

# Opening a Federal Reserve Account

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*To open bank accounts, new customers provide personal information and make a deposit. Within a few minutes (or perhaps a few days), new customers get access to payment services. For many years, the process financial institutions used to open accounts at Federal Reserve Banks was similar. Eligible banks filled out a one-page form and within a week received an account allowing them access to the Federal Reserve's payment systems. Recently, however, Federal Reserve Banks have spent years considering account requests from novel banks.*

*This Article examines the Federal Reserve's process for evaluating requests for accounts. Using interviews, court documents, and other sources, it analyzes recent account requests from a cannabis credit union, a narrow bank, a public bank, a cryptocurrency custody bank, and a trust company. These requests reveal a lack of transparency and consistency. Most district Federal Reserve Banks do not explain how institutions should apply for accounts. It is not clear who decides whether to open the account. While the Federal Reserve Banks all evaluate risk associated with accounts and payments, the twelve Reserve Banks may not have the same risk tolerances. Decisions may be inconsistent. Even getting a decision can take years. Unfortunately, the Federal Reserve's recently adopted guidelines, which consist primarily of a risk identification framework, do not fix these problems.*

*Congress should require that the Federal Reserve adopt public procedures describing how account applications are received and processed. These procedures should clarify the roles of the Reserve Banks and the Federal Reserve Board. To ensure that applicants are treated fairly and consistently, the Federal Reserve should publicly disclose information about accountholders, account requests, and account decisions.*

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<sup>†</sup> Alton C. and Cecile Cunningham Craig Professor of Law, University of Alabama. I am thankful to Dan Awrey, Colleen Baker, Mehrsa Baradaran, Peter Conti-Brown, Jillian Eng, Hampton Finer, Charles Gray, Michael Hill, Thomas Hoenig, Brian Knight, Christopher Land, Caitlin Long, Steven Lupien, Mark Mason, James McAndrews, Andrew Morriss, David Portilla, Alicia Randolph, Drew Roberts, Joshua Rosner, Nick Rotchadl, Adam Rust, Trevor Rutar, Andrew Samuel, George Selgin, Mark Van Der Weide, Art Wilmarth, and David Zaring for thoughtful discussions about Federal Reserve accounts. Of course, some of these bright people still disagree with parts of this Article and errors are my own. I am also grateful to the University of Alabama Bounds Law Library, including former staff members Seth Brostoff and Penny Gibson, for their help in tracking down elusive sources.

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## Introduction

To open a bank account, a new customer typically provides personal information and makes a deposit.<sup>1</sup> The bank verifies the customer's identity and assesses whether the new account is too risky.<sup>2</sup> In many cases, this process can be completed in a matter of minutes.<sup>3</sup> In other cases, it takes a few days.<sup>4</sup> Once an account is open, the customer has a safe place to store money<sup>5</sup> and secure ways to send and receive payments.

Financial institutions, like their customers, need a safe place to keep money and ways to facilitate payments. In the United States, the Federal Reserve Banks provide these services.<sup>6</sup> This Article examines the process banks encounter when seeking a Federal Reserve account and access to Federal Reserve operated payment systems.

Although Federal Reserve Banks have been providing account and payment services since their inception,<sup>7</sup> these accounts are not open to everyone. Until 1980, Federal Reserve accounts “were for the most part . . . available only to banks that were members of the Federal Reserve System.”<sup>8</sup> In 1980, Congress passed the Monetary Control Act, giving all depository institutions access to Federal Reserve accounts.<sup>9</sup>

But how does a bank get a Federal Reserve account? Following the Monetary Control Act of 1980, banks opening an account at the Federal Reserve encountered a process like that of customers opening standard bank accounts. The bank applicant completed a one-page form identifying itself, agreeing to be bound by the Federal Reserve's account policies, and listing the people to whom the Federal Reserve Bank should direct questions regarding the account.<sup>10</sup>

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1. Elise Craig, *How to Open a Bank Account*, N.Y. TIMES, June 27, 2021, at MK9.

2. 31 C.F.R. § 1020.220 (2022); Michael S. Barr, *Banking the Poor*, 21 YALE J. ON REGUL. 121, 181 (2004); René Bennett, *What to Do if a Bank Rejects You for a Checking Account*, BANKRATE (Oct. 27, 2017), <https://www.bankrate.com/banking/checking/bank-denied-you-for-a-checking-account/> [https://perma.cc/RSQ9-3NZ4].

3. See, e.g., *How to Open a Checking Account Online*, HUNTINGTON, <https://www.huntington.com/learn/checking-basics/how-to-open-a-checking-account> [https://perma.cc/EGJ6-2QK2] (stating that “it takes just 5 to 10 minutes to open a bank account”).

4. See, e.g., *Applying for Bank Accounts FAQs*, BANK AM., <https://www.bankofamerica.com/deposits/applying-for-accounts-faqs/> [https://perma.cc/DVJ6-BB9K] (stating that bank account applications “will be processed in 1 to 2 business days”).

5. The Federal Deposit Insurance Corporation insures deposits at each bank up to \$250,000 per depositor in each ownership category. 12 U.S.C. § 1821(a)(1)(E) (2018); *Deposit Insurance FAQs*, FDIC <https://www.fdic.gov/resources/deposit-insurance/faq/> [https://perma.cc/5LFY-9XZQ].

6. FED. RSRV. SYS., THE FED EXPLAINED: WHAT THE CENTRAL BANK DOES 86-87 (11th ed. 2021), <https://www.federalreserve.gov/aboutthefed/files/the-fed-explained.pdf> [https://perma.cc/KN6N-7PHZ] [hereinafter THE FED EXPLAINED].

7. *Id.* at 87.

8. *Id.*

9. Pub. L. No. 96-221, 94 Stat. 132 (1980).

10. *Operating Circular No. 1*, FED. RSRV. BANK OF DALLAS app. 1 (Jan. 2, 1998)), <https://fraser.stlouisfed.org/title/district-notice-federal-reserve-bank-dallas-5569/federal-reserve-standardized-operating-circulars-546823> [https://perma.cc/PE8B-BXHF] [hereinafter *Operating Circular 1* (1998)].

Federal Reserve Banks opened accounts with little independent investigation as to the riskiness of the applicant.<sup>11</sup> For many years, the Federal Reserve Banks' forms implied that account opening was quick, noting that "[p]rocessing may take 5-7 business days."<sup>12</sup>

At some point, however, the Federal Reserve changed its approach to processing account requests. Rather than encountering a process like opening a bank account, some recent Federal Reserve account applicants have encountered a lengthy process more like applying for a bank charter.<sup>13</sup> It took the Territorial Bank of American Samoa more than a year and a half to secure its account with the Federal Reserve Bank of San Francisco (San Francisco Fed).<sup>14</sup> During that year, the San Francisco Fed and the Federal Reserve Board peppered the public, uninsured bank with questions about its riskiness.<sup>15</sup> Other applications seem to be languishing in an extensive risk assessment process. The Federal Reserve Bank of New York (New York Fed) has spent more than five years considering an account application from TNB, a narrow bank that would deposit all its customers' money in a Federal Reserve account.<sup>16</sup> And the Federal Reserve Bank

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11. See Telephone Interview with Thomas Hoenig, Former Pres., Fed. Rsr. Bank of Kansas City (Mar. 11, 2020) (explaining that prior to the recent novel bank applications, there was little controversy over Reserve Bank accounts and applications were routinely granted); Peter Conti-Brown, *The Fed Wants to Veto State Banking Authorities. But Is That Legal?*, BROOKINGS (Nov. 14, 2018), <https://www.brookings.edu/research/the-fed-wants-to-veto-state-banking-authorities-but-is-that-legal/> [<https://perma.cc/5XMS-ACZV>] (describing the process of getting a Federal Reserve account as "[f]ormerly[] routine").

12. See *Operating Circular No. 1: Account Relationships*, FED. RSRV. BANK OF DALLAS, app. 1 (Aug. 30, 2002), [https://fraser.stlouisfed.org/title/5569/item/547312?start\\_page=3](https://fraser.stlouisfed.org/title/5569/item/547312?start_page=3) [<https://perma.cc/2PH5-TAYM>] [hereinafter *Operating Circular 1 (2002)*] (providing a form master account agreement that noted: "[p]rocessing may take 5-7 business days"); *Operating Circular No. 1: Account Relationships*, FED. RSRV. FIN. SERVS., app. 1 (Sept. 2011), <https://web.archive.org/web/20210626181245/www.frb services.org/binaries/content/assets/crsocms/forms/accounting/master-account-agreement-oc1-app1-rv.pdf> [<https://perma.cc/2A5W-VYQC>] ("Processing may take 5-7 business days."). The "5-7 business day" language remained in the form until August 16, 2021. See *Summary of Changes to Operating Circular 1*, FED. RSRV. FIN. SERVS. (2021), <https://www.frb services.org/binaries/content/assets/crsocms/resources/rules-regulations/081621-oc1-summary-of-changes.pdf> [<https://perma.cc/MT42-9QLA>] (noting that the form's footer had been amended); *Operating Circular 1: Account Relationships*, FED. RSRV. FIN. SERVS., app. 1 (Aug. 16, 2021), <https://www.frb services.org/binaries/content/assets/crsocms/forms/accounting/master-account-agreement-oc1-app1-rv.pdf> [<https://perma.cc/RBA4-5ZXC>] [hereinafter *Operating Circular 1 app. 1 (2021)*].

13. See *FAQs: How Can I Start a Bank?*, BD. GOVERNORS FED. RSRV. SYS. (Aug. 2, 2013), [https://www.federalreserve.gov/faqs/banking\\_12779.htm](https://www.federalreserve.gov/faqs/banking_12779.htm) [<https://perma.cc/AW3A-2U4W>] ("Starting a bank involves a long organization process that could take a year or more, and permission from at least two regulatory authorities. Extensive information about the organizer(s), the business plan, senior management team, finances, capital adequacy, risk management infrastructure, and other relevant factors must be provided to the appropriate authorities.").

14. See Rob Blackwell, *How Far Does American Samoa Have to Go to Get a Bank?*, AM. BANKER (July 31, 2017, 5:11 PM EDT), <https://www.americanbanker.com/news/how-far-does-american-samoa-have-to-go-to-get-a-bank>, 2017 WLNR 23650294 (noting that although the Territorial Bank of American Samoa opened in October 2016, it had not yet received a Federal Reserve account in August 2017); Fili Sagapolutele, *TBAS Opens "Master Account" with the Federal Reserve Bank*, SAMOA NEWS (Apr. 7, 2018, 6:24 AM), <https://www.samoanews.com/local-news/tbas-opens-master-account-federal-reserve-bank> [<https://perma.cc/G8QL-28R7>].

15. See *infra* notes 323-329 and accompanying text.

16. See *TNB USA Inc. v. Fed. Rsr. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020), 2020 WL 1445806, at \*9 (dismissing the applicant's suit against the New York Fed on ripeness grounds even though the New York Fed had been investigating the application since 2017).

of Kansas City (Kansas City Fed) has been reviewing an application from Kraken, a Wyoming cryptocurrency custody bank, for more than two years.<sup>17</sup>

This is the first scholarly Article to examine the Federal Reserve’s process for handling account and payment services requests. Describing the Federal Reserve’s account request process is not straightforward. The statutory text governing Federal Reserve accounts is sparse, and regulations do not flesh out the procedures. The district Federal Reserve Banks responsible for opening accounts and operating the payment systems are secretive. They have few publicly available policies governing access to accounts. The Federal Reserve Banks claim they are not subject to the Freedom of Information Act.<sup>18</sup> When faced with information requests, they withhold most information related to their accounts or payment services.<sup>19</sup> They do not generally provide public information explaining their decisions.<sup>20</sup>

Using interviews, court filings, information requests, press reports, and other sources, this Article provides a more complete picture of the process novel banks encounter when seeking access to Federal Reserve accounts and payment services. It explores in-depth the experiences of Fourth Corner Credit Union (a cannabis credit union in Colorado), TNB (a non-lending bank in Connecticut), Custodia (a cryptocurrency custody bank in Wyoming), Territorial Bank of American Samoa (a public bank), and Reserve Trust (a fintech trust in Colorado).<sup>21</sup>

The handling of these account requests raises serious questions about the Federal Reserve’s process. It is not apparent how applicant banks should request

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17. Cynthia Lummis, Opinion, *The Fed Battles Wyoming on Cryptocurrency*, WALL ST. J. (Nov. 30, 2021, 6:14 PM ET), <https://www.wsj.com/articles/the-fed-battles-wyoming-cryptocurrency-powell-brainard-bitcoin-digital-assets-spdi-fintech-11638308314> [<https://perma.cc/247N-EZ67>].

18. See, e.g., *Freedom of Information Requests*, FED. RSRV. BANK OF N.Y., <https://www.newyorkfed.org/aboutthefed/freedom-of-information-requests> [<https://perma.cc/U2S9-3T2W>] (stating that although the “[t]he Federal Reserve Bank of New York is not an agency as defined by the Freedom of Information Act (FOIA) and is therefore not subject to the provisions of FOIA,” it nevertheless “is committed to complying with the spirit of FOIA”). Others believe that the regional Federal Reserve Banks are within the scope of FOIA. See, e.g., Karla Karlson, Comment, *Check and Balances: Using the Freedom of Information Act to Evaluate the Federal Reserve Banks*, 60 AM. U. L. REV. 213 (2010).

19. See generally Benjamin W. Cramer & Martin E. Halstuk, *Crash and Learn: The Inability of the Transparency Laws to Penetrate American Monetary Policy*, 25 WM. & MARY BILL RTS. J. 195 (2016) (describing legal attempts to gather information from the Federal Reserve Board and Reserve Banks using the Freedom of Information Act).

20. Cf. E-mail from Craig C. Zahnd, Sr. Vice Pres., Gen. Couns. & Chief Compliance Officer, Fed. Rsr. Bank of Kansas City to Tom Jones, Pres., Am. Accountability Found. (Sept. 22, 2022) (“Documents related to a request for a master account are not made available under our policy because sharing this information could impede Bank operations.”); E-mail from Erik Z. Revai, Gen. Couns., Fed. Rsr. Bank of S.F. to author (July 24, 2019) (on file with author) (declining to provide information on account restrictions for a novel bank); Letter from Sen. Pat Toomey to Esther L. George, Pres., Fed. Rsr. Bank of Kansas City (Feb. 1, 2021) (explaining that when Senator Toomey requested information about meetings held between the Kansas City Fed staff and an applicant for an account, the Bank staff told the Senator “that they believed the records and information requested may contain confidential supervisory information”).

21. See *infra* Section III.A-E.

an account or what materials they must provide.<sup>22</sup> It is unclear who is deciding the outcomes of such requests. The Federal Reserve Board seems actively involved in risk assessments of novel banks, but the Board is not transparent about its role.<sup>23</sup> Novel banks undergo a risk assessment, but there are no processes or bright-line rules that would facilitate consistent decisions across the twelve Federal Reserve Bank districts.<sup>24</sup> Some account decisions seem more driven by politics than by risk. Novel banks requesting Federal Reserve accounts often wait years for a decision. The Federal Reserve does not make any of its decisions public.

Recognizing that the process for handling account applications could benefit from “a more transparent and consistent approach,” the Federal Reserve Board recently adopted Guidelines for Evaluating Account and Services Requests.<sup>25</sup> The Guidelines identify risks that the Federal Reserve Banks should consider and specify that applications from institutions without a federal regulator should receive greater scrutiny.<sup>26</sup> These Guidelines, in effect, formalize the chartering-like process novel banks have encountered in the last few years.<sup>27</sup> But the Guidelines do little to provide the transparency and consistency the Federal Reserve claims to value. Indeed, the Federal Reserve Board explicitly rejected suggestions, like publicly disclosing account decisions, that would have allowed others to evaluate the fairness and consistency of account access decisions.<sup>28</sup>

Because the Federal Reserve seems uninclined to fix its account procedure problems, Congress should legislatively improve the process. The first step is for Congress to require that the Federal Reserve adopt public procedures explaining how institutions can request accounts and services, what materials they must provide, and when they can expect the Federal Reserve to act on requests.<sup>29</sup> Other bank supervisory applications (chartering, deposit insurance, etc.) routinely provide these procedural safeguards.<sup>30</sup> If the Federal Reserve’s account application process resembles a chartering review, it should be subject to similar safeguards. Next, the Board of Governors of Federal Reserve System should be transparent about the gatekeeping role it plays with respect to account and payment services.<sup>31</sup> The Federal Reserve Board should not be able to evade public scrutiny of its decisions by claiming that the Reserve Banks hold ultimate discretion over accounts. Finally, Congress should require that the Federal

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22. *See infra* Section IV.A.

23. *See infra* Section IV.B.

24. *See infra* Section IV.C.

25. Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. 51099, 51099 (Aug. 19, 2022).

26. *Id.* at 51106-10.

27. *Cf. id.* at 51099 n.3 (acknowledging that “[i]n developing the Account Access Guidelines, the Board sought to incorporate as much as possible existing Reserve Bank risk management practices”).

28. *See id.* at 51102.

29. *See infra* Section VI.A.

30. *See infra* notes 505-509.

31. *See infra* Section VI.B.

Reserve disclose its decisions to deny account or services.<sup>32</sup> This would allow observers to assess whether Federal Reserve Banks’ decisions are fair and consistent. It would also provide future applicants information to evaluate the likelihood of securing an account and may prevent some banks from needlessly traveling an unfruitful path.

## I. Federal Reserve Accounts & Payments

The Federal Reserve System (the Federal Reserve) was created by Congress in 1913.<sup>33</sup> Today a collection of twelve privately-owned Federal Reserve Banks geographically dispersed throughout the country acts as the “operating arms” of the System.<sup>34</sup> These are the entities that provide accounts and payment services. The Reserve Banks are supervised by the Board of Governors of the Federal Reserve System (the Federal Reserve Board or the Board)—an independent government agency with seven members who are appointed by the President and confirmed by the Senate.<sup>35</sup> The Board oversees the Reserve Banks’ provision of accounts and payment systems by developing regulations and exercising supervisory authority over the Reserve Banks.<sup>36</sup>

Federal Reserve Bank accounts, or “master accounts”<sup>37</sup> as they are called by the Federal Reserve, provide financial institutions with two important services. First, a Federal Reserve account provides an extremely safe place to deposit money and earn interest. While there are many private places to invest

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32. See *infra* Section VI.C.

33. Federal Reserve Act of 1913, Pub. L. No. 63-43, 38 Stat. 251.

34. Comm. for Monetary Reform v. Bd. of Governors of the Fed. Rsrv. Sys., 766 F.2d 538, 539-40 (D.C. Cir. 1985) (“The Federal Reserve Banks are private corporations whose stock is owned by the member commercial banks within their districts.”); THE FED EXPLAINED, *supra* note 6, at 8, 10-12 (describing the Reserve Banks’s role in “providing key financial services that undergird the nation’s payment system”).

35. 12 U.S.C. § 241 (2018); 44 U.S.C. § 3502(5) (2018).

36. 12 U.S.C. § 248(a), (j) (2018) (granting the Board authority “[t]o examine at its discretion the accounts, books, and affairs of each Federal reserve bank” and “[t]o exercise general supervision over . . . Federal reserve banks”); THE FED EXPLAINED, *supra* note 6, at 86 (“In general, the Board is responsible for developing regulations and supervisory policies for elements of the payment system that fall within the Federal Reserve’s jurisdiction.”).

37. *Operating Circular 1: Account Relationships*, FED. RSRV. FIN. SERVS. § 2.2(c) (Aug. 16, 2021), <https://www.frbservices.org/binaries/content/assets/crsocms/resources/rules-regulations/081621-operating-circular-1.pdf> [<https://perma.cc/9ZAJ-7465>] [hereinafter *Operating Circular 1* (2021)]. In other contexts, people advocate discarding the use of the word “master” over concerns that the term “evoke[s] racist history.” See Kate Conger, *Racial Justice in the Machine*, N.Y. TIMES, Apr. 13, 2021, at B1 (discussing use of the term “master” in computer programming); see also Sydney Franklin, *It May be Time to Retire the ‘Master Bedroom,’* N.Y. TIMES, Aug. 9, 2020, at RE10; Dina LaPolt, *Why the Music Industry Must Remove the Racist Term ‘Master Recording’ from Its Vocabulary*, VARIETY (Apr. 11, 2022, 12:49 PM PT), <https://variety.com/2022/music/opinion/remove-master-recording-slave-1235230283/> [<https://perma.cc/G3CQ-J3KV>]; Rob Parker, *We’ve Lived with ‘The Masters’ Name Long Enough*, DEADSPIN (June 22, 2020, 1:55 PM), <https://deadspin.com/we-ve-lived-with-the-masters-name-long-enough-1844121041> [<https://perma.cc/ZC4R-2X7T>] (advocating that famous golf tournament held at the Augusta National Golf Club be renamed because “[w]hen you hear anyone say the Masters, you think of slave masters in the South”). Because the Federal Reserve describes its accounts as “master accounts” and industry participants routinely use the term, it would be confusing to eliminate that term from this Article. Nevertheless, I have attempted to minimize its use.

money, none provide the same level of security.<sup>38</sup> Second, an account gives a bank access to payment systems operated by the Federal Reserve. The Federal Reserve operates check clearing, wire transfer, and automated clearinghouse payment systems. Payments on these networks settle through Federal Reserve accounts.<sup>39</sup> By statute, the Federal Reserve must price these payment services at cost.<sup>40</sup> Without an account, a bank, business, or individual must find a correspondent bank<sup>41</sup> with a Federal Reserve account that is willing to hold its deposits and process its payments, usually for an additional fee. Having direct access to a Federal Reserve Bank account avoids an intermediary and the associated fees and risks. This Part describes the historical evolution of Federal Reserve accounts and payments focusing on their legal underpinnings.

### A. Accounts & Payment Services

Since Congress created the Federal Reserve System in 1913, the regional Federal Reserve Banks have been authorized to receive deposits from “member banks.”<sup>42</sup> Nationally chartered banks must become “members” of the Federal Reserve by purchasing stock in the Federal Reserve Bank in their district.<sup>43</sup> State-chartered banks are also eligible to become members by purchasing stock; however, doing so gives the Federal Reserve supervisory authority over the bank.<sup>44</sup>

Federal Reserve accounts were crucial to one of the goals animating the creation of the Federal Reserve—the goal of improving payment systems.<sup>45</sup> In its early days, the Federal Reserve’s payment systems included centralized check clearing services and a wire transfer system (called Fedwire).<sup>46</sup> The Reserve

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38. Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. 51099, 51108 (Aug. 19, 2022) (“Balances held in Reserve Bank accounts present no credit or liquidity risk making them very attractive in times of financial or economic stress.”); John Crawford, Lev Menand & Morgan Ricks, *FedAccounts: Digital Dollars*, 89 GEO. WASH. L. REV. 113, 116 (2021) (“Central bank accounts consist of base money, meaning they are fully sovereign and will not default no matter how large the balance.”); see also *supra* note 5 (describing the limits of FDIC insurance).

39. Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. at 51106 n.1 (noting that Federal Reserve financial services transactions must settle in a bank’s “master account with a Federal Reserve Bank or in the master account of another institution that has agreed to act as its correspondent”); THE FED EXPLAINED, *supra* note 6, at 90 (“Settlement is the actual transfer of funds between the payer’s financial institution and the payee’s financial institution.”).

40. 12 U.S.C. § 248a(c)(3) (2018).

41. Heath P. Tarbert & Liangshun Qian, *The Perils and Promise of Correspondent Banking*, 133 BANKING L.J. 53, 54 (2016) (“Correspondent banking is the provision of banking services by one bank (the ‘correspondent bank’) to another (the ‘respondent bank’).”).

42. Federal Reserve Act of 1913, Pub. L. No. 63-43 § 13, 38 Stat. 251, 263.

43. 12 U.S.C. § 222 (2018).

44. *Id.* §§ 321, 325.

45. Paul M. Connolly & Robert W. Eisenmenger, *The Role of the Federal Reserve in the Payments System*, in THE EVOLUTION OF MONETARY POLICY AND THE FEDERAL RESERVE SYSTEM OVER THE PAST THIRTY YEARS: A CONFERENCE IN HONOR OF FRANK E. MORRIS 131, 134 (Fed. Rsrv. Bank of Boston, 2000); O.M. W. Sprague, *The Federal Reserve Act of 1913*, 28 Q. J. OF ECON. 213, 215 (1914).

46. See Connolly & Eisenmenger, *supra* note 45 (discussing the Federal Reserve’s historical check clearing role); Sprague, *supra* note 45, at 215 (describing the Federal Reserve as “empowered to



Banks added the Automated Clearinghouse (ACH) network, a system for processing batched electronic small-dollar payments, in the 1970s.<sup>47</sup> Federal Reserve Bank accounts facilitate these payment services by providing a way for banks to settle payments among themselves.<sup>48</sup> For example, if two banks each have a Federal Reserve Bank account, the Federal Reserve can settle a wire transfer by taking money from the originating bank's account and depositing it in the receiving bank's account. Federal Reserve accounts also facilitate private payment systems by providing settlement services.<sup>49</sup>

While initially the Reserve Banks could only accept deposits from “member banks,”<sup>50</sup> over time, Congress has expanded the list of entities eligible for Federal Reserve accounts. In 1917, nonmember banks and trust companies became eligible to open Federal Reserve accounts “solely for the purposes of exchange or collection” if the bank or trust company “maintains with the Federal reserve bank of its district a balance sufficient to offset the items in transit held for its account by the Federal reserve bank.”<sup>51</sup> The Federal Reserve hoped that allowing nonmember banks to have clearing accounts would encourage more banks to use the Federal Reserve check clearing services.<sup>52</sup>

The Monetary Control Act of 1980 further expanded the list of institutions eligible for Federal Reserve accounts. In addition to “member banks,” “other depository institutions” became eligible to open accounts.<sup>53</sup> This change accompanied new provisions that made all depository institutions, including thrifts and credit unions, subject to deposit reserve requirements.<sup>54</sup> While these institutions were not required to maintain their own Federal Reserve account for holding reserves,<sup>55</sup> allowing them access to accounts gave a broader range of institutions this safe option. Congress also expanded the list of institutions eligible for clearing accounts. In addition to the nonmember banks and trust

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undertake the business of collecting and clearing checks throughout the entire country”); *Federal Reserve Operation in Payment Mechanisms: A Summary*, 62 FED. RESRV. BULL. 481, 486 (1976), [https://fraser.stlouisfed.org/title/62/item/20419/toc/287392?start\\_page=26](https://fraser.stlouisfed.org/title/62/item/20419/toc/287392?start_page=26) [https://perma.cc/4VR7-X5D8] (describing wire services that first used Morse code and later used a teletype system); WALTER E. SPAHR, *THE CLEARING AND COLLECTION OF CHECKS* 291-329 (1926) (discussing the Federal Reserve Banks’ “inter-district clearing of checks and drafts” and “telegraphic transfers, growing out of any inter-district transfer of funds”).

47. Anatoli Kuprianov, *The Monetary Control Act and the Role of the Federal Reserve in the Interbank Clearing Market*, *ECON. REV.* 23, 25 (July/Aug. 1985).

48. THE FED EXPLAINED, *supra* note 6, at 86-87.

49. *Policies: The Federal Reserve in the Payments System*, BD. GOVERNORS FED. RESRV. [https://www.federalreserve.gov/paymentsystems/pfs\\_frpaysys.htm](https://www.federalreserve.gov/paymentsystems/pfs_frpaysys.htm) [https://perma.cc/4HK8-R3GD].

50. Federal Reserve Act of 1913, Pub. L. No. 63-43 § 13, 38 Stat. 251, 263.

51. Act of June 21, 1917, Pub. L. No. 65-25, § 4, 40 Stat. 232, 235.

52. James N. Duprey & Clarence W. Nelson, *A Visible Hand: The Fed's Involvement in the Check Payments System*, *FED. RESRV. BANK OF MINNEAPOLIS Q. REV.*, Spring 1986, at 27; 3 FED. RESRV. BD., *ANN. REP. FOR THE YEAR 1916*, at 12, 28 (1917).

53. Monetary Control Act of 1980, Pub. L. No. 96-221 § 105, 94 Stat. 132, 139 (codified at 12 U.S.C. § 342 (2018)).

54. *Id.* § 103, 94 Stat. at 133-34 (codified at 12 U.S.C. § 461(b) (2018)).

55. Reserves may be held “in the Federal Reserve Bank of which [the depository institution] is a member or at which it maintains an account” or in a correspondent bank with a Federal Reserve account. *Id.* § 104, 94 Stat. at 139 (codified at 12 U.S.C. § 461(c)(1) (2018)).

companies that were previously eligible for clearing accounts, “other depository institutions” are now also eligible.<sup>56</sup>

### *B. Master Accounts*

Following the passage of the Monetary Control Act, the Federal Reserve Banks began encouraging nonmember banks and thrifts to use their payment services.<sup>57</sup> Soon the Reserve Banks were opening accounts for newly eligible financial institutions.

