coinbase

To:

The Board of Governors
of the Federal Reserve System

20th Street & Constitution Ave NW
Washington, DC 20551

Date:

20 May 2022

Re: Coinbase's response to the Federal Reserve's discussion paper on a U.S. CBDC

Coinbase Global, Inc. (**Coinbase**) welcomes the opportunity to comment on the discussion paper, "Money and Payments: The U.S. Dollar in the Age of Digital Transformation," released by the Board of Governors of the Federal Reserve System (the **Fed**).

We appreciate your outreach to a wide range of stakeholders and look forward to continued engagement with you on the development of a U.S. central bank digital currency (**CBDC**).

Sincerely,

Faryar Shirzad
Chief Policy Officer
Coinbase Global, Inc.

coinbase

Money and Payments: The U.S. Dollar in the Age of Digital Transformation
Coinbase's response to the Federal Reserve's discussion paper on a U.S. CBDC

Coinbase's mission is to increase economic freedom in the world. Everyone deserves access to financial services that can help empower them to create a better life for themselves and their families. We believe that crypto is a pillar of financial inclusion and, by building the cryptoeconomy, we are helping to create a fairer, more accessible, efficient, and transparent financial system. Coinbase started in 2012 with the radical idea that anyone, anywhere, should be able to send and receive Bitcoin easily and securely. Today, we provide a trusted and easy-to-use platform relied on by approximately 98 million verified users, 13,000 institutions, and 230,000 ecosystem partners in over 100 countries to access the broader cryptoeconomy.[1]

We recognize that launching a U.S. CBDC is an important public policy decision, and our voice is one among many in your consideration of the interests of the American public. We expect that consumer demand for digital forms of money will grow as the technology improves and awareness increases. In parallel, we expect that the U.S. government's interest in implementing a CBDC will grow as other countries adopt CBDCs of their own to meet this demand. For these reasons, we think the Fed should carefully consider what role a CBDC can and should play in the U.S. financial system, as well as how best to design and launch a U.S. CBDC if it would serve the public interest.

The Fed has already signaled one key design decision, which is for individual users to receive CBDC services from private sector intermediaries, not the Fed itself. This creates specific design considerations as to what role the Fed expects private sector firms to play and how to properly incentivize appropriate business practices for those firms.

If the Fed were to pursue a U.S. CBDC, we believe the interests of the public must be at the center of every decision, and the design should aim to:

- Promote financial inclusion
- Define expectations for intermediaries on key aspects of users' experience
- Preserve the balance between data privacy protections and law enforcement needs
- Provide offline capabilities
- Enable programmability and interoperability
- Recognize that a U.S. CBDC and stablecoins can coexist
- Prioritize the interests of the public over incumbent financial institutions

[1] About Coinbase, https://www.coinbase.com/about

We hope that the Fed will continue engaging with the public on these points with additional opportunities to comment as plans for a potential U.S. CBDC become more developed.

Financial inclusion

Too many individuals in the United States remain unbanked or underbanked. According to the Fed's own report on the Economic Well-Being of U.S. Households in 2020, 5% of U.S. adults are unbanked and 13% are underbanked.[2] Many of these individuals are members of marginalized communities – for example, while only 12% of White adults are underbanked or unbanked, 40% of Black adults and 30% of Hispanic adults are underbanked or unbanked.[3] In a similar survey conducted by the FDIC, commonly cited reasons for not having a bank account included not having enough money to meet minimum balance requirements, and fees being too high or unpredictable.[4]

Surveys on Americans' level of interest and attitude towards digital assets supports the argument that they have the potential to promote financial inclusion. A 2020 survey conducted by Coinbase found that Black Americans show more interest than other respondents in understanding digital assets, with 70 percent being interested, compared to 42 percent of White Americans.[5] College-educated Black Americans are nearly twice as interested as their White American counterparts, with 75 percent interested in learning more versus 39 percent of their White American counterparts. When broken down by age, 21 percent of Black Americans over the age of 55 are very interested in learning about crypto, compared to 6 percent of White Americans over the age of 55.

A CBDC could make the U.S. payment system faster and more efficient, and thereby reduce the overall cost of financial services. A CBDC could also make financial services more accessible and more appealing for all Americans, including unbanked and underbanked individuals. Coinbase strongly urges that the design of a potential CBDC prioritize financial inclusion.

---

[2] Fed, Report on the Economic Well-Being of U.S. Households in 2020 (May 2021)
[3] Id.
[4] FDIC, How America Banks: Household Use of Banking and Financial Services, 2019 FDIC Survey (October 2020)
[5] Coinbase Reports: Black Americans & Crypto (13 Feb 2020)

Private sector intermediation
We agree that the Fed should not provide CBDC services directly to individuals. Doing so would require the Fed to develop massive infrastructure in retail banking and finance, where it has no experience or expertise. Adopting an intermediated model will position the private sector to continue in its fundamental role as the primary driver of innovation and economic growth.

