

## Lael Brainard: Delivering fast payments for all

Speech by Ms Lael Brainard, Member of the Board of Governors of the Federal Reserve System, at the Federal Reserve Bank of Kansas City Town Hall, Kansas City, Missouri, 5 August 2019.

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It is a pleasure to be here in Kansas City with Federal Reserve Bank President Esther George to talk about the future of America's payment system.<sup>1</sup>

Our payment system is a vital part of America's infrastructure that touches everyone. The choices we make about our payment infrastructure today will affect all Americans many years into the future. Today I am excited to announce the Federal Reserve will invest in a new service to help ensure that real-time payments are available to everyone. The Federal Reserve will develop the FedNow Service<sup>SM</sup>, a real-time payment and settlement service for the future.<sup>2</sup> Everyone deserves the same ability to make and receive payments immediately and securely, and every bank deserves the same opportunity to offer that service to its community. FedNow will permit banks of every size in every community across the country to provide real-time payments to their customers.

Today, whether you are relying on ACH, a debit card, or a check, it can take as much as a few days to get access to your funds. With a Federal Reserve real-time retail payment infrastructure, the funds would be available immediately—to pay utility bills or split the rent with roommates, or for small business owners to pay their suppliers. Immediate access to funds could be especially important for households on fixed incomes or living paycheck to paycheck, when waiting days for the funds to be available to pay a bill can mean overdraft fees or late fees that can compound. Similarly, getting immediate access to funds from a sale in order to pay for supplies can be a game changer for small businesses, potentially avoiding the need for costly short-term financing.

Last November, we asked the public about possible actions the Federal Reserve could take to support interbank settlement of faster payments.<sup>3</sup> We received more than 350 comments on a Federal Reserve faster payment service, representing nearly 800 organizations. Fully 90 percent of these comments called for the Federal Reserve to operate a real-time service for faster payments. Support came from a wide range of stakeholders, including individuals, merchants, fintech firms, and banks.<sup>4</sup> Commenters noted that the Federal Reserve would ensure equitable access to banks of all sizes nationwide by operating a real-time service for faster payments alongside the private-sector system. Commenters highlighted the importance of safety in faster payments and noted the Federal Reserve's record of resiliency, especially during periods of stress. Commenters observed that a Federal Reserve real-time retail payment service would increase competition, decrease market concentration, and provide a neutral platform for innovation.

This broad support echoes and expands on the conclusions of the Faster Payments Task Force. Similarly, the U.S. Treasury Department recommended that "the Federal Reserve move quickly to facilitate a faster retail payment system, such as through the development of a real-time settlement service that would also allow for more efficient and widespread access to innovative payment capabilities."<sup>5</sup>

In determining the path forward, we are building on the Federal Reserve's long history of operating payment systems as a core part of the nation's payment infrastructure. Since they opened for business around the country in 1914, as directed by the Congress, the Federal Reserve Banks have provided payment and settlement services—in healthy competition with private-sector providers—to achieve public benefits ranging from resiliency to innovation to equal access. When you look across the current payment infrastructure, whether in check processing, automated clearinghouse (ACH) services, or funds transfers, you will see a Federal Reserve

service operating alongside private-sector providers. The General Accountability Office has concluded that the Federal Reserve's provision of payment services has benefited the U.S. payment system and its users.<sup>6</sup>

The Federal Reserve does not have regulatory authority over the pricing set by a private-sector system or to require a private-sector system to extend the service to banks of all sizes, particularly the last mile. In some other countries, central banks have been assigned the responsibility for regulating payment systems. However, this is not the approach that Congress has taken. Instead, the Federal Reserve's role as an operator has long been seen as an effective approach to promote accessible, safe, and efficient payments in the United States.

Through the FedNow Service, we will provide a foundation for the future—a modern payment infrastructure that allows innovation and competition to flourish and delivers faster payments safely and securely for all. To ensure fast payments are available to everyone, FedNow will be accessible to all banks, no matter the size. Given our long-standing service connections with more than 10,000 banks across the country, the Federal Reserve is uniquely placed to deliver this outcome.

The bar is high when we assess whether the Federal Reserve should provide a new payment and settlement service, as it should be. We have carefully analyzed the criteria of the Monetary Control Act and long-standing Federal Reserve policies, considered the comments provided by a wide range of stakeholders, and studied the experiences of foreign central banks.<sup>7</sup> We are not making this decision lightly. On balance, after carefully weighing important considerations on both sides, we have concluded it is our responsibility to take action in support of a real-time payment infrastructure accessible to all. While we will work hard to stand up the FedNow Service in a timely manner, our most important goal is to achieve nationwide access for all, reflecting our public mission.