The Federal Reserve Banks started using the term “master accounts” in 1998.<sup>58</sup> Before that time, some banks held more than one Federal Reserve account, and some banks had accounts at more than one Federal Reserve Bank.<sup>59</sup> The Federal Reserve Banks consolidated these accounts “into a single (master) account” to better accommodate newly authorized interstate bank branching.<sup>60</sup> With the new “master account” system, the Federal Reserve no longer separated “reserve accounts” and “clearing accounts.”<sup>61</sup> According to the Federal Reserve, a “master account” is “the record of financial transactions that reflects the financial rights and obligations of an accountholder and the Reserve Bank with respect to each other, and where opening, intraday, and closing balances are determined.”<sup>62</sup>

At the same time the Federal Reserve Banks began using the term “master accounts,” they adopted uniform operating circulars to “make it easier for depository institutions to conduct business with multiple Reserve Banks.”<sup>63</sup> Operating Circular 1 covers “Account Relationships.”<sup>64</sup> It “establish[es] the terms for opening, maintaining, and terminating master accounts.”<sup>65</sup>

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56. *Id.* § 105, 94 Stat. at 140 (codified at 12 U.S.C. § 342 (2018)).

57. *Cf.* James Rubenstein, *Fed. Regions Go on Road to Brief New Constituents*, AM. BANKER, Sept. 18, 1980, at 3 (reporting that the Minneapolis Fed sent nonmember banks and credit unions an invitation to informational meetings stating that “[w]hile services will not become available until next year, it is not too early to learn about what the Federal Reserve has to offer”).

58. Press Release, Fed. Rsr. Bank of St. Louis (May 2, 1996), [https://fraser.stlouisfed.org/files/docs/publications/frbsl\\_news/frbsl-news-release-19960502.pdf](https://fraser.stlouisfed.org/files/docs/publications/frbsl_news/frbsl-news-release-19960502.pdf) [<https://perma.cc/2QFL-YBMG>].

59. *Id.*

60. *Interstate Branching: New Account Structure*, FED. RSRV. BD. (Sept. 27, 2002), <https://www.federalreserve.gov/generalinfo/isb/qanda.htm> [<https://perma.cc/QH9N-6KU5>].

61. *Id.*

62. *Operating Circular 1 (1998)*, *supra* note 10, § 1.2(a).

63. Letter from Helen E. Holcomb, First Vice Pres. & CEO, Fed. Rsr. Bank of Dallas to the CEO of each financial institution in the Eleventh Federal Reserve District (Nov. 12, 1997), <https://fraser.stlouisfed.org/title/district-notice-federal-reserve-bank-dallas-5569/federal-reserve-standardized-operating-circulars-546823> [<https://perma.cc/PE8B-BXHF>].

64. *Operating Circular 1 (1998)*, *supra* note 10, § 2; *Operating Circular 1 (2021)*, *supra* note 37, § 2.

65. *Operating Circular 1 (1998)*, *supra* note 10, § 1.1; *see also Operating Circular 1 (2021)*, *supra* note 37, § 1.1 (“This operating circular and its appendices (‘Circular’) set forth the terms under which a Financial Institution may open, maintain, and terminate a Master Account with its Administrative Reserve Bank (ARB).”).

Typically, this process for opening an account was quick—for many years the Federal Reserve Banks’ forms suggested it could be accomplished in five to seven business days.<sup>66</sup> The Reserve Banks did not conduct much of their own investigation when considering new account applications.<sup>67</sup> Instead, the Reserve Banks relied on the fact that the depository institution had been vetted by some other federal or state bank supervisor.<sup>68</sup> Applications were rarely, if ever, denied.<sup>69</sup> Today, Operating Circular 1 is substantially similar to its predecessors.<sup>70</sup> Yet recent account requests from novel financial institutions have drawn scrutiny. Before examining some of those novel applications, Part II discusses the written procedures for requesting Federal Reserve accounts and payment services in Operating Circular 1 and elsewhere.

## II. Account Procedures

As Part I suggests, the statutory authority governing Federal Reserve accounts is short on procedures. Instead, the process for opening and maintaining an account is largely governed by Operating Circular 1, a uniform account agreement of sorts, which was first adopted by the Federal Reserve Banks in 1998.<sup>71</sup> Reserve Banks may have their own internal policies, but only the Federal Reserve Bank of New York has published a guiding handbook.<sup>72</sup>

### A. Statutory & Regulatory Authority

Section 13 of the Federal Reserve Act, as amended, identifies four types of financial institutions eligible for Federal Reserve Bank accounts: member banks,<sup>73</sup> depository institutions,<sup>74</sup> nonmember banks,<sup>75</sup> and trust companies.<sup>76</sup>

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66. See *supra* note 12.

67. See Telephone Interview with Thomas Hoenig, *supra* note 11; Conti-Brown, *supra* note 11.

68. Cf. Policy on Payments System Risk, 71 Fed. Reg. 36800-1, 36806 (June 28, 2006) (explaining that in adopting risk policies it was not “intend[ing] to exert or create new supervisory or regulatory authority over any particular class of institutions or arrangements where the Board does not currently have such authority”).

69. See Reporter’s Transcript of Oral Argument at 37-39, *Fourth Corner Credit Union v. Fed. Rsv. Bank of Kansas City*, 154 F. Supp. 3d 1185 (D. Colo. 2016) (explaining that in the previous ten years, the Kansas City Fed had not denied any applications for accounts).

70. See generally *Operating Circular 1 (2021)*, *supra* note 37.

71. See *supra* notes 62-71; *infra* 85-108; and accompanying text.

72. See *infra* Section II.C.

73. 12 U.S.C. § 221 (2018) (defining “member bank” as “any national bank, State bank, or bank or trust company which has become a member of one of the Federal reserve banks”).

74. *Id.* § 461(b)(1)(A) (defining “depository institution” to include federally insured banks and credit unions as well as institutions that are eligible “to make application to become an insured bank” or credit union).

75. Nonmember banks are presumably banks that are not members of the Federal Reserve System. *Id.* § 221 (defining “bank” “to include State bank, banking association, and trust company”).

76. Federal statutes do not further define the term “trust company.” In general, trust companies “administer trusts and estates.” ANDREW P. SCOTT, CONG. RSCH. SERV., R47014, ANALYSIS OF BANK CHARTERS AND SELECTED POLICY ISSUES 14 (2022). “They make money by effectively charging management fees for overseeing the assets that have been assigned to them by clients or by taking a percentage of the assets once a trust is transferred to a third party.” *Id.*

Reserve Banks are authorized to receive general deposits from member banks and depository institutions.<sup>77</sup> The Federal Reserve Banks are also authorized to hold accounts “solely for the purposes of exchange or of collection” for nonmember banks, trust companies, and other depository institutions, provided that the account holder “maintains with the Federal Reserve bank of its district a balance in such amount as the Board determines taking into account items in transit, services provided by the Federal Reserve bank, and other factors as the Board may deem appropriate.”<sup>78</sup>

Section 13 of the Federal Reserve Act is supplemented by the Monetary Control Act of 1980. It provides that “[a]ll Federal Reserve bank [payment] services . . . shall be available to nonmember depository institutions and such services shall be priced at the same fee schedule applicable to member banks, except that nonmembers shall be subject to any other terms, including a requirement of balances sufficient for clearing purposes, that the Board may determine are applicable to member banks.”<sup>79</sup>

Neither the Federal Reserve Act nor the Monetary Control Act describe how financial institutions should request accounts or payment services. They also do not describe the process Reserve Banks should use when considering account access requests, allowing access to payment services, or closing an account.<sup>80</sup>

The Federal Reserve has promulgated some regulations governing accounts and payment services. For example, Regulation D governs bank reserve requirements, specifying that reserves can be kept in vault cash, “[i]n the institution’s account at the Federal Reserve Bank in the Federal Reserve District in which the institution is located,” or in a “pass-through” account with a correspondent bank.<sup>81</sup> Regulation J provides rules governing the collection of checks and other items that settle through the Federal Reserve.<sup>82</sup> But neither of

77. See 12 U.S.C. § 342 (2018).

78. *Id.*

79. Monetary Control Act of 1980, Pub. L. No. 96-221 § 105, 94 Stat. 132, 141 (codified at 12 U.S.C. § 248a(c)(2) (2018)).

80. This lack of process has led some to conclude that Congress did not intend that the Reserve Banks evaluate account requests. Instead, they argue that the statutes require Federal Reserve Banks to open accounts for all legally eligible financial institutions. See, e.g., *Fourth Corner Credit Union v. Fed. Rsr. Bank of Kansas City*, 861 F.3d 1052, 1067-74 (10th Cir. 2017) (per curiam) (Bacharach, J.); *Opposition to Defendant’s Motion to Dismiss at 14-19, TNB USA Inc. v. Fed. Rsr. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020), 2019 WL 2098395; Conti-Brown, *supra* note 11. The Federal Reserve rejects this interpretation of the statute and asserts broad discretion to deny or limit account and payment services access. *Guidelines for Evaluating Account and Services Requests*, 87 Fed. Reg. 51099, 51106 (Aug. 19, 2022) (“[I]t is important to make clear that legal eligibility does not bestow a right to obtain an account and services.”); *Federal Reserve Accounts and Services*, FED. RSRV. BANK S.F., <https://www.frbsf.org/banking/about/what-we-do/accounts-services/> [<https://perma.cc/NS5D-BBWV>] (“Approval of an application for an account or services is at the [San Francisco Fed’s] discretion.”). Resolving the extent of the Federal Reserve’s discretion is beyond the scope of this Article.

81. 12 C.F.R. § 204.5(a) (2022). A bank serving as a correspondent must “pass-through” the respondent’s reserves to the Federal Reserve Bank. See *id.* § 204.5(d)(4).

82. *Id.* § 210.25(a).

these regulations discusses financial institution access to account and payment services.

### *B. Operating Circular 1*

Federal Reserve Board regulations require the Federal Reserve Banks to issue operating circulars governing their payment services.<sup>83</sup> Since 1998, the Reserve Banks have issued uniform operating circulars.<sup>84</sup> Operating Circular 1 provides “the terms under which a Financial Institution may open, maintain, and terminate a Master Account.”<sup>85</sup>

A financial institution’s account must be held at the Federal Reserve Bank in the district where the bank is headquartered.<sup>86</sup> For example, a national bank headquartered in New York would request an account from the New York Fed and a state-chartered bank in Wyoming would request an account from the Kansas City Fed. In general, a financial institution can only hold one master account.<sup>87</sup>

A master account is identified by an institution’s primary nine-digit routing transit number.<sup>88</sup> Routing numbers are “assigned by the American Bankers Association (ABA) Registrar of Routing Numbers.”<sup>89</sup> (The ABA is a trade group of “FDIC insured banks and trust companies.”)<sup>90</sup> Under ABA policy, “[t]o be eligible for a Regular Routing Number, a bank must be eligible to maintain an account at a Federal Reserve Bank.”<sup>91</sup> When the ABA is uncertain whether a bank requesting a routing number is legally eligible, it asks for clarification from the Federal Reserve Bank in the applicant’s district.<sup>92</sup> Operating Circular 1 does not address which institutions are legally eligible.<sup>93</sup>

Operating Circular 1 has a three-paragraph section describing how to “establish a Master Account.”<sup>94</sup> First, the institution requesting the account must pass resolutions authorizing individuals to conduct business on behalf of the

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83. *Id.* §§ 201.3, 210.25(c), 201.40(c).

84. Letter from Helen E. Holcomb to CEO of each financial institution in the Eleventh Federal Reserve District, *supra* note 63; *Operating Circulars*, FED. RSRV. FIN. SERVS. (Feb. 26, 2000), <https://web.archive.org/web/20000226001833/https://www.frbservices.org/industry/operatingcirculars.cfm> [https://perma.cc/EBY5-JB6C].

85. *Operating Circular 1 (2021)*, *supra* note 37, § 1.0.

86. *Id.* § 2.5.

87. *Id.* § 2.1.

88. *Id.* § 2.2(e).

89. *Id.* § 2.2(g) (noting that routing transit numbers are also known as ABA numbers).

90. *About Membership*, AM. BANKERS ASS’N, <https://www.aba.com/about-us/membership/details> [https://perma.cc/4KM2-ZKTZ].

91. *Routing Number Policy & Procedures*, AM. BANKERS ASS’N (Jan. 28, 2022), <https://www.aba.com/news-research/research-analysis/routing-number-policy-procedures> [https://perma.cc/6VGS-AKBD].

92. *Id.*

93. *See Operating Circular 1 (2021)*, *supra* note 37, § 2.2(c) (defining “financial institution” to include “member bank,” “depository institution,” and “any other entity authorized to have a Master Account with a Reserve Bank”).

94. *Id.* § 2.6.

institution.<sup>95</sup> The Reserve Banks provide a one-page board resolution form.<sup>96</sup> Once an institution has adopted the resolution, it must provide a copy of the resolution and an official authorization list containing the signatures of the authorized individuals.<sup>97</sup> “An Authorized Individual must then execute a Master Account Agreement . . . .”<sup>98</sup>

The Master Account Agreement is one page.<sup>99</sup> It identifies the institution’s routing number, name, and address.<sup>100</sup> It lists the individuals to whom the Reserve Bank should direct questions about the accounts.<sup>101</sup> And finally, it states that the institution agrees to all Federal Reserve operating circulars.<sup>102</sup>

Nothing in Operating Circular 1 suggests that the process of opening a Federal Reserve account is time-consuming for either the requesting institution or the Reserve Bank. Indeed, for nineteen years, the Master Account Agreement stated that “[p]rocessing may take 5-7 business days.”<sup>103</sup> Currently, however, Operating Circular 1 and the account agreement do not address the expected length of the account opening process.

Operating Circular 1 contains several risk-management measures. Every account is “subject to other applicable Federal Reserve regulations and policies relating to accounts maintained at Reserve Banks such as . . . the Federal Reserve Policy Statement on Payment System Risk.”<sup>104</sup> The Reserve Bank “may require a Financial Institution that engages in certain transactions to maintain adequate balances with a Reserve Bank in such amount as the [Reserve Bank] determines.”<sup>105</sup> Accountholders cannot have a negative account balance overnight.<sup>106</sup> As collateral to cover overdrafts or other obligations, accountholders pledge all their property in the possession or control of any Reserve Bank (money in the master account, government securities held for the institution, etc.).<sup>107</sup>

Operating Circular 1 states that the Reserve Bank “may terminate a Master Account Agreement . . . at any time by notice to the Account Holder but will endeavor to give not less than five business days prior notice.”<sup>108</sup> Circular 1 does

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95. *Id.*

96. *Resolutions Authorizing an Institution to Open and Maintain Accounts and Use Services*, FED. RSRV. FIN. SERVS. (June 18, 2004), <https://www.frbsservices.org/binaries/content/assets/crsocms/forms/accounting/acct-holder-resolution.pdf> [<https://perma.cc/M5N9-2Q5P>].

97. *Operating Circular 1 (2021)*, *supra* note 37, § 2.6; *Federal Reserve Bank Official Authorization List*, FED. RSRV. FIN. SERVS. (Aug. 2012), <https://www.frbsservices.org/binaries/content/assets/crsocms/forms/accounting/acct-holder-list-rv.pdf> [<https://perma.cc/KBM6-KDXH>].

98. *Operating Circular 1 (2021)*, *supra* note 37, § 2.6.

99. *Operating Circular 1 app. 1 (2021)*, *supra* note 12.

100. *Id.*

101. *Id.*

102. *Id.*

103. *See supra* note 12 comparing appendix 1 in historic operating circulars.

104. *Operating Circular 1 (2021)*, *supra* note 37, § 1.0.

105. *Id.* § 2.11.

106. *Id.* § 5.1.

107. *Id.* § 5.3.

108. *Id.* § 2.10.

not provide standards for closing accounts or redress for institutions that believe their account was unfairly closed.

### C. New York Fed's Handbook

In addition to Operating Circular 1, Federal Reserve Banks may have other policies and procedures governing accounts. In 2004, the Federal Reserve Board significantly revised its policy statement on systemic risk in payment systems.<sup>109</sup> It instructed the Federal Reserve Banks to adopt risk management rules and procedures to comply with the best practices identified in the policy statement.<sup>110</sup> Recognizing that access to payments systems presents risk, the policy explained: “[e]xamples of key features that might be specified in a system’s rules and procedures are controls to limit participant-based risks, such as membership criteria based on participants’ financial and operational health[.]”<sup>111</sup>

Despite the Board’s recommendation that Reserve Banks adopt account access policies, only the Federal Reserve Bank of New York has publicly released such a policy.<sup>112</sup> The New York Fed’s first public document was 2017 guidance for “high risk” accounts.<sup>113</sup> By 2020, that guidance was expanded to a full-fledged Account and Financial Services Handbook that applies to novel banks that maintain or apply for an account. Specifically, the Handbook covers applicants that are “not subject to the supervision of a primary federal supervisor” or that “engage[] in activity that the [New York Fed] determines in its sole discretion, is unusual when compared to Financial Institutions with a similar type of charter or license or is otherwise unusual or suspicious.”<sup>114</sup>

The New York Fed instructs novel account applicants to provide written notice of their intent to seek services, rather than submit a completed account agreement.<sup>115</sup> The Handbook provides a list of documents that an applicant must

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109. Policy on Payments System Risk, 69 Fed. Reg. 69926 (Dec. 1, 2004).

110. *Id.* at 69928-29.

111. *Id.* at 69931 n.15. Although the policy has been revised several times, the Board’s instruction to Federal Reserve Banks to consider limiting risk through membership criteria remains. *Federal Reserve Policy on Payment System Risk*, BD. OF GOVERNORS OF THE FED. RSRV. SYS, 13 n.28 (2021), [https://www.federalreserve.gov/paymentsystems/files/psr\\_policy.pdf](https://www.federalreserve.gov/paymentsystems/files/psr_policy.pdf) [<https://perma.cc/7QFR-DUPS>].

112. Federal Reserve Bank Services, the organization that manages the Federal Reserve’s payment services, provides only New York’s Handbook on its web page. *District Information Forms*, FRBSERVICES.ORG, <https://www.frb services.org/forms/district-information> [<https://perma.cc/CRQ7-BT5R>].

113. *Guidance for Federal Reserve Financial Services Applicants that are Deemed High Risk by the Federal Reserve Bank of New York*, FED. RSRV. BANK. OF N.Y. (July 19, 2017), <https://web.archive.org/web/20171121230512/https://www.frb services.org/assets/forms/accounting/guidance-high-risk-new-york.pdf> [<https://perma.cc/N7S9-PA7S>].

114. *Account and Financial Services Handbook*, FED. RSRV. BANK OF N.Y. (Feb. 25, 2020), <https://www.frb services.org/binaries/content/assets/crsocms/forms/district-information/0220-frbny-financial-services-handbook.pdf> [<https://perma.cc/R4YZ-VJBX>] [hereinafter *N.Y. Fed Handbook*].

115. *Id.* at 3-5; *Supplemental Terms and Conditions Governing the Provision of Financial Services to High-Risk Customers*, FED. RSRV. BANK OF N.Y. § 2.6.1 (Feb. 25, 2020), <https://www.frb services.org/binaries/content/assets/crsocms/forms/district-information/0220-frbny->

provide when seeking a new account—everything from the applicant’s charter to a Know Your Customer questionnaire, to financial statements, to detailed business plans.<sup>116</sup> Novel applicants must demonstrate their resilience to operational risks, including that their technological systems adequately protect against cyber risks.<sup>117</sup> Moreover, novel applicants are required to “submit an assessment of an Independent Consultant or Auditor” as to whether the applicant has an adequate risk-based compliance framework, including “programs that adequately identify, assess, respond to, communicate, escalate, and monitor compliance risks associated with money-laundering, terrorist financing, and U.S. economic sanctions.”<sup>118</sup> In some cases the Reserve Bank may request meetings or calls with the applicants to “discuss any areas of concern.”<sup>119</sup>

The Handbook says little about how long the application process takes. The only deadline applies to the applicant, not the Reserve Bank. If the New York Fed has “follow-up questions or other requests,” the applicant has “30 calendar days” to answer or provide the requested documents.<sup>120</sup> If the applicant does not respond promptly, the New York Fed may deny the account request.<sup>121</sup> The Reserve Bank will generally notify applicants if their submission is acceptable or if additional information is required.<sup>122</sup>

In addition to the account agreement from Operating Circular 1, novel banks in the Federal Reserve’s second district must agree to supplemental terms and conditions.<sup>123</sup> Those terms and conditions give the Reserve Bank supervision-like authority over the novel bank. The Reserve Bank, for example, may at any time “conduct a review of the Customer’s operations and records as they relate to the Customer’s use of its Master Account and/or Financial services.”<sup>124</sup> In addition to providing access to documents and operations, the novel bank must “facilitate interviews for the [Reserve] Bank with Customer personnel” and “provide appropriate workspace to the [Reserve] Bank during those reviews.”<sup>125</sup> If the Reserve Bank identifies any “red flags” the novel bank

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supplemental-terms-and-conditions-for-high-risk-customers.pdf [https://perma.cc/U2XY-9W96] [hereinafter N.Y. Fed Terms & Conditions].

116. See generally *N.Y. Fed Handbook*, *supra* note 114. The New York Fed reserves the right to request additional information and documentation. *Id.* at 1. The San Francisco Fed’s webpage also provides a brief list of documents required when requesting a Federal Reserve account or services. *Federal Reserve Accounts and Services*, FED. RSRV. BANK S.F., <https://www.frbsf.org/banking/about/what-we-do/accounts-services/> [https://perma.cc/TL9P-JU56].

117. *N.Y. Fed Handbook*, *supra* note 114, at 1.

118. *Id.* at 5, 7-8.

119. *Id.* at 5.

120. *Id.* at 4.

121. *Id.* at 5.

122. *Id.* at 4.

123. *Id.* at 3; *N.Y. Fed Terms & Conditions*, *supra* note 115. In addition to these standard additional terms, the Reserve Bank can impose bank specific conditions and restrictions on novel bank accounts. *N.Y. Fed Terms & Conditions*, *supra* note 115, § 3.

124. *N.Y. Fed Terms & Conditions*, *supra* note 115, § 2.4.

125. *Id.*



must provide an explanation within ten days.<sup>126</sup> The novel bank also must inform the New York Fed of any material changes in its operations including changes in its business plan, regulatory or criminal investigations, changes in its means of facilitating payments, and changes in its ownership or legal structure.<sup>127</sup>

The New York Fed’s terms and conditions outsource some review and monitoring to external auditors and consultants. If the Reserve Bank requests it, a novel bank must engage a consultant to provide real-time transaction monitoring.<sup>128</sup> During the monitoring period all transactions must be approved by the monitor before they will be processed by the Reserve Bank.<sup>129</sup> The monitor must prepare a written report for both the novel bank and the Reserve Bank.<sup>130</sup> The Reserve Bank can also request that novel banks engage a consultant to “review the Customer’s past transaction activity” for compliance with anti-money laundering and export control laws.<sup>131</sup> Again, the consultant would report findings to the novel bank and the Reserve Bank.<sup>132</sup>

Although the Handbook usefully alerts novel applicants to the information required to request an account and risk-vetting conducted, it is careful to avoid binding the New York Fed to any procedural course or substantive outcome. The phrase “sole discretion” appears 25 times in the 14-page Handbook.<sup>133</sup>

#### *D. Federal Reserve Financial Services*

While the Reserve Banks are tasked with considering new account requests, the task of connecting an accountholder to the Federal Reserve’s payment rails falls to Federal Reserve Financial Services (FRFS), “an integrated organization within the Federal Reserve that is responsible for managing critical payment and securities services.”<sup>134</sup> The FRFS web page described the steps necessary to

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126. *Id.* § 2.5 (noting that the New York Fed can choose to extend the time). “Red flags” include violations of the Handbook or Terms and Conditions, “[u]nusual or suspicious activity,” an abnormal number of transactions when compared with the customer’s past practices, and regulatory or criminal investigations. *Id.* app. B.

127. *Id.* §§ 2.1.4, 2.6.2.

128. *Id.* § 2.2.3.

129. *Id.*

130. *Id.*

131. *Id.* § 2.2.4.

132. *Id.*

133. See generally *N.Y. Fed Handbook*, *supra* note 114. For example, the New York Fed “reserves the right, in its sole discretion, to determine whether a Financial Institution meets the factors set forth in this Handbook, or to consider any other factor [the Reserve Bank] determines to be relevant, or to grant, deny, restrict, suspend, terminate, or otherwise modify a Financial Institution’s access to any [Reserve Bank] account or Federal Reserve financial service.” *Id.* at 1.

134. *About Federal Reserve Bank Services*, FED. RSRV. FIN. SERVS., <https://www.frbfinancialservices.org/about/services> [<https://perma.cc/XN8M-LPP9>]. FRFS is overseen by the Financial Services Policy Committee, which “is composed of three Reserve Bank Presidents and two Reserve Bank first vice presidents.” See U.S. GOV’T ACCOUNTABILITY OFF., GAO-16-614, *Payment Services: Federal Reserve’s Competition with Other Providers Benefits Customers, but Additional Reviews Could Increase Assurance of Cost Accuracy*, 80 n.1 (2016), <https://www.gao.gov/assets/gao-16-614.pdf> [<https://perma.cc/ES5L-DFJU>]; FED. RSRV. BANK OF CHIC., ANN. REP. (2012), <https://www.chicagofed.org/-/media/publications/annual-report/2012-annual-report-pdf.pdf> [<https://perma.cc/CQ9M-UKGC>].

access payment services.<sup>135</sup> Nothing there seems to contemplate an extensive risk-vetting process by FRFS staff, separate from that performed by the Reserve Bank staff when opening an account.

Financial institutions that have not previously done business with FRFS are first instructed to call their Federal Reserve Bank.<sup>136</sup> The institution should be ready to provide its bank charter type, routing number, opening date, and whether it plans to process and settle transactions in-house or via a third-party processor.<sup>137</sup> Second, the institution should choose which Federal Reserve services it wants (check clearing, ACH, wire, etc.).<sup>138</sup> Third, the institution should decide how it wants to access the payment systems.<sup>139</sup> FRFS provides several technology options depending on the institution's needs and existing computer hardware and software.<sup>140</sup> Fourth, if the institution is opening a Federal Reserve account, it should "complete the Board Resolution and Official Authorization List form at least eight weeks before [the] institution plans to open for business."<sup>141</sup> These are the forms required by Operating Circular 1. FRFS also requires additional forms specific to the payment services requested.<sup>142</sup> Some services require scheduled testing to make sure that the system is functioning before the institution begins to use the system.<sup>143</sup> Finally, for an institution opening an account, FRFS advises the institution to "ensure that an authorized bank official is available at 9 a.m. on opening day for a confirmation call from the Federal Reserve Banks so that your Fed account will formally be opened by noon that same day."<sup>144</sup> In five easy steps, and within a contemplated eight weeks, a new financial institution can use Federal Reserve payment services.

### III. Novel Bank Applications

Reading the statutes, Operating Circular 1, and Federal Reserve Financial Services' web page gives the impression that financial institutions' path to Federal Reserve payments is straightforward and quick.<sup>145</sup> But this is not always the case. Recently, novel banks seeking Federal Reserve accounts have

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135. *New Financial Services Customer-Setup Services or Access*, FED. RSRV. FIN. SERVS., <https://www.frbsservices.org/resources/service-setup/new-customer.html> [<https://perma.cc/7QBS-6TZ6>].

136. *Id.*

137. *Id.*

138. *Id.*

139. *Id.*

140. *Fedline Solutions*, FED. RSRV. FIN. SERVS., <https://www.frbsservices.org/fedline-solutions/> [<https://perma.cc/AW69-M9VN>].

141. *New Financial Services Customer*, *supra* note 135.

142. *See, e.g., FedACH Participation Agreement Part 1: Agreement to Terms and General Participant Information*, FED. RSRV. FIN. SERVS. (Apr. 11, 2019), <https://www.frbsservices.org/binaries/content/assets/crsocms/forms/ach/part-1-rv.pdf> [<https://perma.cc/Q2SF-8VA3>].

143. *See, e.g., Fedwire Funds Service Setup Steps*, FED. RSRV. FIN. SERVS., <https://www.frbsservices.org/financial-services/wires/service-setup/steps.html> [<https://perma.cc/SW4Q-WDN7>].

144. *New Financial Services Customer*, *supra* note 135.

145. *See supra* Sections II.B and II.D.

encountered a murky, lengthy process from which some might not ever emerge. Using interviews, information requests, court filings, and press reports, this Part explores the Federal Reserve’s handling of novel account applications. It examines account requests from a cannabis credit union, a public bank, a narrow bank, a cryptocurrency custody bank, and a fintech trust company.

