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FedNow: The Future of Real-Time Payments

Why Credit Unions Can't be Fast Followers

A White Paper

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Executive Summary

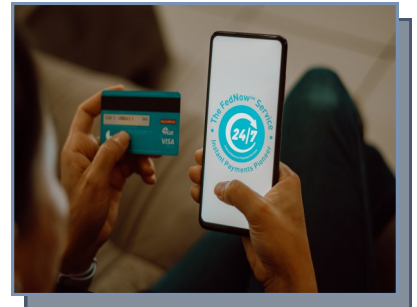
Designed to maintain uninterrupted 24/7/365 processing with security features to support payment integrity and data security, The Federal Reserve's FedNow Service, launched in 2023, seeks to capitalize on the ever-growing and popular closed loop, peer-to-peer payments (P2P) market made popular by the likes of Zelle.

No stranger to the payments industry, The Federal Reserve settles, on average, \$5 trillion in transactions every day through various platforms, serves over 9,200 financial institutions (FIs), and employs nearly 2,000 employees who work in one of the 12 Federal Reserve Bank locations. Successfully launching and branding its real-time payments service to the general banking public, however, will take time as FedNow faces competition.

The Financial Brand recently reported that there are approximately 118 million customers enrolled with Zelle, which was launched in 2017 and is operated by Early Warning Services, a joint venture of Bank of America, Capital One, JPMorgan Chase, PNC, Truist, U.S. Bancorp and Wells Fargo. In 2023, Bank of America reported that it processed more outbound Zelle payments than outbound checks. Today, Zelle's network includes more than 2,000 participating banks and credit unions. Al Ko, chief executive officer of Early Warning Services, recently noted that 80 percent of Americans who have checking accounts can access Zelle through their FI's banking app.

According to ACI Worldwide's March 2023 report, more than 70 countries support real-time payments, representing \$195 billion in transactions (in 2022). India, which launched its Unified Payments Interface real-time payments platform in 2016, is the largest market by volume, with 89.5 billion transactions, followed by Brazil, China and Thailand. "The U.K., Canada, Germany, the U.S., Italy and France — all top 10 global economies by GDP — placed 9th, 19th, 29th, 33rd, 36th and 41st, respectively," the report offered.

Noting that the U.S. is a market where "regulators strongly favor non-intervention," the report stated that FedNow is "a highly significant milestone for real-time." Realizing the severity of the aforementioned competition and the manner in which banking preferences are changing, The Fed is also determined to compete against another U.S.-based RTP player, The Clearing House's real-time payment (RTP) service. Launched in 2017, the service is also owned by some of the world's largest FIs and each day clears and settles more than \$2 trillion through wire, ACH, check image and RTP.



While Zelle and Venmo users are largely unaware of the FedNow Service, The Fed is optimistic about future adoption rates. In January 2024, six months after its launch, the FedNow counted 500-plus FIs actively participating as receivers or senders on the network, which beat out The Clearing House that purported approximately 400 bank and credit union RTP clients.

"The Federal Reserve settles \$5 trillion in transactions every day through various platforms and serves over 9,200 financial institutions."

FIs using FedNow include a range of banks and credit unions headquartered in 45 states. The size of these institutions, which include JPMorgan, US Bank, Wells Fargo, Veridian Credit Union, Star One Credit Union and HawaiiUSA Federal Credit Union, varies from \$500 million to \$3 trillion in assets.

While FedNow currently doesn't have its own app, in the coming years customers of banks and credit union members whose FI signed up for the FedNow Service can use their FI's app, website, and other interfaces to send instant payments directly from their bank accounts quickly and securely.

The purpose of this white paper is to educate and inform credit union executives on the benefits and challenges of adopting the FedNow Service, while underscoring the perils of deploying FedNow without proper due diligence, oversight and strategic planning. To this end, the white paper will lean on industry research as well as share experiences from credit unions and credit union service organizations (CUSOs) that have successfully rolled out the FedNow Service to respective membership.

Call to Action: Reasons to Adopt FedNow Service in 2024

To appreciate the significance of the FedNow offering, and before noting reasons to adopt the service, it's helpful to revisit a historic milestone event. In 1972, after a few years of working with California bankers who were concerned about the viability of paper checks, The Federal Reserve Bank of San Francisco began operating the first automated clearing house (ACH) payments. Soon after, other regions began offering ACH services to the point that in 1978 the Federal Reserve was able to link these ACH regions together, resulting in an industry first: the ability to communicate and process inter-regional banking transactions.

