

December 14, 2018

Via Electronic Submission

Ann Misback, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551
regs.comments@federalreserve.gov

Re: Docket NO. OP-1625

Dear Ms. Misback:

SHAZAM appreciates the opportunity to comment on Potential Federal Reserve Actions to Support Interbank Settlement of Faster Payments. This is a critical issue facing community financial institutions.

SHAZAM is owned by more than 500 community financial institutions and provides processing services to more than 1,200 community financial institutions. As a result, our over-arching desire is to ensure that ANY U.S. payment system that evolves (card, real-time, ACH, wire, faster payments or future systems) has a methodology in which community financial institutions and their customers can be assured to having open, nondiscriminatory access. Without such access, small to mid-sized financial institutions will become disenfranchised from any proprietary payment systems developed by the largest institutions that have greater means and resources.

SHAZAM is thankful for the efforts that the Federal Reserve has taken to bring the industry together to collaborate on payments system improvements. This work has built a solid foundation for the future of payments. As noted in the Strategies for Improving the U.S. Payment System, the Federal Reserve plays an important role in promoting a safe, efficient and broadly accessible U.S. payment system. We feel very strongly that the Federal Reserve, with its broad powers and capacity, is in the best position to develop, promote and enforce uniform technical and operating standards that should be developed through an inclusive (public and private) structure.

The Federal Reserve need not independently dictate standards, but facilitate how ubiquity, through interoperability, with the Federal Reserve as an operator can be accomplished. It's important that horizontal interoperability, i.e. operability across many varying solutions versus vertical interoperability where essentially many service providers utilize one solution, is developed. The result of such horizontal interoperable efforts will assure nondiscriminatory access and ultimately result in ubiquitous interoperability within the payment system.

We would also ask that the Federal Reserve work to preserve and continue to improve critical elements of existing payment systems that work very effectively today, particularly as they relate to ensuring competition among payment organizations and financial institutions of all sizes.

Our responses to the questions follow:

1. Is RTGS the appropriate strategic foundation for interbank settlement of faster payments? Why or why not?

Yes. RTGS, through the use of master accounts at the Federal Reserve, is the appropriate strategic foundation for interbank settlement of faster payments – especially for the credit push model. However, we don't think the Federal Reserve should unnecessarily limit the use of RTGS to only faster payment systems. As the Federal Reserve considers its role in supporting faster payments, it also should focus on its broader role in providing settlement services to enable an efficient payments system composed of a myriad of payment types, including the Automated Clearing House Network,



wire transfer and card systems. Traditional payment methods are safe, reliable and ubiquitous, but do not settle fast. As a result, a gap has emerged between the capabilities of traditional payment methods and end user expectations for enhanced payment speed, convenience and accessibility. Many financial institutions currently provide (as required through network rules) funds to their customers before funds are actually received through settlement. This process is transparent to the end user, but the situation presents risk to the financial system if settlement is not completed. While there have been recent settlement advances using joint accounts, this should not be the foundational element of an RTGS system. Joint accounts remove liquidity from the system because joint account funds are not readily available to joint account holders. Additionally, joint accounts do not earn interest, cannot be used to meet reserve requirements, and do not qualify for overdraft protection, thus furthering limiting the effectiveness in using joint accounts as a foundational element of an RTGS system.

The benefits of an RTGS system administered using master accounts are numerous, specifically as they pertain to the availability of funds. Implementation of an RTGS system nearly eliminates this risk and funds can be made available to the end user after settlement has been completed. Financial institutions that initiate these payments to others will be able to maintain funds availability to pay for credits they initiate. Implementation of an RTGS system is beneficial to the interest of the public, support the overall U.S. economy, and will significantly advance the payment system.

2. Should the Reserve Banks develop a 24x7x365 RTGS settlement service? Why or why not?

Yes, the Reserve banks should develop a 24x7x265 RTGS settlement service. As noted on the Federal Reserve website, the responsibilities of the Federal Reserve fall into four general areas.

