IV. A Path to a Fast Payment Service by the Fed

A. Introduction

The Board of Governors of the Federal Reserve (Fed) announced on August 5, 2019 that the Fed will develop a real-time payment and settlement system service called the FedNow Service (FedNow).[1] FedNow proposes to support a fast payment, namely, "a payment in which the transmission of the payment message and the availability of 'final' funds to the payee occur in real time or near-real time on as near to a 24-hour and seven-day (24/7) basis as possible,"[2] with a real-time gross settlement system.[3] This move by the Fed corresponds to the recent technological developments and changing expectations about the payment system.[4] In fact, shortly before the Fed's announcement, each house of Congress introduced a bill called the "Payments Modernization Act of 2019," to encourage the development of a real-time payment and settlement service in the United States and to authorize the Fed to undertake the task.[5] However, some

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[1] Press Release, Bd. of Governors of the Fed. Reserve Sys., Federal Reserve announces plan to develop a new round-the-clock real-time payment and settlement service to support faster payments (Aug. 5, 2019), https://www.federalreserve.gov/newsevents/pressreleases/other20190805a.htm [https://perma.cc/FS3C-NG6C] (announcing the development of "a new round-the-clock real-time payment and settlement service, called the FedNow℠ Service, to support faster payments in the United States").

[2] COMM. ON PAYMENTS & MKT. INFRASTRUCTURES, BANK FOR INT'L. SETTLEMENTS, FAST PAYMENTS – ENHANCING THE SPEED AND AVAILABILITY OF RETAIL PAYMENTS 6 (2016), https://www.bis.org/cpmi/publ/d154.pdf [https://perma.cc/7ZY8-3P9B] [hereinafter CPMI FAST PAYMENTS] (providing the definition of a fast payment and its characteristics).

[3] Federal Reserve Actions to Support Interbank Settlement of Faster Payments, 84 Fed. Reg. 39,297, 39,297–99 (Aug. 9, 2019) [hereinafter 2019 FR Notice] (outlining the background of the Fed's decision to develop a fast payment service with a real-time gross settlement system).

[4] THE FED. RESERVE BANKS, PAYMENT SYSTEM IMPROVEMENT – PUBLIC CONSULTATION PAPER 1–2 (2013), https://fedpaymentsimprovement.org/wp-content/uploads/2013/09/Payment_System_Improvement-Public_Consultation_Paper.pdf [https://perma.cc/7JSD-5VKU] (observing the application of new technologies in the payment system and "the changing payment preferences of end users").

[5] Payments Modernization Act of 2019, H.R. 3951, 116th Cong. (2019) (proposing that "funds deposited be available for withdrawal in real time" and that the Fed "create a real time payment system"); Payments Modernization

reservations about FedNow have been raised, and the details of the service and the Fed's authority, or lack thereof, to develop such service require scrutiny.[6]

This article discusses the development of FedNow and its advantages and disadvantages. First, Part B provides a general introduction to a fast payment service. Part C then begins with a brief overview of the Fed and discusses the FedNow and its features. Part D demonstrates the Fed's favorable assessment of FedNow based on its criteria. Lastly, Part E illustrates countervailing concerns about FedNow as well as counterarguments to those concerns.

B. Introduction to a Fast Payment Service

Recent technological developments have resulted in various changes to the modern payment system, which has significant implications for retail payments.[7] This article focuses on a retail payment system, which is "[a] funds transfer system that typically handles a large volume of relatively low-value payments in such forms as che[ck]s, credit transfers, direct debits and card payment transactions."[8] A payment system is comprised of three processes: an end-

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Act of 2019, S. 2243, 116th Cong. (2019) (asserting the need to develop a fast payment service by the Fed).

[6] *See* Ike Brannon, *Would the Federal Reserve's push to offer Real-Time Payments survive Regulatory Scrutiny?*, FORBES (Sept. 5, 2019, 1:33 PM), https://www.forbes.com/sites/ikebrannon/2019/09/05/would-the-federal-reserves-push-to-offer-real-time-payments-survive-regulatory-scrutiny/#7ad18754b818 [https://perma.cc/Z9HW-46GB] (arguing that the Fed's development of a fast payment service may fail to establish ubiquitous fast payment system and may violate the legal requirement under the Monetary Control Act); PYMNTS, *Congress Presses Fed on Real-Time Payments Plan*, PYMNTS.COM (Sept. 27, 2019), https://www.pymnts.com/news/b2b-payments/2019/house-committee-fed-fednow-real-time-payments/ [https://perma.cc/LS43-SNHN] (reviewing the concerns about FedNow raised during a congressional committee hearing including its development timeline and interoperability).

