsection. Among other things, these activities restrictions would prohibit a permitted payment stablecoin issuer from engaging in maturity or liquidity transformation or incurring a material amount of liabilities other than its payment stablecoin liabilities. These restrictions will reinforce the protections against losses provided by the reserve requirements and capital requirements.

Regulatory Framework Modeled on Regulation of the Dual-Banking System

The proposed regulatory framework for payment stablecoins appears to have been modeled on the framework for regulating, examining and supervising the dual banking system. This framework has existed in one form or another since the enactment of the National Bank Act

in 1863. As a result of its long existence, the framework for regulating, examining and supervising banks under the dual-banking system is well understood. The STABLE Act seems to reflect the time-honored principles that if it ain't broke, don't try to fix it and don't reinvent the wheel.

Dual-Banking System

Federal depository institutions. Under the dual banking system, national banks and federal thrifts are regulated, examined and supervised under the National Bank Act and the Home Owners Loan Act, respectively, as administered by the Office of the Comptroller of the Currency (OCC). Federal credit unions are regulated, examined and supervised under the Federal Credit Union Act by the National Credit Union Authority (NCUA). National banks are required to become members of the Federal Reserve System and are therefore subject to the Federal Reserve Act, as administered by the Federal Reserve. Federal thrifts are permitted but not required to become members of the Federal Reserve System. Deposit insurance from the FDIC is optional for both, but most of them apply for such deposit insurance.

State depository institutions. State-chartered depository institutions are regulated, examined and supervised under the banking laws of their states, as administered by their relevant state banking supervisors. If their deposits are insured, they are subject to certain additional federal standards, including a provision that prohibits them from engaging in any activity as principal that a national bank is not permitted to engage in. If state IDIs elect to become members of the Federal Reserve System, they are also subject to the additional regulation, examination and supervision of the Federal Reserve. If they do not elect to become members of the Federal Reserve System, they are subject to the additional regulation, examination and supervisory of the FDIC. Uninsured state-chartered depository institutions and nonbank financial companies are not subject to any federal banking rules or oversight unless they are affiliated with an IDI, but are typically subject to state regulation such as state money transmission or licensed lender laws.

Bank Holding Company Act (BHC Act). If an IDI has a top-tier parent holding company, that top-tier parent would be treated as a bank holding company (BHC) for purposes of the BHC Act. The BHC Act imposes activity and investment restrictions on the BHC and its direct and indirect nonbank subsidiaries. It also imposes certain reporting and other requirements on the BHC and its direct or indirect nonbank subsidiaries, including being subject to the regulation, examination and supervision of the Federal Reserve.

The BHC Act generally prohibits a BHC and its direct or indirect non-bank subsidiaries from engaging in any activity that is not so closely related to banking as to be a proper incident thereto. If a BHC qualifies as a financial holding company (FHC), it is permitted to engage in a broader range of activities — namely, any activity that is financial in nature, incidental to a financial activity or complementary to a financial activity. The OCC has determined that acting as a custodian for digital assets, including stablecoins, is a permissible activity for national banks.[13] As a result, that activity would be permissible for a BHC. But the Federal Reserve has not yet determined whether acting as a principal or agent with respect to cryptoassets is financial in nature, incidental to a financial activity or complementary to a financial activity for purposes of the BHC Act.

State-Federal Regime for Permitted Payment Stablecoin Issuers

Similarities. The proposed regulatory framework for payment stablecoins has several features in common with the state-federal framework for the dual banking system. Under the STABLE Act, payment stablecoin issuers that are national trust banks or subsidiaries of insured national banks or federal thrifts are subject to regulation, examination and supervision under Section 4(a) of the STABLE Act by the OCC. Those that are subsidiaries of federal credit unions are subject to regulation, examination and supervision under Section 4(a) by the NCUA.

Payment stablecoin issuers that are subsidiaries of state-chartered IDIs are subject to regulation, examination and supervision under Section 4(a) or 4(b) by their state payment stablecoin regulators, which are generally the same as the state's banking agency. Any state-level regime under Section 4(b) must meet the federal standards and requirements in Section 4(a). If a payment stablecoin issuer is the subsidiary of a state member IDI, the subsidiary will be subject to the additional regulation, examination and supervision by the Federal Reserve. If it is the subsidiary of a state nonmember IDI, it will be subject to additional oversight by the FDIC. Payment stablecoin issuers that are uninsured state-chartered depository institutions, state trust companies or their subsidiaries are subject to state but not any additional federal oversight unless they are affiliated with an IDI just like their counterparts in the dual-banking system.

