

Best Buy Co., Inc.'s Response

Federal Reserve's Public Consultation Paper

Submitted by Dee O'Malley

December 2013

Best Buy Co., Inc. ("Best Buy", or "we") is the world's largest multi-channel consumer electronics retailer with stores in the United States, Canada, China, and Mexico. BestBuy.com is among the top ten retail websites in the United States and we have the number one customer loyalty program of its kind. There are more than 1 billion visitors to our website and 600 million visits to our U.S. stores each year.

We welcome the opportunity to submit comments on behalf of its United States organization in response to the Payment System Improvement - Public Consultation Paper ("Consultation Paper") issued by the Federal Reserve Banks on September 10, 2013. Best Buy applauds the Federal Reserve's leadership role both in recognizing the need to develop ubiquitous near real-time payment solutions for low value transactions in the United States and in launching an initiative to address this important issue.

Please contact Dee O'Malley, Senior Director, Payments Acceptance, Financial Services with any questions regarding this response to the Consultation Paper

General

- 1) Are you in general agreement with the payment system gaps and opportunities identified above? Please explain, if desired.

Yes. As detailed in the Retail Industry Leaders Association's Response to the Federal Reserve's Public Consultation Paper, dated December 2013 ("RILA's Response"), improvements to the U.S. payment system are needed to benefit all constituents, including consumers, merchants and issuers. The current system should be updated and enhanced to align with the way consumers want to transact and to keep pace with the rapid technological advancements. If the gaps are not properly and expeditiously addressed, they will pose greater security, fraud and legal risks, which will negatively impact consumers and all stakeholders

- i) What other gaps or opportunities not mentioned in the paper could be addressed to make improvements to the U.S. payment system?

The following should be part of any new U.S. payments system assessment:

- **Security**
There are important technology and operational gaps in the security of the card payments processes which are in need of remediation including the continued use of static payment credentials, reliance on a signature as a valid cardholder verification method and lack of investment in interim secure payment solutions for mag stripe technologies.
- **Card Fraud & EMV**
Attention is needed in regard to Europay, Mastercard and Visa ("EMV"), as currently brought to market by the payment card brands in the United States. We believe EMV as implemented in Europe in 2005 worked well for the point

of sale payment systems by reducing card present fraud. However, a significant increase in card-not-present fraud continues to manifest itself and has resulted in a shift in fraud from 'one bucket to another'. Compounding this in the US is the decision to support chip and signature as a cardholder verification method (CVM) versus mandating chip and PIN. The expected increases in card not present fraud combined with not fully securitizing the point of sale much of the value EMV can bring in reducing fraud. There is a need to look broadly at consumer payment patterns and preferences and make adjustments - with input from all stakeholders - which address fraud through all current and potential future channels.

- **Payment Economics**

Best Buy's primary concern with the identified gaps is that it assumes that 'in place' systems and processes would be maintained and extended. We believe that without systemic changes in the way the primary payment card stakeholders interoperate both systemically and operationally, the U.S. will continue to have one of the most expensive card payment systems in the developed world. A key outcome of this process should be a method for ensuring that the systemic and operational processes can more closely reflect those of countries whose costs, risks and benefits appear to be apportioned amongst all key payment stakeholders and includes merchants. We believe the bipartisan debit card interchange fee reforms enacted in 2010 are an important step in the right direction.

ii) Are you in general agreement with the desired outcomes for payment system improvements over the next 10 years? Please explain, if desired.

Best Buy agrees with the desired outcomes for payment system improvements; however, as detailed in RILA's Response, meaningful changes are needed to ensure that systemic flaws are not perpetuated.

iii) What other outcomes should be pursued?

Desired Outcome 6:

Market based pricing for card payments should be encouraged by reducing the barriers to entry for other potential competitors in the card processing market. This could be done through incenting financial institutions, processors and others who might have the ability to enter the market but are concerned about the cost, retribution from existing providers, and risks.

2) In what ways should the Federal Reserve Banks help improve the payment system as an operator, leader, and/or catalyst?

We believe there are a variety of implementation roles the Federal Reserve could play relative to the key payment initiatives, including the roles detailed below. We also support the RILA position that using existing government bodies (e.g. the Federal Financial Institutions Examination Council - FFIEC) or any future body which would include merchant's full participation would be a significant contributor to improving the US payments landscape.

