Payments Pros – The Payments Law Podcast: The Future of Payments: Exploring FedNow With the Payments Professor
Hosts: Keith Barnett and Carlin McCrory
Guest: Kevin Olsen

Keith Barnett:

Welcome to another episode of *Payments Pros*, a Troutman Pepper podcast focusing on the highly regulated and ever-evolving payment processing industry. This podcast features insights from members of our fintech and payments practice, as well as guest commentary from business leaders and regulatory experts in the payments industry. My name is Keith Barnett and I'm one of the hosts of the podcast.

Before we jump into today's episode, let me remind you to visit and subscribe to our blog, ConsumerFinancialServicesLawMonitor.com. And don't forget to check out our other podcasts on Troutman.com/Podcast. We have episodes that focus on trends that drive enforcement activity, digital assets, consumer financial services, and more. So make sure to subscribe to hear the latest episodes.

Today, Carlin and I are joined by Kevin Olsen from Pidgin to discuss faster payments and FedNow and what financial institutions and fintechs who connect with financial institutions need to implement faster payments. We will also explore faster payments use cases, what the onboarding process looks like and more.

Kevin is the Senior Vice President of Innovation and Strategy at Pidgin, which is a secure, real-time payments platform that enables financial institutions, business owners, and individuals to process transactions faster with lower fees. Engineered to deliver innovation both today and in the future, Pidgin allows financial institutions to send and receive faster payments almost instantly, but in a more secure way than virtual wallet alternatives.

Kevin, we are looking forward to the discussion today, and I'll just kick it over to you and Carlin.

Kevin Olsen:

All right.

Carlin McCrory:

Thanks so much, Kevin. We are absolutely thrilled to have you on. Kevin is very entertaining and great at explaining faster payments. So we'll just go ahead and dive in. Kevin, I think most of our audience is aware, but can you at least just describe what a faster payment is?

Kevin Olsen:

Okay. A faster payment is basically a payment that goes faster than our regular old payments. Now what's that really mean? Because when you say faster payment, usually the lawyers go, "What's faster mean?" Right. So we got to explain it for everybody.

And the reality is what we're looking at nowadays is there's faster ACH, which is same to ACH, it goes faster than the classic two day, but it's limited to business days. So when people say faster payments nowadays and ones that go through financial institutions, through the secure rails of financial institutions, you're typically talking about RTP, which are real-time payments that are offered from The Clearing House, or FedNow, which are instant payments offered by the Federal Reserve.

Now, in both of these payments, they're going to take place in under 20 seconds and they're available every day, all day, any day. They are restricted to just financial institutions within the US. They are credit push only systems, but when you talk faster payments, typically that's what most people are referencing, either the RTP payments or the FedNow instant payments.

Carlin McCrory:

We discussed FedNow on a prior episode of Payments Pros, but can you remind the audience what was the big deal with FedNow launching? And you discussed a little bit about RTP, but can you discuss the differences between the two?

Kevin Olsen:

Oh, absolutely, because a lot of people ask all the time what is different? I mean, RTP has been around since 2017. FedNow just got launched in July of 2023. And if you compare, if you look at the two systems, they seem to be almost identical. I mean, the way that they both processed instant or in real time, the way that they are credit push only systems, the way they work with the ISO formatting, the way that they have the request for payment, a lot, I mean a lot of similarities. But the big difference comes down to RTP is offered by The Clearing House. And The Clearing House is a private sector bankers' bank is the best way to look at it. They are the commercial bank or the bank that works for and processes payments on behalf of basically the top 25 banks in the US. Versus FedNow is an offering direct from the Federal Reserve banks.

FedNow is something that was built with the entire industry, the entire banking, even electronic payments industry have an input say so in how the development of FedNow took place. And it is again, an offering that comes directly from the Federal Reserve banks. So it's more considered public because of how it works and it's available to all financial institutions.

But I do have to add, The Clearing House does allow for anyone who wants to, US-based of course routing numbers are required, but anyone who wants to can sign up and use the RTP network as well.

Carlin McCrory:

Great. Thanks for that clarification. Can you discuss some of the use cases for FedNow?

