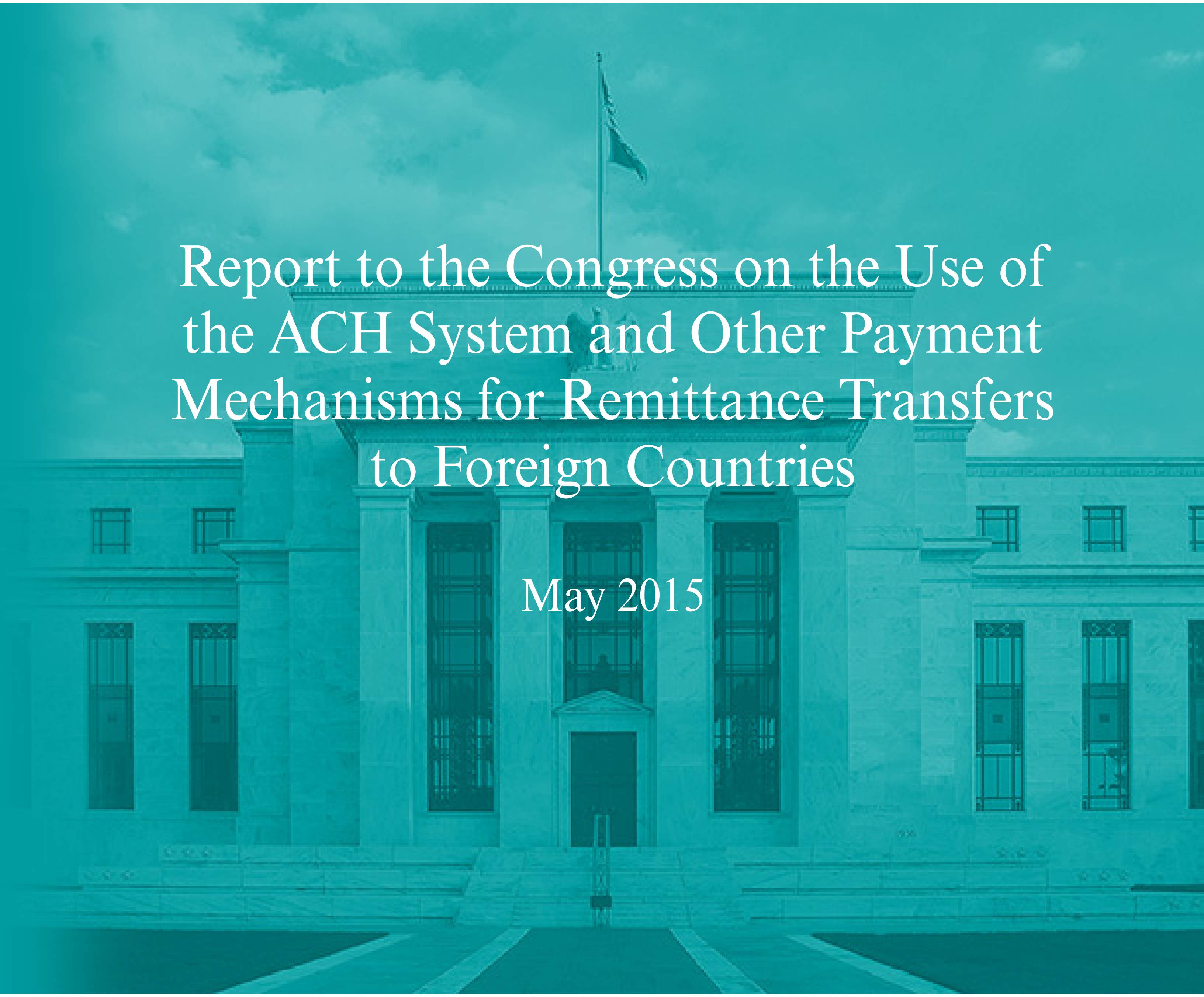

# Report to the Congress on the Use of the ACH System and Other Payment Mechanisms for Remittance Transfers to Foreign Countries