Intermediaries should be subject to rigorous standards regarding their operational resilience, financial resources, technical expertise, risk management and compliance programs, among other key areas. Any company that meets these standards, including both banks and nonbanks, should be eligible to provide CBDC services. Allowing regulated nonbanks to intermediate CBDC will create opportunities for a wider, more customized, and more compelling set of digital services to users.

Based on our experience serving retail customers over the past decade, we believe the Fed should set clear expectations in the following areas:

- **User experience**. A positive user experience for CBDC services should include a simple onboarding process, intuitive interface, clear views of relevant information on assets and transactions, and responsive customer service. We believe the best approach is to set minimum standards, but not to impose uniformity. A wide range of intermediaries should develop competitive CBDC service offerings, empowering consumers to test the options in an open market that incentivizes continuous improvement.

- **Customer support**. A robust customer service function will be important to establishing trust with users, especially during the initial period of a potential U.S. CBDC launch. This should include, at a minimum, 24/7 availability of phone support from a capable human being with little hold time, a virtual chatbot and a clear FAQ page.

- **Customer protection.** Intermediaries should have policies and procedures addressing any CBDC-specific consumer protections and a thorough understanding of what those protections mean from a user's perspective. For example, intermediaries should be responsible for clearly informing users of their rights and any limitations on their ability to halt, reverse, or dispute transactions that may arise from a U.S. CBDC's ability to achieve settlement finality more quickly than traditional payment rails.

coinbase

Across all of these points, we recommend that the Fed work closely with private sector intermediaries on development, testing and pilot projects well in advance of a potential launch. We believe that early engagement and collaboration between the Fed and intermediaries will result in a better user experience and quality of services for the American public.

Anti-money laundering and data privacy

U.S. anti-money laundering (**AML**) regulations under the Bank Secrecy Act (**BSA**) require financial gatekeepers, such as banks and money services businesses (**MSBs**), to implement effective an AML program, which includes collecting identifying information on customers, monitoring transactions, screening for sanctions, maintaining records, and filing suspicious activity reports, among other things. The same framework applies to virtual asset services providers (**VASPs**), which are required to register as MSBs with the Financial Crimes Enforcement Network (**FinCEN**). VASPs, such as centralized exchanges, must implement effective AML programs to prevent bad actors from misusing the financial system. Some VASPs, including Coinbase, also participate in mandatory 314(a) information sharing, which requires them to respond to requests for information issued by FinCEN and law enforcement.

Any U.S. CBDC transaction conducted through a regulated intermediary should be covered by the same AML controls. Whether a VASP or any other type of financial institution, law enforcement should have the ability to use the information collected under these programs to monitor for large-scale trends in illicit activity and investigate specific bad actors.

It is important to recognize that digital assets provide greater visibility to law enforcement than fiat currency-based payments because they are recorded on a permanent and public blockchain that contains key transactional information, such as the date and time, type of asset, amount transacted, wallet addresses involved, and unique transaction identifiers. When combined with analytic tools, law enforcement (and compliance teams) can trace the entire history of a wallet from the very first transaction, follow transactions in real time, and even group transactions according to risk-level based on wallet addresses. A blockchain-based U.S. CBDC provides similar benefits to law enforcement. Given the unique benefits that digital assets provide to law enforcement, it is unnecessary for any incremental surveillance features to be built into a U.S. CBDC.

In considering a CBDC it is important to balance these benefits against exposing consumers to privacy risk. Imposing additional surveillance or KYC requirements on a U.S. CBDC would run counter to the public interest. Successful implementation of a U.S. CBDC requires consumer confidence, which would be undermined by the imposition of unnecessary, burdensome, and invasive additional requirements. Requesting further personal information from users above and beyond that which is already required by financial intermediaries also creates opportunities for exploitation by bad actors. Lastly, given the existing BSA requirements imposed on the very financial services companies that would serve as intermediaries for a U.S. CBDC, law enforcement already has good mechanisms for obtaining information on potentially illicit activity.

Offline capabilities

A U.S. CBDC should have the ability to operate in the absence of a reliable internet connection, so that users are consistently able to access their funds. A loss of CBDC access could exacerbate the negative effects of a natural disaster or disruption to the power grid, or leave users vulnerable during more common situations, such as driving through rural and low communication service areas.

We believe it is important to consider designs that would mitigate these concerns. For example, CBDC accounts could be linked to a plastic card or similar physical device, which would make CBDC usable at least as broadly as debit and credit cards today. A more complete offline solution may also involve providing the functionality for a device such as a smartphone to store offline information about pending transactions and execute these transactions once returned to connectivity. Any solution that the Fed considers should be subject to extensive testing to ensure its integrity and avoid potential problems such as double spending.

