



November 4, 2019

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

Re: Federal Reserve Actions to Support Interbank Settlement of Faster Payments – Notice
and Request For Comment
Docket No. OP - 1670

Dear Ms. Misback,

Southern Financial Exchange ("SFE"), a payments association with financial institution ("FI") members in Alabama, Arkansas, Louisiana, Mississippi and Tennessee, welcomes the opportunity to submit this comment letter to the Board of Governors of the Federal Reserve System (the "Board"). This is in response to the notice and request for comment ("RFC") regarding the proposal to develop a new real-time gross settlement service called FedNow. While we see value in the FedNow initiative, our membership believes more immediate need is expanding the National Settlement Service ("NSS") and Fedwire operating hours. As explained further below, we urge the Board to not let the FedNow proposal distract from the expansion of the National Settlement Service ("NSS") and Fedwire operating hours.

Summary of RFC

The Board determined that the Federal Reserve Banks ("Fed") should develop a new interbank 24x7x365 real-time gross settlement service with integrated clearing functionality to support faster payments. This service would support FIs' clearing and settlement of end-to-end real-time payment services and provide the infrastructure to promote ubiquitous, safe, and efficient faster payments in the United States.

A synopsis of the proposed credit push environment is as follows:

Sender initiates a payment through their FI, the sending FI validates the receiving account number by sending a message through FedNow. If the receiving FI sends a positive response, payment is made by debiting and crediting the respective Fed Accounts. Sending and receiving FIs are responsible for debiting and crediting customer accounts immediately and for notifying their customers. All transactions are final and irrevocable.

Commentary

Feedback from a sampling of SFE members on this topic indicates the following:

General Observations

- **Strong overall support for FedNow.** Many of our members have strong ties to the Fed and would be concerned if development of FedNow should falter. SFE members believe that the FedNow service can co-exist and extend the reach of faster payments solutions beyond what the private sector can achieve alone.
- **Speed to market is a concern.** The current payments landscape has real-time solutions that have been developed and are gaining momentum. SFE members view the timeline for FedNow discussed in the RFC to reach the market is viewed as too long and believe this timeline may undercut the value of the FedNow solution in creating ubiquity in the market.
- **Fedwire and NSS remain priorities.** SFE membership supports the continued efforts by the Board to modernize the payments industry. However, modernization of Fedwire and the NSS is a more urgent priority for SFE members. The Fed's concerns over FedWire support of Asian Markets, while legitimate, impact development efforts of faster payment solutions. Additional information on this issue is included later in this document.
- **Additional specificity is critical.** Membership viewed the RFC as very general in nature. The Fed appears to lack a solid plan of work to move FedNow forward in a reasonable timeframe. As a result, our membership asks the following questions:
 - Will any regulatory changes be necessary to better support faster payments or is the existing regulatory environment satisfactory?
 - Existing faster payment solutions define "finality of payment" as the point the sender releases the funds, essentially treating these electronic transactions the same as the sender putting cash in the mail. As the volume of immediate payment solutions grow the volume of fraudulent transactions may increase. Should additional consumer protections exist in this environment? Will FedNow facilitate a dispute resolution process?
 - According to a recent Faster Payments Council survey, the vast majority of respondents viewed interoperability between faster payment solutions as "very important". Interoperability has worked well for ACH payments over the past 40 years and offers a path to achieving ubiquity. How will FedNow integrate with current solutions?

- Governance – The private sector ACH governance model has proven successful over the past 40 years. Will this same model or a new governance model and standards be introduced to help achieve and support interoperability?
- The RFC refers to respondents of the previous RFC expressing concern that existing communication channels between the Fed and FIs for Wire and ACH entries are insufficient to support real-time messaging and entry volumes. Can the Fed provide details regarding infrastructure changes necessary to support FedNow?