While an impressive track record, it's fair to say that The Fed took a slow, methodical approach to launching a RTP network, mainly due to the lessons learned rolling out ACH. During a February 2024 Fintech One-to-One podcast, Mark Gould, chief payments executive for Federal Reserve Financial Services, told host Peter Renton the reason for this conservative approach was The Fed's focus on ensuring a streamlined digital onboarding experience for all FIs.



"There are 9,200 financial institutions in the United States. If we want to get every single one of them connected, we really don't want a line out the door and around the corner. We really want to avoid that," Gould said. "Our record from a bank signing a contract to being live on the platform is eight days. That's a result of investing in this digitized onboarding experience."



The FedNow Service is available to depository FIs that are eligible to hold accounts at the Reserve Banks under applicable federal statutes and Federal Reserve rules, policies, and procedures. “Participants can designate a service provider or agent to submit or receive payment instructions on their behalf. Participants will also be able to settle payments in the account of a correspondent if they choose to do so,” The Fed stated. “Merchants, consumers, or non-bank payment service providers can access the service through depository institutions as they do today with other payment systems.”

Now that Federal Reserve has its proverbial FedNow ducks in a row, the question for credit unions is: Do we need the FedNow Service now or can we take a “wait and see” approach and allow our members to use alternative services?

“We asked ourselves, what’s the cost of not doing it,” said Jennifer Brantner, vice president, payments at the \$4.8 billion, Eau Claire, Wisc.–based Royal Credit Union. The credit union, which supports more than 300,000 members at 26 branch locations, went live with the FedNow Service in September 2023.

“We weren’t the first, but we were an early adopter,” she added of the process that took less than two months to roll out. “We thought about whether to just do send or send and receive, so there are many methodical ways you can dissect FedNow that’s palatable and lets you do it at your own pace, but it’s



important to also ask: Why you are adopting it and how it will best serve your members?”

Like Royal Credit Union, many C-level credit executives are asking similar questions about FedNow because in order to attract and maintain membership, best-in-class RTP rails have to be offered, otherwise members will continue to use competing services, such as Zelle and Venmo. So among leading reasons to adopt FedNow is eliminating challenger banking options, which, in turn, allows credit unions to have more equity and access to membership. This approach also provides credit unions with a holistic view of the member relationship, including onboarding and validating new members as well as meeting the expectations of existing ones.

The Federal Reserve states that the term “faster payments” broadly describes what the FedNow Service will deliver (i.e., payments that can be sent and received within seconds at any time of the day, on any day of the year, such that the receiver can use the funds almost instantly). The Fed also notes that the term “instant payment” refers to a payment in which an end user receives funds in “near real-time” and at any time, with the immediate interbank settlement of the payment also having occurred. Zelle, for example, can be paid instantly in some cases, or depending on the thresholds for the institution, some transactions can take up to three days to pay, making Zelle a faster payment solution, not an instant one.

Aside from offering a viable alternative to existing payment services, FedNow also provides other banking options that Zelle and Venmo do not. These include the following transactions: payroll services; business-to-business (B2B), allowing consumers to pay rent or other services; person-to-government (P2G), allowing consumers to pay taxes; and business-to-government (B2G), allowing payments from business to the IRS and other entities.

“I’ll go out on a limb and say, in five years, every financial institution will be equipped to at least receive instant payments, and many should be equipped to send them as well,” Gould noted. “Businesses across the country will have started to think about how they can use instant payments to provide better service, whether it’s instant settlement payments for insurance payouts or things like that, or more quickly getting money into the hands of consumers when they’re owed [money].”

Hurdles and Challenges: What Credit Unions *Really* Need To Know about FedNow

While the FedNow Service enables individuals and businesses to send and receive payments within seconds at any time of the day, on any day of the year, there are issues that adopters should be aware of before embarking on the process.

From a use case stance, consumers and businesses can only send and receive payments through the FedNow Service with other consumers and businesses whose FIs also have the service, which may require inquiries that could bother users. This was among issues Royal Credit Union considered, noted Brantner. “FedNow also comes with a cost, as everything does,” she noted.

