



## FedAccounts Would Provide Economic Relief—and Inclusion—in the Short and Long Term

The COVID-19 pandemic is exposing structural flaws in our economy that have made the crisis far worse than it should have been. Rampant inequality, disinvestment in public institutions, and a persistent erosion of worker protections have created a precarious economy that has collapsed under the immediate crisis. The result: Over 20 million individuals have lost their jobs in the last month alone, predominantly workers from low-income and Black and brown communities.

Congress has acted quickly, appropriating billions of dollars to stem the economic bleeding. But response efforts that fail to address the underlying structural flaws could actually exacerbate inequality. One of the clearest examples is the lack of access to bank accounts. Congress authorized \$1,200 in relief checks to millions of Americans, yet whole segments of the population—indeed, those most in need of this urgent relief—will likely wait six to eight weeks for these funds because they lack access to a functioning bank account. (This is on top of check-cashing fees of up to 3.5 percent.) And with 40 percent of Americans unable to cover a \$500 emergency even before the pandemic hit, this delay could mean financial devastation for too many. Meanwhile, those with economic privilege can expect to have their money seamlessly direct deposited into their bank accounts.

**Fortunately, Congress can fix this immediate problem, while simultaneously addressing structural flaws in our financial system, by directing the Federal Reserve (the Fed) to offer bank accounts to all US residents.** First proposed by Morgan Ricks, John Crawford, and Lev Menand,<sup>1</sup> and building on Mehrsa Baradaran’s postal banking proposal,<sup>2</sup> these “FedAccounts” would be a public option for basic banking services. In the short term, FedAccounts would be a seamless and effective way to deliver relief funds to all eligible recipients. In the longer term, FedAccounts would remedy long-standing systemic problems with our banking system that have disproportionately burdened low-income communities, ultimately bringing about transformational change to the American monetary-financial system.

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<sup>1</sup> Ricks, Morgan, John Crawford, and Lev Menand. 2018. “Central Banking for All: A Public Option for Bank Accounts.” New York: Great Democracy Initiative. <https://greatdemocracyinitiative.org/wp-content/uploads/2018/06/FedAccountsGDI.pdf>.

<sup>2</sup> Baradaran, Mehrsa. 2014. “It’s Time for Postal Banking.” Harvard Law Review 127, no. 4 (February). <https://harvardlawreview.org/2014/02/its-time-for-postal-banking/>.

## A Proposal for a FedAccount

Currently, only banks and certain governmental entities are allowed to have accounts with the Federal Reserve, the central bank of the United States. But it doesn't have to be this way. A FedAccount would entitle all US citizens, residents, and domestically domiciled businesses and institutions to open an account with the Fed. Under Ricks, Crawford, and Menand's proposal, FedAccounts would offer all of the functionality of ordinary bank transaction accounts, except for overdraft coverage. They would also have all the special features that banks currently enjoy on their central bank accounts:

- FedAccounts would pay the same interest rate that commercial banks receive on their balances (rates had been 1.75 percent as recently as last year, versus a mere 0.05 percent average rate on ordinary checking accounts and 0.08 percent on savings accounts);
- They would have no interchange fees, minimum-balance requirements, or other hidden costs, and no one would be denied access for profitability considerations;
- Payments between FedAccounts would clear in real time, just like interbank payments processed by the Fed. The system would work like existing, popular peer-to-peer payment services (e.g., Paypal, Venmo, Square Cash), except that users would never need to "cash out" their balances to a bank account—because FedAccount is a bank account;
- FedAccount balances would be fully sovereign money, just like reserve balances that commercial banks hold. There would be no possibility of default on balances of any size, rendering deposit insurance superfluous.

## Benefits of FedAccounts

### **FedAccounts are an efficient and equitable way to deliver government dollars.**

First and foremost, FedAccounts provide a quick and seamless way to deliver government money to citizens. With the creation of a FedAccount, the government could distribute stimulus payments, particularly to those who are both most in need and hardest to reach. The government could deposit the funds directly, with no waiting periods, and people could withdraw the money at ATMs or move the money to other bank accounts.

### **FedAccounts would promote financial inclusion while addressing structural inequalities perpetuated by our current banking system.**

Beyond the immediate benefits, FedAccounts would serve the broader good of democratizing banking. Because FedAccounts would not have any fees or minimum balance requirements and would be marketed

explicitly as a public service, they would attract millions of people currently without bank accounts. In short, it would—as Ricks, Crawford, and Menand argue—transform the US account-money system into public infrastructure akin to roads, sidewalks, public libraries, the judicial system, and law enforcement.

More broadly, FedAccounts would provide an attractive alternative to our current payment delivery system—a system that benefits banks and shadow financial industries at the expense of poor people. Our current payment delivery system is filled with unnecessary delays. Checks, for example, still take several business days to clear, and credit card payments may not settle for two days. These payment delays are costly for the economy as a whole, and they can trigger debt spirals for paycheck-to-paycheck households that have no cash reserves. This time gap creates demand for payday lenders and check cashers. Banks, too, have developed a profitable business model by allowing debits to clear before the check does and charging customers hefty overdraft fees (sometimes multiple in a day). With 75 percent of the overdraft fees paid by 8 percent of customers,<sup>3</sup> the effect is a wealth transfer from the poorest customers to bank shareholders.

The instant payment feature of FedAccounts would help households avoid overdraft fees by giving them faster access to the money that they earned and reducing the need to rely on payday loans or check cashing. And the impact could be substantial. Bank overdraft fees plus fees collected by check-cashing companies are estimated to have cost households more than \$100 billion since 2008.<sup>4</sup> Eliminating just 10 percent of overdrafts, payday loans, and check cashing would restore around \$3.5 billion a year<sup>5</sup> to working families. Eliminate a higher share, and that could reach tens of billions a year that could be solved by real-time payments.