	Leader (Federal Reserve Banks as champion)	Catalyst (Federal Reserve Banks as regulator)
EMV	<ul style="list-style-type: none"> ▪ Heavier engagement in EMV Migration Forum (EMF) as setting the tone for the EMV migration. Currently, the brand strategy puts the consumer card experience at 	<ul style="list-style-type: none"> ▪ Encourage 'open' EMV technology and intellectual property through providing appropriate financial and regulatory guidance in areas of standards and through standards bodies

	the point of sale at risk. The emerging recommendations and positions are very concerning and will result in a confusing, disjointed, and ultimately less secure experience at the point of sale	
Mobile Payments	<ul style="list-style-type: none"> ▪ Encourage the development of solutions which could be used across a broad array of technologies through the publishing of standards, producing of technology, or creation of regulations which encourage open, market-driven solutions 	<ul style="list-style-type: none"> ▪ Institute regulations which encourage open, market-driven solutions
Fraud Mitigation	<ul style="list-style-type: none"> ▪ Encourage open, cross-pollination of fraudulent account information, when appropriately identified 	<ul style="list-style-type: none"> ▪ Provide the regulatory framework which allows for the sharing of fraudulent accounts when identified
Security	<ul style="list-style-type: none"> ▪ Support technology providers who work with banks in facilitating technologies which focus on dynamic account generation which could lead to eliminating the payment card industry data security standards (PCI-DSS) 	<ul style="list-style-type: none"> ▪ Incent the development and implementation of dynamic payment generation technologies
Payment Economics	<ul style="list-style-type: none"> ▪ Lead in the definition of open and freely available standards for mobile payments and EMV debit application in order to ensure merchants can exercise their routing rights 	<ul style="list-style-type: none"> ▪ Implement rules designed to ensure competitive pricing in payments markets through reducing barriers to entry for competitors

Ubiquitous near-real-time payments

3) In discussions with industry participants, some have stated that implementing a system for near-real-time payments with the features described in the second desired outcome (ubiquitous participation; sender doesn't need to know the bank account number of the recipient; confirmation of good funds is made at the initiation of the payment; sender and receiver receive timely notification that the payment has been made; funds debited from the payer and made available in near real time to the payee) will require coordinated action by a public authority or industry group. Others have stated that current payment services are evolving toward this outcome and no special action by a public authority or industry group is required.

i) Which of these perspectives is more accurate, and why?

Implementing a system for near-real-time payments with the features described in the second desired outcome will require coordinated action by a public authority or industry group. The current system benefits the legacy payment providers and there are no current incentives to implement changes that will benefit the payment system stakeholders.

ii) What other perspective(s) should be considered?

The interests of the merchants and the consumers we serve are closely aligned. In order to make near, real-time payments for merchants and the consumers we serve, there will need to be strong action and facilitation amongst all stakeholders to incent the market to bring the appropriate technology to market.

- 4) The second desired outcome articulates features that are desirable for a near-real-time payments system. They include:
- a) Ubiquitous participation
 - b) Sender doesn't need to know the bank account number of the recipient
 - c) Confirmation of good funds is made at the initiation of the payment
 - d) Sender and receiver receive timely notification that the payment has been made
 - e) Funds debited from the payer and made available in near-real time to the payee
- i) Do you agree that these are important features of a U.S. near-real-time system? Please explain, if desired.

Yes, these generally should be the characteristics of a near-real-time payment system; however, we encourage a broader view beyond transfers between bank accounts. This should be extended to include a wider array of payment types used in today's world including what could be new and emerging tender types (e.g., digital currency, loyalty points, etc.) which are growing rapidly in popularity and consumer demand.

- ii) What other characteristics or features are important for a U.S. near-real-time system?

A core principle should be equitable access, security, dynamic and one-time use technology for POS and .com/CNP transactions, and the prevailing economics need to be based on a cost+ system.

- 5) Near-real-time payments with the features described in the second desired outcome could be provided several different ways, including but not limited to:
- a) Creating a separate wire transfer-like system for near-real-time payments that leverages the relevant processes, features, and infrastructure already established for existing wire transfer systems. This option may require a new front-end mechanism or new rules that would provide near-real-time confirmation of good funds and timely notification of payments to end users and their financial institutions.
 - b) Linking together existing limited-participation networks so that a sender in one network could make a payment to a receiver in another network seamlessly. This option may require common standards and rules and a centralized directory for routing payments across networks.
 - c) Modifying the ACH to speed up settlement. This option may require a new front-end mechanism or new network rules that would provide near-real-time confirmation of good funds and timely notification of payments to end users and their financial institutions. Payments would be settled periodically during the day.
 - d) Enhancing the debit card networks to enable ubiquitous near-real-time payments.
 - e) Implementing an entirely new payment system with the features described in the second desired outcome above.
- i) What would be the most effective way for the U.S. payment system to deliver ubiquitous near-real-time payments, including options that are not listed above?

