Office of Commissioner
Rohit Chopra

UNITED STATES OF AMERICA
Federal Trade Commission
WASHINGTON, D.C. 20580

November 7, 2019

Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue N.W.
Washington, D.C. 20551

RE: Federal Reserve Proposal to Develop Round-the-Clock, Real-Time Payments System *FedNow Service*

Dear Chairman Powell and Members of the Board of Governors:

I write to share my formal submission outlining my support for the Federal Reserve's proposal to develop the *FedNow Service*, a new, round-the-clock, real-time payments system. The proposal is a natural extension of the Federal Reserve's existing role in check clearing, wire transfers, and the automated clearinghouse (ACH) system. A private megabank monopoly over our electronic payments system will suppress innovation and distort incentives in our markets.

By establishing a public competitor, the Federal Reserve will ensure that small banks, credit unions, and other new entrants can access and build upon the payments infrastructure of the future. To that end, my comment outlines three arguments in support of the Federal Reserve's development of a real-time payments system. First, introducing a public competitor will prevent a Wall Street megabank monopoly. Second, a public competitor will check private-sector abuse. Third, the Federal Reserve will provide proven benefits as a public competitor.

It is the duty of the Board of Governors to prudently oversee and promote the flow our currency. The Federal Reserve must play a role as a public competitor to prevent a megabank monopoly over a core function of our financial system. As large private firms on Wall Street and Silicon Valley seek to leverage their market power through control of critical infrastructure, it is more important than ever for the Board to implement this proposal quickly.

If you have any further questions, please do not hesitate to contact me. Thank you for considering this comment, and I look forward to monitoring this proceeding carefully.

Respectfully submitted,

Rohit Chopra

Rohit Chopra

Before the
BOARD OF GOVERNORS
OF THE FEDERAL RESERVE SYSTEM
Washington, D.C. 20551

Federal Reserve Actions to Support Interbank Settlement of Faster Payments	)	Docket No. OP-1670

COMMENT OF
FTC COMMISSIONER ROHIT CHOPRA[*]

I write to outline support for the Federal Reserve's proposal to develop the *FedNow Service*, a new, round-the-clock, real-time payments system. The proposal is a natural extension of the Federal Reserve's existing role in check clearing, wire transfers, and the automated clearinghouse (ACH) system. A private megabank monopoly over our faster payments system would suppress innovation and distort incentives in our markets. The Federal Reserve should not cede control of the plumbing of our future payments system to Wall Street.

By way of background, I serve as a Commissioner of the Federal Trade Commission (FTC). The FTC is the primary federal agency focused on competition, privacy, and data security issues. The FTC enforces a wide range of laws that safeguard the economy and families from abuse. In the payments sector, the FTC has rulemaking and enforcement authority under the Gramm-Leach-Bliley Act's Safeguards provisions.[1] The FTC is also charged with enforcing a critical provision of the Dodd-Frank Wall Street Reform and Consumer Protection Act that protects families and businesses against anticompetitive abuses by payment networks, such as Visa and Mastercard.[2]

Prior to taking office as a Commissioner, I served as an Assistant Director at the Consumer Financial Protection Bureau, where I oversaw the agency's efforts on student financial services. I

[*] This comment represents my own views and does not necessarily reflect those of the Federal Trade Commission or any other Commissioner.

[1] For example, the FTC charged PayPal's Venmo service with a slew of violations for its business practices. *See* Press Release, Fed. Trade Comm'n, PayPal Settles FTC Charges that Venmo Failed to Disclose Information to Consumers About the Ability to Transfer Funds and Privacy Settings; Violated Gramm-Leach-Bliley Act (Feb. 27, 2018), https://www.ftc.gov/news-events/press-releases/2018/02/paypal-settles-ftc-charges-venmo-failed-disclose-information.

[2] Section 1075 of the Dodd-Frank Act amended the Electronic Fund Transfer Act. The amendment was codified by the Federal Reserve as Regulation II prohibiting network exclusivity on debit cards. It also restricts issuer and network inhibitions on merchant transaction routing choice. I am committed to ensuring high levels of compliance with the rule and pursuing significant consequences for those that evade it.

worked extensively on payments issues affecting students receiving Pell Grants and federal student loans, including the U.S. Department of Education's Cash Management Rule that gave students quick access to their money and eliminated many conflicts of interest.[3]

Everyone stands to benefit from a faster payments system that provides round-the-clock, real-time access to funds. It promises to give people and businesses the kind of instant accounting that is currently only possible with cash. People can count and track the money in their wallet or cash register with confidence. But the same cash-flow certainty is nearly impossible with funds in a bank account, which may take days to reflect a payment by check, debit card, or ACH.[4] These delays can vary in length, adding further instability and unpredictability. In the meantime, people risk spending money that they don't have and businesses risk operating in the red as they wait to get paid.