Kevin Olsen:

Oh, this is going to be a long podcast if we're going to go into use cases, because there are so many. When you hear instant payments, a lot of people just right away go, "So we're going to have a P2P solution." Yeah, you actually do have a P2P solution, meaning person-to-person, consumer-to-consumer. Absolutely. That is a possibility and it is a good use case. But there's also what we call A2A or account-to-account, you might even hear refer to as Me2Me type transactions where let's say I want to be able to move money from my bank account to an investment account or maybe to another bank or credit union's account. And I can do that in seconds by using the FedNow or RTP services.

But then you start getting into businesses and especially the request for payment. And the request for payment is a system where a secure message through secure banking channels is sent. That message is sent, it's received, and it says, "Hey, would you like to pay for your bill? Would you like to be able to pay, say your electric bill? Would you like to be able to pay for maybe checkout at a retail location," something like that. And the consumer, the person receiving it could also be a business has the option to be able to say yes or no. And when they say yes, then it's a credit push that goes out.

It can totally, and I believe will totally revolutionize how BillPay takes place because it's going to be so much lower cost, yet have the security that's still in place and eliminate a lot of the headaches that go along with being able to reconcile the data back to the payment and match everything up that a lot of businesses have when it comes to working with those types of things.

Plus, it's easy for a consumer. It allows me to have more control over my accounts. It allows me to be able to forecast more what's going to happen with my own cashflow. And if I go into the business side of things, that's another use case and benefit that I have, is from a business point of view, I have the ability to be able to send the request for payments to collect on invoices. I have the ability to pay invoices using the FedNow or RTP systems. I have the ability to move or sweep money from one account to another.

I look at all the industries that are out there and there are just a plethora of use cases. A lot of them are going to be say emergency situations. Like for example, if we have a payroll that gets missed. If you've ever been in a situation where somebody forgot to get a payroll file processed, it's a nightmare, especially for the financial institution because they're trying to get all these wires out to help everybody make sure they get money that day. And it becomes very pricey. It's very cumbersome.

Whereas FedNow in that emergency situation, people would quit calling going, "Where's my money? How come I didn't get paid?" Because in seconds you'd be able to have that money to them. I hope the government announces exactly what they will do. We know the government is involved, US Treasury is involved with FedNow, but I would love to see them do things like do payouts for let's say Social Security, first time you sign up, get that out there right away.

I think a real major use case that I'd love to see from the government is my tax return. Get it to me in seconds any day of the year, any day of the week. I mean I would love that. And also FEMA. If we have a natural disaster, that is a situation where the US treasury take advantage. I haven't said they did or will, but I hope they will, where it would be a major use case that they could get money in the hands of Americans that have just been through some type of disaster.

Keith Barnett:

That's really interesting. If you don't mind me interjecting for a second, these all sound like great, wonderful things, but I assume that there are some risks attended with this. Do you mind discussing what the risks are, if any?

Kevin Olsen:

It's a payment. That right away means it's going to have risk. There's no payment channel that exists today that doesn't have some type of risk. And if we look, I got to say the F word, fraud. It's out there. It happens all the time with every payment channel we work with. And the reality is if you look at like checks, you have a physical document that is traveling around with all your information on it. Hackers love that. Fraudsters love that. Whereas if we go over to FedNow, it will have risk, there's no doubt about it, but it eliminates some of the risk we see in other payment channels.

One of the things is it is instant. It happens in 5 to 20 seconds. These payments are done. Funds availability is a requirement in about 99% of the situations that you're going to see. Meaning that if an account is compromised, if you sent money to the wrong person like a fraudster, that money could truly be gone in seconds and you may not be able to get it back.

So that is really the biggest concern right there because the money travels so fast. So people say these faster payments equals faster fraud. I don't agree with that, not at all. Because the reality is payment channels get blamed for the fraud that takes place when they're just a delivery mechanism. My opinion, fraud always happens before the payment and the payment channel gets blamed for it because a person gets tricked, a person sends money to somebody they shouldn't have or they didn't think about or the account gets taken over. The fraudsters just use whatever system works for them to be able to get the funds over. So there is that risk.