Admittedly, these case studies are not standard account applications. They are all “novel” banks—banks with nonstandard structures or business models. The novel banks profiled here were selected because there was some public information about their account requests. In all but one of the cases, the applicants chose to discuss their account requests. The other case attracted scrutiny from members of Congress. Because the Federal Reserve is so secretive, it is difficult to know whether these experiences are typical of novel bank applicants. We do not know, for example, how often novel banks request Federal Reserve accounts or how long it typically takes the Federal Reserve to reach decisions on account requests. Nevertheless, the experiences of these novel banks are similar enough to raise serious questions about the Federal Reserve’s process for handling novel account requests. It is unclear how banks should request accounts, who reviews requests, and what sort of risks are acceptable. These process deficiencies impact not just these banks but also other novel banks.

#### A. Cannabis Credit Union

The first Federal Reserve account application to receive significant public attention was from Fourth Corner Credit Union, a *de novo* institution that intended to serve the cannabis industry. Its application process was lengthy and highlights confusion about what materials financial institutions should submit when requesting a Federal Reserve account.

Although marijuana was (and is) illegal under federal law,<sup>146</sup> Colorado legalized it under state law.<sup>147</sup> The federal government lacked the will and the resources to punish most marijuana-related crimes, so the cannabis industry in Colorado grew.<sup>148</sup> But the state-legal cannabis industry was plagued with banking problems.<sup>149</sup> Because marijuana was still illegal under federal law, handling funds from the industry violated federal anti-money laundering laws.<sup>150</sup> At a minimum, the federal Financial Crimes Enforcement Network (FinCEN) and federal bank regulators expected banks to perform costly and detailed

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146. 18 U.S.C. §§ 802(6), 812(c)(10), 841(a) (2018).

147. COLO. CONST. art XVIII, § 16(1)(a).

148. See Robert A. Mikos, *Medical Marijuana and the Political Safeguards of Federalism*, 89 DENV. U. L. REV. 997, 1009 (2012) (stating that “the federal government lacks the fiscal and political capital needed to enforce [the marijuana] ban”); Alison Felix, *The Economic Effect of the Marijuana Industry in Colorado*, FED. RSRV. BANK OF KANSAS CITY (Apr. 16, 2018), <https://www.kansascityfed.org/denver/rocky-mountain-economist/rme-2018q1/> [<https://perma.cc/ZZ5N-MH7Y>] (detailing the growth of marijuana in Colorado).

149. Julie Andersen Hill, *Cannabis Banking: What Marijuana Can Learn from Hemp*, 101 B.U. L. REV. 1043, 1049-50 (2021); Julie Andersen Hill, *Banks, Marijuana, and Federalism*, 65 CASE W. RSRV. L. REV. 597, 600 (2015).

150. 18 U.S.C. §§ 1956(a)(1)(B), 1957(a) (2018).

reporting for cannabis-related accounts.<sup>151</sup> At worst, financial institutions and their employees faced criminal or regulatory punishment for banking the cannabis industry. Under these circumstances, most banks and credit unions would not open accounts or provide loans to cannabis-related businesses.<sup>152</sup>

Fourth Corner Credit Union intended to be different. It was the brainchild of Mark Mason, a North Carolina attorney, and his son, Alex Mason, a Colorado resident with friends in the cannabis industry.<sup>153</sup> They set out to create a new credit union, chartered under Colorado law, to bank the marijuana industry. In April 2014, Fourth Corner Credit Union submitted its application for a Colorado charter.<sup>154</sup> By November, Colorado banking officials granted the charter.<sup>155</sup> Its request to the American Bankers Association was similarly straightforward. Fourth Corner requested a routing number in August 2014 and received one within a month.<sup>156</sup>

The snag came when Fourth Corner Credit Union submitted its application to the Kansas City Fed for an account. In theory, Fourth Corner might have avoided opening its own Federal Reserve account by instead conducting transactions through a correspondent bank, but it seems highly unlikely that banks unwilling to serve the cannabis industry directly would have been eager to do so through an intermediary bank. Indeed, that was the point of organizing Fourth Corner Credit Union in the first place. So, in November 2014, immediately after receiving its charter, Fourth Corner Credit Union requested an account from the Kansas City Fed.<sup>157</sup>

Fourth Corner Credit Union's account application consisted of three documents: (1) the account agreement form from Operating Circular 1, (2) a resolution of the Credit Union's board of directors authorizing certain individuals

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151. See FIN. CRIMES ENF'T NETWORK, DEP'T OF THE TREASURY, FIN-2014-G001, BSA EXPECTATIONS REGARDING MARIJUANA-RELATED BUSINESSES (Feb. 14, 2014), <https://www.fincen.gov/sites/default/files/guidance/FIN-2014-G001.pdf> [https://perma.cc/346N-AWCC].

152. See Jennifer Shasky Calvery, Dir., Fin. Crimes Enf't Network, Remarks at Mid-Atlantic AML Conference 4 (Aug. 12, 2014), <https://www.fincen.gov/sites/default/files/2016-08/20140812.pdf> [https://perma.cc/3MCP-8VYF] (stating that 105 financial institutions had "engaged in banking relationships with marijuana-related businesses").

153. Misty Baxter, *Meet the Family Behind the Legal Weed Industry's First Credit Union*, ROLLING STONE (Jan. 8, 2015), <https://www.rollingstone.com/politics/politics-news/meet-the-family-behind-the-legal-weed-industrys-first-credit-union-86721/> [https://perma.cc/5X89-WV7B].

154. First Amended Complaint ¶ 38, *Fourth Corner Credit Union v. Fed. Rsrv. Bank of Kansas City*, 154 F. Supp. 3d 1185 (D. Colo. 2016) (No. 15-CV-01633).

155. Colorado Comm'r of Fin. Servs., Charter No. 272 The Fourth Corner Credit Union (Nov. 19, 2014); David Migoya, *Pot Turns a Huge Corner*, DENVER POST, Nov. 21, 2014, at 11A.

156. First Amended Complaint ¶¶ 44, 47, *Fourth Corner Credit Union v. Fed. Rsrv. Bank of Kansas City*, 154 F. Supp. 3d 1185 (D. Colo. 2016) (No. 15-CV-01633). While the ABA's quick issuance of a routing number suggests that Fourth Corner Credit Union was easily classified as a "depository institution," this may not have been the case. In court filings, Fourth Corner alleged that a few months after it received a routing number, the Kansas City Fed "asked the [National Credit Union Administration] (NCUA) if [Fourth Corner] was 'eligible to make application to become an insured credit union' pursuant to 12 U.S.C. § 1781." *Id.* ¶ 90. According to Fourth Corner, the NCUA later confirmed in writing that Fourth Corner was eligible. *Id.* ¶ 101.

157. *Id.* ¶ 53.

to conduct business on behalf of the Credit Union, and (3) a list of those authorized individuals.<sup>158</sup> “Shortly after submission” the Kansas City Fed’s Financial Management department “verified the authenticity of the signatures on the” documents and confirmed “that the forms were properly completed.”<sup>159</sup> Thereafter, Fourth Corner’s application languished. Representatives for the Credit Union were told the application was waiting for “approval by credit and risk.”<sup>160</sup> When Fourth Corner’s counsel inquired about the “rules pertaining to approval by credit and risk,” they were “advised that no such rules exist.”<sup>161</sup>

In January 2015, Fourth Corner received a letter from Esther L. George, the President of the Kansas City Fed. She explained that “[i]ssuance of a master account is within the Reserve Bank’s discretion and requires that the Reserve Bank be in a position to clearly identify the risk(s) posed by a financial institution and how that risk can be managed to the satisfaction of the Reserve Bank.”<sup>162</sup> However, rather than requesting additional information directly from Fourth Corner, George indicated that the Reserve Bank would consider material that the Credit Union had submitted to the National Credit Union Administration (NCUA) as part of its application for federal share insurance.<sup>163</sup> Representatives from the Reserve Bank and the NCUA discussed Fourth Corner’s application by telephone on at least two occasions.<sup>164</sup> More waiting ensued.

On July 2, 2015, the NCUA denied Fourth Corner’s application for federal share insurance.<sup>165</sup> This alone was not necessarily the death knell for Fourth Corner’s bid to become operational. Credit unions that are eligible to apply for federal share insurance are considered “depository institutions” that are legally eligible to apply for an account.<sup>166</sup>

Nevertheless, on July 16, 2015, the Kansas City Fed denied Fourth Corner Credit Union’s request for an account.<sup>167</sup> The denial letter focused primarily on the risks presented by Fourth Corner. The Reserve Bank wrote: “As a de novo depository institution, there is no historical record for the Bank to review, and the NCUA found insufficient information to assess [Fourth Corner’s] ability to safely and soundly operate and comply with applicable laws and regulations,

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158. *Id.* ¶¶ 57-58.

159. *Id.* ¶ 59.

160. *Id.* ¶ 61.

161. *Id.* ¶ 62.

162. *Id.* ¶ 100.

163. *Id.*

164. *Fourth Corner Credit Union v. Nat’l Credit Union Admin.*, No. 15-CV-01634 (D. Colo. June 25, 2018), 2016 WL 9735755, at \*1 (discussing a discovery dispute over notes made during these calls).

165. First Amended Complaint ¶ 112, *Fourth Corner Credit Union v. Fed. Rsrv. Bank of Kansas City*, 154 F. Supp. 3d 1185 (D. Colo. 2016).

166. 12 U.S.C. §§ 342, 461 (2018). Under Colorado law, Fourth Corner may be able to operate with private share insurance. *See Hill, supra* note 149, at 624 n.133 (explaining that the Colorado credit union regulator would have to find the private share insurance comparable to federal insurance).

167. Letter from Esther L. George, Pres., Fed. Rsrv. Bank of Kansas City, to Deirdra A. O’Gorman, CEO, The Fourth Corner Credit Union, July 16, 2015 (Doc. 01019611484, *Fourth Corner Credit Union v. Fed. Rsrv. Bank of Kansas City*, 861 F.3d 1052 (10th Cir. 2017) (No. 16-1016)).

including Bank Secrecy Act and Anti-Money Laundering responsibilities.”<sup>168</sup> Of course, this is always a problem with de novo depository institutions because they are, by definition, new.<sup>169</sup> The Kansas City Fed explained it was particularly concerned because Fourth Corner would “focus on serving marijuana-related businesses”—businesses that were illegal under federal law.<sup>170</sup> Moreover, the cannabis industry consisted of “relatively immature businesses operating in an environment of evolving laws and regulations.”<sup>171</sup>

It is not clear whether the Kansas City Fed would deny accounts for all banks whose customers consisted primarily of marijuana-related businesses. Parts of the denial letter are directed at deficiencies in Fourth Corner’s plans. For example, the Reserve Bank noted that Fourth Corner had “not demonstrated its ability to conduct appropriate enhanced monitoring requirements and manage its risk appropriately with respect to its customers with marijuana-related businesses.”<sup>172</sup> And the Reserve Bank explained that its “[c]oncern about this high-risk business model [was] heightened by the fact that [the Credit Union would] lack capital at inception, making it unable to absorb losses it may initially incur.”<sup>173</sup> Perhaps a well-capitalized bank with more robust money-laundering controls would have received an account. While Fourth Corner’s application was pending, some banks were serving the cannabis industry without any apparent consequences for their access to Federal Reserve payment systems.<sup>174</sup>

Unhappy with the decision, Fourth Corner Credit Union asked a federal court for an injunction requiring the Reserve Bank to open its account.<sup>175</sup> Fourth Corner argued that Reserve Banks have no discretion to deny account applications to a chartered depository institution.<sup>176</sup> The district court dismissed the case with prejudice, ruling that it could not use its equitable power to facilitate activity that was illegal under federal law—banking and thereby aiding cannabis businesses.<sup>177</sup>

Fourth Corner appealed.<sup>178</sup> Perhaps sensing that it was going to be difficult to convince courts or regulators to allow a financial institution focused on marijuana, Fourth Corner argued that it would serve cannabis businesses only if doing so was legal under federal law.<sup>179</sup> This change led to procedural

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168. *Id.*

169. It is, however, possible that in providing account and payment services, Reserve Banks sometimes apply a different standard to banks with existing accounts than they do when considering access for de novo banks.

170. Letter from Esther L. George to Deirdra A. O’Gorman, *supra* note 167.

171. *Id.*

172. *Id.*

173. *Id.*

174. Calvery, *supra* note 152.

175. *Fourth Corner Credit Union v. Fed. Rsrv. Bank of Kansas City*, 154 F. Supp. 3d 1185, 1185 (D. Colo. 2016), *vacated on appeal by* 861 F.3d 1052 (10th Cir. 2017).

176. *Id.* at 1187-88.

177. *Id.* at 1188-90.

178. *Fourth Corner Credit Union v. Fed. Rsrv. Bank of Kansas City*, 861 F.3d 1052 (10th Cir. 2017) (per curiam).

179. *Id.* at 1055-57 (Moritz, J.), 1058 (Matheson, J.), 1065 (Bacharach, J.).

disagreement among the three-judge panel tasked with deciding the case. Each judge wrote a separate opinion, but ultimately the Tenth Circuit panel remanded the case with “instructions to dismiss the amended complaint without prejudice.”<sup>180</sup> This left Fourth Corner free to file a new application for an account.

On September 12, 2017, Fourth Corner Credit Union submitted new documents to the Reserve Bank requesting an account.<sup>181</sup> Its application included the standard forms regarding individuals authorized to transact business on behalf of the Credit Union.<sup>182</sup> Fourth Corner also provided a copy of the board resolution stating that “[t]he Fourth Corner Credit Union shall not serve marijuana-related businesses until there is a change in federal law that authorizes financial institutions to serve marijuana-related businesses.”<sup>183</sup> This time the Reserve Bank requested additional information, explaining that Fourth Corner’s “unique” application raised “legal and policy questions.”<sup>184</sup> Fourth Corner thought it was entitled to an account, and the Reserve Bank had no authority to request additional information.<sup>185</sup> Rather than provide information, Fourth Corner again asked a federal court to grant an injunction forcing the Reserve Bank to open an account.<sup>186</sup>

While the lawsuit was pending and before any significant motions or briefings, the Kansas City Fed sent Fourth Corner Credit Union a letter conditionally granting account access.<sup>187</sup> There were three notable conditions. First, Fourth Corner promised to obtain NCUA share insurance or private share insurance.<sup>188</sup> Second, the Credit Union committed to adopt a board resolution and amend its bylaws to prevent it from providing “any service to Marijuana-Related Businesses . . . unless and until it becomes lawful under federal law to

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180. *Id.* at 1053 (per curiam).

181. Complaint ¶ 34, Fourth Corner Credit Union v. Fed. Rsr. Bank of Kansas City, No. 17-CV-02361 (D. Colo. Sept. 29, 2017); Answer ¶ 34, Fourth Corner Credit Union v. Fed. Rsr. Bank of Kansas City, No. 17-CV-02361 (D. Colo. Nov. 8, 2017).

182. *See* Complaint ¶ 34, Fourth Corner Credit Union v. Fed. Rsr. Bank of Kansas City, No. 17-CV-02361 (D. Colo. Sept. 29, 2017); Answer ¶ 34, Fourth Corner Credit Union v. Fed. Rsr. Bank of Kansas City, No. 17-CV-02361 (D. Colo. Nov. 8, 2017).

183. Complaint ¶ 41, Fourth Corner Credit Union v. Fed. Rsr. Bank of Kansas City, No. 17-CV-02361 (D. Colo. Sept. 29, 2017); Answer ¶ 41, Fourth Corner Credit Union v. Fed. Rsr. Bank of Kansas City, No. 17-CV-02361 (D. Colo. Nov. 8, 2017).

184. Complaint ¶¶ 33, 50, Fourth Corner Credit Union v. Fed. Rsr. Bank of Kansas City, No. 17-CV-02361 (D. Colo. Sept. 29, 2017); Answer ¶¶ 33, 50, Fourth Corner Credit Union v. Fed. Rsr. Bank of Kansas City, No. 17-CV-02361 (D. Colo. Nov. 8, 2017) (internal quotation marks omitted).

185. Complaint ¶¶ 33, 38-40, 50-52, Fourth Corner Credit Union v. Fed. Rsr. Bank of Kansas City, No. 17-CV-02361 (D. Colo. Sept. 29, 2017).

186. *See id.* at 18, ¶ 1 (requesting injunctive relief).

187. Stipulation of Dismissal, Fourth Corner Credit Union v. Fed. Rsr. Bank of Kansas City (D. Colo. Feb. 2, 2018); Letter from Susan E. Zubradt, Senior Vice Pres., Fed. Rsr. Bank of Kansas City to Deirdra O’Gorman & Christopher E. Nevitt, Fourth Corner Credit Union (Feb. 2, 2018) (copy on file with author).

188. Letter from Susan E. Zubradt to Deirdra O’Gorman & Christopher E. Nevitt, *supra* note 187, at 2.

provide banking or financial service to them.”<sup>189</sup> Third, the Credit Union pledged to adopt a compliance program to prevent inadvertently serving the cannabis industry.<sup>190</sup> The Reserve Bank was aware that its decision on Fourth Corner’s account was likely to receive public attention. It wrote: “This letter does not express the policy views of [the Kansas City Fed] or The Board of Governors of the Federal Reserve System, nor does it contain any supervisory, regulatory, or enforcement guidance or precedent.”<sup>191</sup>

So far, Fourth Corner Credit Union has been unsuccessful in its quest to secure private share insurance.<sup>192</sup> It is again pursuing NCUA share insurance with a promise not to bank cannabis-touching businesses unless authorized under federal law.<sup>193</sup> As a result, Fourth Corner still has not opened a Federal Reserve account.

### *B. Narrow Bank*

Another Federal Reserve account application from a proposed bank without deposit insurance has been pending for years. TNB USA Inc. began trying to open an account at the New York Fed in the fall of 2017.<sup>194</sup> TNB stands for “[T]he [N]arrow [B]ank.”<sup>195</sup> It intends to accept deposits, but not make loans.<sup>196</sup> The delay for TNB’s application seems driven by Federal Reserve Board concerns about TNB’s impact on the Fed’s ability to conduct monetary policy. But it is not clear what role, if any, the Reserve Board plays in evaluating accounts requests.

TNB’s business plan rests on the Federal Reserve’s decision to begin paying interest on banks’ excess reserves in 2008.<sup>197</sup> The Federal Reserve hoped that by paying interest on excess reserves (IOER), banks would hold excess reserves in Federal Reserve accounts when the IOER rate exceeded the interest

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189. *Id.* Fourth Corner also promised not to subsequently amend its bylaws to allow service to cannabis businesses until federal law allowed those banking services. *Id.*

190. *Id.*

191. *Id.* at 3.

192. E-mail from Mark Mason, Att’y, Fourth Corner Credit Union to author (Feb. 2, 2021) (on file with author).

193. *Id.*

194. TNB USA Inc. v. Fed. Rsr. Bank of N.Y., No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020), 2020 WL 1445806, at \*2.

195. *About Us*, TNB, <https://www.tnbusa.com/about/> [<https://perma.cc/DF66-PUW7>].

196. Complaint ¶ 2, TNB USA Inc. v. Fed. Rsr. Bank of N.Y., No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020).

197. Banks must keep a minimum amount of reserves on deposit with the Federal Reserve. 12 U.S.C. § 461 (2018). Banks, however, can choose to maintain Federal Reserve balances exceeding that required; these are excess reserves. *TNB USA Inc.*, 2020 WL 1445806, at \*1. Congress authorized the Federal Reserve to begin paying interest on both required and excess reserves during the 2008 financial crisis. Financial Services Regulatory Relief Act of 2006, Pub. L. No. 109-351, §§ 201-03, 120 Stat. 1966, 1968-69 ) (codified at 12 U.S.C. § 462(b)(12) (2018)) (authorizing the Federal Reserve to begin paying interest on October 1, 2011); Emergency Economic Stabilization Act of 2008, Pub. L. No. 110-343, § 128, 122 Stat. 3765, 3796 (accelerating the date the Federal Reserve could begin paying interest to October 1, 2008); *see also* Reserve Requirements of Depository Institutions, 73 Fed. Reg. 59482 (Oct. 9, 2008) (announcing the Federal Reserve’s plan to pay interest on excess reserves).



from lending to other banks.<sup>198</sup> Thus, in setting the IOER rate, the Federal Reserve could effectively set a lower bound for the federal funds rate (the rate at which banks lend to each other).<sup>199</sup>

But what the Federal Reserve sees as a tool of monetary policy,<sup>200</sup> TNB plans to translate into a money-making opportunity. TNB's CEO and chairman of the board, James McAndrews, headed the research division at the New York Fed from 2010 to 2016.<sup>201</sup> While there, he studied both the Fed's use of IOER and the Fed's creation of a facility to pay interest to select non-bank institutional investors.<sup>202</sup> From this grew the idea of a private sector narrow bank.<sup>203</sup> McAndrews left the New York Fed in 2016 and began organizing TNB.<sup>204</sup>

TNB wants to accept deposits from institutional investors, like money market funds and pension funds, who are not themselves eligible for Federal Reserve accounts.<sup>205</sup> TNB will then place all its customers' deposits in its Federal Reserve account, earning the IOER rate of interest.<sup>206</sup> "TNB will pay interest to its depositors at a . . . lower rate, thereby earning a . . . profit."<sup>207</sup> The appeal for

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198. Reserve Requirements of Depository Institutions, 73 Fed. Reg. at 59482; *TNB USA Inc.*, 2020 WL 1445806, at \*2.

199. *TNB USA Inc.*, 2020 WL 1445806, at \*1.

200. Press Release, Bd. of Governors of the Fed. Rsrv. Sys., Board Announces that It Will Begin to Pay Interest on Depository Institutions' Required and Excess Reserve Balances (Oct. 6, 2008, 8:15 AM ET), <https://www.federalreserve.gov/newsevents/pressreleases/monetary20081006a.htm> [<https://perma.cc/LJ5Z-9ENF>].

201. See Binyamin Appelbaum, *Former Official Sues the Fed for Rejecting a Plan for a New Kind of Bank*, N.Y. TIMES, Sept. 7, 2018, at B7; Editorial, *Narrow Odds for Narrow Banks*, WALL ST. J. (Sept. 12, 2018, 7:00 PM ET), <https://www.wsj.com/articles/narrow-odds-for-narrow-banks-1536793230> [<https://perma.cc/YHF6-Z24G>].

202. See Antoine Martin, James McAndrews, Ali Palida & David Skeie, *Federal Reserve Tools for Managing Rates and Reserves*, FED. RSRV. BANK OF N.Y. STAFF REP. 642 (2019), [https://www.newyorkfed.org/medialibrary/media/research/staff\\_reports/sr642.pdf](https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr642.pdf) [<https://perma.cc/KWE2-M7RF>]; James McAndrews & Andrew Kroeger, *The Payment System Benefits of High Reserve Balances*, FED. RSRV. BANK OF N.Y. STAFF REP. 779 (2016), [https://www.newyorkfed.org/medialibrary/media/research/staff\\_reports/sr779.pdf?la=en](https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr779.pdf?la=en) [<https://perma.cc/CS2F-R98R>]; Michael Derby, *Bank Sues New York Fed Over Lack of Account*, WALL ST. J. (Sept. 5, 2018), <https://www.wsj.com/articles/bank-sues-new-york-fed-over-lack-of-account-1536185523> [<https://perma.cc/N466-29KL>].

203. James McAndrews, Chairman & CEO, TNB USA Inc., *Narrow Banking: Delivering Safety and Competition to the Market for Large Deposits, Address at the Harvard Law School Conference Money as a Democratic Medium*, YOUTUBE (Dec. 15, 2018), [https://www.youtube.com/watch?v=YPudibodp\\_E](https://www.youtube.com/watch?v=YPudibodp_E) [<https://perma.cc/B5U8-EEVQ>] (1:01:21)).

204. See Applebaum, *supra* note 201, at B7 (stating that McAndrews "left the Fed in 2016"); Complaint at 10, *TNB USA Inc. v. Fed. Rsrv. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020) (stating that "TNB began discussions with the [Connecticut Department of Banking]" in July 2016).

205. Letter from James McAndrews, Chairman & CEO, TNB USA Inc. to Ann E. Misback, Sec'y, Bd. of Governors of the Fed. Rsrv. Sys. 1 n.1 (June 11, 2021), [https://www.federalreserve.gov/SECRS/2021/July/20210708/OP-1747/OP-1747\\_061121\\_138143\\_448935872132\\_1.pdf](https://www.federalreserve.gov/SECRS/2021/July/20210708/OP-1747/OP-1747_061121_138143_448935872132_1.pdf) [<https://perma.cc/WSH9-DS4U>]; Complaint ¶ 1, *TNB USA Inc. v. Fed. Rsrv. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020).

206. Complaint at 9, *TNB USA Inc. v. Fed. Rsrv. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020).

207. *Id.*; see also Memorandum of Law in Support of Defendant Fed. Rsrv. Bank of N.Y.'s Motion to Dismiss at 1, *TNB USA Inc. v. Fed. Rsrv. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020) ("TNB seeks to open a deposit account at the New York Fed not so that it can engage in the typical business of banking, but solely so that TNB can park the funds of its wealthy, institutional depositors in the account and pass TNB's IOER earnings on to them, after taking a cut for itself.").

potential TNB depositors is two-fold. First, TNB would provide a safe and liquid place for institutional investors to hold cash.<sup>208</sup> Second, TNB “would offer its customers a higher rate than they could earn [from such low-risk deposits] elsewhere.”<sup>209</sup>

To implement this plan, TNB sought a banking charter from the Connecticut Department of Banking.<sup>210</sup> Because TNB’s deposit base would consist of large institutional investors with deposits well beyond the insurable amount, TNB did not request deposit insurance from the FDIC.<sup>211</sup> On August 10, 22, 2017, Connecticut issued a temporary certificate of authority for TNB’s bank.<sup>212</sup> It included several conditions that TNB would have to satisfy before opening the bank. One of the conditions was that TNB provide “evidence that the [New York Fed] would open a master account for TNB.”<sup>213</sup>

In September 2017, TNB sought a routing number from the ABA.<sup>214</sup> The ABA requested confirmation of TNB’s eligibility from the New York Fed.<sup>215</sup> TNB and the New York Fed discussed whether TNB was eligible given the conditional nature of its Connecticut charter, but the New York Fed eventually agreed “that TNB would be eligible for a master account upon issuance of” final approval from Connecticut to open the bank.<sup>216</sup> Within a few months, TNB had a routing number,<sup>217</sup> but that was only the first hurdle.

The New York Fed began conducting due diligence to decide whether to allow TNB to open an account.<sup>218</sup> The New York Fed deemed a due diligence risk assessment necessary because TNB would be uninsured and have no federal

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208. “Narrow Bank” Challenges Traditional Industry Model, But Fed Pushes Back, S&P GLOB. MKT. INTEL. (Mar. 27, 2019), <https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/narrow-bank-challenges-traditional-industry-model-but-fed-pushes-back-49204495> [<https://perma.cc/EFF9-Y5AB>]; Gavriel Schreiber, *The Narrow Bank Update: SDNY Dismisses TNB Suit*, JUST MONEY (Mar. 30, 2020), <https://www.printfriendly.com/p/g/spTct8> [<https://perma.cc/KUU6-WQ7Q>].

209. *Narrow Odds for Narrow Banks*, *supra* note 201.

210. *TNB USA Inc. v. Fed. Rsrv. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020), 2020 WL 1445806, at \*2.

211. Complaint at 9, *TNB USA Inc. v. Fed. Rsrv. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020). Other commentators have noted that narrow banks that invest in only liquid, safe assets have little need for deposit insurance. *See* Schreiber, *supra* note 208 (stating that because “[a]ll money deposited at TNB will be in the Fed[,] . . . there is no risk of TNB being unable to meet demands for deposits”).

212. *New Banks in Connecticut*, STATE CONN. DEP’T BANKING, <https://portal.ct.gov/DOB/Bank-Information/Bank-Information/New-Banks-in-Connecticut> [<https://perma.cc/332A-KC3J>] (noting that temporary certificates are effective for eighteen months, but that TNB’s was extended on January 25, 2019, August 18, 2020, and February 9, 2022).

213. Complaint at 10, *TNB USA Inc. v. Fed. Rsrv. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020).

214. *TNB USA Inc.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020), 2020 WL 1445806, at \*2.

