American Bankers Association
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Ann E. Misback
Secretary
Board of Governors of the Federal Reserve System
20th and Constitution Avenue, NW
Washington, DC 20551

Re: Docket No. OP-1664, Potential Modifications to the Federal Reserve Banks' National Settlement Service and Fedwire Funds Service to Support Enhancements to the Same Day ACH Service and Corresponding Changes to the Federal Reserve Policy on Payment System Risk.

Dear Ms. Misback:

The American Bankers Association[1] (ABA) is pleased to submit comments to the Board of Governors of the Federal Reserve System (Board) regarding the potential modifications to the National Settlement Service[2] (NSS) and Fedwire Funds Service[3] (Fedwire). The proposal to extend these services operating hours was made in order to accommodate an additional same-day ACH (SDA) settlement window that will occur late in the afternoon. In order for the private sector ACH operator (The Clearing House) to settle these later transactions, NSS needs to stay open longer. Consequently, Fedwire would also need to extend its hours.

The result of the modifications as proposed will compress the window of time between Fedwire's closing for the day and reopening for the next business day. In effect, there will be less time to adjust balances and address any processing issues than is currently allowed. This Request for Comment seeks input on the effect these extended operating hours may have on participants, including a risk of increasing the frequency of delays in reopening Fedwire.

[1] The American Bankers Association (ABA) is the voice of the nation's $17 trillion banking industry, which is composed of small, regional, and large banks that together employ more than 2 million people, safeguard $13 trillion in deposits, and extend nearly $10 trillion in loans.
[2] The NSS is a multilateral settlement service owned and operated by the Federal Reserve Banks. NSS allows financial institutions that settle for participants in private sector clearing and/or settlement arrangements. The settlement agent designated by the participants within the arrangement, electronically submits settlement files to the Federal Reserve Banks and debit and credit entries are posted to the participants' designated master account.
[3] Fedwire is a real-time gross settlement funds transfer system operated by the Federal Reserve Banks. Financial institutions originate these inter-bank funds transfers and the Federal Reserve Banks debit funds from the sending bank and credit the funds to the receiving bank.

Summary of Comments

ABA supports the modifications to the operating hours of NSS that include an increase to the extension threshold to $2 billion and shortening the required buffer between the closing and reopening of Fedwire from 120 minutes to 90 minutes.

ABA concurs that this proposal meets the Federal Reserve criteria for major system enhancements.

ABA concurs with the required changes to the Payment System Risk Policy associated with extending Fedwire operating hours an additional 30 minutes.

Background

In 2018, a Nacha proposal was passed to add a third SDA window creating an opportunity for financial institutions to submit SDA transactions by 4:45 pm ET with settlement at 6:00 pm ET. This is especially valuable for financial institutions and customers residing in time zones beyond the East Coast. In order to accommodate this new window, changes to NSS and Fedwire operating hours are required. The proposed modifications focus on ways to enable an additional SDA window.

The proposal would compress the time between when these systems are closed for the day and when they reopen later in the evening. This means that under the proposal, there will be less time allowed for the use of Fedwire to reposition balances and manage liquidity. Under the current policies, financial Institutions may request an extension to the Fedwire Funds third party cutoffs or Fedwire Funds closing when there is an imbalance in excess of $1 billion. The Board states that these extensions happen approximately twice per month. <u>However, delays to Fedwire reopening only occur approximately only once per year under the current conditions.</u>

	Current Closings/Cutoffs	**Proposed Closing/Cutoffs**
NSS closing	5:30 PM ET	6:30 PM ET
Fedwire Funds third party cutoff	6:00 PM ET	6:45 PM ET
Fedwire Funds closing	6:30 PM ET	7:00 PM
Fedwire Funds reopens	9:00 PM ET	9:00 PM ET

The RFC seeks comments on the possible effects of compressing this window and the possible use of mitigation tools to reduce the risk of additional delayed openings of Fedwire.

NSS/Fedwire Closing and Cutoff Analysis

The proposed changes extend the operating hours of NSS by one hour and Fedwire by 30 minutes, thereby compressing the time window between the closing and reopening of Fedwire from 150 minutes to 120 minutes. Existing Board policy requires that there be a two hour gap between the closing and opening of Fedwire. The compressed window reduces the amount of time for financial institutions to manage their balances and overcome any technical challenges that may arise. Financial institutions will be required to modify their operating procedures to meet the tighter timeline. The shorter time frame may also result in an increase in the number of extension requests to keep Fedwire open for financial institutions to facilitate discount window loans or subsequent overnight overdrafts.

Currently, extensions to the Fedwire Funds third party-cutoff can be requested only if the deficit exceeds $1 billion. These extensions typically take about 30 minutes and usually do not result in delays because they are resolved by 7 PM and the two hour period between the closing one day and the opening of the next, at 9 PM is not breached.

Under the proposed modifications and the Board's current two hour period policy, any extension of Fedwire beyond 7 PM would result in a delayed Fedwire reopening for the next day. The Board projects that this would result in opening delays 24 times per year, far more than the once per year experienced currently.

