



November 7, 2019

Via Electronic Submission

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-1670; Federal Reserve Actions to Support Interbank Settlement of Faster Payments

Dear Ms. Misback:

BAFT (the Bankers Association for Finance and Trade)¹ respectfully submits the following letter in response to the request for comments by the Board of Governors of the Federal Reserve System (“the Federal Reserve”) on the August 9, 2019 Federal Register notice entitled *Reserve Actions to Support Interbank Settlement of Faster Payments* (“the 2019 Notice”).² BAFT has long supported the development of national faster payments capabilities and shares the Board’s goals that such payments be ubiquitous, efficient, and safe.

In this response, BAFT reiterates and expounds on certain themes in its December 14, 2018 response (“December Comment Letter”)³ to the November 15, 2018 Federal Register notice entitled *Potential Federal Reserve Actions to Support Interbank Settlement of Faster Payments* (the “2018 Notice”).⁴ Such themes include the importance of interoperability of RTGS solutions for faster payments, the need for a tool to manage liquidity in Federal Reserve accounts on a 24x7x365 basis, and the development of a new payments infrastructure that is modern and

¹ BAFT is an international financial services trade association whose membership includes large global and important regional banks headquartered in 61 countries around the world, financial services providers, and a growing number of non-bank and financial technology companies. BAFT provides advocacy, thought leadership, education and training, and a global forum for its members in the areas of transaction banking, including cross-border payments, international trade finance, and compliance. For nearly a century, BAFT has played a special role in expanding markets, shaping legislative and regulatory policy, developing business solutions, and preserving the safety and soundness of the global financial system.

² Federal Reserve Actions to Support Interbank Settlement of Faster Payments, 84 Fed. Reg. 39297 (Aug. 9, 2019).

³ Letter from Samantha J. Pelosi, Senior Vice President, Payments & Innovation, BAFT to Ann E. Misback, Secretary, Board of Governors of the Federal Reserve System re: Docket No. OP-1625; Potential Federal Reserve Actions to Support Interbank Settlement of Faster Payments, December 14, 2018 (“December Comment Letter”).

⁴ Potential Federal Reserve Actions to Support Interbank Settlement of Faster Payments, 83 Fed. Reg. 57351 (Nov. 15, 2018).

flexible. We also provide feedback on the characteristics of the FedNow service as outlined in 2019 Notice.

I. Thematic Comments

A. Liquidity Management Tool

In its December Comment Letter regarding the 2018 Notice, BAFT urged the Federal Reserve to prioritize the development of a liquidity management tool (“LMT”) that would enable transfers on a 24x7x365 basis to all accounts held by a commercial bank at the Federal Reserve.⁵ BAFT argued that the Federal Reserve’s provision of a LMT should be independent from a decision on whether to develop a RTGS service for faster payments.⁶ BAFT stated that,

[i]f necessary, the Fed could initially expand the operating hours of Fedwire or the NSS to something less than 24x7x365 availability to allow banks to manage liquidity. Ideally, the Fed would expeditiously build and launch a separate LMT that would serve as one facet of its holistic, long-term plan to modernize the US payments system. If the Fed does decide to develop a RTGS Service, the long-term LMT should be developed in tandem with the RTGS Service to properly align the design and to facilitate the testing and implementation of both services [together].⁷

BAFT is encouraged by the Federal Reserve’s announcement in the 2019 Notice that it will explore expansion of the Fedwire Funds Service (“Fedwire”) and National Settlement Service (“NSS”) operating hours to permit commercial banks to manage their liquidity. We understand that the aging infrastructure and systemic importance of Fedwire merits additional analysis by the Federal Reserve of the impact of such expansion. However, the Federal Reserve should complete its analysis and begin development of the LMT, whether through the expansion of Fedwire hours or other means, by year-end 2020. The Federal Reserve also should commit to the implementation of a LMT with 24x7x365 availability before or in tandem with the launch of FedNow. As discussed in more detail below, a LMT is a fundamental component of a modern, efficient, and safe faster payments system. Once operational, the LMT tool should be available for the use of any organization holding an individual or joint account at the Federal Reserve and in connection with any financial services offered by the Federal Reserve Banks.

B. Interoperability

BAFT considers two faster payments solutions to be interoperable when a customer of a bank participating in one solution can initiate a transaction to be received by a customer of a bank

⁵ December Comment Letter at 4.