Modernizing National Settlement Service and FedWire

- SFE members believe that any action on FedNow should not detract from or delay efforts to expand NSS and FedWire and by extension industry efforts to expand the number of windows used for Same Day ACH. In addition, FedWire support of activities in Asian markets creates delays in the development efforts of faster and more efficient payment solutions in the United States – this particularly impacts FIs in the Pacific Time Zone and further west.
- Requests to modernize NSS have been made since at least 2013 by Nacha. The Fed's own 2015 paper "Strategies for Improving the U.S. Payment System" included an action item to expand the operating hours and other capabilities of the NSS. Since that time, the Fed has agreed to expand NSS operating hours by only 30 minutes. Overwhelming support from the industry for Nacha's Same Day ACH proposal makes it clear that further action is necessary.
- Modernizing Fedwire and NSS to encompass a true 24x7x365 calendar day basis provides a strong capability for the future of payments, thereby providing opportunities for expanded Fedwire, ACH, and innovative faster payment solutions. To illustrate the criticality of this issue, ACH Operators process ACH files 23¼ hours per banking day (from 3 a.m. to 2:15 a.m. ET on the next day), but interbank settlement is restricted to hours when NSS and other Fed systems are open and available. In a similar fashion, the private-sector RTP Operator processes entries outside of the operating hours of NSS, but interbank settlement cannot occur until the Fed opens the NSS on the next banking day or the next banking day following a weekend and/or holiday.
- The RFC clearly states that the Board believes that a 7-day accounting regime is appropriate for the FedNow Service. Most FIs have already adopted a 7-day processing regime for payment services such as online banking (balances and bill-pay transactions), ATM, and debit card transactions. Moving to a 7-day accounting regime will take considerable effort, but the RFC also states that FIs may continue to offer other accounting approaches such as the existing 5-day accounting in place today. SFE membership would like to encourage modernizing efforts of NSS and FedWire to embrace the opportunity to re-align the start and end of the banking day with the U.S. calendar day.
- FedNow would record and report transactions as they occur, each day of the week, including weekends and holidays. Consumers expect systems that are being marketed as real-time payment systems to post entries on a calendar day basis, not the day after the

holiday weekend. However, the RFC proposes much less than a 24x7x365 real-time end-of-day environment for settlement due to the restrictions that currently exist in Fedwire and NSS. FedNow without real-time settlement will create windows of counterparty risk and potential reconciliation items for participating FIs between the time of the transaction and time of settlement within the payment system. Modernizing NSS allows innovation that is stymied in today's environment.

Fed Account Balances, Interest, and Correspondent Banks

- Under a 7-day account practice, FIs must manage their account to have a positive end-of-day balance (at 6:30 PM ET) to avoid intraday and overnight overdrafts including weekends and holidays. Because FedWire currently does not operate in a 24x7x365 basis, FIs will need to utilize anticipatory prefunding of the master account to cover potential debit activity that may occur through the FedNow Service between 6:30 PM ET and midnight or on weekends or holidays.
- While the proposed \$25,000 transaction limit may mitigate a large part of the problem, funds management of Fed accounts will become more complex in a 24x7x365 environment where payments settle continuously in master accounts. The RFC proposes changes to the FedLine® network, enhancing that system to support the FedNow's 24x7x365 processing environment. The Fed is conducting analysis of when it may be beneficial to extend discount window operations to include weekends or holidays. If the Board confirms a need exists to extend access to the discount window, the FedNow Service would provide access to intraday credit under the same terms and conditions as for current Federal Reserve services. Such intraday credit would lower the risk that payments will be rejected when sent due to lack of funds. SFE membership recommends that extending FedWire and access to the discount window to a 24x7x365 basis simplifies efforts for participating FIs to manage Fed balances.
- One of the primary changes from the Federal Register's November 2018 notice is the planned flow of real-time entries directly to the FI's master account at the Fed. Balances held in a master account earn interest and can be used to meet reserve requirements. SFE membership recognizes this change as a significant improvement, negating the previous proposed use of subaccounts and the need for a liquidity tool for managing balances between the master account and a subaccount. Expanding the operating hours of FedWire to a 24x7x365 basis will allow FedWire to be used as a liquidity management tool.
- Innovation – FedNow may increase innovation by incentivizing correspondent banks to develop services to manage multiple Fed accounts for their correspondents. Another possible option is for downstream correspondents to direct FedNow transactions to a correspondent bank's master account.

Fed Services

SFE membership strongly believes that all features that are built to support a real-time gross payment system (such as, extension of NSS and FedWire operating hours, directory services, or fraud prevention tools) need to be universally available regardless of the payment system. All Fed services should be available as, "a neutral platform to offer competitive and innovative faster payments to end users."

Education

Member owned payment associations such as Southern Financial Exchange, provide direct educational opportunities to over 90% of all U.S. financial institutions. This positions the payment associations as a unique resource to provide training and education on faster payment solutions. For over 40 years, the Fed has assisted (through train-the-trainer and other programs) in the educational effort of the payment associations, and we would like to encourage continued partnership with these organizations.

On behalf of Southern Financial Exchange and our members, thank you for this opportunity to respond and for your consideration of these comments.

Respectfully submitted,



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