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Federal Reserve Banks
Financial Services

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Re: Payment Systems Improvement – Public Consultation Paper Comments

Dear Sirs:

Contact Name:	Lawrence F. Buettner
Organization Name:	Wausau Financial Systems
Type:	Technology Solution Provider/Processor

WAUSAU Financial Systems is a leading provider of receivables processing technology. Our products are used by more than 350 banks, telecommunication and insurance companies for processing lockbox transactions, remote deposit capture, and mobile capture payments. Although we have strong legacy roots in the capture of paper remittance processing, we are in the vanguard of innovation into digital payments.

The Federal Reserve Banks has laid out an ambitious vision for the payments industry in the *Payment System Improvement Consultation Paper*. WAUSAU is pleased to add our response to the public dialogue which the Federal Reserve has encouraged through the comment period on this topic. We have structured our response to correspond to the questions included in the *Paper*.

Q1. In general, WAUSAU recognizes the growing demand for an improved payment process that reaches beyond the historic Federal Reserve perspective of interbank safety and soundness and now envisions encompassing the initiators and recipients of payments. We believe the Federal Reserve can play an important role as a market catalyst for faster payment improvements.

Q2. One area that is not included in the envisioned state is detail regarding improved fraud protection for all of the participants. Consumers are rightfully concerned about identity theft and financial fraud through current digital payment methods, which encourages the continued use of checks. Banks can act both as a payment processor and a settlement bank for third party initiated transactions. As such, banks need to be adequately compensated for the service and yet not unduly penalized by regulation and fraud losses. Payment recipients need to be assured of finality of payment once the transaction is received which is today only provided by Fedwire transactions.

Q3. The *Paper* in some respects is a departure from the Federal Reserve Banks traditional role in the payments process. The historic role has been focused on safety and soundness covering areas such as finality/settlement risk and insuring operational integrity of the payments networks used by banks. The *Paper's* vision interjects the Federal Reserve Banks as both regulator and market catalyst. There is a wide dichotomy between the two. In the role of catalyst, speed will be an important element for achieving the stated vision. If the timeframe is too long, the risk of being obviated by other market solutions becomes real. The expected timeframe for full deployment needs to be more fully detailed. Secondly, in the role of regulator, the compliance burden to meet new mandates needs to be better balanced so that innovation is not stifled by process, cost and time. The banking industry is historically slow to bring new products to market, especially payments products due to the number of customers served and the associated operational and reputational risks associated with payment products issues. The regulatory scrutiny needs to allow banks to take some market risk which other non-bank payment participants enjoy.

Q4. WAUSAU believes contrary to our reservations above, the Federal Reserve Bank is in the best situation to be the market catalyst for the envisioned changes in payments. In the last five years, there has been a significant consolidation in the banking industry. This topic is widely discussed in the context of "too big to fail". In the cash management business, there has been a significant consolidation of the treasury services business into the largest banks. The result is almost reaching oligarchy proportions.

As an example, the NACHA membership vote to approve changes for a more real-time ACH network was recently defeated. This is in part due to the NACHA voting rules and the reported potential interest of a few major banks to develop a competing solution. The industry needs a catalyst that will insure that all participants can have a level playing field in the payments industry. The other unintended consequence of the concentration of the treasury services business is the reduction in the number of technology suppliers as the market for software services shrinks to the largest banks. If the Federal Reserve Bank is going to become a market catalyst it needs to insure that there is wide access for participation by all banks and an equally wide opportunity for suppliers to spur investment and innovation to complete the *Paper's* vision.

Q5. Consumers are demanding a friendlier and less "bank" centric payment process that fits easily into their mobile and internet experience. From a generational perspective, the millennia+ generations use cash and checks as a last resort. The envisioned outcome for consumer payments must strive to this objective.

Q6. There are a number of commercial and industry sponsored directory products or services that have gained only fledgling adoption when compared to the total number of payments processed. NACHA, AvantGard, Payment Pathways and others are early innovators in this space. Ubiquity will be enhanced through the use of these types of directory services. At the same time, there cannot be a plethora of competing directories which would create consumer confusion and possibly interject concern about usability and payment execution. The Federal Reserve can act as a catalyst for the use of existing commercially available intellectual property and the choice of a single industry solution or required interoperability between multiple providers.