215. *Id.*

216. *Id.*

217. *Id.*

218. Complaint at 12, *TNB USA Inc. v. Fed. Rsrv. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020).

supervisor.<sup>219</sup> As part of the risk assessment, TNB responded to a series of document and information requests, including requests for information about creditworthiness and anti-money laundering issues.<sup>220</sup> The New York Fed advised TNB that it should not submit its formal application for an account until the due diligence process was completed.<sup>221</sup>

During the due diligence process, attorneys at the New York Fed became concerned about “the novelty of TNB’s business model” and consulted with the Federal Reserve Board.<sup>222</sup> The Board became concerned that allowing IOER to pass through TNB to institutional investors “could complicate the implementation of monetary policy, disrupt financial intermediation, and negatively impact our nation’s financial stability.”<sup>223</sup> In particular, the Board was concerned that, unlike traditional banks, a narrow bank would earn interest at the IOER rate without being constrained by “the costs of capital requirements and other elements of federal regulation and supervision.”<sup>224</sup> TNB believes the Board’s concerns are misplaced. It believes that “TNB’s business model will, if anything, only enhance the efficacy of IOER as a policy tool.”<sup>225</sup>

On Valentine’s Day 2018, “TNB’s principals and legal advisors met in Washington, D.C. with several members of the [New York Fed] and the Board’s staff, including its General Counsel” to advocate for TNB’s account.<sup>226</sup> But the Federal Reserve Board was apparently not feeling the love, and review of TNB’s account application continued. On April 26, 2018, TNB submitted a written response to the policy concerns to both the New York Fed and the Federal Reserve Board.<sup>227</sup> The next day, TNB submitted a formal application requesting an account.<sup>228</sup> Shortly thereafter, the New York Fed’s general counsel wrote that the New York Fed was not prepared to issue the account because “senior policy

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219. Memorandum of Law in Support of Defendant Fed. Rsrv. Bank of N.Y.’s Motion to Dismiss at 6, *TNB USA Inc. v. Fed. Rsrv. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020).

220. Complaint at 12, *TNB USA Inc. v. Fed. Rsrv. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020).

221. *Id.*

222. Memorandum of Law in Support of Defendant Fed. Rsrv. Bank of N.Y.’s Motion to Dismiss at 7, *TNB USA Inc. v. Fed. Rsrv. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020).

223. Memorandum of Law of Amicus Curiae the Bd. of Governors of the Fed. Rsrv. in Support of Defendant the Fed. Rsrv. Bank of N.Y.’s Motion to Dismiss, *TNB USA v. Fed. Rsrv. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020).

224. Advance Notice of Proposed Rulemaking: Regulation D: Reserve Requirements of Depository Institutions, 84 Fed. Reg. 8829, 8830 (Mar. 12, 2019). The Board also worried that the narrow bank might draw deposits away from traditional banks, requiring those banks to seek more expensive funding to provide credit to consumers and businesses. *Id.*

225. Complaint at 19, *TNB USA Inc. v. Fed. Rsrv. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020). TNB explains that by passing much of the IOER along to depositors TNB would “more efficiently and effectively transmit[] rising Federal Reserve interest rates to TNB depositors.” *Id.* TNB claims that concerns about the potential size and volatility of TNB’s deposit base can be effectively managed by measures such as counterparty caps, aggregate caps, and throttling depositor’s movement of funds. McAndrews, *supra* note 203, at 1:01:56–1:06:04; Letter from James McAndrews to Ann E. Misback, *supra* note 205, at 5.

226. Complaint at 14, *TNB USA Inc. v. Fed. Rsrv. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020).

227. *Id.*

228. *Id.*

officials at the Board . . . have expressed the strong view that the New York Fed should not approve TNB's request."<sup>229</sup>

Frustrated that its process of opening an account was dragging on, TNB filed suit against the New York Fed on August 31, 2018.<sup>230</sup> It asked the court to declare that TNB was entitled to a Federal Reserve account.<sup>231</sup>

While the suit was pending, the Federal Reserve Board issued an advance notice of proposed rulemaking seeking comments on whether the Federal Reserve should amend its regulations to "lower the rate" of IOER for "institutions that hold a very large proportion of their assets in the form of balances at Reserve Banks."<sup>232</sup> The notice summarized the Board's policy concerns surrounding "narrowly focused business models that involve taking deposits from institutional investors and investing all or substantially all of the proceeds in balances at Reserve Banks."<sup>233</sup>

Days later, the New York Fed asked the court to dismiss the case on ripeness grounds because TNB's "application for a master account is still under consideration."<sup>234</sup> The New York Fed said it was still considering whether TNB's "business plan and proposed capital structure" allowed it to be classified as a "depository institution" and therefore eligible to apply for an account.<sup>235</sup> Apparently, the New York Fed did not consider that issue closed when it allowed the ABA to issue TNB's routing number.<sup>236</sup> TNB protested that the New York Fed had effectively denied its application by refusing to act.<sup>237</sup>

The federal district court found that the New York Fed had "not reached a decision on TNB's application."<sup>238</sup> Accordingly, the court dismissed the case because TNB lacked standing and its claim was unripe.<sup>239</sup> Rather than appeal the district court's opinion, TNB decided to "work directly with the Federal Reserve

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229. Opposition to Defendant's Motion to Dismiss at 11, *TNB USA Inc. v. Fed. Rsr. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020) (citing Letter from Michael Held, Gen. Couns., Fed. Rsr. Bank of N.Y., to Thomas E.L. Dewey, Dewey Pegno & Kramarsky LLP (May 16, 2018)).

230. Complaint, *TNB USA Inc. v. Fed. Rsr. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020).

231. *Id.* at 23.

232. Advance Notice of Proposed Rulemaking: Regulation D: Reserve Requirements of Depository Institutions, 84 Fed. Reg. 8829, 8829 (Mar. 12, 2019).

233. *Id.*

234. Memorandum of Law in Support of Defendant Fed. Rsr. Bank of N.Y.'s Motion to Dismiss at 7-9, *TNB USA Inc. v. Fed. Rsr. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020); *see also* *TNB USA Inc. v. Fed. Rsr. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020), 2020 WL 1445806, at \*4.

235. Memorandum of Law in Support of Defendant Fed. Rsr. Bank of N.Y.'s Motion to Dismiss at 7 n.4, *TNB USA Inc. v. Fed. Rsr. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020).

236. *See supra* notes 214-217 and accompanying text (discussing TNB's path to an ABA routing number).

237. Opposition to Defendant's Motion to Dismiss at 11, *TNB USA Inc. v. Fed. Rsr. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020).

238. *TNB USA Inc. v. Fed. Rsr. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020), 2020 WL 1445806, at \*6.

239. *Id.* at \*6-10.

to resolve” the account issue.<sup>240</sup> More than five years after raising the issue of an account with the New York Fed, TNB still has no official answer.

### C. Cryptocurrency Custody Bank

Other Federal Reserve account applications have also spent years in the due diligence process. Custodia, a Wyoming special purpose depository institution, applied for an account at the Kansas City Fed in 2020.<sup>241</sup> Custodia hopes to accept U.S. dollar-denominated deposits and provide cryptocurrency custody services.<sup>242</sup> Although Wyoming consulted with the Federal Reserve in developing its special purpose depository institution charter, the Federal Reserve’s delay appears to be driven partly by concerns about the charter. The Kansas City Fed undertook an extensive review process. It finally denied Custodia’s request in 2023 after Custodia challenged the long delay in court.<sup>243</sup> Custodia believes that the Kansas City Fed’s risk-vetting process did not comply with the law and has promised to pursue its legal remedies.<sup>244</sup>

Cryptocurrencies (and blockchain technology underpinning some cryptocurrencies) are, of course, relatively new.<sup>245</sup> As cryptocurrencies have grown in popularity, many states have considered and enacted statutory modernizations to address the unique issues they present.<sup>246</sup> But so far Wyoming is leading the way.<sup>247</sup> In 2018, the Wyoming legislature created the Blockchain

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240. *Minutes of Special Meeting of the Connecticut Department of Banking Requested by the Organizers of TNB Bank for Extension of the Temporary Certificate of Authority*, STATE OF CONN. DEP’T OF BANKING (Aug. 18, 2020), <https://portal.ct.gov/-/media/DOB/Enforcement/FID/TNB-USA-Special-Meeting-8-18-2020-Minutes.pdf> [https://perma.cc/F738-H58E].

241. Lummis, *supra* note 17. Three additional banks, Kraken (parent company Payward, Inc.), Commerce Financial, Inc., and Wyoming Deposit & Transfer (trade name BankWyse), have received Wyoming special purpose depository institution charters. *Kraken Wins Bank Charter Approval*, KRAKEN (Sept. 16, 2020), <https://blog.kraken.com/post/6241/kraken-wyoming-first-digital-asset-bank/> [https://perma.cc/6WCC-LTSV]; Nate DiCamillo, *Commerce Financial Becomes Fourth Wyoming Chartered Crypto Bank*, COINDESK (Sept. 14, 2021, 9:38 AM EDT), <https://www.coindesk.com/business/2021/08/11/commerce-financial-becomes-fourth-wyoming-chartered-crypto-bank/> [https://perma.cc/2ACE-LGNJ]. Kraken has also requested a Federal Reserve account, and its request has been similarly delayed. Lummis, *supra* note 17. This section studies Custodia because it has extensively discussed its request for a Federal Reserve account.

242. *Avanti Granted Bank Charter and Approval of Business Plan for Digital Asset Custody and Tokenized U.S. Dollar*, CUSTODIA (Oct. 28, 2020), <https://custodiabank.com/press/bank-charter-granted/> [https://perma.cc/MZ82-BQ9T].

243. Kyle Campbell, *Kansas City Fed Rejects Custodia’s Master Account Application*, AM. BANKER (Jan. 27, 2023, 6:07 PM EST), <https://www.americanbanker.com/news/kansas-city-fed-rejects-custodias-master-account-application>, 2023 WLNR 3332024.

244. *Id.*

245. One of the earliest U.S. law review articles using the term “cryptocurrency” appeared in 2012. Nikolei M. Kaplanov, Note, *Nerdy Money: Bitcoin, the Private Digital Currency, and the Case Against Its Regulation*, 25 LOY. CONSUMER L. REV. 111 (2012).

246. *Chain Reaction: Blockchain Enters the Mainstream*, GLOB. BLOCKCHAIN BUS. COUNCIL, 53 (2020), <https://gbbccouncil.org/wp-content/uploads/2020/01/GBBC-2020-Annual-Report.pdf> [https://perma.cc/LQ6H-SBPk].

247. *Id.*; Caitlin Long, *What Do Wyoming’s 13 New Blockchain Laws Mean?*, FORBES (Mar. 4, 2019, 7:29 AM EST), <https://www.forbes.com/sites/caitlinlong/2019/03/04/what-do-wyomings-new-blockchain-laws-mean/?sh=396b27df5fde> [https://perma.cc/3Q6T-5YX2].

Task Force to “identify governance issues related to blockchain technology and develop appropriate legislation.”<sup>248</sup> The next year, with the Taskforce leading the way, the Wyoming legislature passed a flurry of laws related to cryptocurrency and blockchain technology.<sup>249</sup> Among those laws was one creating a special purpose depository institution (SPDI, pronounced “speedy”) charter.<sup>250</sup> The law allows SPDIs to provide cryptocurrency custody services, accept deposits, and provide payment services.<sup>251</sup> However, unlike traditional banks, SPDIs cannot make loans.<sup>252</sup> Moreover, SPDIs have a one hundred percent reserve requirement for their U.S. dollar deposits.<sup>253</sup> The reserves must be held in liquid assets (for example, deposits in a Federal Reserve account) and cannot be encumbered.<sup>254</sup>

From the beginning, Wyoming understood that access to the Federal Reserve’s payment systems would be critical to the success of its SPDIs.<sup>255</sup> The Wyoming legislature crafted the SPDI statute to ensure that SPDIs meet the legal eligibility requirements for Federal Reserve accounts and payment services. The statute calls the banks “depository institutions” and provides that they can accept deposits.<sup>256</sup> Wyoming also sought to ensure that its supervision of the SPDIs would be robust enough to alleviate Federal Reserve concerns about undue risk. In developing the legal framework for SPDIs, Wyoming officials held “more than 100 meetings with the Board of Governors and the [Kansas City Fed].”<sup>257</sup>

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248. 2018 Wyo. Sess. Laws 390.

249. 2019 Wyo. Sess. Laws 197 (“Financial Technology Sandbox”); 2019 Wyo. Sess. Laws 485 (“Wyoming Utility Token Act-Property Amendments”); 2019 Wyo. Sess. Laws 346 (“Commercial Filing System”); 2019 Wyo. Sess. Laws 328 (“Special Purpose Depository Institutions”); 2018 Wyo. Sess. Law 160 (“Special Electric Utility Agreements”); 2019 Wyo. Sess. Law 345 (“Corporate Stock-Certificate Tokens”); 2019 Wyo. Sess. Law 99 (“Banking Technology and Stock Revisions”); 2019 Wyo. Sess. Law 322 (“Digital Assets-Existing Law”).

250. 2019 WYO. SESS. 328 (codified as amended in WYO. STAT. ANN. §§ 13-12-101 to 13-12-126 (West 2023)).

251. WYO. STAT. ANN. § 13-12-103 (West 2023) (allowing SPDIs to engage in “nonlending banking business” and provide “payment services” and “custodial services” under Wyoming’s digital assets statute). Subsequently, the Wyoming Division of Banking promulgated an administrative framework and developed an examination manual outlining the supervisory oversight of these new banks. 21-2-20 WYO. CODE R. §§ 1-13 (LexisNexis 2023); *Special Purpose Depository Institutions Examination Manuals*, WYO. DIV. OF BANKING (Jan. 2021), [https://drive.google.com/file/d/14dA8hrR59aGsKZYxAolWQ7dVr32cr\\_Vw/view?usp=sharing](https://drive.google.com/file/d/14dA8hrR59aGsKZYxAolWQ7dVr32cr_Vw/view?usp=sharing) [https://perma.cc/KJB4-AWBP].

252. WYO. STAT. ANN. § 13-12-103(c) (West 2023).

253. *Id.* § 13-12-105.

254. *Id.*

255. See Chris Matthews, *How Wyoming Became the Promised Land for Bitcoin Investors*, MARKETWATCH (Apr. 24, 2021, 8:21 AM ET), <https://www.marketwatch.com/story/how-wyoming-became-the-promised-land-for-bitcoin-investors-11619201182> [https://perma.cc/29JE-WT27] (quoting then Wyoming Commissioner of Banking Albert Forkner as stating that access to Federal Reserve accounts is “borderline essential” for the success of the SPDI charter).

256. WYO. STAT. ANN. §§ 13-12-101, 13-12-103(b)(vii)(E), 13-12-104 (West 2023).

257. Lummis, *supra* note 17. An early draft of the Wyoming legislation required the state attorney general to sue if the Federal Reserve did not open accounts for SPDIs. Patrick Wolfenbarger, *Federal Reserve Delays Approval of Master Accounts for Wyoming Special Purpose Depository Institutions*, WYO. BUS. REP. (Apr. 24, 2022), [https://www.wyomingnews.com/wyomingbusinessreport/current\\_edition/federal-reserve-delays-approval-of-master-accounts-for-wyoming-special-purpose-depository-institutions/article\\_17cd42c9-6204-5568-a6aa-a5e19b760d9c.html](https://www.wyomingnews.com/wyomingbusinessreport/current_edition/federal-reserve-delays-approval-of-master-accounts-for-wyoming-special-purpose-depository-institutions/article_17cd42c9-6204-5568-a6aa-a5e19b760d9c.html) [https://perma.cc/J363-BGN2]. The provision was removed before the bill’s passage “to avoid friction” with the Federal Reserve. *Id.*

Despite Wyoming's efforts, none of its SPDIs have received Federal Reserve accounts.

By fall 2020, the Wyoming Division of Banking had granted Avanti Financial Group Inc., later renamed Custodia Bank, Inc. ("Custodia"), a SPDI charter.<sup>258</sup> Custodia seeks to provide cryptocurrency custody services for institutional customers like crypto companies, hedge funds, pension funds, and family offices.<sup>259</sup> Its business plan includes providing a "real-time payment settlement solution" for "institutional traders and corporate treasurers."<sup>260</sup> Custodia sees value in "connect[ing] digital assets with the legacy financial system" including the payment services offered through the Federal Reserve.<sup>261</sup> Given the 100% reserve requirement for U.S. dollar deposits held by SPDIs, Custodia did not require FDIC insurance.<sup>262</sup>

Custodia formally began seeking a Federal Reserve account in October 2020.<sup>263</sup> The Kansas City Fed received the complete charter application Custodia had submitted to the Wyoming Division of Banking.<sup>264</sup> The Kansas City Fed also received all the due diligence that the Wyoming regulator conducted as part of

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258. *Avanti Granted Bank Charter and Approval of Business Plan for Digital Asset Custody and Tokenized U.S. Dollar*, *supra* note 242; *Avanti Is Now Custodia, Announces Countdown to Launch in Q2*, CUSTODIA (Feb. 16, 2022), <https://www.custodiabank.com/press/avanti-is-now-custodia-announces-countdown-to-launch-in-q2> [<https://perma.cc/BS6E-3UKC>]. To avoid confusion, I have chosen to use the name Custodia regardless of whether the bank was known as Avanti or Custodia at the time the event occurred.

259. Maria Aspan, *How Caitlin Long Turned Wyoming into Crypto Country*, FORTUNE (July 29, 2021), <https://fortune.com/2021/07/29/caitlin-long-wyoming-crypto/> [<https://perma.cc/P93X-RDB3>]; Penny Crosman, *Avanti Got a Bank Charter. Here's What's Next on Its Agenda*, AM. BANKER (Nov. 5, 2020, 1:30 PM EST), <https://www.americanbanker.com/news/avanti-got-a-bank-charter-heres-whats-next-on-its-agenda>, 2020 WLNR 31586623; Michael del Castillo, *Why a New Breed of Banks Are Renouncing FDIC Insurance*, FORBES (Apr. 16, 2020, 6:00 AM EDT), <https://www.forbes.com/sites/michaeldelcastillo/2020/04/16/caitlin-long-interview-on-why-bitcoin-needs-new-banks/?sh=577a176d362b> [<https://perma.cc/6RU3-ZPPM>].

260. *Avanti Financial Group Announces Accelerated Charter Application*, CUSTODIA (July 23, 2020), <https://www.custodiabank.com/press/bank-charter-application-accepted> [<https://perma.cc/LZ6M-SCHJ>].

261. *Digital Asset Banks*, DIGIT. ASSETS COUNCIL OF FIN. PRO., <https://dacfp.com/yp/digital-asset-banks/> [<https://perma.cc/AP8S-V7N2>]; *see About Us*, CUSTODIA, <https://avantibank.com/about> [<https://perma.cc/NPQ9-Q4TL>].

262. Under Wyoming law, SPDIs are not required to seek deposit insurance, but they may choose to do so. WYO. STAT. ANN. § 13-12-108 (West 2023); Special Purpose Depository Institution Information Security Examination Manual, WYO. DIV. OF BANKING § 1 n.1 (Jan. 2021). Custodia promised "to hold a minimum of \$1.08 in cash and short-term high-quality liquid assets such as T-Bills to back each \$1.00 of customer deposits during its first three years." *Roughstock Wrangling Ideas for Better Banking*, CUSTODIA, <https://custodiabank.com/roughstock/> [<https://perma.cc/Y6AZ-8XDZ>].

263. Kevin Travers, *Avanti, Crypto Banks Shut Out*, LENDIT FINTECH (Nov. 22, 2021), <https://www.lendacademy.com/avanti-crypto-banks-shut-out/> [<https://perma.cc/4KLD-M4E5>]; *Avanti Statement on Its Application to Become a Federal Reserve Bank Member*, CUSTODIA (Aug. 28, 2021), <https://custodiabank.com/press/avanti-statement-on-its-application-to-become-a-federal-reserve-member-bank/> [<https://perma.cc/J27R-NL2Y>] (noting that Custodia "delivered its proposed business plan to the Federal Reserve Bank of Kansas City" on June 22, 2020, prior to receiving its Wyoming charter).

264. Telephone Interview with Christopher Land, former Gen. Couns., Wyo. Div. of Banking (Feb. 9, 2022).

the charter application process.<sup>265</sup> The Federal Reserve did not request any additional information.<sup>266</sup>

Yet Custodia's application languished. After several months, Custodia sought to convince the Kansas City Fed of its commitment to regulatory compliance by applying to become a Federal Reserve member bank.<sup>267</sup> If granted membership, Custodia would have been subject to the Federal Reserve's supervisory authority.<sup>268</sup>

But federal supervision was not the only hold up. Notwithstanding Wyoming's clear law authorizing SPDI's to accept deposits,<sup>269</sup> there was confusion about whether Custodia was a "depository institution" eligible for a Federal Reserve account and ABA routing number. More than a year after receiving a charter, Custodia did not have an ABA routing number.<sup>270</sup> While Custodia's request for a routing number was pending, the ABA provided a statement to Congress critical of Wyoming SPDIs that "urge[d] the Federal Reserve Board to delay granting non-traditional entities like [Wyoming SPDIs] access to master accounts or Reserve Bank payments services."<sup>271</sup> Finally, in early 2022, the ABA issued Custodia's routing number.<sup>272</sup> Neither the Federal Reserve nor the ABA provided a public explanation of this decision, but Custodia says it received a letter from the Kansas City Fed confirming that it "is legally eligible for a master account."<sup>273</sup>

But even with a routing number in place, the Kansas City Fed did not open an account for Custodia. Senator Cynthia Lummis (R-Wyo.) accused the Federal

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265. *See id.*

266. Complaint ¶ 36, *Custodia Bank, Inc., v. Fed. Rsr. Bd.*, No. 22-CV-00125 (D. Wyo. Nov. 11, 2022).

267. *Avanti Statement on Its Application to Become a Federal Reserve Member Bank*, *supra* note 263.

268. 12 U.S.C. § 325 (2018).

269. WYO. STAT. ANN. §13-12-105(b)(ii) (West 2023).

270. *See* Lummis, *supra* note 17; Nick Reynolds, *Wyoming's Crypto Sector's Fate Up to Federal Regulators*, OIL CITY NEWS (Sept. 26, 2021), <https://oilcity.news/community/2021/09/26/wyomings-crypto-sectors-fate-up-to-federal-regulators/> [<https://perma.cc/EA2R-YF2B>] (noting that Kraken's request for a routing number was similarly delayed); *see also supra* notes 91-93 and accompanying text (explaining that financial institutions must be eligible to receive a Federal Reserve account in order to receive an ABA routing number).

271. *Banking Innovation or Regulatory Evasion? Exploring Trends in Financial Institution Charters: Virtual Hearing Before the Subcomm. on Consumer Prot. & Fin. Insts. of the H. Comm. on Fin. Insts.*, 117th Cong. 169 (2021) (statement for the record on behalf of the Am. Bankers Ass'n).

272. Nikhilesh De, *Caitlin Long's Wyoming Crypto Bank Takes a Step Toward Fed Membership*, COINDESK (Feb. 9, 2022, 7:28 PM EST), <https://www.coindesk.com/policy/2022/02/10/caitlin-longs-crypto-bank-takes-a-step-toward-fed-membership/> [<https://perma.cc/BLK7-72NP>]. Kraken also received an ABA routing number. Nikhilesh De, *Kraken Hits Key Milestone in Quest to Gain Fed Account, Equal Treatment with Traditional Banks*, COINDESK (Mar. 28, 2022, 3:42 PM EDT), <https://www.coindesk.com/policy/2022/03/26/kraken-hits-key-milestone-in-quest-to-gain-fed-account-equal-treatment-with-traditional-banks/> [<https://perma.cc/AAW7-F8QN>].

273. Complaint ¶¶ 33, 43, *Custodia Bank, Inc. v. Fed. Rsr. Bd.*, No. 22-CV-00125 (D. Wyo. Nov. 11, 2022); Defendant Fed. Rsr. Bank of Kansas City's Answer ¶¶ 33, 43, *Custodia Bank, Inc. v. Fed. Rsr. Bd.*, No. 22-CV-00125 (D. Wyo. Nov. 11, 2022).



Reserve of “starving [account] applicants until they die.”<sup>274</sup> Sick of waiting, Custodia filed suit against the Kansas City Fed and the Federal Reserve Board requesting that the court issue “an order compelling the Board and/or the Kansas City Fed to promptly decide Custodia’s application for a master account.”<sup>275</sup> Among other things, Custodia argued that the Kansas City Fed had been ready to open Custodia’s account in early 2021, but that the Federal Reserve “Board asserted control over the decision-making process” and then stalled the process.<sup>276</sup>

The Federal Reserve Board, however, denied that it was the functional decisionmaker for Custodia’s account request. The Board filed a preliminary motion asking the court to dismiss Custodia’s case against it because “the Board, a federal agency, does not exercise deposit-taking functions [and is] not an appropriate defendant.”<sup>277</sup> The Board argued that the Reserve Banks, not the Board, are the entities that are statutorily authorized to evaluate account requests and open accounts.<sup>278</sup>

The federal district court declined to dismiss Custodia’s complaint against the Board. It explained that “Custodia has plausibly alleged the Board of Governors has participated in or interfered with the consideration and the decision of Custodia’s master account application.”<sup>279</sup> However, the court emphasized that whether “the Board of Governors in fact inserted itself into the [Kansas City Fed’s] consideration of Custodia’s application” was a matter of fact that would be determined later.<sup>280</sup>

Then, as the parties were preparing for discovery, the Federal Reserve Board announced that it had denied Custodia’s request for Federal Reserve membership.<sup>281</sup> The Board explained that “the firm proposed to engage in novel and untested crypto activities that include issuing a crypto asset on open, public and/or decentralized networks.”<sup>282</sup> The Board concluded that this “novel business model and proposed focus on crypto-assets present[s] significant safety and soundness risks.”<sup>283</sup> The Board also found that “Custodia’s risk management

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274. *Nomination of Jerome H. Powell, of Maryland, to be Chairman of the Board of Governors of the Federal Reserve System: Hearing Before the S. Comm. on Banking, Hous., & Urb. Affs.*, 117th Cong. 33-34 (Jan. 11, 2022) (statement of Sen. Cynthia Lummis).

275. Complaint ¶ 81, *Custodia Bank, Inc. v. Fed. Rsrv. Bd.*, No. 22-CV-00125 (D. Wyo. Nov. 11, 2022).

276. *Id.* ¶¶ 6, 36.

277. Defendant Bd. of Governors of the Fed. Rsrv. Sys.’s Memorandum of Points and Authorities in Support of its Motion to Dismiss at 1, *Custodia Bank, Inc. v. Fed. Rsrv. Bd.*, No. 22-CV-00125 (D. Wyo. Nov. 11, 2022).

278. *Id.*

279. *Custodia Bank, Inc. v. Fed. Rsrv. Bd.*, No. 22-CV-00125 (D. Wyo. Nov. 11, 2022), 2022 WL 16901942, at \*4.

280. *Id.* at \*7.

281. Press Release, Bd. of Governors of the Fed. Rsrv. Sys., *Federal Reserve Board Announces Denial of Application by Custodia Bank, Inc. to Become a Member of the Federal Reserve System* (Jan. 27, 2023), <https://www.federalreserve.gov/newsevents/pressreleases/orders20230127a.htm> [<https://perma.cc/QV44-W9QY>].

282. *Id.*

283. *Id.*

framework was insufficient to address concerns regarding the heightened risks associated with its proposed crypto activities, including its ability to mitigate money laundering and terrorism financing risks.”<sup>284</sup>

The Fed’s denial of Custodia’s membership application was not necessarily dispositive for Custodia’s account request. Depository institutions are eligible for accounts regardless of their membership status. But later that day, a filing in the Custodia lawsuit revealed that the Kansas City Fed had denied Custodia’s account application.<sup>285</sup> Although the court filing said that the Kansas City Fed sent Custodia a letter “providing the basis for that decision,” that letter was not publicly released.<sup>286</sup> Custodia has said that it plans to continue its litigation arguing that the Reserve Banks lack “congressional authority to pick and choose which institutions can have master accounts.”<sup>287</sup>

Perhaps further court proceedings will reveal more information about the Federal Reserve’s handling of Custodia’s application. Until then, we have scant information about why the Federal Reserve denied the account and why it took the Federal Reserve so long to reach a decision. Well before the Federal Reserve announced its decision on Custodia’s account, Chairman Jerome Powell suggested that the Federal Reserve has concerns about the risk that SPDIs as a group pose to the payment system. He explained: “We want to be really careful, because they are hugely precedential . . . . If we start granting these there will be a couple hundred of them pretty quicky, and we have to think about the broader safety and soundness implications.”<sup>288</sup> But he did not further address specific risks.<sup>289</sup> At any rate, if there is a path for Wyoming SPDIs to get Federal Reserve accounts it will not be speedy.

