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COMMERCE, SCIENCE, AND TRANSPORTATION
ENVIRONMENT AND PUBLIC WORKS

12 July 2021

Board of Governors of the Federal Reserve System
20th Street & Constitution Avenue, NW
Washington, DC 20551

(*sent electronically)*

Re: Comment Letter—Proposed Guidelines for Evaluating Account and Service Requests (Board Docket No. OP-1747)

Dear Chair Powell and Members of the Board,

Thank you for the Board of Governors' ("Board") attention to the important issue of depository institution access to accounts and services ("master account") at the Federal Reserve Banks ("Reserve Banks"), and for the opportunity to comment on the draft proposal under consideration.

This is an area of growing interest to many depository institutions and an area that will immensely benefit from uniform, even-handed prudential standards firmly grounded in the statutory factors established by Congress in the Federal Reserve Act. The proposed guidelines are also an important step towards promoting responsible innovation in our financial system.

Many of the entities which will benefit from these guidelines are not fully within the regulatory perimeter of the Board and other prudential supervisors currently. In an era of technology that is disrupting certain preconceived notions in the financial services industry, it is advantageous for supervisors to fully understand the business models and operations of financial technology companies and to ensure that they are managing their risks. The proposed guidelines are an important first step towards bringing more innovative business models into the system and facilitating appropriate supervision, commensurate with other depository institutions.

Furthermore, encouraging settlement in central bank money through a depository institution master account is itself an important step in reducing systemic risk. There is virtually no credit or settlement risk associated with a master account. Consequently, depository institutions, affiliate non-bank financial institutions and customers can have confidence that their value is buffered from systemic risks of the U.S. financial system. In a correspondent scenario above the deposit insurance limit, the failure or impairment of one depository institution can have knock-on effects on other depository institutions and financial entities, like broker-dealers. Facilitating greater settlement in central bank money for depository institutions—within the bounds set by Congress—will therefore have a positive effect.[1]

[1] *See, e.g.*, Mark Carney, *The Art of Central Banking in a Centrifugal World,* at *9, Bank for Int'l Settlements (28 June 2021), *available at* https://www.bis.org/events/acrockett_2021_speech.pdf ("More generally, the ability to access central bank money acts as an anchor for value, given cash is a universally available and accepted safe asset.").

Instead of a digression into each component part of the proposed guidelines, this letter will analyze specific issues that I feel need clarification or emphasis. I look forward to collaborating with you and Board staff to continue to make progress in this important area and to ensure we have a robust, safe, efficient and innovative payment system that underscores the United States' leadership role in the global financial services industry.

1. Eligibility

The proposed guidelines correctly recognize that, in existing law, both federally-insured and non-federally insured depository institutions are legally eligible for Reserve Bank accounts and services.[2] This comports with Congress' statutory mandate in the Federal Reserve Act that a "depository institution" which is either an "insured bank" and one which is "eligible to make application to become an insured bank" is eligible to apply for a master account.[3] Furthermore, the guidelines also recognize that both a state and federal bank supervisor are not legally required.[4]

It is important to note that Congress delegated to the Federal Deposit Insurance Corporation ("FDIC") the authority to determine the scope of depository institutions eligible for insurance under the Federal Deposit Insurance Act by explicitly referencing "section 5 of such Act [the FDI Act]" in 12 U.S.C. § 461.[5] In a 1980 interpretive letter, the FDIC adopted guidance regarding eligibility to apply for deposit insurance under the authority granted by Congress in the Monetary Control Act of 1980, which amended the Federal Reserve Act. It is a well-established principle of statutory interpretation that a particular provision's placement in the statute book is not dispositive of the meaning of the enacted text.[6] The 1980 FDIC guidance establishes the following criteria for determining if a depository institution is eligible for insurance under the FDI Act:

(1) A bank must be engaged in the business of receiving deposits other than trust funds (based on the text of 12 C.F.R. § 303.14), acknowledging that "[t]he authority to receive deposits is not a generally recognized implied power of a corporation. Such power must be expressly conferred . . ."; and
(2) A state-chartered financial institution must be chartered by its state of incorporation as a "bank," and the FDIC will look to the characterization of the institution by the laws under which the institution is created.[7]

The FDIC confirmed the first principle in a subsequent 1985 advisory opinion, noting that Colorado law did not explicitly authorize a trust company to receive deposits, and that Colorado