### **Building a Modern Payment Infrastructure**

A key foundation of the payment infrastructure is interbank clearing and settlement—the movement of funds and the associated information between banks. Today, the U.S. retail payment infrastructure lags behind many other countries. Europe, Mexico, and Australia have already implemented real-time interbank clearing and settlement capabilities. In contrast, here in the United States, the gap between the transaction capabilities in the digital economy and the underlying payment and settlement capabilities continues to grow.<sup>8</sup>

Early adopters of fast payment services rely on a legacy infrastructure that was not designed to support faster payments. For example, some services offer real-time funds availability to certain consumers, but they conduct interbank settlement on a deferred basis using legacy systems. This type of settlement entails a buildup of obligations—like IOUs between banks—that could present real risks to the financial system in times of stress. These are not resilient long-term solutions for our dynamic economy and the banks that support it.

We are seeing some companies looking to establish a payment system that bypasses our banks and our currency. Facebook's Libra project raises numerous concerns that will take time to assess and address. But one thing is clear: consumers and businesses across the country want and expect real-time payments, and the banks they trust should be able to provide this service securely—whatever their size. To provide everyone with the ability to send and receive funds securely on a 24x7x365 basis, banks need to embrace and invest in real-time innovations, and the Federal Reserve needs to provide a safe and efficient real-time interbank clearing and settlement service accessible to all banks.

We are proud of our strong record of cooperating with and supporting private-sector services, while fostering competition for public benefit. We have provided vital support to the sole private-

sector provider of real-time settlement for faster payments, and we will continue to do so. The Federal Reserve provided a joint account to enable the private-sector operator to offer real-time payments. Moreover, today we are announcing our intent to explore the expansion of Fedwire Funds Service and National Settlement Service operating hours to support the efficiency of the joint account structure for the private-sector real-time gross settlement (RTGS) service and provide broader benefits. That said, the joint account structure, with its requirement of prefunding and settlement on a private ledger, is fundamentally different from the approach the Federal Reserve will use to settle transactions directly between banks.

## **Fostering a Dynamic and Resilient Payment Infrastructure That Serves Everyone**

The Federal Reserve is committed to fulfilling our public policy goals in a spirit of cooperation and competitive fairness. We are pleased that the private-sector faster payment service is in the market, and we see important benefits from the resilient and competitive market that would result from the FedNow Service providing an alternative consistent with the requirements of the Monetary Control Act. The requirement to consider the best way to make our payment and settlement services accessible to banks across the country, along with long-standing principles including cost recovery over the long run, guides our assessment of when the Federal Reserve should engage in the payment system.<sup>9</sup> In setting fees, the Federal Reserve is required by statute to "give due regard to competitive factors and the provision of an adequate level of such services nationwide."<sup>10</sup> I want to share with you some of the analysis—viewed through the prism of our public policy goals of accessibility, safety, and efficiency—that we considered in making today's decision.

Accessibility means serving more than 10,000 banks of varying sizes and missions that are in communities all around the country. It turns out no single private-sector provider of any U.S. payment system has ever achieved nationwide reach on its own, whether it be checks, ACH, cards, or wire transfers. Acting alone, a single private-sector RTGS service will face significant challenges in establishing an accessible infrastructure for faster payments with nationwide reach. In contrast, because of our experience with providing other services, the Federal Reserve already has invested in connections and customer service relationships with nearly every bank, small and large, across the country.

Currently, we provide payment services to nearly all banks either directly or indirectly. With our 12 regional Reserve Banks, we have the capacity to meet the needs of banks serving different communities and with different needs and operating models. For that reason, commenters stated that the Federal Reserve is uniquely positioned to offer nationwide access to a new payment and settlement service for faster payments. FedNow will allow faster payments to reach banks of all sizes and their customers across the country, which is especially important for rural communities, who often struggle with access to financial services.

Guided by our public mission, the Federal Reserve serves the needs of all banks, no matter how small or challenging to reach, and with competitive fairness. In response to our request for feedback last November, several commenters emphasized how much they value the Federal Reserve's mission of providing nationwide access on fair, transparent terms and expressed concern that a sole private-sector RTGS service provider may be less likely to exhibit the same commitment over the long run.

Safety is also vital. If the Federal Reserve does not establish the FedNow Service, there will be a single provider of real-time retail payment services. We are mindful of the serious safety issues associated with a single point of failure, a risk that will rise as faster payments grow. Stakeholders have noted the importance of having access to more than one real-time payment service for back-up purposes in order to provide resiliency through redundancy. In fact, many banks already take advantage of having connections to multiple operators today in check, ACH, and wire services. The Federal Reserve has always had a vital role in promoting the safety and

stability of the U.S. payment system by providing liquidity and operational continuity especially in times of stress. The FedNow Service would allow the Federal Reserve to extend this role into the real-time retail payment market.