[7] Zhiling Guo et al., *Near Real-Time Retail Payment and Settlement Systems Mechanism Design* 1–2 (SWIFT Inst., Working Paper No. 2014-004, 2015), https://swiftinstitute.org/wp-content/uploads/2015/11/WP-No-2014-004-1.pdf [https://perma.cc/23AM-M22B] (remarking on the effects of technological innovation on the retail payment and settlement system).

[8] COMM. ON PAYMENTS & MKT. INFRASTRUCTURES, BANK FOR INT'L. SETTLEMENTS, A GLOSSARY OF TERMS USED IN PAYMENTS AND SETTLEMENT

user service, a clearing service, and a settlement service.[9] The end-user service constitutes an initiation of a transfer of funds by an end-user, such as an individual or a business, through its bank and a communication about the transfer between the payor and its bank.[10] After a payment is initiated, the clearing service between a payor's bank and a payee's bank takes place, where the two banks exchange a payment message that contains necessary information to make debits and credits to the respective accounts of the payor and the payee.[11] Lastly, the settlement service consummates the payment by making debits and credits to the respective accounts of the payor's bank and the payee's bank with a central bank—which in the United States is the Fed—or other settlement institution.[12]

A traditional payment takes some time to complete those processes, ranging from several hours to a few days, and funds become available to the payee only after the completion of such processes.[13] On the other hand, a fast payment makes funds available to a payee around the clock immediately, or almost immediately, after a payor

SYSTEMS 15, https://www.bis.org/dcms/glossary/glossary.pdf?scope=CPMI&base=term (last updated Oct. 17, 2016) [https://perma.cc/GM6A-KL32] [hereinafter CPMI GLOSSARY] (providing the definition of a retail payment system).

[9] Potential Federal Reserve Actions to Support Interbank Settlement of Faster Payments, Request for Comments, 83 Fed. Reg. 57,351, 57,355 (proposed Nov. 15, 2018) (to be codified at 12 C.F.R. ch. II) [hereinafter 2018 FR Notice] ("To complete a payment between two bank accounts, three key levels of the payment processes are necessary: End-user services, clearing services, and interbank settlement services.").

[10] *Id*. (explaining that an end-user service allows "an end user to communicate with their bank about the need to make a payment and the details of that payment").

[11] *Id*. at 57,356 (indicating that a clearing service involves an interaction between "the sending and receiving banks . . . based on the payment information received from end users and the protocols associated with a payment service").

[12] *Id*. (illustrating that a settlement service allows "the sending and receiving banks transfer assets to each other to satisfy the interbank obligations that arise from end-user payments" through the adjustment of "balances in banks' settlement accounts on the books of a settlement institution").

[13] CPMI FAST PAYMENTS, *supra* note 2, at 8 ("[T]raditional retail payments typically involve delays in the clearing or settlement of payments (or both), with the payee not receiving final funds until the completion of those steps.").

initiates the payment.[14] Such funds are final, meaning that "the payee has unconditional and irrevocable access" to the funds.[15] The expected benefits of a fast payment to end users include the ability to send and receive payments, especially time-sensitive payments, fast and in real time and improved cash management.[16] The banks may also anticipate increased profits from saving costs for maintaining and modernizing traditional payment services as well as from providing additional services in connection with a fast payment service.[17]

While fast payments allow payees to have essentially immediate access to final funds at any time, the settlement service does not need to occur in real time and may be completed after final funds become available.[18] On the one hand, a fast payment service with a deferred net settlement (DNS) system completes the settlement service after final funds become available to payees.[19] In this case, the adjustment of the respective accounts of a payor's bank and a payee's bank occurs on a net basis at one or multiple times in a day.[20] On the other hand, a fast payment service with a real-time gross settlement (RTGS) system—which is what FedNow proposes to provide—

[14] 2018 FR Notice, *supra* note 9, at 57,356 ("In a faster payment, the three levels of the payment process are structured so that senders can immediately initiate, and recipients can immediately receive, payments at any time."); CPMI FAST PAYMENTS, *supra* note 2, at 9 ("[A] fast payment yields final funds to the payee almost immediately and at any time . . . .").

[15] CPMI FAST PAYMENTS, *supra* note 2, at 6 (providing the definition of final funds).

[16] *Id*. at 45–46 (exemplifying situations where a fast payment may be advantageous to its end users).

[17] *Id*. at 47 (describing potential benefits of a fast payment to banks, including "reduced investment costs for the maintenance and upgrade of legacy systems," lower "variable cost of managing fast payments," and "cross-selling of additional financial products to customers, using the fast payment functionality").

[18] *Id*. at 9 (highlighting that "a fast payment might be completed from the end-user point of view . . . [but] the settlement of transactions between [banks] need not necessarily be completed before the payee has final funds").

[19] *Id*. at 35 (discussing the concept of deferred settlement).