⁶ *Id.*

⁷ *Id.*

participating in another solution in a manner that is frictionless to both end-users. As BAFT communicated in its December Comment Letter on the 2018 Notice, such interoperability between RTGS services supporting faster payments is imperative.⁸ We stated that,

[i]f the RTGS Service is not interoperable with other comparable solutions like [Real Time Payments], banks will have to participate in two or more duplicative and expensive systems or in a single system with the knowledge that a customer's order will fail when the recipient's bank participates in an alternative system. Both options will significantly impede the adoption of faster payments in the US through the introduction of significant cost to and fragmentation of the market.⁹

Most persons and organizations that submitted comment letters on the 2018 Notice took the same position as BAFT with respect to interoperability. Therefore, BAFT is dismayed by the Federal Reserve's statement in the 2019 Notice that it merely "intends to explore ... interoperability."¹⁰ Indeed, to support its assertion that the proposed FedNow service meets the conditions of the Monetary Control Act of 1980 ("MCA"), the Federal Reserve cites several factors – such as "nationwide reach,"¹¹ resiliency/redundancy, and efficiency – that are attainable only through interoperability with the Real Time Payments ("RTP") solution offered by The Clearing House ("TCH").

BAFT strongly recommends that, before expending significant time and resources on the development of FedNow, the Federal Reserve consult with TCH to determine if FedNow can be designed and built so that it is interoperable RTP. Should both organizations conclude that interoperability is technologically infeasible,¹² the Federal Reserve should not proceed with the service because of the complexity, risk, and cost it would introduce into the US faster payments system.

If the interoperability is feasible, the Federal Reserve should incorporate into the FedNow service the amount limits, variant of the ISO messaging standard, operating rules, and method of on-boarding banks that TCH chose for RTP. It should also build "cross-border functionality"

⁸ *Id.* at 6.

⁹ *Id.*

¹⁰ 2019 Notice at 39318.

¹¹ 2019 Notice at 39311. BAFT notes that "accessibility," the first of 35 and a subcomponent of the "ubiquity" category of effectiveness criteria agreed upon by the Faster Payments Task Force ("FPTF") for the evaluation of faster payments solutions, includes characteristics such as the ability to reach any payee, widespread adoption, and interoperability – not "nationwide reach." FPTF, Faster Payments Effectiveness Criteria, January 26, 2016, page 7. Available at <https://fedpaymentsimprovement.org/wp-content/uploads/fptf-payment-criteria.pdf>.

¹² TCH has previously indicated that interoperability with RTP may not be feasible from a **technical** standpoint. Because faster payments clear and settle simultaneously and are processed within seconds on a single platform, interoperability between platforms could slow processing times and introduce settlement risk.

(another subcomponent of the “ubiquity” category of the FPTF effectiveness criteria)¹³ into the design of the FedNow service. Such functionality would support cross-border faster payments, a concept that a few banks in Asia / the Pacific have already proved possible by “connecting” two national faster payments infrastructure platforms through the correspondent banking system.

C. Design of a Modern and Flexible US Payments System

We repeat the belief expressed in our December Comment Letter that the Federal Reserve’s development of a LMT and an interoperable FedNow service should be a part of a greater, long-term plan to modernize and improve the US payments system.

Incremental modifications, like the addition of features or extension of operating hours, to existing systems may acceptable in the short-term. But, the Board and the Federal Reserve Banks should come together to build new and flexible services as part of a holistic plan to modernize and integrate the payment rails that the Federal Reserve Banks currently operate. Any long-term tool or service introduced by the Fed should enhance the resiliency, safety, and soundness of the entire US payment system by, for instance, serving as a contingency to [FedACH or Fedwire] or as the technical foundation for a next generation ACH or wire system. The Fed should align the design with the principles applied to systemically important infrastructures. In addition, given the rapid pace of technolog[ical] innovation, a new tool or rail must be enabled for multiple technology refresh cycles through its operating life.¹⁴

The Federal Reserve acknowledges that the MCA requires the introduction of a new service like FedNow to “yield long term benefits to the public and the economy as a whole.”¹⁵ Accordingly, the Federal Reserve’s decision to enter into the faster payments marketplace should be motivated by the belief that its involvement is necessary to achieve a ubiquitous, safe, efficient, and effective national faster payments system, rather than a desire to compete with the private sector’s existing service. BAFT urges the Federal Reserve to make the improvement of the nation’s payments ecosystem its primary consideration in designing, pricing, and operating the FedNow service and offering ancillary services.

For FedNow to be a viable service when launched, it will need to offer functionality comparable or superior to that offered by the more mature RTP service of 2023/2024. Therefore, the Federal Reserve must continuously monitor the market for and incorporate emerging trends and best practices while also building out its own solution. BAFT recommends that the Federal

¹³ Faster Payments Effectiveness Criteria at 9.

¹⁴ December Comment Letter at 3-4.

¹⁵ 2019 Notice at 39309.

