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December 14, 2018

Via Electronic Submission
To regs.comments@federalreserve.gov

Ms. Ann E. Misback, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue N.W.
Washington, DC 20551

Re: **Docket No. OP-1625**
City National Bank Comments re: Potential Federal Reserve Actions to Support Interbank Settlement of Faster Payments

Dear Ms. Misback,

City National Bank (“City National”) appreciates the opportunity to provide comments to the Board of Governors of the Federal Reserve System (“Board”) in response to its request for comment (“FR Notice”) about potential actions that the Federal Reserve could take to promote ubiquitous, safe, fast, and efficient payments in the United States. As a premier financial institution long dedicated to providing our clients complete financial solutions, we understand firsthand that payments expectations are swiftly evolving towards methods that are broadly accessible, reliable, and safe, and able to provide results in “real time.” In light of this, we strongly support the Board’s continuing role in promoting faster, safe, ubiquitous payments that can be made 24/7 anywhere in the United States. This includes our support for a liquidity management tool, which could improve the real-time settlement infrastructure for faster payments by mitigating risk that can arise for banks outside of standard business hours. However, we have concerns about the real-time gross settlement (“RTGS”) service model proposed in the FR Notice, which should be further

evaluated and addressed by the Board, before stakeholders can meaningfully assess and determine whether the RTGS model would truly further the goal of a faster payments solution in the United States.

Background

City National Bank is a national banking association formed in 1954. Over the course of its 65-year history, City National has grown and prospered by focusing on its model of client-centric service and relationship banking. In November 2015, when City National merged with Royal Bank of Canada, its asset size was approximately \$35.6 billion. In the three short years since the merger, City National has grown quickly and recently reached \$50 billion in assets as a wholly owned subsidiary.

Our growth from a modestly sized financial institution to one with \$50 billion in assets provides us with the unique perspective of an institution that has always had to think and act nimbly—particularly in the operations context, where maximizing resources, prioritizing key objectives, and focusing on value and efficiency have been key to our success in delivering premier payments services to our clientele.

City National is a significant participant in U.S. payment systems and clears over \$1 trillion in payments annually. City National has also been actively involved with The Clearing House Payments Company (“TCH”), the Board, and the payments industry at large, in the collective effort to develop a ubiquitous, nationwide payment system that would provide faster payments on a 24/7 basis. As you know, the RTP Network is the first and only payment system with real time settlement available at this time, and is owned and operated by TCH. City National is one of the Class AA owners of TCH, and has a strong interest in the success of the RTP Network, both in that capacity and as a U.S. financial institution dedicated to servicing its clients.

Comments on the Proposed Actions

In its FR Notice, the Board requested input on two specific concepts. First, feedback was sought on whether the Reserve Banks should develop a service for the 24/7/365 real-time interbank settlement of faster payments. Second, input was requested regarding a liquidity management tool that would enable the movement of funds 24/7 among Federal Reserve accounts. It is our understanding that the two concepts are being proposed and assessed independently of each other. We address each of them in turn below.

1. The Federal Reserve has a critical role to play in ensuring access to, and the broad adoption of, faster payments in the U.S.; however, launching a parallel public sector RTGS service at this time will slow the industry’s progress towards near-universal reach (“ubiquity”).

A. Launching a parallel RTGS system at this time would set back the industry’s progress.

While the RTP Network is still in its early stages, TCH has indicated that the RTP Network is expected to reach almost 50% of deposit accounts in the U.S. by the end of 2018, and estimated to reach nearly 70% of U.S. deposit accounts by the end of 2019. Beyond that, TCH indicates that it has a credible plan for reaching near ubiquity in the U.S. by the end of 2020, which was the overarching faster payments goal originally articulated by the Federal Reserve when it convened the Faster Payments Task Force (“FPTF”).