[20] 2018 FR Notice, *supra* note 9, at 57,358 ("After collecting and netting settlement information related to groups of payments, the centralized entity submits information on net obligations to an interbank settlement system, which then adjusts the account balances of all participating banks on the settlement institution's books."); CPMI FAST PAYMENTS, *supra* note 2, at 35 ("The multilateral net positions between the participating [banks] may be settled once or multiple times per day.").

completes the entire payment processes including the settlement service before final funds become available to payees.[21] In this case, the adjustment of the respective accounts of a payor's bank and a payee's bank occurs "on a transaction-by-transaction basis"[22] essentially immediately and around the clock.[23]

C. What Is FedNow?

Since the passage of the Federal Reserve Act in 1913, the Fed has played an important role in maintaining the U.S. monetary and financial system.[24] One of the Fed's primary functions as the central bank of the United States has been to provide infrastructure for clearing and settlement services without liquidity risk or credit risk, and the Fed has provided numerous financial services including the automated clearinghouse, check collection services, FedWire Funds Services, and the National Settlement Services.[25] In particular, beginning in 2013, the Fed has taken several steps toward a fast and efficient payment and settlement system as part of its modernization efforts.[26] After soliciting public input through a consultation paper in 2013,[27] the Fed not only

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[21] 2018 FR Notice, *supra* note 9, at 57,359 ("In an RTGS arrangement for faster payments, final funds are made available to the recipient only after interbank settlement has occurred between the banks that are party to the transaction.").

[22] CPMI GLOSSARY, *supra* note 8, at 9 (providing the definition of a gross settlement).

[23] 2018 FR Notice, *supra* note 9, at 57,359 ("RTGS-based faster payments involve both completion of end-user payments and settlement of interbank obligations on a payment-by-payment basis in real time and at any time.").

[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 4 (2016) (elaborating on the creation of the Fed and its roles as the central bank of the United States).

[25] 2019 FR Notice, *supra* note 3, at 39,298–99, 39,298 n.7 (delineating the Fed's role in the U.S. payment system and its related services).

[26] 2018 FR Notice, *supra* note 9, at 57,353 ("Beginning in 2013, the Federal Reserve established a new initiative . . . with the objective of engaging with the payment industry and other stakeholders to upgrade and enhance the nation's payment system.").

[27] THE FED. RESERVE BANKS, *supra* note 4, at 1 (stating the contexts and purposes of the Fed's public consultation paper).

put forth five desired outcomes and a set of strategies[28] but also convened the Faster Payments Task Force comprised of more than 300 experts and stakeholders.[29] Accordingly, the Fed now seeks to develop FedNow with the goal of advancing "ubiquitous, safe, and efficient" fast payment service in the United States.[30]

The Fed proposed that FedNow would be a fast payment service with a RTGS system that "would process individual payments within seconds"[31] and that it is expected to be available in 2023 or 2024.[32] FedNow would be available to banks, or "depository institutions includ[ing] commercial banks, savings banks, savings and loan associations, and credit unions,"[33] that are "eligible to hold accounts at the [Federal] Reserve Banks under applicable federal statutes and Federal Reserve rules, policies, and procedures."[34] It would "support credit transfers, where a sender initiates a payment to an intended receiver."[35] Its settlement service would occur "through debit and credit entries to balances in banks' master accounts at the [Federal] Reserve Banks."[36] It would initially have a limit up to $25,000 in order to allow the processing of a large volume of transactions and also to prevent fraudulent transaction attempts.[37] The Fed has not yet announced pricing information for FedNow.[38] In addition, while the Fed acknowledges that interoperability with existing private-sector fast

[28] FED. RESERVE SYS., STRATEGIES FOR IMPROVING THE U.S. PAYMENT SYSTEM 2 (2015), https://fedpaymentsimprovement.org/wp-content/uploads/strategies-improving-us-payment-system.pdf [https://perma.cc/L58X-2KB2] (outlining the desired outcomes and strategies based on the Fed's public consultation paper published in 2013).
[29] 2018 FR Notice, *supra* note 9, at 57,353–54 (illustrating the Fed's move towards a fast payment service).
[30] 2019 FR Notice, *supra* note 3, at 39,299 (indicating the Fed's objective to develop FedNow for faster payments in the United States).
[31] *Id*. at 39,317 (giving a general description of FedNow).
[32] *Id*. at 39,301 ("Pending engagement with the industry, the [Fed] anticipates [FedNow] will be available in 2023 or 2024.").
[33] *Id*. at 39,298 n.2 (noting the definition of a bank).
[34] *Id*. at 39,318 (declaring the availability of FedNow limited to banks holding accounts at the Fed).
[35] *Id*. at 39,317 (describing a credit transfer system).
[36] *Id*. (elucidating the settlement service of FedNow).
[37] *Id*. at 39,317 & n.100 (justifying the initial service limit amount of FedNow).
[38] *Id*. at 39,320 ("Before [FedNow] is launched, the Fed will announce the service's fee structure and fee schedule.").