Any payment system which would represent ubiquitous near-real-time payments should include the following components as key to the underlying framework:

- **Market Pricing**
Cost must be tied to 'market forces' which are clearly a 'free' market. The current card payment market lacks real competition and we would encourage efforts to reduce the barriers for entry to potential competitors.
- **Open Standards**
Although not every payment type or area should be based on open standards, we believe that relative to core capabilities such as real-time payments, EMV, and mobile payments, an open standards-based approach is the most cost effective method which would lead to the most creative and innovative solutions. The approach could include a range of options, including one in which the federal government facilitates the development of standards which could fall under a variety of licensing processes and agreements. The federal government should play a role in the standards and technology areas by facilitating the development of open standards and ensuring that the market then uses those standards in an efficient and open fashion
- **Flexible and Extendable**
Any near-real-time system should be flexible and able to accommodate the broadest range of payment types.

ii) What are the likely pros and cons or costs and benefits of each option? What rule or regulation changes are needed to implement faster payments within existing payment processing channels?

	PRO	CON
a)	<ul style="list-style-type: none"> ▪ Hardware and software are 'in place' ▪ Scalable ▪ Reliable ▪ Trusted ▪ 'Good funds' model 	<ul style="list-style-type: none"> ▪ Economics would need to be understood (Pricing, risk, security)
b)	<ul style="list-style-type: none"> ▪ Standards are key to the success of this option 	<ul style="list-style-type: none"> ▪ Common standard required ▪ Too many 'moving parts' ▪ Difficult to ensure compliance
c)	<ul style="list-style-type: none"> ▪ Hardware and software are 'in place' 	<ul style="list-style-type: none"> ▪ Many system/operational challenges
d)	<ul style="list-style-type: none"> ▪ Hardware and software are 'in place' 	<ul style="list-style-type: none"> ▪ Many hurdles in connecting 'end points'
e)	<ul style="list-style-type: none"> ▪ Market pricing (Potentially) ▪ Open Standards (Potentially) 	<ul style="list-style-type: none"> ▪ Cost ▪ Trust ▪ Security

iii) Is it sufficient for a solution to be limited to near-real-time authorization and confirmation that good funds are on their way, or must end-user funds availability and/or interbank settlement take place in near-real time as well?

We anticipate different needs, based upon payment type and other circumstances. We encourage an approach that allows for the spectrum of payments participants to be able to 'buy-in' to the services that best meet their needs, keeping in mind that a multi-channel approach is warranted.

- iv) Which payment scenarios are most and least suitable for near real-time payments? (B2B, P2P, P2B, POS, etc.)

There is a case that could be made for real-time payments across all identified payment channels. Our interest is in retail point of sale transactions and .com transactions which are certainly suitable use cases.

- 6) Some industry participants have said that efforts to make check payments easier to use, such as by enabling fully electronic payment orders and/or by speeding up electronic check return information, will incrementally benefit the payment system. Others argue the resources needed to implement these efforts will delay a shift to near-real-time payments, which will ultimately be more beneficial to the payment system. Which of these perspectives do you agree with, and why?

There have been significant advances in check electrification which have positively impacted check acceptance at the point of sale e.g. Check 21. We support efforts which focus resources on enabling real time payments at the point of sale as the value this could bring to consumers and merchants is well founded.

- 7) How will near-real-time payments affect fraud issues that exist with today's payment systems, if at all?

We are supportive of the industry perspective - articulated through RILA - which details a specific framework for real-time payments, the recommended governance model and recommendation that fraud should be the responsibility of the stakeholder(s) who has the greatest ability to prevent it.

- i) Will near-real-time payments create new fraud risks? If yes, please elaborate on those risks.

The greatest risk is 'claw backs'. The technology and solutions which are brought to market to enable any future real-time payment system should be accompanied by new regulations to eliminate any penalties, contractual prohibitions, or other restrictions for use of such a system.

- 8) To what extent would a ubiquitous near-real-time system bring about pivotal change to mobile payments?

The most impacted area of the payments value chain of a real-time payments capability will most likely be in person-to-person payments. The major limitation of person-to-person adoption to date has been payment timing and funds availability, required banking relationships, regulatory complexity, and lack of ubiquity or ease of use. If a real-time payment system is truly cross-bank capable and provides an easy to use consumer process this could be one of the more transformative outcomes of any real time payment capability.