With regard to costs outside what the credit union outlays to provide the service, the Federal Reserve requires a \$25 monthly FedNow Service participation fee for each routing transit number (RTN) that enrolls to receive credit transfers in the service. Additionally, a fee of \$0.045 per transaction to be paid by its sender, including returns. A fee of \$0.01 for a request for payment (RFP) message is to be paid by the requestor, including both requests for a new payment or funds to be returned. A business, the Fed further noted, can send an RFP through the FedNow Service to a participating FI to request payment of a bill, invoice, or other amount owed by the receiving financial institution’s customer.

FedNow will be offered via third parties participating in the payment space, which means that FIs need to either revise their current agreement (if the core is certified with FedNow) or work with a third party that is also certified with their core/and can process FedNow. To this end, Brantner said the biggest decision Royal Credit Union made was selecting a knowledgeable vendor that is well-versed in this niche space.

“You don’t just slap a link on your online banking channel for your member’s to use FedNow. You need to partner with someone who takes a holistic approach,” she continued. “I would not advise a credit union to partner with a company that will only provide the FedNow services as you need a company that can help you leverage all of your existing services along with FedNow.”

After vetting a host of vendors, Royal Credit Union chose Alacriti, a Piscataway, N.J.–based fintech company specializing in payments and money movement. “They have number of different solutions,” she shared. “Most of the different partners we considered and looked at had FedNow tied in with their payment hub, with some offering different wire solutions and end-to-end capabilities that make it easier on the backend to administer all of these different payment tools.”



In many cases, this vendor selection process is greatly aided by partnering with a proven technology consulting firm that can not only assist credit unions in the vetting process, but also oversee the adoption, testing and implementation phases of rolling out the FedNow Service.

Among leaders in the RTP space assisting FIs with integrating FedNow is Aptys Solutions. The Plano, Texas–based credit union and Bank service organization (CUSO/BSO) provides electronic payment processing software for FIs and was a participant in the preliminary stages of the FedNow pilot program. Today, the company services over 95 FIs with FedNow Services including “Send,” “Receive,” and/or “Settlement” capabilities, which Aptys Solutions President and CEO Naseer Nasim said underscores the company’s dedication to delivering end-to-end digital payments with seamless interoperability across payment rails including RTP/TCH, ACH, wires, check, and mobile payments.

“Instant payments including FedNow and RTP are reshaping our industry. These latest payment rails require real-time interoperability of banking solutions to support 24/7/365 banking. Integration between payments, core account processing, digital banking, fraud and risk management are key to making real-time banking a reality. In another word, open banking,” said Nasim.

“No matter the size of the institution, what FedNow requires is that core operating systems are open and, at minimum, have application interface programming (API),” he continued. “The broad application of real-time payment for consumers, businesses, and government in 2024 and beyond is a game changer. Consumers, businesses, and financial institutions are demanding 24/7/365 service to move money swiftly and to have immediate access to their funds regardless of banks, applications, and vendors involved. The uniqueness of FedNow puts us in a completely new and different world than we have been putting up with for decades.”

While the costs involved to roll out FedNow is a reasonable concern for some credit unions, Eric Dotson, Aptys Solutions executive vice president of sales, noted that along with providing members with next generation instant payment technologies, credit unions that adopt FedNow will realize other benefits.

“You no longer have staff sitting there managing ACH or wire transfers and that is something most people don’t realize—that the credit union will have less work and cost involved in managing and maintaining these services,” Dotson continued. “And FedNow allows you to bring business customers back to the community credit union because now they can get the services they couldn’t get before.”

By name recognition alone, FedNow may inspire more confidence in membership than fintech challengers, but even still, another leading concern for many credit union executives considering adoption is security and fraud. Royal Credit Union, for example, weighed this issue when determining whether to opt for both the sending and receiving of funds through FedNow. Currently, the credit union offers the latter, but that could change in time.



Aptys Solutions CEO
Naseer Nasim

“We looked at the fraud and security in general and there is certainly risk on the receive side, but there is more risk on the send side. It’s certainly on my mind because fraud is part of my organization here—I can’t put in payment rail without accounting for fraud,” Brantner said. “So we are very much watching that as much as we can in real-time and making adjustments to strategies as we go.”

