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President and CEO
Federal Reserve Bank of Cleveland
1455 East Sixth Street
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Attention: Federal Reserve Financial Services Policy Committee

Filed Electronically to: comment@fedpaymentsimprovement.org

Re: Payment System Improvement - Public Consultation Paper

Ladies and Gentlemen:

Google applauds the Federal Reserve Banks' effort to improve the speed and efficiency of the U.S. payments system, while maintaining protections for users and intermediaries, through its initiative for Payment System Improvement, discussed in the Public Consultation Paper, released on September 10, 2013 (the "Consultation Paper"). We agree with the Reserve Banks' stated vision that the needs of end users should drive the improvements to the U.S. payments system.

We also commend the Reserve Banks for initiating an inclusive process to solicit feedback on this initiative. Internet payments companies and intermediaries have unique expertise and should play a greater role in informing the next iteration of the U.S. payment system. Internet payments companies and intermediaries are relatively recent newcomers to the payments space, and they interact on multiple levels with payment networks, consumer and business users, and merchants through various interfaces. As such, these companies have a holistic view of the payments system and can lend valuable expertise and perspective to inform this process.

Our comments in this submission are based on the experience Google has gained in developing new and useful payment options for consumer and business users and merchants. Google Payment Corp., a subsidiary of Google Inc., provides a range of different payment services including card processing for online merchants, person-to-person and person-to-business payments, and mobile wallet payments for consumers and merchants. Google provides these payment services, depending on the service, through its authority as a licensed money transmitter and/or under payment processing agreements with a number of U.S. financial institutions. In addition to designing services for other users, Google itself is a significant user of all of the current systems – ACH payments, card payments, wire transfers and checks — as a payee, receiving payments from its customers, and as a payer, making payments

in connection with our AdSense and Google Play products. We encourage the Reserve Banks to continue to leverage the payments and technical expertise of companies such as Google as the Reserve Banks explore improvements to the U.S. payment system.

I. Google Supports a Ubiquitous, Open, and Flexible Payment System to Adapt to Future Users' Needs.

Google believes that emerging and existing entrants in the payments system have only scratched the surface in how to apply mobile devices to support a ubiquitous and secure commerce experience that brings enhanced value to all parties involved in the transaction. Consequently, we support three primary design objectives for evaluating any potential changes to the U.S. payment system: 1) ubiquity, 2) open access, and 3) flexibility.

Ubiquity. Google supports the Reserve Banks' Desired Outcome 2 stated in the Consultation Paper, for enabling a ubiquitous electronic retail payment solution that does not require the user to know the bank account number of the recipient, delivering funds to recipients in real-time or near real-time. Technology has enabled new, effective mechanisms for authenticating the sender, as well as for routing the payment to the recipient, which obviate the need for a solution requiring bank account information to be provided for electronic fund transfers/payments. Finding a new payment system settlement mechanism would provide greater convenience to retail customers and be a boon to new payments innovations.

Ubiquity will allow all payees and payers to access, or to be reached through, a new or enhanced ACH payment system. Ubiquity of an underlying payment system would encourage payment intermediaries to compete in the payments industry and develop new features and innovations benefitting consumers and businesses.

Open Access. The goal of a ubiquitous system goes hand-in-hand with ensuring that new entrants may directly participate in the system. In the current environment, we have found that innovation is often stifled by friction among the numerous parties today involved in processing and settling a payment transaction, over issues such as access rights to the device used to initiate the payment and the associated information capabilities available to each party. Today, U.S. payments must ride the "rails" of proprietary networks and standards, resulting in high fragmentation that serves to limit innovation. Payment networks, carriers, device original equipment manufacturers (OEMs), and banks have implemented proprietary processes, essentially acting as "gatekeepers" to the U.S. payments processing function. Developing an open payment system would enhance competition in the payments industry, which will in turn provide greater choice and benefits to consumer and business users.

