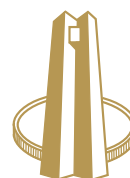


**Review of the
National Payment System Act 78 of 1998**

Policy paper
September 2018



South African Reserve Bank

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1. Introduction

- 1.1 In terms of section 10(1)(c) of the South African Reserve Bank Act 90 of 1989, as amended (SARB Act),¹ the South African Reserve Bank (SARB) is required to perform such functions, implement such rules and procedures and, in general, take such steps as may be necessary to establish, conduct, monitor, regulate and supervise payment, clearing or settlement systems. Furthermore, the National Payment System Act 78 of 1998 (NPS Act)² provides for the management, administration, operation, regulation and supervision of payment, clearing and settlement systems in the Republic of South Africa, and to provide for connected matters.
- 1.2 A national payment system (NPS) broadly encompasses the total payment process from payer to beneficiary, and includes all the systems, mechanisms, institutions, agreements, procedures, rules and laws that come into play from the moment an end user – using a payment instrument – issues an instruction to pay a beneficiary/recipient, through to the final interbank settlement of the transaction in the records of the central bank. It enables transacting parties to exchange value to conclude financial transactions, which is core to the smooth functioning and growth of the economy. Therefore, it is crucial for payment systems to remain stable, safe, efficient and transparent, and to ensure that potential risks are adequately addressed.
- 1.3 A payment system, as defined by the Bank for International Settlements (BIS),³ consists of a set of instruments, procedures and rules for the transfer of funds between or among participants, and includes the participants and the entity operating the arrangement. Payment systems are usually categorised into large-value payment systems (handling large-value, low-volume and high-priority payments) or retail payment systems (handling large-volume, low-value transactions).
- 1.4 Following the 2007–08 global financial crisis, the global financial regulatory environment underwent rigorous reforms aimed at achieving broader public policy objectives relating to financial stability, safety and efficiency, consumer protection, transparency and competition. The reforms included standards/recommendations from the international and regional policymaking and/or standard-setting bodies such as the Group of Twenty (G20), Financial Stability Board (FSB), BIS Committee on Payments and Market Infrastructures (CPMI), International Organization of Securities Commissions (IOSCO), and the Southern African Development Community (SADC). Regulatory authorities have been under tremendous pressure to regularly review and strengthen their respective regulatory and legislative frameworks, and to align these with applicable best international standards and practices to ensure coordinated and consistent regulation across jurisdictions.
- 1.5 In addition, as the payments industry becomes increasingly innovative and digital, and financial technology (fintech) becomes more advanced and faster, the emergence of new payment methods, technologies, services, risks, participants and ‘payment systems’ have become increasingly prominent and continue to challenge the traditional payments landscape. Regulatory and legislative frameworks thus need to be flexible and adaptable to these changes and need to provide an enabling environment for innovation to thrive, while remaining robust and resilient to risks that may impact the safety and efficiency of the payment systems. Global policy developments relating to financial inclusion, access to the payment system by non-banks, consumer protection, financial stability, effectiveness, integrity and competition, international best standards and practices, and recommendations from global policy and standard-setting bodies as well as assessment institutions

1 [http://www.resbank.co.za/AboutUs/Legislation/Documents/SARB%20Act/1\)%20%20South%20African%20Reserve%20Bank%20Act,%201989%20\(Act%20No.%2090%20of%201989\).pdf](http://www.resbank.co.za/AboutUs/Legislation/Documents/SARB%20Act/1)%20%20South%20African%20Reserve%20Bank%20Act,%201989%20(Act%20No.%2090%20of%201989).pdf)

2 [https://www.resbank.co.za/RegulationAndSupervision/NationalPaymentSystem\(NPS\)/Legal/Documents/NPS%20Act.pdf](https://www.resbank.co.za/RegulationAndSupervision/NationalPaymentSystem(NPS)/Legal/Documents/NPS%20Act.pdf)

3 <https://www.bis.org/dcms/glossary/glossary.pdf?scope=CPMI&base=term>



such as the World Bank and the International Monetary Fund (IMF) have necessitated a rethink of the adequacy and relevance of the existing payments regulatory framework.

- 1.6 In South Africa the financial sector is undergoing significant transformation under the umbrella of financial sector regulatory reform (Twin Peaks). Twin Peaks aims to achieve a stable financial system that works in the interests of financial customers and supports balanced and sustainable economic growth in the Republic of South Africa. The legislation implementing the Twin Peaks regulatory architecture – the Financial Sector Regulation Act 9 of 2017 (FSR Act) – took effect on 1 April 2018. The FSR Act, among other things, introduces conduct regulation and supervision of payment service providers (PSPs) in the NPS by the Financial Sector Conduct Authority (FSCA). This is aimed at strengthening consumer protection in the NPS. However, in terms of section 109 of the FSR Act, the FSCA may not implement a standard that imposes requirements on PSPs without the concurrence of the SARB.
- 1.7 In view of the above, the SARB took a decision to review the NPS Act to, among other things, assess its adequacy and effectiveness in achieving a safe and efficient NPS in the rapidly evolving financial and payments landscape. The review is aligned with the global trend of regularly reviewing perimeters of regulation to strengthen current regulatory frameworks or, where necessary, extend the regulatory net to previously unregulated sectors of the economy. Importantly, it is in accordance with section 15 of the NPS Act which requires the SARB to review the NPS Act from time to time and recommend required amendments to the Minister of Finance.
- 1.8 For the purpose of this policy paper, the following terms are defined as follows:
 - 1.8.1 **Regulation** entails the development and issuance of legal and regulatory frameworks, including primary legislation, subordinate legislation, directives, position papers and frameworks in respect of the NPS.
 - 1.8.2 **Supervision** entails the monitoring and enforcement of compliance with the legislative and regulatory framework by regulated financial institutions, critical service providers and financial market infrastructures (FMIs).
 - 1.8.3 **Oversight** is defined by the BIS CPMI as “a central bank function whereby the objectives of safety and efficiency are promoted by monitoring existing and planned payment, clearing, settlement and related arrangements, assessing them against these objectives and, where necessary, inducing change.”⁴

