



AFJM's May 19, 2022, response to the Fed's January 2022 paper on "Money and Payments: The U.S. Dollar in the Age of Digital Transformation"

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CBDC Benefits, Risks, and Policy Considerations

1. What additional potential benefits, policy considerations, or risks of a CBDC may exist that have not been raised in this paper?

*A potential benefit, not considered in this paper, is that CBDC can provide a pathway toward ending bank creation of money altogether. Compelling reasons for ending bank creation of money have been given recently by Omarova in "The People's Ledger" (<https://scholarship.law.vanderbilt.edu/vlr/vol74/iss5/1/>) and previously by many others (see *THE LOST SCIENCE OF MONEY*, by Stephen Zarlenga, 2002). In that way money creation through the Fed can become available to serve the needs of society as a whole. Banks can continue to meet borrowing needs by lending pre-existing CBDC instead of creating it themselves out of credit. Money created by a public central bank can be directed to meeting public needs.*

Indeed, we believe the only logical, viable, stable, Constitutional, economically sound and just way for CBDC to be introduced is part and parcel with sovereign money reform, as laid out in the 2011-12 National Emergency Employment Defense Act (<https://www.congress.gov/bill/112th-congress/house-bill/2990>), which the Alliance For Just Money (monetaryalliance.org) has updated for 2022 as the American Monetary Reform Act (AMRA, available upon request, reform@monetaryalliance.org).

Another potential benefit of the shift from bank created money to central bank created money is that it could begin to address the extreme maldistribution of wealth that currently threatens democracy and social stability. New money created by banks goes to those who already have money; it concentrates wealth. Spending of newly created money on public needs through CBDC provided to the government with no corresponding debt has the potential to counteract wealth concentration by distributing the country's resources more evenly, and more justly.

2. Could some or all of the potential benefits of a CBDC be better achieved in a different way?

Yes. Digital currency could be issued by the Treasury Department instead of by the Fed. New money could then be spent into circulation, as the Greenbacks were, rather than being lent into circulation. That could bring the expansion of public debt to a close. It would have to be done with guardrails against government spending exceeding the capacity of the economy to use it for expanded production of goods and services. The above-mentioned legislation lays out how this transition to wholly public money can be achieved in a graceful and timely manner and be effectively maintained and modulated over time by an independent monetary authority in the Treasury.

3. Could a CBDC affect financial inclusion? Would the net effect be positive or negative for inclusion?

It could have a positive effect, but it depends upon how it is done. Automatic opening of Fed Accounts for everyone, plus access through the post office could certainly improve financial inclusion.

4. How might a U.S. CBDC affect the Federal Reserve's ability to effectively implement monetary policy in the pursuit of its maximum-employment and price-stability goals?

Monetary policy, via the setting of interest rates and open market QE, has never been very effective in achieving these ends.

A. A CBDC which can be channeled into government spending in the public interest could certainly do a better job of keeping people employed. There is certainly much to be done that can be done by human power.

B. Having the central bank (or monetary authority in the Treasury) actually control the money supply would do much to control booms and busts that are known to be accentuated by bank creation of money. Price stability is shaken by booms and busts, although it is also affected by other things. Central bank control of the money supply could potentially eliminate or at least attenuate the boom/bust oscillations, but it would depend on the ability of the government bureaucracy, including elected representatives and monetary professionals all working as public servants, to be able to respond with adequate speed.

5. How could a CBDC affect financial stability? Would the net effect be positive or negative for stability?

As pointed out in #4 above, central bank or public control of the money supply could switch the money supply system from being an unstable, positive feedback system to being a stable negative feedback system. In the current system of bankmoney creation, the money supply grows when growth is not needed and shrinks when it is needed – the boom/bust amplifier. Central bank control, done in partnership with the Treasury Department could reverse that and stabilize the system.

6. Could a CBDC adversely affect the financial sector? How might a CBDC affect the financial sector differently from stablecoins or other nonbank money?

The financial sector will have to change in response to the introduction of CBDC. If money creation shifts from commercial banks to the central bank, banks will have to shift their business plan. They will have to shift to credit intermediation from credit generation, in the terms of Hockett and Omarova's "The Finance Franchise" (<https://scholarship.law.cornell.edu/clr/vol102/iss5/1/>).

