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Improving the U.S. Payment System: Progress, Challenges, and Opportunities Ahead

Remarks by

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The views expressed by the author are her own and do not necessarily reflect those of the Federal Reserve System, its governors, officers or representatives.

Good morning. I am pleased to be with you today to discuss the work of our payments coalition to improve the speed, efficiency and security of the U.S. payment system.

When we began this work nearly two years ago, we understood it would be challenging. We set forth ambitious outcomes that called for a new and different environment in which payments could be made on mobile platforms, on any day, in real time, and with the certainty that the highest level of security would protect both the sender and the recipient in the transaction. We also understood the need to act deliberately, but on an aggressive schedule, because we saw countries around the world moving swiftly to develop their own real-time payments infrastructure.

Today, I would like to spend some time updating you on the progress of this work. I'll discuss the approach we have taken to facilitate this activity and provide some detail about the work being done by both our Faster Payments and Secure Payments Task Forces. I'll conclude with a few thoughts on where their efforts are headed and what to expect in the year ahead, including some of the challenges we will face.

The Case for Faster Payments in the United States

The U.S. payment system effectively supports the largest economy in the world, and has a long history of evolving to meet changing needs. In early 2015, the Federal Reserve issued a call to action in the form of a paper, titled ***Strategies for Improving the U.S. Payment System***, that outlined the collective thinking of U.S. payment system stakeholders and the Federal Reserve on ways to improve the system.

The vision set out in the paper framed specific strategies designed to meet the growing demands of American consumers and businesses that continue to shift their daily transactions toward e-commerce and Internet-enabled technologies. The strategies are based on five desired outcomes for improvements in the following areas: speed, security, efficiency, cross-border payments and industry collaboration. We also committed to make improvements to the payment services provided by the Federal Reserve.

As the central bank of the United States, the Federal Reserve is uniquely positioned to facilitate the stakeholder collaboration needed to provide widespread access and the adoption of new payment system capabilities. For at least the last 50 years, mutual cooperation on payment issues between the Federal Reserve and the private sector have contributed to a more resilient payment system, yielding significant benefits to the public and the economy as a whole.

To be sure, this approach has had its detractors, including those who thought that any attempt to produce significant change in our diverse payments landscape would be hampered by proprietary interests and a lack of cooperation. But that thinking underestimated the interest and willingness of industry participants to cooperate and to produce a result that none could achieve on their own.

Over the past two years, we have brought together hundreds of interested parties and stakeholders in a broad and highly-motivated coalition that is working together to identify both the promise and the challenges of making end-to-end payment system improvements a reality.

Faster Payments Task Force

Central banks around the world have used government mandates to provide the control and direction needed to complete large-scale national initiatives such as payment system improvement. Here in the United States, the absence of a government mandate and the recognition that significant investments in legacy systems were in place, led to a different approach.

The Faster Payments Task Force now has more than 320 members comprising a variety of interests: technology providers; small, medium and large financial institutions; payment networks; trade associations; business end users; and a small number of government officials. Importantly, and in many respects unique to such initiatives, the Task Force also includes the representation of consumer groups.

The Task Force has made remarkable progress and I'd like to give you a sense of what has been accomplished. Early on, the Task Force committed to a framework that would ensure decisions and work products would have the broad support of its membership, both within and across the various groups represented. With this understanding, they were able to define detailed criteria for judging the effectiveness needed to deliver faster payments and assess alternative approaches for faster payments solutions.

In January, the Task Force created a portal-based forum where solution providers, from both the general public and within the Task Force, could showcase their payments capabilities. In this way, firms intending to create full end-to-end payment solutions were able to view technologies and services that might help fill gaps in their proposals. To date, more than 30 firms — from small startups to large payments and technology

companies — have submitted product descriptions or short videos to the online forum, offering a range of expertise.

Soon after the creation of the capability showcase forum, the Task Force solicited proposals for faster payment solutions. Those making submissions were asked to illustrate what their solution would do at each stage of the end-to-end payments process, from the initiation of a transaction through the completion of a payment and reconciliation of account balances. An outside consultant, McKinsey & Company, was chosen to conduct an independent assessment of each proposal against the criteria developed by the Task Force.

In total, 22 proposals have been reviewed in the first phase of the assessment process that occurred from May through September of this year. Just last week, the proposals were released to both the Faster Payments Task Force and the Secure Payments Task Force, for review and critical feedback. After receiving comments, those who submitted the proposals will decide whether to remain in the process and release their proposals to the general public. The proposals that remain will be included in the Task Force's Final Report to be published in 2017, along with the assessment results and Task Force commentary.

Beyond the evaluation of individual proposals, the Task Force review will consider broadly the structural challenges that could affect the implementation of faster payments solutions. In a session later today, you'll hear more about how the Task Force is considering these issues, but let me share some of my views now for the challenges to be addressed.

