

September 25, 2019

Statement for the Record

On behalf of the

American Bankers Association

before the

Banking, Housing, and Urban Affairs Committee

Of the

United States Senate

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Chairman Crapo, Ranking Member Brown and Members of the Committee, the American Bankers Association (ABA) is pleased to submit this statement for the record on the important topic of Facilitating Faster Payments in the United States. The ABA is the voice of the nation's \$18 trillion banking industry, which is composed of small, mid-size, regional and large banks that together employ more than 2 million people, safeguard \$13 trillion in deposits and extend more than \$10 trillion in loans.

We appreciate the interest of the committee in examining this important and timely issue. ABA has been a strong advocate for real-time payments in the U.S. We believe every bank in the country and their customers will benefit from a seamless and ubiquitous system. As the committee is aware, on August 5th, the Federal Reserve (Fed) announced its intention to create a faster payments network. The proposed FedNow Services will be a real time gross settlement service. The Fed's decision will help speed the nation's transition to real-time payments, but it will take time to build as it is not expected to be active until 2023 or 2024.

The FedNow network will compete with The Clearing House's Real Time Payments network (RTP), which is now live and can reach over 50% of the deposit accounts in the U.S. The Clearing House has offered RTP since 2017. If launched skillfully, the Fed's new rail could ultimately enhance the adoption of faster payments by seamlessly integrating with other offerings in the marketplace. However, if FedNow does not prioritize certain characteristics such as interoperability with well-established solutions, a flat pricing model without volume discounts, and a strong oversight plan for core service providers, or if it freezes decision-making during a protracted

development and launch period, it could slow the adoption of faster payments and cause confusion and fragmentation.

To move the United States toward an efficient, secure, ubiquitous real-time payment environment without undue delay, ABA believes that market participants should focus on six key issues and capabilities.

Interoperability

The Federal Reserve is proposing to enter a market where another operator already has access to more than 50% of deposit accounts and will continue to grow market share while FedNow is in development over the next 4-5 years. Both systems will be run on a cost recovery basis as non-profit utilities with the goal of achieving ubiquity – connecting to every financial institution in the U.S. Volume is critical so the competing systems must be able to interoperate. The ability to originate a real time payment on one platform and have it be received on another platform is essential to deliver a positive customer experience. Without interoperability, banks would be forced to choose between offering a payment network or networks that cannot reach all people, or operate multiple networks which cannot accept payments from one another. The first choice would result in a fragmented system that would not serve consumers and the second choice would be inefficient and expensive to operate.

Despite a broad-based request from industry during last year’s comment period, the Federal Reserve Notice made no commitment to achieving interoperability with the already existing in-market solution RTP Network on the first day of operation. Further, the Federal Reserve opined that it would be acceptable if “nationwide reach” was attained through multiple networks that were not interoperable.

Interoperability should be the highest priority for FedNow as the Federal Reserve begins system development. FedNow must be interoperable with RTP on day one, otherwise banks would be forced to operate duplicative real-time payment systems in order to service all of their customers. FedNow and RTP should start working today to enable interoperability. Interoperability will make both networks more attractive to the marketplace.

Chartered Financial Institution Access

Banks, as licensees chartered by federal and state authorities and regularly examined for compliance with regulations, are the only participants permitted to access the existing Fed payment systems by statute. This is appropriate due to the importance of protecting consumer funds, data, and privacy. Banks are held to high standards in those areas and also maintain capital reserves to ensure and offer deposit insurance

The Federal Reserve and Congress should protect consumers, financial institutions, and the payment system itself by strengthening the current laws and policies in place to protect consumers and the payments system.

Liquidity Management Tool (LMT)

An LMT would help financial institutions manage fund balances in a “real-time” environment. The private sector TCH RTP solution requires that banks participating in the service prefund their account. There is the possibility that some payments will not be completed if the prefunded balance drops to zero due to there being an imbalance in funds being paid out without offsetting incoming payments. If this happens overnight or on a weekend when Fedwire is closed, then outgoing payments cannot be made by the bank affected. We live in a world that does not stop at night or on weekends and our payment systems should reflect that fact.

The Federal Reserve should implement a 24x7x365 LMT solution as soon as possible. In fact there is no need to link this with FedNow development. The LMT would be a great asset to in-market faster payment solutions and moving the central bank to continuous payments processing is essential for modernizing the U.S. payments system.

Equitable Pricing

The Federal Reserve employs volume discounts for some current payment products like FED ACH. This means prices are lower for banks that transact in bulk while smaller banks with lower transaction volumes pay higher per-unit costs. The FedNow notice provided very little insight into the future pricing structure other than to state that more information would be made available closer to the implementation date in 2023 or 2024.

The Federal Reserve should provide more information regarding the proposed pricing structure and commit to a flat per-transaction pricing scheme without volume discounts.

Core Service Provider Oversight

Community banks rely on technology infrastructure that supports everything from accepting deposits to originating loans, all of which tie into operating the core ledger that keeps track of customer accounts. Three companies control the delivery of core services to approximately 80-90% of community and mid-size banks. Often products like FedNow must be integrated into the core service provider systems to allow banks to offer the service to its customers. This integration process can take time and delay implementation timelines for large technology projects like FedNow. Some core service providers are still working on partnerships with P2P services Zelle and TCH RTP. Implementation of these payment solutions has been slower than projected.

The Federal Reserve must work closely with, and provide close oversight of, the core service providers to ensure that they have all of the specifications and technical requirements they need, when they need it, to ensure that all banks have fair access to faster payments solutions within a reasonable amount of time at a fair cost.

Implementation Timeline

The FedNow notice projects that the first live transaction will take place in 2023 or 2024. This long period of time before processing makes FedNow a less attractive product. Banks that want to offer faster payment solutions to their customers sooner will opt for private sector solutions before FedNow goes live. Or, customers that want to participate in faster payments will move accounts to financial institutions that offer them that access immediately. There is also the possibility that some banks will wait for FedNow, ensuring that their customers will not be able to participate in faster payments for 3-5 years. This potential fragmentation harms the entire marketplace.

The Federal Reserve should strive to get FedNow operational and interoperable on a faster timeline to maximize the number of possible endpoints in the shortest time possible to leverage the network effect and to avoid the possible negative consumer experiences at banks that don't offer timely faster payment solutions.

Conclusion

Thank you for conducting this hearing on faster payments. Congress has the ability to influence the shape of FedNow so it can reach and benefit everyone in the United States within a reasonable amount of time safely and securely. We look forward to working with Congress, the Board, and all of the participants in the payments marketplace to ensure that the payment system becomes faster and stays safe.