Finally, the benefits of inclusion would extend beyond these households themselves. People and businesses on the other side of payments would gain from transacting with fully banked individuals. For instance, employers would save administrative costs from using direct deposit instead of cutting physical checks. Many businesses would benefit from customers' use of convenient and reliable automatic bill pay. Government agencies would benefit from easier administration of benefit transfers and tax refunds.

## **FedAccounts would boost small businesses and consumers in a time of crisis by reducing payment system frictions.**

Beyond the direct effects on financial inclusion, the FedAccount would also have ancillary benefits for businesses, especially those hardest-hit by the current economic crisis. The COVID-19 pandemic has placed enormous pressure on small businesses struggling with liquidity. In addition to the welcome perks of higher interest rates, the instant payments component could help businesses manage cash flow because they would provide greater control over the timing and certainty of payments. Companies may receive money faster and get more accurate snapshots of their current cash position. Moreover, the real-

<sup>3</sup> Bakker, Trevor, Nicole Kelly, Jesse Leary, and Éva Nagypál. 2014. "Data Point: Checking Account Overdraft." Washington, DC: Consumer Financial Protection Bureau. [https://files.consumerfinance.gov/f/201407\\_cfpb\\_report\\_data-point\\_overdrafts.pdf](https://files.consumerfinance.gov/f/201407_cfpb_report_data-point_overdrafts.pdf).

<sup>4</sup> Klein, Aaron. 2018. "Potential Federal Reserve Actions to Support Interbank Settlement of Faster Payments Docket No. OP-1625." Memorandum to Board of Governors of the Federal Reserve System. Brookings Institution. [https://www.federalreserve.gov/SECRS/2018/December/20181221/OP-1625/OP-1625\\_121418\\_133277\\_428769914666\\_1.pdf](https://www.federalreserve.gov/SECRS/2018/December/20181221/OP-1625/OP-1625_121418_133277_428769914666_1.pdf).

<sup>5</sup> Ibid.

time payments could reduce risk since payments are immediate, potentially eliminating the possibility that a customer or another business would initiate a payment and then cancel it after goods have been shipped. Finally, reducing aggregate interchange fees would be a boon to merchants, particularly for small businesses that can't negotiate with card networks for special interchange rates. Ultimately, the benefits would also be passed along to consumers in the form of lower prices for goods and services.

### **FedAccounts would help stimulate the economy by generating substantial revenue.**

Far from overburdening the public fisc, the FedAccounts might generate significant fiscal revenue. Currently, the Fed remits tens of billions of dollars to the Treasury every year in profits from investing the trillions of dollars that it holds.<sup>6</sup> If millions of people, businesses, and large corporations carry FedAccounts, the Fed's balance sheet would grow, and the remittances could increase, even after factoring in the cost of account maintenance. Not only would this additional fiscal revenue not be economically distortive, it would actually remove existing distortions by reducing implicit subsidies or “economic rents” that the financial system extracts from the public sector.

### **FedAccounts would increase the efficacy of monetary policy.**

This is particularly relevant, given the Fed's importance during times of economic crisis. One of the Fed's primary tools to influence macroeconomic policy is raising or lowering interest rates for banks on their central bank accounts, known as interest on reserves (IOR). The theory is that IOR will shape bank behavior, with a subsequent ripple effect for the macroeconomy, as banks “pass through” the IOR to market interest rates. Problematically, banks have often failed to pass through the rates. The Fed has effectively been subsidizing banks by paying them tens of billions of dollars per year. Broad adoption of FedAccounts would ameliorate or eliminate this problem since banks would no longer be needed as an intermediary; individuals and businesses would receive that interest on their balances directly. This would give the Fed far more precision and ability to directly impact the economy—a tool that is badly needed in our current recession.

### **FedAccounts would strengthen financial and macroeconomic stability.**

Finally, assuming the Fed wins big institutional accounts, FedAccounts could crowd out runnable cash equivalents by making pure sovereign money widely available in “account” form, all but eliminating a primary cause of macroeconomic disasters. History has shown time and again that runnable cash equivalents—basically, the financial sector's short-term and demandable debt—present a grave threat to the broader economy. Though deposit insurance basically ended runs on deposits, modern panics have involved runs on institutional deposit substitutes, such as repo, Eurodollars, and money market mutual fund shares. FedAccounts would offer a compelling alternative to private cash equivalents: pure sovereign money paying the interest-on-reserves rate, an asset currently available only to banks.

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<sup>6</sup> Board of Governors of the Federal Reserve System. 2020. “The Federal Reserve's Balance Sheet.” Credit and Liquidity Programs and the Balance Sheet. Last updated March 19, 2020. [https://www.federalreserve.gov/monetarypolicy/bst\\_fedsbalancesheet.htm](https://www.federalreserve.gov/monetarypolicy/bst_fedsbalancesheet.htm).

## Conclusion

Many aspects of the financial system—including payments and access to safe deposits—are essential services that must be provided for all and should be considered a public utility. Unfortunately, monetary dysfunction has played a persistent role in US history, profiting banks at the expense of low-income communities. As an economic crisis approaching the magnitude of the Great Depression unfolds, we are witnessing the painful and compounding consequences of this dysfunction: Millions of Americans are waiting for desperately needed checks.

Fortunately, we think the opportunity to address this flawed banking system is in reach, and getting there would not be all that difficult. The FedAccounts would allow checks to be delivered quickly to those most in need. More broadly, it would reshape the sovereign “account money” system into an open-access resource, just like the sovereign physical currency system. The effects would be transformative: expanding financial inclusion, supporting small businesses, and creating long-term structural change for our economy.

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