payment services[39]—including the RTP network operated by The Clearing House Payments Company L.L.C. (RTP)[40]—would contribute to ubiquity, the Fed expects to consider not only interoperability but also other means to achieve nationwide reach.[41]

D. Favorable Assessment by the Fed

In accordance with its policy,[42] where the Fed introduces new services or major service enhancements, such services must satisfy all of the following criteria: the Other Providers Criterion, the Public Benefits Criterion, and the Cost Recovery Criterion.[43] First, the Other Providers Criterion establishes that a service "should be one that other providers alone cannot be expected to provide with reasonable

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[39] Memorandum from the U.S. House Comm. on Fin. Servs. Majority Staff to the Members of the Comm. on Fin. Servs. 2 (Sept. 23, 2019), https://docs.house.gov/meetings/BA/BA00/20190926/110016/HHRG-116-BA00-20190926-SD002-U3.pdf [https://perma.cc/FC3V-TCWF] ("[T]here are several private sector initiatives underway, some which would make funds available to the recipient in real time (with deferred settlement) and some of which would provide real-time settlement.").

[40] *About RTP*, THE CLEARING HOUSE PAYMENTS CO., https://www.theclearinghouse.org/payment-systems/rtp (last visited Nov. 16, 2019) [https://perma.cc/5DW5-Q9U7] ("The RTP® network from The Clearing House is a real-time payments platform that all federally insured U.S. depository institutions are eligible to use for payments innovation.").

[41] 2019 FR Notice, *supra* note 3, at 39,318 (recognizing that, in a market of multiple fast payment service providers, ubiquity of a fast payment service "can be achieved in multiple ways, such as by banks participating in multiple services, or through interoperability where direct exchange of payments across services is possible").

[42] *Policies: The Federal Reserve in the Payments System*, BD. OF GOVERNORS OF THE FED. RESERVE SYS., https://www.federalreserve.gov/paymentsystems/pfs_frpaysys.htm (last updated Nov. 20, 2008) [https://perma.cc/E8BX-SCA7] [hereinafter *The Fed Policies*] ("[T]he role of the Federal Reserve in providing payment services is to promote the integrity and efficiency of the payments mechanism and to ensure the provision of payment services to all depository institutions on an equitable basis, and to do so in an atmosphere of competitive fairness.").

[43] 2019 FR Notice, *supra* note 3, at 39,303 ("The policy specifically addresses the introduction of new services or major service enhancements in light of the Board's overall expectations and requires all of the [three] criteria to be met.").

effectiveness, scope and equity."[44] Second, the Public Benefits Criterion establishes that the Fed "must expect that its providing the service will yield a clear public benefit."[45] Third, the Cost Recovery Criterion establishes that the Fed "must expect to achieve full recovery of costs over the long run."[46]

The Fed indicated that, on balance, FedNow satisfies the three aforementioned criteria.[47] Regarding the Other Providers Criterion, the Fed relied on facts that there are more than 10,000 banks in the United States with diverse size, practices, and interests and that RTP, currently the only private-sector RTGS service, is primarily available only to a few large banks.[48] Moreover, the Fed referred to the history of the payment system in the United States in that "no single private-sector payment service provider of traditional services, such as check, ACH, funds transfer, or payment card services, has done so alone."[49] The Fed maintained that the Other Providers Criterion is satisfied given the difficulties in providing a fast payment service with a RTGS system, both nationally and equitably to all banks.[50] The Fed also demonstrated that the Other Providers Criterion is met in light of the expected problems in the absence of competition, such as discouragement of innovation and an increase in price.[51] Similarly, with respect to the Public Benefits Criterion, the Fed took into account the diversity

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[44] *The Fed Policies*, *supra* note 42 (describing the requirement under the Other Providers Criterion).
[45] *Id*. (describing the requirement under the Public Benefits Criterion).
[46] *Id*. (describing the requirement under the Cost Recovery Criterion).
[47] *See* 2019 FR Notice, *supra* note 3, at 39,303–14 (substantiating the Fed's assessment that FedNow satisfies the three criteria).
[48] *Id*. at 39,306–07 (identifying that "the U.S. banking system (and, by extension, the payment ecosystem) is extremely diverse, with a wide variety of market participants and stakeholders that have heterogeneous circumstances, interests, and needs" and that RTP has focused on "providing services primarily to a small number of large banks in the United States").
[49] *Id*. at 39,306 (stressing the difficulty that private-sector service providers have faced in implementing payment services nationwide).
[50] *Id*. at 39,306–08 (expressing that "it is unlikely that the private-sector RTGS service for faster payments alone will reach the thousands of small banks necessary to yield nationwide scope, even in the long term").
[51] *Id*. (opining that "a single service provider without competition can yield undesirable outcomes for faster payments, such as lower service quality or higher prices" and that "a single provider may focus on specific use cases that do not promote the potential for faster payments to be used in a wide variety of ways").