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[2] *Proposed Guidelines for Evaluating Account and Service Requests,* Bd. of Gov. of the Fed. Res. Sys., 86 Fed. Reg. 25865, 25866 (11 May 2021) ("Reserve Bank assessments of access requests from non-federally-insured institutions, however, may require more extensive due diligence.") [hereinafter Proposed Guidelines].
[3] 12 U.S.C. § 248a; 12 U.S.C. § 461(b)(1)(A).
[4] Proposed Guidelines, at 25866–68 ("state and/or federal supervisors").
[5] 12 U.S.C. § 461(b)(1)(A).
[6] *See, e.g.,* 5 U.S.C. Front Matter, at 10 (2021) ("An inference of a legislative construction is not to be drawn by reason of the location in the United States Code of a provision enacted by this Act or by reason of the caption or catchline thereof.").
[7] *Statement Regarding Eligibility To Make Application To Become an Insured Bank Under Section 5 of the Federal Deposit Insurance Act*, Fed. Deposit Ins. Corp., 45 Fed. Reg. 77517–18 (24 Nov. 1980).

law authorizing fiduciary activities involving the receipt of customer funds was not sufficient.[8] This letter emphasized that the state law characterization of the institution's powers was paramount and, additionally, that:

> [w]e find nothing in any other provision of C.R.S. § 11-23-103 that empowers a trust company to engage in the business of receiving deposits, other than "trust funds," as defined in section 3(p) of the FDI Act. To meet the threshold requirement, trust companies need first to be empowered to receive deposits, on a simple debtor-creditor basis, from individuals, corporations, partnerships, or other eligible entities, acting in their respective rights and capacities as such.[9]

Following the 1985 interpretive letter, the Colorado General Assembly amended its trust company statutes to sever the link between customer fiduciary funds and deposits, authorizing Colorado trust companies to "maintain savings deposits, time deposits, and certificates of deposit and other accounts for which a trust company is empowered to act under this article."[10] Most importantly, the FDIC affirmed that "[t]he authority to accept 'deposits other than trust funds' must be expressly granted by state law; inasmuch as the authority to receive deposits is not a generally recognized implied power of a corporation, the FDIC will not infer such authority in the absence of an express statutory grant."[11]

Consequently, if authority to receive deposits is clearly established as a matter of state law with respect to a chartered banking corporation, it is abundantly clear that the institution meets the definition of "depository institution" for the purposes of relevant sections of the Federal Reserve Act and threshold legal eligibility for a master account. Mark Carney, former Governor of the Banks of England and Canada, rightly has acknowledged that matters relating to the eligibility of financial institutions to access central bank money is a matter best left to the political branches:

> Given the broader issues that the new money raises … authorities beyond central banks should shape the decisions about which private options get the possibility of [central bank money] access, while the central bank will always be the final arbiter of who is able to draw upon it.[12]

2. Role of Chartering Authority/Supervisor

The proposed guidelines state that Reserve Banks "should incorporate, to the extent possible, the assessments of an institution by state and/or federal supervisors into its independent assessment of the institution's risk profile."[13]

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[8] *Deposit Insurance for Colorado Trust Companies*, Advisory Op. 85-14, Fed. Deposit Ins. Corp. (17 Jun. 1985), *available at* https://www.fdic.gov/regulations/laws/rules/4000-1770.html.
[9] *Id.*
[10] *Insurance Coverage of Deposits Maintained in Colorado Trust Companies*, Advisory Op. 88-67, Fed. Deposit Ins. Corp., (23 Oct. 1988), *available at* https://www.fdic.gov/regulations/laws/rules/4000-3570.html.
[11] *Id.*
[12] Carney, *supra* note 1, at *9.
[13] Proposed Guidelines, at 25868.

This statement recognizes the fact a depository institution's chartering authority and primary supervisor understands the characteristics and risks of the institution in the most detailed manner. While the guidelines appropriately require each Reserve Bank to conduct its own assessment, the Reserve Bank analysis should give great weight to the chartering authority's views and the Reserve Bank should generally accept them if the Reserve Bank determines that the views of the primary supervisor have a sound basis in the principles of bank supervision and appropriate law.