Stablecoins are an entirely unsatisfactory basis for a money supply. Despite promises of staying linked to the dollar through risk-free investment in treasuries, they will go beyond it, just as Money Market Mutual Funds can and did. Stablecoins will have to be bailed out in the next crash just as MMMFs were in 2008.

7. What tools could be considered to mitigate any adverse impact of CBDC on the financial sector? Would some of these tools diminish the potential benefits of a CBDC?

During the transition from money creation by commercial banks to money creation by the central bank, banks may have to borrow from the Fed in order to sustain their liquidity. In the long run, investment money flowing into banks for lending on a credit intermediation basis will sustain liquidity.

8. If cash usage declines, is it important to preserve the general public's access to a form of central bank money that can be used widely for payments?

Yes. It is also clear that digital access is not available to nor preferred by all, and we also must be ready for internet and/or electric grid disruptions. Thus, cash must remain a sanctioned and accessible medium of exchange. It should be forbidden for a business or unit of government not to accept legal tender of any form.

9. How might domestic and cross-border digital payments evolve in the absence of a U.S. CBDC?

In the absence of a CBDC banks will continue operating their payment services, but other private digital currencies and so-called "stablecoins" will compete and are likely to destabilize the system.

10. How should decisions by other large economy nations to issue CBDCs influence the decision whether the United States should do so?

*The decision of whether, how, and when to implement CBDCs should be based on a studied conclusion that it will help the United States people, not on whether other countries are doing it. But if we don't move to have better control over our monetary system and economic resources, we will fall behind. Credit guidance, that is, directions from the central bank over how and from Congress over where newly created money goes—can play a major role. It was essential for the rapid recovery of Japan following WWII, as documented by Richard Werner in his 2003 book, *PRINCES OF THE YEN*, and for the rapid industrialization of China in the recent past decades.*

11. Are there additional ways to manage potential risks associated with CBDC that were not raised in this paper?

A. RISK OF CHANGE TO FINANCIAL-SECTOR MARKET STRUCTURE. A non-interest-bearing CBDC is the way to go. A CBDC must function to protect the payment system, not serve as an investment vehicle. Investments should reside in the private sector. CBDC must provide safety, not a profit source.

B. SAFETY AND STABILITY OF THE FINANCIAL SYSTEM. It is not clear that limits will need to be placed on CBDC holdings, especially if the CBDC is non-interest bearing. Should a need for limits become apparent, it can be achieved via demurrage on the portion of a balance that exceeds the limit for longer than allowed, a charge that can be easily avoided by the account holder moving the excess CBDC to a time deposit, savings-and-loan account, or investment fund.

C. EFFICACY OF MONETARY POLICY IMPLEMENTATION. The real purpose of monetary policy is to determine how much money is and should be in the system and how needed new money is introduced into circulation (i.e., spent, lent, given, or invested) or (much rarer) how to withdraw some existing money from circulation (i.e., taxed or borrowed out of the economy). Congress then decides who gets the new money for what public purposes. Currently the Fed does not

control the money supply. It influences it by the setting of interest rates and open market operations, but these are weak tools. They are clumsy, imprecise, and only indirect.

With CBDC, money creation by banks could be halted and the Fed could actually control the money supply in the public interest. In addition, all the seigniorage from the creation and first use of newly issued CBDC, coins, and even paper bills can go to the public sector, unlike in our 109-year-old FRBS in which banks gain the seigniorage from all the paper notes and bankmoney, which together comprise over 96% of our money supply. This would be a net gain for the public.

12. How could a CBDC provide privacy to consumers without providing complete anonymity and facilitating illicit financial activity?

Government needs to know financial information from individuals in order to receive or refund taxes and to determine if they are paying their taxes appropriately. Anonymity would only facilitate illicit activity. Powerful private companies already monitor how we spend our money. We see a strong need for privacy and respect for privacy, but no need for anonymity. What is needed is more transparency, not less. There are already certain "firewalls" within the government to protect financial information, particularly between the IRS and other branches. Such could be created to protect CBDC accounts to strike the proper balance among privacy, confidentiality, accountability, and transparency.

Within commerce, the vast majority of money transactions are transparent; we write checks, use credit cards, bank transfers, etc. That private information is protected and regulated and subject to normal legal accountability and due process. A relatively small amount of money is in the form of cash which does provide near anonymity, though each bill has identifiable serial numbers and dates. The same level of legal protections and privacy should and can be provided to CBDC as is provided for our current form of digital money (bankmoney). The same level of accountability by users of the public utility, legal tender, should also be expected.