Flexibility. We urge the Reserve Banks to consider how possible changes to the U.S. payment system can be made to provide greater flexibility to accommodate and take advantage of the innovation in personal computing and communication which we cannot yet predict. For example, just in the past few years, consumer access to smartphones, data networks and online services has surfaced new ways in which consumers and businesses can directly or indirectly initiate payments, and for

intermediaries to process payments with banks and other networks. Smartphones provide new ways of identifying the customer at the point of sale for the customer to authenticate and confirm that a payment is requested, and for a payment intermediary and bank to exchange transaction, authorization and settlement data. The Reserve Banks should consider how the payment system can maintain flexibility to accommodate swift and transparent transactions initiated through non-traditional means.

Furthermore, we support enhancements to authentication and other security-oriented processes and requirements that are data-driven. These approaches should be flexible and driven by risk analysis by the provider of the payment product or service. We would be glad to discuss with the Reserve Banks the challenges that Google has encountered with respect to this topic and our views on areas upon which a new or enhanced payment system may improve.

II. We Agree Improvements Are Needed as Payments Innovation is Rapidly Reaching a Plateau in the Current U.S. Payments System.

Both bank and non-bank payment intermediaries have created innovative products and services in the last few years. However, enhancements are needed to the U.S. payment system if payment providers are to continue innovate and meet expectations of how a 21st century payments system should work.

Google recognizes the risk factor associated with inadvertent failed payment (such as a non-sufficient funds (NSF) payment) or fraud by the payor. The card networks do provide certain features that address risk of non-payment/settlement of funds. However, requiring all new payment products to run through the card networks would not be efficient and would impose limits on innovation. The card systems have a proprietary set of rules and product requirements that enforce conformity at the expense of rapid innovation. In addition, the card systems do not offer a neutral settlement feature that would support non-card payment innovation.

By contrast, the ACH payment network is more flexible because it is a more neutral settlement network for debit and credit payments, which can be used by financial institutions as well as non-financial institution payment intermediaries. However, one of the primary limitations on innovation in the payments space is the fact that the current ACH system (i) does not support real-time or near real-time settlement of funds between parties; and (ii) does not provide the merchant payee/receiver of the funds with real or near-real time information regarding payment status (such as confirmation or guarantee of a pending payment).

As the Reserve Banks have noted, ACH is not a real-time payment mechanism; rather, it is a batch payment system that settles two days after initiation of the debit or credit payment. This timing for settlement does not meet end-users' expectations that payment should settle near the time of initiation, causing user confusion and potentially increased overdraft risk to the user. The lack of real time settlement or another informational exchange regarding the payment status in the ACH system also exposes the merchant and payment intermediaries to risk, which would be diminished by decreasing the time for settlement. Presently, there is no clear way for payment companies to innovate around these risks, without a fundamental change

to the way in which the ACH system operates. Finally, the current ACH system does not provide information, such as account status or authentication of users' status, that would allow payment intermediaries to better manage risk of an unauthorized mechanism.

We view ubiquity of a new or enhanced ACH payment system as a critical element of any improvements to the U.S. payment system. There are several benefits to building a new or enhanced payment system on an ACH framework. For example, the ACH payment system is the only electronic system today that offers ubiquity for sending and receiving payments – access to all deposit accounts in the United States. This makes it a desirable payment system for settling and processing payments in support of new payment models (wallets, phones, P2P, etc.). In addition, the ACH system is the only system that provides both credit and debit functionality (push and pull of payments) that are needed for new payment products.

Enhancements to the current ACH system should include features that provide near real time settlement of funds or that otherwise allow the receiver of the payment to determine that good funds will be made available to the receiver on the anticipated settlement date. An issue related to achieving such an enhanced system is greater assurance around the identification and authentication of persons sending payments. The benefits of faster payments would be undermined if there is not improvement and uniformity in the manner in which senders are authenticated. The ACH system itself does not provide data or other services that would support the payment originator's authentication of the sender.