The problems caused by payment delays are most acute for people living paycheck-to-paycheck and small businesses that can't afford to have their daily operating expenses tied up for days. When managing money is like balancing on a tightrope, any misstep can lead to financial freefall. Delayed payments ratchet up the risk that the funds are not available when the transaction finally goes through. One forgotten transaction or accounting error can lead to expensive overdrafts and late fees that compound and spiral. A few days delay in access to funds can mean covering the gap with disastrous, expensive payday loans and other short-term credit.

Real-time payments promise to keep the money in people's pockets that might otherwise be lost to the expensive uncertainty of delay. Financial shortfalls have generated substantial profits for banks, payday lenders, and other financial service providers. According to data released by the FDIC, people paid $11.45 billion in overdraft fees in 2017.[5] The payday industry vacuums up nearly $8 billion in fees every year.[6] The ability to manage money in real time will make it much easier for people and small businesses to avoid the missteps that create these high costs.

The demand for faster payments is high, given the pent-up frustration with high-cost bank accounts and the expectations created by the widespread adoption of other real-time technologies. In the high-speed digital economy, truly instantaneous funds exchanges and immediate funds access are becoming increasingly important.[7] Real-time transactions are standard practice in many advanced economies and America has fallen behind waiting for a

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[3] Program Integrity and Improvement, 80 Fed. Reg. 67126 (Oct. 30, 2015) (codified at 34 C.F.R. pt. 668).

[4] Testimony of Robert A. Steen On Behalf of the Independent Community Bankers of America, Before the Task Force on Fin. Tech of the H. Comm. On Fin. Servs.: Hearing on The Future of Real-Time Payments, at 2 (Sept. 26, 2019), https://financialservices.house.gov/uploadedfiles/hhrg-116-ba00-wstate-steenb-20190926.pdf.

[5] PETER SMITH, CENTER FOR RESPONSIBLE LENDING, THE STATE OF HIGH-COST OVERDRAFT PRACTICES IN 2017, at 1 (2018), https://www.responsiblelending.org/research-publication/unfair-market-state-high-cost-overdraft-practices-2017; *see also*, Renae Merle, *Trump administration may overhaul rules limiting bank overdraft fees*, WASH. POST (May 14, 2019), https://www.washingtonpost.com/business/2019/05/14/cfpb-launches-review-regulations-limiting-overdraft-fees/.

[6] DIANE STANDAERT ET AL., CENTER FOR RESPONSIBLE LENDING, PAYDAY AND CAR-TITLE LENDERS DRAIN NEARLY $8 BILLION IN FEES EVERY YEAR (updated Apr. 2019), https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-statebystate-fee-drain-apr2019.pdf.

[7] Steen, *supra* note 4, at 2-3.

bank-owned solution.[8] According to the Independent Community Bankers of America (ICBA), 40 real-time payments systems are live globally, including in Europe, Mexico, and Australia.[9]

The faster payments system's highest value is as an infrastructural platform for innovation in the financial sector. Like other public utilities, the faster payments system will deliver the most benefit as a means for many, not an end for a few. The system's long-term success will be measured in the ubiquity, interoperability, and safety of real-time payments. As a distributed network, the faster payments system becomes more valuable to each user as the number of users increases, which is why ubiquity is so critical. That ubiquity depends on the development of uniform standards that allow it to connect seamlessly with the technologies used by different banks. The network must be safe and secure from hackers to encourage widespread adoption.

Without a public competitor, the fate of faster payments is uncertain. The entire banking sector will be dependent on the ability and willingness of a group of Wall Street megabanks to deliver a faster payments system that benefits all stakeholders. That ability is in question as the development of a private faster payments system through The Clearing House (TCH), an entity owned by big Wall Street banks, has been sluggish[10] since it was announced in 2014.[11] Also doubtful is the willingness, as the financial incentives that drive Wall Street suggest that the long-term interests of all participants are likely to fall to the wayside in pursuit of short-term profits.

The private sector's lagging efforts to meet the demand for immediate funds transfers have opened the door to attempts to bypass our banking system altogether. Under the auspices of making payments faster and cheaper, Facebook has announced plans to launch Libra, a new private currency and payments system. The vague and scant details on the tech platform's proposed shadow global central bank have sounded international alarm bells, particularly in light of Facebook's ongoing scandals and reputation for abuse.[12] The laundry list of risks raised by the Libra project will take time to unpack and address. I share the serious concerns raised by Chairman Jerome Powell[13] and Governor Lael Brainard.[14] But regardless of Libra's ultimate

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[8] FASTER PAYMENTS TASK FORCE, THE U.S. PATH TO FASTER PAYMENTS, FINAL REP. PT. ONE: THE FASTER PAYMENTS TASK FORCE APPROACH (Jan. 2017), https://fasterpaymentstaskforce.org/wp-content/uploads/faster-payments-final-report-part1.pdf.