There's also, let's say more of a concern. With it being 24/7/365, being able to manage, maintain, monitor all of that activity, it's a concern because financial institutions might say, "We've never done that with an instant payment before." But I say to them, "Don't you have ATM machines? Haven't ATM machines been available 24/7/365 out in the general public? I mean they're out in the open for years, and you've been able to manage those. You've been able to work with card networks that are 24/7/365 as well." So a lot of the risks that we see that come with these instant payments, they're actually risks that we deal with in all payment channels.

Keith Barnett:

Well, that's interesting. So what does the adoption of the FedNow service actually look like?

Kevin Olsen:

I went and looked today just to know exactly how many institutions were going to be on board. And when we go back to July 20th, FedNow launched 35 institutions. Not a whole lot, especially when there's almost 10,000 in the US. And here we are today about six months later, and there are 177 that are currently showing on the Fed website as far as these are live participants. So that's actually showing some really good growth.

If I compare that to The Clearing House and RTP, they've been around since 2017 and they're just now approaching 400 members in years. So in months FedNow has gotten about half as many members as what we see with The Clearing House. In my opinion, to be able to see those numbers jump from 35 to 177 and just a handful of months shows that there's actually going to be some rapid adoption of the FedNow system.

Keith Barnett:

Do you know or can you speculate as to the reason why the adoption rate seems to be moving at a faster pace with FedNow than the others?

Kevin Olsen:

Oh, okay. A lot of that is just a matter of view and opinion. If you look at The Clearing House, they bank the largest financial institutions. So you'll see your Wells Fargos, Bank of Americas, Chase Manhattan, and that's a lot of activity. That's a lot of accounts. That's a lot of businesses. It's a network I believe you want to be involved in.

However, a lot of smaller institutions, they look to the Fed to be the one that provides them with the services, provides them with the options. They're doing almost all their processing directly through the Fed, and they don't have those relationships with The Clearing House. So they have that, I want to say trust in what they know and don't want to go outside of their proverbial sandbox that they've been working in and want to be able to stick with and have everything flow through a singular channel or really through the Fed, through multiple different payment channels because it's what they're most comfortable with and it's what they've done for years.

Carlin McCrory:

Kevin, how would a bank or credit union access FedNow?

Kevin Olsen:

A bank or credit union to be able to access FedNow is one of the biggest questions I get nowadays. For the past couple of years it's been, "What is FedNow? How's it work? What's it mean to me? How am I going to use it?" But now it's like I'm getting these emails all the time on how do I actually get on board? How do I actually get access to this?

And the answer to that is a bank or a credit union needs to determine if they're going to connect directly themselves. That's option number one, where they would establish a connection directly to the Federal Reserve banks themselves and the FedNow system, or a bank or credit union can work with a third-party service provider. That's something like Pidgin. That's what we do, is we provide the access, the tunnel, the highway, the super-fast highway for financial institutions, banks, and credit unions to have that pipeline into the FedNow service.

There is another option though, which we call working with a correspondent. Now, correspondents are going to be things like bankers' banks or corporate credit unions, financial institutions that help other financial institutions. It could even be a large regional as well. They do a couple things. They could either provide help and access for the connection to FedNow, or they can provide some additional services to help in the managing and the monitoring that's required for having a 24/7/365 service. But you're going to go one of those three routes.

The most popular really is the service provider because that's very similar to what we see in other payment channels as well. Not too many actually do direct connect anymore, at least not as much as they used to in the past.

Carlin McCrory:

We have a lot of fintech clients. How could a fintech access FedNow?

Kevin Olsen:

You can actually go similar routes. You'll want to first of all talk to the current financial institution you do your banking with. See if they have any options that are available for you to make use of their routing number because you do have to have use of a routing number if you want to be able to process transactions on behalf of somebody else.

If it's a fintech that just wants to be able to make payments or receive payments for themselves as a business, then again, still talk to your bank or your credit union. They'll be able to do that for you. But if you want to process on behalf of somebody else, you can actually call a service provider like Pidgin.

We do work with other fintechs to help them to be able to have an access channel for it. Or you talk to your banks that they are able to provide use of their routing number. It's not something that every bank's going to do though. I got to let you know that. But there are some that are willing to work with fintechs out there to be able to provide them with that opportunity.