1. Conducting the nation's monetary policy by influencing money and credit conditions in the economy in pursuit of full employment and stable prices.
2. Supervising and regulating banks and other important financial institutions to ensure the safety and soundness of the nation's banking and financial system and to protect the credit rights of consumers.
3. Maintaining the stability of the financial system and containing systemic risk that may arise in financial markets.
4. Providing certain financial services to the U.S. government, U.S. financial institutions, and foreign official institutions, and playing a major role in operating and overseeing the nation's payments systems.

From SHAZAM's perspective, direct Federal Reserve involvement as an RTGS provider is critical and necessary to meet the services outlined in items numbered 3 and 4. Based on the history of the U.S. payment system as well as reviewing faster payments systems that currently exist in several other countries, many of which are driven through central banks, it's necessary that the Federal Reserve provide this service to provide open, nondiscriminatory access to the faster payments system.

Due to the proprietary interests of an incumbent network operator (owned by large financial institutions), it's unlikely that the U.S. payments system will advance in an effective manner consistent with the Faster Payments Task Force's recommendations and assessment criteria without the Federal Reserve serving in an operational capacity that serves smaller financial institutions. A Federal Reserve product offering allows aggregation of transaction volume which will likely lead to reasonable costs for small and mid-sized financial institutions. Historically, this model has proven effective when the Federal Reserve helped advance both check and ACH systems by serving its role as a service provider, specifically serving as an alternative to the private sector operator, The Clearing House. We believe that the Federal Reserve serving in a faster payments operational capacity will have the same positive outcome and help ensure universal interoperability, resulting in



ubiquity. Thus, if a faster payments service provider is unable to directly settle with another faster payments service provider it can settle through the Federal Reserve to ensure interoperability of the transaction.

As noted in the Strategies for Improving the U.S. Payment System, the Federal Reserve plays an important role in promoting a safe, efficient and broadly accessible U.S. payments system. As part of fulfilling this mission, we would ask that the Federal Reserve work to preserve critical elements of existing payments systems that work very effectively today, particularly elements that ensure competition among payment organizations and financial institutions of all sizes. In the current environment, we often find that many of these effective elements are under attack by large payment organizations and financial institutions.

3. If the Reserve Banks develop a 24x7x365 RTGS settlement service,

a. Will there be sufficient demand for faster payments in the United States in the next ten years to support the development of a 24x7x365 RTGS settlement service? What will be the sources of demand? What types of transactions are most likely to generate demand for faster payments?

Yes. There will be sufficient demand for faster payments in the U.S. in the next 10 years to support the service and the demand will continue to increase into the unforeseeable future. While person-to-person payments is the predominant use case today, additional use cases (employer to employee, consumer to business, and business to business) will closely follow suit. Further, the development of this system is necessary to strategically advance the U.S. payment system and the U.S. economy. Instant “anything” is the expectation of many Americans today and will only increase and the financial system (as provider of these services) needs to be able to meet the expectations of speed, convenience, accessibility and security.

Within the U.S. economy there are numerous examples of “faster” services that have proven successful and are considered the norm. Examples include the package delivery system, FedEx, online shopping site, Amazon Prime and electronic communication tool, text messaging. Payments should be delivered in much the same way. The implementation of an RTGS system will help advance payments in such a way that’s difficult for us to currently envision. Additionally, as the costs of funds rise, the demand and interest for faster payments will increase.

b. What adjustments would the financial services industry and its customers be required to make to operate in a 24x7x365 settlement environment? Are these adjustments incremental or substantial? What would be the time frame required to make these adjustments? Are the costs of adjustment and potential disruption outweighed by the benefits of creating a 24x7x365 RTGS settlement service? Why or why not?

Adjustments within the financial services industry to support an RTGS environment would be necessary. However, given that traditional payment methods will remain in place, the operational changes, such as funds management and reconciliation, for institutions that support RTGS will be incremental and analogous to providing any new optional service. When a financial institution is only a receiver, the adjustments will be nominal. And, if the Federal Reserve implements a liquidity management tool, the impact of funds management changes would be lessened.