May 2015

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

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# Introduction

Section 1073(b) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) directs the Board of Governors of the Federal Reserve System (the Board) to provide biennial reports to the Congress over 10 years regarding the Board's work with the Federal Reserve Banks (Reserve Banks) and the U.S. Department of the Treasury (Treasury) to expand the use of the automated clearinghouse (ACH) system and other payment mechanisms for remittance transfers to foreign countries.[1] Section 1073(b) instructs the Board to include in its report an analysis of adoption rates of international ACH transactions (IATs) rules and formats, the efficacy of increasing adoption rates, and potential recommendations to increase adoption. Pursuant to this statutory direction, the Board is issuing this third biennial report.[2]

[1] Pub. L. No. 111-203, 124 Stat. 2065 (2010). As defined by section 1073(a) of the Dodd-Frank Act, a remittance transfer is an electronic transfer of funds—requested by a consumer located in the United States—to a consumer or business in a foreign country.

[2] The Board consulted with the Reserve Banks and the Treasury to develop this report. The Board's previous reports were published in July 2011 and April 2013, see Board of Governors of the Federal Reserve System (2011), *Report to the Congress on the Use of the Automated Clearinghouse System for Remittance Transfers to Foreign Countries* (Washington: Board of Governors, July), www.federalreserve.gov/boarddocs/rptcongress/ACH_report_201107.pdf, and (2013), *Report to the Congress on the Use of the Automated Clearinghouse System for Remittance Transfers to Foreign Countries* (Washington: Board of Governors, April), www.federalreserve.gov/publications/other-reports/files/ACH_report_201304.pdf.

# Developments

This section highlights key developments since the Board's second biennial report in 2013, which include publication of the Federal Reserve System's *Strategies for Improving the U.S. Payment System* paper (Strategies Paper), issues relating to economic sanctions and anti-money-laundering requirements, implementation of and revisions to the remittance transfer rule, and new remittance data reporting.

## Payment System Improvements

On January 26, 2015, the Federal Reserve released the Strategies Paper, which presents a multifaceted plan for collaborating with payment system stakeholders—including large and small businesses, emerging payments firms, card networks, payment processors, consumers, and financial institutions—to enhance the speed, safety, and efficiency of the U.S. payment system.[3] One of the desired outcomes for the U.S. payment system set forth in the Strategies Paper is enhanced cross-border payments, including remittance transfers, specifically "[b]etter choices for U.S. consumers and businesses to send and receive convenient, cost-effective and timely cross-border payments."[4] The Strategies Paper identifies several strategies for improving cross-border payments in support of this desired outcome, including assessing payment formats and considering enhanced Reserve Bank services.

In 2014, the Reserve Banks and industry stakeholders (the co-sponsors) concluded a business case assessment of the use of the ISO 20022 payment format standard in the United States.[5] The co-sponsors evaluated whether adoption of the standard in the United States was necessary for U.S. businesses, financial institutions, and payment networks to remain interoperable and competitive with other markets and for the U.S. dollar to maintain its attractiveness as a global currency. The co-sponsors determined that, although there was no overarching financial business case at the time of the assessment, there may be strategic reasons for adoption of the standard.[6] For that reason, the co-sponsors identified several key recommendations:

3 Federal Reserve System (2015), "Strategies for Improving the U.S. Payment System," (Federal Reserve System, January), fedpaymentsimprovement.org/wp-content/uploads/strategies-improving-us-payment-system.pdf. The Strategies Paper communicates desired outcomes for the payment system and outlines the strategies the Federal Reserve will pursue, in collaboration with stakeholders, to help the country achieve these outcomes. See also, Federal Reserve System (2013), "Payment System Improvement—Public Consultation Paper," (Federal Reserve System, September), fedpaymentsimprovement.org/wp-content/uploads/2013/09/Payment_System_Improvement-Public_Consultation_Paper.pdf (Consultation Paper). The Consultation Paper shared the Federal Reserve's perspectives and sought industry input on the key gaps and opportunities in the current U.S. payment system and on desired outcomes. Enhancement of cross-border payments was initially expressed as one desired outcome in the Consultation Paper and was incorporated as a desired outcome in the Strategies Paper after additional consideration and industry input.