TCH reports that most of the largest banks and many more financial institutions in the U.S. are well underway in their integration efforts onto the RTP Network. More importantly, major processors and other technology delivery services have started developing or have already developed critical infrastructure and services for the TCH system, such as fraud detection capabilities.

City National is currently integrating to the RTP Network and is well aware that accessibility to any real-time payment system requires substantial investment of internal resources by a financial institution.¹ A parallel RTGS service would introduce significant complexity to an institution's faster payment service offerings, which translates to additional costs and resources to implement and manage such systems as well. As a result, connection to more than one system may end up being feasible only for the largest depository institutions, impeding the stated goal of ubiquity while placing community institutions at a competitive disadvantage.

If the Federal Reserve announces plans to develop its own system for faster payments, many financial institutions, in particular smaller to mid-sized banks and credit unions, will likely suspend their plans to move forward with the RTP Network and adopt a "wait and see" approach in order to better evaluate the practicalities, costs, participation levels, and interoperability capabilities of the parallel RTGS system. Additionally, vendors and utilities building products and services to integrate with the RTP Network may do the same. This "wait and see" approach by various segments of the industry will be fundamentally at odds with the progress towards ubiquity, especially if interoperability is uncertain (discussed in greater detail in next Section).

Beyond this, the timeframe for platform development is another key consideration. Even if the Federal Reserve had already begun the design process for a parallel RTGS system, technology vendors would still be years away from development of functionalities for the operation of the platform, and financial

¹ The investment includes money, time, staffing, and other resources to ensure that implementation and integration is successful, secure, and in compliance with applicable laws and regulations. Additional considerations include the development of user interfaces, entitlements, potential directory of institutions for each system, determination of the applicable settlement process, fraud detection, technology enhancements, coding, and maintenance, among others that need to be addressed.

institutions would in turn be years away from developing their own back-end operations for the RTGS settlement service.

City National supports the Federal Reserve's objectives in exploring the best means to bring real-time payments to near-universality in the U.S. However, many of the potential benefits referenced in the FR Notice—including accessibility by all financial institutions, greater overall safety and resiliency of the faster payment market, and efficiencies like competition and innovation—are not yet clearly explicated, and may be contingent on interoperability (a key concern we address further in Section 1(B) below). In other words, the benefits and consequences of a separate Federal Reserve RTGS service offering are not clear enough to us, to warrant the introduction of a parallel public option, particularly given the FPTF's goal of reaching ubiquity by 2020.

B. Interoperability is critical, and should drive the Federal Reserve's inquiry.

To the extent the Board decides to develop a parallel faster settlement solution, that solution must be interoperable with the RTP Network. Otherwise, such a solution would be counter to the goals of broad accessibility by all financial institutions and greater overall safety and resiliency of the faster payment market.

We have observed that fragmentation already existing in the faster payments arena (for example, in the person-to-person payment applications space) has created confusion in the marketplace, detracted from progress toward ubiquity, and presented a disproportionate challenge for small and mid-sized community institutions.

Lack of interoperability would also reduce the safety of the real-time settlements systems. From a purely operational point of view, each point of connection to a payments operator increases the risk of a failure. Beyond that, addressing real-time fraud detection on a real-time network is a considerable challenge from an operations and programming/processing perspective. It is not

immediately clear how real-time fraud detection can occur across two payments systems that are not interoperable. Related security issues like authentication, security protocol verification, and dispute resolution considerations introduce new openings for cross-channel fraud and must also be addressed if interoperability between the systems is not a given. Ultimately, interoperability serves to protect depositors, and it is our position that without it, the operational risks become unpalatable for our institution.

Given these issues, we believe it necessary to underscore the industry's concerns that interoperability between a parallel RTGS system and the existing RTP Network system would be highly challenging and resource-intensive, and may not even be feasible. To the extent a parallel RTGS service is being considered, the Federal Reserve should treat this issue as a threshold inquiry that must be further investigated and meaningfully addressed with the faster payments market stakeholders. Proposed solutions to these challenges are likely to require substantial investigation and further study, from technical, functional, and legal (risk-shifting) perspectives, among others. The Board should ensure it adequately considers the time and resources that such evaluation will require. To the extent interoperability cannot be achieved, we believe this further calls into question whether parallel systems are, in fact, beneficial to the market.