of U.S. banks, the existence of the private-sector RTGS service without a nationwide reach, and the Fed's continued relationships with all U.S. banks as a payment services provider.[52] The Fed asserted that the Public Benefits Criterion is satisfied because the public would benefit from FedNow's accessibility, safety, and efficiency.[53]

Lastly, the Fed evaluated the Cost Recovery Criterion by considering the requirements under the Depository Institutions Deregulation and Monetary Control Act of 1980 (MCA) and a set of pricing principles established by the Fed.[54] The pricing principles under the MCA state that "[o]ver the long run," fees for the Fed services "shall be established on the basis of all direct and indirect costs actually incurred in providing the [Fed] services" and that "the pricing principles shall give due regard to competitive factors and the provision of an adequate level of such services nationwide."[55] Furthermore, the pricing principles established by the Fed stipulate that the Fed must intend "fees be set so that revenues for major service categories match

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[52] *Id*. at 39,309–10 (observing that the Fed has a "demonstrated history of providing nationwide access to payment services" and that "the Federal Reserve's presence as an operator has improved competition and efficiency, leading to lower prices and accelerated payment system improvements").

[53] *Id*. at 39,310 ("The expected public benefit stems in large part from contributions [FedNow] would make towards achieving nationwide reach of an RTGS infrastructure for faster payments, promoting the safety and resiliency of that infrastructure, and encouraging competition between payment services.").

[54] *Id*. at 39,312 ("[The] Cost Recovery Criterion accounts for the requirements in the MCA . . . [and] the [Fed] further considers its policy, 'Principles for the Pricing of Federal Reserve Bank Services' (pricing principles), and its previous application of those principles to existing services."); *see* Depository Institutions Deregulation and Monetary Control Act of 1980, Pub. L. No. 96-221, § 107, 94 Stat. 132, 140–41 (1980) (codified, as amended, at 12 U.S.C. § 248a (2012)) (requiring the establishment of the pricing principles and the schedule of fees for "Federal Reserve bank services to depository institutions"); *Policies: Principles for the Pricing of Federal Reserve Bank Services*, BD. OF GOVERNORS OF THE FED. RESERVE SYS., https://www.federalreserve.gov/paymentsystems/pfs_principles.htm (last updated Nov. 20, 2008) [https://perma.cc/2HBR-H8GQ] [hereinafter *The Fed Pricing Principles*] ("The [Fed] has adopted [a set of] pricing principles, which incorporate both the specific statutory requirements of the Monetary Control Act and provisions intended to fulfill its legislative intent . . . .").

[55] 12 U.S.C. § 248a (2012) (specifying the principles for the pricing of the Fed services to banks).

costs."[56] They also provide that, "[d]uring the initial start-up period, however, new operational requirements and variations in volume may temporarily change unit costs for some service categories."[57] In addition, they set forth that "[t]he structure of fees and service arrangements may be designed both to improve the efficient utilization of Federal Reserve services and to reflect desirable longer-run improvements in the nation's payment system."[58]

While acknowledging that it does not expect to achieve full recovery of costs of FedNow within the ten-year period, which is typically applied to existing, mature services, the Fed claimed it will eventually satisfy the Cost Recovery Criterion.[59] In justifying its assertion, the Fed demonstrated that neither the MCA itself nor its legislative history defines the time period that constitutes the long run.[60] The Fed also insisted that, unlike other existing, mature services, FedNow is a new service that would require high development costs and initially have a low and unpredictable customer base.[61] Accordingly, the Fed determined that full recovery of costs of FedNow outside the ten-year timeframe is consistent with the aforementioned pricing principles and, therefore, that the Cost Recovery Criterion is satisfied.[62]

[56] *The Fed Pricing Principles*, *supra* note 54 (indicating a pricing principle that is additional to those prescribed in the MCA).
[57] *Id*. (qualifying the aforementioned pricing principle).
[58] *Id*. (exhibiting another pricing principle that is additional to those prescribed in the MCA).
[59] 2019 FR Notice, *supra* note 3, at 39,313 ("[T]he [Fed] expects that [FedNow] would achieve full recovery of costs over the long run, although the first instance of long-run cost recovery is expected to occur outside the 10-year period that the [Fed] typically applies to existing, mature services.").
[60] *Id*. ("The MCA does not specify the 'long- run' period over which Federal Reserve services must recover costs, nor does the legislative history of the MCA indicate that Congress intended a specific length of time for the cost recovery period.").
[61] *Id*. (justifying the difference on the grounds that "a new service generally involves high development costs" and that "a new service may not initially have a critical mass of customer participation and, as a result, is likely to have low and unpredictable initial volumes").
[62] *Id*. at 39,313–14 (asserting that FedNow "is nevertheless expected to achieve full recovery of costs over the long run in compliance with the [Fed]'s Cost Recovery Criterion" and that "an expected cost recovery period of longer than 10 years is appropriate").