Finally, competition will promote efficiency and innovation. The U.S. real-time retail payment infrastructure stands to gain from competition, including through higher service quality and lower prices over the long run, which in turn should support wider adoption.

The FedNow Service will provide a neutral foundation for innovation and competition in end-user faster payment services. In response to the request for feedback, merchants and fintech companies commented that a Federal Reserve real-time retail payment service could broaden the scope for innovation in faster payments. They noted that a single provider that is owned and operated by one segment of the payment industry may focus on a narrow set of use cases that do not reflect the full breadth of possible use cases for faster payments. Recognizing the vibrancy of our payment industry, the addition of the FedNow Service could provide a springboard for broader private-sector participation in the development of innovative end-user services.

## Looking Forward

With the announcement of the Federal Reserve real-time payment service, we are embracing a path that will bring transformative, rather than incremental, change to the retail payment infrastructure in the United States. The FedNow Service will run continuously at all times of the day, every day of the week, consistent with the needs of faster payments and will be designed to process large volumes of payments rapidly.

In the months ahead, we intend to explore a variety of approaches to achieving a real-time retail payment infrastructure with nationwide reach. One such approach might be for different payment services to interoperate by exchanging payments among the services directly. Such interoperability is an important goal that we will pursue as standards, technology, and industry practices change over time, although it is not yet clear whether it will be an initial feature.

The Federal Reserve plans to devote the necessary resources to deliver the highest quality FedNow Service in a timely manner. We are working to streamline our internal processes to move quickly in the market. President George will play an integral role in this new process, and the Conference of Reserve Bank Presidents has pledged its support.

It is important for the Federal Reserve, working with the payment industry, to act quickly in finalizing the initial business requirements of the FedNow Service. We will need to hear the views of payment system stakeholders on the features of the FedNow Service, as discussed in the *Federal Register* notice announced today. We will engage with the industry through groups and forums to finalize the design and features of the service. We hope that these conversations will provide an opportunity for stakeholders to work together to shape the evolution of the U.S. payment system.

Earlier this month, I joined my Reserve Bank colleagues for a visit with bankers and community organizations in Scranton, Pennsylvania, to hear about the biggest challenges they are facing. The head of a bank that has been serving the Scranton area for more than a century told me that for his community bank to remain competitive in its payment offerings, it is vital to be able to rely on the Federal Reserve for real-time payments just as he does for check, ACH, and wire transfer. I appreciate the importance of community banks to the economic health of our communities, and I recognize the role of the Federal Reserve in enabling community banks to offer payment services on a competitive basis. I am confident that by working together with all payment system stakeholders, we can collectively achieve widespread, safe, and efficient faster payments that will benefit all.

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- <sup>1</sup> I am grateful to Susan Foley and Anjana Ravi of the Federal Reserve Board for their assistance in preparing this text. These remarks represent my own views, which do not necessarily represent those of the Federal Reserve Board or the Federal Open Market Committee.
  - <sup>2</sup> [Federal Reserve Actions to Support Interbank Settlement of Faster Payments \(PDF\)](#) (August 5, 2019).
  - <sup>3</sup> Lael Brainard, "[Supporting Fast Payments for All](#)" (remarks at the Fed Payments Improvement Community Forum, Chicago, October 3, 2018).
  - <sup>4</sup> [Potential Federal Reserve Actions to Support Interbank Settlement of Faster Payments \(PDF\)](#), Request for Comments, 83 Fed. Reg. 57,351 (November 15, 2018).
  - <sup>5</sup> Steven T. Murchin and Craig S. Phillips, [A Financial System That Creates Economic Opportunity: Nonbank Financials, Fintech, and Innovation \(PDF\)](#) (Washington: U.S. Department of the Treasury, July 2018), 156.
  - <sup>6</sup> See, e.g., U.S. Government Accountability Office, [Federal Reserve's Competition with Other Providers Benefits Customers, but Additional Reviews Could Increase Assurance of Cost Accuracy](#), GAO-16-614 (Washington: Government Accountability Office, August 2016).
  - <sup>7</sup> Board of Governors of the Federal Reserve System, "[The Federal Reserve in the Payments System](#)" (Issued 1984; revised 1990).
  - <sup>8</sup> FIS Global, "[2018 Flavors of Fast](#)."
  - <sup>9</sup> Board of Governors of the Federal Reserve System, "[Principles for the Pricing of Federal Reserve Bank Services](#)" (Issued 1980); and Board of Governors, "The Federal Reserve in the Payments System."
  - <sup>10</sup> [Depository Institutions Deregulation and Monetary Control Act of 1980](#), Pub. L. No. 96-221 (March 31, 1980).