



# Financial Services Management

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## Treasury Digital Dollar

### Cite

H. R. 7231, Electronic Currency and Secure Hardware Act (E-Cash Act)

### Recommended Distribution:

Policy, Legal, Government Relations

### Website:

<https://www.congress.gov/bill/117th-congress/house-bill/7231?q=%7B%22search%22%3A%5B%22hr+7231%22%2C%22hr%22%2C%227231%22%5D%7D&r=6&s=1>

### Impact Analysis

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- Although the proposal is clearly constructed more by academics and advocates than policymakers, legislation to create Treasury-issued electronic cash or independent action under current law along similar lines is possible, especially if the Fed's CBDC efforts become bogged down, as advocates fear.
- E-cash is intended only as a physical-cash substitute, but the bill also proposes additional uses – e.g., benefit distribution – that complicate its design and contradict over-arching objectives (e.g., anonymity).
- Implementation is mandated on an expedited basis, which is sure to prove challenging given the complexities of e-cash on its own and in concert with the broader system of money and payments.
- A complex "fund" mandated for the Fed to back e-cash appears to be an attempt to get around the challenges of allowing Treasury to create money even though it is a principal central-bank obligation. Its functionality is uncertain.

### Overview

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Progressive Democrats in the House have introduced an alternative digital-dollar proposal ("e-cash") to the "FedAccount" construct urged by Senate progressives<sup>1</sup> that mandates an electronic currency created by the Treasury Department to devise an electronic substitute for physical fiat currency. The measure acknowledges at least some of the challenges in doing so (e.g., obstacles for those with disabilities or limited broadband access), but nonetheless mandates a very fast-paced implementation schedule that is governed by a new Treasury office with senior status and considerable independence. While a new inter-agency council would be established to address issues such as conflicts between e-cash issuance and monetary policy, the bill itself otherwise fails to address this fundamental question, as well as many others such as how it achieves privacy and anonymity goals while ensuring AML compliance and financial inclusion. However, the e-cash idea nonetheless lays out a path that

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<sup>1</sup> See **CBDC7**, *Financial Services Management*, July 27, 2021.

could either supplement CBDC or substitute for it based on what the Federal Reserve decides to do after reviewing comments on its discussion draft<sup>2</sup> and whether the White House concurs with that path or seeks a new one to achieve the President's digital-asset objectives.<sup>3</sup>

## Impact

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As envisioned in this bill, e-cash is a very different approach to sovereign currency creation than CBDC, first and foremost because it would not be issued by a central bank and thus would be separate from monetary policy. The extent to which the government could use e-cash to achieve fiscal aims is not discussed in any way in the bill, but Treasury's ability to issue unlimited amounts of e-cash do provide scope for a new form of money creation that might not only be exempt from Congressional scrutiny, but also run counter to the Fed's intentions unless the measure also stipulated that the amount of e-cash in circulation may not exceed that of the physical cash it replaces. As drafted, Treasury could issue e-cash in any amount it desired.

In addition to possibly conflicting with monetary policy, the measure might also complicate Federal Reserve actions with regard to liquidity within the banking system, with this also a risk related to other federal banking agencies even though the bill text references only the Fed. The Fed is to ensure that nothing about e-cash adversely affects financial-system liquidity, but it could only do so without implementing any changes that directly affect e-cash. If the Fed also supposed to do something about e-cash that ensures it does not adversely affect credit availability for low-and-moderate income communities. Again, how it would do so if e-cash disintermediates bank deposit-taking is not made at all clear.

The bill also sets an array of social-welfare objectives for e-cash related not only to anonymity and privacy, but also the role of the private sector. As discussed below, third parties could not play many of the roles now associated with physical cash or private virtual currencies, nor could Treasury make use of the blockchain or certain other innovations to issue e-cash. The extent to which this complicates implementation, especially on the short timeframe demanded (see below), is not addressed. Third-party e-cash distributors (e.g., banks) are exempt from liability for mistaken actions, a provision which could create considerable consumer risk akin to that of using check-cashing companies if this is read to mean that false withdrawals of cash from a customer's account cannot be recouped by the defrauded customer.

Another practical problem is that e-cash providers could charge nothing for the hardware necessary to access it nor could any fees, including those related to interchanges, apply. For e-cash to work without dedicated hardware, it would need to be compatible with existing electronic devices obtained at cost to consumers much as consumers now use their own resources to hold physical cash in a physical wallet. However, digital cash is of course different and requires

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<sup>2</sup> See **CBDC10**, *Financial Services Management*, January 7, 2022.

<sup>3</sup> See **CRYPTO26**, *Client Report*, March 9, 2022

systems and devices that may be considerably more costly (smart phones) or incompatible with Treasury's preferred standards due to hardware-provider liability or other obstacles to introduction. Interestingly, Treasury could apparently distribute hardware for e-cash use as long as it charges a "reasonable" price for doing so to someone – no one could charge consumers any fee for this hardware. This might allow for the introduction of sophisticated e-cash equipment but put the federal government into a novel, controversial role as a direct provider of consumer-payment technology.

The bill's strong desire for privacy and anonymity conflicts with its effort to ensure that e-cash is not an avenue for AML or sanctions violations. The measure expressly bars any entity who would access consumer e-cash information from gathering it. This would of course preclude filing of suspicious activity reports (SARs) and currency transaction reports (CTRs) even though the measure also includes express provisions designed to permit CTR filing.

Finally, the entire e-cash program is to be financed via a new "overdraft" facility at the Fed. This appears to be an effort both to prevent the need for any appropriated funds even though doing so is authorized and it may also be an effort to coordinate e-cash issuance with the Fed's efforts to control the money supply. How it would do so and the effect this would have on the Fed's portfolio and thus on its current approach to conducting monetary policy is not at all clear.