E. Countervailing Concerns and Refutations

While the Fed argues in favor of its development of FedNow,[63] the following three countervailing concerns about FedNow deserve attention: (1) shortcomings of a RTGS system, (2) challenges related to the cost recovery, and (3) the existence of the private-sector RTGS service.[64] Nonetheless, these countervailing concerns may not ultimately put a halt to FedNow.[65]

1. Shortcomings of a RTGS System

First, a fast payment with a RTGS system has certain inherent vulnerabilities.[66] While a fast payment with a RTGS system is generally not susceptible to credit risk, it is still susceptible to liquidity issues.[67] By its nature, a fast payment with a RTGS system requires banks to have sufficient liquidity of funds at all times in order to meet the demands of their customers.[68] Such liquidity issues are particularly problematic for small banks, which do not have the same liquid capital as large banks, or in times of financial crisis.[69] Furthermore, a fast payment with a RTGS system more likely invites fraudulent

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[63] *See supra* notes 42–62 and accompanying text (describing the Fed's favorable assessment of FedNow).
[64] *See infra* notes 66–83 and accompanying text (considering three arguments against FedNow).
[65] *See infra* notes 84–98 and accompanying text (discussing refutations to the three countervailing concerns about FedNow).
[66] CPMI FAST PAYMENTS, *supra* note 2, at 47–51 (discussing various risks associated with a fast payment service).
[67] *Id.* at 48–49 (finding that "liquidity risk arises in the fast clearing and settlement system, because the participating [banks] require liquidity" for the settlement service, even though "[c]redit risk does not normally affect the fast clearing and settlement systems").
[68] *Id.* at 49 ("In fast payment systems with real-time settlement, liquidity needs are continuous, and payments could be rejected if the payer's [bank] lacks funds for settlement.").
[69] Julius Weyman, *Risks in Faster Payments* 4 n.4 (Fed. Reserve Bank of Atlanta, Retail Payments Risk Forum Working Paper, 2016), https://www.frbatlanta.org/-/media/Documents/rprf/rprf_pubs/2016/risks-in-faster-payments.pdf [https://perma.cc/K6KK-JT8W] (noting that "[f]unding liquidity is most commonly an issue for small businesses at almost any time and can become particularly acute during financial downturns or crises").

transaction attempts than traditional payment methods.[70] A fast payment with a RTGS system may have difficulty in detecting and recovering funds from fraudulent transaction attempts because payees have essentially immediate access to funds and such funds are final.[71] In addition, given the substantial use of financial technologies in a fast payment, such fraud risk may be further intensified by cyber risk, which is "the risk of harm, disruption, or damage . . . from some type of failure of [banks'] information technology systems."[72]

2. *Challenges Related to Cost Recovery*

Moreover, as aforementioned, uncertainties remain whether and when the Fed would achieve full recovery of costs of FedNow.[73] The fact that FedNow is a new service that would require high development costs and initially have low and unpredictable customer base undermines the prospect of full recovery of costs even after the conventional ten-year timeframe.[74] Moreover, the existence of more than 10,000 heterogeneous banks[75] may hinder full recovery of costs, especially if costs depend on the number of banks or their diverse sizes, practices, and interests.[76] In addition, a bill recently introduced

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[70] CPMI FAST PAYMENTS, *supra* note 2, at 50 ("[T]aking into account the end-to-end speed and, in particular, the immediacy of funds availability, fast payment services may be a more attractive target for fraud than traditional retail payments.").
[71] *Id*. ("If funds are immediately and unconditionally available to the payee, a fraudster could attempt to quickly withdraw the funds before the fraud is detected, and measures to reverse or recall fraudulent fast payments may have limited effectiveness.").
[72] Weyman, *supra* note 69, at 14–15 (describing the exacerbation of fraud risk by cyber risk).
[73] *See supra* Part D (demonstrating the Fed's expectation to achieve full recovery of costs of FedNow in the long run, albeit not within ten years).
[74] 2019 FR Notice, *supra* note 3, at 39,313 (observing that some commentators found the full recovery of costs of FedNow unlikely given "the significant cost of developing and operating such a service").
[75] *Id*. at 39,300 n.19 (noting that "[t]he United States has more than 10,000 depository institutions that vary greatly in terms of size, level of technical capabilities, operational practices, and customers and communities served").
[76] CLAIRE GREENE ET AL., COSTS AND BENEFITS OF BUILDING FASTER PAYMENT SYSTEMS: THE U.K. EXPERIENCE AND IMPLICATIONS FOR THE UNITED STATES 42 (2014), https://www.bostonfed.org/publications/current-policy-perspectives/2014/costs-and-benefits-of-building-faster-payment-systems-the-

