

43 consumer, small business, civil rights, community and legal service groups

September 9, 2021

By email to regs.comments@federalreserve.gov
Ann E. Misback, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Ave. NW
Washington, DC 20551

Re: Collection of Checks and Other Items by Federal Reserve Banks and Funds Transfers Through Fedwire, Docket No. R-1750; RIN 7100-AG16

The 43 undersigned consumer, small business, civil rights, community and legal service groups appreciate the opportunity to comment on the Federal Reserve Board's (FRB) proposed rules for implementing the FedNow payment system. We believe that an FRB real time payment system can provide competition and, if properly designed, can ensure that all consumers and businesses benefit from the widespread availability of person-to-person payments systems and faster financial transactions. At the same time, as many of our groups previously commented,¹ it is essential to ensure rigorous protections as the FRB develops the FedNow service in order to ensure that the system is safe to use.

The FRB should not launch the FedNow service until sufficient protections ensure that the service is safe and reliable for consumers and small business users. The proposed rules do not meet that standard. In particular, the system must protect consumers and small businesses from fraud and mistakes. Scams and errors can be devastating and have a particularly harsh and targeted impact on low-income families and communities of color. Below, we first discuss our overall concerns with the proposed FedNow system, and we then note some specific issues with the proposed rules.

The FedNow System Should Not Launch Until it is Safe to Use

The ability of anyone to receive money electronically quickly, with immediate funds availability and finality, is ideal for scammers. Existing faster payment services in the United States as well as abroad have already been exploited and see fraud at higher rates than traditional payment systems.² Scams often take the last dollar from those least able to afford it, and often target

¹ See Comments of 28 consumer, civil rights and community advocates re: Docket No. OP – 1670, Federal Reserve Actions to Support Interbank Settlement of Faster Payments (Nov. 7, 2019), <https://www.nclc.org/images/pdf/cons-protection/coalition-letter-interbank-settlements.pdf>.

² Analysts estimate that fraud rates on person-to-person platforms are three to four times higher than for traditional payment methods. See Nathaniel Popper, "When Your Last \$166 Vanishes: 'Fast Fraud' Surges on Payment Apps," New York Time (Oct. 11, 2020), <https://www.nytimes.com/2020/10/11/technology/fraud-payment-apps.html>. See generally Testimony of John Breyault, Vice President of Public Policy, Telecommunications, and Fraud,

immigrants³ and other communities of color.⁴ Yet the FRB's proposed rules replicate the problems in the existing private marketplace for existing faster payments services, where consumers and small businesses are not protected from fraud or errors, service providers do not take responsibility for building protections into the system, and institutions that create and hold accounts that enable scammers to receive fraudulent payments are not responsible for their customers' conduct.

The response of current faster payment systems to fraud has primarily been to say: "Only use this with people you know," or "We warned you to be careful." But disclosures and warnings to consumers are an old-fashioned and ineffective method of consumer protection, especially in combatting fraud, since fraudsters create and abuse trust. In this modern era of big data, artificial intelligence, and machine learning, payment systems that take responsibility for fraud will develop sophisticated, ever-improving methods of preventing, detecting and remedying it that are far more effective than warnings to consumers. For that to happen, however, the system needs to incorporate incentives for the financial services providers in the payments chain to design robust fraud and error prevention and remediation methodologies.

That is, rules must protect consumers and small businesses against fraud in the inducement and impose ultimate liability on the institution that received the fraudulent payment. (The consumer should be reimbursed in the first instance from their bank, which in turn can pass on the liability to the receiving institution.) Liability for the receiving institution is consistent with their obligations under existing know-your-customer and anti-money laundering obligations to ensure that accounts are not opened with fraudulent identities and that an institution's customers are not using an account for illegal purposes.

Rules that protect consumers and small businesses will give the providers of faster payment systems the incentive to develop and constantly improve measure to prevent fraud in the first place and to stop it as soon as possible. That is exactly what happens today with credit cards. The law does not tell institutions how to prevent fraud; it merely protects consumers and incents institutions to constantly improve their fraud prevention and monitoring tools.

National Consumers League, on "Protecting Consumers from Financial Fraud and Scams in the Pandemic Recovery Economy" Before the United States Senate Committee on Banking, Housing, and Urban Affairs Subcommittee on Financial Institutions and Consumer Protection (Aug. 3, 2021),

<https://www.banking.senate.gov/download/brevault-testimony-8-3-21>; Ed Mierzwinski et al., MASSPIRG Education Fund, "Virtual Wallets, Real Complaints" (June 2021), <https://uspirg.org/blogs/eds-blog/usp/virtual-wallet-payment-app-complaints-skyrocket>.

³ <https://www.consumer.gov/articles/1017-scams-against-immigrants>.

⁴ Anthony Hill, ABC Action News, "In-depth: Top scams that are targeted against the Black community; how to avoid falling victim; 41% of African Americans say they were targeted by a scam" (Aug. 12, 2021); <https://www.abcactionnews.com/news/in-depth/in-depth-top-scams-that-are-targeted-against-the-black-community-how-to-avoid-falling-victim>; Josh McCormack, Salud America, "Scammers Target Latinos, Blacks More Than Other Groups" (Aug. 31, 2021), <https://salud-america.org/scammers-target-latinos-blacks-more-than-other-groups/>; Matthew Petrie, AARP, Consumer Fraud in America: The Latino Experience (Aug. 2021), <https://www.aarp.org/research/topics/economics/info-2021/scam-experiences-hispanic-latino.html>.

