Real-time payments strategy

Key focus areas for financial institutions to address
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How are faster payments transforming the payments industry?

Countries around the world are moving to real-time payments (RTP) as businesses and consumers are looking for ways to send and receive money in a more effective, secure and faster way to accomplish near-real-time exchange of funds. In some of these countries, faster payment networks are enabling transactions to clear in minutes or even seconds, supported by common standards and economic incentives to participate.

In the US, RTP infrastructure is being implemented and driven by both public and private sector players (i.e., the Federal Reserve Bank (the Fed) and The Clearing House), with the goal of making faster payments available to any consumer and business in the next three to five years. In order to smoothly adjust to a new payment environment, these players are not only focusing on developing the necessary infrastructure, but also on establishing rules and frameworks to operationalize RTP in the US payments industry.¹,²
What is driving the faster payments environment?

New payment platforms and solutions, updated regulations addressing payment effectiveness and security, and higher expectations from merchants and consumers are driving the growth of faster payments. How is your organization adjusting to the new payments environment?

<table>
<thead>
<tr>
<th>Innovation</th>
<th>Technology innovation: New domestic person-to-person (P2P) payment providers are popping up on a regular basis, due to catalysts like social platforms, digital currencies and near-field-communication (NFC) based payments.</th>
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</thead>
<tbody>
<tr>
<td>Globalization</td>
<td>Worldwide trend: As the roster of countries adopting real-time payments grows, the pressure on other countries to lay the groundwork and support speedy payments is likely to increase.</td>
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<tr>
<td>Customers</td>
<td>Customer expectations and demographics: Due to rapidly changing customer demographics, many consumers now expect almost everything to be available in real time.</td>
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<td>Merchants</td>
<td>Merchants’ expectations: Many small businesses and large retailers alike are looking at real-time payment to enhance their cash flow management, reduce fraud activity and provide incremental value to their customers.</td>
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<tr>
<td>FinTech</td>
<td>New players and business models: In the last few years, numerous FinTech startups have launched with a focus on mobile payments. The focus tends to be on new real-time services.</td>
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<tr>
<td>Industry</td>
<td>Industry momentum: Industry participants across the globe are accelerating the path to real-time payments. In the US, the Fed, NACHA and The Clearing House are working collaboratively and independently to make faster payments a reality.</td>
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</tbody>
</table>
How organizations are responding to faster payments

Road map to your faster payments solution

Defining the RTP strategy and implementation approach opens a host of questions for financial institutions to consider in order to understand the right offerings and pricing for addressing customers’ (both consumer and commercial) needs, the technology and operations capabilities required to offer RTP solutions, the impact in core payment processing, supporting functions and the technology landscape, as well as the risks associated with such an endeavor.

As financial institutions answer these and other questions, they also need to evaluate the solution options, the right partners and the optimal vendor choices.

- What are the lessons learned from global initiatives?
- Which initiatives and standards are likely to succeed in the US?
- How will these efforts ultimately fit with the Fed’s faster payment framework?
- Which capabilities are required to launch a real-time payments solution (e.g., process automation, core payments processing, finance/accounting, fraud, risk/controls)?
- What are the gaps in the existing environment vs. leading practices?
- Which scalability, availability or performance issues might be created?
- What is required for tech ecosystem readiness to transition to RTP?
- What are the payment channel impacts and overlaps?
- How will messaging/tokenization standards (ISO 20022) affect technology infrastructure upstream and downstream?
- What are the process, policies, exception handling, risk and compliance impacts?
- What is required to allow 365/24/7 support?
- What are the key use cases for real-time payments in the wholesale space?
- Over time, how will other businesses benefit?
- Which solutions are available in the market and how effectively will they integrate with The Clearing House solution?
- How well are these solutions positioned to meet current and potential future business requirements?
- How can the plan be structured today to allow maneuverability tomorrow?
- Which operational changes will need to be made (call center staffing, posting policies, etc.)?
- How will treatment of nonstandard elements, unique risk/fraud and regulatory components be addressed?
- What are the required changes to the control environment?
- How do lines of defense change with new capabilities and solution configuration?
- Does the third-party vendor approach make sense?
Holistic faster payments approach

Adopting a holistic approach toward faster payments will help support strategic choices that are not tied to a single industry, while also helping organizations leverage the opportunity to advance broader payment initiatives. Building a faster payments strategy and implementation plan requires a steering program that understands the market dynamics; considers the organization’s vision; and can bring together the business, technology, operations, risk and compliance and support functions to execute on the overall vision and plan.

