Strategies for Improving the U.S. Payments System: Maintaining the Momentum

Remarks by

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May 4, 2017
Faster Payments Task Force Meeting
Chicago, Ill.

Good morning. It is my pleasure to join you today to recognize the tremendous contributions you've made to this public-private effort aimed at improving the nation's payments infrastructure. This is one of the most ambitious undertakings in the history of our country's payments system and one that is essential to the growing and evolving demands of businesses and consumers. I also want to thank Gordon Werkema and his team for the expertise and leadership they've brought to this engagement on behalf of the Federal Reserve.

Charting a course for faster payments has been demanding, but the progress we've seen is rewarding. It signals that even as more work lies ahead, we can build on the experience of the past two years to achieve the desired outcomes identified in the 2015 paper *Strategies for Improving the U.S. Payment System*. This morning, I'd like to talk briefly about the progress achieved to date and then offer my thoughts on the road ahead for the Federal Reserve and the payments industry.

Before I continue, now would be a good time to remind you that the views I express here are my own and not those of others in the Federal Reserve System.

Progress report

In 2012, the Federal Reserve was among those noting that the U.S. payment system was undergoing a period of rapid change, and contemplating the implications. Consumers and businesses were turning increasingly to e-commerce and Internet-enabled technologies. In the midst of this transition, payment security was being challenged by new, dynamic, and escalating threats.

Traditional payment services had been adjusting slowly to these changes, while emerging players were coming to market with innovative product offerings. Avoiding fragmentation and facilitating end-to-end adoption required a more coordinated rather than organic approach to ensure that issues of access and security could be broadly considered.

A path forward took shape with extensive industry dialogue in the form of the *Strategies for Improving the U.S. Payment System* paper published in 2015. Within the paper were strategies based on five desired outcomes for improvements in the following areas: speed, security, efficiency, cross-border payments and industry collaboration.

As this group knows better than anyone, industry stakeholders and the Federal Reserve have invested significantly over the past two years in efforts to advance toward the desired outcomes outlined in that paper. While some thought our efforts would fall victim to proprietary interests and a lack of cooperation, substantial measureable progress has been made on a number of issues and there is significant momentum towards addressing some of the more intractable issues that will demand a more sustained focus.

Earlier this year, the Task Force released *Part One* of its final report and I look forward to seeing *Part Two* when it becomes available this summer. Once completed, this document will share assessments of proposals for faster payments solutions and recommend next steps for the industry to take to achieve safe and accessible faster payments capabilities. Together, these documents will provide a comprehensive report of the Task Force's work. Feedback from private sector providers suggests they have found this work to be worthwhile and promising as they seek to design and deliver faster payment capabilities to end users.

Of course, while the Task Force has been at work on these issues, the payments system has continued to evolve. Innovation and new capabilities have emerged from the private sector and the Federal Reserve also has continued to improve the services it provides. For example, same-day ACH credit payments began flowing through the networks last fall, with 13 million payments cleared same-day in the first 100 days. Although not real-time, this development is an important and tangible step toward faster payments in the United States. Additionally, global messaging standards (ISO 20022) have been adopted for better interoperability. Innovations in the card space now facilitate real-time P2P transfers via credit push. And many fintech and social media entities are delivering payment services with some real-time attributes through stored value or card on file models. The payments industry is also exploring models that leverage virtual currency and distributed ledger technology in delivering faster payment solutions.

The Road Ahead

While the efforts of the Federal Reserve and the Faster Payments Task Force have driven significant progress, we recognize that the desired outcomes identified in the 2015 paper have yet to be realized. With continuing technological innovation and the emergence of new potential security threats, real work remains if we are to achieve and maintain a safe, ubiquitous, faster payments capability.

Ongoing innovation and market activity, including a variety of proposals reviewed by the Task Force, suggests the potential for multiple solutions in the faster payments market. However, the lack of established industry standards and rules could hinder interoperability of these solutions, resulting in fragmentation and inhibiting competition over time. Such conditions could negatively affect the ability to "pay anyone" and constrain access and adoption. Study of the payment system also teaches that over time, consolidation of providers seeking economies of scale and scope may occur, adversely affecting competition, an essential ingredient to innovation and serving the needs of consumer and business end users. I am encouraged by the amount of attention that you've given to considering these kinds of critical issues and challenges.

Further progress is needed in other aspects as well. As highlighted in the Strategies paper, developing settlement services to support real-time payments is yet to be addressed. Faster payment capabilities that rely on current settlement systems would have end user service gaps or real-time end user service offerings with deferred settlement. Deferred interbank settlement could create credit or liquidity risks for financial institutions and potential risk for the financial system. We will continue to work with the industry to understand such issues as solutions are implemented.

The Federal Reserve's role

Over the next decade, I anticipate that changes to the payments system will only accelerate, but in uncertain ways. As it has done in the past, the nature of the Federal Reserve's engagement going forward will likely evolve.

The Faster Payments Task Force is only the most recent example of the cooperation between the Federal Reserve and the private sector that has historically contributed to a more efficient and effective payments system. This history includes the development of routing numbers, the growth of the automated clearing house network and the crafting of Check 21 legislation.

A secure and smooth-functioning payments system is a critical component of economic growth and stability. Recognizing this, the Federal Reserve has sought to promote its "integrity and efficiency … and to ensure the provision of payment services to all depository institutions on an equitable basis … in an atmosphere of competitive fairness."[1]

The Federal Reserve's dual role as an operator and regulator in the U.S. payments system is often viewed as unique relative to approaches in other countries. Throughout U.S. history, consumers, merchants, financial institutions, policymakers and others have grappled with the question of who is ultimately responsible for what congressional leaders in 1913 called the "highways of commerce." From the chaos of the early 19th century through today's digital transactions, there has been a spirited debate over the central bank's roles and responsibilities.[2]

Today's active participation in a range of activities positions the Federal Reserve to bring perspective and insight to the challenges and emerging issues affecting the payments landscape. While some public authorities in other countries have acted based on explicit mandates, the Federal Reserve has leveraged the experience of its existing central bank roles to serve as a catalyst for critical improvement to the payments systems. In this role, we have facilitated the important work of the more than 300 individuals involved in the Task Force. And, as is noted in the strategies paper, the Federal Reserve remains committed to serving as a leader, convener and catalyst as appropriate to foster a well-functioning payments system for the public.

I very much look forward to continuing our work with the industry to shape the necessary improvements in our payments system that support confidence, economic growth and global competitiveness going forward.

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[1] The Federal Reserve in the Payments System, revised 1990

[2] See: Medley, Bill. *Highways of Commerce: Central Banking and the U.S. Payments System*. Federal Reserve Bank of Kansas City, 2014.