4 Federal Reserve System (2015), "Strategies for Improving the U.S. Payment System," p. 2.

5 ISO 20022 is the standard for financial messaging created by the International Organization for Standardization. See "ISO 20022 Universal financial industry message scheme," www.iso20022.org/ (accessed March 24, 2015). The co-sponsors included the Federal Reserve Bank of New York, The Clearing House Payments Company L.L.C., NACHA—The Electronic Payments Association, and the Accredited Standards Committee X9—Financial Industry Standards, Inc.

6 See Federal Reserve Financial Services, "Research Results Summary—ISO 20022 Business Case Assessment," fedpaymentsimprovement.org/wp-content/uploads/iso_20022_business_case.pdf (accessed March 24, 2015). The co-sponsors engaged an external consultant to evaluate the business case for adoption of ISO 20022 payment messages by payment participants. The consultant determined that there was not a compelling financial business case for adoption of the standard in the United States because of a general lack of understanding of ISO 20022 and a satisfaction with the status quo among the broader spectrum of U.S. payment stakeholders. The consultant did, however, identify several strategic reasons for adoption of the ISO 20022 standard. First, the ISO 20022 format would enable the United States to maintain parity with other global markets. Second, standardizing message formats allows for consolidation of payment platforms at banks and corporations, which could promote straight-through processing and drive down costs. Finally, a common format promotes ease of transacting domestically and globally by using a single, open standard rather than multiple proprietary standards.

- promote the ISO 20022 standard through planning and education and develop a national strategy for adoption
- enable the ISO 20022 standard for cross-border payments
- consider additional issues such as adoption of the standard for domestic payments and for new products and services

Going forward, the co-sponsors intend to identify specific "pain points or opportunities" that the ISO 20022 standard could address.[7] The Federal Reserve made clear in the Strategies Paper that it intends to work with the co-sponsors to consider ISO 20022 implementation strategies.[8]

The Reserve Banks' current international ACH service, called FedGlobal® ACH Payments (FedGlobal), which facilitates remittance transfers and other cross-border payments, provides service to 35 countries in North America, Latin America, and Europe.[9] In 2013, the Reserve Banks made available the FedGlobal® Formatting Aid, which assists FedGlobal subscribers in meeting Dodd-Frank Act disclosure requirements by producing a receipt with transaction details for the sender.

To further facilitate remittance transfers and other cross-border payments, the Reserve Banks continue to assess possible expanded service offerings. The Board noted in its 2013 report that the Reserve Banks issued a request for information (RFI) in late 2012 regarding various international payments products and services. As a result of the RFI, the Reserve Banks issued a request for proposal (RFP) in late 2013 to identify methods for expanding FedGlobal's geographic reach.[10]

The Board also noted in its 2013 report plans to assess wire-transfer service options for expanding cross-border payments. Since then, the Federal Reserve completed a review of one possible option that would enable Federal-Reserve-account-holding institutions participating in the Federal Reserve's wire service (the Fedwire® Funds Service) to send cross-border payments. After considering the costs, benefits, and risks, the Federal Reserve has determined not to pursue at this time an international wire-transfer service as an option for expanding cross-border payments. The Federal Reserve continues to evaluate FedGlobal in light of similar factors.