Given the nature of market-driven solutions, interoperability will be a key concern. This is one of the current payments system gaps that led to establishing the Faster Payments Task Force. Markets have produced a number of fragmented solutions that deliver desired functionality, but have failed to deliver a ubiquitous and seamless experience for end users.

Interoperability requires a careful consideration of rules, standards and governance. We take for granted the ubiquity of our current infrastructure as represented in the use of debit and credit cards, ACH and check transactions. But, the interoperability we enjoy with these systems today didn't happen overnight. In fact, it took years and in some cases was cobbled together piece by piece across multiple providers. As we contemplate faster payment capabilities for the United States, the industry has an opportunity to take a more proactive approach on these issues and consider a path to adoption so that all consumers and businesses may benefit from these capabilities.

Progress on bringing faster payments to the United States must keep in focus the fundamental responsibility to ensure the overall safety and integrity of the payment system. Real-time payments present some new risks in addition to those with which we are already familiar.

Experiences around the world and here in our own system prove that these risks can be effectively managed and real-time payments can be safely and securely provided. However, the challenges we face in successfully achieving our desired outcomes for faster payments will require the same industry collaboration that has brought us to this point. I commend the efforts of the Task Force to anticipate these challenges and opportunities, and I look forward to their recommendations in this regard.

Secure Payments

Regarding the issue of security, there should be no doubt that dynamic, persistent and escalating threats are challenging public confidence in the U.S. payment system. The growing scale, sophistication, and global nature of cyber threats, along with the proliferation in points of vulnerability, has made security a key priority for financial institutions, payments providers, central banks and regulators around the world.

More than 170 individuals joined the Secure Payments Task Force in 2015 to address the most pressing challenges in our existing payment systems and to define the criteria for a safe and secure faster payments future. Let me highlight two areas where this Task Force is focused today.

Preventing and managing fraud is a key challenge given certain inherent limitations and weaknesses in existing payment systems and processes. Today, there is no universally accepted way to establish and verify the identity of a payment system participant. The Task Force has begun to address this problem. Their work will consider the identification and adoption of payment identity management practices, as well as the opportunities to share fraud and cyber-threat information and how to analyze related data.

These efforts all promise to produce valuable information, tools and insight for the industry. Driving widespread adoption of security improvements, however, remains a considerable challenge. Fortunately, U.S. payment system security is strong. And although we remain vigilant, we must keep pace with the rapidly-evolving and expanding risks that threaten the payments ecosystem. I commend the work of the Secure Payments Task Force and the collaboration it brings to these important issues.

Beyond Task Force Efforts

In addition to the work of these Task Forces, the Federal Reserve itself is involved in improving efficiency in the payment system. Through its longstanding partnership with the Business Payments Coalition, real progress has been achieved in terms of educating small businesses on electronic payments, advancing the development and adoption of standards, and understanding and addressing the barriers to straight-and-through processing. Of note this year is the establishment of the Business Payments Directory Association, which is working to create a business-to-business directory to facilitate easy, electronic origination of business payments.

And in discussing our collective accomplishments in improving the payment system, the industry realized an important milestone last month to enhance the speed of the ACH network with implementation of the first phase of SameDay ACH. Within the Fed, we've invested in speeding check clearing and ACH payments, enhancing settlement services, and enriching information services to better support risk and compliance management needs. In partnership with the industry, we are working to align wire transfer and ACH systems to global message standards to meet user needs, pave the way for greater domestic and cross-border interoperability, and ensure a U.S. payment system that is relevant and competitive in the global market.

Looking Ahead

After almost two years, I am pleased at the progress we've made. We expect to mark some significant developments next year. In the first half of 2017, the Faster Payments Task Force is scheduled to issue its report in two parts. The first is expected to

lay out the case for faster payments in the United States, and to describe the process undertaken to evaluate proposals for improvements. The second part of its report will include their review of the specific proposals submitted. It will outline what an end-to-end faster payment system could look like in the United States and discuss the possible effectiveness of different proposals, while highlighting strategic issues deemed important to the successful development of faster payments and actions needed to advance implementation and adoption.

Likewise, the Secure Payments Task Force is likely to publish its views on the key issues it has identified, including payment identity management, information sharing, data protection, and other payment system security issues sometime next year.

These reports will mark important milestones, but I believe our greatest challenge going forward is maintaining the momentum we have achieved so far. It's also likely that some of our most difficult tasks lay ahead. Much of our collective work to date might be described as identifying or designing solutions. We all know that in a marketplace as complex as our payment system, the real work comes in driving successful implementation and adoption all the way from the central infrastructures through the banking and technology spaces to the hundreds of millions of consumers and business who use these services.

As some of these first steps in our payments improvement journey draw to a close or reach major milestones over the next year, we look forward to further collaborating to divine the way forward toward our desired outcomes. The Fed's priority in this important initiative has been to advance and support improvements that are in the public interest and will contribute to long-term financial stability and economic growth. We remain

committed to achieving those outcomes so that consumers and businesses have access to an efficient, real time and highly secure payment network in the United States.

Thank you.