Many large financial institutions provide Fedwire services to their customers to make transactions at the opening of each day that are often in conjunction with the opening of Asian financial markets. Any delays in Fedwire reopening are serious matters that interfere with financial institutions providing services to the customers. The potential of having Fedwire delayed twice per month is not acceptable.

Risk Mitigation

The Board proposes three options that would reduce the risk of Fedwire opening delays:

1. Increase the current $1 billion threshold needed to make an extension request. This level has not increased since 1997. The Board estimates that increasing the threshold level to $5 billion would reduce the number of extension requests in half. Making this change, the Board estimates, would reduce the number of expected delayed openings to 12 per year.
2. Change the policy requiring a two-hour window between the closing of Fedwire and its reopening for the next day to 90 minutes. This would allow Fedwire extensions that are 30 minutes or less to occur without delaying the reopening at 9 PM. The Board estimates that this would reduce the number of delayed openings to around five per year.
3. Implement both changes 1 and 2. Increasing the threshold for making extension requests to $5 billion and shortening the period allowed between the closing and reopening of Fedwire would decrease the number of delayed openings to approximately three per year.

ABA Recommendation Regarding NSS/Fedwire Closing and Cutoff

ABA recommends increasing the extension request threshold to $2 billion <u>and</u> reducing the two-hour window between the closing and reopening of Fedwire to 90 minutes.

The $1 billion threshold remains unchanged since it was established 22 years ago in 1997. If the threshold were adjusted based on the Consumer Price Index[4] that figure would change to $1,609,100,000. ABA recommends raising the threshold to $2 billion, higher than the existing limit, but

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[4] U.S Department of Labor, https://www.bls.gov/data/inflation_calculator.htm

lower than the Board proposal. This will reduce the number of smaller extension requests, but still allow requests for larger imbalances to be made.

Reducing the two-hour window will allow 30 additional minutes for the reduced number of extensions to be processed. The Board has stated that this is usually enough time to complete them. Financial institutions will need to refine their operating procedures to accommodate this compressed window, but that is preferable to having an increase in delayed openings.

The combination of these two changes would reduce the number of extension requests and allow more time to address those that are made. The result would be to lower the number of expected opening delays to less than five depending on the mitigating effect of the threshold increase. The effect of this proposed policy should be monitored closely and if the results in practice are higher than the policies should be revisited promptly.

Major Service Enhancements Analysis

When new payment services or major enhancements to new services are considered by the Board, three criteria must be met:

1. Costs must be recovered over the long run; and
2. The service must serve a clear public benefit; and
3. The service must be one that the other providers cannot be expected to provide with reasonable scope, effectiveness, and equity.

The Board expects to incur costs when making the initial changes and with additional staffing to manage the extended work day. The Board expects the initial technical costs to be minimal and to recover those costs, and the ongoing costs, through the existing fees charged for NSS and Fedwire.

These enhancements will enable a third SDA window to be established in the late afternoon on the East Coast allowing more time for all financial institutions to utilize the service. This is valuable because transactions such as late payroll submissions as well as business to business payments, and consumer to business payments can be completed later in the day.

There is no other provider of services similar to NSS that manages debits and credits to and from financial institutions. NSS settles The Clearing House's privately operated ACH transactions. Without the changes to the NSS and Fedwire the third SDA window could not be offered.

ABA Recommendation Regarding Major Service Enhancements

ABA concurs that the NSS and Fedwire changes meet the criteria for the Board to approve this major enhancement.

Payment System Risk Analysis

Federal Reserve Policy on Payment System Risk (PSR Policy) establishes "posting rules" when applying debits and credits tin financial institutions accounts for different payment types. These rules determine if a financial institution has a positive or negative balance (daylight overdraft). When certain daylight overdrafts occur, interest charges are assessed using a formula that assumes the current 21.5 hours a day that Fedwire is open. When the length of the operating hours change the formula must change.

Under the proposal, Fedwire operating hours would be extended by 30 additional minutes or 22 hours a day, resulting in the effective daily rate increasing from 0.004479 to 0.004583, or an increase of about 2.4%. These calculations are made each minute over the newly extended day and the net result, excluding small overdrafts that are waived would result in a net increase of less than 1/10 of one percent.

ABA Recommendation regarding Payment System Risk Analysis

ABA concurs with the proposed changes to the PSR Policy regarding daylight overdraft calculations.

Conclusion

ABA appreciates the opportunity to present its views on the Board's Request for Comment on potential modifications to the NSS and Fedwire systems to enable a third SDA window. ABA supports the proposed enhancements with the modifications noted in this letter and we urge the Board to closely monitor any increase in the frequency of delayed openings of Fedwire to determine if additional modifications are warranted. Additionally, we encourage the Board to issue final guidance on these changes as soon as possible to allow financial institutions adequate time to make any needed operational adjustments.

Sincerely,

Stephen K. Kenneally
Senior Vice President, Payments