[9] Steen, *supra* note 4, at 2.

[10] On slow adoption of TCH's RTP System, Former Chair of the FDIC Sheila Bair states, "As yet, it has failed to gain significant traction, with relatively low volumes and few banks participating beyond the big ones that own TCH." Sheila Bair, *Why the Fed is right to step in and finally make real-time payments happen*, YAHOO! FINANCE (Sept. 4, 2019), https://finance.yahoo.com/news/fednow-real-time-payments-sheila-bair-175320549.html.

[11] Sarah Todd & Kevin Wack, *The Clearing House to Build Real-Time Payments System*, AM. BANKER (Oct. 22, 2014, 7:28 PM), https://www.americanbanker.com/news/the-clearing-house-to-build-real-time-payments-system.

[12] I joined several global data protection regulators to highlight a number of concerns that go beyond financial system stability and resilience. *See* Joint statement from Representatives of the Global Community on global privacy expectations of the Libra network (Aug. 2, 2019), https://ico.org.uk/media/about-the-ico/documents/2615521/libra-network-joint-statement-20190802.pdf.

[13] Pete Schroeder & Trevor Hunnicutt, *Fed chief calls for Facebook to halt Libra project until concerns are addressed*, REUTERS (July 10, 2019, 10:58 AM), https://www.reuters.com/article/us-usa-fed-powell-libra/fed-chief-calls-for-facebook-to-halt-libra-project-until-concerns-addressed-idUSKCN1U51VE.

[14] Leal Brainard, Governor, Fed. Res., Address at the Peterson Institute for International Economics and Princeton University's Bendheim Center for Finance Conference: The Future of Money in the Digital Age (Oct. 16, 2019), https://www.federalreserve.gov/newsevents/speech/brainard20191016a.htm.

fate, the proposal's emergence underscores the appetite for real-time payments and the urgency of intervention by the Federal Reserve.

By establishing a public competitor, the Federal Reserve will ensure that small banks, credit unions, and other new entrants can access and build upon the payments infrastructure of the future. To that end, my comment outlines three arguments in support of the Federal Reserve's development of a round-the-clock, real-time payments system. First, introducing a public competitor will prevent a Wall Street megabank monopoly. Second, a public competitor will check private-sector abuse. Third, the Federal Reserve will provide proven benefits as a public competitor.

Preventing a Megabank Monopoly

Without a public competitor, big banks on Wall Street will have a natural monopoly thanks to high barriers to entry. The biggest barrier is structural. Within the financial sector, banks are the only private firms that can ultimately administer the current payments system because of their accounts with the central bank -- the place where transactions are finally settled. Financial technology startups that have tried to provide real-time payment services have been limited by their dependency on banks. Such services typically only work when both the sender and receiver have accounts at participating banks. Participants of the megabank-owned RTP System must maintain a pre-funded reserve or clearing account with a Federal Reserve Bank to support payment transfers.[15] This requirement has limited participation[16] in the private network to depository institutions.[17] The high cost of upfront investment, complexity, and network effects further exclude all but the biggest Wall Street banks.

Checking Wall Street Abuse

Introducing a public competitor is the sole means of holding the payments market accountable for operating openly and fairly, since the Federal Reserve has very limited authority to regulate or supervise the payments system.[18] Based on real-world experience, an unregulated monopoly of essential infrastructure is unlikely to deliver the benefits that a competitive market would produce.

Consumers, small businesses, small banks, and small credit unions lack the market power to compel those benefits or check predatory abuse from an unaccountable megabank monopoly. Absent competitive pressure or government oversight, a private payments monopoly will have unilateral control over the development, availability, and pricing of the system. With no alternative payments choice, industry participants and consumers alike will be forced to play by Wall Street's rules or sit on the sidelines, even if it means accepting a subpar product, paying jacked up prices, or agreeing to the megabanks' self-interested terms.

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[15] *Real-Time Payments Participation Rules*, THE CLEARING HOUSE PAYMENTS CO. LLC, at 5 (Oct. 30, 2017), https://www.theclearinghouse.org/payment-systems/rtp/-/media/d0314d2612ab4619b3c09745b54cf96f.ashx.

[16] Only 15 financial institutions—out of nearly 11,000 nationwide—are actively engaged on the network; *see* Steen, *supra* note 4, at 3.

[17] The Clearing House Payments Co. LLC, *supra* note 15 at 3.

[18] Federal Reserve Actions to Support Interbank Settlement of Faster Payments, 84 Fed. Reg. 39297, 39308 (Aug. 9, 2019) (proposed Aug. 9, 2019).