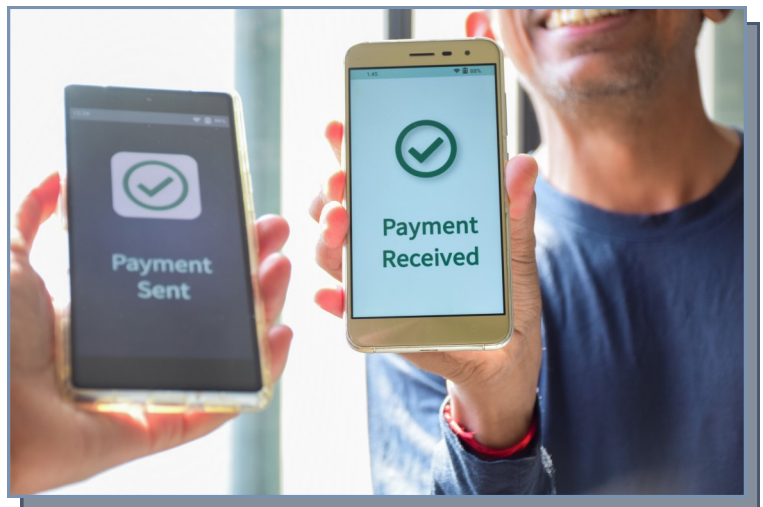
Nasim further explained that the reason most FIs currently prefer the receive and settlement side of the equation is because consumers are concerned with settling the instant payment transaction, but that too will change in time.

“An FI can have multiple Send points but only one Receive and Settlement. While FedNow Send can be integrated or embedded as part of an FI’s existing digital banking, and cash management solution, FedNow Receive, on the other hand, requires single integration with the core account processing system, a single point of receive from consumer, business and government through different send channels and your FIs must clear it and settle it in its own Federal Reserve Bank master account or designate a correspondent, such as corporate credit union or bankers’ bank,” Nasim said.

“FedNow Request For Payment (RFP) are additional capabilities to expand FedNow capabilities for consumers and businesses to request instant payment,” he continued. “So depending on an organization’s strategy, analysis, as well as where they see clients’ demand, most FIs while enrolling in all FedNow Services, they work with their providers to activate FedNow Services one step at a time as they get deeper and deeper into instant payments.”

To avoid the possibility of money laundering under FedNow, the FI’s compliance department, audit, and BSA/AML must limit amounts sent and received. Since the transaction is instant, and money can be moved fast, it is imperative for the FIs to set limits and have processes to catch any repeated or aggregate monies being sent or received. The credit union’s fraud department, therefore, will need to be able to increase the limits or reduce them to better reflect the needs of its membership. According to *NerdWallet*, The Fed currently caps transfer amounts at \$500,000, and sets the default transfer limit at \$100,000.

“We put in a core set of tools at launch that enable banks to do things like set transaction limits that are lower than the network level ones. Another really important thing that we did at the outset was require anybody on the FedNow platform to report any fraudulent transaction that they receive. That’ll enable us to start building a database of any fraudulent transaction and the characteristics of it,” Gould continued. “So over time, we’ll have a sense and be able to deter fraud in a way that we couldn’t at the outset. We have plans to introduce additional controls, risk mitigation tools to give banks tools to augment their own fraud control mechanisms.”



FedNow Future: Why Credit Unions Can't be Fast Followers

While historically the credit union industry has been apprehensive about adopting new technologies too quickly, industry experts say credit unions shouldn't take a wait-and-see approach with FedNow. If they do, they could risk losing current and future generations of members.

"There is no such thing as fast followers in real-time payments," said Nasim. "You are either a follower or a leader. If the industry waits and doesn't have the product ready—the send, receive and request for payment—this window of opportunity will only open for a limited time."

Among benefits of adopting FedNow is that the service allows members to conduct all of their real-time payments transactions with their credit union. This provides the credit union with a better understanding of their members, while building unique, personalized relationships. Whether to adopt FedNow immediately or later in 2024 and beyond, however, depends on each FI, explained Brantner.

**"There is no such thing as fast followers in real-time payments.
You are either a follower or a leader."**

"It truly comes down to who needs faster payments. And when dealing with FedNow specifically, you need to determine the use case. There are many other models out there, including P2P models like Venmo and Zelle. For most consumers that model works just fine," said Brantner. "So you have to determine if there is more of an advantage to moving your members to that type of product. But also think about other uses like your business members experiencing payroll issues. So, it's a matter of determining what will be best for all you members moving forward."