Whether the envisioned state is a real-time or a near real-time solution, payment finality needs to be included in the feature set. This can be achieved by shortening the settlement windows for existing payment networks or introducing multiple settlement times during the day.

Banks commonly provide most consumer based internet payment products at free or near-free cost. Same day (i.e.: emergency) consumer payments are usually premium priced by most banks. The envisioned state offers consumers a tremendous reduction in these service fees. Given the risk consumer payments represent to the payment processor and the basic understanding consumers have of payments (i.e.: payment is only initiated against available funds and is final once sent), P2P and P2B are the most likely payments that should move to a real-time payment and finality. Conversely, corporate customers are charged for most treasury services products. Since finality of payment is a benefit to the recipient, the ability for a bank or a directory service provider to charge additionally for this benefit should be factored into the cost benefit analysis to gain bank endorsement and consumer and corporate participation.

The average middle market corporate lockbox volume for B2B payments is in the range of 300-500 payments per month. The number of ACH payments may not yet approach this level for most corporates. Although the velocity of available funds due to finality of payment is an attractive element when measured against reducing days sales outstanding (DSO), the practical benefit will be the reduction in the back office effort associated with return items and missing remittance invoice details. Finality, therefore, does not initially need to be instantaneous but can evolve to that state over a period of time.

The envisioned state is all encompassing and does not lend itself to a single big bang approach. Industry participants may not have the time and financial resources to absorb the full vision without an orderly deployment process. The initial steps should leverage existing payment networks, such as ACH and debit card networks, by correcting some of the issues associated with settlement timeliness and finality of payment.

Q8. Payment fraud costs banks and payment receivers billions of dollars annually. Access security will be an essential element for both consumer and corporate users to embrace the envisioned state. Authentication and access security must be assumed for full market adoption.

In the envisioned state, the role of the payment initiator will need to be redefined. Many third party payment processors initiate payments without real-time access to the available balances of the payer. The settlement occurs, in many cases, via an ACH payment that is not real-time. This leaves the bank with the credit risk of the return payment or assuming the credit risk of the third party processor. A shift to a real-time payment state will redefine the relationship between third party processors and banks. Will the direct access to the payment networks be an unfair advantage for banks, or will the envisioned state require a new definition of non-bank payment processors and their role in payment finality?

Q9. Real-time consumer payments initiated by a mobile device supported by an easily accessible directory will have a direct impact of reducing check volume. The decrease in check volume could be analogous to the drop experienced with the advent of internet home banking.

The 2013 AFP Electronic Payments survey indicates for the first time that 50% of B2B payments will be made via ACH. Corporate treasurers indicate that they are very likely to initiate a project to further accelerate the shift from checks to ACH. The envisioned state and associated directory will address one of the primary reasons for the slow adoption of ACH payments, the lack of the banking details to pay electronically.

Q10. The U.S. payment process is a very disjointed amalgam of players between banks, third party processors, consumers and corporates. As previously noted some of the largest players have achieved a market position where they control the ability for an orderly transition to a new payment vision. Many of the new payment innovations circumvent the safety and soundness of the current payment system by playing at the edges of the payment process without the risk controls required by banks (i.e.: BitCoin). If the Federal Reserve Banks did not take any action to modernize the current payments process, there is the potential for increased instability in U.S. payments. Additionally, failure to act will reduce the number of banks who can afford to participate in the emerging payment choices and potentially drive up costs to consumers. In addition, failure to act will reduce innovation and the number of technology providers capable and willing to make the investments for new products. A perfect example is the lack of technology solutions for ACH and CORE processing. The market is dominated by a few number of technology suppliers with little incentive to make innovative changes due to the slow pace of change. There are relatively few other vendor alternatives and few new entrants into this space due to the lack and speed of innovation.

Q11. The envisioned state will require an orderly transition as multiple systems within most banks will need to be changed to interoperate in a real-time payments world. The envisioned change might accelerate the adoption of payment hubs within banks to bring together the necessary data for operating in a real-time payments world.

An orderly transition from near-real time to real-time payments could occur over a five to seven year period. This time period accounts for the introduction of new regulations and technology changes. Inherent in the speed of change will be the clarity that participants will need to build the investment case for new technology and projects. In the new role of market catalyst, the Federal Reserve Banks will need to create the framework for innovation and the path for revenue realization for participants to justify the required investments.