in the U.S. House of Representatives called the "Federal Reserve Accountability and Justification Act" proposes to require the Fed to satisfy the requirements including the Cost Recovery Criterion before introducing new services or substantially changing existing services.[77] Under the MCA, the Fed may be prohibited from providing its payment service when it fails to meet the Cost Recovery Criterion.[78]

3. *The Existence of the Private-Sector RTGS Service*

In addition, the existence of RTP raises opposition to the Fed's development of FedNow, mostly from large banks and private-sector payment service providers.[79] While the diversity of U.S. banks, the existence of the private-sector RTGS service without a nationwide reach, and the Fed's continued relationships with all U.S. banks as a payment services provider advocate for the development of FedNow,[80] the development of FedNow may also result in "market inefficiencies such as fragmentation and increased connection costs" and the hindrance of the advancement of RTP.[81] Moreover, where the Fed is

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uk-experience-and-implications-for-the-united-states.aspx [https://perma.cc/47BG-UGSG] (maintaining that "[i]f adoption costs of a new payment network depend on the number of banks or the dispersion of deposits among banks, then U.S. costs could be higher" than those incurred in the United Kingdom for its Faster Payment Service).

77 Federal Reserve Accountability and Justification Act, H.R. 3928, 116th Cong. (2019) (demanding that "the [Fed] satisfy certain requirements before providing any new payment service, or substantially changing or expanding any existing payment service").

78 *The Fed Policies*, *supra* note 42 (stating that "[i]f it becomes clear, however, that the service cannot be expected to meet cost-recovery objectives, the [Fed] would reassess the appropriateness of continuing to provide the service after taking into account its other objectives" and giving an example that "several Reserve Banks have stopped offering cash transportation in areas where an adequate level of this service is otherwise provided by the private sector").

79 *See, e.g.,* 2019 FR Notice, *supra* note 3, at 39,305, 39,309 (displaying arguments against the Fed's development of FedNow on the basis of RTP and its services).

80 *Id*. at 39,309–10 (illustrating the facts in favor of the Fed's development of FedNow).

81 *Id*. at 39,305, 39,309 (reviewing potential harms of FedNow in consideration of the fact that a private-sector RTGS service already exists).

not fully committed to the interoperability between FedNow and RTP,[82] FedNow may fail to accomplish a ubiquitous and efficient fast payment system.[83]

4. *Refutations to the Countervailing Concerns*

Nevertheless, those countervailing concerns may be either mitigated by additional measures or outweighed by the expected benefits of FedNow. To begin with, in connection with the Other Providers Criterion and the Public Benefits Criterion, the expected benefits from the Fed's development of FedNow appear to be reasonably substantial.[84] Then, regarding the first countervailing concern, the Fed is well-positioned to reduce liquidity risk as the central bank of the United States.[85] The Fed provides intraday liquidity to eligible banks[86] for its current payment services.[87] Accordingly, the Fed may alleviate liquidity risk in connection with FedNow by providing intraday credit, thereby leading to a safe fast payment service.[88] Furthermore, a credit transfer feature would systematically render FedNow less vulnerable to fraud risk.[89] Additionally, fraud risk may be managed not only by

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[82] *Id*. at 39,318 ("[T]he Federal Reserve intends to explore both interoperability and other paths to achieving nationwide reach in support of ubiquitous faster payments . . . .").

[83] Brannon, *supra* note 6 ("The market bifurcation that will ensue from the Fed's entry into the market will dissipate nearly all of the benefits from having such a system in the first place.").

[84] *See supra* Part D (discussing the assessment that FedNow would bring about an effective and accessible fast payment service nationwide).

[85] CPMI FAST PAYMENTS, *supra* note 2, at 60 (observing that central banks "normally establish and operate mechanisms to provide intraday liquidity (usually against collateral or at a certain cost)").

[86] 2019 FR Notice, *supra* note 3, at 39,319 n.115 (noting that "[i]ntraday credit is generally available to banks that are financially healthy and have regular access to the discount window").

[87] *Id*. at 39,319 ("To support their current payment services, the [Federal] Reserve Banks provide liquidity in the form of intraday credit, also known as daylight overdrafts, to eligible banks and subject to the Federal Reserve's Policy on Payment System Risk (PSR Policy).").

