ASK KENNEDY
February 2, 2022

Topics Covered:

- Member Questions
- Federal Reserve Paper on Central Bank Digital Currency
- 2022 NDBA Events

Question #1: Does North Dakota law require a power of attorney form to submit a request to place a lien on a vehicle title? Can a bank sign the Purchaser's Certification on behalf of the borrower?

Response: **Section 35-01-05.1 of the North Dakota Century Code governs security interests in vehicles and provides in relevant part:**

1. **No security interest, including a security interest under chapter 41-09, in a vehicle, including a manufactured home, which is not inventory held for sale is valid as against subsequent purchasers and encumbrances of the property in good faith and for value unless the security interest is clearly indicated upon the certificate of title to the vehicle or unless such certificate of title is in the possession of the secured party, provided, however, that a purchase money security interest under chapter 41-09 in a manufactured home is perfected against the rights of judicial lien creditors and execution creditors on and after the date the purchase money security interest attaches, and provided further the holder of a security interest in or a lien on a manufactured home may deliver lien release documents to a person to facilitate conveying or encumbering the manufactured home. A person receiving documents so delivered holds the documents in trust for the security interest holder or the lienholder.**

There is no specific law that protects that protects a bank from the liability that is placed on the signer of the Purchaser's Certificate. The language before the signature line (which is required for the buyer or applicant) says the following:

> **"The buyer (applicant), subject to the penalties of law, certifies the purchase price of the vehicle. The buyer makes application for certificate of title to the vehicle, having acquired it subject to the liens stated. The buyer certifies the vehicle is and will continue to be insured while operating upon public streets and highways."**

Signing this would open the bank up to liability as the signer/applicant. Instead, the bank should have the buyer sign the application at the bank and have the bank fill in the lienholder information and send in the application on the borrower's behalf.

Federal Reserve Paper on Central Bank Digital Currency

On January 20, 2022, the Federal Reserve released a paper discussing the pros and cons of a central bank digital currency (CBDC). This session of Ask Kennedy focuses heavily on a discussion surrounding this topic. Please see the attached paper.

Mark Your Calendars: NDBA Events in 2022

The North Dakota Banker's Association has many exciting and informational events planned for 2022. Below are some special dates to mark on your calendars –

- **CONFERENCES**
  - **NDBA/SDBA 2022 Bank Management Conference**
    February 18-19, 2022 | Scottsdale, AZ

    NDBA's annual Bank Management Conference addresses current issues in the banking industry, including strategic issues, technology trends, regulatory and economic changes, and leadership topics.
  - **2022 Tri-State Trust Conference**
    April 26-28, 2022 | Delta Hotel by Marriott, Fargo, ND

    Sponsor/Exhibitor Registration Form available here.
  - **2022 NDBA/SDBA Annual Convention**
    June 14-15, 2022 | Radisson Hotel, Bismarck, ND
    More information to come.
  - **2022 Ag Credit Conference**
    October 5-6, 2022 | Delta Hotel by Marriott, Fargo, ND
- **SCHOOLS**
  - **Dakota School of Lending Principles**
    Hosted by South Dakota Bankers Association
    March 29-April 1, 2022 | Best Western Ramkota Hotel, Aberdeen, SD
  - **Dakota School of Banking**
    June 5-10, 2022 | Jamestown, ND | University of Jamestown
  - **National School for Experienced Ag Bankers**
    June 20-23, 2022 | Spearfish, SD | Black Hills State University

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NORTH DAKOTA BANKERS ASSOCIATION

DIGITAL CURRENCY

WHAT BANKS NEED TO KNOW

On January 20, 2022, the Federal Reserve issued a paper, *Money and Payments: The U.S. Dollar in the Age of Digital Transformation*, exploring the implications of, and options for, issuing a U.S. Central Bank Digital Currency. The Fed is seeking comments to specific questions from stakeholders that might use a CBDC or be affected by its introduction. You can comment until May 20, 2022 using the form at: https://www.federalreserve.gov/apps/forms/cbdc.

THE BASICS OF DIGITAL CURRENCY

COMMON TYPES OF DIGITAL CURRENCIES

Central Bank Digital Currencies (CBDCs)
CBDCs are a digital representation of fiat currency, and are monetary instruments that are direct liabilities of a central bank.

Stablecoins
A privately issued cryptocurrency designed to maintain a stable value by linking its value to stable reserve assets, such as fiat currencies. In the U.S., stablecoins are primarily used to facilitate trading, lending, and borrowing of other digital assets.

Other Cryptocurrencies
A privately issued digital representation of value that is not necessarily attached to fiat currency, but accepted as a means of payment and can be transferred, stored, or traded electronically.