As the use of faster payments continues to become more widespread, banks have turned to partnerships to help them quickly adapt to the changing environment. A recent example involves many diverse parties, such as US banks, merchants, consumer groups and technology providers, collaborating within the Fed’s Faster Payments Task Force to outline the primary attributes and requirements of a ubiquitous and safe real-time payments environment. The following are ways financial institutions can utilize partnerships to their benefit:

- Satisfy customer needs that can’t be addressed with their current resources in order to provide an enhanced customer experience and reach a new or different audience
- Lessen the cost of developing, implementing and operating faster payments capabilities on their own
- Form strategic alliances (i.e., Visa and Stripe) to accelerate time to market and broaden the range of capabilities offered
- Compete with nonbanks in unfamiliar payment spaces such as P2P by aligning with bank-owned solutions such as Zelle
- Learn best practices from FinTechs, specifically in relation to customer experience and brand loyalty
1 Business strategy
Defining a customer-centric business strategy requires alignment with market needs.
• Assess current products and services and align RTP core competencies with customer needs
• Identify pilot use cases, new products and strategic opportunities
• Develop pricing and non-pricing (e.g., value) strategies
• Leverage opportunity to advance broad payment initiatives (e.g., payment hub)
• Capture opportunity to upgrade digital channels

2 Technology delivery
Scaling the technology architecture requires alignment with the enterprise payments strategy.
• Design solution so it leverages standards and is not tied to a single industry utility
• Model changes to intraday and batch capacity requirements
• Standardize shared RTP rails across the bank (e.g., commercial and consumer)
• Share payment platform for all RTP methods and types
• Assess impact to high availability/disaster recovery (HA/DR) strategies

3 Operations readiness
Shifting from a batch environment requires end-to-end processing alignment.
• Design cross-channel alignment for consistency across customer visibility and touch points
• Assess impact of 365/24/7 support
• Assess impact to supplemental functions, including marketing, liquidity, reconciliation accounting and finance
• Embed flexibility to make changes to business rules in real time
• Assess changes to good funds model

4 Regulatory risk and controls
Designing risk and control measures requires enhanced automation for real-time payments.
• Design operational and technical resiliency for availability
• Put security controls in place that scale to the threat
• Build or enhance real-time monitoring and alerting capabilities (e.g., liquidity)
• Consider regulatory inputs (e.g., AML and Office of Foreign Assets Control (OFAC))
How are US players evolving to a faster payments environment?

The market has seen many new faster payment initiatives being developed or discussed among established organizations such as the Fed, NACHA, The Clearing House, Visa, MasterCard and emerging market entrants such as Zelle, Dwolla and Ripple. While different parties are undertaking a faster payments initiative, they are not all addressing the same use cases or strategic areas. In this rapidly changing environment, US organizations are asking the following: which faster payments market solutions are most valuable, which ones will provide ubiquity and the best customer experience, and what is the best way to integrate them into the overall customer journey and technical and operational road map for change?
### Marketplace Highlights

| **Federal Reserve Board** | • Acts as an enabler and not a solution provider of faster payments  
• Beyond secure payments, the Fed has created the Faster Payments Task Force, which provided a framework and criteria for the US payments system; there is now a working committee developing governance, standards, etc., to provide the blueprint for the US³  |
| **NACHA** | • As of September 2017, same-day ACH debits and credits are available within the US⁴  
• In December 2017, NACHA released the ISO 20022 Validator Tool, which will enable businesses, software and solution providers, and financial institutions to instantly validate translated files, correct errors and download amended files, thus facilitating the integration of ISO 20022 payment messages with the ACH network⁵  |
| **The Clearing House** | • Is designing and building a real-time payments solution that will facilitate real-time messaging (both for money movement and information) with near-real-time settlement  
• Will support all major payment use cases: business to business (B2B), business to consumer (B2C), person to person (P2P) and consumer to business (C2B) for credit push payments  
• Will provide options to use The Clearing House services (e.g., directory, tokenization and fraud) or leverage other third-party solutions  |
| **Early Warning Services (EWS)** | • Provides near-real-time payment solutions to financial institutions as part of the Zelle (formerly clearXchange) network  
• Leverages its network directory of registered banks to enable money movement using customer email or mobile phone  
• Supports P2P and also select B2C (e.g., disbursements) and C2B (e.g., consumer to financial institution (FI) bill pay) for credit push payments  
• Both EWS and Zelle are currently utilizing debit cards and ACH⁶  |
| **Visa and MasterCard** | • Provide solutions that leverage debit networks (Visa Direct and MasterCard Send) to deliver funds in near-real time to debit cards of participating FIs  
• Visa Direct (solution that enables businesses to use cards consumers already have in their wallets to send and receive digital payments and facilitate real-time delivery of funds) push payments use existing debit or prepaid accounts to send money using original credit transactions (OCTs) directly to all eligible Visa accounts⁷  
• Support P2P and select B2C (e.g., disbursements) and C2B (e.g., credit card bill pay) for credit push and pull payments  
• Visa and MasterCard have different partnerships with providers like FIS, JHA, Hyperwallet, PayPal and EWS, helping them to broaden the solution reach⁸  |
| **FinTechs** | • Mobile payment offerings such as Square, Venmo (PayPal) and Apple Pay are actively redefining customer expectations across immediacy, security and ease of use when speaking to the concept of faster payments  
• Emerging entrants to the field such as Dwolla are further proliferating the development of same-day ACH payouts⁹  |
| **Early adopters** | • Owner banks of Zelle, a P2P service, enabled real-time payments within its network in 2015 and extended the service to the entire network in 2017¹⁰  
• The Clearing House announced that two early-adopter banks exchanged the first real-time payment (a B2B payment) using the newly developed RTP system in December 2017¹¹  |
Which impacts and concerns need to be on your radar?