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284. *Id.*

285. Joint Motion of Defendants Fed. Rsrv. Bank of Kansas City & Fed. Rsrv. Bd. of Governors to Dismiss the Complaint as Moot, *Custodia Bank, Inc. v. Fed. Rsrv. Bd.*, No. 22-CV-00125 (D. Wyo. Nov. 11, 2022) (stating that the Kansas City Fed denied Custodia’s account request on Jan. 27, 2023, the same day the Board denied Custodia’s membership application).

286. *Id.* at 1.

287. Campbell, *supra* note 243.

288. *Nomination of Jerome H. Powell, of Maryland, to be Chairman of the Board of Governors of the Federal Reserve System: Hearing Before the S. Comm. on Banking, Housing, & Urban Affairs*, 118th Cong. 34 (statement of Jerome H. Powell, Chair, Bd. of Governors of the Fed. Rsrv. Sys.); *see also* Defendant Bd. of Governors of the Fed. Rsrv. Sys.’s Memorandum of Points and Authorities in Support of its Motion to Dismiss at 2, *Custodia Bank, Inc. v. Fed. Rsrv. Bd.*, No. 22-CV-00125 (D. Wyo. Nov. 11, 2022), 2022 WL 16901942 (describing Custodia’s application as “precedent-setting”).

289. For banking trade groups’ criticisms of the Wyoming SPDI charter, *see Beware the Kraken*, BANK POL’Y INST., 1 (Oct. 21, 2020), <https://bpi.com/wp-content/uploads/2020/10/Beware-the-Kraken.pdf> [<https://perma.cc/KHG3-4NA6>]; *Why a Wyoming Charter is No Hail Mary for the Anti-Fractional Banking Team*, BANK POL’Y INST. (Nov. 6, 2020), <https://bpi.com/wp-content/uploads/2020/11/Why-a-Wyoming-Charter-Is-No-Hail-Mary-for-the-Anti-Fractional-Banking-Team.pdf> [<https://perma.cc/J36C-Y839>]; and *Banking Innovation or Regulatory Evasion? Exploring Trends in Financial Institution Charters: Virtual Hearing Before the Subcomm. on Consumer Prot. & Fin. Insts. of the H. Comm. on Fin. Insts.*, 117th Cong. 166, 168-69 (2021) (statement for the record on behalf of the Am. Bankers Ass’n).

*D. American Samoa's Public Bank*

Not all novel bank account requests have been denied or left in limbo. In 2018, the San Francisco Fed opened an account for the Territorial Bank of American Samoa, a publicly owned bank.<sup>290</sup> But even this successful application raises questions about the lengthy, opaque process and the Federal Reserve Board's role in account opening decisions.

American Samoa is a U.S. territory comprised of an archipelago of Pacific islands located about half-way between Hawaii and Australia.<sup>291</sup> Due to its remote location and property laws,<sup>292</sup> banking has never been plentiful in American Samoa.<sup>293</sup> Banking was so scarce that in 1914, the U.S. Navy (which administered the territory at the time) established the Bank of American Samoa.<sup>294</sup> For many years it was the only bank.<sup>295</sup> It operated as a publicly owned bank<sup>296</sup> until it was purchased by the privately owned Bank of Hawaii in 1969.<sup>297</sup> By the beginning of the twenty-first century, American Samoa had only two deposit-taking banks: Bank of Hawaii and ANZ Amerika Samoa Bank.<sup>298</sup> As an Australian bank with no branches in the continental United States, ANZ's services did not easily allow U.S. payments.<sup>299</sup> In addition, ANZ was not

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290. Sagapolutele, *supra* note 14.

291. *World Factbook: American Samoa*, CENT. INTEL. AGENCY (Sept. 20, 2022), <https://www.cia.gov/the-world-factbook/countries/american-samoa/> [<https://perma.cc/HL79-RUTD>].

292. In American Samoa, only those who are at least one-half Samoan by blood are allowed to own property. AM. SAMOA CODE ANN. § 37.0204(b) (2021). “[O]ver 90 percent of the land is communally owned.” *Community Reinvestment Act Performance Evaluation, Bank of Hawaii*, FED. RSRV. BANK OF S.F. (Aug. 8, 2016). In addition, “[t]here are no written records of any kind indicating land ownership prior to 1900, as there was essentially no ‘government’ that originally owned the land and granted title to private citizens . . . . Because there were no legal descriptions of the property, claims based on oral traditions were very complicated and subject to continuing dispute.” James R. Thornbury, *A Time for Change in the South Pacific*, 67 REV. JUR. U.P.R. 1099, 1101 (1998).

293. See Adrian E. Tschoegl, *Foreign Banks in the Pacific: A Note*, 40 J. PAC. HIST. 223, 233 (2005); Andrew Van Dam, *When Banks Abandoned American Samoa, the Islands Found a Solution Nobody Had Used in a Century*, WASH. POST (May 9, 2018, 7:00 AM EDT), <https://www.washingtonpost.com/news/wonk/wp/2018/05/09/when-banks-abandoned-american-samoa-the-islands-found-a-century-old-solution-that-could-be-the-future-of-finance/> [<https://perma.cc/QRV6-9VR8>].

294. CODIFICATION OF THE REGULATIONS & ORDERS FOR THE GOVERNMENT OF AMERICAN SAMOA § 16 (1921); H. F. BRYAN, AMERICAN SAMOA: A GENERAL REPORT BY THE GOVERNOR 98 (1927).

295. BRYAN, *supra* note 294, at 98; NAVY DEP'T, AMERICAN SAMOA: INFORMATION ON AMERICAN SAMOA TRANSMITTED BY THE UNITED STATES TO THE SECRETARY-GENERAL OF THE UNITED NATIONS PURSUANT TO ARTICLE 73(E) OF THE CHARTER 22 (1947); Tschoegl, *supra* note 293.

296. The Bank of American Samoa was regulated only by the government of American Samoa, the officials of which also largely ran the bank. OREN E. LONG & ERNEST GRUENING, STUDY MISSION TO EASTERN [AMERICAN] SAMOA, S. DOC. NO. 87-38, at 80 (1961).

297. S. REP. NO. 91-996, at 1 (1970).

298. Amerika Samoa Bank was founded in 1979. *Community Reinvestment Act Performance Evaluation, Amerika Samoa Bank*, FED. DEPOSIT INS. CORP. (June 8, 1998) [<https://perma.cc/35UH-EFYK>]. It was purchased by the large Australia and New Zealand Banking Group (ANZ) in 2001. See *Community Reinvestment Act Performance Evaluation, Amerika Samoa Bank*, FED. DEPOSIT INS. CORP., 3 (Jan. 19, 2010) [<https://perma.cc/9NSS-SKLA>]; *Community Reinvestment Act Performance Evaluation, ANZ Guam, Inc.*, FED. DEPOSIT INS. CORP., 1-2 (Aug. 12, 2019) [<https://perma.cc/3294-ZBRG>].

299. *Id.*

equipped to handle payments for the government of American Samoa.<sup>300</sup> Consequently, Bank of Hawaii was the primary financial institution for most people and businesses in American Samoa.<sup>301</sup>

Then, in 2012, Bank of Hawaii announced it was exiting the American Samoa market.<sup>302</sup> This left the Territory scrambling for other ways to connect to U.S. payment systems. A delegation tried to persuade other Hawaiian banks to open a branch in their Territory.<sup>303</sup> Locals tried to start a de novo community bank and a credit union.<sup>304</sup> These efforts were all unsuccessful.<sup>305</sup> The government of American Samoa moved its accounts to Zions Bank, a Utah bank that did not intend to open a local branch.<sup>306</sup>

Perhaps because American Samoa had a history with a government-owned bank, or perhaps because there were no other options, the Territory turned to a public bank.<sup>307</sup> Its leaders knew that getting cooperation from federal banking regulators was going to be difficult. In the wake of the 2008 financial crisis, the FDIC effectively stopped granting deposit insurance for de novo bank charters.<sup>308</sup> In addition, FDIC policy made it clear the agency was less likely to grant insurance to a publicly owned bank than a privately owned one.<sup>309</sup> Rather than pursue federal deposit insurance, the American Samoa government settled on a business model like that of the Bank of North Dakota, the only successful public bank operating in the U.S. at the time.<sup>310</sup> The Bank of North Dakota operates without deposit insurance but has an account and payment services provided by the Minneapolis Fed.<sup>311</sup> Even here though, the precedent was thin.

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300. *Id.* at 3.

301. Blackwell, *supra* note 14.

302. BANK OF HAWAII, ANN. REP. 1 (2012).

303. Dave Segal, *American Samoa Courting Hawaii Bankers*, HONOLULU STAR-ADVERTISER (Dec. 31, 2012), <https://www.staradvertiser.com/2012/12/31/business/american-samoa-courting-hawaii-bankers/> [https://perma.cc/5H97-GDJB].

304. See Fili Sagapolutele, *American Samoa Turns to Internet for Banking*, USA TODAY (Sept. 30, 2013, 9:30 PM ET), <https://www.usatoday.com/story/money/business/2013/09/30/american-samoa-turns-to-internet-for-banking/2899241/> [https://perma.cc/Z4DB-R4GR]; Blackwell, *supra* note 14.

305. Blackwell, *supra* note 14.

306. Dave Segal, *Zions Bank to Take Over Payroll Processing in American Samoa*, HONOLULU STAR-ADVERTISER (Mar. 12, 2013), <https://www.staradvertiser.com/2013/03/12/breaking-news/zions-bank-to-take-over-government-payroll-processing-in-american-samoa/> [https://perma.cc/H2DQ-SVFE]; Sagapolutele, *supra* note 304.

307. See Blackwell, *supra* note 14.

308. David Zaring, *Modernizing the Bank Charter*, 61 WM. & MARY L. REV. 1397, 1399 (2020).

309. Applications for Deposit Insurance, 63 Fed. Reg. 44752, 44760-61 (Aug. 20, 1998); Applications for Deposit Insurance, 62 Fed. Reg. 52869, 52871 (Oct. 9, 1997).

310. See Blackwell, *supra* note 14 (reporting that American Samoa's approach was partly inspired by the Bank of North Dakota); Telephone Interview with Drew Roberts, CEO, Territorial Bank of Am. Samoa (Aug. 28, 2019) (explaining that American Samoa did not immediately apply for deposit insurance because FDIC was not regularly granting insurance applications for de novo banks and the bank organizers believed the FDIC was unlikely to approve insurance for a public bank).

311. *History of BND*, BANK N.D., <https://bnd.nd.gov/history-of-bnd/> [https://perma.cc/6E5W-ZVQA].

The Bank of North Dakota, chartered in 1919, gained its access to Federal Reserve payment services before deposit insurance was ubiquitous.<sup>312</sup>

Nevertheless, American Samoa, with help from a group of Utah-based bank consultants, pushed ahead.<sup>313</sup> In 2015, its legislature, the Fono, approved a charter for the Territorial Bank of American Samoa (TBAS).<sup>314</sup> The Fono also created a new Office of Financial Institutions to supervise and regulate the government-owned bank.<sup>315</sup>

While the Fono could create a bank and a bank regulator, it could not connect that bank to the U.S. payment system. Initially, TBAS planned to rely on correspondent banking services, but TBAS could not find a bank to process its payments.<sup>316</sup> TBAS also had trouble securing an ABA routing number. Although the Fono had clearly authorized TBAS to accept deposits,<sup>317</sup> the ABA asked the San Francisco Fed to confirm that TBAS was eligible to maintain an account.<sup>318</sup> The Federal Reserve, however, did not readily confirm TBAS's eligibility.<sup>319</sup>

In October 2016, TBAS opened without an ABA routing number or Federal Reserve account.<sup>320</sup> Customer demand for accounts was robust.<sup>321</sup> Yet without access to U.S. payment systems, TBAS could not even offer its customers checks.<sup>322</sup>

With deposits pouring in, TBAS set out to convince the Federal Reserve that not only was it eligible to receive an ABA routing number, but it also deserved an account with the San Francisco Fed. Although the San Francisco Fed would operate the account, TBAS's organizers soon found themselves working with the Federal Reserve Board in Washington, D.C.<sup>323</sup> Federal Reserve

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312. The Bank of North Dakota has held an account at the Federal Reserve since at least 1942. See *G.4 State Member Banks of the Federal Reserve*, BD. GOVERNORS FED. RESRV. SYS. 1, 14 (1942), [https://fraser.stlouisfed.org/title/1063/item/40828?start\\_page=15](https://fraser.stlouisfed.org/title/1063/item/40828?start_page=15) [<https://perma.cc/5QQJ-PVVP>].

313. Van Dam, *supra* note 293.

314. AM. SAMOA CODE ANN. § 28.0202 (2021); *Territorial Bank of American Samoa Details Its Origins*, SAMOA NEWS (Sept. 19, 2016, 10:20 AM), <https://www.samoanews.com/local-news/territorial-bank-american-samoa-details-its-origins> [<https://perma.cc/U6ZC-DSAD>].

315. AM. SAMOA CODE ANN. §§ 28.0208, 28.1202 (2021).

316. TBAS planned to use Zions Bank as its correspondent. *Treasurer: Zions Will Only Support ASG Charter Bank*, SAMOA NEWS (Feb. 4, 2015, 2:45 PM), <https://www.samoanews.com/treasurer-zions-will-only-support-asg-charter-bank> [<https://perma.cc/9W9D-BXUS>]. But Zions Bank withdrew its offer to provide the services intimating that its federal regulator, the Office of the Comptroller of the Currency, was concerned about the risk. Telephone Interview with Drew Roberts, *supra* note 310. TBAS contacted about thirty additional banks, but they also declined to provide correspondent banking services. *Id.*

317. AM. SAMOA CODE ANN. § 28.0206(c) (2021) (authorizing TBAS to “engage in all banking and trust company functions, including receiving deposits of money”).

318. Blackwell, *supra* note 14.

319. *Id.* (reporting that TBAS requested an ABA routing number in July 2016).

320. Joyetter Feagaimaalii-Luamanu, *Territorial Bank of American Samoa Opens Its Doors*, PACIFIC ISLAND REP. (Oct. 4, 2015, 2:22 PM), <https://web.archive.org/web/20210819210759/http://www.pireport.org/articles/2016/10/04/territorial-bank-american-samoa-opens-its-doors> [<https://perma.cc/Q56Y-UWMZ>]; Blackwell, *supra* note 14.

321. Blackwell, *supra* note 14.

322. *Id.*

323. *Id.* (reporting that “[t]he Federal Reserve Bank of San Francisco . . . has sent the case to the Federal Reserve Board to review given the unusual circumstances”).

Board General Counsel Scott Alvarez met with TBAS on numerous occasions.<sup>324</sup> He requested that TBAS provide written documents addressing numerous issues. Was TBAS eligible for an account?<sup>325</sup> How would TBAS protect itself from government pressures?<sup>326</sup> Could the newly created Office of Financial Services adequately supervise the bank?<sup>327</sup> How was TBAS different from the Development Bank of Puerto Rico—a public bank that failed while TBAS’s request for a routing number was pending?<sup>328</sup> TBAS organizers did their best to address these and other Federal Reserve concerns.<sup>329</sup> They also emphasized that denying access to the Federal Reserve’s payment systems left thousands of American Samoans, many of whom live in poverty, without access to adequate banking.<sup>330</sup> Still, TBAS seemed to be making little progress.<sup>331</sup>

TBAS’s break came when Randal Quarles was appointed to the Federal Reserve Board. Quarles had previously led the Utah-based Cynosure Group and knew some of TBAS’s Utah-based organizers.<sup>332</sup> Within a month of Quarles’s confirmation, TBAS organizers had met with him in Utah<sup>333</sup> and were on their way to receiving authorization to receive a routing number.<sup>334</sup> TBAS organizers

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324. *Id.*; Telephone Interview with Drew Roberts, *supra* note 310.

325. Telephone Interview with Drew Roberts, *supra* note 310.

326. *American Samoa Bank Struggles to Provide Some Services*, RADIO NEW ZEALAND (Mar. 27, 2017, 1:01 PM), <https://www.rnz.co.nz/international/pacific-news/327556/american-samoa-bank-struggles-to-provide-some-services> [<https://perma.cc/BP64-D4GW>].

327. Telephone Interview with Drew Roberts, *supra* note 310.

328. *Id.*; see also Andrew Scurria, *Puerto Rico Government Development Bank Opts to Liquidate*, WALL ST. J. (Apr. 28, 2017, 12:55 PM ET), [https://www.wsj.com/articles/puerto-rico-government-development-bank-opts-to-liquidate-1493386141?mod=article\\_inline](https://www.wsj.com/articles/puerto-rico-government-development-bank-opts-to-liquidate-1493386141?mod=article_inline) [<https://perma.cc/ZA28-KQB2>] (describing the financial difficulties of the Puerto Rico Development Bank and its decision to liquidate).

329. Telephone Interview with Drew Roberts, *supra* note 310.

330. See *id.* (explaining that TBAS asked the Federal Reserve to consider the importance of access to banking in American Samoa, especially given the Federal Reserve’s responsibilities under the CRA); *Community Reinvestment Act Performance Evaluation: ANZ Guam, Inc.*, FED. DEPOSIT INS. CORP., 16 (Aug. 12, 2019) (“As of the 2010 U.S. Census, the population is 55,519, of which 54.5 percent were below the poverty level and approximately 23.8 percent of the population is unemployed.”).

331. Telephone Interview with Drew Roberts, *supra* note 310.

332. See Van Dam, *supra* note 293 (noting that Quarles came to the Federal Reserve Board “from the Utah-based Cynosure Group”); Telephone Interview with Drew Roberts, *supra* note 310 (describing the consultants’ familiarity with Quarles from their Utah banking experience).

333. See *Bill Will Allow for TBAS Routing Number Says Governor*, TALANEI (Dec. 14, 2017), <https://www.talanei.com/2017/12/14/bill-will-allow-for-tbas-routing-number-says-governor/> [<https://perma.cc/9RW2-LJP2>] (reporting that Governor Lolo Moliga and others met with Randal Quarles in Utah in November 2017); Telephone Interview with Drew Roberts, *supra* note 310 (stating that TBAS organizers met with Quarles within two or three weeks of his confirmation to the Federal Reserve Board).

334. Quarles had one concern for TBAS to address: TBAS had originally been organized in a holding company structure. Fili Sagapolutele, *Two Words in the TBAS Statute Blamed for Stalling the Issuance of a Routing Number*, SAMOA NEWS (Nov. 28, 2017, 12:08 PM), <https://www.samoanews.com/local-news/two-words-tbas-statute-blamed-stalling-issuance-routing-number> [<https://perma.cc/7W5C-KCEB>]; *Bill Will Allow for TBAS Routing Number Says Governor*, *supra* note 333. Quarles was concerned that this brought the holding company within the Bank Holding Company Act, which was not a good fit for a publicly owned bank. Telephone Interview with Drew Roberts, *supra* note 310. To alleviate this concern, the Fono amended the statute to eliminate the holding company. *Bill Will Allow for TBAS Routing Number Says Governor*, *supra* note 333.

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credit Quarles with understanding the need for banking in American Samoa.<sup>335</sup> Ultimately, the Federal Reserve's decision to grant TBAS an account may have been driven more by benefits that TBAS provides to the people of American Samoa, rather than by the risk TBAS presents.<sup>336</sup>

On December 26, 2017, the ABA assigned TBAS a routing number.<sup>337</sup> Shortly thereafter, TBAS learned the San Francisco Fed would open TBAS's account, subject to conditions.<sup>338</sup> TBAS then entered an agreement with the Reserve Bank setting restrictions for its use of the account.<sup>339</sup> Among other things, TBAS agreed to maintain more capital than would be required for an FDIC insured bank.<sup>340</sup> It promised to hold more reserves in its account than would be required under Regulation D.<sup>341</sup> It committed to send the Federal Reserve monthly financial statements.<sup>342</sup> It also agreed to provide regular audit reports, including reports of independent Bank Secrecy Act audits.<sup>343</sup>

On April 7, 2018, more than a year and a half after requesting a routing number, TBAS announced it had opened its account at the San Francisco Fed.<sup>344</sup> TBAS now uses the Federal Reserve for cash services, check clearing, ACH, and wire transfers. TBAS is not allowed to borrow at the discount window.<sup>345</sup> Consumers in American Samoa have access to checking accounts and debit cards.<sup>346</sup>

TBAS's banking supervisor is a one-person shop.<sup>347</sup> No Federal Reserve personnel nor any other federal bank supervisor has ever visited TBAS in

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335. Van Dam, *supra* note 293; Rob Blackwell, *American Samoa Finally Gets a Public Bank*, AM. BANKER (Apr. 30, 2018, 9:45 PM EDT), <https://www.americanbanker.com/news/american-samoa-finally-gets-a-public-bank-and-us-states-are-watching>, 2018 WLNR 13190692.

336. Telephone Interview with Drew Roberts, *supra* note 310 (explaining that he believes the decision to grant the account was driven by concerns about banking access in American Samoa).

337. Fili Sagapolutele, *Routing Number in Place, Now TBAS Works to Set up Master Account*, SAMOA NEWS (Feb. 8, 2018, 11:51 AM), <https://www.samoanews.com/local-news/routing-number-place-now-tbas-works-set-master-account> [<https://perma.cc/YV5P-CHMR>].

338. *Id.*

339. Telephone Interview with Drew Roberts, *supra* note 310. I requested a copy of this agreement from the San Francisco Fed. E-mail from author to Erik Revai, Gen. Couns., Fed. Rsr. Bank of S.F. (June 25, 2019) (on file with author). The Reserve Bank declined to provide it, claiming that although it is not governed by the Freedom of Information Act, any material "describing restrictions or limitations placed on TBAS related to its master account" could be withheld under "Exemption 10 [which] provides that the FRBSF may decline to disclose records contained in statements of account or which reflect entries made to any account maintained at FRBSF." E-mail from Erik Z Revai, Gen. Couns., Fed. Rsr. Bank of S.F. to author (July 24, 2019) (on file with author).

340. Telephone Interview with Drew Roberts, *supra* note 310 (stating that TBAS needs to maintain a capital ratio of between fourteen and sixteen percent).

341. *Id.*; see also 12 C.F.R. § 204.4 (2023) (describing the computation of required reserves).

342. Telephone Interview with Drew Roberts, *supra* note 310.

343. *Id.*

344. Sagapolutele, *supra* note 14.

345. Telephone Interview with Drew Roberts, *supra* note 310.

346. See *Consumer Accounts*, TERRITORIAL BANK OF AM. SAMOA, <https://www.mytbas.com/consumer-accounts#1> [<https://perma.cc/D936-A5FQ>]. *Territorial Bank of American Samoa Introduces TBAS Debit Mastercard*, SAMOA NEWS (Aug. 3, 2020, 2:48 PM), <https://www.samoanews.com/local-news/territorial-bank-american-samoa-introduces-tbas-debit-mastercard> [<https://perma.cc/DTY2-AVXZ>].

347. Telephone Interview with Drew Roberts, *supra* note 310.

American Samoa.<sup>348</sup> The San Francisco Fed manages the risk posed by TBAS remotely by reviewing the information TBAS provides and monitoring TBAS's account activity. TBAS uses its account primarily for clearing. Its number of transactions is relatively low, and the bank seeks to avoid daylight overdrafts.<sup>349</sup>

While TBAS has an account now, if the San Francisco Fed becomes concerned, it might close the account. Moreover, the banking options in American Samoa have become even more limited. In fall 2022, ANZ closed its operations in American Samoa, leaving the Territory without an insured bank.<sup>350</sup> Because TBAS became the only in-person bank option, its deposits ballooned from \$140 million to over \$400 million.<sup>351</sup> Disruption to TBAS operations would leave American Samoa without any banking options. TBAS acknowledges that the current situation is not ideal. It has been exploring options to privatize, to get federal deposit insurance, or to have the government of American Samoa guarantee its deposits.<sup>352</sup> For the time being, however, TBAS must hope that its relationship with the San Francisco Fed remains stable.

#### *E. Fintech Non-Depository Trust*

One bank that lost its Federal Reserve account is The Reserve Trust Company ("Reserve Trust"), a Colorado-chartered non-depository trust company.<sup>353</sup> As the self-described "first fintech trust company with a Federal Reserve master account," it "enable[d] U.S. and international companies to seamlessly move money via the first cloud-based payment system connected directly to the Federal Reserve."<sup>354</sup> Like the previously discussed account requests, Reserve Trust's experience reveals confusion about the account request process and questions about the Federal Reserve Board's role in accountholder risk-vetting.

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348. *Id.*

349. *Id.*

350. *Important Information about ANZ in American Samoa*, ANZ, <https://www.anz.com/americansamoa/en/about-us/important-information-about-anz-in-american-samoa/> [<https://perma.cc/9EE2-L3DP>]; *ANZ to Close American Samoa, Sell Guam Businesses*, ISLANDS BUS. (Apr. 1, 2022), <https://islandsbusiness.com/news-break/an/> [<https://perma.cc/66ZB-SBM8>]; *Community Bank of American Samoa Proposes Buying Territorial Bank of Samoa*, ISLANDS BUS. (June 28, 2022), <https://islandsbusiness.com/news-break/community-bank-of-american-samoa/> [<https://perma.cc/WN7L-8GZQ>].

351. Joyetter Fa'apouli Feagaimaalii, *Frustration Voiced Over Supplement Budget Funds Meant for Manu'a*, SAMOA NEWS (Dec. 8, 2022, 8:57 AM), <https://www.samoanews.com/local-news/frustration-voiced-over-supplemental-budget-funds-meant-manua/> [<https://perma.cc/9YN9-S43Y>].

352. *American Samoa Reveals Plans to Privatise Govt Bank*, RADIO NEW ZEALAND (Mar. 21, 2019, 9:11 AM), <https://www.rnz.co.nz/international/pacific-news/385234/american-samoa-reveals-plans-to-privatise-govt-bank> [<https://perma.cc/SYV6-35P3>]; *Community Bank of American Samoa Proposed Buying Territorial Bank of Samoa*, *supra* note 350; Fili Sagapolutele, *TBAS Board is Proposing Legislation for ASG to Guarantee Deposits*, SAMOA NEWS (Apr. 4, 2022, 7:55 AM), <https://www.samoanews.com/local-news/tbas-board-proposing-legislation-asg-guarantee-deposits> [<https://perma.cc/8GJ3-CZFH>].

353. *Built on Trust*, RSRV. TRUST (Feb. 6, 2022), <https://web.archive.org/web/20220206172925/https://www.reservetrust.com/> [<https://perma.cc/3FAY-X7W6>].

354. *Id.*



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Reserve Trust was born in the aftermath of the 2008 financial crisis. “After the crisis, banks in the U.S. went through a process called derisking, which meant they shed businesses that on a risk-return basis weren’t as strong as other businesses. One of those included the handling of U.S. dollar payments, particularly in emerging countries.”<sup>355</sup> Reserve Trust founders Dennis Gingold and Justin Guilder set out to “build a new type of financial institution that was focused on helping to provide U.S. dollar payment services, especially to emerging fintechs in markets around the world.”<sup>356</sup> On September 27, 2016, Reserve Trust received a non-depository trust company charter from the Colorado Division of Banking.<sup>357</sup> Shortly thereafter, Reserve Trust requested an account from the Kansas City Fed.<sup>358</sup>

After reviewing Reserve Trust’s account request for less than a year, the Kansas City Fed denied it.<sup>359</sup> In later explaining its decision, the Kansas City Fed wrote that Reserve Trust had been legally ineligible for an account “[b]ecause [Reserve Trust] did not meet the definition of a depository institution.”<sup>360</sup> To be a depository institution, a financial institution must accept non-trust deposits.<sup>361</sup> Under Colorado law, only trust companies with FDIC insurance are legally authorized to receive non-trust deposits.<sup>362</sup> But Reserve Trust was not FDIC-insured.<sup>363</sup> This might explain why the Kansas City Fed determined that Reserve Trust was ineligible. Of course, according to Section 13 of the Federal Reserve Act, trust companies are legally eligible to maintain clearing accounts.<sup>364</sup> It is not clear why the Kansas City Fed did not rely on the trust company provision to conclude Reserve Trust was legally eligible.

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355. Mary Ann Azevedo, *Reserve Trust Raises \$30.5M to Become the ‘Stripe for B2B Payments’*, TECHCRUNCH (Aug. 4, 2021, 11:00 AM EDT), <https://tcrn.ch/3C88U5M> [<https://perma.cc/MML2-DEPU>].

356. *Id.*

357. 107 COLO. DIV. OF BANKING ANN. REP. 16 (2016), <https://spl.cde.state.co.us/artemis/regserials/reg21internet/reg212016internet.pdf> [<https://perma.cc/85AH-XXKC>].

358. *Statement*, FED. RSRV. BANK OF KANSAS CITY (Feb. 7, 2022), [https://www.kansascityfed.org/documents/8617/Statement\\_02\\_07\\_2022.pdf](https://www.kansascityfed.org/documents/8617/Statement_02_07_2022.pdf) [<https://perma.cc/EXE6-T2VG>] (stating that Reserve Trust “requested a master account from the Kansas City Fed in September 2016”).