The initial costs for the financial institutions providing payment services will be recoverable as many of these investments have already been made. In some cases, financial institutions will have large incremental costs because they are lagging in technology. As previously noted, this is a strategic conversation. History tells us that advances can be made through Federal Reserve involvement much like the cash letter presentment currently in place. The success of that initiative allowed numerous check cashing centers to be shut down faster than anticipated and the benefits are still being realized. The same will be true for a Federal Reserve supported RTGS product.



- c. **What is the ideal timeline for implementing a 24x7x365 RTGS settlement service? Would any potential timeline be too late from an industry adoption perspective? Would Federal Reserve action in faster payment settlement hasten or inhibit financial services industry adoption of faster payment services? Please explain.**

The United States faster payments process significantly lags behind than many other countries. As a result, the Federal Reserve needs to take swift and decisive action immediately. The Faster Payments Task Force outlined ubiquity in 2020 as a key goal and many organizations have taken the Federal Reserve's lead and are working toward this goal. The Federal Reserve should have this service available in 2020. Many community financial institutions will only use a tool provided by the Federal Reserve and those institutions who are evaluating their strategic need for faster payments, the 2020 availability date will fit their needs. When selecting service providers, financial institutions want choice and flexibility and the Federal Reserve providing this service will provide a viable alternative.

The current market is fragmented with many unregulated players joining the system every day. Federal Reserve action is in the best interest of the public and its participation will help provide a safe, secure payment system that passes regulatory scrutiny. We believe Federal Reserve action would hasten both the financial services industry and public adoption of faster payment services.

- d. **What adjustments (for example, accounting, operations, and agreements) would banks and bank customers be required to make under a seven-day accounting regime where Reserve Banks record and report end-of-day balances for each calendar day during which payment activity occurs, including weekends and holidays? What time frame would be required to these changes? Would banks want the option to defer receipt of such information for nonbusiness days to the next business day? If necessary changes by banks represent a significant constraint to timely adoption of seven-day accounting for a 24x7x365 RTGS settlement service, are there alternative accounting or operational solutions that banks could implement?**

As noted previously, there would be necessary adjustments. However, these adjustments would not be so dramatic as to place undue burden on financial institutions. Most core systems, whether in-house or service bureau, should be able to handle processing on a 365-day calendar.

The critical change would be the differentiation between a processing day and business day for non-credit push payments. Debit payments require the ability to be returned and if return windows were tied to the business day concept using the federal government calendar there would not be issues; however, if a 24-hour rule were enforced many operational changes would be necessary.

Community banks would likely prefer an option to defer receipt of transactions to the next business day until such time they can fully support a 24x7x365 system. However, options for deferred receipt proved to be ineffective when the Federal Reserve banks tried to establish same-day ACH with optional receipt prior to the NACHA rules changes. While conceptually it could have been effective, not enough financial institutions registered for the service to make it viable.

- e. **What incremental operational burden would banks face if a 24x7x365 RTGS settlement service were designed using accounts separate from banks' master accounts? How would the treatment of balances in separate accounts (for example, ability to earn interest and satisfy reserve balance requirements) affect demand for faster payment settlement?**

We believe the incremental operational burden if the service used accounts separate from master accounts would be nominal. Financial institution employees are experts at reconciling accounts, a separate account under the master would not be a burden if it was treated the same as the master account. All accounts at the Federal Reserve banks should receive interest, satisfy reserve requirements and be treated with zero risk from a risk-based capital calculation.