## What's Next

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This bill was introduced on March 28 by Reps. Stephen Lynch (D-MA), Jesus Garcia (D-IL), Ayanna Pressley (D-MA), Alma Adams (D-NC), and Rashida Tlaib (D-MI).

If enacted, e-cash would proceed on a very rapid pace, with the bill requiring Treasury to set up a two-tier pilot, meeting an array of very detailed requirements even though the director of the office charged expressly with its governance (see below) may not have been nominated or confirmed by that time. The bill does not appear to give Treasury authority in the absence of a program director to undertake this pilot, despite the express mandate to do so. The pilot program will – among other things – have "proof of concept" e-cash programs up and running within 180 days of enactment, with these pilots running for no more than a year thereafter. A large field test would be required no later than two years after enactment running no more than an additional two years. These deadlines could, however, be extended by the program director if necessary to ensure technology security and integrity, but not apparently for any other reason.

There is no Senate companion bill and enactment in this Congress is unlikely. However, variations on Treasury e-cash are possible without statutory change; to the extent this measure advances, Treasury is likely to look at this option even if it is not among those included in the report to the President mandated in the executive order.

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## Analysis

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The provisions discussed below would be governed by a new Electronic Currency Innovation Program in the Treasury Department, with the details of who should head it, who should organize it, and what it must do also detailed in the legislation. The head of this program would be appointed by the President and confirmed by the Senate for a five-year term designed to give him or her authority and political independence.

The bill would also create a Digital Dollar Council akin in stature and mandate to the FSOC to coordinate Treasury's activities with the rest of the government, as well as a Monetary Privacy Board of presidentially appointed and Senate confirmed members to ensure that Treasury's actions preserve personal privacy. The Board would also assess any other federal digital-currency efforts, presumably including a central-bank digital currency.

### **A. Statutory Objectives**

The bill includes a detailed list of statutory objectives which e-cash would need to achieve. In addition to the specific provisions defining e-cash described below, the statutory objectives include that:

- e-cash should be owned, held, and otherwise used by the public without need for third-party hardware involving third-party custodians or payment processors;
- all hardware devices authorized to hold e-cash are to be protected from any form of surveillance technology; and
- e-cash must promote universal access especially for persons with disabilities, low-income individuals, and communities with limited access to the internet or other telecommunications networks.

Treasury is also to advance inclusion for marginalized communities and promote transparency via the use of open-source or similar technology wherever possible.

### **B. Electronic Dollar**

Treasury is told to promote and facilitate the development and deployment of an electronic version of the U.S. dollar for public use that "replicates" the physical dollar regarding privacy, anonymity, and minimal transaction costs to the greatest extent possible. This electronic dollar is to be known as e-cash and would also have to be:

- payable to the bearer;
- legal tender;
- an obligation of the United States;
- created and issued into circulation by the Treasury in such quantity, form, and ways as Treasury dictates. The FRB would play no role in this form of money creation;
- distributed directly to, used by, and otherwise held by the general public;

- capable of instantaneous, final, and secure peer-to-peer offline transactions using secure hardware that does not require DLT or other forms of subsequent settlement;
- inter-operable with all existing financial-institution and payment systems generally accepted standards and other protocols detailed in the bill;
- classified and regulated the same as other money for AML and similar purposes;
- distinguishable from any other form of electronic money issued by the U.S. Government, including any CBDC and any other currency instruments issued pursuant to other provisions in this bill and relevant consumer protections and payment standards issued by Treasury or the new office governing e-cash; and
- not considered public debt for fiscal purposes.

### ***C. Liability***

Neither Treasury nor any other government issuing agency or third-party e-cash distributors could be held liable for unauthorized transactions as long as relevant disclosures and consumer protections are met.

### ***D. Preemption***

State consumer laws are preempted except to the extent that the CFPB agrees that they may prevail.

### ***E. Additional Requirements***

The bill requires in addition that:

- Treasury may charge a "reasonable" price for selling relevant hardware;
- no other fees would be allowed;
- the government or an issuer may provide hardware only in response to an express consumer request without charge to consumers. No service or interchange fees could apply;
- an array of disclosures set by the CFPB would apply to the government and third-party e-cash distributors;
- e-cash balances are to be exempt assets in bankruptcy proceedings;
- transactional data generated by e-cash may "in no circumstance" be gathered by the U.S. Government, e-cash distributors, or other parties. This may inhibit the kind of reporting now associated with cash for AML and related purposes, although the bill appears to intend that CTRs capture e-cash transactions because it provides for CTRs for e-cash at higher reporting thresholds than those applied to physical cash. E-cash possession or use could also not be considered evidence of a crime on its own;

- the federal government would need to accept e-cash for all purposes and provide any form of government benefit in e-cash upon request (whose request is not made clear);
- any person accepting physical cash would also need to accept e-cash when practicable and reasonable; and
- the Fed would need to ensure that e-cash has no adverse liquidity impact on banking organizations or their capacity to provide credit to under-served populations. Any other adverse impact on credit availability could apparently be accepted. Whatever the Fed does is also not to have any impact on e-cash, making it unclear exactly what the FRB could do about any of these mandates.

### ***F. Funding***

Although the bill provides for appropriations to fund Treasury and related activities, it also creates a "Treasury Electronic Currency Innovation Fund Account" at the New York Federal Reserve Bank from which Treasury would actually fund all expenses related to this program via overdrafts from the Federal Reserve that must always be honored. These overdrafts are also not to be considered public debt, with any Fed losses to be treated only as impaired assets exempt from inclusion in the Federal Reserve System's accounts. The FRB would apparently need to remit funds to Treasury from its operations or portfolios without regard to any losses incurred in connection with e-cash.