Q12. As noted throughout our response, a directory will be an essential element in the success of the envisioned state. A major inhibitor for consumer adoption is the disclosure of a bank account in order to receive a payment. There are a few recent P2P payment programs introduced where shielding the bank account number is possible but they are limited to payers and receivers from the same bank. To achieve full consumer adoption and ubiquity a directory is essential. Unlike the corporate ACH payment process, where the receiver can request a debit block to their account, similar services are not readily offered or can be effectively managed in a consumer payment environment.

In both the research conducted by the Receivables Coalition and AFP, the lack of bank account information is one of the highest impediments for moving from check to ACH payments. In the AFP survey, 48%of organizations are likely to convert a majority of B2B payments made to major suppliers from checks to electronic payments in the next 3 years. In addition, 57% of organizations cite cost savings as a top benefit of transitioning to electronic payments. A directory service would reduce the effort to switch from checks to digital payments.

Q13. The migration from checks to digital payments is inevitable and will bring the U.S. on par with other developed economies. Without a timetable and a target the effort will languish. In conjunction with an orderly transition period, target percentages should be achievable within five to seven years. There is some precedent but not to the same magnitude for targets. Healthcare payments have historically been paid via check. The migration from check to digital payment was discussed for many years by market participants but with little progress. The Affordable Care Act has provided impetus for the change after an initial comment and transition period for technology changes. Given the magnitude of the change for the Federal Reserve Bank envisioned state, the transition period may be longer but with phasing from near real-time to eventually real-time payments meaningful progress can be made within reasonable periods.

Q14. The accelerated migration from checks to digital payments will not occur without some form of impetus. The primary reason checks volume continues to decline slowly is the relative ease of issuing a check. Checks require at a minimum the payee name and an address if it is to be mailed; all of which are readily available for most consumer and corporate payments and require no additional effort. Once viable alternatives exist, which address ease of use (i.e.: mobile devices supported by a directory), can market forces be applied to influence usage patterns. Increased check clearing fees, both physical and electronic, can be imposed to address the residual check volumes. However, unless viable alternatives are available, the potential exists for market participants to find alternative mechanisms to continue to support check usage.

Q15. The broader adoption of the ISO 20022 standard would not of itself improve cross-border payments. The investment to retool existing technology is too large and would be too costly to replace solely for a change in standards, especially since it currently works reliably well. The introduction of ISO 20022 should be done in concert with other infrastructure changes to support the new envisioned state.

Q20. The Federal Reserve Banks has made a valuable contribution for advancing the payments landscape through the publishing of the *Paper* and seeking industry comment. The *Paper* lays out a vision for which the industry can react. The current payments landscape and check volumes are a residual artifact left from the automation of U.S. payments which began in earnest in the 1980s. The period between then and now saw tremendous improvement primarily as automation facilitated a greater velocity of transactions. The technology underpinnings from the 1980s still support the current processes but are archaic (i.e.: some are still batch or window based) and do not serve the consumer or corporate users well. Current expectations and technology require a more instantaneous world that is provided by most internet experiences but not fully available in most banking transactions.

The private sector collaborated effectively through the last three decades. The banking landscape has fundamentally changed during this period and new non-bank payment alternatives have been developed in response to perceived service gaps and needs. However, the current concentration of services volumes into the largest banks potentially is a harbinger of less innovation and the lack of a level playing field for all participants. The added consequence is potentially higher costs for consumers and corporates for payment services.

The Federal Reserve Banks can play a vital role in changing the current payments landscape. Through both its regulatory authority and service offerings it can both push and facilitate the change in the payments landscape without being a detriment to private sector innovation and profits. Through regulatory promulgation of target decreases in check payments the private sector can develop plans for innovation. Likewise as a service provider, the Federal Reserve Banks can be the provider of last resort for core technology components, such as a directory, if the private sector cannot come to an agreement on a solution.
WAUSAU appreciates the opportunity to provide these comments and looks forward to further participation in the dialogue that will ensue as a new path for the payments landscape is defined.

Respectfully,

Lawrence F. Buettner
Senior Vice President – Innovation
WAUSAU Financial Systems