## Economic Sanctions and Anti-Money Laundering

The Board has noted since its first report that concerns regarding compliance with economic sanctions and anti-money-laundering requirements, including the Bank Secrecy Act (BSA), may cause depository institutions to take a cautious approach to providing international payment services.[11] Over the past four years, high-profile compliance deficiencies, significant civil money penalties, and other compliance program costs have increased financial institutions' focus on their obligations under the BSA and its implementing regulations.[12]

Anecdotal evidence suggests that, in light of these obligations and associated costs, depository institutions are making business decisions to reexamine their cross-border payment service offerings and account relationships. Specifically, reports suggest that large depository institutions may be reducing or restricting correspondent banking relationships, which in turn may limit the ability of smaller depository institutions to provide remittance transfer services.[13] Reports also suggest that depository institutions may be terminating the accounts of some non-bank payment providers that offer financial services

7 Federal Reserve Financial Services, "Research Results Summary—ISO 20022 Business Case Assessment," p. 2.

8 The Federal Reserve will also encourage the co-sponsors to express intent to support ISO 20022, with the timing, means, and scope of adoption to be determined once more detailed work is complete.

9 The Reserve Banks, through FedGlobal, offer international ACH services to depository institutions, which in turn can offer the services to their customers. The service began as a pilot program for outbound commercial ACH transfers from the United States to Canada in 1999. In providing FedGlobal, the Reserve Banks act as a gateway operator to establish interfaces with foreign payment systems. The Retail Payments Office of the Federal Reserve Bank of Atlanta manages the Reserve Banks' check and ACH services, including FedGlobal.

10 The Reserve Banks received 13 responses from the 80 entities to which the RFP was issued.

11 The term "depository institution" in this report means insured depository institutions, as defined in section 3 of the Federal Deposit Insurance Act (12 U.S.C. 1813), and insured credit unions, as defined in section 101 of the Federal Credit Union Act (12 U.S.C. 1752).

12 31 CFR Chapter X.

13 See, for example, International Chamber of Commerce, (2014), *ICC Trade Register Report Summary—Global Risk in Trade Finance*, Version 1 (June 18), www.iccwbo.org/Data/Documents/Banking/General-PDFs/ICC-Trade-Register-Report-2014-SUMMARY/; Patrick Jenkins (2013), "Banks Pull Back from Risky Regions," *Financial Times*, (April 21), www.ft.com/cms/s/0/47c3432a-aa5d-11e2-9a38-00144feabdc0.html#axzz2R9GHVilt (registration required).

to consumers, such as money services businesses.[14] Without accounts at depository institutions, some nonbank payment providers may be unable to access the financial system and therefore may be unable to continue providing services, including remittance transfer services.[15]

Treasury has encouraged an international survey, to be led by the World Bank, to gather more comprehensive information on the scope, drivers, and effects of potential challenges faced by money services businesses in gaining financial access. The World Bank plans to circulate the survey later this year to governments, money services businesses, and depository institutions. The Federal Reserve is also discussing the issues of financial access and the reduced number of correspondent banking relationships with depository institutions and other public authorities, both within the United States and internationally.

## Remittance Transfer Rule Updates

In 2013, the Board noted that, in addition to economic sanctions and anti-money laundering regulatory requirements, depository institutions were concentrating compliance efforts on the Consumer Financial Protection Bureau's (CFPB) remittance transfer rule, which amends Regulation E.[16] The rule became effective on October 28, 2013, and provides certain protections to consumers sending remittance transfers, including required disclosures, error resolution, and cancellation rights.[17]

On September 18, 2014, the CFPB amended the remittance transfer rule to extend until July 2020 a temporary exception for insured depository institutions providing remittance transfers.[18] Depository institutions may estimate the amount of funds to be received by the designated recipient if the institution is unable to know the actual amount for reasons beyond its control.[19]

The CFPB extended the exception after determining that termination of the exception in July 2015 would negatively affect the ability of depository institutions that are remittance transfer providers to send compliant remittance transfers. At the same time, the CFPB made several clarifications and technical corrections.[20] On September 12, 2014, the CFPB also finalized a rule to implement its supervisory authority

[14] In November 2014, for example, the Financial Crimes Enforcement Network (FinCEN) called attention to the issue, stating that "Money services businesses ('MSBs'), including money transmitters important to the global flow of remittances, are losing access to banking services, which may in part be a result of concerns about regulatory scrutiny, the perceived risks presented by money services business accounts, and the costs and burdens associated with maintaining such accounts." See FinCEN (2014), *FinCEN Statement on Providing Banking Services to Money Services Businesses* (Washington: FinCEN, November 10), www.fincen.gov/news_room/nr/pdf/20141110.pdf (footnote omitted).