DIGITAL CURRENCY EXCHANGES

Digital currency exchanges allow users to exchange digital assets in exchange for other assets (such as fiat money or other digital currencies). Exchanges are subject to state regulations as money transmitters/money services businesses and to Know Your Customer regulations. Such exchanges can also offer other services resembling retail banking services.

DIGITAL LEDGERS

Transaction records (including participants' identities) are recorded on a digital ledger. Digital ledgers may be centralized or decentralized (through use of distributed ledger technology). Cryptocurrencies use distributed ledgers.

Centralized Ledgers
Centralized ledgers establish a single authority to approve transactions and maintain records.

Decentralized/Distributed Ledgers
Decentralized digital ledgers (hereafter referred to as distributed ledgers) use a shared electronic database where copies of the same information are stored and recorded on a distributed network of computers. The information cannot be modified unless a consensus is reached that the information is valid, meaning that any attempt at modification on one computer will not have an effect. Blockchain is a type of distributed ledger.

Distributed ledgers may be public or private, depending on whether the ledgers can be accessed by anyone or only by certain pre-selected network participants.

Public Distributed Ledger (also called "open" or "permissionless")
There is no central owner who controls network access. Anyone with a computer serve with the relevant software can joint the network and add transactions to the ledger.

Private Distributed Ledger (also called "permissioned")
Network members are pre-selected by an owner or an administrator of the ledger who controls network access and enforces the rules of the ledger.

**Note: The Federal Reserve's paper does not appear to specifically discuss whether a potential U.S. CBDC would use distributed ledger technology or a centralized database.*

KEY POINTS IN FEDERAL RESERVE PAPER

- CBDC defined as a digital liability of the Federal Reserve that is widely available to the general public
- The Fed is looking at an intermediated model in which intermediaries (potentially commercial banks and regulated nonbank financial service providers) offer services to manage CBDC holdings and payments.
- Intermediary would likely provide compliance with anti-money laundering and other rules
- Widely available CBDC would be a close or perfect substitute for commercial bank money, which could reduce the aggregate amount of deposits in the banking system
- Interest-bearing CBDC could result in shift away from low-risk assets, including shares in money market mutual funds, Treasury bills, and other short-term instruments

CBDC MODELS AND POTENTIAL EFFECTS

DIRECT VS. INDIRECT/INTERMEDIATED

The Fed's paper notes that initial analysis favors an **intermediated model**. A memo for the Committee on Financial Services dated July 23, 2021 explains the different models for CBDCs as follows:

"One-tier models (also called "direct CBDCs") establish the central bank as the user-facing enterprise, providing accounts and customer services directly to retail customers.

In contrast, two-tier systems (or "indirect CBDCs") feature private financial services providers (e.g., banks, payment platforms) as an intermediary between retail customers and the central bank. In a two-tier system, the payment service provider is responsible for furnishing customer accounts (including digital wallets), handling retail payments, and maintaining compliance with financial crime obligations, leaving the central bank to handle only the digital wholesale payments."

POTENTIAL EFFECTS

The same memo provides the potential implications of CBDC for the traditional reserve banking system:

Traditionally, banks and credit unions make money through maturity transformation, taking on short-term liabilities in the form of deposits and lending that money out in the form of longer-term assets, like mortgages. **The introduction of CBDCs could fundamentally disrupt this system since the FI would not be able to use the CBDCs that would be stored in the wallets that they manage in a two-tier system** or would not play a role whatsoever in a one-tier system. **Additionally, in certain situations, CBDCs could also pose a risk to financial stability in a system due to concerns around flights to safety in times of economic stress. In a system where there is no limit on the amount of CBDC that one person can control, individuals may move all their assets into CBDCs, which the government guarantees, potentially causing stress at FIs and within other segments of the financial system. Among other things, this could have implications for deposit insurance and the bank resolution framework that prioritizes retail depositors.** Models can account for this possibility by limiting the amount of CBDC an individual can control or the overall amount in the system."

FEDERAL RESERVE'S QUESTIONS

The Federal Reserve is seeking comments on twenty-two questions, which include the following:

- Whether a CBDC could adversely affect the financial sector, and how it might do so differently from stablecoins or other nonbank money
- What tools could mitigate adverse impact on the financial sector, and would these tools diminish the benefits of a CBDC
- How could a CBDC provide privacy to consumers without providing complete anonymity and facilitating illicit financial activity?
- Should a CBDC be legal tender?
- Should a CBDC pay interest?
- Should the amount of CBDC held by a single end user be subject to quantity limits?
- What types of firms should serve as intermediaries for CBDC? What should be the role and regulatory structure for these intermediaries?