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Secretary
Board of Governors of the Federal Reserve
20th Street and Constitution Ave.
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RE: Docket No. OP-1747

Secretary Misback:

My thanks to you and the Board of Governors for the opportunity to comment on the proposed guidelines for evaluating account and services requests (proposed guidelines). As a member of the Community Depository Institutions Advisory Council (CDIAC), I have presented the concerns of Community Depository Institutions to the Board of Governors at both the Fall 2020 and Spring 2021 meetings. Further, as an engaged member of the Nebraska Bankers Association (NBA) I have worked closely with members of this association in identifying and defining the varying risks associated with this issue. With that in mind, you will find that my forthcoming comments are consistent with those expressed by the NBA.

At the heart of this issue is the protection of the integrity of the payment system, whose trust and reliability has been created and earned by the Federal Reserve System and Community Depository Institutions for over a century. Should the Federal Reserve move forward with implementing guidelines to evaluate applications for payment and master account services, at a minimum the following discussion points must be considered to help support the continued integrity of the payment systems and mitigate risks to the Federal Reserve Bank and the U.S. financial system:

Establish a coordinated evaluation committee. The decision to allow access to Reserve Bank accounts and services will have consequences for the Federal Reserve System, financial institutions, and potentially markets and the broader economy. Given this broad effect, and to advance the stated goal of creating a uniform evaluation policy, the Federal Reserve System should create a coordinated Board-led evaluation committee to review all applications for Reserve Bank accounts and services. Such centralization would improve the evaluation process and bring the unique expertise and perspective of Reserve Bank and various functional expertise of the Board to the review, bringing system-wide perspectives to bear.

Ensure an independent assessment of an institution's risk profile. In several sections, the Guidelines recommend that when evaluating an application a Reserve Bank incorporate, to the extent possible, the assessments of the applicant's state or federal supervisor into its own "independent assessment". While the perspectives of an entity's primary regulator should be considered where possible, we strongly support the Board's position that such assessments are insufficient, and the need for an "independent assessment" by the Board and Reserve Banks, which has a payment system oversight and financial stability mandate, is imperative.

Mandate ongoing Federal Reserve System review of entities not subject to federal supervision. Participants in the payment system should not be evaluated solely on policies and procedures outlined on their application. Rather, if granted access to the payment system, entities should be subject to ongoing supervision and disclosure requirements to ensure that they continually meet the Federal Reserve's expectations.

At a minimum, applicants should meet the standards required of federally insured or supervised financial institutions. In order to be granted an account, we recommend that entities must meet on an ongoing basis, the robust safety and soundness standards that federally insured or regulated institutions must meet. Applying such standards will ensure the applicant has sufficient capital and liquidity to weather stressful times, as well as robust and ongoing risk management identification, mitigation, and management processes, to mitigate the risk of shock transmission across the payment system.

The Guidelines for should be more precise. More clarity is needed on how the evaluation factors are defined and what standards must be met to obtain access to a Reserve Bank account and services. Clear and specific safety and soundness, and risk management standards will make the applying entities stronger, likely helping to mitigate concerns about the potential risks they pose. Moreover, a set of clear and precise standards and expectations would make the process more transparent and help ensure that the Reserve Banks apply, subject to coordination committee recommendation, the standards consistently.

Require audited financial reports. The Reserve Banks must be able to assess the condition of the account holders on its balance sheet on an ongoing basis. For those entities that do not file detailed Reports of Condition and Income (Call Reports) or similar reports, we recommend that periodic publicly disclosed and audited financial disclosures be required for access to Reserve Bank accounts and payment services. This reporting would provide the Reserve Banks and market participants the information necessary to assess an entity's condition on an ongoing basis.

Consumer protection. In order to obtain an account and to the extent the applicant services consumer customers, entities must demonstrate that they have an effective program to meet all relevant consumer protections, including those related to Regulation E.

Principle I – Institution Eligible Institutions

The Guidelines provide that those entities eligible to apply for access are limited to member banks or other entities that meet the definition of a "depository institution" under Section 19 (B) Federal Reserve Act. However, we do not believe that legal eligibility should be the sole criteria for granting access to FRB accounts and services. We would recommend that any entity that is not federally insured and which does not engage in any of the "core" banking activities, (such as accepting deposits and making loans of fiat current) should not have access to the payment system.

Importantly, any entity allowed to participate in the payment system must be subject to robust safety and soundness, regulation and supervision, on an ongoing basis, in order to protect all payment system participants and the payment system itself.

Not all entities that meet the eligibility requirements are federally insured or subject to federal supervision. In addition, in many instances, state supervision and regulation of entities with novel business models may lack the resources and thus the expertise to provide adequate supervision and regulation of these entities. As a result, as a criteria for initial consideration of granting access to FRB accounts and services, applicants should, at a minimum, meet (1) prudential and safety and soundness regulations which are equal to or greater than federally-regulated banks, including those relating to capital, liquidity, operational, and general risk management; (2) BS, AML, and U.S. sanctions program compliance; (3) requirements pursuant to the Graham-Leach-Bliley Act of 1999; and (4) federal consumer protection rules.