Indeed, such a bad deal is virtually inevitable without regulation or competition. As the exclusive faster payments provider, a megabank monopoly would have little reason to expand access, upgrade, or innovate. In fact, limiting such benefits would further their narrow interests. Blocking or limiting the access and participation of small banks, credit unions, and new entrants could eliminate the competitive threat they pose. Avoiding investments in expensive upgrades would mean more profit. Slowing innovations that might be costly, unpredictable, and disruptive could help them maintain their monopoly. Combined, this anticompetitive, rent-seeking behavior would significantly reduce both economic efficiency and the value of the system to its participants.

There are already indications that abuse is likely. TCH initially promised not to offer volume discounts, which would make the service cheaper for the big banks with the most transactions. Then they caveated their pledge, saying that they would agree not to discount the service for themselves only if they have no competitor.[19] Robert A. Steen, who runs a community bank in Iowa, aptly noted that TCH was essentially saying, "Trust us. We won't behave like a monopoly as long as we *can be* a monopoly."[20] While this caveat has since been removed from TCH's website, there is nothing to stop them from adding it back at a later date.

Further, TCH's faster payments rules give it "sole discretion" to require a participant to stop using a "particular Third-Party Service Provider" and "make alternate technical connection arrangements to continue its access to and use of the RTP System."[21] The only oversight of the system appears to be an annual "self-audit" verifying compliance with the RTP Participation and Operating Rules. TCH notes that it "does not require [the RTP self-audit] to be completed using any specific set of procedures or approach."[22]

Providing Proven Benefits as a Public Competitor

The Federal Reserve already successfully competes in other parts of the payment system. For nearly half a century, all major payments systems — including those for processing checks, facilitating direct deposits, and wire transfers — have depended on both private and Federal Reserve systems.[23] The Government Accountability Office has concluded that the Federal Reserve's participation in the payment services market has benefited the U.S. payment system and its users.[24]

The most important benefit that the Federal Reserve provides is one it is uniquely capable of delivering – universal reach. There are more than 10,000 depository institutions in the United

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[19] Steen, *supra* note 4, at 3.
[20] *Id*.
[21] The Clearing House Payments Co. LLC, *supra* note 15, at 4
[22] *RTP® Participant Self-Audit Workbook*, THE CLEARING HOUSE PAYMENTS CO. LLC, at 1 (July 19, 2019), https://www.theclearinghouse.org/payment-systems/rtp/self-audit.
[23] Bair, *supra* note 7.
[24] U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-16-614, PAYMENT SERVICES: FEDERAL RESERVE'S COMPETITION WITH OTHER PROVIDERS BENEFITS CUSTOMERS, BUT ADDITIONAL REVIEWS COULD INCREASE ASSURANCE OF COST ACCURACY (2016), https://www.gao.gov/products/GAO-16-614.

States, and it would be impossible for the private Wall Street consortium to develop relationships with all of them. No private payments service has ever done so.

The Federal Reserve has established over its history a broad reach as a provider of payment and settlement services to all of these depository institutions. As noted by Ester George, president of the Federal Reserve Bank of Kansas City, "Through these connections, the Federal Reserve's existing payment services allow banks of every size to serve the needs of thousands of communities across the United States with competitive, fair and transparent access."[25] According to the ICBA, "The Fed is trusted among community banks."[26]

In expanding its role as public competitor, the Federal Reserve will make sure than no small bank or credit union is left behind in the transition to real-time payments. George points out that "[p]roviding this degree of comprehensive nationwide reach is something that we believe will present significant challenges to other providers in the current market landscape."[27] ICBA says that it would not have the direct access that the Federal Reserve provides from "the largest banks or their proxy which historically have served as a settlement provider for only a few of the nation's 11,000 financial institutions."[28]

Additional benefits include creating redundancy to an essential system, keeping prices competitive, operating with transparency, creating uniform standards, and guarding against barriers to innovation and participation.

Conclusion

It is the duty of the Board of Governors to prudently oversee and promote the flow our currency. The Federal Reserve must play a role as a public competitor to prevent a megabank monopoly over a core function of our financial system. As large private firms on Wall Street and Silicon Valley seek to leverage their market power through control of critical infrastructure, it is more important than ever for the Board to implement this proposal quickly.

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[25] Statement by Esther George on Behalf of the Fed. Res. System, Before the Task Force on Fin. Tech of the H. Comm. on Fin. Servs.: Hearing on The Future of Real-Time Payments, at 2 (Sept. 26, 2019), https://financialservices.house.gov/uploadedfiles/hhrg-116-ba00-wstate-georgee-20190926.pdf.
[26] Steen, *supra* note 4, at 5.
[27] George, *supra* note 25, at 2.
[28] Steen, *supra* note 4, at 5.