Differences. The proposed regulatory scheme for payment stablecoins has two features that are different from the dual banking system. The first is that payment stablecoin issuers that are not IDIs or subsidiaries of IDIs are subject to regulation, examination and supervision under Section 4(a) or 4(b) by the OCC or their state payment stablecoin regulators, depending on whether they apply to the OCC to be a Federal qualified nonbank payment stablecoin issuer or to their state payment stablecoin issuer to be a State qualified nonbank payment stablecoin issuer.

The second is that the ultimate parent of a permitted payment stablecoin issuer would not be subject to the BHC Act or provisions substantially similar to those in the BHC Act. The STABLE Act reflects the view that permitted payment stablecoin issuers are fundamentally different from and less risky than IDIs engaged in maturity or liquidity transformation.

The principal purpose of the BHC Act was originally to prevent banking groups from avoiding federal laws against interstate branching by a single bank. Before enactment of the BHC Act, banking groups could engage in banking across state lines without violating the law against interstate branching by establishing BHCs that would establish or acquire bank subsidiaries in multiple states instead of establishing branches from a single bank across state lines. The BHC Act sought to discourage those structures by imposing activities restrictions on any BHC that had two or more bank subsidiaries. It generally prohibited BHCs that had more than one bank subsidiary from engaging in any activities that are not so closely related to banking as to be a proper incident thereto. In 1970, Congress amended the BHC Act to extend the activities restrictions to BHCs that had only one bank subsidiary. In 1994, Congress enacted the Riegle-Neal Interstate Banking and Branching Efficiency Act, which repealed the long-standing federal prohibition on nationwide branching. In 1999, the Gramm-Leach-Bliley Act permitted BHCs that qualified as FHCs to engage in any activity that is financial in nature, incidental to a financial activity or complementary to a financial activity.

The STABLE Act would not amend the term "bank" in the BHC Act to include a permitted payment stablecoin issuer.[14] Nor would it impose activities or investment restrictions substantially similar to those in the BHC Act on the parent companies of payment stablecoin issuers unless they were otherwise BHCs for purposes of the BHC Act. It would not prohibit large technology companies that are not predominantly engaged in activities that are financial in nature, incidental to a financial activity or complementary to a financial activity to directly or indirectly acquire or maintain a controlling interest in a permitted payment stablecoin issuer. Nor would it do so assuming that acting as an issuer, principal or agent with respect to stablecoins or other cryptoassets would be considered financial in nature, incidental to a financial activity or complementary to a financial activity for purposes of any such prohibition.

As noted above, the STABLE Act reflects the view that permitted payment stablecoin issuers are fundamentally different from and less risky than IDIs engaged in maturity or liquidity transformation. Thus, imposing the activities or investment restrictions of the BHC Act or substantially similar restrictions on their affiliates is not justified. Unlike the deposit liabilities of IDIs, the stablecoin liabilities of permitted payment stablecoin issuers are required to be 100% backed by high quality liquid assets and are not FDIC insured. Permitted payment stablecoin issuers are also prohibited from engaging in maturity or liquidity transformation and from having any material liabilities other than their stablecoin liabilities. Finally, permitted payment stablecoin issuers do not have access to the Federal Reserve's discount window or benefit from any other aspect of the federal safety net.

In contrast to the STABLE Act, the discussion draft released by Ranking Member Maxine Waters in December 2024 would require the Federal Reserve to issue regulations:

- prohibiting a "non-financial commercial company" to acquire control of a "registered payment stablecoin issuer or licensed nonbank entity"; and

- requiring that "the activities of all affiliates of the registered payment stablecoin issuer or licensed nonbank entity be financial activities or incidental to such financial activities."[15]

The discussion draft does not define the term "non-financial commercial company". The draft does not specify or require the Federal Reserve to determine that acting as an agent or principal with respect to cryptoassets is or would be a financial activity or incidental to a financial activity. As noted above, the Federal Reserve has not yet determined that such activities are financial in nature, incidental to a financial activity or complementary to a financial activity for purposes of the BHC Act.