- f. **Regarding auxiliary services or other service options,**



- i. **Is a proxy database or directory that allows faster payment services to route end-user payments using the recipient's alias, such as email address or phone number, rather than their bank routing and account information, needed for a 24x7x365 RTGS settlement service? How should such a database be provided to best facilitate nationwide adoption? Who should provide this service?**

While directories or other ancillary services are not directly needed for 24x7x365 RTGS settlement services only, these ancillary services can serve an important need in advancing the payments ecosystem. SHAZAM strongly believes the Federal Reserve must provide an open and interoperable directory service (database) that payment and financial service providers and financial institutions can utilize as part of the authentication process and assist in the routing of a faster payment. This must be a consumer level directory that would include such items as email and mobile phone numbers. The directory should support one-to-many relationships such as one email address that works with many providers. The Federal Reserve bank's database should be part of a federated group of databases that are trusted, secure and able to communicate with each other to translate alias information into routable information, including bank routing and account information. Such a directory is vital in establishing interoperability. It would provide all institutions access to real-time payments, regardless of their solution, further encouraging the adoption of real-time payments among all financial institutions.

This directory would allow payments to act as text messaging does now. Individuals can send, and receive, a text message, regardless of the carriers used. If the Federal Reserve doesn't provide a directory service which all faster payment solutions integrate with the ability to determine how to access consumer accounts will be controlled by a single solution provider. Community institutions will lose choice and innovation will be hampered.

Additionally, the payments directory should be channel agnostic. In strategy #4 of the SIPS report, the Federal Reserve committed to fostering greater interoperability of directories for electronic payments. As noted previously, directory services should be made available to multiple payment systems as a key way to foster electronic payments and reduce check payments.

- ii. **Are fraud prevention services that provide tools to detect fraudulent transfers needed for a 24x7x365 RTGS settlement service? How should such tools be provided? Who should provide them?**

Direct fraud prevention services are not immediately necessary. All financial institutions have access to fraud detection services through their current providers. These providers can expand their service to include faster payments. However, to the extent that the Federal Reserve can provide a complimentary, systemic service on top of traditional fraud detection systems, would be beneficial. Such services could include working with providers to develop a shared database of bad actors, providing data identifying fraudulent trends, and blocking services for unsafe payments. These services are not immediately necessary, and development should be de-prioritized in favor of the base RTGS and directory services. However, the Federal Reserve should continue to evaluate the potential benefit of expanding fraud prevention services as faster payments evolve.

- iii. **How important are these auxiliary services for adoption of faster payment settlement services by the financial services industry? How important are other service options such as transaction limits for risk management and offsetting mechanisms to conserve liquidity? Are there other auxiliary services or service options that are needed for the settlement service to be adopted?**



The directory service is critically important to the faster payments ecosystem. Directory services are fundamental to the proper routing of payments and are necessary for interoperability and ubiquitous acceptance.

As previously noted, risk management tools, while also important, don't need to be directly provided by the Federal Reserve. Other providers can logically, and innovatively, provide these services that can enhance competition and lower the cost of processing payments for end users. Other auxiliary services may be necessary as the faster payments ecosystems evolves. The Federal Reserve will be in the best position to help preserve critical elements of the payment system to help ensure competition among payment organizations and financial institutions of all sizes.

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

The question of interoperability is the lynchpin for the kind of faster payments ecosystem the Federal Reserve envisions. It's critical that the Federal Reserve understand that the faster payments system, as it currently exists, is fragmented. This fragmentation restricts access, limits competition and creates a burden for community institutions.

Currently, there are multiple P2P payment solutions in the marketplace and none are interoperable with one another. As an example, P2P solutions like SHAZAM BOLT\$ are often denied from being able to route P2P transactions to DDA accounts of large financial institutions. This effectively requires community financial institution customers to use the large bank solutions — their competitors — to meet customer needs. Obviously, this relationship presents tremendous risk to the community financial institution as they have now, effectively provided their customer information to a consortium of the country's largest institutions. We don't believe it's acceptable for community institutions to have to "default" to using these applications and technologies to meet the needs of their customers.