Carlin McCrory:

And then on the same topic, what does this onboarding process look like both for a bank or credit union, but then also the onboarding process for a fintech?

Kevin Olsen:

It's really great to see that question coming up. Having worked in this industry for so long, for years it's been really cumbersome for people to get on with new products and services directly to the Fed. And that's because there had to be contracts and they required wet signatures. The ink had to dry before the contract could be approved and processed through multiple departments.

Well, the process now is actually rather quick. Within 30 to 90 days, depending on how you go about your connection, if it's an established provider or a new provider or if you're doing it yourself, you will be able to fill out the paperwork. They do now accept electronic signatures. Some examples of that paperwork are like in the appendixes of Operating Circular 8, which nobody really wants to read, but they're there if you want to go look them up. And you fill out your applications, you fill out the agreements, you get everything signed, and then you're going to go through a testing process.

Now, the Fed's done an incredible job. They've always made sure to have what they call representatives, service managers that help with the relationships, the relationship managers that are there to work with each individual institution to make sure that they have what they need from the Fed. They now also have what they call an onboarding manager that will work directly with the financial institution to get them on board.

Now, if I take it from the point of view of Pidgin, we also have our onboarding team. Our onboarding team works with the onboarding manager at the Fed to get one of our customers' banks or credit unions or even fintechs to be able to be on board. So you have a team of people that is there, really handholding you through the process. And like I said, it happens rather quickly. You get the paperwork signed. You start doing testing to get certified. You also have to provide options for how you're going to use the service, which there's really not that many, not in comparison to some other things that we do. And once that's all in place, like I said, 30 to about 90 days later, you could be processing live transactions.

Carlin McCrory:

Wow, that's really fast for the process from start to finish.

Kevin Olsen:

Faster onboarding for faster payments. Right?

Carlin McCrory:

Makes sense.

Keith Barnett:

One last question. So how can people get educated on FedNow and on other faster payment options?

Kevin Olsen:

I go by the name of Payments Professor. If you go out to the YouTube, I've got a Payments Professor channel out there, put videos out all the time. I've even done Instagram where I will answer anybody's question, even some really crazy absurd ones, let's just say in 60 seconds or less. And then there's the Payments Professor website where there are in-depth courses that are out there to be able to help you.

Now, some people though don't like my style and are like, "You're a little bit too weird for me." And that's where I would say you could go to the payment associations, organizations like EPCOR or Macha or ePayResources. They are out there offering solutions for electronic payments education, especially FedNow and RTP to their members. Or you can go to the FedNow Explorer website. The FedNow Explorer website has some great content. A lot of my content I can tell you comes from what is made available publicly to everybody on the FedNow Explorer website when it comes to educating people on FedNow.

Keith Barnett:

And the only thing I didn't catch was what's your Instagram handle again?

Kevin Olsen:

Payments Professor.

Keith Barnett:

Oh, that's it. Okay. So no underscore, nothing like that?

Kevin Olsen:

I've worked real hard. I'm making the bow tie known.

Keith Barnett:

Fair enough. Yes. And we all know the bow tie. We have been to the excellent webinars and in-person seminars that you've done, and we feel extremely fortunate to have you here today.

Kevin Olsen:

Thank you.

Keith Barnett:

This has been a great presentation. I've learned a lot from you, not only from this presentation, but from other presentations you have done. We've relied upon you quite a bit and we really, really do enjoy listening to you and learning from you.

Kevin Olsen:

I tell everybody I do this because of those comments right there. Regulations, rules behind electronic payments, it can be complicated, especially when it's something brand new we've never dealt with. So my goal is to make it fun, to make it entertaining, to make it engaging so that people can learn this, so that they can provide safety and security to their account holders, to their institution, and most of all, advance their knowledge and their careers.

Keith Barnett:

That's great. We appreciate it. Thank you for joining us today, and thanks to our audience for listening to today's episode. And don't forget to visit our blog, ConsumerFinancialServicesLawMonitor.com and subscribe so you can get the latest updates. And please be sure to subscribe to this podcast via Apple Podcast, Google Play, Stitcher, or whatever platform you use, and we look forward to the next time.