



November 12, 2017

Mr. Kieran J. Fallon  
Senior Deputy General Counsel  
Government, Regulatory Affairs & Enterprise Risk  
The PNC Financial Services Group, Inc.  
800 17<sup>th</sup> Street, N.W.  
PNC Place, 12<sup>th</sup> Floor  
Washington, DC 20006

Subject: PNC Bank, N.A. (Bank) Membership in The Clearing House's Real-Time Payment System (RTP)

Dear Mr. Fallon:

This responds to your request that the Office of the Comptroller of the Currency (OCC) confirm that it is permissible for the Bank to become a Funding Participant in RTP, developed and operated by The Clearing House Payment Company, LLC (TCH).<sup>1</sup> The Bank proposes to join RTP as a Funding Participant to facilitate the provision of real-time, small dollar, irrevocable payment services to its customers. In connection with its participation as an RTP Funding Participant,<sup>2</sup> the Bank must establish a prefunded, joint account<sup>3</sup> with other RTP Funding Participants (RTP Joint Account) at the Federal Reserve Bank of New York (FRBNY). To establish the RTP Joint Account, all RTP Funding Participants must enter into an agreement with

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<sup>1</sup> RTP is a proposed real-time, gross, small-dollar payment system developed by TCH that will operate 24 hours a day, seven days a week. TCH expects to launch the system in a pilot phase by the end of 2017.

<sup>2</sup> RTP has two types of participants: Funding Participants and Non-Funding Participants. A Funding Participant will be a joint owner of the RTP Joint Account, provide its prefunded contribution directly to the RTP Joint Account, and receive direct distributions from the RTP Joint Account. Non-Funding Participants must process transactions through a Funding Participant.

<sup>3</sup> A joint account is an account at a Reserve Bank that is shared by multiple financial institution owners, who are each individually eligible to hold a separate account at a Reserve Bank. The joint account owners jointly share the rights and liabilities associated with the joint account. *See, e.g.*, Final Guidelines for Evaluating Joint Account Requests, 82 Fed. Reg. 41951 at 41,952 (Sept. 5, 2017). To enable the 24/7 operation of RTP, RTP Funding Participants will prefund the RTP Joint Account. This will permit RTP to settle transactions outside of Reserve Bank business hours.

a Reserve Bank (Joint Account Agreement).<sup>4</sup> This Joint Account Agreement requires the Bank to provide an open-ended indemnity to the Reserve Bank for certain losses.<sup>5</sup> The Bank requests OCC confirmation that it may become an RTP Funding Participant, even though such membership would subject it to open-ended liability<sup>6</sup> for certain losses of the Reserve Bank.

For the reasons discussed below, we conclude that a national bank (bank) may join a payment system such as RTP.<sup>7</sup> As discussed in more detail below, before entering into an agreement to join a payment system, the bank should notify its EIC of its proposed membership in the payment system.<sup>8</sup> Additionally, the bank should evaluate the risks posed by such membership and ensure it can identify, measure, monitor, and control the associated risks. In addition, once the bank has become a member of the payment system, it should monitor the risks of membership on an ongoing basis. This ongoing review should be designed to ensure the bank is able to identify, measure, monitor, and control the potential exposures stemming from its membership in the payment system, including any indemnity provided to a third party such as a Reserve Bank as a condition of payment system membership. To the extent a bank identifies risks through this review that raise safety and soundness concerns, the bank should: (i) notify its EIC as soon as the concern is identified; and (ii) take appropriate actions to remediate the risk, in consultation with its EIC.<sup>9</sup>

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<sup>4</sup> See Joint Account and Services Agreement Relating to RTP. RTP Funding Participants also must sign the Joint Account Agreement as a condition of membership in RTP.

<sup>5</sup> Under the terms of the Joint Account Agreement, this indemnity may extend to multiple Reserve Banks.

<sup>6</sup> “Open-ended liability” refers in this context to liability that is not capped under the rules of the payment system, the Joint Account Agreement, or otherwise (e.g., by negotiated agreements or controlling law of the jurisdiction).

<sup>7</sup> The OCC expects that it would apply the procedures established in this interpretive letter to existing payment system memberships that involve a material change to the liability or indemnification provisions of the membership agreement.

<sup>8</sup> This notice should generally be provided at least 30 days in advance of a bank becoming a member of a payment system. The OCC recognizes that the facts and circumstances of your request necessitated a shorter timeframe.

<sup>9</sup> This EIC notice requirement and ongoing risk monitoring procedure supersede the EIC no-objection process outlined in OCC Interpretive Letter 1140 (IL No. 1140). See OCC Interpretive Letter No. 1140 (Jan. 13, 2014). The OCC expects that this transition from the no-objection process to notice and ongoing risk monitoring will enhance prudential supervision of bank payment system activities by ensuring that banks evaluate the risks of membership both at the time of membership and on an ongoing basis. Additionally, the notice and remediation provisions set forth in this letter establish clear OCC expectations for a bank that identifies risks in the course of its ongoing monitoring that present safety and soundness concerns. Notwithstanding the transition to this notice process, banks may continue to consult IL No. 1140 to inform the risk analyses and controls contemplated under this letter. For example, the criteria identified in IL No. 1140 for an effective risk management program for payment system activities may be instructive.

