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Stimulus Payments and Some Troubling Views from the New York Times

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We're beginning to learn some banking lessons from the current crisis, and one of them is the virtues of electronic payments. Around the world, businesses, individuals and government are able to make secure real-time payments. Yet when it came time to distribute CARES Act funds, Treasury most frequently chose to make electronic payments using the Federal Reserve's automated clearing house (ACH) network and post-date payments, delaying delivery of funds by several days; worse yet, for tens of millions of Americans, Treasury issued a paper check that had to be mailed, cashed, cleared and settled.

It doesn't have to be this way. In November 2017, the banking industry established a Real Time Payments (RTP) system that, as the name suggests, allows for real-time payments among businesses and consumers. The system allows instantaneous and irrevocable payments, with messaging capacity and robust security. Unlike the ACH system, it operates 24/365.

The system exists in fact, not in theory. Currently 53% of deposit accounts in the U.S. are reachable; by the end of 2020, the number will be close to 80% as community banks and credit unions increasingly join the network through their processors (e.g., Jack Henry). Real-time payments are being made every minute of the day.

What does this mean for government programs? Nothing prevents the Department of the Treasury from using this system to make its disbursements -- whether that is tax refund, social security payment, or stimulus payment. Currently, though, the Bureau of the Fiscal Service makes 100% of its electronic payments through the ACH network, using the Federal Reserve as its exclusive agent (without having used a competitive bidding process).

These facts are difficult to ignore, but in a recent editorial, the *New York Times* managed the trick, stating falsely that, "Under the current system, even the fastest payments – direct deposits – move much more slowly in the US than in many developed nations."

Adding insult to injury, the *Times* blamed this imagined technology gap on the greed of the banking industry, "The banking industry doesn't mind the wait. Banks have developed a lucrative business in allowing customers – particularly those waiting for a check to clear – to withdraw more money than is legally available, and then charging a hefty fee for the overdraft." The fact that the nation's largest banks collectively have now spent billions of dollars to build and implement a real-time payment system that would effectively end this lucrative business did not merit a mention.

The *Times* also failed to note the major reason payments are delayed: fraud, and the resulting need to confirm that the payment is valid. Small businesses are not able to bear those costs, so banks are required to police the payment system. This includes not only rejecting clearly fraudulent payments, but also adjudicating disputes between merchants and dissatisfied customers. Real-time payments eliminate this problem because the payments are final and irrevocable.

Of course, it is quite possible that the editorial board ignored the RTP program simply because it is operated by large banks, and that arrangement barred editorial contemplation. RTP is operated by The Clearing House, which is owned by 24 of the nation's largest banks. That said, The Clearing House has been successfully operating since 1853 and processes on average 75 million payments each day, with an average daily value of $1.9 trillion, across its ACH, wire, check and RTP systems. The Clearing House operates as a utility, and it retains earnings only sufficient to fund research and development. It pays no income or dividends to its owner banks. Rather, it seeks to drive down the cost of clearing and settling payments through innovation and expertise. The Justice Department has already determined that its RTP system would not be anti-competitive.

The solution of the *Times* was to give every American a bank account at the Federal Reserve. This is a radical idea, with bad consequences too many to name. For a sample, though, consider a speech last year by Agustín Carstens, General Manager of the Bank for International Settlements (the parent organization of the Basel Committee on Banking Supervision):

> If bank deposits shift to the central bank, lending would need to shift as well. So, in addition to the deposit business, the central bank would be taking on the lending business. The central bank would need to meet business owners, interview them about why they need a loan, and decide on how much each should receive. We can ask ourselves whether this is the kind of financial system that we would like to have as the ultimate set-up…. For instance, the central bank could make do without a lending operation if it sends customer deposits to the commercial banks by opening central bank accounts at commercial banks. In effect, the central bank would be lending to the commercial banks so that they could lend on to the customers.
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> However, the bigger issue has to do with the division of labour between commercial banks and the central bank…. There are historical instances of one-tier systems where the central bank did everything. In the socialist economies before the fall of the Berlin Wall, the central bank was also the commercial bank. But I do not think we can hold up that system as something that will serve customers better.
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> Less dramatically, publicly owned banks in many developing economies are hardly paragons of efficient allocation of funds or of good service. Although established with the best intentions, in practice they often verge on being highly bureaucratic institutions susceptible to political influence, in particular to directed lending to politically favoured sectors of the economy.
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> We know from historical experience – especially in emerging market economies, but also advanced economies – that, during times of financial stress, money moves away from banks that are perceived as risky towards banks that are perceived as safer…. In such scenarios, imagine that depositors also have the choice of putting their money in a digital currency of the central bank or in the central bank deposit account directly. It is not far-fetched to imagine that a premium would open up, where one euro of deposits in the commercial bank buys less than one euro's worth of central bank digital currency.

These are the kind of concerns that should give anyone pause. Particularly if the United States already has a real-time payments system open and operating and eliminating the need for such a radical, dangerous step.

Appendix:

Aside from its glaring omissions and conceptual problems, the *Times* editorial makes numerous factual mistakes. For those who care about the details, here is sample:

NYTimes: “Thanks to outdated Fed regs that let banks delay deposits, the money that reached American’s on Wednesday was dispatched from Washington on Friday. That is barely faster than pony express”

***Facts**:*

- The implication that banks sat on the money is simply false; they received funds on Wednesday, and credited consumer accounts the same day.
- File distribution from the Treasury’s Bureau of the Fiscal Service (BFS) and the Federal Reserve started Friday April 10th and was completed Monday morning.
- It was a BFS decision or IRS limitation that meant ACH files were post-dated for Wednesday, not a bank rule or practice. In fact, the banks had unsuccessfully urged BFS/Fed to make the effective date Monday, which the banks could have accommodated.

***NYTimes**:* “If everyone has a Fed account, with none of the fees or minimum balance restrictions that discourage millions of Americans from opening accounts at commercial banks, then it would be easier to distribute stimulus payments – particularly to those who are both most in need and hardest to reach… People could withdraw the money at ATMs, make the payments with debit cards or move the money to a bank”

Facts: Just for starters:

- Many Americans don’t have bank accounts because they do not wish to provide documentation and allow transaction monitoring that banks are required to seek and conduct under anti-money laundering regulations. Would the Fed bank be exempt from these rules?
- Try a Google search for “free checking no minimum balance” and then reevaluate the premise of the *Times*.
- It is unclear what ATMs customers would be using in the world of the *Times*. Banks would no longer have an incentive to maintain them, and non-bank operators would wish to charge fees that the *Times* presumably would outlaw.
- For this Federal Reserve account, money would be deposited through benefit payments, and withdrawn (maybe) through ATMs; however, there is no mention of using the money to make payments. Presumably, this would mean transferring the money from the Federal Reserve to a bank, though one wonders why anyone would then establish a Fed account in the first place; alternatively, it would mean the Federal Reserve taking on all the operational and credit risk of running a deposit business, including the aforementioned fraud monitoring.

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