Some would argue that allowing, or even promoting, this relationship is advantageous as it helps achieve ubiquity. However, if ubiquity is obtained through community institutions being forced to use the large bank consortiums then the public's payment needs are not properly being served. Proper RTGS ubiquity will only be obtained when multiple service providers are required to be interoperable, this will also help fuel payment competition between service providers and ultimately be in the public's best interest. While the private sector may eventually be able to support interoperability through patchwork reciprocal agreements and consolidation (as was done over 18 years with ATM processing) there is no certainty that the private sector will support nondiscriminatory consumer access of the faster payments system. The Federal Reserve is well positioned to initiate the developing of uniform technical and operating standards to assure interoperability of the faster payments system, which in turn will assure the competitive livelihood of small to mid-sized community financial institutions.

h. Could a 24x7x365 RTGS settlement service be used for purposes other than interbank settlement of retail faster payments? If so, for what other purposes could the service be used? Should its use be restricted and, if so, how?

We see no reason why a 24x7x365 RTGS settlement system should be limited to only faster payments. The mission of the central bank is to provide a settlement infrastructure on which the private sector can provide payment services that serve the broad public interest. Clearly, other payment systems (e.g. ACH, wire, card) could also benefit from the existence of an RTGS system. The RTGS system should be channel agnostic with regard to all aspects of the proposal — settlement services, directory services and liquidity management. The Federal Reserve banks and the industry need to continue the expansion of wire transfer hours, add more check presentment windows, and offer several more ACH same-day presentment windows as



transitional steps that can move payments forward prior to the implementation of an RTGS system.

- i. **Are there specific areas, such as liquidity management, interoperability, accounting processes, or payment routing, for which stakeholders believe the Board should establish joint Federal Reserve and industry teams to identify approaches for implementation of a 24x7x365 RTGS settlement service?**

The Federal Reserve has played a critical role as a convener of industry stakeholders to support its mission to foster safety and efficiency of the payment settlement system over the last several years. This, combined with the existing knowledge based of Federal Reserve staff, makes the Federal Reserve well-suited to develop and roll out products to the industry. It's now time to move forward and develop the products that have been requested by the Faster Payments Task Force, provide these products to all financial institutions, and help ensure the continued modernization of the payments industry.

As demonstrated with the Faster Payments Task Force as well as the ACH system there have been numerous examples of successful private-public sector partnerships. Continuing this private-public sector partnership with teams to address liquidity management, interoperability, accounting processes and payment routing (while products are being developed) will only advance the overall payment industry.

4. **Should the Federal Reserve develop a liquidity management tool that would enable transfers between Federal Reserve accounts on a 24x7x365 basis to support services for real-time interbank settlement of faster payments, whether those services are provided by the private sector or the Reserve Banks? Why or why not?**

Yes. The development of a liquidity tool is needed to ensure a consistently positive end user experience and minimize disruptions that could be caused by insufficient liquidity. However, this tool should support all payment systems and not be tied specifically to faster payments. Financial institutions now, and in the future, will have an increased need to manage their liquidity related to settlement. This tool continues to allow the Federal Reserve to provide mechanisms for the settlement of payment obligations between and among financial institutions using balances at the central bank. This will help ensure stability within the payments system.

5. **If the Reserve Banks develop a liquidity management tool,**
 - a. **What type of tool would be preferable and why?**

- i. **A tool that requires a bank to originate a transfer from one account to another**
- ii. **A tool that allows an agent to originate a transfer on behalf of one or more banks**
- iii. **A tool that allows an automatic transfer of balances (or "sweep") based on pre-established thresholds and limits**
- iv. **A combination of the above**
- v. **An alternative approach**

The liquidity management tool should include the functionality listed previously. Most financial institutions will prefer to utilize a tool that allows an automatic transfer of balances (or sweep) based on pre-established thresholds and limits. However, contingencies must be made available to ensure all liquidity needs are met. Many community institutions may want the option to allow an agent, processing organization, the ability to originate a transfer on their behalf. This would help minimize the operational impacts upon community institutions of having a 24x7x365 RTGS system.



- b. Would a liquidity management tool need to be available 24x7x365, or alternatively, during certain defined hours on weekends and holidays? During what hours should a liquidity management tool be available?**

The tool should be made available 24x7x365. The Federal Reserve could start with the tool being available during non-Fed hours and then work with the industry to determine if more availability is necessary.

