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November 7, 2019

VIA EMAIL: regs.comments@federalreserve.gov

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

RE: Federal Reserve Actions to Support Interbank Settlements of Faster Payments [Docket No. OP-1670]

Dear Secretary Misback:

The National Association of Convenience Stores ("NACS") and the Society of Independent Gasoline Marketers of America ("SIGMA") (collectively "the Associations") submit this letter in response to the Board of Governors of the Federal Reserve System's ("Fed" or "Board") notice and request for comments ("Notice") regarding its forthcoming payments service, the FedNow Service ("FedNow" or "Service").[1] The Associations applaud the Fed for its decision to update the nation's payment infrastructure to support faster and more efficient payments and especially support its choice to create a Service that operates in real time: 24 hours a day, 7 days a week, and 365 days a year. As described in the Notice, faster payments will improve cash flow and reduce costs of payments for small businesses, like the Associations' members.[2] Furthermore, the Associations support the Fed's decision to administer FedNow rather than cede control of the Service to private industry, which has been historically anticompetitive.

More in-depth comments on the Board's Notice can be found below.

I. BACKGROUND

A. The Associations' members process 75 billion payment transactions per year, yet the industry is made up predominately of small businesses that operate on narrow margins.

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[1] Board of Governors of the Federal Reserve System, Notice and Request for Comment, *Federal Reserve Actions to Support Interbank Settlements of Faster Payments*, 84 Fed. Reg. 154 (Aug. 9, 2019), https://www.govinfo.gov/content/pkg/FR-2019-08-09/pdf/2019-17027.pdf [hereinafter "Notice"].

[2] Notice *at* 39298.

The convenience store and fuel retailing industry as a whole operates more than 153,000 stores across the United States.[3] In 2018, the fuel wholesaling and convenience industry employed more than 2.375 million workers and generated $654.3 billion in total sales, representing more than 3 percent of U.S. Gross Domestic Product.[4] Because of the number of fuel and other transactions in which the industry engages, fuel retailers and marketers handle approximately one of every 30 dollars spent in the United States. Convenience stores serve about 160 million people per day—around half of the U.S. population—and the industry processes nearly 75 billion payment transactions per year.

Nevertheless, the convenience store and fuel retail industry is truly an industry of small businesses. Approximately 63 percent of convenience store owners operate a single store. The retail convenience store and fuel market is one of the most competitive in the United States. The Associations' members operate on small profit margins (around 1.7 percent) and are unable to absorb incremental cost increases without passing them on to consumers. In 2018, industry credit card fees eclipsed pretax profits for the first time since 2014: the industry paid $11.1 billion in card fees compared to $11 billion in pretax profits. In fact, swipe fees associated with payment card transactions are the second highest operating expense for convenience stores—second only to labor.

B. The United States payments system has been historically inefficient and anticompetitive—and it is lagging behind other countries.

Today, traditional payment methods, including cash, checks, credit cards, debit cards, and ACH payments, are used widely throughout the United States. Yet, these payment methods are not fast enough to meet the needs of the modern economy. Unsurprisingly, therefore, the U.S. payments system is becoming outdated while the systems in other countries, which have focused on faster payment technologies, advance. According to the FIS, 54 countries currently have real-time payments systems—an increase from 40 countries since just last year.[5] The FIS report goes on to explain that those nations have fostered financial innovation by supporting faster payments and marketplace competition.[6] The implication is clear—the U.S. must create a nationwide real-time payments system to be competitive, efficient, secure, and innovative.

Historically, however, systems in which the Fed has not been an active participant (e.g., the payment card marketplace) are notable for their anticompetitiveness, inefficiency, opacity, and fraud. In systems where the Fed has been an active participant (and service provider), such as the automated clearinghouse ("ACH") system, the system is marked—in contrast—by cost and process efficiency,

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[3] NACS is an international trade association representing the convenience store industry with more than 2,100 retail and 1,600 supplier companies as members, the majority of whom are based in the United States. SIGMA represents a diverse membership of approximately 260 independent chain retailers and marketers of motor fuel.

[4] All of the data points in Section I. A. come from the NACS, State of the Industry: Annual Report (2018).

