

Remarks by

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In August of last year, Treasury Secretary Rubin asked me to coordinate Treasury's activities in the electronic money and electronic commerce areas. In addition to being flattered, I also felt the Secretary's request made sense for several reasons. The OCC had already become active in electronic money issues, due in large part to the interest shown in e-money and e-banking by the banks we supervise. We had already begun to consider a variety of e-money related questions concerning bank safety and soundness, stability of the financial system, law enforcement, bank operations, and consumer issues.

We also had a historic tie to this issue. After all, Abraham Lincoln and Treasury Secretary Chase created the Office of the Comptroller of the Currency 1863 as a keystone in the issuance and supervision of the United States' first paper currency -- national bank notes. So, from a historical standpoint, policy issues related to new forms of money were hardly unfamiliar to us.

As I have proceeded with this coordination effort, I have been impressed not only with the high level of expertise and ability throughout the Treasury Department, but also with how the responsibilities of the various Treasury bureaus are closely connected to most of the key e-money and e-commerce concerns. For example, FinCEN, Secret Service, BATF, IRS and Customs all have important institutional interests in financial crimes issues. The FMS is the nation's biggest collector and payor of moneys. And the Treasury Secretary, OCC and OTS have concerns about financial stability. Accordingly, through our activities to coordinate this wide array of interests, we at the OCC have further refined our appreciation for and understanding of e-money and the issues it presents.

Today, I would like to share with you some insights that we have gained about the complex of issues surrounding the development of e-money and e-commerce. These insights were gleaned in part from periodic meetings with officials of the Treasury Department and other agencies of the government, as well as from discussions with congressional leaders such as Congressman Castle -- who, I might note, has done a very fine job of focusing public attention on these issues in a responsible way. Perhaps even more importantly, along with my colleagues at the OCC and Treasury, I have learned a great deal from numerous meetings we have set up with a broad spectrum of

private sector interests, many of whom are in this room, including financial institutions, non-financial institutions, communications providers, and consumer groups.

Perspective and Proportion

One set of lessons that we have learned from these meetings and discussions I would put under the heading of perspective and proportion.

There have been a lot of "gee whiz" articles written about virtual money and banking in cyberspace. In fact, the term "cyberspace" originated in a 1983 science fiction novel to describe a future world where paper money had been virtually eliminated (except for limited black market business) and all commerce took place on a huge interconnected electronic matrix. Now, only 13 years after the book was published, the Internet is a reality and we're talking about cards with stored electronic value. This in turn has occasioned some call for immediate government involvement in the area.

Despite all the hoopla and concern about potential new electronic banking products, there are several reasons for government to be cautious.

First, only a modest amount of e-money business is actually being conducted as of this moment. The fact is that today there is no meaningful use of open-system stored value cards in this country. And pilot projects aside, I do not believe we will see a robust use of this technology in America for the next two to five years. The same can be said for banking over the Internet.

Second, somewhat like Moliere's Bourgeois Gentilhomme who learned he had been speaking prose all his life, all of us recognize that electronic payments are not a brand new invention. At a wholesale level, electronic payments have been going on for quite some time. And over time, we have found ways to deal with crime and with other safety and soundness issues in this area.

Third, these technologies are rapidly evolving. At this point, it is extremely difficult to predict what products will ultimately emerge or which products should be the focus of our attention.

Moreover, it is very much in the private sector's interest to solve many, if not all of the problems, that would concern public policy makers. For example, any responsible issuer of e-cash knows that he has to have a safe and reliable product or the public will not use it as a cash replacement. And, indeed, as we have seen e-cash products being introduced in Denmark, Portugal, Belgium and Finland, that is exactly what has happened. In all these countries a considerable effort has been successfully expended to make sure that e-cash did not become a source of money laundering or counterfeiting.

Long Term Implications

A second set of lessons that we have learned is that, while the short term effects of e-money may be somewhat overblown, the long term implications of this phenomenon are often underappreciated.

If I asked virtually anyone in this room whether we will see considerable changes in our economy as a result of electronic money and banking, I am sure we would all answer with an emphatic yes. There is clearly a freight train coming down the tracks, and we can see its headlight and hear it chugging in the distance. Just because it hasn't arrived yet doesn't mean we shouldn't start getting ready.

Hence, while I do believe we should not overreact in the short term, I also believe that the long term implications of these new technologies are extremely important, and that it is essential to identify those implications and prepare to deal with them.

Let me suggest a few of these long term implications.

First, e-money and e-banking are fast making geography irrelevant. You hear that so much you might not have stopped to think what it means, so let me repeat it. Geography is becoming irrelevant.

Unfortunately, while geography may be becoming irrelevant from the standpoint of business operations and communications, it's still very much a part of the laws and regulations that govern the provision of financial products and services in this country.

Indeed, the laws and regulations governing our banking system -- and much of the rest of our financial services system -- are integrally tied to geography. Geography determines much of what both national and state banks can and cannot do. Geography drives much of the allocation of responsibilities between different regulatory bodies -- not only in banking, but also in insurance, securities, and other financial services areas. Geography has a lot to do with the protections consumers of financial services enjoy. Geography has a lot to say even about the very enforceability of the commercial transactions that constitute the business of financial services.

So on the one hand, we have the commonplace observation that new technologies are making geography irrelevant. But on the other hand, the legal structure that governs our activities as regulators and the activities of the institutions we regulate still has geography at its core.

