

New FedNow Rules Lack Fraud Protection

May 19, 2022

Fed to launch FedNow instant payments service in 2023

WASHINGTON - The final FedNow rules announced today by the Federal Reserve Board lack protection against scams and fraud, which, if unaddressed, could leave consumers exposed when the payment service launches next year, warns advocates at the National Consumer Law Center, National Consumers League, and National Community Reinvestment Coalition (NCRC) warn.

"An instant payments service like FedNow can have a lot of benefits to consumers. The coming FedNow service will prevent instant payments from being controlled by the largest banks, but fraud protection is critical and is sorely missing," **said Lauren Saunders, associate director at the National Consumer Law Center.** "The new FedNow rules leave payments exposed to the same type of fraud that plagues Zelle today. The Fed must take measures before FedNow launches to ensure that it does not become a haven for fraud, and the CFPB and Congress must enact rules to make all person-to-person payment services safe."

The groups appreciate that the discussion of the rules did state: "The [Federal Reserve] Board believes strengthening consumer protections related to instant payments broadly is a desirable goal and supports commenters' suggestions for examining Regulation E as a potential tool."

"NCL regularly hears from thousands of consumers every year who are defrauded into sending money to scammers, including many who have lost their life's savings," **said John Breyault, National Consumers League Vice President of Public Policy, Telecommunications, and Fraud.** "These crimes work because payment networks - particularly peer-to-peer payment systems - were designed with speed and convenience, not security, in mind. The Federal Reserve must not ignore these lessons with FedNow. Doing so will only exacerbate a problem that costs consumers hundreds of millions, if not billions, of dollars in losses annually."

"It would be a mistake to underestimate the risk of fraud in FedNow," **said Adam Rust, Senior Policy Advisor at NCRC.** "We appreciate that the Fed is going to offer this service, but it is important that they get it right. We believe that the use of faster payments, not just to pay other people but also to pay businesses, will expand greatly in the next few years, which in turn could trigger even greater fraud. In the United Kingdom, where faster payments were introduced earlier, regulators report that 96 percent of "sender-authorized" fraud involves a faster payment, and the UK regulator will be requiring banks to offer scam victims compensation. That underscores why we cannot have a system in the United States that leaves consumers vulnerable to induced fraud."

FedNow will be a new bank-to-bank payment rail, similar to The Clearing House's Real Time Payments (RTP) that undergirds Zelle, enabling nearly instantaneous payments between individuals and also to and from businesses. Recent news reports have highlighted the lack of fraud protections in Zelle, prompting three senators to write a letter to Zelle's parent company expressing alarm.

In September, 43 consumer, small business, civil rights, community and legal service groups urged the Fed not to launch the FedNow service until it was safe, and in particular until it had protection against fraud in the inducement and mistakes. While FedNow payments will be covered by the Electronic Fund Transfer Act, which provides protection against unauthorized charges and errors, the EFTA currently does not protect consumers when they are defrauded into send money to a

scammer, and banks interpret the EFTA not to protect consumers against mistakes that are easy to make in Zelle and similar payment systems.

The Board finalized the rules largely as proposed, and rejected most of the suggestions made by consumer groups. The Fed did clarify that financial institutions may place a hold on FedNow payments received where there is reasonable cause to believe that a FedNow payment may be related to fraudulent activity.

“Banks that allow scammers to receive payments and financial institutions that design payment services must take responsibility for the fraud they allow into the system. Everyone will be better off if consumers are protected from fraud and have confidence when using new payment systems, and if banks and payment providers have an incentive to prevent fraud,” **Saunders added.**

The House of Representatives Financial Services Committee recently put forward a draft bill, the Protecting Consumers From Payment Scams Act, to address the issue. Consumer groups have also called on the Consumer Financial Protection Bureau to issue rules to protect consumers from fraud and errors in electronic payments.

For more information:

- Comments on proposed FedNow rules: Coalition, NCLC/NCRC/NCL and joint industry-consumer comments, Sept. 9, 2021
- Written testimony for House Financial Service Committee hearing on digital wallets, Apr. 28, 2022