The Federal Reserve should consider issues relating to authentication of the sending customer in the context of enhancements to the ACH system. Today, authentication of the sender (the customer whose account will be debited by the ACH entry) of an ACH payment is the responsibility of the payment originator under the payment system rules. Enhancements to the ACH system should allow payment originators to be confident that the identification of payment senders is accurate and secure, all while maintaining privacy. To the degree banks and other payment participants can agree to a common framework around how users are authenticated, all parties to the ACH system will benefit.

Another area worth investigating in an enhanced ACH system is increased interoperability by permitting the portability of consumer financial data. While some services exist today to permit users to aggregate their financial records, such as bank or credit transaction history, there could be easier and more predictable mechanisms for users to allow third party to access to this data.

If an enhanced ACH payment system, or a new similar electronic funds transfer system, provided payment intermediaries (such as the merchant's bank or processor) with real time settlement or information regarding payment status, this change to the payment system would spur additional innovation within the private sector to provide consumer and business users with even greater options for making payments via mobile devices, personal computers, and tablets, as well as devices yet to be invented.

In sum, we encourage the Reserve Banks to consider either a new payment

system or enhancements to existing infrastructure, e.g. Fedwire or ACH, that will allow payments companies to efficiently reach all payors/payees, regardless of with whom they hold a bank or other financial account, and/or the payments company with which the payor or payee chooses to contract for payment services.

III. We Support the Federal Reserve In Coordinating Payment System Stakeholders to Develop Consensus for Payment System Improvement.

The U.S. is in danger of falling behind other nations with advanced banking systems. The U.S. has been a leader in advancing new payment technologies that mitigate risks to the global payment system, while increasing efficiencies for consumers and businesses on a global basis. However, in recent years, bank-centric payments systems have advanced further in other areas of the world, such as the U.K. and Australia towards more real-time payments. If the U.S. does not move to a real-time/near real-time payments infrastructure, the U.S. system may become unsuitable for businesses to offer payment functionality to U.S. customers that would be available in other regions of the world. In addition, if the U.S. system fails to keep pace with innovation, it will hinder U.S. businesses' ability to conduct efficient international commerce as well as interoperate with international payment systems.

Given the complexity of the U.S. payments system and varied interests of networks, incumbents and new entrants, the Federal Reserve can play an important role in fostering inter-industry cooperation and planning. This role could be useful in overcoming many of the challenges in achieving a faster and more efficient payments system. The Federal Reserve should work to help solve coordination problems among the different stakeholders that would be necessary to migrate to a new payment model.

Promoting faster and more efficient payments is not always a simple coordination problem, however. Many incumbent interests have developed around inefficiencies in the current system, and these interests will be difficult to overcome. We firmly support the Federal Reserve working with all stakeholders in the payment system, including the current incumbents and new entrants, as part of its leadership in helping the payments industry reach a consensus for a new or enhanced payment system. The Federal Reserve must assume a leadership role in implementing changes to the payment system if consensus among all stakeholders cannot be reached.

The Fed should also continue to take a goal-oriented approach to improving the U.S. payment system. We also suggest, consistent with our experience developing user-facing products and services, that the Fed focus on the U.S. payments system from the perspective of end-users. This approach can help avoid devoting attention to small, incremental improvements that will result in a payments system that lags behind available innovations and the international community.

In this regard, it may be helpful in the next stage for the Reserve Banks to have a few proposed payment system models or enhancements (such as proposed changes to the current ACH system) to which the stakeholders could react and provide input, even if at a very preliminary stage. It may be helpful for payment

intermediaries and other stakeholders to understand the range of enhancements or new payment systems that are possible and/or the range of roles the Federal Reserve is willing to play for coordination of the payments industry.

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Google appreciates the opportunity to comment on the Reserve Banks' thoughtful questions on the future of the U.S. payments system raised in the Consultation Paper. If the Reserve Banks would find it useful, we would like to offer as a resource our considerable substantive payments as well as technical expertise in this area, as the Reserve Banks move forward with further discussion of this initiative and specific options with stakeholders in the payments industry.

Sincerely,

Adrienne Biddings
Public Policy & Government Relations Counsel