

General Discussion

Building a Safer Payment System Through Collective Action

Mr. Dubbert: Very good, we will open it up for questions from the audience. Let me start. Governor Powell, obviously, all of us have heard a great deal about the Office of Personnel Management (OPM) breach in recent days and weeks. If you might reflect on that, the scale of that breach, and its impact on the federal government. Is it a watershed moment perhaps in how we rally collective resources of the government and the private sector to try to move forward to address the underlying issues there?

Mr. Powell: I will say that it seems to me to be a very important event and something that we are living with daily. I have a great portion of the administrative responsibilities that the governors share on the Federal Reserve Board. So I will just say that we are very focused now on understanding what happened. We are still learning very much what happened over at OPM. We are focused on communicating about that to our employees. And we are focused on looking out for our employees. We are determined to look out for the best interests of our employees throughout the Federal Reserve System on this. I would just say we are living through this personally right now at the Fed, through the whole system, particularly at the Board, and living the reality that we all face.

Mr. Stervinou: You talked about basically moral suasion and the role of the Federal Reserve and the Board of Governors in driving the market toward the goal of faster payments and security. When we talk about security, there is the oversight capacity and the supervisory capacity of the Federal Reserve. Do you think that there is a need also to go further, to push the market a little bit more in the direction of more security? I mean, to use your mandate to actually drive a little bit more the security aspects of what the market players are putting in the field?

Mr. Powell: Thank you for your question. Remember what we do is we supervise banks, not all financial institutions, just banks—state member banks and all the holding companies. At our Federal Financial Institutions Examination Council, we have guidance in place and we do supervise banks. Guidance requires banks to have secure information programs and that kind of thing. So it is an area of intense focus for small, medium and large banks, and for our supervision of them. We have people who are expert in that area who really focus just on that, and it goes to both the security program and also the response program. So we are doing a great deal. I think any of our regulated entities would tell you that it is a major focus. It is also a focus for us in our own payment activities. I think it is important to say again that we do not have this plenary authority over the financial system or over the whole payment system, which I think some other countries—and I am not recommending these things—have much more consolidated financial systems than we do and have much more concentrated authority to regulate and supervise them. Our own authority is quite specific and does not extend to non-regulated entities. Now, I would also add that many entities are regulated at the state level and also regulated by other federal entities. It is not that they are completely unregulated, but they are not regulated by the central bank or by other banking regulators. And just to echo that, it is something we spend a great deal of time on as do all of the financial institutions we supervise.

Mr. Grover: When consumers and businesses are asked whether they like the idea of faster payments, they almost universally or certainly a large number say yes. Do you think, however, there is a commercial case to be made for faster payments?

Mr. Powell: So the question is whether there is sort of a commercial use case, and I think the answer is yes. I think one needs to be objective about it. We looked carefully at what the use cases were, and they exist. Consumers do want some faster payments, businesses want some faster payments; not every payment needs to be made instantaneously. So the initial use case may be fairly confined in scope. On the other hand, it is really hard to know. Once faster payments come along, it may be that adoption is very wide and there is quite a lot of adoption and support for it. But we are very mindful of where; that it is just not some broad thing where everyone needs every payment to be settled right away. That is really not the case.

Mr. Carr: Governor, I really appreciated your comment that—I wrote this down—“Preventive measures are not enough,” and your talk about insider issues. I do not really understand why there has not been a wholesale movement to encryption of data so that when we are penetrated and when our people make mistakes, we are better protected; we are coming up to the EMV period here. Oct. 1 is a big day. There are many of us putting a lot of energy and effort into rolling out EMV, and I am getting chip cards these days, and when I use my chip card on Oct. 2 and there is a breach, my PIN is still going to be exposed. I just wonder whether consumers are going to be expecting to have fewer problems with breaches because of EMV. Certainly it is going to be more difficult, impossible perhaps, to make counterfeit cards, but the data is still there to do card-not-present fraud for these chip cards. And it baffles me why we have not moved to chip and PIN with these transactions to protect them, and if we have not, why in the world are we not encrypting this data? That is an observation. I just appreciate your comments.