[15] At least one report expressed concern that this would be the case for providers of remittance transfer services to Somalia. See Scott Paul, Anne-Marie Schryer-Roy, Ben Murphy, and Ed Pomfret. Adeso, Global Center on Cooperative Security, Oxfam International, Joint Agency Briefing Note (2015), *Hanging by a Thread* (February 19), www.oxfam.org/sites/www.oxfam.org/files/file_attachments/bn-hanging-by-thread-somalia-remittances-190215-en.pdf. However, the U.S.-Somalia corridor may be an especially unique scenario given Somalia's current financial infrastructure.

[16] 12 CFR 1005.

[17] 78 FR 30661 (May 22, 2013). The rule, discussed in greater detail in the Board's 2013 report, implements section 1073(a) of the Dodd-Frank Act and requires a remittance transfer provider to supply senders with written prepayment disclosures that contain, among other things, (1) the exchange rate, (2) fees, and (3) the amount to be received by the designated recipient in the foreign country. The remittance transfer provider is also required to furnish a written receipt that, in addition to the information from the prepayment disclosure, must include the promised date that funds will be delivered to the recipient and information regarding the sender's error-resolution rights under section 1073(a). The amendments also set forth requirements regarding (1) timing of disclosures and receipts, (2) provision of estimates for certain disclosures, (3) error resolution, and (4) procedures for cancellations or refunds.

[18] Section 1073 of the Dodd-Frank Act as implemented in 12 CFR 1005.32(a)(2), see 79 FR 55970 (September 18, 2014). The statute provides that the exception would expire on July 21, 2015, but establishes that the CFPB may extend the exception to July 21, 2020, if it determines that the termination of the exception in July 2015 would negatively affect the ability of depository institutions to send remittance transfers.

[19] Provided that a sender is sending a remittance transfer from the sender's account with the depository institution.

[20] The clarifications and technical corrections include (1) clarifying that U.S. military installations abroad are considered to be located in a state for purposes of the rule; (2) clarifying that whether a remittance transfer from an account is for personal, family, or household purposes may be determined by ascertaining the primary purpose of the account; (3) clarifying that faxes are considered writings for purposes of satisfying certain provisions of the rule that require remittance transfer providers to provide disclosures in writing, and that, in certain circumstances, a provider may provide oral disclosures after receiving a remittance inquiry from a consumer in writing; (4) permitting providers to include the CFPB's new remittance-specific consumer web pages as the site that providers must disclose on remittance transfer receipts; and (5) clarifying two of the rule's error-resolution provisions.

over nonbank money transfer providers conducting more than one million international money transfers annually.[21]

## New Data Reporting

Effective March 2014, the Federal Financial Institutions Examination Council (FFIEC) revised the Consolidated Reports of Condition and Income (Call Report) to start collecting information about remittance transfers.[22] As a result, the Call Report now collects information about ACH, wire transfers, and proprietary services that are used to provide remittance transfer services to consumers.[23] Institutions with more than 100 transactions must also provide an estimated number and dollar value of those transfers.[24]

21 79 FR 56631 (September 23, 2014). See 12 CFR 1090.107.

22 The Call Report provides financial data regarding condition and results of operations of most institutions insured by the Federal Deposit Insurance Corporation (FDIC). Data are reported as of the close of business on the last calendar day of each calendar quarter (report date). Call Reports must be submitted no more than 30 calendar days after the report date (submission date).