Protecting consumers and small businesses will make the system safer by ensuring that reports of fraud are collected, aggregated, and acted on. If the response of a consumer's bank to a fraud report is simply "sorry, you have no protection," then those fraud reports will not be passed back to the Federal Reserve Banks or the receiving institution. The system will have no ability or incentive to aggregate fraud reports from various sources to detect patterns. Indeed, the FRB, as the centerpiece of this faster payment system, must itself develop tools to aggregate and share information.

The FedNow system also must be built to prevent and resolve costly errors. Private faster payment systems prioritize ease, speed and convenience over safety. That is not right. The FRB would never allow one of its employees to send government funds using simply a cell phone number as an identifier or without the ability to correct a mistaken decimal point. The FRB should not develop a system that it would not use itself. Here too, the FRB should aggregate and share information. For example, a central directory of end users could check the consistency of the information provided and enable payors to verify the recipient.⁵ A directory would help to ensure that consumers are sending funds to the correct person, and might also be used to ensure that an email, cell phone, or other identifier are not linked to the wrong account or an imposter account.

The FRB, as a public agency, has a public responsibility to ensure that its system is safe, especially for those users for whom fraud or errors can be devastating. The FRB can provide be a model for other systems developed by private companies that do not have the same public accountability.

While some will object that fraud and error prevention will slow down the system and undermine the goal of speed and finality, speed should not come at the expense of safety. The vast majority of payments can still be processed immediately with immediate funds availability. The system can be calibrated to speed through payments that have a low risk of fraud or errors and to set up speed bumps where the risk is higher. If overall rates of fraud and errors are low, the system can handle them, and if they are high, then clearly changes are necessary. But even a single mistaken or fraudulent payment can be devastating to an individual.

The Consumer Financial Protection Bureau (CFPB) should play an integral role in working with the FRB to ensure that the FedNow ecosystem is safe for participants. The two agencies should work closely together – and make recommendations to Congress if necessary -- to develop a comprehensive set of proposed regulations that both facilitates faster payments and protects consumers and small businesses. Among other issues, FedNow and all P2P systems should operate on a good funds model and not trigger overdraft fees.

⁵ However, as discussed in our earlier comments, *see id.*, privacy is essential. Institutions should only be able to access to the consumer data needed for each real time payment transaction and should not be able to use the directory for debt collection, marketing or other purposes.

Aspects of the Proposed Rules are Problematic

In addition to the overall lack of protections, there are some specific parts of the proposed rules that are concerning. These include:

- **Article 4A of the Uniform Commercial Code (UCC) should not apply to consumer payments, even in the absence of a clear conflict with the Electronic Fund Transfer Act (EFTA).** Article 4A was developed to cover large transactions between sophisticated parties with equal bargaining power. It was not created for small users operating under contracts of adhesion and does not create a consumer-friendly regime. Article 4A should not be simply transplanted onto transactions for which it was not designed. For similar reasons, Article 4A is also not an appropriate framework for many small business users, who lack any EFTA rights yet look more like consumers than the larger businesses envisioned for Article 4A.
- **Mismatched information indicating potentially incorrect recipient information should be addressed, not ignored.** The Federal Reserve Banks should look for and act on inconsistencies between the name on a payment order and a number that identifies the recipient, rather than being content to rest on a lack of duty to detect inconsistencies. Again, a directory would help here.
- **Receiving institutions should be permitted to delay acceptance of a payment order or immediate funds availability in cases of suspected fraud or mistake.** They should not be required to make funds immediately available in those circumstances. The grounds for closer scrutiny should be broader than when the recipient is not entitled or permitted to receive a payment due to, for example, U.S. sanctions. Problems are easier to fix if the funds are not gone.
- **International transfers should be forbidden or made consistent with the EFTA.** The EFTA gives senders of international remittances 30 minutes to cancel a transfer. International use may not presently be contemplated – and should not be permitted until the even greater fraud and error resolution risks of international transfers are addressed. The FRB should make clear that the rules only govern domestic use and that international use will not be permitted until further notice and comment on amendments to the rule in order to ensure compliance with the EFTA and any other laws, including 30 minutes delayed acceptance of the payment order.
- **Absent suspected fraud or mistake, consumers should have an enforceable right under the FedNow rules to immediate funds availability.** While the proposed rules require immediate funds availability, they explicitly deny consumers any rights to enforce that availability and relegate them to the much slower funds availability rule of the Expedited Funds Availability Act.

Thank you for considering our comments.

Yours very truly,

Alaska PIRG
American Sustainable Business Council
Americans for Financial Reform Education Fund
Arkansans Against Abusive Lending
Bank On Boston Coalition
Better Markets
Center for Economic Integrity
Center for LGBTQ Economic Advancement & Research (CLEAR)
Charlotte Center for Legal Advocacy
Chinese-American Planning Council (CPC)
Community Development Network of Maryland
Consumer Action
Consumer Credit Counseling Service of Maryland and Delaware, Inc.
Consumer Federation of America
Consumer Reports
Consumers for Auto Reliability and Safety
Delaware Community Reinvestment Action Council, Inc.
Georgia Watch
Legal Aid Justice Center
Main Street Alliance
Maryland Consumer Rights Coalition
National Association of Consumer Advocates
National Community Reinvestment Coalition
National Consumer Law Center (on behalf of its low-income clients)
National Consumers League
National Employment Law Project
New Economics for Women
New Jersey Citizen Action
Progressive Leadership Alliance of Nevada
Prosperity Works
Public Citizen
Public Good Law Center
Public Justice Center
Public Law Center
Revolving Door Project
SC Appleseed Legal Justice Center
Texas Appleseed
Tzedek DC

U.S. PIRG

Virginia Citizens Consumer Council

Virginia Poverty Law Center

Wildfire: Igniting Community Action to End Poverty in Arizona

Woodstock Institute