Customer Protection

Section 8 of the STABLE Act would seek to protect customers that hold stablecoins through a custodian by requiring the custodian to treat the stablecoins and any related private keys, cash and other property as the customers' property, and not the property of the custodian, and to segregate them from any stablecoins and other property owned by the custodian. The Act would also provide that the claims of the customer with respect to any stablecoins or other property held in custody for it by the custodian would have priority over the claims of the issuer

or any creditor of the issuer. That provision should be amended to replace the term "issuer" with the "person described in subsection (a)" — namely, the custodian. If amended in this manner, these customer ownership and priority rules would result in the same outcome as the customer property and priority rules in Section 8-503 and 8-511 of the Uniform Commercial Code. If a customer consents to having all or a portion of its stablecoins or other property pledged to secure an obligation of the custodian or a third party, the secured creditor would step into the shoes of the customer with respect to any claims for stablecoins and or any other property held in custody by the custodian.

CBDC

Various central banks, including the Federal Reserve, have studied whether to issue public money in the form of a CBDC. Some of them other than the Federal Reserve have started issuing foreign-currency denominated CBDCs. Proposals to establish a U.S. CBDC have been highly controversial mainly because of the adverse impact that a retail or wholesale CBDC could have on the financial privacy and freedom of ordinary Americans. Just last year, the House passed H.R. 5403, the CBDC Anti-Surveillance State Act. Representative Patrick McHenry, then the Chairman of the House Financial Services Committee, introduced that bill with the following statement:

> "This bill is straightforward. It halts unelected bureaucrats from issuing a central bank digital currency, or CBDC, that would be detrimental to Americans' right to financial privacy. We've already seen examples of governments weaponizing their financial system against their own citizens. For example, the Chinese Communist Party uses a CBDC to track spending habits of its citizens. This data is being used to create a social credit system that rewards or punishes people based on their behavior. That type of financial surveillance has no place in the United States."[16]

This concern echos concerns expressed by various Federal Reserve Board governors or former governors. For example, Governor Chris Waller has long taken the position that the Federal Reserve should not create a CBDC that competes with stablecoins and other existing forms of private money unless there is a clear problem for the CBDC to solve.[17] In a speech late last year, he elaborated:

> "In a speech I gave in August 2021, I asked, what problem would a CBDC solve? In other words, what market failure or inefficiency demands this specific intervention? In more than three years, I have yet to hear a satisfactory answer as applied to CBDC."[18]

Former Federal Reserve Vice Chairman for Supervision, Randal Quarles, compared CBDC to wearing parachute pants — a fad in the 1980s that disappeared almost as quickly as it burst into popular culture.[19] He too asked what problem a CBDC was supposed to solve and whether its alleged benefits were greater than its clear risks to financial privacy and freedom. He concluded that private money in the form of stablecoins would produce virtually all of the benefits that a CBDC would allegedly produce without any of the risks. Federal Reserve Chairman Jerome Powell recently told Senator Bernie Moreno that the Federal Reserve would not create a CBDC so long as he is the Federal Reserve Chairman.[20]

Other prominent critics of a U.S. dollar CBDC include Norbert Michel of the Cato Institute[21] and Dante Disparte of Circle, a prominent stablecoin issuer.[22] Michel has argued that various existing and emerging forms of private money, including bank deposits and stablecoins, provide virtually all of the alleged benefits of a CBDC without any of its significant risks. Norbert has argued that the serious risks of CBDCs include:

- *Financial Privacy Risks.* "A CBDC could spell doom for what little financial privacy protections Americans still have because it would give the federal government complete visibility into every financial transaction."[23]

- *Risks to Core Freedom.* "With so much data in hand and consumers so closely connected to the central bank, a CBDC would provide countless opportunities for the government to control citizens' financial transactions and, therefore, their lives. For instance, such control could be preemptive (prohibiting and limiting purchases), behavioral (spurring and curbing purchases), or punitive (freezing and seizing funds). The programming capabilities of a CBDC could mean that people would be prohibited from buying certain goods or limited in how much they might purchase."[24]

The Federal Reserve issued a report in January 2022 on the benefits and risks of a CBDC.[25] The report concluded that if the Fed were ever to establish a CBDC, it should be structured to be "privacy-protected, intermediated, widely transferable, and identify-verified."[26] The report identified several risks with CBDCs, including the privacy risk noted by Michel and the following financial stability risk, at least with retail CBDCs:

