Insight

Debunking Debanking

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Executive Summary

- Fair access initiatives by the federal financial regulators and Congress are seeking to make debanking – referring to the banking practice of closing accounts with little or no warning – illegal.
- These policies fail to consider that debanking nearly always occurs at the instigation of federal regulators exerting pressure on banks to work with certain legal customers and not others.
- Banks are perfectly placed to make risk-based lending decisions, but successive administrations have proven incapable of resisting the urge to advance various policy goals by seeking to determine whom banks bank.

Introduction

In December 2024, Marc Andreessen, general partner of venture capital firm Andreessen Horowitz and former co-founder of Netscape, appeared on the Joe Rogan podcast and noted an epidemic of crypto start-ups that had been "debanked" – having had their bank accounts closed with little or no explanation. Despite precipitating significant conversation in the media and in Congress, debanking is not a new phenomenon. Administrations have long sought to exercise control over financial markets by favoring or disfavoring certain industries in order to meet certain policy goals. These artificial constraints on the operation of competitive markets – and governments picking regulatory winners and losers – always lead to adverse outcomes and increased prices for consumers.

Although the impetus for debanking efforts nearly always flows from government, banks and other financial services actors have borne a disproportionate amount of blame for account closures. Both the Senate and the House of Representatives are currently considering fair access legislation that would guarantee access to traditional banking services to all legal customers and enact strict penalties for banks that engage in debanking. The result of these initiatives would be an increased compliance burden for banks coupled with a punitive system of penalties for breach – all to address a problem created by politicians and bank supervisors.

A History of Debanking

Banks spend billions of dollars and millions of hours determining who they will and will not provide banking services to. Debanked customers fall into one of two categories: the illegal and the uneconomic. First, banks work with law enforcement under the Bank Secrecy Act to detect and deter money laundering, terrorist financing, and financial flows from other illegal activities, and the regulatory framework places a heavy burden of responsibility on banks to get this right. Second, as private actors, banks should be free to not engage with customers that are an economic liability – clients with very low credit scores, where there is a high risk of delinquency, or extremely limited opportunities for a return on investment. Some proponents of relatively lax banking regulations go further and note that access to credit is not a constitutional right – banks should have the opportunity to decline a customer without stating a reason.

Banks must work with their regulators and supervisors, however, and this is where a third category of debanked customer arises: the politically disfavored. In modern times, this reached its apogee with the Obama Administration's Operation Choke Point. Starting in 2013, banks were allegedly pressured by the Department of Justice and federal financial regulators to cease the provision of services to firearm dealers, payday lenders, and other legal businesses, ostensibly for the high risk of fraud these businesses presented. Banks, of course, are entirely capable and in fact much better placed to identify the economic risks of the customers they do or do not contract with. Instead, the program seemed to represent a "thinly veiled ideological attack on industries the Obama administration doesn't like."

Despite the backlash to Operation Choke Point, the Biden Administration seemed to simply repeat the same procedure beat for beat when in 2024 the Federal Deposit Insurance Corporation (FDIC) identified crypto companies as high risk, leading to the "over thirty" examples of crypto firms identified by Andreessen as having been debanked. Senator Cynthia Lummis, (R-WY) in a hearing on debanking, noted that the Federal Reserve had instructed examiners to consider "controversial activity or comments" as grounds for debanking. The Trump Administration reversed this guidance but went further by seemingly indicating that crypto "must" be banked. From an economic perspective, such an approach represents significant risk, as exposure to crypto assets was a key factor in the bank failures of 2023. From a policy perspective, government dictating with whom banks must engage is no different from dictating with whom they must not. Governments cannot be in the business of picking regulatory winners or losers – and that is the concern of critics of fair access legislation.

The Promise and Threat of Fair Access

In early 2021, the first Trump Administration's Office of the Comptroller of the Currency (OCC) announced a final rule to prevent debanking. The Fair Access to Financial Services rule would require any OCC-regulated bank holding more than $100 billion in assets to make financial services available to all "in its geographic area," and "on proportionally equal terms," forbidding banks from denying services to customers on anything other than a quantitative basis. The rule saw significant pushback from industry, with the most notable criticism being the inability of banks to consider reputational risk and other non-quantifiable factors in making lending decisions. The OCC paused the rule in the first few days of the Obama Administration, but certain states have since enacted similar laws, most notably Florida and Tennessee.

Senator Kevin Cramer (R-ND) and Representative Andy Barr (R-KY) introduced legislation to codify the OCC's approach in 2021 and 2023. Banks found to be in breach of the Fair Access to Banking Act could potentially see the revocation of their access to deposit insurance, the discount window, and other necessary aspects of modern banking. How odd that the bill sponsors believe the appropriate response to a bank debanking certain customers would be penalties leading to the likely shuttering of the entire bank, thus debanking all their customers.

Capitalism at its core is based on the benefits provided by market incentives. The appropriate role of government should be to encourage the growth of companies in providing the products and services to whatever interest groups are determined by shareholder demand. Instead, increasingly strident demands from either end of the political spectrum seek to tell financial firms what products they should offer, and to whom. The efficient flow of goods and services around markets requires choice. Private actors should be able to choose with whom they will do business. Any restrictions on the ability to choose will necessarily harm consumers the most, particularly where those restrictions are in excess of the limits already placed on their activities by regulators and the markets.

Marc Andreessen noted some 30 companies in his experience that had been debanked by the Biden Administration. It is worth noting that evidence as to the actual existence of debanking remains largely anecdotal – it is simply not obvious that a significant enough population of the aggrieved exists to justify a legislative response.

Conclusions

While banks might not be interested in politics, politicians remain very interested in banks. If debanking exists – and the true scope of the issue may be overblown – it exists as a result of the direct interference of government. Making debanking illegal and punishing banks for simply following the heavy-handed "advice" of supervisors, regulators, and administrations is farcical and mildly Orwellian. A government solution today to a government problem created yesterday that punishes free markets for executing government's will should not be preferable to simply checking ideological and social goals at the door.