[5] *See* FIS, Flavor of Fast Report 2019, Global Highlights, *available at* https://www.fisglobal.com/flavors-of-fast; *see also* Flavor of Fast Report 2018, *available at* http://empower1.fisglobal.com/rs/650-KGE-239/images/FLAVOR-OF-FAST-Report-2018.pdf?mkt_tok=eyJpIjoiT0RRNU1qVTFNbVkwTldSayIsInQiOiJBeFp6K29BTEJHZGdwR3Q3ZWRiRmpHUllldFJpYytTOXRpcmF2a3MxVUV5anNcL0RnUlRNZElwdHI1UkNpdkFPVUpZQTJ2YTN0ajIwNnFXdGFGeFJDVEdlVkh2cmNMRnlweTF5K2V5U1wvWlY0Y2IxTzQ3OXZ6TG5JZHllIcUxpbnQwIn0%3D.

[6] *Id.,* Flavor of Fast Report 2019, Open APIs and New Services.

competition, and transparency. The U.S. cannot and must not depend on the already dominant, incumbent financial services market players to drive faster payments innovation—only the Fed can make this happen effectively for it is the only entity that has the right incentives to accomplish such a transition and do so without using its role to block healthy market competition from the marketplace.

II. COMMENTS ON THE FEDNOW SERVICE

Updating the nation's payment system so that it can process real-time transactions would benefit the market and the broader economy. As such, the Associations support FedNow and offer these comments for consideration.

A. FedNow's interoperability will be critical to ensuring it achieves ubiquity.

A successful transition to a faster payments system, like FedNow, will depend on its ubiquity and accessibility. The best way to achieve ubiquity will be to ensure platform interoperability. Without platform interoperability, FedNow will not result in the universal adoption that is necessary to upgrade the nation's payments system. As the Board itself notes, no single private-sector provider can provide ubiquity.[7] The Service's interoperability, however, will ensure broad adoption and marked increases in the volume of faster payments rather than the need for every financial institution to transition to its own limited system.

The reason for this is supported by the ACH experience: when a system is interoperable, many different service providers can compete with one another for market share. Then, institutions that are unlikely to develop such services on their own (i.e., smaller financial institutions and retailers) will nonetheless drive adoption of the service among their account holders because they will have the ability to choose the optimal provider of settlement services. Furthermore, the Board should consider future-looking interoperability (i.e., interoperability vis-à-vis FinTech, virtual currency providers and other market innovators) as well. In this way, the Fed will encourage innovation by increasing the likelihood that Service will continue to evolve as technology advances.

B. FedNow transactions should not be limited to $25,000.

The Associations urge the Fed to reconsider its proposed initial value limit of $25,000 for payments settled through FedNow.[8] Limiting transactions to under $25,000 would limit retailers' ability to utilize Fed Now for business-to-business transactions. The Associations' members frequently make payments to suppliers and other services providers for amounts in excess of $25,000 (for example, when a fuel marketer purchases fuel from a supplier). Prohibiting larger transactions through FedNow will require retailers to use traditional payment methods in addition to FedNow, which will delay the adoption of the faster payment system and its uptake by the retail community. Moreover, limiting a retailer's use of FedNow will keep it from the benefits that the Fed has identified as valuable to small businesses.[9]

[7] Notice *at* 39300. "No traditional payment system, including checks, ACH, funds transfers, or payment cards, has ever achieved nationwide reach through a single private-sector provider."

[8] Notice *at* 39317.

[9] *Supra* Note 2.

C. FedNow transactions should be final.

The Associations support the Fed's decision to make FedNow transactions final.[10] In order to develop a real-time payments system, the payments must be just that—finalized in real time. What's more, requiring transactions that "cannot be canceled or revoked" will discourage fraudulent chargebacks to retailers. Consumers have every right to dispute a charge that they did not make. Unfortunately, the major card networks often burden retailers with the amounts of these charges that are found to be fraudulent—even when authorization for the payment was received. That should not be. In 2019, retailers pay an average of $3.13 for every $1 of fraud.[11] These costs include charges from the bank, loss of merchandise, and administrative costs, among others. For small businesses that operate on tiny margins, high fraud costs cut into profit and disrupt cash flow. FedNow can and should operate differently.