C. The Federal Reserve can best serve the payments industry and end-users by ensuring that the ecosystem supporting real-time payments remains robust, safe, efficient, and fair, to facilitate universal access by all financial institutions regardless of size.

The Federal Reserve has been, and we believe will continue to be, instrumental in aiding the broad adoption of faster payments in the U.S. Already, its assembly of the FPTF and its call for comment on the proposals outlined in the FR Notice have brought to light extensive discussion, debate, and proposed strategies

from financial institutions large and small, technology providers, regulatory bodies, and end-users, among others.

Given the considerable resources required to establish a new payments rail, smaller to mid-sized institutions face the greatest barriers to entry; yet, their participation is equally as important as that of the larger institutions in order to achieve ubiquity. With this in mind, we note that TCH has committed to maintain flat pricing regardless of the participant's size, with no volume discounts and no minimum volume requirements, for all RTP Network participants. We commend TCH for this commitment, as these are measures that directly address concerns from smaller or mid-sized institutions. In keeping with that effort, rather than establishing a separate real-time payment system for which interoperability, time frames (e.g., for development and launch), and functionality are currently unknown, the Board may wish to consider whether other efforts (such as the proposed liquidity management tool, educational outreach, industry guidance, etc.) may be more appropriate and beneficial to help ensure that access to real-time payments remains equitable and is not further delayed.

The Federal Reserve may also wish to consider acting as an access gateway for smaller institutions to integrate onto the RTP Network. This could ease integration challenges for community institutions by providing a standardized approach for connecting to the platform, as an alternative to proceeding with a separate parallel system.

Finally, as a related point, we also note that in other countries that have adopted faster payments methods, financial institutions saw a considerable shift away from other legacy payments systems once the real-time payments system(s) became available. The Board may wish to evaluate the expected impact that large-scale movement to a real-time system could have on other payment systems, and consider whether there are ways to leverage the other legacy systems and/or make them more robust in this area as well.

2. We support the development of a liquidity management tool to enable transfers to support liquidity or funding needs during non-standard business hours, such as weekends and holidays.

As the FR Notice acknowledged, the longstanding tradition that banking services are rendered only during “banking hours” on “banking days” has become outdated. City National agrees that a liquidity management tool will improve the level of participation by banks in real-time settlement infrastructure for faster payments. Beyond this, we note that the legacy payment services would also benefit from enhancements to faster settlement and funds availability methods.

As the central bank, the Federal Reserve is the appropriate entity to free up “trapped liquidity” by moving balances in Federal Reserve accounts during non-standard operating hours in order to effect payments during weekends or holidays. Although 24/7/365 availability of such a tool is a worthy objective, even a limited expansion to identified weekend and holiday hours would assist financial institutions in managing fund balances dedicated for settling faster payment transactions.

As a Federal Reserve member Bank, City National is also interested in how the Federal Reserve account, in a 24/7/365 environment, would be balanced on non-business days. Currently, if there are large intra-day charges, there is time to resolve a balance deficiency and the member bank has the ability to go to the market and acquire funds to resolve by the end of the business day. It would be valuable to understand from the Federal Reserve how large settlements on non-business days would be treated under expanded operating hours.

City National encourages the Federal Reserve to consider implementing a liquidity management tool independent of any other actions in consideration to facilitate faster payments. Exploration of expanded hours available through other payment channels should also be considered.

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Conclusion

City National appreciates the opportunity to share its observations and concerns by commenting on this FR Notice. If you have any questions, or wish to discuss our comments or concerns, please feel free to contact the undersigned.

Very truly yours,



T. Richard Shier
Executive Vice President