- c. Could a liquidity management tool be used for purposes other than to support real-time settlement of retail faster payments? If so, for what other purposes could the tool be used? Should its use be restricted and, if so, how?**

As previously noted, a liquidity management tool could also be utilized within other payment systems, including ACH and card. We do not believe the tool's use should be restricted.

- 6. Should a 24x7x365 RTGS settlement service and liquidity management tool be developed in tandem or should the Federal Reserve pursue only one, or neither, of these initiatives? Why?**

Both a settlement service and a liquidity management tool should be developed. Development of these tools should begin immediately. However, we would expect that due to the complexity of developing an RTGS system that the liquidity tool would be available to the industry sooner. The tool could then be used to as noted for other use cases, including ACH, card and wire.

- 7. If the Federal Reserve pursues one or both of these actions, do they help achieve ubiquitous, nationwide access to safe and efficient faster payments in the long run? If so, which of the potential actions, or both, and in what ways?**

Yes. Both actions will be beneficial to achieving interoperability, ubiquity, and most importantly nondiscriminatory access to the payments system. As previously noted, the current system is fragmented, and the industry needs the Federal Reserve to step in to ensure the payments system is safe, efficient and accessible to all eligible financial institutions. We very strongly feel that the Federal Reserve, with its broad powers and capacity, is in the best position to develop, promote, and enforce uniform technical and operating standards that should be developed through an inclusive (public and private) structure. The result of such efforts will assure nondiscriminatory access and ultimately result in ubiquitous interoperability within the payment system.

- 8. What other approaches, not explicitly considered in this notice, might help achieve the broader goals of ubiquitous, nationwide access to faster payments in the United States?**

In addition to ensuring that developed systems (RTGS and liquidity management tool) and ancillary efforts (directory services) are available for all payment types, the Federal Reserve should expand the capabilities and operating hours of the existing National Settlement Service. Today's policy of expanding service hours by reopening NSS after 9:00 p.m. on tomorrow's banking date is not responsive to the needs of the industry to settle later in the same banking calendar day.

We would also ask that the Federal Reserve work to preserve critical elements of existing payment systems that work very effectively today, particularly as they relate to ensuring competition among payment organizations and financial institutions of all sizes. We often find that many of these currently effective elements are under attack by large payment organizations and financial institutions. One example we would offer is Regulation II, which requires two unaffiliated debit card networks for each transaction. This provision should be preserved in the faster payments ecosystem to allow the continued ability of all payment organizations and community financial institutions to effectively compete against larger organizations.

- 9. Beyond the provision of payment and settlement services, are there other actions, under its existing authority, the Federal Reserve should consider that might help its broader goals with respect to the U.S. payment system?**



At a minimum, the Federal Reserve should continue in a public-private sector planning, facilitating, and project managing role to ensure the proper development of an inclusive governance framework and ensure the proper development and enforcement of uniform technical and operating standards. We have seen the tremendous benefits of the Federal Reserve's work as a convener and the Fed should continue to provide a framework for stakeholders to collaborate and aid in the development of rules and standards for the universal sharing of faster payment transactions. We have been encouraged by the positive reception to this concept from many financial institutions and service providers. While it may be possible that some incumbent payments organizations may not participate because they believe it doesn't serve their best interests. Given the Federal Reserve was able to bring both large and small players in the industry together for extensive participation in all efforts to date, we believe the Federal Reserve can continue to be successful serving as planning, facilitating, and project managing capacity.

Additionally, we would ask that the Federal Reserve maintain their current underwriting requirements and that access to its services continue to be provided through a regulated, depository financial institution. Making Federal Reserve services directly available to non-regulated organizations has the possibility to introduce unnecessary risk to an already stable financial system.

Thank you for the opportunity to provide input on this important matter.

Sincerely,

A handwritten signature in black ink that reads "Paul A. Waltz". The signature is written in a cursive, flowing style.

Paul Waltz
President and CEO