Despite our belief in the possibility of good government, much of the public is skeptical. The Fed being bank-focused and the limitless role of money in politics today are reasons for distrust. This skepticism and wide-spread ignorance about money and our monetary system are the best protections our current system has, a state of affairs we find tragic. Recent actions by federal governments to shut off the bank accounts of people and foreign governments when they don't like what those parties are doing, without the formal processes required by law, makes achieving CBDC and Just Money much harder.

13. How could a CBDC be designed to foster operational and cyber resiliency? What operational or cyber risks might be unavoidable?

This is an important concern. But it is not unique to CBDC. It is a growing challenge that CBDCs and any sovereign Just Money system share with all types and levels of industry, financial and otherwise. Regarding operational and cyber resiliency for CBDC, central banks and their associations such as the Bank for International Settlements (BIS) have been developing payment, clearing, and settlement systems over centuries already, for the digital age since 1980 (<https://www.bis.org/cpmi/history.htm?m=3066>). Technologies like blockchain, cryptography,

and distributed ledgers can also play a role in CBDC if they prove to be compatible with the demands of ecological sustainability.

Regarding cybersecurity, correcting our money system will not alleviate all financial fraud. But it will eliminate the moral hazard widely understood to be built into modern banking (see McMillan's 2014 THE END OF BANKING, pp. 16, 40-46, 84, 98, 117, 179-80). That will foster operational, cyber, and human resiliency not only for our money system but also in the wider economy, especially in big tech, and in the culture at large.

14. Should a CBDC be legal tender?

Absolutely. Without it being legal tender, you would just be playing games at the expense of people and planet.

CBDC Design

15. Should a CBDC pay interest? If so, why and how? If not, why not?

No. As stated above, a CBDC must function to protect the payment system and to protect the money used in the payment system by providing a safe digital account. Money is not a liability but our liquid asset. CBDC is not to function as an investment vehicle. Investments and profit-making should reside in the private sector. CBDC must provide safety, not a profit source.

16. Should the amount of CBDC held by a single end user be subject to quantity limits?

This is not likely to be needed as long as CBDC accounts remain non-interest-bearing. The rules should apply equally to all forms of money. See also our response to #11.

17. What types of firms should serve as intermediaries for CBDC? What should be the role and regulatory structure for these intermediaries?

For CBDC to be inclusive, many intermediaries have to be involved. For transaction accounts, as long as the contracts with the intermediaries are well written, it could be a variety of firms, public or private, including post offices and public banks. They will have to be compensated appropriately for the work they perform as intermediaries. In the case of usage of private firms, the cost could be borne by the individual holders of the Fed Account as the market bears. In the case of usage of the post office or other public providers, the cost, if borne by users, must be kept low.

Savings-and-loan and investment services for central bank money (CBM), including CBDC, should be entirely in the private sector. Trying to placate private industry is not the job of government. Banks or peer-to-peer lenders should do what they do best, authenticate and facilitate loans to credit-worthy borrowers, lending their own money or savers' time deposits; they should no longer be able to create money out of credit. Investment firms will invest their and their shareholders' or investors' funds at their own risk. If Congress wants to appropriate funds for certain types of public purpose lending, this may be funneled through the Treasury's underwriting facilities.

The payments system of banks, savings-and-loan, credit card providers, etc. has to be appropriately regulated, and so should any fintech competitors among those systems. But, as McMillan (2014) points out, once money and credit are distinct, with the public creation and modulation of money and the private organization of credit, “credit no longer requires a special treatment....Government should implement a competitive regulatory framework around credit that treats the financial industry just like any other industry. In essence, such a framework includes an effective and efficient legal system to enforce private contracts, the prosecution of market participants that engage in fraudulent practices, and antitrust laws to ensure that markets are not cartelized or monopolized by powerful actors” (pp. 165-6).

18. Should a CBDC have “offline” capabilities? If so, how might that be achieved?

Probably not. This is a digital currency; that means online and/or in electronic accounts. Offline transactions can still occur using US bills and coins issued by the central bank or Treasury Department. Small denomination and refillable CBDC smart cards like gift cards or sim cards could be purchased and used at retail stores that have or develop their own internal point-of-sale swiping systems.