[88] *Id*. ("Intraday credit supports the smooth functioning of the payment system by supplying temporary liquidity to cover shortages that can result when the timing of payment inflows and outflows are not balanced.").

[89] *Id*. at 39,317 n.99 ("Because credit transfers require the sender to authorize and initiate each individual payment, services based on such transfers can decrease the risk of fraudulent or otherwise unauthorized payments.").

transactions monitoring both by banks and the Fed[90] but also, as aforementioned, by the service amount limit.[91]

As to the second countervailing concern, because neither the MCA itself nor its legislative history specifies the period that constitutes "the long run,"[92] imposing an undifferentiated timeframe may deprive the Fed of the opportunity to modernize the U.S. payment system.[93] The Fed's development of the FedACH service is a case in point: the FedACH service's long-term public benefits justified an extended cost recovery period and its cost recovery was accordingly achieved.[94] Moreover, under the MCA, the Fed may still weigh FedNow's benefits against challenges associated with the cost recovery.[95] In light of FedNow's expected benefits to the public, its expected cost recovery outside the ten-year time frame may not be sufficient to stop the Fed from developing FedNow.[96] Lastly, with

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[90] *Id*. at 39,320 (anticipating that "participating banks would continue to serve as a primary line of defense against fraudulent transactions" and that, "[a]t the payment system level, [FedNow] could offer additional fraud mitigation features, such as payment monitoring to alert participating banks of unusual transactions").

[91] *See supra* note 37 and accompanying text (indicating that the service amount limit would help alleviate fraud risk); *see also* Weyman, *supra* note 69, at 17 ("A review of systems already in place suggests that one of the more prudent mitigating controls for a faster payment scheme may be a dollar threshold.").

[92] *See supra* note 60 and accompanying text (deducing that the cost recovery period needs not be a ten-year period).

[93] 2019 FR Notice, *supra* note 3, at 39,313 ("Applying such a standard could limit the Federal Reserve's ability to develop new services or undertake major service enhancements that support the provision of an adequate level of services nationwide or induce desirable long-term changes in the payment system.").

[94] *Id*. at 39,313–14 (explaining the development of the FedACH service and its cost recovery, where "the service first achieved annual cost recovery nearly 15 years after launching a pilot in 1972, and achieved 10-year cost recovery after more than 20 years of operation").

[95] *The Fed Policies*, *supra* note 42 ("Because the Monetary Control Act directs the Federal Reserve to give due regard to competitive factors, a decision would have to be made whether the public benefits of continuing to offer the service justify the shortfall.").

[96] *See* 2019 FR Notice, *supra* note 3, at 39,314 (claiming the compliance with the MCA's requirement on the grounds that, "in the absence of the FedNow Service, the objective of achieving an adequate level of service nationwide to

regard to the third countervailing concern, the existence of a private-sector RTP may not be an adequate reason to forgo the development of FedNow given the considerable advantages of a fast payment service.[97] Furthermore, the simple existence of RTP, without more, may be the very reason for the Fed's entry into the fast payment service; such advantages of a fast payment service may not be realized to the fullest extent without competition and cooperation.[98]

F. Conclusion

The Fed's decision to develop FedNow is laudable considering its expected benefits, and it is generally supported by the public.[99] In particular, a fast payment service would help not only consumers and businesses in managing their money but also banks in generating profits.[100] On the other hand, some reservations about whether the Fed can and should develop FedNow have been identified, including shortcomings of a RTGS system, challenges related to the cost recovery, and the existence of a private-sector RTGS service.[101] However, a comprehensive understanding of a fast payment service and FedNow's specific features would likely favor the Fed's development of FedNow.[102]

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support the development of ubiquitous RTGS-based faster payments in the United States is unlikely to be realized").

[97] *See supra* notes 16–17 and accompanying text (manifesting expected benefits of a fast payment service to its participants).

[98] 2019 FR Notice, *supra* note 3, at 39,300 (speculating that "a single provider of RTGS services for faster payments without competition is likely to create undesirable outcomes for pricing, innovation, service quality, and reach" whereas "[t]he presence of multiple RTGS services for faster payments could yield efficiency benefits such as lower prices, higher service quality, and increased innovation").

[99] *See generally id*. (indicating that most commentators are positive about the Fed's plan to develop FedNow).

[100] *See supra* notes 16–17 and accompanying text (describing expected benefits of a fast payment service to both end users and banks).

[101] *See supra* notes 66–83 and accompanying text (demonstrating the three countervailing concerns about FedNow).

[102] *See supra* notes 84–98 and accompanying text (arguing against the countervailing concerns about FedNow).

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