> "Because central bank money is the safest form of money, a widely accessible CBDC would be particularly attractive to risk-averse users, especially during times of stress in the financial system. The ability to quickly convert other forms of money—including deposits at commercial banks—into CBDC could make runs on financial firms more likely or more severe. Traditional measures such as prudential supervision, government deposit insurance, and access to central bank liquidity may be insufficient to stave off large outflows of commercial bank deposits into CBDC in the event of financial panic."[27]

President Biden issued Executive Order 14067 in February 2022 directing the U.S. Treasury to conduct another study, describing the creation of a CBDC to be a matter of the "highest urgency" for the Biden Administration.[28] In September 2022, the U.S. Treasury published its report.[29] Its first recommendation was for the government to "[a]dvance work on a possible U.S. CBDC, in case one is determined to be in the national interest."[30] One of President Trump's first Executive Orders in 2025 reversed this policy on CBDCs. It repealed Executive Order 14067 and directed the U.S. government to take "measures to protect Americans from the risks of [CBDCs], which threaten the stability of the financial system, individual privacy, and the sovereignty of the United States, including by prohibiting the establishment, issuance, circulation, and use of a CBDC within the United States."[31]

Prominent advocates for a U.S. CBDC have included Senator Elizabeth Warren,[32] former Senator Sherrod Brown,[33] Harvard economics professor Kenneth Rogoff,[34] U.C. Hastings, Columbia and Vanderbilt law professors John Crawford, Lev Menand and Morgan Ricks,[35] and

Cornell law professor Saule Omarova.[36] Former Federal Reserve Governor Lael Brainard[37] and former Under Secretary of the Treasury Nellie Liang have argued that CBDCs may have benefits that outweigh their risks.[38] *Financial Times* journalist Martin Wolf has gone so far as to argue that all forms of private money should be banned.[39] Former Senator Brown and the law professors have all argued that a CBDC would foster financial inclusion by giving every U.S. citizen direct access to CBDC tokens, eliminating the role of commercial banks in creating private money and relegating them to the role of acting as mere distributors of the Fed's CBDC tokens.[40] Professor Rogoff has argued that a CBDC would enhance the Federal Reserve's monetary policy tools by giving it an effective tool to enforce negative interest rates,[41] the modern equivalent of monetary debasement.[42]

Conclusion

Payment stablecoins are a modern, digital version of private money. If a permitted stablecoin issuer has a properly calibrated reserve of liquid assets, capital buffer and no material amount of liabilities other than its stablecoin liabilities, as contemplated by the STABLE Act, its payment stablecoins should be as safe as insured bank deposits and central bank money. A CBDC would be a new form of public money that would compete with payment stablecoins and other forms of private money, such as demand deposit claims against commercial banks. The proponents of a U.S. CBDC have not demonstrated that the alleged benefits of a CBDC are greater than its costs and risks in terms of threats to financial privacy, financial freedom, financial stability, cybersecurity losses and other risks. Given the seriousness of these risks, the legal standard should be that the alleged benefits clearly outweigh the costs and risk. Nor have the proponents demonstrated that payment stablecoins issued by private actors would not produce most if not all of the alleged benefits of a CBDC without any of its risks. Finally, they have not demonstrated that the alleged risks of payment stablecoins would not be adequately addressed by a properly calibrated reserve, capital requirements, limits on non-stablecoin liabilities and the other provisions of a sound federal regulatory framework like the one that would be established by the STABLE Act.

Notes

[1] Paul H. Douglas, Earl J. Hamilton, Irving Fisher, Willford I. King, Frank D. Graham & Charles R. Whittlesey, *A Program for Monetary Reform* (July 1939), transcript of original plan at https://web.archive.org/web/20121103110209/http://home.comcast.net/~zthustra/pdf/a_program_for_monetary_reform.pdf. According to the authors of this program, otherwise known as the Chicago Plan, money issued by 100% reserve banks would have been as safe or safer than banks whose deposits were insured by the Federal Deposit Insurance Corporation, without creating the sort of moral hazard created by deposit insurance. The authors also argued that 100% reserve banking would not have any impact on monetary policy because every dollar of money issued by such a bank would be backed by a dollar of public monetary assets that would have been taken out of circulation.