Programmability and interoperability

Programmability and interoperability are critical for the benefits of a U.S. CBDC to be fully realized as payment systems continue to evolve. Programmability refers to the existence of money in a digital form, with a mechanism for specifying its automated behavior through a computer program – in short, making it possible for developers to build applications that serve users in new and creative ways.[6] Interoperability refers to the ability of payment systems to communicate, execute instructions and transfer data among one another.[7]

We urge the Fed to enable programmability and interoperability to the fullest extent that can be achieved in line with its other policy objectives. A U.S. CBDC should support smart

---

[6] FEDS Notes, What is programmable money? (23 June 2021)
[7] BIS, Central bank digital currencies: system design and interoperability (September 2021)

contracts that make it possible for transactions to be executed automatically when specified conditions are met. It should also be interoperable with as wide a range as possible of other payment instruments, including both U.S. and non-U.S. fiat currencies as well as other digital assets. We believe that integrating these features into the design of a U.S. CBDC will, over time, unlock a wealth of innovative potential far beyond what may be foreseeable when it is launched.

Coexistence of stablecoins and a CBDC

A number of commentators have noted the risk that a U.S. CBDC could "crowd out" privately issued digital currencies, such as stablecoins, or even argued that "crowding out is the point of introducing a CBDC."[8] It would be a serious mistake to make this a significant goal in its own right, and we do not believe the Fed intends to do so.[9] In designing a U.S. CBDC, we urge the Fed to focus solely on providing the greatest value to the public. We trust in the innovative power and resilience of the digital asset ecosystem to handle any short-term issues that may arise as a byproduct of this ultimate objective.

In the long run, we believe that a U.S. CBDC can coexist with and complement privately issued stablecoins. This is particularly likely to be true to the extent that a U.S. CBDC's functionality is limited for policy reasons, e.g. interest rate and balance limits, as discussed below. In contrast, the private sector will always be more flexible and responsive to users' needs and demands. So long as a U.S. CBDC is not hostile to innovation, the private sector will find ways to capitalize on the opportunities created by a U.S. CBDC to provide better services to the public. For example, a stablecoin that is backed by a U.S. CBDC could effectively extend its functionality to new and existing public blockchains, or enable its use in a greater range of smart contracts and applications. The U.S. financial system has fostered prosperity for decades with a combination of public and private money, and we believe the country is best served by maintaining this balance in the digital assets space.

Prioritize the public's interest over incumbent interests

Many policymakers and analysts globally have expressed a concern that CBDCs will disintermediate banks or catalyze bank runs by enticing consumers to move their money out of commercial bank deposits into CBDCs. Policy solutions to minimize this risk have been proposed, particularly the setting of limits on the amount held by any one party and the avoidance of paying interest on CBDC. The European Central Bank, for example, is

---

[8] Congressional Research Service, [Central Bank Digital Currencies: Policy Issues] (7 Feb 2022) p. 15
[9] Bloomberg, [Powell Says Private Coins Could Compete With Fed Digital Dollar] (11 Jan 2022)

considering imposing limits on individuals' holdings of a digital euro to no more than €3,000 at a time.

While we recognize this topic spans a monetary policy conversation that may extend beyond the scope of Coinbase's focus as a business, we urge the Fed to recognize user acceptance and practicality as important goals, and to impose limits on individuals' U.S. CBDC holdings and transaction volumes only to the extent they are necessary to other fundamental policy objectives.

First, while we recognize that limits may be necessary on the amount of interest that can be paid on CBDC balances, or on the amount of CBDC that an individual can hold or use, the Fed should also consider the extent to which these limitations could make a U.S. CBDC less attractive, especially compared to other options that are currently available to the general public (such as opening a savings account that earns interest with a bank). We understand that paying interest on a CBDC would create new competitive pressures for incumbent banks. In our view, competition is an attribute of a healthy financial market, and like banks do today, they would need to find ways to incentivize customers to use their services. Provided that the policy framework can allow these market forces to play out without undue risk of financial instability, we believe there is a path forward that would make a U.S. CBDC attractive.

Second, numerous practical challenges of using a CBDC could arise if quantity limits are set on the amount held by any one party. For example, a small business with a seasonal cycle may have significant mismatches in the timing of its annual revenues relative to its annual expenses, which means that limits on the amount of CBDC holdings at one time could impact such a business differently from one whose revenues and expenses are more aligned over the course of a year. Such a business could accordingly experience a greater operational challenge if it is limited to holding only a certain amount. To address this, an exception could be made for certain small businesses to hold a larger amount of CBDC, but to do so will require care and foresight. If quantity limits are necessary for the design of a CBDC, an alternative is to set quantity limits as high as feasible to bear such users' interests in mind. Coinbase therefore recommends that the principal concern in these design decisions should be to best serve the public, without undue focus on preserving incumbent financial institutions' current role in the financial system.

Conclusion

Coinbase appreciates the Fed's active engagement in the ongoing discussions on exploring the possibility of a U.S. CBDC. We look forward to continuing to share our experience and expertise for the benefit of the public.

We thank the Fed for addressing this important issue and for considering our response.