- 9) What would be the implication if the industry and/or the Federal Reserve Banks do not take any action to implement faster payments?

There are two primary areas which would be negatively impacted:

- **International Reputation**
It appears that we are not progressing to the degree that other developed countries are relative to security and real time payments.
- **Competitive Business Advantage**
The U.S. risks loss of business and investment if our banking system cannot align with what is a standard in the rest of the world. Real-time payments, both from the payer

and receiver, have an advantage. This is not to say that every interaction and every transaction is required to be in 'real-time'. However, for many transactions that U.S. consumers make on a daily basis, this would add to the ability of merchants, banks and others to validate funds availability sooner, allow for more nimble risk mitigation strategies, and more effectively fund accounts and help liquidity.

- i) What is the cost, including the opportunity cost, of not implementing faster payments in the United States?

Please see comments above.

As discussed we believe there is an opportunity and hard cost which at some point will be damaging to the US from a reputational and commercial viability standpoint.

- 10) To what extent will the industry need to modernize core processing and other backend systems to support near-real-time payments?

In order to address this sufficiently, the federal government should first understand what the industry requirements are from all the key stakeholders (including merchants and their customers), analyze impacted systems, perform a gap analysis and then recommend a solution.

With that in mind the following should be key capabilities which should be part of any real-time payments system overhaul and something which core payment systems should be able to support:

- (1) Dynamic Credentialing**
- (2) Real-time fraud detection**
- (3) Good funds with reversibility**
- (4) Good funds with no reversibility**
- (5) Multi-device support
PC, Tablet, Phone, other**
- (6) Multi-Channel support
POS & CNP**

- i) What is the likely timeframe for any such modernization?

A 10-year horizon was referenced in the Consultation Paper. We see this as a capability which should be brought to market in the next 5 years.

- 11) Some industry participants suggest that a new, centralized directory containing account numbers and routing information for businesses and/or consumers, to which every bank and other service providers are linked, will enable more electronic payments. A sender using this directory would not need to know the account or routing information of the receiver.

- ii) What are the merits and drawbacks of this suggestion?

Centralization of account could be a viable option. Best Buy's thoughts on merits and drawbacks are listed below.

Merits include:

- More streamlined account validation process**
- More efficient account management**
- Easier to provide a 'single view' for those with multiple accounts**

Drawbacks:

- **A single source of failure**
- **Massive overhaul of systems (potentially)**
- **Single target for what could be constant probing and attacks**

iii) What is the feasibility of this suggestion?

The larger the system, the less flexible and the more difficult (and expensive) it will be to maintain over time. So, in essence it is intriguing but there are significant downsides which would need to be mitigated in order to make this a viable system.

Electronification

12) Some industry participants say that check use is an enduring part of the U.S. payment system and that moving away from checks more aggressively would be too disruptive for certain end users.

iv) Is accelerated migration from checks to electronic payment methods a high-priority desired outcome for the U.S. payment system? (Accelerated means faster than the current trend of gradual migration.)

Checks will be part of the U.S. payments ecosystem for a long time to come. However, Best Buy's customers' usage of checks has declined significantly over the past several years. We recommend continued progress as appropriate technologies are identified and brought to market, yet we do not see this as something which should be allocated unnecessary attention or resources. It is noteworthy that it costs much less for merchants to process checks than it does to process debit and credit card transactions in these modern times.

v) Please explain, if desired.

vi) If yes, should the Federal Reserve Banks establish a target for the percent of noncash payments to be initiated via electronic means, by a specific date? For example: "By the year 2018, 95% of all noncash payments will be made via electronic means."

vii) What is the appropriate target level and date?

13) Business-to-business payments have remained largely paper-based due to difficulties with handling remittance information. Consumer bill payments also are heavily paper-based due to the lack of comfort some consumers have with electronic alternatives. In addition, many small businesses have not adopted ACH for recurring payments due to technical challenges and/or cost constraints. The payment industry has multiple efforts underway to address these issues.

viii) To what extent are these efforts resulting in migration from checks to other payment types?

ix) What other barriers need to be addressed to accelerate migration of these payments?

x) What other tactics, including incentives, will effectively persuade businesses and consumers to migrate to electronic payments?

xi) Which industry bodies should be responsible for developing and/or implementing these tactics?

Cross-border payments

14) To what extent would the broader adoption of the XML-based ISO 20022 payment message standards in the United States facilitate electrification of business payments and/or cross-border payments?

Strategies that leverage open standards meet one of the conditions for encouraging technology providers to enter a marketplace and provide 'standards based solutions'.