D. The Fed should focus on cost recovery as it creates a pricing structure for FedNow.

The primary reason for the Fed to develop and implement FedNow is that the American economy will benefit (many times over) from a faster payment system. Ultimately, whether the Fed achieves cost recovery or not is a secondary issue. What matters in this instance is that the U.S. financial system will benefit far more than what the Fed will ever spend on this effort.

With that in mind, the Associations believe it is imperative that the Fed structure its service pricing for cost recovery only, as it did with the ACH system, rather than a fee structure designed to create a profit. The Fed has shown that it develops infrastructure and operations at a level that is beneficial to other market players, who are willing to pay for those services. And, because financial institutions generally depend on the Board's settlement services *while* competing with each other for market share, history shows that those institutions will likely use FedNow and drive its adoption—which will ensure that the Fed will recover its costs over time.

The ACH system stands in stark contrast to the payment cards market, where the Federal Reserve is not a participant.[12] That monopolistic market, which is dominated by a small number of large payment networks, is notable for its lack of competition, opacity, inefficiency, high costs, fraud, and general lack of innovation. There is no incentive for the private companies that control the anticompetitive payment card market to invest in efficient, real-time payments, unless doing so will allow them to create a dominant position in the faster payments system, because they derive overinflated profits from their dominance of the current payment card market. Any change that might benefit the market but could add uncertainty or risk to the control exercised by the incumbent networks is routinely opposed by those networks and by the financial institutions that derive large fees from the current arrangement.

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[10] Notice *at* 39317.

[11] LexusNexis, 2019 True Cost of Fraud—Retail Edition *available at https://risk.lexisnexis.com/insights-resources/infographic/2019-true-cost-of-fraud-retail-edition*.

[12] Privatized payment systems, if operating in competitive markets, would serve a critical function of balancing profit and market benefit, but this is clearly not the case today. In the absence of truly competitive markets, the public benefit of electronic payments must be established by central authority until competition in private markets can flourish. In this manner, the Federal Reserve successfully implemented ACH, drove adoption and efficiencies, all while creating market space for private associations to compete and improve the system.

E. Fraud prevention services should be a consideration in FedNow's development.

The Associations believe that fraud prevention and data security services are needed for FedNow. If the Service, however, is designed to support interoperability, efficiency, and competition, fraud prevention and data security services will evolve and be pushed by the system's participants, namely financial institutions and retailers, rather than the Fed.

For example, the Fed is considering creating a directory service to connect public identifiers with banking information rather than requiring account information for every transaction. The development of a directory service will protect sensitive consumer data while increasing the uptake of FedNow. The Fed, however, must be cautious when designing the directory service. It is imperative that all market players using FedNow are required to protect consumer data. If the financial services industry has exemptions from data security requirements, retailers will be unfairly burdened and consumers will not be adequately protected.

Furthermore, the Fed must establish general system standards that apply to all stakeholders to prevent fraud. This is how it works in the ACH system, which exhibits remarkably low fraud rates. (Incidentally, this is also the exact opposite of the payment card system, where the Fed is absent, marketplace competition is stunted, and fraud rates are unacceptably high.) Thus, the Board does not need to police fraud for FedNow. In a fair competitive system, market participants will have an incentive to prevent fraud, and will, in fact, develop measures to enhance security.

F. The Fed should continue stakeholder engagement throughout the development process.

The Associations appreciate the Fed's willingness to engage with stakeholders as they consider a faster payments system. As the Fed develops and implements FedNow, the Associations urge the Board to continue to enlist the participation and feedback from a broad range of key stakeholders, including, but not limited to, merchants, consumer advocates, payment processors, financial institutions, financial technology firms, and related financial network service providers.

III. CONCLUSION

The Associations thank you for the opportunity to provide these comments. NACS and SIGMA stand ready to provide additional feedback and assistance should the Federal Reserve have further questions.

Sincerely,

Douglas S. Kantor
Counsel to NACS and SIGMA