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BY ELECTRONIC MAIL (regs.comments@federalreserve.gov)

Board of Governors of the Federal Reserve
System 20th Street and Constitution Avenue NW
Washington, DC 20551
Attn.: Ms. Ann Misback, Secretary

Re: Docket No. OP-1625 – Potential Federal Reserve Actions to Support Interbank Settlement of Faster Payments, Request for Comments

To Whom It May Concern:

This letter modifies, replaces and supersedes our letter to the Board of Governors of the Federal Reserve System dated December 14, 2018.

Frost Bank, a Texas state bank ("Frost"), is writing in response to the request by the Board of Governors ("Board") of the Federal Reserve System for comments and input regarding potential actions which the Board may consider taking to promote ubiquitous, safe, and efficient faster payments in the United States by facilitating real-time interbank settlement of faster payments. Frost's prudential regulatory agency is the Federal Reserve Bank of Dallas, and we are providing this response to the Board because we believe it is critically important that the financial services industry continue to work to improve the efficiency and security of the clearing services and interbank settlement services.

This letter summarizes our responses to the Board's request, and attached hereto are more detailed answers to key questions posed at the November 9, 2018 Town Hall meeting.

We do not believe that Real-Time Gross Settlement ("RTGS") service should be pursued by the Federal Reserve at this time. However, we do believe that the Liquidity Management Tool ("LMT") should be pursued and would facilitate real-time interbank settlement of faster payments in conjunction with existing procedures/solutions which are already available through The Clearing House ("TCH"). More specifically, the Real Time Payments ("RTP") network in which TCH has invested to date should continue to be improved to facilitate faster payment processing.

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If the Federal Reserve develops additional real-time payment capabilities beyond the necessary liquidity management functions, doing so may (1) set back or undermine the progress that has been made so far, (2) inhibit the ubiquity that the industry seeks to achieve, and (3) increase financial institutions' operating costs as a result of their need to interface with multiple networks. It is important that Federal Reserve resources be focused on complementing RTP capabilities by way of implementing LMT and promoting or aiding adoption of RTP.

Our recommendation that RTGS not be pursued does not mean we believe the Federal Reserve should not be involved in TCH RTP development. On the contrary, we believe that the Federal Reserve has a very important role to play in working with TCH to ensure a fair and non-discriminatory payments environment for financial institutions of all types and sizes. In particular, the Federal Reserve should help ensure that the concerns of smaller financial institutions are addressed in the continuing development and deployment of RTP.

We appreciate the opportunity to provide our comments to the Board for consideration. Please contact the undersigned at the telephone number or email address above with any questions you may have, or for further information regarding the contents of this letter.

Sincerely yours,

FROST BANK

By: 

Carolyn H. Martin

Senior Vice President/Production Unit Manager

Attachment – Responses to Key Questions from November 9, 2018 Town Hall Meeting

ATTACHMENT

Responses to Key Questions from November 9, 2018 Town Hall Meeting

Questions about potential 24x7x365 RTGS settlement service

- Is RTGS the appropriate strategic foundation for interbank settlement of faster payments in the United States?

No, we do not believe this to be the case.

- Will there be sufficient demand for faster payments to support the development of this service?

There is sufficient demand for development of a service, and such a service (TCH's RTP) is already in development. The financial services industry does not need a second capability as represented by RTGS.

LMT, however, is different. The financial services industry is experiencing substantial and accelerating acceptance of Zelle® and debit network transfers. While the consumer enjoys near-immediate availability of these funds, financial institutions must wait one to two days, if not longer, for settlement of funds. As these types of payments grow and as performance pressure increases as RTP processing is added to the payments system, financial institutions could begin to experience liquidity challenges. That is why the LMT should be developed in conjunction with TCH. Further, Federal Reserve resources and focus should be directed at accomplishing final development of the current established infrastructure, rather than adding another variable that could delay the realization of nationwide ubiquity.

- What is the ideal time to market for this service?

N/A

- What adjustments would the industry and its customers need to make to operate in a 24x7x365 environment?

Recording and reporting of end-of-day balances on a 24x7x365 basis could ultimately result in a regulatory requirement for the financial services industry to update its core systems (DDA and General Ledger) on a seven-day basis. This could significantly increase participating institutions' operating costs. An affordable, and to the extent practicable, automated balance transfer solution could reduce costs and mitigate the aforementioned challenges.

Consumers, however, will see little or no change to their day-to-day banking processes.

- How would the demand for, and the cost of using, this service be impacted by design features such as seven-day accounting, use of dedicated settlement accounts, etc.?

N/A

- Are auxiliary services, such as a payment directory or fraud prevention services, needed for this service?

Encrypted data files are exchanged between financial institutions and the Federal Reserve regularly. Fraud prevention and the maintaining of proxy databases should fall to the financial institutions.

- How critical is interoperability between RTGS services for faster payments to achieving ubiquity?

Interoperability is one of the reasons that Frost takes the position that the current system that TCH has established must be further developed to achieve industry goals. Development of RTGS increases risk of a fractured financial system that is much more difficult to monitor and manage. For example, the potential lack of accepted standards concerning transmission types and contents could significantly limit the ubiquity of faster payments and substantially increase costs to any participating institution.

Questions about potential liquidity management tool

- Will there be sufficient demand to support the development of this tool?

Yes. Liquidity is a key safety and soundness factor, and financial institutions must have the ability to manage liquidity in consonance with RTP. An LMT should be flexible and allow a financial institution to originate a transfer from one account to another and allow automatic transfers based on parameters defined by the financial institution. A combination of those two approaches should be available.

- Would this tool need to be available 24x7x365, or alternatively, during certain defined hours on weekends and holidays?

LMT should be available 24x7x365 to complement RTP.

- Could this tool be used for purposes other than to support real-time settlement of retail faster payments?

Concentration on RTP will expedite development and implementation of the services. Additional applications can be considered after implementation and efficient daily operation are achieved by a sufficient number of financial institutions.

- How much would this tool help foster ubiquitous access to safe and efficient faster payments?

LMT should be developed in tandem with RTP introduction and in a manner that includes input from current and future industry payment services alike. This approach will help to achieve ubiquitous, nationwide access to a safe and efficient faster payments system which is not now universally available.

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