[2] Virtually all commercial banks today maintain only a fractional reserve of high quality liquid assets (HQLAs) to back their demand deposit liabilities. The largest banks are also required to maintain a reserve of HQLAs equal to 100% of a presumed outflow of cash under severely adverse economic conditions as defined by regulation. The rest of their assets consist of longer-term and other illiquid loans, investments and other assets, which is why they are described as engaging in maturity or liquidity transformation: they transform longer-term and less liquid assets into demand deposit claims and other short-term or more liquid liabilities, and vice versa.

[3] For example, private credit money in the form of book entries on account books, promissory notes or trade tokens was the most common form of money for retail transactions in early England and America. It was issued by private actors pursuant to a natural or common-law right to do so, without the need for a government license or charter. The smallest gold or silver coins minted by the government had face amounts and market values that were several times higher than the price of a loaf of bread, a gallon of milk, a dozen eggs or a mug of beer. Private credit money satisfied the demand for something that could be used to pay for these basic commodities that the public money did not satisfy. See, e.g., Christine Desan, *Making Money: Coin, Currency and the Coming of Capitalism*, ch. 5 (Oxford Univ. Press 2014); Richard L. Bushman, *The American Farmer in the Eighteenth Century*, pp. 5-6 (Yale Univ. Press 2018).Bruce H. Mann, *Neighbors and Strangers: Law and Community in Connecticut, 1690-1760*, pp. 13-14 (Harvard Univ. Press 1987); William T. Baxter, *The House of Hancock: Business in Boston, 1724-1775*, pp. 39-40, 184-195, 204-208 (Harvard Univ. Press 1945). When goldsmith, private and country banks issued promissory notes designed to circulate as paper money in Great Britain starting around 1650, they also did so pursuant to the natural or common-law right to issue promissory notes without the need for a government license or charter. Even the Bank of England issued its banknotes for nearly two centuries pursuant to the natural or common-law right to do so. It did not receive an express license or charter from Parliament to issue banknotes until 1844 or later. These traditional actions reflect the general principle in the Western legal tradition that people have the freedom to engage in any activity they want unless the activity has been expressly prohibited by the government. See Thomas Hobbes, *Leviathan*, Book 2, Chapter 21 (1651), in Machiavelli, Hobbes, Great Books of the Western World, Vol. 23, p. 116 (U. Chi. Press & Encyclopedia Brittanica 1952). See also Isaiah Berlin, *Liberty* (Oxford University Press 1969); Eugene Schlossberger, *Entitlements, Liberties, Permissions, and the Presumption of Permissibility*, 34 J. Social Philosophy 537-544 (2003); *Positive and Negative Liberty*, Stanford Encyclopedia of Philosophy, https://plato.stanford.edu/entries/liberty-positive-negative/ (visited January 11, 2025).

[4] Bank of England Act, 7 Ann. c. 30, § LXI (1708).

[5] The monopoly included an exception for all banking partnerships with six or fewer partners. *Id*. That exception described virtually all of the English goldsmith, private and country banks that existed or were formed between 1650 and 1826. Those common-law banks issued paper money alongside the Bank of England and were responsible for virtually all of the paper money that circulated outside of London until 1826. In that year, the exception was expanded to include all common-law joint stock banks regardless of the number of their stockholders. Country Bankers Act of 1826, 7 Geo. 4 c. 46. At the same time, the Bank of England was authorized to open branches outside of London. *Id*. In 1844, the Bank of England's monopoly started a long march to becoming absolute throughout England, which was finally achieved in 1903. Bank of England, § 2: Bank Notes, pp. 25-37, The Statutory Rules and Orders Revised, Being the Statutory Rules and Orders (Other than Those of a Local, Personal, or Temporary Character) in Force on December 31, 1903, vol. I. The Bank of New York similarly commenced operations and started issuing paper money as a common-law bank in 1784 before it obtained a charter from the New York legislature in 1791. Henry Williams Domett, *A History of the Bank of New York, 1784-1884*, pp. 18-19, 31, 34-35 (G.P. Putnam's Sons 1884). Many if not most U.S. banks in the late 18th and early 19th centuries commenced operations as common-law banks before receiving bank charters from their respective state legislatures. See, e.g., An Act to Incorporate Certain Banks There Named, and to Extend the Charters of Existing Incorporated Banks, Acts of the First Session of Fourteenth General Assembly of the State of Ohio, vol. 14, pp. 913-924 (Chillicothe, OH: Nushee & Denny, February 23, 1816) (incorporating the following joint stock company banks that had previously commenced operations as common-law banks: Lebanon Miami Banking Company, Bank of Cincinnati, Urbana Banking Company, Columbiana Bank of New Lisbon, Farmers, Mechanics and Manufacturers' Bank of Chillicothe and the German Bank of Wooster). Even the Bank of England initially issued its banknotes pursuant to the common-law right to do so. It did not receive an express license or charter from Parliament to issue banknotes until at least 1844. Bank Charter Act of 1844, 7&8 Vict. c. 32. Professor Lawrence White has referred to unchartered British banks as free banks, especially those in Scotland. Lawrence H. White, *Free Banking in Britain: Theory, Experience and Debate, 1800-1845*, ch. 2 (Cambridge Univ. Press 1984). I prefer the term common-law banks to avoid confusing Scottish, English or Irish *unchartered* banks with U.S. *chartered* banks that were chartered under the so-called free-banking laws in the United States. At a minimum, I would call British unchartered banks classical free banks to distinguish them from U.S. chartered banks that were chartered under the U.S. free-banking laws.