I commend President George and the Federal Reserve Bank of Kansas City's collaborative and transparent process in analyzing Wyoming's special purpose depository institution bank charter over the last year. This exemplifies the "extensive due diligence" cited in the proposed guidelines.[14] The Board and Reserve Banks should ensure that "extensive due diligence" has a defined end point and that a decision is rendered in an appropriate timeframe without delay.

I am pleased that the "extensive due diligence" in which many of the Wyoming charter applicants have undergone is nearing completion. However, it is important the Federal Reserve take swift action on the pending Wyoming applications after finalization of the proposed guidelines, given that the Wyoming applicants meet all factors of the proposed guidelines.

3. Conditions

The proposed guidelines appropriately assume that each master account application is different, and that each Reserve Bank should have the flexibility to only approve certain accounts or services with respect to a particular depository institution. This is reflective of the fact that each depository institution's relationship with a Reserve Bank should be tailored to the business model of the institution.

For example, the Wyoming special purpose depository institution is prohibited from on-balance sheet lending by law.[15] The Wyoming special purpose depository institution is nonetheless a "depository institution" and "state bank" because it accepts demand deposits and serves a custodial bank function—acknowledged by the Board to be a critical function for the financial system, and one in which certain existing banks focus a majority of their operations upon.[16] For these reasons, a Wyoming special purpose depository institution likely does not require access to the discount window and presents a reduced credit risk to a Reserve Bank because of the requirement that it maintain 100% of demand deposits as high-quality, liquid assets.[17] Similarly, a nationally-chartered trust company is not permitted to accept deposits under the National Bank Act,[18] and

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[14] *Id.* at 25866.
[15] *See* Wyo. Stat. § 13-12-103.
[16] *Regulatory Capital Rule: Revisions to the Supplementary Leverage Ratio To Exclude Certain Central Bank Deposits of Banking Organizations Predominantly Engaged in Custody, Safekeeping, and Asset Servicing Activities*, Bd. of Govs. of the Fed. Res. Sys., 85 Fed. Reg. 4569, 4570 (27 Jan. 2020) ("Fiduciary and custody clients often maintain cash deposits at the banking organization in connection with these services. Clients typically maintain cash positions consisting of funds awaiting investment or distribution that are often in the form of deposits placed in banking organizations. These cash deposits help facilitate the administration of the custody account. Under U.S. generally accepted accounting principles (U.S. GAAP), cash deposits at a banking organization are a deposit liability and thus appear on the banking organization's balance sheet.").
[17] *See, e.g.*, Wyo. Stat. § 13-12-105(a).
[18] 12 U.S.C. § 92a(d) ("No national bank shall receive in its trust department deposits of current funds subject to check or the deposit of checks, drafts, bills of exchange, or other items for collection or exchange purposes.").

does need to use U.S. Dollar services, but the trust company may want to use certain securities-related services.

4. Conclusion

I commend the Board and staff for their work on this important, emerging issue and their ongoing mission to promote responsible innovation in our financial system. This is essential to ensuring America remains a leader in global financial services for the next generation.

I believe Wyoming has acquitted itself well over the last two years in responsibly integrating digital assets into our banking system. The proposed guidelines appropriately require each Reserve Bank to evaluate whether the chartering authority has a robust regulatory program to oversee a depository institution. From developing the first holistic legal framework around digital assets in the United States, to developing a 771-page supervisory manual for bank digital asset activities, my home state has demonstrated that responsible innovation can effectively co-exist with responsible risk management and bank-grade regulatory requirements.

The proposed guidelines rightly acknowledge that master account access is not an endorsement of the business model or approval of the activities of a depository institution, and consequently, any policy or precedent-focused concerns should be cabined exclusively within the articulable risks of a particular institution, e.g., Bank Secrecy Act/sanctions, operational risk, credit risk to Reserve Banks, etc.[19]

It is important that Wyoming's special purpose depository institutions begin operations as soon as possible, in light of the "extensive due diligence" that has already occurred, and the fact that it is better to have these activities inside the regulatory perimeter than outside.

I strongly encourage you to finalize the proposed guidelines as soon as possible to bring much-needed clarity to this space. I will be monitoring further developments closely.

Thank you again for the Federal Reserve's focus on this important issue and for the hard work of Board staff in preparing the proposed guidelines.

Sincerely,

Senator Cynthia M. Lummis

[19] Proposed Guidelines, at 25867 ("Establishment of an account and provision of services by a Reserve Bank under these guidelines is not an endorsement or approval by the Federal Reserve of the institution.").