## Background and Discussion

RTP is a real-time, gross, small-dollar<sup>10</sup> payment system that TCH plans to launch initially as a pilot program. Both as a pilot and when fully-scaled, RTP will utilize a prefunded, joint account at the Reserve Bank to send and receive payments for participating institutions.<sup>11</sup> As a condition of using the RTP Joint Account, the Reserve Bank requires each RTP Funding Participant to sign an agreement jointly and severally indemnifying the Reserve Bank for certain losses associated with the operation of the RTP Joint Account. This indemnity is open-ended.<sup>12</sup>

Participation in RTP is restricted to depository institutions.<sup>13</sup> TCH, as the operator of RTP, must approve any new participant in the system and may take action against a participant that does not abide by the RTP rules.<sup>14</sup> Members may voluntarily leave RTP with at least 30 days' notice<sup>15</sup> and an RTP Funding Participant may terminate its joint account liability to the Reserve Bank with one day's notice.<sup>16</sup> To further reduce member exposure, TCH will limit its liability to members<sup>17</sup> and will restrict the responsibilities of the Reserve Bank.<sup>18</sup> Similarly, the Reserve Bank is able to revoke an institution's status as a joint account owner if the Reserve Bank believes that institution poses inappropriate risks to the Reserve Bank.<sup>19</sup> Payments processed through RTP will be final and irrevocable, thus reducing the settlement risks to the Bank. TCH

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<sup>10</sup> The initial payment limit will be \$25,000. The Bank expects TCH will increase the limit to \$100,000 in a few years, once RTP is more established.

<sup>11</sup> The Bank explains RTP uses the joint account because of the lower credit risk associated with an account at the Reserve Bank. Furthermore, as mentioned above, the prefunded nature of the account permits RTP to settle transactions outside of Reserve Bank business hours.

<sup>12</sup> See Joint Account Agreement, Section 4.6; Letter from TCH to Kathy Oldenborg, Director of Payments Risk Policy (June 27, 2017) at 2 (“Although there is no financial cap to the indemnity...the likelihood of a loss resulting from the indemnity to the [Reserve Bank] appears both practically limited and remote.”).

<sup>13</sup> The term “depository institution” includes: insured depository institutions under 12 USC 1813(c)(2); uninsured branches or agencies referred to in 12 USC 1813(c); and insured credit unions under 12 SC 1752(7). See Real-Time Payment Participation Rules (Participant Rules), Section I – General Eligibility Requirements (Sept. 2016).

<sup>14</sup> See Participant Rules, Sections I.A.5, IV, and VIII.

<sup>15</sup> See Participant Rules, Section VII - Resignation.

<sup>16</sup> See Joint Account Agreements, Sections 2.2 and 6.5 (stating that a resignation as a joint account owner is effective on the next Fedwire business day).

<sup>17</sup> See Participant Rules, Section X - Liability.

<sup>18</sup> See Real-Time Payments Operating Rules (Operating Rules), Section VI.C – Prefunded Balance Account and Requirements (May 2017).

<sup>19</sup> See Joint Account Agreement, Section 6.7.

rules also outline the methodology that will be used to allocate losses to members in the event of a claim by the Reserve Bank.<sup>20</sup>

The Bank identifies a number of business needs that support its participation in RTP. For example, membership in RTP will help the Bank address the needs of its retail customers and small businesses that desire faster, more convenient methods to transfer funds. Membership in RTP will allow the Bank to provide mobile payments opportunities to customers while simultaneously providing the standards for reliability, security, and consumer protection associated with depository institutions.

National banking law permits national banks, their operating subsidiaries, and their foreign branches to engage in payments related activities as activities within the business of banking, subject to safety and soundness limitations.<sup>21</sup> Memberships in payment systems can give rise to safety and soundness issues, including open-ended liability on members for losses associated with the system stemming from, for example, exposures to counterparty, sovereign, and operational risks.<sup>22</sup> For this reason, a bank seeking to join a payment system must submit a written notice to its EIC that describes the nature, scope, and extent of its activities, participation, and membership in the payment system before becoming a member.<sup>23</sup> The bank should ensure that its involvement in the payment system can be conducted in a safe and sound manner. In this regard, the bank must ensure that it can identify, measure, monitor, and control its exposures to the payment system and third parties both at the time of membership and on an ongoing basis, including having appropriate systems and controls in place.

## Conclusion

We conclude that the Bank may become an RTP Funding Participant subject to the notice condition set forth in this letter. As discussed, this conclusion provides that the Bank should

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<sup>20</sup> See Operating Rules, Section VI.H – Indemnification of Prefunded Balance Account Bank.

<sup>21</sup> See, e.g., OCC Interpretive Letter No. 1014 (Jan. 10, 2005); OCC Interpretive Letter No. 929 (Feb. 11, 2002); and OCC Interpretive Letter No. 993 (May 16, 1997) (IL No. 993). Payment system activities (e.g., electronic payments message transmission, electronic payments processing, and payments settlement among members) are clearly within the business of banking and are functionally consistent with the primary role of banks as financial intermediaries. See IL No. 993, *supra*. See also Conditional Approval Letter No. 220 (Dec. 2, 1996) (“Banks are the most important institutional participants in . . . payments systems. They deal with cash, issue, process, clear and settle checks and similar monetary instruments, administer credit card and debit card programs for consumers and merchants, and transfer funds electronically in a variety of situations and circumstances.”); IL No. 1140 (“National banking law permits national banks, their operating subsidiaries, and their foreign branches to engage in payments related activities, as activities within the business of banking, subject to safety and soundness limitations.”).

<sup>22</sup> See Banking Circular 235, International Payments Systems Risks (May 10, 1989) (BC-235).

<sup>23</sup> This is a notification provision only and does not require a bank to receive a non-objection from the EIC as specified in IL No. 1140.

ensure that it can engage in the activity on a safe and sound basis both at the time of membership and on an ongoing basis.

I trust this is responsive to your inquiry. If you have additional questions, please contact Casey Laxton, Counsel, Securities and Corporate Practices Division, at (202) 649-5510.

Sincerely,

*//Signed//*

Karen Solomon  
Acting Senior Deputy Comptroller and Chief Counsel