We would also recommend that the Federal Reserve employ a coordinated application review process since application decisions, criteria, standards and requirements will have a broad effect across the Federal Reserve System. A coordinated application review process will contribute to the goal of creating a uniform evaluation policy for review of all application, thereby ensuring consistent application of the final guidelines across all of the reserve banks.

Principal II – Reserve Bank Risk Exposure

The comprehensive prudential regulatory framework to which banks are subject fairly and adequately addresses the risks inherent in the “core” activities of the business banking. Under the proposed Guidelines, the bank regulatory framework serves as the baseline for assessing the risk profile of entities requesting access to the payments system.

However, while a good starting point to evaluate applicants seeking access to the accounts and services of the Federal Reserve System, the risk profile of entities that may be legally eligible to hold accounts at the FRB will most likely require additional review and enhanced measures to mitigate the risk of their activities. As a result, the Board should consider additional standards and processes for entities that are legally eligible for master accounts, commensurate with the risks the entities pose.

We believe that the Guidelines should require robust risk management and stress testing frameworks. In this regard, we would recommend that entities desiring access to the payments system have robust risk management frameworks and governance arrangements in place, similar to those employed by traditional banks, regarding liquidity risk, credit risk, interest rate risk, operational and other risk, as appropriate. Furthermore, these entities should be required to engage in periodic stress testing and other analysis to prepare for and mitigate stressed economic and business conditions.

It is vitally important that the Guidelines establish appropriate levels and composition of capital and liquidity for new entrants to the payment system. All entities must meet high capital, liquidity, and general risk management standards to ensure that a sufficient level of capital and liquidity is maintained, commensurate with risks posed by unique business activities. The Board should require, as a condition to obtaining a master account or access to FRB services that entities maintain capital levels

comparable to that with which federally-insured banks must comply. Even higher capital requirements should apply as needed, commensurate with an entity's complexity and risk profile. In addition, since all entities that may legally qualify for access to FRB accounts and services are federally insured or have access to the discount window, the Guideline should clarify the liquidity requirements necessary to compensate for the absence of deposit insurance and access to the discount window.

It is important that all interested parties, are able to assess an eligible entity's financial condition and ability to settle and process payments. Accordingly, the Federal Reserve should make public, audited financial statements a condition of access to a master account. Public and frequent reporting of key financial data, including capital levels and composition of high-quality liquid assets, will assist in ensuring that new entrants into the payments system, do not create undue risks to the FRS, the banking industry, or the broader financial system.

Access to FRB accounts and services should be accompanied by requirements that entities demonstrate that their cyber security, operational resilience, and business continuity practices are aligned with their risk, pursuant to the FFIEC *Information Technology Handbook* and other federal guidance.

Eligible institutions holding crypto assets may be exposed to additional operational and cyber risks targeting distributed ledger platforms. Accordingly, we would encourage the Board to require any applicants holding crypto assets to mitigate the operational risks associated with holding crypto currencies and similar digital assets identified by the Basel Committee.

Principal III – Payment System Risk Exposure

Federally insured banks are subject to robust regulation and consumer protection requirements. These regulations and requirements are essential to maintaining and enhancing confidence in the payment system.

Similar controls should be applied to all applicants for FRB accounts and services. If an entity's business model presents additional risk, it must be subject to a commensurate risk mitigation program, including appropriate levels of capital and liquidity.

Principal IV – Risks to the U.S. Financial System

The proposed Guidelines state that "provision of account services to an institution should not create undue risk to the stability of the U.S. financial systems". Some state-chartered entities, such as the special-purpose depository institutions or "digital asset banks" will deal extensively with crypto assets. The present volatility of this marketplace could adversely affect the institutions or "banks" that are dealing in crypto assets as their core business activity and could significantly affect their revenue streams. The stress that disruption or instability in the crypto currency market would have on these institutions and "banks" could have an adverse impact on the broader banking and payments system. If these new potential entrants are not held to the same regulations as banks that are federally insured, granting access to FRB accounts and services will present significant potential risks, increasing the risk to the overall financial system, especially in times of economic hardship and stress. Based on the foregoing, entities that are not federally insured should, if they are to be granted access to FRB accounts and services, receive enhanced review, commensurate with the risks they pose.

Principal V – Prevent Financial Crimes

All applicants, particularly those dealing extensively in crypto assets should have a BSA/AML compliance program that includes robust internal controls, independent auditing and compliance appropriate training for staff, and senior management commitment. If it is engaging in the emerging financial transactions such as crypto currency custody and related payments services, it should be held to a risk management standard commensurate with their risk profile. We would further recommend that each entity be required to identify the counterparties in crypto currency transactions and have a robust anti-money laundering regime, requiring them to be able to identify the country of origin of crypto currency transactions.

Again, thank you for the opportunity to comment on this critically important issue. The decision to allow access to Federal Reserve Bank accounts and services has potentially tremendous implications and consequences to the Federal Reserve System, Community Depository Institutions, and the broader economy. Because of this, the Federal Reserve should establish detailed, transparent requirements and proper oversight to evaluate applications and protect the payment system.

Sincerely,



Brad Koehn,
Regional President