Technology – how can you evolve your legacy technology to provide long-term agility?

As your organization seeks to move toward faster payments, the issue of aging legacy infrastructures will increasingly come into focus. The move to faster payments will take place in stages, with a variety of approach options coming not only from NACHA but also from players like The Clearing House, the Fed and even nonbank FinTech innovators. As organizations assess the near-term changes associated with same-day ACH, they must also consider future faster payment options. Legacy architecture with inflexible payment systems that each must link to a host of other core applications will be increasingly problematic to maintain in this dynamic, faster payment environment. As such, technology plans for the near-term, same-day ACH changes would be well advised to lay a foundation for longer-term payment architecture challenges. The goal is to make choices that address both today’s and tomorrow’s needs, and that are grounded in thorough cost and benefit analysis that balance the needs of customer experience, cost, agility and future growth.

Operations – which operational changes will need to be made?

Many of the payments systems operate through a batch process. Some of the key issues that banks face are that these type of near-real-time payments cannot be done through traditional batch-based systems, where end-to-end money movement can take days. This situation not only brings challenges to the system architecture, but also to associated processes. A near-real-time payments system may provide further incentive for banks to either consolidate their disparate payment systems into a payment hub or review the payment hub they already have in order to understand its ability to support 365/24/7 core payment processing and the extraction and use of valuable information that accompanies payments.

Thus, the faster payments environment will have a large impact on financial institutions’ operations. The following are some of the primary operational questions and issues financial institutions need to address:

• How will you staff your call centers for 365/24/7 support and prepare employees for the inevitability of new questions?
• Which processes will change and will you need to redesign batch processes?
• How will you ensure that information is available to clients in real time and on the channel on which they want to access it?
• Does your organization have the procedures and controls in place to support new product offerings (e.g., create invoice and request for payment)?
• On the clearing and settlement front, how will your business adjust to the impacts to float, settlement and posting processes, and intraday liquidity management?
• How will you deal with processes and organizations where manual activities are still standard operating procedure? Are those practices sustainable in a real-time environment?
• Do you have the security and authentication controls in place to reduce the significant risk associated with real-time money movement?

From fraud and risk management to impacts to third-party vendors, organizations will face a range of impacts to operations, all of which need to be understood and planned for.

Regulatory and compliance – how do you address regulatory and compliance risks?

Anyone who has experienced the last decade in the financial services industry can attest to the dramatic impact of regulatory and compliance issues. For every change, it continues to be important to look at regulatory implications, such as impact to anti-money laundering practices, customer communications, unfair acts and deceptive practices, and the myriad other regulations that can be affected when money and information move faster.

The challenges of compliance, especially regarding customer transparency, will become particularly challenging if customer expectations in relation to real-time money movement aren’t matched with real-time online account updates, changes to credit limits and other outcomes. Because so many payment systems operate in batch mode, reconciliation of payments that are initiated in near-real time may not match how the payments are received, potentially resulting in customer confusion or erroneous treatment (e.g., late payment fees). As payments speed up, organizations need to plan how they will address the fundamental regulatory and compliance risks.
Customer experience – how is communication with your client affected?

