

WHITE PAPER

Instant Payments

What to Know and Where to Start

For the first time in decades, the financial services industry is buzzing about a new payments rail that stands to have a deep impact on how businesses and people pay each other: instant payments (also often called real-time payments). Even though The Clearing House has offered its RTP® network for years, the Fed launched its FedNow® network in July 2023, bringing the instant payments functionality to more financial institutions.



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What Are Instant Payments?

Basically, RTP and FedNow deliver around-the-clock instant settlement. They're the first payment systems in the U.S. to support only the ISO 20022 messaging standard, and they're the first payment systems in the world to support real-conversational payments. These systems include a broader payment message set that covers the life cycle of a payment and enables the invoice/remittance data and other useful information to travel with that payment from start to finish.

On the consumer side, RTP and FedNow provide financial institutions with another option to provide fast, safe, person-to-person payments within their current digital banking platforms. The instant payments networks are also bringing innovation to bill pay and P2P models. Traditionally, billers have had the ability to deliver bill notifications or e-bills, but consumers must pay them outside of the delivery channel. With instant payments networks and financial institutions' digital banking platforms, consumers can receive a bill—complete with details—and immediately pay it, pay part of it, or schedule a payment for later.

Of course, consumers have long had access to instant payments through services such as Venmo and Zelle. But the ability to include payment details as well as settle those payments instantly will be critical to driving adoption outside of existing closed networks. Consumers are looking for ubiquity within the payments system.












The value of instant payments goes beyond just payment immediacy in commercial and small business banking, as well: better management of cash flow and timing of payments, streamlined accounts payable/accounts receivable processes, the ability to introduce new products or services using these new payment messages, and a reduction in the likelihood of NSFs and reversals as payments move to instant payment rails, to name a few. And the benefits apply across business segments—small and large.

The availability of instant payments is also driving innovative solutions that solve problems beyond traditional payment initiation. Integrated payables and API integration between digital banking systems and accounting systems have the potential to solve problems across the entire payment life cycle, including reduction in days sales outstanding (DSO) and days payables outstanding (DPO) for businesses. These solutions will create new non-interest revenue opportunities for financial institutions and deepen their relationships with their customers.



What Are the Use Cases?

The use of instant payments is applicable across segments:

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|-------------|---|-------------|--|
| B 2 B |  A small business paying an urgent invoice in order to receive goods or services | P 2 P |  College roommates splitting monthly rent and utility payments |
| |  A restaurateur who pays for farm-fresh produce from the local farmer to serve that evening's dinner specials | |  A head of household sending emergency funds to a family member on vacation |
| B 2 C |  Insurance companies and healthcare plans pay claims with immediate confirmation | G 2 C |  A government agency paying out emergency disaster relief funds to citizens impacted by a natural disaster |
| |  A retail bank distributing personal loan proceeds to a dealership on behalf of a customer who is at the showroom buying a new car | | |
| C 2 B |  Consumer pays utility bill in response to Request for Payment from the biller. | C 2 G |  A tax payer making a tax payment in time for the April 15 deadline |
| |  A busy working individual paying for general services around the house such as the gardener, cleaning services, or child care provider | |  A retail investor sending real-time money transfers to his or her investment account |
| A 2 A | | A 2 A | |
| | | | |

Source: The Clearing House

Big Questions

More financial institutions are looking into what instant payments mean for their organizations, and, understandably, they have a lot of questions.

How are instant payments different from same-day ACH?

RTP and FedNow network payments are credit push only and clear and settle individually in real time with immediate finality. Same-day ACH payments are cleared in batches and finally settle after the payments clear.

What is the difference between RTP and FedNow?

RTP is the instant payments network of The Clearing House, and FedNow is the network of the Federal Reserve. A financial institution must participate in a network to receive or originate its transactions. Although both use the same international message standard, ISO 2022, each network has its own message specifications, settlement processes, and unique rules.

How many U.S. financial institutions currently participate?

As of April 2024, the RTP network had almost 600 participants, and FedNow had more than 700.

What are the transaction types—or messages—involved with instant payments?

Message types include:

- Credit transfer or push—meaning that the person or business making the payment instructs their financial institution to make the payment
- Request for Payment
- Request for Information
- Remittance Advice
- Request for Return of Funds

Are there transaction limits?

Yes, the credit transfer limit on the RTP network is currently \$1 million. For FedNow, it is \$500,000. These are the network limits, although financial institutions may set a lower limit for their customers.

How do I connect?

There is an ecosystem of involved parties and systems behind the instant payments process, each with its own part to play. It's important for financial institutions to understand that getting started with instant payments isn't one relationship with one vendor, and financial institutions have choices to make depending on their goals and budgets.



The Instant Payments Ecosystem

Enabling instant payments requires a workflow that includes several players: the payer, the recipient, the financial institution, the third-party service provider, and the instant payments network.

