



## Pondering Payments: Challenges of Reaching All Americans

by:

June 29, 2020

As the effect of the COVID-19 pandemic has reverberated, the payments system has continued to operate, ensuring that the economy continues to function. Although there have been changes in the ways transactions are occurring, the payments infrastructure that supports them is working well—though perhaps not as fast as some would like. A more pressing issue, however, is how to reach consumers who do not have the ability to receive payments electronically into a bank account.

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In response to the pandemic, the federal CARES Act, which provides emergency relief programs to small businesses and consumers, was signed into law. As a result, consumers are receiving economic impact payments (EIP) to help combat the financial effects. The U.S. Treasury Department began sending EIPs to consumers April 15, and much attention has been paid to how quickly the payments are reaching consumers. The majority of EIPs are being deposited electronically into bank accounts using tax return, Social Security Administration and information entered into an Internal Revenue Service (IRS) portal. A limited number of payments is being funded through deposits to prepaid cards. And finally, those without a bank account or who don’t provide the IRS with bank account information are receiving payments by checks in the mail; unfortunately, many of these recipients will be low-income families who may need the funds the most.

The EIP process reveals that a more efficient solution for making payments in a crisis is needed for both those with and without bank accounts. It would be beneficial not only to make payments faster, but also to ensure the reachability of all U.S. households. Proposed options that may facilitate these outcomes could include utilizing existing nonbank services, creating some form of central bank digital currency (CBDC), using real-time payment rails, and/or developing a federated directory.<sup>[2]</sup>

Nonbank prepaid cards are one means to make electronic payments to those without a bank account. Many of these services enable direct deposit of funds such as payroll and income tax refunds to be made directly to the card account. Prepaid cards typically are network-branded and may be used at any point of sale that accepts that network's payments. Prepaid cards also may be used online to make payments and, with the use of a PIN, cash can be withdrawn at an ATM. While nonbanks are the providers of these prepaid products, they generally work with depository institutions to ultimately facilitate the payment. The Consumer Financial Protection Bureau has taken steps to make it easier for consumers to receive pandemic-relief payments on prepaid cards, including the EIPs authorized in the CARES Act. As a result, nonbank service providers such as PayPal and Netspend were able to offer customers with accounts meeting certain requirements the option to receive direct deposit of the EIP funds. The availability of these accounts is helpful, but likely not a solution for all unbanked consumers. Given the pandemic, those who rely on public internet access may find that access more difficult to obtain. However, once such accounts are established, the opportunity exists to take advantage of mobile wallets offered by these and other similar providers. While falling short of the access that being banked would offer, such services do provide an entry point to more efficient financial services.

Another option is a version of a CBDC put forth by Congress as part of the CARES Act, though not included in the law.<sup>[3]</sup> Current U.S. legislation proposes pass-through "digital dollar" wallets, where digital dollars are digital ledger balances recorded as liabilities in the accounts of Federal Reserve Banks. This account-based vision of a CBDC would not require new payment rails and likely would resemble central bank reserves. The hope is that those who currently do not have a bank account would be able to open a "FedAccount" at a location such as a post office. However, questions remain as to whether those without a bank account would choose to open a FedAccount. For example, those citing privacy as a reason for being unbanked may not be inclined to open an account with the Federal Reserve due to uncertainty about how much information the Federal Reserve would be required to know about each account.

Alternative CBDC models also have been proposed as possible solutions. Unlike FedAccounts, these models create an entirely new instrument on a new payments platform that often is meant to resemble a digital version of cash. While it is understandable in theory that a digital version of cash makes the payments seem likely to go quicker, more needs to be understood about how a CBDC could reach consumers, such as how to verify the wallets of a CBDC user and how these would be registered for such a distribution. Proper payment authentication still would need to occur regardless of instrument, so simply allowing someone to create a CBDC wallet would not necessarily mean that the Treasury would be willing to send money to it. And as with any CBDC proposal, there are numerous issues that would need to be addressed prior to issuance.

Funds transfers using real-time, instant payment systems would improve both reachability and speed, as well as move funds safely and efficiently. These types of payments require an infrastructure that connects banks across the country. This nationwide reach may be achieved through the presence of the existing instant payments service, The Clearing House's

Real-Time Payments, and the Federal Reserve Banks' FedNow<sup>SM</sup> Service, which is being built. The FedNow Service is expected to provide public benefits related to the safety, efficiency and accessibility of instant payments, specifically through its ability to reach over 10,000 of the country's diverse depository institutions. Instant payments such as those transmitted over these new payment rails enable end users to access their funds in near real-time, with immediate settlement between depository institutions. As a result, these payments will offer a better alternative to existing electronic payment methods, but the question of how to reach those without bank accounts still would remain.

To more efficiently reach all consumers, a directory that can be used to find end-user information, agnostic to the method of payment delivery, could be a part of a solution. Owner(s) of the directory(ies) could have relationships with payment providers that would facilitate routing to the appropriate entities for distribution to their customers. However, there are matters that still would need to be addressed with a directory, such as ensuring that data is protected, identifying the payment recipient digitally, and resolving questions of ownership of and the means by which various directories connect or can be accessed.

The combination of an instant payments service with nationwide reach, with a robust directory service, would address some of the challenges creating inefficiencies in emergency relief payments today. However, also causing delays are other time-consuming endeavors that the payment alternatives cannot solve because they are unrelated to how the payment is sent: determining who gets the money and where the money should be sent. These problems largely exist regardless of the payment method chosen; with regard to the former, that is a policy issue that lies outside of payments, and with regard to the latter, the only suggestion that seeks to address it is the directory.

*Continued, concerted efforts are needed on several important fronts:*

- researching how best to reach the unbanked and underbanked;
- investigating the role of nonbanks and understanding opportunities for their involvement;
- exploring experimentation and motivations for a CBDC; and
- determining the optimal directory model to gain desired benefits while managing risks.

For our part as the central bank, and a provider of payment services to U.S. depository institutions, the Federal Reserve is focused on providing modern, fast, safe payments by building and operating the FedNow instant payments rail. Although this platform will not be a solution for all of the issues noted here, history has shown that a solid foundation is key to the efficient flow of payments, and to promoting innovations that enrich end users' experiences with the payments system. I believe these steps are critical, and ultimately, they hold the promise of getting us closer to the goal of reaching all Americans.

## Endnotes

- [1] Accessed May 7, 2020, at <https://www.fdic.gov/news/news/press/2018/pr18077.html>
- [2] A federated directory is one that enables a collection of directories and other sources of data to be combined and treated as a single hierarchical directory. For example, Zelle person-to-person payments utilize a directory that enables end users to pay other end users using trusted, registered providers.
- [3] While discussion in the United States is increasing, central banks have researched CBDC for years; see Jesse Maniff, [KC Fed Payments System Research Briefing](#), February 2020.
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