19. Should a CBDC be designed to maximize ease of use and acceptance at the point of sale? If so, how?

Yes. Payment by check or electronic transfer should be made possible to convert one’s bank money to CBDC. Use of debit cards should continue with CBDC. The so-called fintech industry is developing and providing these services already. Again, we advocate all US money in circulation, whether paper, coin, digital or account-based, be public money and legal tender, what we call sovereign or Just Money.

20. How could a CBDC be designed to achieve transferability across multiple payment platforms? Would new technology or technical standards be needed?

Different payment platforms will simply need their own CBDC accounts. As described by Hockett and Omarova in their 2017 “The Finance Franchise,” this occurs now with “peer-to-peer” payment systems in that these platforms all have their own bank accounts.

21. How might future technological innovations affect design and policy choices related to CBDC?

Technology does drive change, but it should not obscure the fundamentals of policy making in a democracy. The fundamentals are that we need a monetary system, free of special privilege, that serves all. We need a reliable, secure, and easily accessible payment system, but we do not need to optimize wealth accumulation by pandering to the needs of financial traders for ultrafast transactions.

22. Are there additional design principles that should be considered? Are there tradeoffs around any of the identified design principles, especially in trying to achieve the potential benefits of a CBDC?

Design principles to achieve the potential benefits of a CBDC are the following:

A. In shifting to CBDC, money creation itself must shift entirely from commercial banks to the Fed or central bank, as detailed in Omarova’s 2021 “The Peoples’ Ledger,” and Huber’s 2017 “The case for a central-bank currency register” (<https://sovereignmoney.site/how-to-account->

for-sovereign-money). The payment system must come to reside wholly in an institution that can offer the full faith and credit of the United States Government. The “tradeoff” here is that it will require a change in business plans for commercial banks, in which their lending will no longer be based on creating deposits, but will utilize pre-existing money coming into banks from savers as time deposits, or from investors, or from the Fed itself, if needed.

B. The Fed or central bank must be enabled to fund the federal government directly with zero-interest loans—essentially grants if not actually sovereign money—issued either in perpetuity or with guaranteed, unlimited rollover privileges in order that government can meet public needs by spending (or giving, investing, or lending interest-free) in the public interest limited, not by money, but only by the availability of labor and of sustainably available raw materials.

C. CBDC accounts must be free of interest payments and be available to all who participate legally in the nation’s economy. Access to accounts must be easily and safely available through both private and public intermediaries, for instance through post offices, as suggested above, for those without internet service.

FURTHER COMMENT: The definition of CBDC given in the 2nd paragraph of the Executive Summary and on p. 13 of the Fed paper “Money and Payments: the US Dollar in the Age of Digital Transformation” is inappropriate. It is an anachronism, a holdover from the age of gold-backed dollars; it does not describe a monetary system of fiat money. There is absolutely no justification for regarding CBDC as a liability of the central bank. Rather it is described properly as our social equity (Kumhof et al., 2020, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3730608) or our liquid asset (Huber, 2017, cited above).

These features of a monetary system, which can be utilized in or be the context for CBDC, were put in the form of legislation and introduced into Congress in 2011 as the National Emergency Employment Act (NEEA Act, <https://www.congress.gov/bill/112th-congress/house-bill/2990>). The Alliance For Just Money (AFJM, monetaryalliance.org) has updated this legislation for 2022 as the American Monetary Reform Act (AMRA, available upon request, reform@monetaryalliance.org).

Finally, at AFJM’s annual meeting in July 2020, the AFJM membership ratified a “Resolution on the Establishment of a National Commission of Inquiry Into the Monetary System of the United States of America” passed by our Board in March 2020 and first proposed in 1994 by renowned U.S. economist Dr. Hyman Minsky. This Resolution, including a link to Dr. Minsky’s paper, are available at <https://www.monetaryalliance.org/resolution-number-one/>. AFJM continues to believe the US Monetary System is our most primary matter of public policy, and it warrants open, broad, public dialogue in the halls of Congress, in the state houses, county boards, city and town councils, and in the classrooms, community centers, and places of business across this country, including within the Board of Governors and the 12 FRBs of the Federal Reserve System.

We would be at your service for fuller exploration of and collaboration on the ideas presented here. Thank you for your time and consideration. We look forward to hearing from you.

~~Board of Directors, Alliance For Just Money, Inc., May 19, 2022