What conclusions should we draw from this juxtaposition? Let me suggest several. First, we as regulators and policy makers have a lot of work ahead of us if we are serious about bringing our financial system into step with these emerging realities of

the marketplace. This task -- far more than any of the proposals that are now or have recently been debated in Congress -- constitutes the real work of modernizing our financial system.

In addition, this task is international in scope. These technologies break down not only state barriers, but national barriers as well. To bring order out of the world that will be created by these new technologies, international cooperation will be necessary.

A second long term implication that will flow from e-money is that payments and banking as we know it will in fact be fundamentally changed.

With each successive generation of computer hardware and software, e-money and e-commerce are becoming more user friendly. It is also almost a truism that as younger generations enter the banking system, they will become increasingly attuned to relying on technology to conduct their personal and business affairs. Moreover, as computing speeds increase and costs decrease, paper-based, physical delivery systems of financial products will become increasingly less attractive.

Accordingly, what is viewed as something of a curiosity today -- banking on the Internet -- could well become commonplace in the future, as will the use of smart cards in place of much of paper currency and coins.

No, branch banking will not end tomorrow and some branches may exist for generations. However, for the most part, and most probably within our lifetimes, we will be looking at a banking and payments system that will allow us to conduct most financial transactions electronically -- paying for consumption and making investments. Some entity will help us with these intermediation functions. It might well be a sophisticated bank, or a small local bank, or perhaps even a software company. The winner will depend upon who is the safe, efficient, sophisticated provider.

Similarly, in terms of the financial and financially-related products we want -- credit, insurance, access to markets, advice, money management etc. -- banks may well be the providers of choice. However, whether they are will depend upon the degree to which they are able to compete with other providers. No matter what, consumers should benefit from that competition.

A third implication of increased reliance on e-cash and e-banking is that it could bring about fundamental changes in our lives that go well beyond the immediate changes in banking and commerce. Consider the advent of the automobile -- hailed by virtually everyone as a marked advance over the horse drawn carriage. But the changes wrought by the automobile in terms of where and how we live and work have been more profound than a mere change in modes of transportation. I suspect the same

may well be true of electronic banking and commerce.

Questions for Policymakers

Now where does this leave policy makers? On the one hand I am suggesting that the long term implications of the e-money and e-payments phenomena are very far reaching indeed. On the other hand I have noted that in the short term, change is coming more slowly than the current hype would lead us to believe. Moreover, we are not sure exactly what kinds of e-money and e-payments systems will actually emerge -- nor are we sure the degree to which the technologies themselves or the parties that exploit the technologies will find a way to resolve the potential issues arising from the use of the technologies.

In this current state of uncertainty and opportunity where the outlines of real products are just beginning to emerge, I strongly believe it is essential for any responsible policy maker to expend a great deal of effort understanding well the emerging technologies, potential new products and issues they present. I also believe it is incumbent on any responsible policy maker to exercise discipline in not rushing to make new rules until there is a genuine need to do so.

E-money and e-payments will be an area of evolving technology that holds very great promise -- not just for those who take advantage of the new technologies -- but also for those who will be employed by what could well be an extremely important new area of industry and commerce for this country. Inappropriate and excessive regulation can badly damage the promise that these new technologies hold.

Having said that, a disciplined approach to regulation and supervision must not become code word for regulatory laxity. It is quite likely that as the precise forms of these new products and services emerge, new laws and regulations will be needed. Accordingly, it is essential that government continue to be aggressively on top of new developments so that, when it becomes necessary to act, it can do so with a scalpel and not a meat ax.

Staying on top of the issues that the new technologies present is no mean feat. There are plenty of serious issues. Let me share with you a number of the issues that we have been considering in our Treasury coordination efforts. I tend to group these in terms of near, medium and longer term issues.

Near term issues include:

Potential criminal activity: We are considering the degree to which new payments systems give rise to financial crimes such as counterfeiting, money laundering, theft, fraud (including tax evasion), and others. We are focusing particularly on the potential severity of any e-money related criminal activity and steps that could be taken to contain this activity.

Consumer issues: Do these technologies present the consumer with any meaningful risks? If so, what are they and how significant are they? What disclosure if any is necessary to ensure that consumers are aware of these risks?

Safety and soundness issues: What risks does issuing e-money and/or engaging in financial activity on the Internet present? How significant are these risks? And, how can they be best dealt with? If we need to regulate banks in terms of safe and sound participation in e-payments issues, do we need to regulate non-bank players as well?

Medium and longer term issues include:

Access to credit and services issues: To what degree will the new technologies increase or decrease access to credit and other financial services for low and moderate income Americans?

Geography-based issues: A successful e-money system will require a greater degree of certainty than we have today as to who is liable where, and under what law. And, we are going to have to resolve these questions not just domestically but internationally.

Payments system issues: To what degree will a robust e-money system present risks to our payments system? What implications are there if any for systemic risk? What implications are there for measurement or influence over the money supply?

And finally seignorage issues: Are there any material seignorage issues with respect to this technology, particularly given the amount of U.S. currency in circulation abroad?

Conclusion

Whether near term or longer term, it should be emphasized that these are all very real and important issues that have to be considered with very great care as the e-money phenomenon continues to develop -- and it will develop. At the same time, as I noted earlier we must use genuine discipline to make sure that we understand this area well, that we do not act until we are sure we are dealing with genuine problems, and that when we do act, we make sure we are doing so in the most effective and efficient way possible.

If we as policy makers do exercise care and discipline, the growth of e-money and e-payments can proceed in a way that is fair, safe and dynamic. Moreover, it is an area where participating in the dynamic change and growth, as opposed to unnecessarily impeding it, will yield very great benefits for consumers, business and our national economy.

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