359. *Id.* (stating that Reserve Trust requested an account in September 2016 and the request “was denied in mid-2017”).

360. *Id.*

361. See 12 U.S.C. § 461(b)(1)(A) (2018) (stating that a financial institution is a “depository institution” if it has federal deposit or share insurance, or if it is eligible “to make application to become an insured bank” or credit union); *Statement Regarding Eligibility to Make Application to Become an Insured Bank Under Section 5 of the Federal Deposit Insurance Act*, 45 Fed. Reg. 77517 (Nov. 24, 1980) (stating that a bank is eligible to apply for FDIC insurance if the bank has clear statutory authority to accept non-trust deposits and does in fact accept non-trust deposits).

362. COLO. REV. STAT. § 11-109-201(1)(d) (2022) (stating that trust companies may “[r]eceive and maintain savings deposits, time deposits, and certificates of deposit . . . subject to the restrictions of section 11-109-204”); *id.* § 11-109-24 (stating that “[n]o trust company may accept or hold savings deposits, time deposits, or certificates of deposit pursuant to 11-109-201(1)(d) unless such deposits are insured by the federal deposit insurance corporation”).

363. RSRV. TRUST, *supra* note 353 (stating that its “escrow deposits are not FDIC insured”).

364. 12 U.S.C. § 342 (2018) (noting that trust companies can maintain an account at a Federal Reserve Bank “for the purposes of exchange or of collection”).

In any event, the Kansas City Fed soon changed course. According to the Kansas City Fed: “[a]fter this denial, [Reserve Trust] changed its business model and the Colorado Division of Banking reinterpreted the state’s law in a manner that meant [Reserve Trust] met the definition of a depository institution.”<sup>365</sup> Accordingly, the Kansas City Fed opened Reserve Trust’s account.<sup>366</sup> Reserve Trust founder Dennis Gingold said that “Colorado’s state government had confirmed that the company was ‘authorized to accept deposits that may be federally insured.’”<sup>367</sup> Reserve Trust described itself as receiving “escrow deposits” which were “not time or savings deposits” or “transactional accounts.”<sup>368</sup> But the Colorado Division of Banking says that it had not reinterpreted state law.<sup>369</sup> Again, the Federal Reserve’s opaque process prevents us from effectively evaluating its decision.

Reserve Trust soon began touting the advantages of its Federal Reserve account. Its webpage boasted that as “the first fintech trust company with a Federal Reserve master account,” Reserve Trust “provid[ed] payments services that financial institutions and fintechs have previously only been able to obtain from correspondent and sponsors banks.”<sup>370</sup> Based in part on the value of having a Federal Reserve account, Reserve Trust was able to raise \$30.5 million in Series A financing.<sup>371</sup>

Reserve Trust’s Federal Reserve account did not go unnoticed by other novel banks. People questioned why Reserve Trust, which lacked a federal

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365. *Id.*

366. *Id.*

367. Kate Davidson & Victoria Guida, *Republicans Delay Vote on Biden Fed Nominees, Turning up Heat on Raskin*, POLITICO (Feb. 15, 2022, 12:25 PM EST), <https://www.politico.com/news/2022/02/15/republicans-delay-vote-on-biden-fed-nominees-turning-up-heat-on-raskin-00009016> [<https://perma.cc/S2QQ-9FXU>]; see also Dennis M. Gingold, Opinion, *Fed Nominee Sarah Raskin Did Nothing Wrong*, WALL ST. J. (Feb. 16, 2022, 2:05 PM ET), <https://www.wsj.com/articles/fed-nominee-sarah-bloom-raskin-reserve-trust-banking-regulator-11644879651> [<https://perma.cc/F287-77ZP>].

368. RSRV. TRUST, *supra* note 353.

369. Letter from Kenneth Boldt, State Bank Comm’r, Colo., to the author (Feb. 15, 2022) (on file with author).

We consider the statement that the Division “reinterpreted” state law as a misrepresentation of our practice. The Division regularly receives requests from state-chartered entities to provide clarifications to existing laws based on facts and information we receive from the entity. The analysis of the laws is consistent, while what can change outcomes to our analysis are the facts provided by the entity. We are precluded from providing legal counsel to the entity. Further, the Division does not, nor has the authority to, change, modify or reinterpret any law without engaging in the rulemaking process.

*Id.*

370. RSRV. TRUST, *supra* note 353. Reserve Trust handled both domestic and cross-border payments for its fintech customers. *API Links FinTechs to Fed Payment Rails*, PYMTS (Aug. 9, 2021), <https://www.pymnts.com/digital-first-banking/2021/apis-that-link-to-fed-master-account-poised-to-jump-start-scale-fintech-b2b-payments/> [<https://perma.cc/L6A6-HACM>]; Azevedo, *supra* note 355.

371. Azevedo, *supra* note 355; Amias Gerety, *Why QED Invested in Reserve Trust*, QED INVS. (Aug. 4, 2021), <https://www.qedinvestors.com/blog/why-qed-invested-in-reserve-trust> [<https://perma.cc/EX9N-C94E>].

regulator, received a Federal Reserve account while TNB and Custodia were still waiting for decisions.<sup>372</sup> Some suspected that Reserve Trust received preferential treatment because one of its board members, Sarah Bloom Raskin, had previously served on the Federal Reserve Board.<sup>373</sup> Indeed, after Raskin joined Reserve Trust's board, the Kansas City Fed reversed course and opened Reserve Trust's account.<sup>374</sup> The accusations of corruption came to a head when President Biden nominated Raskin to serve as the Federal Reserve Board's vice chair for supervision.

As part of Raskin's nomination process, members of the Senate Banking Committee questioned whether she had improperly used her Federal Reserve connections to get Reserve Trust an account.<sup>375</sup> Raskin said she did not remember making any calls to the Kansas City Fed on Reserve Trust's behalf.<sup>376</sup> But Reserve Trust founder Dennis Gingold admitted that "Raskin had called the Fed about the master account at his behest, because he was worried that the central bank was not giving the reapplication a fair consideration."<sup>377</sup> He claimed that the call "lasted two minutes and was 'insignificant.'"<sup>378</sup> Raskin ultimately requested that her nomination be withdrawn.<sup>379</sup>

Notwithstanding the congressional scrutiny, it remains unclear what legal and risk analysis the Kansas City Fed completed before opening Reserve Trust's account. Gingold described the Federal Reserve account request process as "opaque" and said that he "does not know what led the Fed to approve the account."<sup>380</sup> Curiously, he also said "that the New York Fed confirmed the dispositive legal conclusions."<sup>381</sup> The Kansas City Fed says that "[a]ll requests for access to a Federal Reserve master account are reviewed to determine legal eligibility, as well as to assess risks posed by an entity's business model to the payment and banking systems."<sup>382</sup> While it assures Congress that it "did not

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372. Letter from James McAndrews to Ann E. Misback, *supra* note 205, at 2; see *Nomination of Sarah Bloom Raskin, of Maryland, to be Vice Chairman for Supervision and a Member of the Board of Governors of the Federal Reserve System: Hearing Before the S. Comm. on Banking, Hous., and Urb. Affs.*, 117th Cong. 28-30 (questioning by Sen. Cynthia Lummis).

373. Jeanna Smilek, Emily Cochrane & Lananh Nguyen, *Skeptical Senators Challenge Biden's Pick for Bank Overseer at the Fed*, N.Y. TIMES, Feb. 4, 2022, at B5.

374. See *id.*; Statement, FED. RSRV. BANK OF KANSAS CITY, *supra* note 358.

375. Smilek *et al.*, *supra* note 373; Alexander Bolton, *Toomey Presses Fed Bank on Whether Raskin Lobbied for Special Access*, THE HILL (Feb. 3, 2022, 5:08 PM ET), <https://thehill.com/homenews/senate/592754-toomey-presses-fed-bank-on-whether-raskin-lobbied-for-special-access/> [<https://perma.cc/CXR4-BFNN>].

376. Jeanna Smialek & Emily Cochrane, *Vote on Biden's Fed Picks Stalls as G.O.P. Boycotts*, N.Y. TIMES, Feb. 16, 2022, at B1.

377. Jeanna Smialek, *Biden's Fed Nominees Frozen as One Faces Questions*, N.Y. TIMES, Mar. 3, 2022, at B4.

378. *Id.*

379. Jeanna Smialek & Emily Cochrane, *Biden Pulls Pick for Fed's Top Bank Regulator*, N.Y. TIMES, Mar. 16, 2022, at B3.

380. *Id.*

381. Gingold, *supra* note 367.

382. Statement, FED. RSRV. BANK OF KANSAS CITY, *supra* note 358.

deviate from its review process in evaluating [Reserve Trust's] request," it has repeatedly declined to further describe that process.<sup>383</sup>

With questions still lingering about Reserve Trust's Federal Reserve account, the Kansas City Fed closed it.<sup>384</sup> According to Senator Pat Toomey (R-Pa.), the Kansas City Fed "determin[ed], among other things, that the company is no longer eligible for one."<sup>385</sup> As a result, Reserve Trust appears to have ceased operations.<sup>386</sup> Although Senator Toomey pressed the Kansas City Fed for further information,<sup>387</sup> his requests were largely fruitless. The Kansas City Fed insists that it "did not depart from a deliberative and thorough analysis of the associated facts and risks" associated with Reserve Trust's account, but it has refused to provide additional information about its process.<sup>388</sup>

#### F. Other Novel Banks

Fourth Corner Credit Union, TNB, Custodia, Territorial Bank of American Samoa, and Reserve Trust are not the only novel banks that have requested Federal Reserve accounts. Kraken, a cryptocurrency exchange with a Wyoming SPDI charter, requested an account more than two years ago, but has not received a decision.<sup>389</sup> Other novel banks do have Federal Reserve accounts. For example, the Bank of North Dakota (an uninsured public bank), has long held a Federal Reserve account and had access to Federal Reserve payment systems.<sup>390</sup> Because the Federal Reserve has not recently provided lists of its accountholders or account applicants, it is difficult to evaluate just how unique the novel banks previously discussed are. This subsection identifies Federal Reserve accountholders with characteristics like the novel banks profiled earlier.

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383. *Id.*

384. Letter from Sen. Pat Toomey, Ranking Member, S. Comm. on Banking, Hous., & Urb. Affs. to Esther George, Pres., Fed. Rsrv. Bank of Kansas City (June 9, 2022), [https://www.banking.senate.gov/imo/media/doc/toomey\\_letter\\_to\\_george\\_on\\_master\\_account\\_revocation.pdf](https://www.banking.senate.gov/imo/media/doc/toomey_letter_to_george_on_master_account_revocation.pdf) [<https://perma.cc/J9X7-8J7L>].

385. *Id.*

386. See Steven T. Dennis, *Toomey Demands Answers From Kansas City Fed on Fintech's Account*, BNN BLOOMBERG (June 9, 2022), <https://www.bnnbloomberg.ca/toomey-demands-answers-from-kansas-city-fed-on-fintech-s-account-1.1776588> [<https://perma.cc/F9US-K7QN>].

387. See Letter from Sen. Pat Toomey to Esther George, *supra* note 384; Kyle Campbell, *The Broad Implications of Pat Toomey's Standoff with K.C. Fed's President*, AM. BANKER (June 19, 2022, 9:00 PM EDT), <https://www.americanbanker.com/news/the-broad-implications-of-pat-toomeys-standoff-with-k-c-feds-president>, 2022 WLNR 19224685.

388. Letter from Esther George, Pres., Fed. Rsrv. Bank of Kansas City to Sen. Patrick Toomey, Ranking Member, Sen. Comm. on Banking, Hous. & Urb. Affs. (June 15, 2022), [https://www.kansascityfed.org/AboutUs/documents/8854/06-16-22\\_Toomey\\_Letter\\_from\\_Esther\\_George.pdf](https://www.kansascityfed.org/AboutUs/documents/8854/06-16-22_Toomey_Letter_from_Esther_George.pdf) [<https://perma.cc/5RL3-29C5>] (claiming that information sought by Senator Toomey was "highly sensitive confidential supervisory information belonging to the Federal Reserve Bank of Kansas City").

389. Lummis, *supra* note 17.

390. See *supra* notes 311-312 and accompanying text.

## 1. Credit Unions Without Federal Insurance

Some credit unions and financial cooperatives have Federal Reserve accounts even though they have no federal deposit insurance and no federal regulator. A minority of states allow their state-chartered credit unions to purchase private share insurance instead of the federal NCUA share insurance.<sup>391</sup> All of these privately insured credit unions (currently 103 in number) are insured by American Share Insurance.<sup>392</sup> Although they have no federal regulator, thirty of these privately insured credit unions are listed in the Federal Reserve's database of Fedwire "participants."<sup>393</sup> Fedwire "participants" must have their own master account.<sup>394</sup> Accordingly, the Fedwire participant database is a partial list of Federal Reserve master account holders.<sup>395</sup>

Similarly, Puerto Rico has credit union-like financial "cooperativas."<sup>396</sup> Their share insurance and supervision are provided by the Public Corporation for the Supervision and Insurance of Cooperatives of Puerto Rico (COSSEC, for its Spanish acronym).<sup>397</sup> Again, although these cooperativas have no federal

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391. Hill, *supra* note 149, at 623 n.129.

392. Stephanie O. Crofton, Luis G. Dopico & James A. Wilcox, *American Share Insurance: The Sole Surviving Private Deposit Insurer in the United States*, 28 *ESSAYS IN ECON. & BUS. HIST.* 27 (2010). Search Page, AM. SHARE INS., [https://www.americanshare.com/cu-financials/\[https://perma.cc/NTW6-EBNB\]](https://www.americanshare.com/cu-financials/[https://perma.cc/NTW6-EBNB]) (choose "All States" from "State" dropdown; then click "Show Matches") (listing 103 credit unions with ASI primary insurance).

393. Comparing the list of privately insured credit unions with the Fedwire participant database yields thirty credit unions: Abbott Laboratories Employees Credit Union (IL), Alliance Credit Union (TX), Beacon Credit Union (IN), Boulder Dam Credit Union (NV), CAHP Credit Union (CA), Christian Community Credit Union (CA), Clark County Credit Union (NV), Firefighters Community Credit Union (OH), Glendale Area Schools Credit Union (CA), Greater Cincinnati Credit Union, Inc., (OH), IH Credit Union, Inc. (OH), IH Credit Union (OH), Interra Credit Union (IN), Kane County Teachers Credit Union (IL), Kemba Indianapolis Credit Union (IN), MC Credit Union (TX), Members Preferred Credit Union (ID), Monterey Credit Union (CA), MyUSA Credit Union (OH), Post Office Credit Union of Maryland, Inc. (MD), Rocky Mountain Credit Union (MT), SafeAmerica Credit Union (CA), San Francisco Fire Credit Union (CA), Services Credit Union (IL), Silver State Schools Credit Union (NV), South Bay Credit Union (CA), Staley Credit Union (IL), Taleris Credit Union, Inc. (OH), TruPartner Credit Union (OH), United Texas Credit Union (TX), and WinSouth Credit Union (AL). *Search for Fedwire Participants*, FED. RSRV., <https://www.frbservices.org/EPaymentsDirectory/searchFedwire.html> [https://perma.cc/WD89-R4H3] [hereinafter *Fedwire Search*]; Search Page, AM. SHARE INS., *supra* note 383.

394. See Collection of Checks and Other Items by Federal Reserve Banks and Funds Transfers Through Fedwire, 86 Fed. Reg. 31376, 31378 (proposed June 11, 2021) (to be codified at 12 C.F.R. § 210) ("[P]articipants in the Fedwire Funds Service are limited to settling their activity over that service in their own master account."); *Fedwire Funds Service Disclosure*, FED. RSRV. FIN. SERVS., 5 (Nov. 28, 2021), <https://www.frbservices.org/binaries/content/assets/crsocms/financial-services/wires/funds-service-disclosure.pdf> [https://perma.cc/4HMY-3MEN] ("Every Fedwire Funds Service participant must maintain a master account at a Reserve Bank.").

395. The Fedwire participant database is only a partial list of master account holders because an institution might have an account but choose not to be a Fedwire participant.

396. P.R. LAWS ANN., tit. 7, §§ 1362, 1363 (2023); see also Tony Budet, *Cooperativas Proudly Serve Their Members*, CREDIT UNION NAT'L ASS'N (Aug. 24, 2022), <https://news.cuna.org/articles/121368-cooperativas-proudly-serve-their-members> [https://perma.cc/J3QM-YWFR] ("Even though cooperativas and credit unions offer similar products and services, their structure, regulator, and insurer are different.").

397. P.R. LAWS ANN., tit. 7, §§ 1334 (2023).

regulator, a few have Federal Reserve accounts.<sup>398</sup> It is not clear whether these credit unions and cooperativas were subject to rigorous risk assessments before their accounts were opened.<sup>399</sup>

## 2. Puerto Rican “Offshore” Banks

Puerto Rico also has International Banking Entities (IBEs) and International Financial Entities (IFEs),<sup>400</sup> some of whom have Federal Reserve accounts even though they have no deposit insurance or federal regulator.<sup>401</sup> Under Puerto Rican law, IBEs and IFEs operate like offshore banks and can provide financial services (including accepting deposits and making loans) to customers outside of Puerto Rico.<sup>402</sup> They are regulated only by Puerto Rico’s Office of the Commissioner of Financial Institutions.<sup>403</sup> The Federal Reserve’s Fedwire participant database lists nine of these institutions, suggesting they have Federal

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398. The Fedwire participants database lists Banco Cooperativo de Puerto Rico, Cooperativa de Ahorro Cr. Arecibo, and Cooperativa de Ahorro Cr. de Camuy. *Fedwire Search*, *supra* note 384; *see also supra* note 394, 5 (explaining that Fedwire participants must have a master account).

399. When the Federal Reserve Board requested comments on proposed account access guidelines, American Share Insurance filed a comment recommending that privately insured credit unions be subject to the same level of scrutiny as NCUA insured credit unions. *See* Letter from Theresa Mason, CEO, Am. Share Ins. to Ann E. Misback, Sec’y, Bd. Of Governors of the Fed. Rsrv. Sys. (May 5, 2022), [https://www.federalreserve.gov/SECRS/2022/May/20220513/OP-1747/OP-1747\\_050522\\_141806\\_329394943489\\_1.pdf](https://www.federalreserve.gov/SECRS/2022/May/20220513/OP-1747/OP-1747_050522_141806_329394943489_1.pdf) [<https://perma.cc/4BC7-CAVR>]. That letter suggests that subjecting privately insured credit unions to greater scrutiny than other account applicants would be a departure from the Federal Reserve’s past practices. *See id.* (“We further would oppose subjecting current account holders to new standards . . .”).

400. P.R. LAWS ANN., tit. 7, §§ 232e, 3087 (2023); *Entidades Bancarias Internacionales*, P.R. OFICINA DEL COMISIONADO DE INSTITUCIONES FINANCIERAS (Mar. 4, 2022), <https://ocif.pr.gov/Consumidores/Lista%20Concesionarios/Entidades%20Bancarias%20Internacionales.pdf> [<https://perma.cc/GNE5-NNF5>] (listing the licensed IBEs); *Entidad Financiera Internacional*, P.R. OFICINA DEL COMISIONADO DE INSTITUCIONES FINANCIERAS (Mar. 4, 2022), <https://ocif.pr.gov/Consumidores/Lista%20Concesionarios/Entidades%20Financieras%20Internacionales.pdf> [<https://perma.cc/9CBM-DXES>] (listing the licensed IFEs).

401. *See, e.g.,* Ileana Fernández-Buitrago & José Sosa-Lloréns, *International Financial Entities in Puerto Rico*, DLA PIPER (Jan. 18, 2017), <https://www.dlapiper.com/en/us/insights/publications/2017/01/international-financial-entities-in-puerto-rico/> [<https://perma.cc/BFU7-4PNZ>] (“The Federal Reserve Bank of New York has opened banking accounts to IFEs.”); *National Money Laundering Risk*, U.S. DEP’T OF THE TREAS., 70 (2022), <https://home.treasury.gov/system/files/136/2022-National-Money-Laundering-Risk-Assessment.pdf> [<https://perma.cc/7K8Q-V5TN>] (explaining the IBEs and IFEs do not have deposit insurance or a federal regulator).

402. *See* P.R. LAWS ANN., tit. 7, §§ 232j, 3091 (2023); *see also* Alejandro A. Santiago Martínez, *Banking in Puerto Rico: Opportunities for International Financial Entities*, 9 NO. 1 P.R. BUS. L. J. 72, 79-83 (2018) (describing the IBE and IFE charters); U.S. DEP’T OF THE TREAS., *supra* note 401 (describing the regulation of IBEs and IFEs).

403. P.R. LAWS ANN., tit. 7, §§ 3081(c), 3082 (2023).

Reserve accounts.<sup>404</sup> Some have publicly confirmed that they have Federal Reserve master accounts.<sup>405</sup>

There are hints that the New York Fed has concerns about the risk Puerto Rico's IBEs and IFEs pose to the payments system. In 2019, the New York Fed temporarily halted approval of new accounts for these entities "in light of recent events, including the expansion of U.S. economic sanctions relating to Venezuela."<sup>406</sup> Reuters reported that at the time, "[s]ixteen of Puerto Rico's 80 offshore banking and financial firms [were] owned by Venezuelan individuals or companies," and "twelve of the sixteen had Fedwire accounts."<sup>407</sup>

More recently, the U.S. Department of the Treasury has noted that the IFEs "present money laundering vulnerabilities to the U.S. financial system . . . because of their offshore banking business model."<sup>408</sup> Treasury also noted that "Puerto Rico has faced an ongoing financial crisis and disruption in the aftermath of Hurricane Maria, complicating efforts for local supervisors to effectively oversee these entities."<sup>409</sup> Notwithstanding these concerns, the New York Fed opened an account for at least one IFE while the Federal Reserve Board was working to finalize its account and service request guidelines.<sup>410</sup>

A cross-border payments consultant describes the process of getting a Federal Reserve account for a Puerto Rican IFE as "elaborate, time consuming

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404. The IFEs are BanPlus International Bank, Inc., Elite International Bank, Inc., Intercam Banco Internacional, Inc., and Stern Bank LLC. Fedwire Search, *supra* note 393; *Entidad Financiera Internacional*, *supra* note 400. The IBEs are BanCaribe International, Banco San Juan Internacional, Inc., Bancredito International Bank & Trust Corporation, and Facebank International Corporation. Fedwire Search, *supra* note 384; *Entidades Bancarias Internacionales*, *supra* note 400.

405. See *Homepage*, ELITE INT'L BANK, <https://eliteinternationalbank.com/> [<https://perma.cc/4UNH-Q5ZE>]; Press Release, Intercam Banco Internacional Inc., Intercam Banco Internacional Inc. Completes Process for Establishing a Master Account with the NYFED (Dec. 9, 2021), <https://www.prnewswire.com/news-releases/intercam-banco-internacional-inc-completes-process-for-establishing-a-master-account-with-the-nyfed-301440770.html> [<https://perma.cc/4D4G-HX8U>]; Stern International Bank, LINKEDIN, <https://www.linkedin.com/company/stern-bank/> [<https://perma.cc/AJ5Z-GRRT>]; *FACEBANK Confirms Position as Solid International Bank Base in Puerto Rico*, WEEKLY J. (Nov. 4, 2021), [https://www.theweeklyjournal.com/business/facebank-confirms-position-as-a-solid-international-bank-based-in-puerto-rico/article\\_09ee6afc-3da2-11ec-b35c-1b9ec2d18abc.html](https://www.theweeklyjournal.com/business/facebank-confirms-position-as-a-solid-international-bank-based-in-puerto-rico/article_09ee6afc-3da2-11ec-b35c-1b9ec2d18abc.html) [<https://perma.cc/UV49-4UZW>].

One IFE, Standard International Bank, claims on its web page that it "maintains a USD master account in the Federal Reserve Bank of New York." *Fedwire Bank License*, STANDARD INT'L BANK, <https://www.standardintbank.com/misc/license> [<https://perma.cc/V3Z7-9667>]. However, it does not currently appear in the Fedwire participants database. Fedwire Search, *supra* note 384.

406. Luc Cohen & Corina Pons, *New York Fed Cracks Down on Puerto Rico Banks Following Venezuela Sanctions*, REUTERS (Apr. 18, 2019, 4:43 PM), <https://reut.rs/2VSHGux> [<https://perma.cc/F3JF-YW6W>].

407. *Id.*

408. U.S. DEP'T OF THE TREAS., *supra* note 401, at 69.

409. *Id.* at 69-70.

410. Press Release, Intercam Banco Internacional Inc., *supra* note 405 (announcing that Intercam's account was opened on August 26, 2021). Intercam's path to a Federal Reserve account may have been long. It received its Puerto Rico charter in 2016. *Id.*

and very slow.”<sup>411</sup> One IFE that provides digital custody services, FV Bank, has requested a Federal Reserve account, but has not yet received one.<sup>412</sup>

### 3. Novel Business Models & Business Structures

If the Federal Reserve Banks subject any bank with a novel business plan or business structure to heightened risk assessments, then the list of banks receiving such scrutiny might be quite long. For example, Utah-chartered industrial banks have commercial owners that are not subject to Federal Reserve oversight under the Bank Holding Company Act.<sup>413</sup> While this structure is controversial and may introduce risk,<sup>414</sup> most industrial banks appear to have Federal Reserve accounts.<sup>415</sup> Some non-depository state and federal trusts have master accounts although they are not depositories.<sup>416</sup> Even banks with standard charters might have abnormal risk profiles. For example, Partner Colorado Credit Union has long handled a sizable amount of marijuana-related business,<sup>417</sup> yet it is a Fedwire participant.<sup>418</sup> And Bank of New York Mellon provides

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411. *International Financial Services Entities*, MOHR.WORLD, <https://mohr.world/international-financial-entities/#> [https://perma.cc/N93Z-DJG4] (“IFE’s may apply for the opening of Bank Accounts with the Federal Reserve Bank of New York but do not think that the process is easy or fast. It may take lots of paperwork and it may take years.”).

412. Miriam Cross, *Bank in Puerto Rico Launches Its Digital Asset Custody Service*, AM. BANKER (Nov. 9, 2022, 6:00 AM EST), <https://www.americanbanker.com/news/bank-in-puerto-rico-launches-its-digital-asset-custody-service>, 2022 WLNR 35901729.

413. UTAH CODE ANN. §§ 7-8-3 to -21 (2018) (allowing industrial banks); 12 U.S.C. § 1841(c)(2)(H) (2018) (excluding industrial banks from the definition of “bank” under the Bank Holding Company Act).

414. See, e.g., Arthur E. Wilmarth, Jr., *Wal-Mart and the Separation of Banking and Commerce*, 39 CONN. L. REV. 1539, 1544 (2007) (explaining the “contagious losses of confidence resulting from problems at their parent companies” could lead to problems at industrial banks); but see Mehrsa Baradaran, *Reconsidering the Separation of Banking and Commerce*, 80 GEO. WASH. L. REV. 385, 426 (2012) (arguing that “Utah industrial banks are among the healthiest banks in the country”).

415. The following Utah industrial banks are listed in the Fedwire participant database: BMW Bank of North America, Inc., Celtic Bank Corporation, Comenity Capital Bank, First Electronic Bank, LCA Bank Corporation, Medallion Bank, Merrick Bank Corporation, Nelnet Bank, Optum Bank, Inc., Sallie Mae Bank, Square Financial Services, Inc., UBS Bank USA, WebBank, and Wex Bank. *Financial Institutions*, UTAH DEP’T OF FIN. INSTS., <https://www.utah.gov/dfi/FinancialInstitutions.html> [https://perma.cc/WC7Q-MEWZ] (providing a list of Utah-chartered industrial banks); *Fedwire Search*, *supra* note 393.

416. For example, ADP Trust Company, NA, an OCC-chartered national trust bank, is listed in the Fedwire participants database. *Financial Institutions List*, OFF. OF THE COMPTROLLER OF THE CURRENCY (Aug. 30, 2022), <https://www.occ.treas.gov/topics/charters-and-licensing/financial-institution-lists/trust-by-name.pdf> [https://perma.cc/5AZY-4DC7] (listing OCC-chartered trust banks); *Fedwire Search*, *supra* note 393. According to one court filing, others in this group include “a credit card processing company and at least one non-depository investment bank.” Brief of Amici Curiae Members of the U.S. Sen. Banking Comm. & U.S. House of Rep. Fin. Svcs. Comm. in Opposition to Defendant’s Motion to Dismiss at 21, *Custodia Bank, Inc. v. Fed. Rsrv. Bd.*, No. 22-CV-00125 (D. Wyo. Nov. 11, 2022).