[6] Omnibus Excise Tax Act, § 9, 14 Stat. 98, 146 (1866).

[7] 12 U.S.C. 378(a).

[8] Letter dated October 19, 1979 from Philip B. Heymann, Assistant Attorney General, Criminal Division, to Martin Lybecker, Associate Director, Division of Marketing Management, Securities and Exchange Commission.

[9] Critics of stablecoins have exaggerated the risk of a run on payment stablecoin issuers by ignoring how a properly calibrated reserve of liquid assets, capital requirements and activities restrictions would reduce any run risk to a negligible or even infinitesimal level. See, e.g, Report on Stablecoins, President's Working Group on Financial Markets, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency (November 2021) (emphasizing run risk as a major risk to payment stablecoin issuers as if they had the same risk profile as uninsured banks engaged in maturity or liquidity transformation and without adequately considering the offsetting effects of a 100% reserve of high quality liquid assets, a properly calibrated capital buffer to address any residual interest-rate or credit risk in the portfolio of reserve assets or provisions that prohibit the payment stablecoin issuer from incurring any material amount of liabilities other than stablecoin liabilities), available at https://home.treasury.gov/system/files/136/StableCoinReport_Nov1_508.pdf; Adam Levitin, *The GENIUS Act: Insolvency Risk with Stablecoins*, Credit Slips (Mar. 2, 2025), available at https://www.creditslips.org/creditslips/2025/03/the-genius-act-insolvency-risk-with-stablecoins.html.

[10] See, e.g., Frank J. Fabozzi, ed., *The Handbook of Fixed Income Securities*, at 197-98 (McGraw Hill 7th ed. 1983); Andrew Metrick, *The Failure of Silicon Valley Bank and the Panic of 2023*, 38 J. Econ. Persp. 133, 137 (2024).

[11] *Id*.

[12] See, e.g., Randall D. Guynn, *The Deposit Insurance Fund as an Early Resolution Tool* (draft of July 15, 2024), available at https://www.davispolk.com/insights/articles-books/deposit-insurance-fund-early-resolution-tool.

[13] OCC Interpretive Letter No. 1170, *Authority of a National Bank to Provide Cryptocurrency Custody Services for Customers* (July 22, 2020); OCC Interpretive Letter No. 1183, *OCC Letter Addressing Certain Crypto-Asset Activities* Mar. 7, 2025).

[14] A permitted payment stablecoin issuer would not fall within the current definition of the term "bank" in the BHC Act because it would not be an IDI and it would not be engaged in the business of both taking deposits and making commercial loans. Indeed, it would be prohibited by the STABLE Act from making any loans.

[15] Waters Stablecoin Discussion Draft, § 3(e)(2) (Dec. 3, 2024).

[16] Introductory Statement of House Financial Services Chairman Patrick McHenry on H.R. 5403 (Sept. 20, 2023), available at https://financialservices.house.gov/news/documentsingle.aspx?DocumentID=408980.

[17] See, e.g., Christopher J. Waller, Member, Board of Governors of the Federal Reserve System, *The U.S. Dollar and Central Bank Digital Currencies* (Oct. 14, 2022).

