Remarks by Under Secretary for Domestic Finance Nellie Liang During Webinar Hosted by Harvard Kennedy School's Mossavar-Rahmani Center for Business and Government

September 20, 2022

INTRODUCTION

Thank you, Tim, for inviting me to speak here today about the recent report on the future of the U.S. money and payment system, which was written as part of President Biden's Executive Order on Ensuring Responsible Development of Digital Assets. This report was released late last week, along with two others led by Treasury: one focused on current use cases for crypto-assets and their effects on consumers, investors, and businesses, and another laying out an action plan to prevent these assets from being used for illicit finance. And next month, the Financial Stability Oversight Council will issue a report on the financial stability risks of digital assets and any regulatory gaps.

To look to the future of money and payments, I want to start with where we are today. The current U.S. system of money and payments has substantial strengths. The system has supported over a century of U.S. economic and financial leadership; is capable of processing an enormous volume of transactions; and is consistent with privacy and other democratic values. But there clearly is room for improvement. Some parts of the payment system are expensive and carry high fees, and other parts are slow. We also need a more inclusive system: The percentage of people in the United States that are unbanked is higher than in all other G-7 countries.

Recent innovations in digital assets and other technologies could have significant implications for money and payments. These innovations include a central bank digital currency (CBDC), retail instant payment systems, and stablecoins.

A CBDC is a digital form of a country's sovereign currency. A U.S. CBDC would serve as legal tender, and be convertible one-for-one into paper currency (Federal Reserve notes) or reserve balances (deposits at the Fed). It would clear and settle with finality and nearly instantly.

Instant payment systems, like the upcoming FedNow, could also support faster and more efficient payments. As currently envisioned, it would use bank deposit money and settle in central bank reserve balances, preserving the core features of major existing money and payment systems. In contrast, stablecoins aspire to be a new type of money supported by a novel payments technology, with implications that are more difficult to predict. A proliferation of stablecoins, or other new forms of private money, that are inadequately regulated could pose risks to financial stability or undermine the singleness of the currency.

With that backdrop, let me turn to the four key recommendations in the report:

RECOMMENDATION 1: ADVANCE WORK ON A POSSIBLE U.S. CBDC, IN CASE ONE IS DETERMINED TO BE IN THE NATIONAL INTEREST.

A U.S. CBDC has the potential to offer significant benefits. It could contribute to a payment system that is more efficient, resilient, and innovative. It could promote financial inclusion and equity by increasing access to the financial system. It could help support U.S. global financial leadership, as well as the effectiveness of U.S. sanctions while also being consistent with privacy and other democratic values. In addition, a CBDC may help preserve the singleness of the currency, which is important for economic growth and stability.

There also could be unintended consequences of a U.S. CBDC, especially depending on how its design affects private financial intermediation. As a liability of the central bank, consumers may prefer it to bank deposits, leading to a reduction in private credit availability. There could be destabilizing runs to U.S. CBDC in times of stress. In addition, because a CBDC would need to be extremely reliable, technological experimentation would likely need to proceed more cautiously than with private sector payment innovations.

There are important design choices to be made to achieve the potential benefits while minimizing the risks, which need additional consideration. For example, a U.S. CBDC could be wholesale or retail, or use direct or indirect access models. Transactions could be tiered based on amount or counterparty type. There also is a need for further research and development on the technology to support a U.S. CBDC, which could take years.

For the U.S. to build capacity to adopt a CBDC, even as deliberations continue about whether one is in the national interest, the report envisions work in three areas.

First, the Federal Reserve should continue evaluating the policy considerations outlined in its January 2022 discussion paper, as well as its research and technical experimentation on CBDCs. The report also suggests that the Fed provide the public with periodic updates on its initiatives.

Second, Treasury will lead an inter-agency working group to support the Fed's efforts and to advance further work on a possible U.S. CBDC. This Working Group will consider the implications of a CBDC in areas such as financial inclusion, national security, and privacy. The Working Group also will leverage cross-government technical expertise as useful for the Fed's efforts.

Third, leadership from the Federal Reserve, the White House, and the Treasury Department will meet regularly to discuss the progress of the Working Group, and to share updates on CDBC and other payments innovations.

RECOMMENDATION 2: ENCOURAGE USE OF INSTANT PAYMENT SYSTEMS TO SUPPORT A MORE COMPETITIVE, EFFICIENT, AND INCLUSIVE U.S. PAYMENT LANDSCAPE.

Retail instant payment systems transfer funds nearly instantly, as opposed to the multi-day settlement period that occurs on some legacy systems. In the U.S., examples include the Clearing House's RTP Network, launched in 2017, and the FedNow Service, which the Fed plans to launch in 2023. Global experience suggests that instant payments can make the payment system more competitive, efficient and inclusive. Yet the potential benefits could be limited by certain frictions, such as inertia or slow adjustments among consumers, businesses, and financial institutions to change their habits and procedures to incorporate new technologies. In addition, instant payment systems are generally accessible only to depository institutions.

To maximize the benefits from instant payments, the report suggests several efforts. First, the U.S. government should continue outreach efforts around instant payments, with a focus on inclusion of underserved communities. Second, the U.S. government should promote development of technologies that would allow consumers to more readily access instant payment systems. And third, in settings where appropriate, U.S. government agencies, which send and receive millions of payments a day, should consider and support the use of instant payment systems.

RECOMMENDATION 3: ESTABLISH A FEDERAL FRAMEWORK FOR PAYMENTS REGULATION TO PROTECT USERS AND THE FINANCIAL SYSTEM, WHILE SUPPORTING RESPONSIBLE INNOVATIONS IN PAYMENTS.

This recommendation recognizes that nonbanks are increasingly providing payment services, and are contributing to competition, innovation, and inclusion. But, nonbanks that are not adequately regulated and supervised may pose risks to users and the financial system. Today, oversight of nonbank payment providers is generally at the state level, which varies significantly across states, and may not address certain risks in a consistent and comprehensive manner.

Accordingly, the report recommends considering the establishment of a federal framework for nonbank payment providers. A federal framework would provide a common floor for minimum financial resource requirements and other standards that may exist at the state level. It also would complement existing federal AML/CFT obligations and consumer protection requirements that apply to nonbank payment providers.

A federal framework for payments regulation could work in conjunction with a U.S. CBDC or with instant payment systems. It could provide oversight of firms that a U.S. CBDC system may rely on to provide a range of financial services. In addition, it could provide a pathway for nonbank payment providers to participate directly in instant payment systems.

RECOMMENDATION 4: PRIORITIZE EFFORTS TO IMPROVE CROSS-BORDER PAYMENTS.

Cross-border payments – payments that go from one jurisdiction to another -- can take multiple days to clear and may have high fees.

The report’s final recommendation supports work to develop a faster, cheaper, and more transparent international payments system, while considering potential risks associated with greater integration of cross-border payment systems. It recognizes that the United States has a strong national interest in supporting global standards for cross-border payment systems that reflect U.S. values, including privacy and human rights; are consistent with AML/CFT considerations; and protect U.S. national security.

CONCLUDING THOUGHTS

To summarize, digital assets and instant payments can transform money and payments. This report makes four main recommendations to improve the efficiency and inclusiveness of the U.S. money and payments system, support U.S. global economic and financial leadership, while minimizing risks relating to financial stability, consumer protection, and illicit finance. Treasury will continue to work closely with other parts of the government on these important issues.

Fact Sheet: Treasury Report on the Future of Money and Payments