For comparison, Brantner provided Royal Credit Union general RTP "receive" user statistics as well as those from FedNow (it's important to reiterate that FedNow was rolled out in late 2023). For the fourth quarter of 2023, RTP transactions were 11,815, which totaled \$3.4 million. During the same time period, FedNow had 62 transactions, totaling \$5,475. In the first quarter of 2024, RTP transactions were 4,248, which totaled \$1.58 million, and during the same time period, FedNow had 47 transaction, totaling \$3,935.

As more credit unions sign up for FedNow, user statistics, like the figures provided by Royal Credit Union, will increase significantly, Dotson noted. Adopting FedNow, he added, may also allow credit unions to reduce certain IT costs so they can refocus strategies on the member experience. For those credit unions on the FedNow fence, Dotson offered a scenario.

"The way Venmo works is that they take the money out of the credit union and place in its virtual account and they hold those funds. Look to see how many of your transactions are Venmo — all of that is money leaving your financial institution," he continued.



**Aptys Solutions EVP
of Sales Eric Dotson**

“You want to bring that money back into the credit union because with FedNow you have a way of paying in real-time. These are ways a financial institution can look at funding this effort and help them to grow the services they are providing to their members.”

In time, it's estimated that FedNow will impact most all traditional banking procedures. For example, since the exchange of information takes seconds to complete, the usual one to two days for a standard ACH transaction to clear will begin to eliminate check volume. With fewer checks needed to be processed, the need for full-time equivalent employees (FTEs) to post exceptions from check deposits will be reduced. Income from checks may also be impacted as less will be purchased. The X9 file (i.e., mobile deposits) will start to lessen and may result in FIs paying less. And as more traffic is routed to FedNow, RDC/ITC (i.e., the branch) will be impacted, including the number of FTEs needed at the branch and back-office.



Under FedNow, merchant processing may also be reduced, thus impacting interchange fees. If the consumer pays for the services via FedNow, the need for a POS device may also be reduced over time. Square, for instance, is currently used by many merchants at kiosks or at flea markets at a cost to the merchant, and paying the merchant usually takes at least two to three days. Conversely, FedNow is instant and doesn't charge a merchant fee. Zelle does offer this capability in certain P2P situations, but it is not available to merchants. FIs should also anticipate that FedNow will impact wire transfers as this could be the new manner in which consumers send money internationally.

“Some of the fintech companies are now originating the largest number of instant payment transactions. We can't afford to take the back seat when the industry made this payments rail available to us and then let fintechs can take advantage of it and beat us,” warned Nasim. “We are doing everything we can to provide that competitive advantage and leading position. This rail — FedNow — is the first thing to level the playing field since ACH.”

Parting Thoughts: The FedNow/Credit Union Takeway

Whether a credit union undertakes the FedNow adoption process under its own steam, works with a trusted technology consulting firm or partners with companies such as Alacriti or Aptys Solutions, the writing is on the wall: Credit unions can better optimize the member journey and experience by deploying the FedNow Service.

“I’m really counting on fear of missing out (FOMO) within the financial community. If you’re a bank that’s not sure about this, but the bank across the street is offering it, that’s maybe a dangerous position to be in, just from a competitive standpoint,” said Gould. “So as the number of institutions steadily climbs, I’m really counting on FOMO. I think the other thing is that we just need to talk about success stories and talk in story terms about what instant payments are, how they work, and how they’re better.”

As more and more credit unions think about adding the FedNow Service, they can tap into the “people helping people” credit union ethos, which provides critical insights, furthering the cooperative nature of the industry, explained Brantner.

“Over the last six months, I’ve talked to a number of credit union folks because we have adopted FedNow and others are still making the decision. Some people want to see it succeed for a while and then adopt, and others have a measured approach and are making thoughtful decisions with regard to implementation,” said Brantner. “There is a lot of competing view points and none of them are wrong because they are coming from different institutions that all value something different in respect to offering this new payment rail.”

In the final analysis, the FedNow Service has created a foundation for depository institutions nationwide and the broader payment industry. When expertly adopted and implemented, this groundbreaking service will facilitate an efficient real-time, payment system that for the first time will securely connect all payment rails. To this end, the Federal Reserve has once again made history, providing a platform for FIs to enhance the customer and member banking experience today and into the future.



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