417. *Partner Colorado Credit Union Launches its First Cannabis Business Lending Program*, COLORADOBIZ (June 26, 2020), <https://www.cobizmag.com/partner-colorado-credit-union-launches-its-first-cannabis-business-lending-program/> [https://perma.cc/YFF6-VZQJ].

418. See *Fedwire Search*, *supra* note 393.



cryptocurrency custody services, even though it also has a master account.<sup>419</sup> It is unclear whether the Federal Reserve Banks have scrutinized any of these novel banks.

#### IV. Procedural Problems

Perhaps the most noticeable feature of the novel banks' Federal Reserve account requests is the lengthiness of the process. Indeed, this concern has been highlighted in all the recent litigation involving Federal Reserve accounts.<sup>420</sup> But procedural questions extend much further and raise fairness concerns about a system that leaves the important decisions beyond the disinfecting sunlight that transparency would provide.

##### A. Application Process

From the very beginning, novel banks seeking Federal Reserve accounts encountered confusion. How should they request an account? Operating Circular 1 says that an account agreement is needed to open an account.<sup>421</sup> Fourth Corner Credit Union reasonably concluded that the account agreement was the application for an account.<sup>422</sup> But this conclusion poses problems for banks, like TBAS and Custodia, for whom the ABA does not promptly grant an ABA routing number.<sup>423</sup> Without a routing number, a bank cannot complete the account agreement.<sup>424</sup> In these instances, it is unclear what the bank should submit to request an account. The New York Fed's Handbook describes an account request process where the agreement is the near final documents to be completed before the account is opened.<sup>425</sup> But for applicants seeking accounts at the other Reserve Banks, it is not apparent how banks should "request" Federal Reserve accounts.

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419. Anna Hrushka, *Fed Disputes Allegations of Favoritism over BNY Mellon Crypto Move*, BANKINGDIVE (Oct. 21, 2022), <https://www.bankingdive.com/news/federal-reserve-favoritism-bny-mellon-crypto-custodia-bank-wyoming/634698/> [<https://perma.cc/XM4T-GYHZ>].

420. TNB USA Inc. v. Fed. Rsrv. Bank of N.Y., No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020), 2020 WL 1445806, at \*3; Complaint, Fourth Corner Credit Union v. Fed. Rsrv. Bank of Kansas City, No. 17-CV-02361 (D. Colo. Sept. 29, 2017); Complaint ¶ 81, Custodia Bank, Inc., v. Fed. Rsrv. Bd., No. 22-CV-00125 (D. Wyo. Nov. 11, 2022).

421. *Operating Circular 1 (2021)*, *supra* note 37, § 2.6.

422. First Amended Complaint ¶¶ 52-58, Fourth Corner Credit Union v. Fed. Rsrv. Bank of Kansas City, 154 F. Supp. 3d 1185 (D. Colo. 2016) (No. 15-CV-01633) (explaining that Fourth Corner submitted its Account Agreement immediately upon receiving an unconditional credit union charter from Colorado).

423. *See supra* notes 317-319, 334, 263-265, 270-273, and accompanying text.

424. *Operating Circular 1 app. 1 (2021)*, *supra* note 12.

425. *N.Y. Fed Handbook*, *supra* note 114, at 3-5; *N.Y. Fed Terms & Conditions*, *supra* note 115, § 2.6.1. The Handbook is consistent with the New York Fed's handling of TNB's application. TNB submitted its account agreement more than a year after beginning talks with the New York Fed because the New York Fed recommended waiting until the due diligence stage of the process was completed. TNB USA Inc. v. Fed. Rsrv. Bank of NY, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020), 2020 WL 1445806, at \*3-\*5.

The requesting novel banks were also confused about what, if any, materials should be submitted. For example, Fourth Corner Credit Union submitted the account agreement, a board resolution, and a document with signatures of credit union personnel authorized to access the account.<sup>426</sup> But Custodia submitted a business plan and the materials that it provided Wyoming when seeking the SPDI charter.<sup>427</sup> In some cases, the Reserve Bank requested additional information,<sup>428</sup> while in other cases it has not.<sup>429</sup>

The procedural confusion continues after a bank makes an account request. What is happening? Is the Reserve Bank waiting for the applicant to provide further information, deciding whether the applicant is legally eligible, or evaluating the risk presented by the proposed account? For example, the Federal Reserve seems to have delayed confirming that TBAS and Custodia were eligible for a master accounts and ABA routing numbers, even though the banks fit the eligibility category of depository institution.<sup>430</sup> In other instances (Fourth Corner and TNB), the Reserve Bank seems to have reconsidered the issue of legal eligibility even after the ABA routing number had been issued.<sup>431</sup>

Sometimes, the Federal Reserve Board seems to have realized, after applications, that its existing policies and procedures were insufficient to address those applications. While the TNB and Custodia applications were pending, the Board offered proposals with long notice and comment periods that appear to be at least partially sparked by the applications.<sup>432</sup>

The lack of formal process leaves the impression that the Federal Reserve is inventing its review procedures as it goes along. The lack of formal process also opens the Federal Reserve to the criticism that it is deliberately delaying account requests instead of denying them. Unsurprisingly, three novel banks have complained to courts about delays.

### *B. The Board's Role*

The novel bank account requests show that although the Reserve Banks maintain accounts, the Federal Reserve Board sometimes exerts significant influence over account requests. The Territorial Bank of American Samoa attributes its Federal Reserve account to a meeting with a member of the Federal Reserve Board.<sup>433</sup> The New York Fed ascribes its delay on TNB's narrow bank

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426. See *supra* notes 158-164, 181-185, and accompanying text.

427. See *supra* notes 263-265 and accompanying text.

428. See *supra* notes 185-187 (Fourth Corner), 220 (TNB), 325-329 (TBAS), and accompanying text. Reserve Trust's application suggests there is legal confusion over which financial institutions are legally eligible for Federal Reserve accounts. See *supra* notes 359-369 and accompanying text. The Federal Reserve Board recently considered "whether it may be useful to clarify the interpretation of legal eligibility under the Federal Reserve Act," but decided it was "not necessary to do so at this time." Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. 51099, 51103 (Aug. 19, 2022).

429. See *supra* note 266 and accompanying text (Custodia).

430. See *supra* notes 269-273 (Custodia), 317-319 (TBAS), and accompanying text.

431. See *supra* notes 156 (Fourth Corner), 235-236 (TNB), and accompanying text.

432. See *supra* notes 232-233 and accompanying text and *infra* note 463 and accompanying text.

433. See *supra* notes 332-335 and accompanying text.

application to Board concerns.<sup>434</sup> Custodia alleges that “the Kansas City Fed’s consideration and impending approval of Custodia’s application was derailed when, in Spring 2021, the Board asserted control over the decision-making process.”<sup>435</sup> Board Chairman Jerome Powell seemed to acknowledge that the Board was evaluating the Wyoming SPDI applications.<sup>436</sup> And when Fourth Corner Credit Union and TNB sued, the Federal Reserve Board weighed in as *amicus curiae*.<sup>437</sup>

Yet the Board downplays its large and sometimes pivotal role in account requests. Instead, it shifts responsibility for decisions to the Reserve Banks, who it claims are not bound by laws that might constrain the Board.<sup>438</sup> For example, 12 U.S.C. § 4807 requires that federal banking agencies act on applications within one year.<sup>439</sup> The Board argues this deadline is inapplicable because master account applications are made to the Reserve Banks rather than the Board.<sup>440</sup> Similarly, the Administrative Procedure Act (APA) allows courts to “compel agency action unlawfully withheld or unreasonably delayed.”<sup>441</sup> Again, the Board argues that because “Congress did not task the Board with final decisionmaking authority in this matter,” the APA does not provide redress for applicants.<sup>442</sup> Under the Board’s interpretation, the Board could, in its supervisory capacity, delay decisions on master accounts without legal consequence. Extending that same reasoning might insulate the Board from judicial scrutiny of a decision even when the Board’s decision compelled the conclusion reached by a Reserve Bank.<sup>443</sup>

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434. See *supra* notes 226-229 and accompanying text.

435. Complaint ¶ 6, *Custodia Bank, Inc. v. Fed. Rsr. Bd.*, No. 22-CV-00125 (D. Wyo. Nov. 11, 2022).

436. See *supra* note 288 and accompanying text.

437. Memorandum of Law of Amicus Curiae the Bd. of Governors of the Fed. Rsr. in Support of Defendant the Fed. Rsr. Bank of N.Y.’s Motion to Dismiss, *TNB USA v. Fed. Rsr. Bank of N.Y.*, No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020).

438. See Defendant Bd. of Governors of the Fed. Rsr. Sys.’s Memorandum of Points and Authorities in Support of its Motion to Dismiss at 2, *Custodia Bank, Inc. v. Fed. Rsr. Bd.*, No. 22-CV-00125 (D. Wyo. Nov. 11, 2022) (“Although the Board published guidance and exercised general supervisory authority over Reserve Banks, it has not been tasked with deciding individual master account requests. Rather, Congress chose to vest that authority directly in the Reserve Banks . . .”).

439. 12 U.S.C. § 4807(a) (2018) (“Each Federal banking agency shall take final action on any application to the agency before the end of the 1-year period beginning on the date on which a completed application is received by the agency.”).

440. Defendant Bd. of Governors of the Fed. Rsr. Sys.’s Memorandum of Points and Authorities in Support of its Motion to Dismiss at 10-11, *Custodia Bank, Inc. v. Fed. Rsr. Bd.*, No. 22-CV-00125 (D. Wyo. Nov. 11, 2022).

441. 5 U.S.C. § 706(1) (2018).

442. Defendant Bd. of Governors of the Fed. Rsr. Sys.’s Memorandum of Points and Authorities in Support of its Motion to Dismiss at 12-13, *Custodia Bank, Inc. v. Fed. Rsr. Bd.*, No. 22-CV-00125 (D. Wyo. Nov. 11, 2022).

443. The APA allows courts to set aside agency actions that are “arbitrary, capricious, and abuse of discretion, or otherwise not in accordance with law.” 5 U.S.C. § 706(2)(A) (2018). In general, the Board’s regulatory and supervisory actions are subject to the APA. See Daniel K. Tarullo, *Bank Supervision and Administrative Law*, 2022 COLUM. BUS. L. REV. 279, 315-16 (2022) (arguing that some subset of supervisory actions should be beyond APA review). In litigation with Custodia, the Kansas City Fed argues that, unlike the Board, Reserve Banks are not government “agencies” subject to APA

The Board also downplays its role to deflect questions about whether account applications are handled fairly and consistently. When the Board receives requests for documents related to master account applications, it withholds them. For example, when the Board received a Freedom of Information Act request for information regarding Reserve Trust's account, the Board withheld the documents, claiming they "consist of predecisional and deliberative information regarding Reserve Trust's efforts to acquire a master account."<sup>444</sup> If every account decision is deemed to be made by the Federal Reserve Banks rather than the Board, then the Federal Reserve can always withhold information claiming it is "predecisional," even when its supervisory input effectively controls the Reserve Bank decision. This is not consistent with the intent of the Freedom of Information Act. FOIA was intended to provide access to government decisions.<sup>445</sup> In at least some cases, it appears that the Reserve Board, a government agency, is making decisions.

### C. Consistency & Transparency

Novel bank account requests reveal consistency concerns driven partly by a lack of standards and partly by a dearth of transparency. Consider the novel bank arguments: Fourth Corner Credit Union argued that many existing banks were allowed to serve the state-legal marijuana industry without losing access to Federal Reserve accounts or payment services.<sup>446</sup> The Territorial Bank of American Samoa argued that the public Bank of North Dakota had access to a Federal Reserve account and payments for decades without incident.<sup>447</sup> TNB argued its business model was no riskier than the Puerto Rican IFEs.<sup>448</sup> Custodia argues that the Federal Reserve allows other banks to offer cryptocurrency custody services while preventing Custodia from doing the same.<sup>449</sup> And

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constraints. Defendant Fed. Rsr. Bank of Kansas City's Memorandum of Points and Authorities in Support of Its Motion to Dismiss at 13-15, *Custodia Bank, Inc. v. Fed. Rsr. Bd.*, No. 22-CV-00125 (D. Wyo. Nov. 11, 2022). Thus, the Board is pushing responsibility for its decisions to an entity that claims to be beyond procedural constraints and judicial review.

Whether the Kansas City Fed is subject to the APA is unsettled. The Kansas City Fed does not cite any cases so holding. *Id.* Moreover, some courts have held that Reserve Banks are subject to the APA because they act as instrumentalities of the federal government. *Flight Int'l Grp., Inc. v. Fed. Rsr. Bank of Chi.*, 583 F. Supp. 674, 678 (N.D. Ga. 1984), *vacated*, 597 F. Supp. 462 (N.D. Ga. 1984); *Lee Constr. Co. v. Fed. Rsr. Bank of Richmond*, 558 F. Supp. 165, 175 (D. Md. 1982).

444. Letter from Margaret McCloskey Shanks, Deputy Sec'y, Bd. of Governors of the Fed. Rsr. Sys., to Thomas Jones, Pres., Am. Accountability Found. (July 29, 2022) (on file with author) (withholding twelve pages of responsive document under the Freedom of Information Act).

445. See H.R. Rep. No. 89-1497, at 5 (1966), *as reprinted in* 1966 U.S.C.A.N. 2418, 2422 (explaining that FOIA was drafted because at the time there was no law recognizing "the basic right of any person . . . to gain access to records of official Government actions").

446. First Amended Complaint ¶ 33, *Fourth Corner Credit Union v. Fed. Rsr. Bank of Kansas City*, 154 F. Supp. 3d 1185 (D. Colo. 2016) (No. 15-CV-01633).

447. See *supra* notes 310-312 and accompanying text.

448. Letter from James McAndrews to Ann E. Misback, *supra* note 205, at 2-3.

449. Kyle Campbell, *Fed, Custodia Clash Over Discovery Requirements in Master Account Lawsuit*, AM. BANKER (Dec. 5, 2022, 1:48 PM EST), <https://www.americanbanker.com/news/fed->

consistency questions (and allegations of corruption), spilled out into newspapers and a congressional hearing when Reserve Trust, a fintech company without a federal regulator, received a Federal Reserve account but the requests of TNB and Custodia languished.<sup>450</sup>

Inconsistent access to Federal Reserve accounts is harmful. If some Reserve Banks are more permissive than others, it could lead to forum shopping and consolidate risk at the more permissive Reserve Banks.<sup>451</sup> It is unfair to state legislatures and state bank supervisors who cannot control which Reserve Bank’s district they are located within.<sup>452</sup> Inconsistency undermines predictability in outcomes, raising costs for novel bank applicants.<sup>453</sup> It raises questions about whether the Federal Reserve is adequately complying with its statutory mandate to treat member and nonmember banks alike when establishing terms and conditions.<sup>454</sup> Ultimately, inconsistency invites speculation about “improper motives . . . or discriminatory bias in favor or against some” applicants,<sup>455</sup> potentially eroding faith in the Federal Reserve.

From the novel account requests discussed in Part III, it is difficult to determine whether the Federal Reserve Banks are reaching inconsistent conclusions. Unless a novel bank discloses its request for an account, the public may never learn about it. Currently, the Federal Reserve does not provide a list of its accountholders. Those novel banks discussed in this Article are probably only a small subset of novel bank account requests.

There are, however, reasons to worry that the district Federal Reserve Banks have different risk tolerances when evaluating account and services requests. First, although each of the Reserve Banks seemed concerned about the risk associated with each account request, there are no standards to ensure that the Reserve Banks have similar risk preferences. Without standards, there is little to constrain the discretion that the Reserve Banks claim.

Second, there is evidence that in the past, Reserve Banks had different risk tolerances with respect to accounts. Before the passage of the Monetary Control Act, some Reserve Banks liberally opened limited purpose clearing accounts,

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custodia-clash-over-discovery-requirements-in-master-account-lawsuit, 2022 WLNR 39230216 (stating that the Federal Reserve was “applying a staggering double-standard” by allowing Bank of New York Mellon and Farmington State Bank (also known as Moonstone Bank) to provide crypto custody services).

450. See *supra* notes 372-375 and accompanying text.

451. Cf. Proposed Guidelines for Evaluating Account and Services Requests, 86 Fed. Reg. 25865, 25866 (May 11, 2021) (noting the possibility “for forum shopping across Reserve Banks”).

452. See *Operating Circular 1* (2021), *supra* note 37, § 2.2.

453. See Yoav Dotan, *Making Consistency Consistent*, 57 ADMIN. L. REV. 995, 1000 (2005) (noting that consistency “preserves the coherence and predictability of the process of decisionmaking”).

454. 12 U.S.C. § 248a(c)(2) (2018).

455. Dotan, *supra* note 453, at 1000; see also Press Release, Sen. Cynthia Lummis, Lummis Presses Fed Nominee Raskin Over Suspicious Influence Peddling (Feb. 3, 2022), <https://www.lummis.senate.gov/press-releases/lummis-presses-fed-nominee-raskin-over-suspicious-influence-peddling/> [https://perma.cc/GFU7-LC5J] (describing an account access decision as “suspicious” after perceived inconsistent treatment of a fintech applicant for a Federal Reserve account).

while other Reserve Banks refused to open any.<sup>456</sup> More recently, Thomas Hoenig, the President of the Kansas City Fed from 1991 to 2011, said that he believes district Reserve Banks have different risk tolerances.<sup>457</sup>

Third, there appear to be no formal procedures, like information sharing or appeals, that would promote consistent decisions across Reserve Banks. Although the New York Fed may have weighed in on the Reserve Trust account at the Kansas City Fed,<sup>458</sup> it is not clear what role it played in the decision. Moreover, the Reserve Banks have resisted the idea that past decisions create precedent. In granting Fourth Corner Credit Union conditional access to a Federal Reserve account, the Kansas City Fed expressly noted that the letter was not intended to create precedent.<sup>459</sup> Without coordination or respect for precedent, there is no reason to expect that decisions reached without any clear standards would be consistent.

Fourth, when the Federal Reserve Board proposed guidelines for evaluating account and services requests, it billed them as “a more transparent and consistent approach.”<sup>460</sup> There would be no need for guidelines to “promote consistent outcomes across Reserve Banks and to facilitate equitable treatment across institutions”<sup>461</sup> if the Federal Reserve’s existing practices ensured consistency.

Part V examines the Account Access Guidelines that emerged from the 2021 proposal and explains why they do not solve the consistency and transparency issues they were designed to address.

## V. Federal Reserve Board Guidelines

On May 5, 2021, with novel account requests pending, the Federal Reserve Board began a process for adopting Guidelines for Evaluating Account and Services Requests (Account Access Guidelines).<sup>462</sup> What emerged more than a

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456. See Letter X-9187 from Chester Morrill, Sec’y, Fed. Rsrv. Bd., to E.M. Stevens, Chairman, Fed. Rsrv. Bank of Chi., encl. 6, 364, 372 (Apr. 26, 1935), <https://fraser.stlouisfed.org/archival/4957/item/505912> [<https://perma.cc/UGY2-EAP7>] (summarizing each Reserve Bank’s approach to clearing accounts); *Clearing Accounts Allow Access to Service*, DALLASFED ROUNDUP, Jan. 1983, at 3, [https://fraser.stlouisfed.org/title/6376/item/608616/toc/599385?start\\_page=3](https://fraser.stlouisfed.org/title/6376/item/608616/toc/599385?start_page=3) [<https://perma.cc/W4HB-HDFM>] (explaining that prior to 1983 “[p]rocedures for offering [clearing] . . . accounts had varied widely among the Reserve Banks, with some allowing accounts only for institutions that have zero or small reserve balances and others allowing accounts for some larger banks as well”).

457. Telephone Interview with Thomas Hoenig, *supra* note 11.

458. Gingold, *supra* note 367.

459. See *supra* note 191 and accompanying text. Notwithstanding this aversion to precedent, the Federal Reserve Board claims its long scrutiny of Custodia’s account application was warranted because the application is “precedent-setting.” See *supra* note 288 and accompanying text.

460. Proposed Guidelines for Evaluating Account and Services Requests, 86 Fed. Reg. 25865, 25866 (May 11, 2021).

461. *Id.* at 25867.

462. *Id.* at 25865. The Board issued a request for additional comments in early 2022. Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. 12957 (Mar. 8, 2022). Custodia and Kraken had requested access in 2020. Lummis, *supra* note 17. TNB’s account request was also pending. See *supra* note 240 and accompanying text. It seems likely that Intercam Banco Internacional Inc.’s request for an account was pending. See *supra* note 410.

year later was a document directing Reserve Banks to consider a variety of risks when evaluating requests.<sup>463</sup> The Guidelines also confirm that requests from institutions without federal oversight will be more closely scrutinized.<sup>464</sup> The Federal Reserve Board, however, left unresolved many of the procedural defects apparent from the recent novel bank requests.

#### A. Account Guidelines

The Board explained that it developed the Account Access Guidelines because payment technology is rapidly evolving and “novel charter types [are being] authorized or considered by federal and state banking authorities across the country.”<sup>465</sup> As a result, “the Reserve Banks are receiving an increasing number of inquiries and access requests from institutions that have obtained, or are considering obtaining, such novel charter types.”<sup>466</sup> “Given the increase in the number and novelty of such inquiries,” the Board decided that “a more transparent and consistent approach to such requests should be adopted by the Reserve Banks.”<sup>467</sup>

The Board did not create its Guidelines from whole cloth. Instead, it “sought to incorporate as much as possible existing Reserve Bank risk management practices.”<sup>468</sup> “[T]he Board views the final Account Access Guidelines as an evolution of existing practices rather than the creation of ‘new standards.’”<sup>469</sup>

The Guidelines have two sections. The first contains a list of risk management principles that seem collected from risks identified in previous novel bank requests. Those principles are:

- Accountholders should be legally eligible for an account and “should have a well-founded, clear, transparent, and enforceable legal basis for its operations.”
- Accountholders “should not present or create undue credit, operational, settlement, cyber or other risks to the Reserve Bank.”
- Accountholders should not “present or create undue . . . risks to the overall payment system.”
- Accountholders “should not create undue risk to the stability of the U.S. financial system.”
- Accountholders “should not create undue risk to the overall economy by facilitating activities such as money laundering, terrorism financing,

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463. Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. 51099 (Aug. 19, 2022).

464. *Id.*

465. *Id.* at 51099.

466. *Id.*

467. Proposed Guidelines for Evaluating Account and Services Requests, 86 Fed. Reg. 25865 (May 11, 2021).

468. Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. at 51099 n.3.

469. *Id.* at 51106.

fraud, cybercrimes, economic or trade sanctions violations, or other illicit activity.”

- “Provision of an account and services to an institution should not adversely affect the Federal Reserve’s ability to implement monetary policy.”<sup>470</sup>

Within each risk principle, the Guidelines prompt the Reserve Banks to consider an applicant’s financial condition, internal controls, policies, procedures, risk assessments, systems security measures, management expertise, governance arrangements, training programs, and more.<sup>471</sup> The Guidelines instruct Reserve Banks to review risk assessments already performed by an institution’s federal and state supervisors when conducting their own “independent analysis” of each applicant’s risks.<sup>472</sup>

The second section of the Account Access Guidelines is a “three-tier framework” where some requests for access receive greater scrutiny than others.<sup>473</sup> Tier 1 federally insured financial institutions will “generally be subject to a less intensive and more streamlined review.”<sup>474</sup> Next are the Tier 2 institutions that do not have federal insurance but do have a federal supervisor. Tier 2 institutions include: (1) OCC-chartered institutions without deposit insurance like institutions with a national trust bank charter, (2) state-chartered financial institutions without federal insurance that are members of the Federal Reserve System, and (3) Edge and Agreement Corporation and U.S. branches of foreign banks.<sup>475</sup> For an institution with a holding company to be evaluated as a Tier 2 institution, the institution’s holding company must be subject by statute or commitment to oversight by the Federal Reserve.<sup>476</sup> Tier 2 institutions receive an “intermediate level of review.”<sup>477</sup> Tier 3 institutions are those that are not federally insured and do not meet the requirements to be considered Tier 2 institutions.<sup>478</sup> They “will generally receive the strictest level of review.”<sup>479</sup> When an account or payment access request may pose risks to the U.S. financial system or may adversely impact the Federal Reserve’s ability to implement monetary policy, a Reserve Bank should assess the risk “in coordination with other Reserve Banks and the Board.”<sup>480</sup>

Under the Account Access Guidelines, nearly all the novel banks discussed in Part III would be considered Tier 3 institutions subject to strict review. Fourth Corner Credit Union, TNB, the Territorial Bank of American Samoa, Reserve

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470. *Id.* at 51107-09.

471. *Id.*

472. *Id.* at 51106.

473. *Id.* at 51109-10.

474. *Id.* at 51109.

475. *Id.* at 51109-10.

476. *Id.*

477. *Id.* at 51110.

478. *Id.*

479. *Id.*

480. *Id.* at 51108-09.



Trust, privately insured credit unions, cooperativas, and Puerto Rican offshore banks all lack federal deposit insurance and do not have a federal supervisor. The Guidelines seem to formalize the lengthy vetting process that Fourth Corner, TNB, and TBAS encountered. The Guidelines do, however, suggest an alternative path. A Tier 3 institution's request for an account might be viewed more favorably if the institution became a member of the Federal Reserve and subject to the Federal Reserve's supervision.<sup>481</sup>

Finally, the Guidelines emphasize the Reserve Banks' discretion in considering account requests. Indeed, the Board labels the process to get an account as an "account request" rather than "an application."<sup>482</sup> For those that did not get the hint, the Board stresses: "[I]t is important to make clear that legal eligibility does not bestow a right to obtain an account and services."<sup>483</sup> Moreover, "[i]f the Reserve Bank decides to grant an access request, it may impose (at the time of account opening, granting access to service, or any time thereafter) obligations relating to, or conditions or limitation on, use of the account or services as necessary to limit operational, credit, legal or other risks . . . ."<sup>484</sup>

### B. Improvements

The Federal Reserve Board's Account Access Guidelines improve the procedural landscape in some ways. First, by identifying specific risks,<sup>485</sup> the Guidelines give account applicants better notice of the types of information the Federal Reserve Banks may seek as part of the application process. Second, the Guidelines clarify that Reserve Banks should consider the assessments already performed by other federal and state supervisors.<sup>486</sup> Before the Guidelines, it was not clear that Reserve Banks would consider the work of state supervisory authorities. Third, the Guidelines publicly acknowledge that the Board would like the account access decisions to be consistent among the Federal Reserve Banks.<sup>487</sup> Before the Guidelines, the Federal Reserve's repeated insistence that the Reserve Banks have discretion in opening accounts<sup>488</sup> may have been taken as an indication that the Board did not care whether that discretion resulted in different approaches across Federal Reserve Banks.

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481. The Wyoming SPDI Custodia applied for Federal Reserve membership. *Avanti Statement on Its Application to Become a Federal Reserve Bank Member*, CUSTODIA, *supra* note 263. If it had been granted membership, it may have been treated as a Tier 2 institution. However, the Federal Reserve denied its membership application. *See supra* notes 281-284 and accompanying text.

482. Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. at 51106-10.

483. *Id.* at 51106.

484. *Id.*

485. *Id.* at 51106-09.

486. *Id.* at 51107-09.

487. *Id.* at 51106.

488. *See supra* notes 80, 133, 162, and accompanying text.

*C. Remaining Problems*

Still, the Account Access Guidelines stop short of solving the most pressing problems evident in novel bank account requests. In some cases, the Federal Reserve Board explicitly rejected suggestions that would have improved the procedural landscape.

First, although the Guidelines set up a risk-vetting process, the Guidelines do not explain how the account application process works. How should an applicant request an account? What information should an applicant submit? Are there expected timelines for the Reserve Bank to request follow-up information and for the applicant to respond? Will the Reserve Bank notify the applicant when the account request is deemed complete? How long does the Federal Reserve expect the evaluation process will take? Is there an appeal process if the Federal Reserve Bank reaches an unfavorable decision?

The Federal Reserve Board says that the “Reserve Banks are working together, in consultation with the Board, to expeditiously develop an implementation plan for the final Guidelines.”<sup>489</sup> It did not explain what the implementation plan will entail or whether the plan will be public. Perhaps the Reserve Banks will choose to update Operating Circular 1. Perhaps they will choose to adopt a handbook like the one currently used by the New York Fed. And perhaps the implementation plan will answer many of the remaining procedural questions.