15) What strategies and tactics do you think will help move the industry toward desired outcome four - consumers and businesses have greater choice in making convenient, cost-effective, and timely cross- border payments?

There are a number of common elements which we would encourage across the broad array of cross-border financial services:

Pricing Transparency, Ubiquity & Uniformity

Many of costs the cross border solutions provided by the financial services industry are generally lacking in transparency and/or are not known until after the time of transaction. We would encourage a more open system whose costs are clear, uniform and ubiquitous.

Improved Cross-Border Risk Modeling

We would encourage as part of any Federal Reserve fraud system remediation effort that international and cross-border payments be considered as part of that initiative. Much of the cost of cross border transactions is due to the risk of the transaction. It follows that if this risk could be mitigated or reduced the associated costs could be reduced.

Safety

16) Payment security encompasses a broad range of issues including authentication of the parties involved in the transaction, the security of payment databases, the security of software and devices used by end users to access payment systems, and security of the infrastructure carrying payment messages.

xii) Among the issues listed above, or others, what are the key threats to payment system security today and in the future?

The following are important components of payment security to be addressed for each payment type:

- **Cards**

As discussed, there should be an effort to support dynamically generated payment credentials which frees merchants from PCI compliance. The technology exists to provide a merchant with a verifiable payment credential which is not an account number. This could free up millions of dollars across the payments ecosystem which could be used for more valuable purposes. The most promising technology to emerge to secure the point of sale is EMV and that implementation is faltering.

The federal government should ensure new as well as existing providers of electronic payment systems and support are individuals who are not apt to "...Falsify interchange, deliberately misrepresent MCC codes and use extortion and intimidation tactics to enhance merchant retention..." as described recently by Bob Carr, Heartland Payment Systems *Reference: An Open Letter: Let's Put a Stop to Criminal Practices in Our Industry—Now! Oct. 28, 2013, <http://www.digitaltransactions.net/news/story/4341>.*

xiii) Which of these threats are not adequately being addressed?

EMV as constituted is not going to meet the objectives of either fully securing the point of sale or addressing card not present transactions.

xiv) What operational or technology changes could be implemented to further mitigate cyber threats?

There are a variety of technologies that are in the market which could assist in the mitigation of cyber threats. That said, realistically these threats evolve and morph continually and whatever technology is implemented will need to be updated in real time. A central fraud repository across all payment types is something which should be seriously considered

17) What type of information on threat awareness and incident response activities would be useful for the industry?

A national or regional system of fraudulent payment credentials would be very helpful. Assessment should be given to a central repository to serve as an 'early warning system for payments'. The issue with sharing information has always been who is getting the data, what are they going to do with it, and what is going to happen to the data down the road.

One approach could be to develop a system composed of a narrow data set (e.g., payment credential information in-transit, on-us transactions, CVV, account) without any additional information (e.g. SKU level data or personal data such as names, addresses etc..) and make this available through a securitized service which includes rules that govern access, data use and expiration.

xv) How should this information be made available?

The information should be made available across a broad array of transactions (e.g., banks, dotcom, POS, etc.) in real time and via a broad array of devices (e.g. tablets, PC's, phones). This could be in the form of a simple API to a regional or national source which would house 'bad' or compromised account numbers.

18) What future payment standards would materially improve payment security?

Inherent in the new system should be an allocation of risk and costs to the parties with a core focus of completely eliminating the need for merchants to handle account numbers. There are a variety of methods to enable the generation of dynamic credentials which represent an account number for presentment. This would materially improve payment security and free millions of dollars from the 'system' which could be allocated to more productive purposes.

19) What are the obstacles to the adoption of security-related payment standards?

There are two primary impediments:

- **Legacy Infrastructure**
- **Lack of open standards**

20) What collaborative actions should the Federal Reserve Banks take with the industry to promote the security of the payment system from end to end?

The FRB should engage with issuers, merchants, networks, and consumer groups around educating and incenting all parties to advocate and bring awareness to secure cardholder verification methods. Security is reliant on 'rules' and the associated go to market approach. The current card economics and 'rules' structure incent issuers to choose a less secure method of verification which has brought on significant cost to the ecosystem.

21) Please share any additional perspectives on U.S. payment system improvements.

The government has a critical and active role to play in the success of new and emerging payments, particularly in EMV and payment economics (facilitating price competitive marketplaces for financial services). As a major participant in the U.S. payment system as a merchant who constantly strives to improve customer service and experiences, we appreciate the opportunity to help the Federal Reserve in your oversight role to improve our payment system.