Digital Banking Platform

- System that allows requester to initiate
- System that allows recipient to respond
- Connected to third-party service provider

Third-Party Service Provider

- Connected to the networks to route payment from originating system (digital banking platform) to appropriate network
- Pass through of all supported message/transaction types
- Considerations for financial institution:
 - Network participation
 - Supported transaction types

Core Account Processing System

- Receives payments from third-party service provider and credits or debits the account
- System of record

Financial Institution

- Holds relationship with the network and maintains appropriate operating standards set by it
- Responsible for funds
- Responsible for fraud
- Manages settlement processes with network

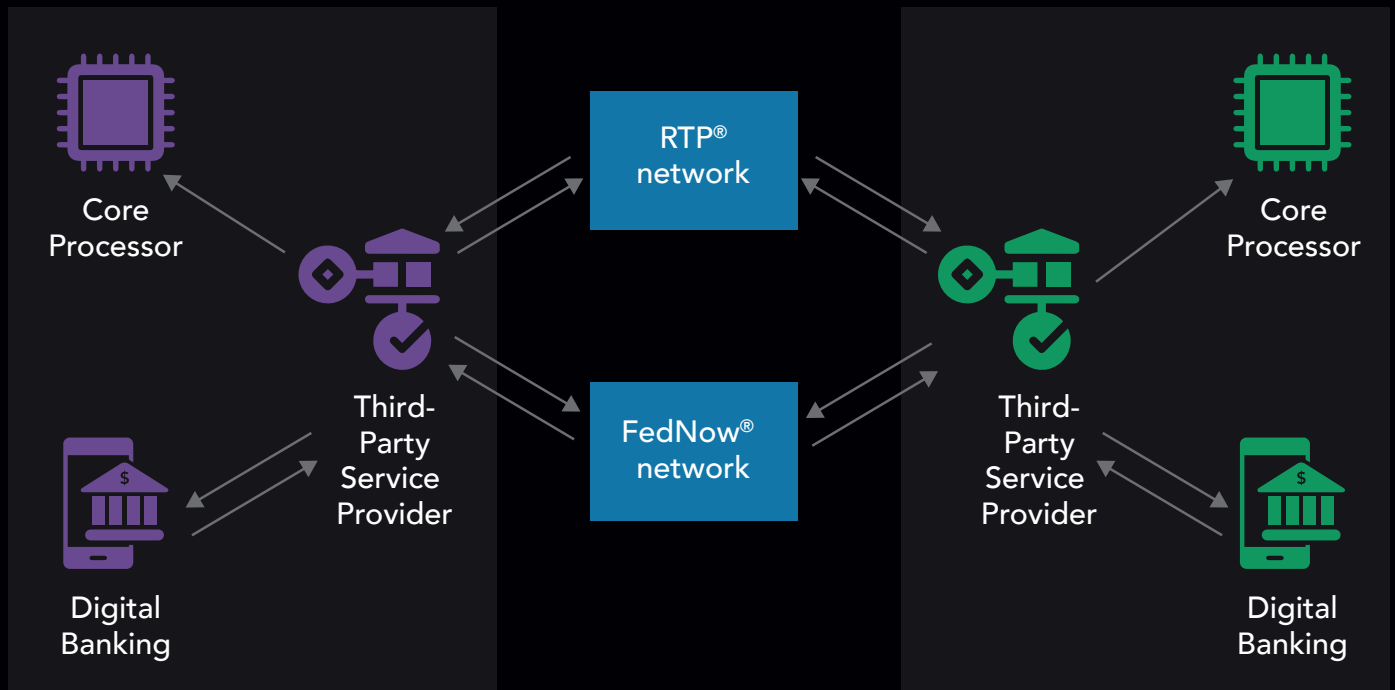


Sending FI

The Instant Payments Ecosystem



Receiving FI



Requesting a Payment

1. Sender issues a request for payment, which can include invoice information or link to the invoice, through their digital banking platform.
2. Request for payment and the accompanying information go to the sender's financial institution's third-party service provider.
3. The sender's financial institution's third-party service provider sends the request for payment and accompanying information to the instant payments network (RTP or FedNow).
4. The instant payments network sends the request for payment and accompanying information to the receiver's financial institution's third-party service provider.
5. The request for payment and accompanying information is displayed in the receiver's digital banking platform.

Sending a Payment/ Responding to a Request for Payment

1. Payer issues a payment or responds to a request for payment through their digital banking platform.
2. Payer's account is debited, and payment goes to the payer's financial institution's third-party service provider.
3. Payment is sent to the instant payments network (RTP or FedNow).
4. The instant payments network sends the payment to the receiver's financial institution's third-party service provider, and receiver's account is credited.
5. Information about payment is available in the receiver's digital banking platform.

Considerations for Financial Institutions

Do I need both RTP and FedNow?

Financial institutions should consider taking advantage of both the RTP and FedNow networks to bring the full capabilities of instant payments to customers. Payments originated within one network can't be received by a financial institution within a different network, so choosing just one network limits customers' options. Third-party service providers will provide connectivity to both networks. In addition, being on both networks helps prepare the financial institution for adding future payments methods.

Should I start with receive-only?

It is recommended that financial institutions start with receive-only to give the institutions time to make any necessary operational adjustments and prepare for the 24x7x365 instant payments environment. This provides immediate value to your customers or members by providing better payment services that they want, and it creates a new deposit channel into the financial institution. Some questions to ask yourself include how will your organization handle maintenance and change management in an always-on system with no scheduled downtime? How will instant payments be managed? Will they have a separate area similar to ACH and wire? How will instant payments affect various departments across your organization, such as Customer Service, Client Servicing, Treasury Operations, etc.?

How will instant payments impact fraud and risk?

The instantaneous, irrevocable nature of instant payments need not cause heightened risk and fraud concern for banks and credit unions. Most security measures the financial institution already takes for other payment methods apply to instant payments, but it's wise to analyze current policies and procedures to look for any pitfalls. As always, communication and training—for staff and account holders—about prevention techniques can go a long way to fighting fraud.

How do I get started?

The first step is to assess your readiness and determine how you'll connect. Visit the [FedNow](#) and [RTP](#) websites for more in-depth information about instant payments, and **contact your Q2 customer success manager to learn how Q2 can help.**