Mr. Powell: That is a great question and I think there are plenty of people in the room who you might address that to as the conference goes on. We do not land on any one particular thing and say we have to do this, but clearly PIN is better than signature, and there are other things that may be better than PIN, and we believe in layering. We are learning as we go and unfortunately one of the ways we learn is by making mistakes and getting breached and figuring it all out. It is one of the purposes of this conference; to try to move that dial forward.

Ms. O'Malley: I am interested, Governor Powell, in your perspective as a member of the Board of Governors on the introduction or the entrance of these new digital giants into the marketplace and the roles they are playing now in authentication and the delivery of payment services to consumers. I am sure the Board of Governors has had a lot of debate and I would be interested in your insights on this issue.

Mr. Powell: And when you say new digital giants, what are we talking about here?

Ms. O'Malley: Apple, Google, etc.

Mr. Powell: The Board of Governors does not have a position on that. It is not something we actually debate. But I think our overall position is to be supportive of innovation in the payments system. Even on Bitcoin, if you saw Chairman Bernanke's letter last year, what he said was, “Look, we

generally support innovation in payments. It is progress.” And again, as I said, what choice do we have? Innovation is ongoing. The thing is it has to be done safely and it has to be done in a way that does not enable money laundering and things like that. So that is not an issue with the companies you mentioned, but it could be with some of the virtual currencies. So I guess just speaking for myself, my broad sense is these are things the consumers want, the consumers are getting, and it is up to those of us in the supervision, regulation, public communication spheres to make sure that the way they get them is well understood by the public and well regulated and supervised by the government so when problems happen, we have anticipated them and done what it is we can do.

Mr. Horwedel: Earlier you spoke about other markets in which there was some sort of government mandate to move payments forward. Given all the inertia in the U.S. payments market, do you really think that it is possible through trying to build consensus that we can draw even with or surpass other markets that are now considerably more advanced than we are in payments?

Mr. Powell: Actually, I do, and I will tell you why. In our system, I do not put a lot of probability on the idea that we will evolve in the direction of a more consolidated financial system or consolidated regulatory, or that we should want to. It is just assumed that it is what it is and it is not going to change, which is very likely. Look at what we have. All of these innovating companies are here. They are in the United States. They are involved, many of them, in our payment system efforts. So we also just have a more flexible economy. We have far less in the way of what economists like to call structural rigidity. So we are able to innovate. I am not saying it is going to be easy, but I actually feel like we have a chance to do something really constructive here with our payment system initiative and I am very excited about the prospects for it. I hope I am not naïve about the difficulties, but we have a lot of assets as well as other attributes.

Mr. J. Williams: Governor, the number of different payment systems that comprise the whole retail payment system is only increasing. New payment mechanisms are being invented almost daily. What do you think the role of retirements and renovation of the legacy payment systems we currently have is in actually reducing the envelope that we are trying to secure? I have to say the United States and many other European countries are not much better than we are in the U.K., but I would be interested in your view.

Mr. Powell: A really interesting question. I guess it would not be inappropriate to share when I joined the Board three-and-a-half years ago, there was an important decision being made over whether we should migrate off Lotus Notes. And we did do that with a lot of pain and suffering too. So I guess that question is probably better addressed to some of our subject matter experts here. But these legacy technologies tend to last a long time. We were talking at dinner last night with Peter Fonash. He said people are still using COBOL actively, which I remember learning about a couple years back in the ninth grade, eighth grade. So you are right, it does present a challenge. But we can push forward and embrace what we seem to be good at, which is technological innovation and flexibility. All we can do is the best we can.

Mr. Dubbert: Governor Powell, thank you very much for being with us today and for your personal leadership on behalf of the Board of Governors in the payment space.

Mr. Powell: Thanks again, and have a great conference.