23 Reported semiannually as of the June 2014 and December 2014 report dates.

24 Reported annually as of the June 2014 report date.

# Adoption Rates

As of December 2014, of institutions completing the Call Report, 3,660 institutions reported offering remittance services to consumers.[25] Of those institutions, 479, or 13.1 percent, provide the option to perform remittances via ACH transfers, which use the IAT format.[26] Commercial IAT volume grew 28.9 percent from 2012, when the Board completed its previous report, to 2014, while overall ACH volume grew 8.9 percent.[27] Through FedGlobal, the Reserve Banks processed 0.2 percent of the total commercial IAT volume handled by the ACH operators in 2014.[28]

As shown in table 1 below, between 2012 and 2014, FedGlobal commercial IAT volume fell by 25.5 percent. This decline was largely due to a high number of low-value class-action settlement payments delivered to Europe that inflated 2012 transaction volume. When compared to 2013, a year without a high volume of these types of payments, FedGlobal commercial IAT volume grew at a modest 5.2 percent in 2014. From 2012 to 2014, FedGlobal commercial IAT value increased 46.4 percent.[29] FedGlobal service to Canada currently represents 62.3 percent of FedGlobal volume, with 70,159 IAT transactions valued at $1.5 billion in 2014.[30]

25 In addition, insured credit unions report the number of international remittances originated year-to-date but do not collect information on the type of service used. These data are collected through the National Credit Union Administration (NCUA).

26 As of June 30, 2014, of the 4,359 depository institutions offering remittance transfer services to consumers, 557, or 12.8 percent, offered consumers the option to complete remittance transfers via ACH transfers, which use the IAT format. The IAT format, a standard entry classification adopted in 2009, does not distinguish among consumer, business, or government transactions. The IAT format replaced two prior formats—consumer cross-border payment and corporate cross-border payment originally established in 1999—that were determined to be inadequate for regulatory compliance purposes. The IAT format allows depository institutions and ACH operators to identify IAT payments.

27 "Commercial" refers to payments initiated by a business or a consumer but not by the U.S. government. The portion of IATs that are "remittance transfers" as defined by section 1073(a) of the Dodd-Frank Act is not determinable from the available data.

28 In 2014, the two U.S. ACH operators processed 18.3 billion total ACH transactions, of which 54.6 million (0.3 percent) were commercial IATs. In 2012, the two U.S. ACH operators processed 16.8 billion total ACH transactions, of which 42.4 million were commercial IATs.

29 Total value of IAT transactions handled through FedGlobal grew from $1.33 billion in 2012 to $1.94 billion in 2014.

30 Transaction volume to Canada increased 65.4 percent from 2012 and 2014, from 42,421 to 70,159 IAT transactions.

**Table 1. International Automated Clearinghouse Transactions (IATs), 2010–14**
**(number of transactions, except as noted)**

| | 2010 | 2011 | 2012 | 2013 | 2014 | 2014 median value |
|---|---|---|---|---|---|---|
| **Total IAT volume** | | | | | | |
| Commercial credits | 2,885,490 | 3,367,318 | 3,660,149 | 3,979,201 | 4,820,058 | _ |
| Commercial debits | 2,104,728 | 24,722,512 | 38,700,280 | 40,601,616 | 49,797,558 | _ |
| **Total** | **4,990,218** | **28,089,830** | **42,360,429** | **44,580,817** | **54,617,616** | _ |
| **FedGlobal IAT volume** | | | | | | |
| Commercial credits | 40,275 | 74,816 | 139,693 | 87,880 | 92,703 | $2,000 |
| Commercial debits | 3,690 | 7,670 | 11,551 | 19,202 | 19,961 | $ 140 |
| **Total** | **43,965** | **82,486** | **151,244** | **107,082** | **112,664** | |

Note: Sources for the IAT volume data are the two ACH operators, FedACH and EPN. Median value was not available for all IAT payments. The data include "inbound" and "outbound" IAT payments. FedGlobal IAT volume reflects the subset of IAT payments that the Reserve Banks handle as gateway operator.

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