But the Guidelines themselves suggest that some problems will persist. First, the slow process is likely to continue. In responding to the Board’s proposed Guidelines, “many commentators recommended that the Board establish timelines within which Reserve Banks must grant or deny requests.”<sup>490</sup> The Board rejected these recommendations, explaining that “[s]etting a specific timeline could result in an increased number of premature or unnecessary denials of access requests in cases where the specified timeline does not allow the Reserve Banks sufficient time to understand the intricacies of the requesting institutions’ risk profiles.”<sup>491</sup> Moreover, Federal Reserve Governor Michelle Bowman warned that the adoption of Guidelines did not mean that account applications would be handled more expeditiously.<sup>492</sup>

Second, the Guidelines leave the Board’s role in the process ambiguous. Reserve Banks are to make account access decisions in “consultation” with the

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489. Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. at 51101; *see also* Press Release, Bd. of Governors of the Fed. Rsrv. Sys., Statement on Guidelines to Evaluate Requests for Accounts and Services at Federal Reserve Banks by Governor Michelle W. Bowman (Aug. 15, 2022), <https://www.federalreserve.gov/newsevents/pressreleases/bowman-statement-20220815.htm> [<https://perma.cc/7QX6-B9H7>] [hereinafter Bowman Statement] (“More work remains to be completed before a process is established to fully implement the guidelines.”).

490. Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. at 51102.

491. *Id.* at 51103.

492. Bowman Statement, *supra* note 489 (“There is a risk that this publication could set the expectation that reviews will now be completed on an accelerated timeline.”).

Board and other Reserve Banks.<sup>493</sup> The Board explains that its role is to provide “oversight,” but the Reserve Banks have “discretion in decision making.”<sup>494</sup> This matches the Board’s pronouncements prior to the Guidelines.<sup>495</sup> As the novel bank applications show, this explanation obscures that decisional nature of the Board’s involvement.<sup>496</sup> It allows the Board to argue that its pivotal decisions are beyond the scope of judicial review.<sup>497</sup> In a court filing made only one day after it posted the final Guidelines on its webpage, the Board argued that its handling of an account application was beyond the reach of statutory procedural safeguards.<sup>498</sup> It seems likely that the Board will continue to argue that its “coordination” role is beyond judicial review. The Reserve Banks are unlikely to clarify the Board’s role.

Third, the Guidelines do not provide any processes or standards to ensure consistency in evaluating account requests. The Guidelines seek to promote consistency by identifying risks that Reserve Banks should evaluate when considering requests for accounts and payment services.<sup>499</sup> But it is not clear that risk-identification was the issue most likely to lead to inconsistent Reserve Bank decisions. As Part III illustrates, before the Guidelines, Reserve Banks often spent substantial time evaluating each applicant’s unique risks, whether those risks related to money laundering, government corruption, operational risk, or risk to the Fed’s ability to implement monetary policy. The problem is not that Reserve Banks do not spot the same risks; it is that they might evaluate those risks inconsistently.<sup>500</sup> What one Reserve Bank sees as an undue risk, another Reserve Bank may see as acceptable. The Board, as the supervisor of the Reserve Banks, is best positioned to ensure consistency, but its Guidelines stop short.

## VI. Fixing the Process

The Account Access Guidelines confirm that Federal Reserve will not, on its own, fix fundamental procedural problems with the Reserve Banks’ handling of account access decisions.<sup>501</sup> Congress has previously shown that it wants a

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493. Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. at 51106.

494. *Id.* at 51103.

495. See Memorandum of Law in Support of Motion of the Bd. of Governors of the Fed. Rsr. Sys. for Leave to File a Brief as Amicus Curiae at 2, TNB USA Inc., Fed. Rsr. Bank of N.Y., No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020) (“The Board oversees the operations of the Federal Reserve Banks, including defendant Federal Reserve Bank of New York . . . .”); Memorandum of Law of Amicus Curiae the Bd. of Governors of the Fed. Rsr. in Support of Defendant the Fed. Rsr. Bank of N.Y.’s Motion to Dismiss at 2, TNB USA Inc., v. Fed. Rsr. Bank of N.Y., Case No. 18-CV-07978 (S.D.N.Y. Mar. 25, 2020) (emphasizing the Reserve Banks’ “discretion over whether to open . . . accounts”).

496. See *supra* Section IV.B.

497. See *supra* notes 438-444 and accompanying text.

498. See *supra* notes 439-442 and accompanying text.

499. See *supra* note 470 and accompanying text.

500. See *supra* Section IV.C.

501. Sadly, the Federal Reserve’s approach to accounts mirrors its actions in other areas. Other researchers have observed: “The Fed’s recent history is marked by a level of secrecy, and absence of comprehensible legal process, and an institutional closure utterly foreign to most federal regulation . . . .”.

wide variety of financial institutions, including those without federal deposit insurance, to have fair access to Federal Reserve accounts and payment services.<sup>502</sup> Congress can ensure that financial institutions receive fair access only by requiring that the Federal Reserve adopt procedural changes to make the process consistent and transparent.

### A. Application Process

Congress should require that the Reserve Banks adopt public application procedures. It should be clear how banks can request access, what material should be provided, when the Federal Reserve Bank considers the application complete, when the Federal Reserve expects to decide, and when the application is granted or denied.

As formalized in the new Account Access Guidelines, the account application process for novel banks (those that the Guidelines place in Tier 2 or Tier 3) involves an intense risk assessment.<sup>503</sup> This risk assessment is like the risk vetting performed by bank supervisors when considering other types of applications. Indeed, part of the justification for subjecting Tier 3 institutions to more intensive review is that they have not previously been scrutinized by a federal bank supervisor.<sup>504</sup> Yet when the OCC reviews an application for a charter, the Federal Reserve considers an application to become a bank holding company, or the FDIC evaluates an application for deposit insurance, there is a clear process. Congress establishes time frames.<sup>505</sup> The agencies create application forms and provide lists of materials that applicants should provide.<sup>506</sup> The Federal Reserve even has E-Apps, “a web-based application that allows banking organizations supervised by the Federal Reserve System to submit applications online.”<sup>507</sup> Handbooks describe the process for applicants and provide direction for agency staff.<sup>508</sup> When an agency concludes that an

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Peter Conti-Brown, Yair Listokin & Nicholas R. Parrillo, *Towards an Administrative Law of Central Banking*, 38 YALE J. ON REGUL. 1, 6 (2021). In this environment it would be foolhardy to expect the Federal Reserve to fix the account opening process itself.

502. See *supra* Section I.A discussing the expansion of institutions eligible for Federal Reserve accounts.

503. See *supra* notes 473-479 and accompanying text.

504. Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. 51099, 51100-01 (Aug. 19, 2022).

505. 12 U.S.C. § 4807 (2018). The Board currently believes this provision does not apply to account requests. See *supra* note 440 and accompanying text.

506. *Interagency Charter and Federal Deposit Insurance Application*, FED. DEPOSIT INS. CORP. & OFF. OF THE COMPTROLLER OF THE CURRENCY (2021), <https://www.fdic.gov/formsdocuments/f6200-05.pdf> [<https://perma.cc/2G5Y-ALMC>].

507. *Electronic Applications and Applications Filing Information*, BD. GOVERNORS FED. RSRV. SYS., <https://www.federalreserve.gov/supervisionreg/afi/afi.htm> [<https://perma.cc/H7U8-WL55>].

508. See, e.g., *Applying for Deposit Insurance: A Handbook for Organizers of De Novo Institutions*, FED. DEPOSIT INS. CORP. (Dec. 2019), <https://www.fdic.gov/regulations/applications/depositinsurance/handbook.pdf> [<https://perma.cc/SFK9-494C>] [hereinafter *Applying for Deposit Insurance*]; *Deposit Insurance Applications: Procedures Manual*, FED. DEPOSIT INS. CORP. (2019), <https://www.fdic.gov/regulations/applications/depositinsurance/procmmanual.pdf>

application contains all of the required information, the agency informs the applicant.<sup>509</sup>

Account request applications should not be subject to a more ambiguous process. Indeed, the New York Fed’s Handbook shows that much more could be done to formalize the application process.<sup>510</sup> The process for accessing accounts and payment services should be substantially similar across Federal Reserve Banks.

Some novel bank critics may worry that a clear account application process will facilitate the approval of excessively risky accounts. But given the long scrutiny of the novel banks discussed in Part III, it seems unwarranted to assume the Reserve Banks would suddenly embrace excessive risk.

### *B. The Board’s Role*

Next, Congress should clarify the Federal Reserve Board’s role in the handling of account and payment services requests. The novel account requests suggest that Reserve Banks will not open a novel bank account without the approval of the Board. Similarly, if the Board believes that an applicant is too risky, a Reserve Bank will not open the account.<sup>511</sup> Yet the Federal Reserve Act assigns responsibility for Federal Reserve accounts to the Reserve Banks.<sup>512</sup> If the Board is going to persist in this practice, it should ask Congress to pass legislation assigning it a role in handling account and services requests. If the Board is going to have a determinative role in the decisionmaking process, applicant banks should have an opportunity to address the Board’s staff directly, rather than communicate through the Reserve Banks as intermediaries. If the Board’s decision effectively denies an applicant access, the applicant should be provided enough information to allow the applicant to evaluate the legal adequacy of the Board’s decision. The Board’s actions should be constrained by the Administrative Procedure Act and subject to judicial review.

Legislation describing the Board’s role in account access decisions would not be unprecedented. In 2010, as part of the Dodd Frank Act, Congress clarified the Board’s role with respect to a narrow subset of Federal Reserve Bank accountholders—financial market utilities.<sup>513</sup> When a financial market utility requests an account, the Board of Governors must provide authorization before

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[<https://perma.cc/34XM-Z997>]; *Comptrollers Licensing Manual: Charters*, OFF. OF THE COMPTROLLER OF THE CURRENCY (2021), <https://www.occ.treas.gov/publications-and-resources/publications/comptrollers-licensing-manual/files/charters.pdf> [<https://perma.cc/S6TE-BSXY>] [hereinafter *OCC Licensing Manual: Charters*].

509. *Applying for Deposit Insurance*, *supra* note 508, at 21; *OCC Licensing Manual: Charters*, *supra* note 508, at 27; *Electronic Applications and Application Filing Information: Processing Stages*, BD. GOVERNORS FED. RSRV. SYS., (Aug. 22, 2011), <https://www.federalreserve.gov/supervisionreg/afi/filingstages.htm> [<https://perma.cc/W2TV-SYJJ>].

510. *See supra* Section II.C.

511. *See supra* Section IV.B.

512. *See* 12 U.S.C. § 342 (2018) (stating that Reserve Banks “may receive . . . deposits”); *id.* § 248a (describing the Fed’s payment services as “Federal Reserve bank services”).

513. 12 U.S.C. § 5465(a) (2018).

a Reserve Bank can open the account.<sup>514</sup> As part of this authorization process, the Board can impose conditions and limitations on the applicant's use of the account.<sup>515</sup> If the utility changes its "rules, procedures, or operations" in a way "that could . . . materially affect[] the nature or level of risks," it must provide the Board 60 days advance notice during which time the Board may object to the change.<sup>516</sup> The Board must also weigh in if a Reserve Bank decides to close a financial market utility's account.<sup>517</sup> Congress could similarly require that the Board provide approval before Reserve Banks open accounts for Tier 2 or Tier 3 banks.

### C. Consistency & Transparency

Next, Congress should ensure that the Federal Reserve is accountable for the consistency of its account access decisions. First and foremost, Congress should require that the Federal Reserve make robust disclosures about accounts and account requests.

Congress has already started down this path. After early drafts of this Article, the Reserve Trust controversy, and the Custodia lawsuit brought Federal Reserve accounts into the limelight,<sup>518</sup> Congress passed a defense appropriations rider requiring that the Fed provide a "public, online, and searchable database that contains . . . every entity that currently has access to a reserve bank master account and services."<sup>519</sup> The Federal Reserve must also provide "a list of every entity that submits an access request for a reserve bank master account and services."<sup>520</sup> For each financial institution, the Federal Reserve must identify whether the institution is federally insured.<sup>521</sup>

Only weeks before Congress passed this legislation, the Federal Reserve Board issued a request for comments on its own proposal to provide a list of

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514. *Id.* § 5465(a); 12 C.F.R. § 234.5(a) (2023).

515. 12 U.S.C. § 5465(e)(1)(A).

516. *Id.* § 5465(e)(1)(A), (E). When a financial market utility proposes a change that "raise[s] novel or complex issues" the Board can extend the review timeline by 60 days. *Id.* § 5465(e)(1)(H).

517. *Id.* § 5465(E)(4).

518. Many commentators recommended that the Federal Reserve provide a list of its accountholders. Senate Banking GOP (@BankingGOP), TWITTER (Aug. 15, 2022, 3:31 PM EST), <https://mobile.twitter.com/BankingGOP/status/1559261461343617024> [<https://perma.cc/GW3H-WAFC>] ("Claiming [master accounts are] . . . confidential business information is as absurd as claiming its [sic] confidential whether a bank has FDIC insurance or a television station has an FCC license."); Jared Klee, *Fed Master Accounts*, FINTECH & FIN. (July 24, 2022), <https://fattailethoughts.substack.com/p/master-account> [<https://perma.cc/X4NN-SL9Q>] ("Even the list of who has a Master Account isn't known. It's a black box and a shocking oversight for such an important part of our banking system."); Julie A. Hill (@ProfJulieHill), TWITTER (June 22, 2022, 4:52 PM EST), <https://twitter.com/ProfJulieHill/status/1539713017402851334> [<https://perma.cc/L95U-RA2C?type=image>] ("[T]he Federal Reserve Banks should be more transparent about master account applications. Tell us who has them, who has requested them, and who has been denied.").

519. James M. Inhofe National Defense Authorization Act for Fiscal Year 2023, Pub. Law No. 117-263 tit. LVII, § 5708 (2022) (to be codified at 12 U.S.C. § 248c). The database must be updated at least quarterly. *Id.*

520. *Id.*

521. *Id.*

institutions with access to Federal Reserve accounts or services.<sup>522</sup> The Board explained that its “proposed list would include all institutions that access Reserve Bank priced financial services directly via a master account and those that access services indirectly via a master account of its correspondent bank.”<sup>523</sup> Each institution would be identified by institution name and “the Reserve Bank district in which the institution is located.”<sup>524</sup> Like the legislation, the Board proposed identifying which institutions were federally insured and which were not.<sup>525</sup> The Board also planned to identify institutions that were recently granted access to an account or services and institutions that no longer have access.<sup>526</sup>

While the legislation requiring disclosure of Federal Reserve accountholders and applicants is an important step forward, it may not be sufficient to allow meaningful review of the Federal Reserve’s account access decisions—particularly if it is implemented as described in the Board’s proposal.

First, Congress did not specify how the financial institutions in the database would be identified.<sup>527</sup> The Board’s proposal would disclose only the bank name and Federal Reserve district.<sup>528</sup> Because many banks have similar names,<sup>529</sup> identifying financial institutions this way could make it difficult to determine which have access to Federal Reserve accounts and services. Other federal financial institution databases provide more information. For example, the Federal Reserve’s own Fedwire Participants database lists the financial institution name, location, and ABA routing number.<sup>530</sup> The Federal Financial Institutions Examination Council’s database provides each institution’s name,

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522. Proposed Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. 68691 (Nov. 16, 2022). Its disclosure proposal was surprising because its Account Access Guidelines adopted only three months before had explicitly rejected any disclosures explaining: “[T]he identity of institutions that maintain accounts at Reserve Banks, or that request access to accounts and services, is considered confidential business information and, as such, public disclosure of account status by the Reserve Banks would not be appropriate.” Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. 51099, 51102 (Aug. 19, 2022).

523. Proposed Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. at 68692 n.8.

524. *Id.* at 68692.

525. *Id.*

526. *Id.* Unlike the legislation, the Board did not propose providing any information about financial institutions that have requested accounts. *Id.*

527. James M. Inhofe National Defense Authorization Act for Fiscal Year 2023, Pub. Law No. 117-263 tit. LVII, § 5708 (2022) (to be codified at 12 U.S.C. § 248c).

528. Proposed Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. 68691, 68692 (Nov. 16, 2022).

529. See, e.g., *Union Nat’l Bank of Texas, Laredo v. Union Nat’l Bank of Texas*, Austin, 909 F.2d 839, 841 n.4 (1990) (“It is worth noting that . . . the advent of branch banking . . . may have led to [the] problem of competing banks with the same name.”); Dennis Darrow, *Similar Name, Different Bank*, PUEBLO CHIEFTAIN (Apr. 16, 2009, 12:01 AM MT), <https://www.chieftain.com/story/business/2009/04/16/similar-name-different-bank/8844476007/> [https://perma.cc/RH9A-XJTL]; Andy Peters, *Seeing Double? Bank Buys Neighbor with Same Name*, AM. BANKER (June 13, 2013, 12:05 PM EDT), <https://www.americanbanker.com/news/seeing-double-bank-buys-neighbor-with-same-name>, 2013 WLNR 14508194.

530. *Fedwire Search*, *supra* note 395.

headquarters address, FDIC certificate number, and ABA routing number.<sup>531</sup> The Federal Reserve could minimize name confusion by providing institutions' addresses and ABA routing numbers. This information would also allow database users to cross-reference the information about Federal Reserve accounts with other financial institution data, like quarterly call reports.

Second, the proposed disclosure categories do not match the way the Federal Reserve evaluates account and service requests. The new statute and the Board proposal both anticipate disclosing information that distinguishes federally insured institutions from those that are not federally insured.<sup>532</sup> But the Board's Account Access Guidelines separate financial institutions into three distinct tiers—one for federally insured institutions, one for institutions without federal insurance but with a federal prudential regulator and Federal Reserve oversight of its holding company, and one for other institutions.<sup>533</sup> The Federal Reserve thinks these types of financial institutions are different enough to warrant different levels of scrutiny. The Federal Reserve should be transparent about the level of scrutiny it applies to each institution.<sup>534</sup> Its disclosures should identify financial institutions by tier.<sup>535</sup> Among other things, this change will allow the public to better evaluate procedural consistency across the Federal Reserve districts.

Similarly, the Federal Reserve's proposed disclosures lump together all financial institutions with "access" to Federal Reserve accounts or services, regardless of whether the institution has a master account or settles transactions through a correspondent bank.<sup>536</sup> But master account access is not the same as correspondent access.<sup>537</sup> Accordingly, the Federal Reserve should identify which

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531. *Search Institutions*, FED. FIN. INSTS. EXAMINATION COUNCIL, <https://www.ffiec.gov/npw/https://perma.cc/CJV6-VM5C>].

532. James M. Inhofe National Defense Authorization Act for Fiscal Year 2023, Pub. Law No. 117-263 tit. LVII, § 5708 (2022) (to be codified at 12 U.S.C. § 248c); Proposed Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. 68691, 68692 (Nov. 16, 2022).

533. Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. 51099, 51107-10 (Aug. 19, 2022).

534. Outside observers may not be able to easily distinguish some Tier 2 institutions from Tier 3 institutions. To be evaluated under Tier 2's intermediate scrutiny, a financial institution's holding company must be "subject to Federal Reserve oversight (by statute or commitments)." *Id.* at 51109-10. A holding company's commitment to Federal Reserve oversight may not otherwise be publicly disclosed.

535. Because the Federal Reserve's Guidelines establishing the three-tiered review is new, the Federal Reserve may not have sorted existing account and service users into these categories. Nevertheless, the Federal Reserve Board affirmed that its Guidelines would "be applied broadly including to existing accounts." *Id.* at 51106. Accordingly, the Federal Reserve should be able to provide these classifications after a reasonable transition period.

536. Proposed Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. 68691, 68692 n.8 (Nov. 16, 2022).

537. Some payment services are available only to institutions that can settle transactions in their own master account. *Operating Circular 1 (2021)*, *supra* note 37, §§ 2.1 n.3, 2.7 (explaining that among other things, Fedwire transactions cannot settle in a correspondent's account). It is not clear whether the Federal Reserve applies the same level of scrutiny to requests for services through a correspondent that it does to requests for master accounts. *See* Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. at 51106 n.1 (stating that the Account Access Guidelines' risk principles apply to services accessed through correspondents but omitting any discussion of correspondent relationships with respect to the tiered review framework).



financial institutions access payment services through a master account and which access services through correspondent banking relationships.

Third, neither the legislation nor the Board's proposal contemplates any explanation of the Federal Reserve's decisions. For example, when the Federal Reserve discloses that it denied an account or service request, it does not publicly disclose why. Perhaps the Federal Reserve determined the institution was legally ineligible. Perhaps the Federal Reserve determined that if there were many more institutions of the same type, it would pose a risk to the payment system. Or perhaps the Federal Reserve had concerns about the applicant's management, policies, or capitalization.

Leaving observers to guess about the Federal Reserve's reasoning for denying requests can be costly for future applicants. If the Federal Reserve decides that certain charters are ineligible, it makes little sense for others with the same charter to seek Federal Reserve accounts. Similarly, if the Federal Reserve concludes that narrow banks cannot have accounts because they threaten the Fed's ability to conduct monetary policy or that cryptocurrency custody services threaten the payment system, the Fed should disclose this information. Otherwise, people waste time and money traveling down the same unfruitful path.

If the Federal Reserve explained its reasons for denying accounts and services, observers would be better able to assess the consistency of Federal Reserve decisions.<sup>538</sup> This could lend credibility to the Federal Reserve and its account-related decisions. As the Reserve Trust experience shows, sometimes the existence of an account leads to more questions than answers.<sup>539</sup> If there was a straightforward explanation about why Reserve Trust was no longer legally eligible for an account, the Federal Reserve might have saved itself the accusations of impropriety by providing that explanation.

Accordingly, the Federal Reserve should provide brief public explanations when it denies account or services requests. It should also provide explanations when it decides to close an account or terminate service. When decisions impact classes of applicants (e.g., those with a particular charter, or those with a particular business plan), the Federal Reserve should provide a decision comprehensive enough to provide guidance for similar institutions. Because the Federal Reserve already provides written decisions to institutions whose requests are declined, making these decisions publicly available should not be onerous.<sup>540</sup>

Of course, not everyone is enthusiastic about more robust Federal Reserve account disclosures. Some are concerned that the disclosures will harm financial institutions. For example, some worry that disclosing information about rejected

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538. Cf. Chad M. Oldfather, *Remedying Judicial Inactivism: Opinions as Informational Regulation*, 58 FLA. L. REV. 743, 791 (2006) (explaining that written court opinions "enable the assessment of courts' performance over a long period of time" making it "possible to determine the extent to which courts are in fact treating like cases alike").

539. See *supra* Section III.E.

540. See *supra* notes 167-171 and accompanying text. If the decision letter contains confidential personal information, that information could be redacted.

applications “might reflect poorly” on the failed applicant.<sup>541</sup> While this reputational risk may be real, we should view it as one of the risks applicants take when they request accounts. Others who make applications to bank supervisors accept this risk as part of the application process. For example, when the OCC denies an application to buy a bank, it might reflect negatively on the company requesting the acquisition.<sup>542</sup> But this does not prevent the OCC from making the disclosure.<sup>543</sup>

Second, some worry that increased transparency will curtail the Federal Reserve’s discretion. According to Derek Tang, an economist at Monetary Policy Analytics: “[I]f who applies, and potentially who gets rejected, is public, then applicants can figure out exactly what the lines are and argue, in court or in public, that treatment has been inconsistent.”<sup>544</sup> But this is a feature, not a drawback, of disclosure. Transparency allows applicants and the public to assess whether account and service requests are handled consistently. The Federal Reserve has no legitimate interest in ensuring that it retains authority to handle applications according to its whims. Applicants that are treated unfairly should have some avenue for redress.

But even robust public disclosure might not be enough to bring consistency. If, after the Federal Reserve makes the disclosures above, it appears that applications for Federal Reserve accounts are not handled consistently, Congress should adopt additional legislation to achieve consistency. There are many possible avenues for improving consistency, many of them procedural. For example, Congress could require that a centralized committee led by the Board review all applications for accounts and services.<sup>545</sup> Congress could require that

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541. Zoe Sagalow, *Fed Guidelines on Master Account Access Leave Lingering Questions*, S&P GLOB. MKT. INTEL. (Sept. 15, 2022), <https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/fed-guidelines-on-master-account-access-leave-lingering-questions-72064673> [<https://perma.cc/XV98-9Q6N>] (quoting Chip MacDonald, managing director of MacDonald Partners); see also Proposed Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. 68691, 68691 (Nov. 16, 2022) (“[T]he Board acknowledges that institutions could face the risk of reputation harm if they are denied access to accounts and services, even if the denial is due to a Reserve Bank’s evaluation of information that is publicly available (e.g., information about an institution’s business model).”).

542. David Breitkopf, *OCC Denies CompuCredit Application to Buy Bank*, AM. BANKER (Oct. 31, 2003, 2:00 AM EST), <https://www.americanbanker.com/news/occ-denies-compucredit-application-to-buy-bank>, 2003 WLNR 4178934 (reporting that the OCC denied the request because it was “too risky” and “its management lacks the proper experience”).

543. See Office of the Comptroller of the Currency, Corporate Decision 2003-11, Statement on the Decision of the Office of the Comptroller of the Currency on the Notice by CompuCredit Corporation of its intent to Acquire a Controlling Interest in Axsys National Bank, Sioux Falls, South Dakota (Sept. 2, 2003), <https://www.occ.gov/topics/charters-and-licensing/interpretations-and-actions/2003/cd03-11.pdf> [<https://perma.cc/3P5F-ZT9Z>].

544. Sagalow, *supra* note 541 (quoting Derek Tang).

545. See Letter from Rose Oswald Poels, Pres. & CEO, Wisc. Bankers Ass’n to Ann E. Misback, Sec’y, Bd. of Governors of the Fed. Rsrv. Sys. (July 12, 2021), [https://www.federalreserve.gov/SECRS/2021/July/20210714/OP-1747/OP-1747\\_071221\\_138239\\_357757418056\\_1.pdf](https://www.federalreserve.gov/SECRS/2021/July/20210714/OP-1747/OP-1747_071221_138239_357757418056_1.pdf) [<https://perma.cc/CD29-MNQ6>]; Letter from James A. Reuter, CEO, FirstBank Holding Co., to Ann E. Misback, Sec’y, Bd. of Governors of the Fed. Rsrv. Sys. (July 8, 2021), [https://www.federalreserve.gov/SECRS/2021/July/20210714/OP-1747/OP-1747\\_070821\\_138241\\_359408681779\\_1.pdf](https://www.federalreserve.gov/SECRS/2021/July/20210714/OP-1747/OP-1747_070821_138241_359408681779_1.pdf) [<https://perma.cc/TLB4-UX5U>] (recommending “a coordinated and centralized committee be formed to evaluate and decide each application for Reserve Bank accounts and services”).

the Federal Reserve adopt an internal appeals procedure to remedy inconsistent outcomes.<sup>546</sup> Congress could clarify that the Reserve Banks are subject to FOIA and the APA.<sup>547</sup> Congress could also encourage consistency through substantive rules. For example, Congress could adopt specific liquidity rules or reserve requirements.<sup>548</sup> Or Congress could state that all legally eligible institutions are entitled to an account without separate risk-vetting conducted by the Federal Reserve.<sup>549</sup>

## Conclusion

Banks of all types need access to Federal Reserve-provided accounts and payment systems. For traditional banks—those that accept federally insured deposits and make loans—access to Federal Reserve payment systems is straightforward. But novel banks spend years trying to navigate a system with no clear application documents, no clear decisionmaker, and sometimes no clear decision. The Federal Reserve Board recently adopted Account Access Guidelines, but they do not solve these problems.

Congress should require that the Reserve Banks adopt public application procedures. The Board should be transparent about the gatekeeping role it plays in account and payment access decisions. The Board's actions should be subject to administrative law constraints. And Congress should require that the Federal Reserve make robust disclosures about account and service access decisions. If these measures do not result in consistent access to accounts and services, Congress should consider additional procedural constraints or legislative directives to ensure that financial institutions have broad access to accounts.

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546. In other contexts, federal bank supervisors are required to provide an intra-agency appeals process for material supervisory determination. See 12 U.S.C. § 4806(a) (2018).

547. See Kyle Campbell, *Toomey-Warren Bill Would Require More Fed Accountability*, AM. BANKER (Dec. 9, 2022, 4:25 PM EST), <https://www.americanbanker.com/news/toomey-warren-bill-would-require-more-fed-accountability>, 2022 WLNR 39839607 (describing bipartisan legislation that would make Federal Reserve Banks subject to the Freedom of Information Act).

548. Cf. Dan Awrey, *Unbundling Banking, Money, and Payments*, 100 GEO. L.J. 715, 774-775 (2022) (arguing that non-bank payment firms be given access to Federal Reserve accounts provided that they “hold 100% of customer deposits in this account”); Letter from James A. Reuter to Ann E. Misback, *supra* note 545 (“We recommend a more precise definition of ‘sufficient liquid resources’ and more specificity with respect to the process by which an entity must identify and measure its liquidity risk.”).

549. Whether all eligible institutions are legally entitled to accounts and payment services under existing law is beyond the scope of this Article.