Shifts in the timing of payment clearing and settlement will have implications for customers (businesses and consumers). What are you going to say to your customers? The most straightforward communications will be structured around new capabilities that add customer value, thus enabling customers to move money more quickly or get paid faster. However, depending on how those changes are implemented, the timing of new, faster payment options may not line up with all customer-facing communications or reporting tools. Implications for everything from real-time alerts to batch-updated online banking files may be affected. With the new same-day ACH windows, certain business practices may need to change as it will no longer be possible to treat all ACH transactions the same way for communications, fee assessment and posting purposes.

For all types of changes, a thorough customer communications plan that covers both customers and employees who will engage with customers can help support good customer relations.
**Faster payments influence the entire payment value chain**

Faster payments’ impact on the entire payment value chain will require financial institutions to implement changes across their end-to-end payments life cycle. The expectation is that to enable and facilitate faster payments transactions, processes throughout the value chain will need to be scaled up and be further automated.

<table>
<thead>
<tr>
<th>Initiate</th>
<th>Validate payment</th>
<th>Process payment</th>
<th>Transmit payment</th>
<th>Clear and settle</th>
<th>Customer alerts</th>
</tr>
</thead>
<tbody>
<tr>
<td>➤ Provide customers with a simple and intuitive experience</td>
<td>➤ Optimize fraud management to fit into a shorter window</td>
<td>➤ Train operations team to process faster payments</td>
<td>➤ Determine impacts to payment priority and payment scheduling based on value date</td>
<td>➤ Transition to multiple clearing and settlement cycles per day</td>
<td>➤ Update customer disclosures and notifications for faster payment options and associated costs</td>
</tr>
<tr>
<td>➤ Accept same-day ACH and immediate payment instructions across multiple channels</td>
<td>➤ Adapt AML/OFAC processes to shortened time frame while ensuring regulatory compliance</td>
<td>➤ Scale exception handling (returns, disputes, etc.) processes</td>
<td>➤ Overlay faster payments processing on a batch processing infrastructure</td>
<td>➤ Post in near-real time to accounts and make funds available to customers</td>
<td>➤ Train customers on how to initiate faster payments</td>
</tr>
<tr>
<td>➤ Inform customers of associated cost when processing payments through faster channels</td>
<td>➤ Impacts to processing of special client instructions</td>
<td>➤ Modify close-of-business processes to handle faster payments</td>
<td>➤ Determine least cost routing mechanism based on payment type, value date and other criteria</td>
<td>➤ Improve liquidity management functions to better manage intraday liquidity</td>
<td>➤ Enable near-real-time transaction status updates and alerts for customers</td>
</tr>
<tr>
<td>➤ Convert batch-based payment instructions to real-time payment messages</td>
<td>➤ Authorize controls regarding clients initiating payments, such as multifactor authentication, biometrics and channel authentication</td>
<td>➤ Determine associated fees and charges (due from customer and due to counterparty)</td>
<td>➤ Support multiple payment instruction formats</td>
<td>➤ Enhance reconciliation processes to factor in multiple settlements within a business day</td>
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<tr>
<td>➤ Share data among different entities</td>
<td></td>
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<td>➤ Connect with various networks (leveraging appropriate rule set)</td>
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How can EY help you?

In this dynamic world, EY stands ready to help you navigate a course toward integrating and implementing faster payments capabilities into your service offerings. EY can help your organization assess leading ways to balance near-term risks and impacts with longer-term technology and operational considerations, so that your organization is well positioned to move forward in this rapidly changing faster payments environment.

Our team has decades of experience leading payments transformation at global financial institutions. The EY team includes former payments executives from top 10 US financial institutions with experience in real-time payments implementation, three of the largest card networks and many of the largest global software providers of payment services. EY’s Payments practice leadership has previously executed, and is currently working on, multiple faster payments initiatives for a range of clients across the globe. This combination of industry and consulting experience brings a practical and nuanced perspective to transformation activities, balancing the need for transformational change with practical organizational and budgetary realities.
Contact us

Contact any of the following Ernst & Young LLP professionals to find out more about EY’s offering in the payments space:

Sean Viergutz
Executive Director
sean.s.viergutz@ey.com

Jennifer Lucas
Executive Director
jennifer.m.lucas@ey.com

Wim Geurden
Executive Director
wim.geurden@ey.com

Matthias Loh
Principal
matthias.loh@ey.com
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