Reserve learn from the experiences of providers and participants in the US as well as other nations to surmount this challenge, reduce the time to market for FedNow, and decrease the number of years required for faster payments to achieve ubiquity in the US.

BAFT's members are located in 61 countries around the globe and include payment infrastructure providers and system operators. Many of our members have participated in the development of a real-time retail payments infrastructure/capability within their respective jurisdictions. Additionally, BAFT recently stood up a working group of members to compare the national faster payment systems of key jurisdictions. This experience makes BAFT uniquely positioned to identify the critical characteristics for inclusion in any potential faster payments solution. We would be happy to share our thoughts with the Federal Reserve as it continues to "convene industry groups and facilitate other outreach forums to gather input on the [FedNow] service."¹⁶

II. Comments on Proposed Features and Functionality

We are cognizant that the Federal Reserve has just begun to conceptualize the FedNow service and that the 2019 Notice provides only a high-level outline of the features and functionality. The Federal Reserve should note, however, that given its Strategies for Improving the U.S. Payment System ("SIPS") Report and leadership of the FPTF, the industry expects that FedNow will meet most, if not all, of the 36 effectiveness criteria for faster payments solutions at the time of its launch. Furthermore, as RTP and faster payments services deployed in other nations continue to evolve over the next 4 to 5 years, banks will come to expect FedNow to include certain additional features considered to be "standard."

Below, BAFT provides its views on the features and functionality of the FedNow service as outlined in the 2019 Notice.

A. Messaging

BAFT agrees that FedNow messages should be based on the ISO 20022 standard and its implementation with respect to faster payments in the United States. RTP and the faster payments systems of several other nations use this formatting. The Federal Reserve should adopt the ISO 20022 Real-Time Payments Group usage guidelines and, when finalized, the Cross-Border Payments and Reporting Plus ("CBRP+") usage guidelines. Adoption would be a major step towards interoperability with other faster payments services.

A request for payment message type should be provided on day one of FedNow's implementation because of the benefit it would bring to the entire US faster payments ecosystem. Such functionality encourages additional end points to use the system and initiate

¹⁶ *Id.* at 39316.

payments. The industry anticipates that RTP will provide this message type by year end, which would be a date 4 to 5 years ahead of FedNow's launch.

B. Settlement, Liquidity and Credit, Accounting Regime, and Business Day

BAFT agrees that the settlement of faster payments in a bank's master account generates less operational burden for a bank than settlement in a separate, dedicated account at the Federal Reserve. Funds in the RTP joint account should be counted as reserves and earn interest, like the funds in a bank's master account, to level the playing field between the faster payments solution of the Federal Reserve and of the private sector.

With respect to the introduction of FedNow, the Federal Reserve should not be tied to decisions of the past. It should consider a LMT available on a 24x7x365 basis to be a prerequisite to the provision of a modern 24x7x365 RTGS service for faster payments. It also should make intraday credit and the discount window available on a 24x7x365 basis to facilitate participants' management of liquidity in their master account and/or RTP joint account.

Similarly, the Federal Reserve should use the transition to a seven-day accounting regime as an opportunity re-align the start and end of the Fedwire/LMT and FedNow business day with the US calendar day. This approach is preferable to that outlined in the 2019 Notice, which would create significant recordkeeping challenges and, potentially, incongruities.

C. Network Access

BAFT supports the Federal Reserve's designation of the FedLine network as the method to connect to the FedNow service because the introduction of a new connection type might create a barrier to participation.

D. Service Pricing

BAFT expects that the Federal Reserve will not engage in anti-competitive pricing practices with respect to the FedNow service.

E. Directory and Fraud Prevention Services

BAFT acknowledges that directories promote faster payments system ubiquity and security. It would be reasonable for the Federal Reserve to build its own directory to support the banks participating in FedNow. The industry and US faster payments system would benefit from the Federal Reserve's leadership in formulating a strategy to link all private sector directories together in a secure manner.

Responsibility for fraud prevention at the end-user level should remain with FedNow participant banks. The Federal Reserve could leverage emerging technology such as artificial

intelligence and its unique vantage point as the FedNow service operator, however, to identify patterns of fraudulent activity across multiple banks or throughout the payments system.

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Thank you for the opportunity to provide comments in response to the 2019 Notice. We appreciate the Federal Reserve's continuing leadership in promoting the development of a ubiquitous, efficient, and safe US faster payments system.

Should you have any questions regarding BAFT's response to the 2019 Notice, please contact the undersigned at spelosi@baft.org or (202) 663-5537.

Sincerely,

/s/

Samantha J. Pelosi, J.D.
Senior Vice President, Payments & Innovation