[18] Christopher J. Waller, Member, Board of Governors of the Federal Reserve System, *What Roles Should the Private Sector and the Federal Reserve Play in Payments?* (Nov. 12, 2024). See also Michelle Bowman, Member, Board of Governors of the Federal Reserve System, *Considerations for a Central Bank Digital Currency* (Apr. 18, 2023).

[19] Randal K. Quarles, Member and Vice Chairman for Supervision, Board of Governors of the Federal Reserve System, *Parachute Pants and Central Bank Money* (June 28, 2021).

[20] Diccon Hyatt, *A Digital Dollar from the Fed? Not on Jerome Powell's Watch*, Investopedia (Feb. 11, 2025).

[21] Testimony of Norbert J. Michel, Vice President and Director Center for Monetary and Financial Alternatives, Cato Institute, Hearing Before the House Financial Services Committee (Sept. 14, 2023); Nicholas Anthony and Norbert Michel, *Central Bank Digital Currency Assessing the Risks and Dispelling the Myths*, Cato Policy Analysis No. 941 (April 4, 2023), available at https://www.cato.org/policy-

analysis/central-bank-digital-currency.

[22] Dante Alighieri Disparte, Chief Strategy Officer and Head of Global Policy, Circle, *The Case Against Central Bank Digital Currencies*, International Economy (Summer 2022).

[23] See Michel Testimony, supra note 21, at 7.

[24] *Id*.

[25] Board of Governors of the Federal Reserve System, *Money and Payments: The U.S. Dollar in the Age of Digital Transformation* (January 2022).

[26] Id. at 2.

[27] Id. at 17.

[28] Executive Order No. 14067, *Ensuring Responsible Development of Digital Assets* (March 9, 2022).

[29] U.S. Department of the Treasury, *The Future of Money and Payments: Report Pursuant to Section 4(b) of Executive Order 14067* (Sept. 2022).

[30] Id. at 2.

[31] Executive Order, *Strengthening American Leadership in Digital Financial Technology* (Jan. 23, 2025).

[32] Greg Ahlstrand, *Elizabeth Warren Calls for US to Create a CBDC*, Coindesk (May 11, 2023).

[33] Banking for All Act, S. 3571 (Mar. 23, 2020) (introduced by Senator Brown) (granting authority for the Federal Reserve to issue a CBDC that would be directly available to all individuals who wanted them).

[34] Kenneth Rogoff, *Covid Coin?*, Project Syndicate Op-ed (August 20, 2020), available at https://www.project-syndicate.org/commentary/covid19-impact-on-rise-of-central-bank-digital-currency-by-kenneth-rogoff-2020-08. See also Kenneth Rogoff, *The Case for Deeply Negative Interest Rates*, Project Syndicate Op-ed (May 4, 2020); Kenneth Rogoff, *The Curse of Cash: How Large Denomination Bills Aid Crime and Tax Evasion and Constrain Monetary Policy*, Part II: Negative Interest Rates (Princeton Univ. Press 2016).

[35] John Crawford, Lev Menand & Morgan Ricks, *FedAccounts: Digital Dollars*, 74 Geo. Wash. L. Rev. 951 (2021); Morgan Ricks, John Crawford & Lev Menand, *Banking for All: A Public Option for Bank Accounts*, The Great Democracy Initiative (June 2018).

[36] See, e.g., Saule T. Omarova, *The People's Ledger: How to Democratize Money and Finance the Economy*, 74 Vanderbilt L. Rev. 1231 (2021).

[37] *Digital Assets and the Future of Finance: Examining the Benefits and Risks of a U.S. Central Bank Digital Currency*, Testimony of Federal Reserve Governor and Vice Chair Lael Brainard Before the House Financial Services Committee (May 26, 2022).

[38] Under Secretary of the Treasury for Domestic Finance, Nellie Liang, Remarks on Next Steps to the Future of Money and Payments, Workshop (Mar. 1, 2023).

[39] Martin Wolf, op-ed, *Strip private banks of their power to create money*, Financial Times (April 24, 2014).

[40] See supra notes 33, 35 and 36.

[41] See *Covid Coin?*, supra note 34.

[42] Debasement was the practice of Roman, medieval and early modern governments to devalue gold or silver coins by reducing the amount of gold or silver bullion in them either by recalling outstanding coins and replacing them with newly minted coins with a reduced amount of gold or silver bullion or by clipping or shaving some of the precious metal off existing coins. The public responded to debasements by increasing the price of goods and services, thus fueling inflation.