4 <https://www.bis.org/dcms/glossary/glossary.pdf?scope=CPMI&base=term>

2. Background

- 2.1 In April 1994 the development of the NPS legal and regulatory framework followed the launch of a collaborative effort between the SARB and the banking industry to formulate a long-term strategy for the development and modernisation of the domestic payment system. This culminated in the development and publication of the *South African National Payment System Framework and Strategy (Blue Book)* by the SARB in 1995, which contained the vision and strategy for the NPS up to 2004.
- 2.2 The *Blue Book* proposed the revision of the legal framework for the South African NPS as well as the legal entrenchment of the statutory powers and responsibility of the SARB regarding the payment system. Support of the

legal framework for the legal enforceability of payment service agreements and legal certainty regarding industry practices was also recommended.

- 2.3 In response, the SARB Act was amended to provide for the role and responsibility of the SARB in the NPS. This entrenched the SARB's role and responsibility in law under section 10(1)(c)(i) of the SARB Act, which empowered the SARB to "perform such functions, implement such rules and procedures and, in general, take such steps as may be necessary to establish, conduct, monitor, regulate and supervise payment, clearing or settlement systems".
- 2.4 The collaborative effort between the SARB and the banking industry also led to the drafting of legislation for the participants and users of the NPS, which resulted in the promulgation of the NPS Act in October 1998. The main aim of the NPS Act is to provide for the management, administration, operation, regulation and supervision of payment, clearing and settlement systems in the Republic of South Africa.
- 2.5 Since its effective date, the NPS Act has been amended by the NPS Amendment Act 22 of 2004, followed by consequential amendments by the National Credit Act 34 of 2005, Co-operative Banks Act 40 of 2007, and the Financial Services Laws General Amendment Act 22 of 2008. Key amendments included the inclusion of the rand as a continuous linked settlement (CLS) currency, the strengthening of the regulatory framework as well as the inclusion of non-bank participants in the NPS. Other than these amendments, there has not been a comprehensive review or amendment of the NPS Act since its effective date. The NPS Act has, therefore, become outdated and no longer provides the robust and adequate framework required to regulate the existing NPS and respond to existing as well as emerging payment risks and developments. This, coupled with the developments referred to in paragraph 1 above, necessitated the review of the NPS Act.
- 2.6 Accordingly, the National Payment System Department (NPSD) of the SARB⁵ initiated the review process of the NPS Act in 2015. The review commenced with an invitation to key NPS stakeholders to make submissions on the required amendments to the NPS Act. The request for submissions was followed by the establishment of the following governance structures:
- 2.6.1 The Standing Committee on the review of the NPS Act, which was established in terms of section 15 of the NPS Act. The Standing Committee comprises regulatory authorities and other relevant departments within the SARB such as the Prudential Authority (PA), Financial Surveillance Department, Financial Stability Department and Currency Management Department, as well as external regulators such as the FSCA, National Credit Regulator, Financial Intelligence Centre (FIC) and National Treasury. The Standing Committee is the decision-making body responsible for recommending the required amendments to the Governor of the SARB and the Minister of Finance.
- 2.6.2 The Expert Group, which is responsible for providing expert advice to the Standing Committee. It is constituted by industry experts appointed in their personal capacity.
- 2.6.3 The Working Group, which is responsible for providing technical, research and drafting support to the Standing Committee. It is an internal structure, supported by National Treasury and the FSCA.

⁵ The National Payment System Department is responsible for the regulation, supervision and oversight of the NPS.

- 2.7 It is expected that the completion date of the review process will be the end of 2020. The next step in the process following this policy paper entails the drafting of the NPS Amendment Bill which will inform the required amendments to the NPS Act.

3. Purpose

- 3.1 The overall purpose of the review was to examine the robustness and resilience of the NPS legislative and regulatory framework in the rapidly evolving, technologically advanced and highly innovative payments landscape. Specifically, the review aimed to highlight the strengths and shortcomings of the current regulatory and legislative framework, and to make policy proposals aimed at addressing the shortcomings and ensuring robust and appropriate regulation of the NPS in alignment with best international standards and practices.
- 3.2 The purpose of this policy paper is therefore to document the strengths and shortcomings of the NPS legislative framework as well as policy issues and recommendations aimed at enhancing the robustness and effectiveness of the NPS regulatory framework. It is aimed at informing the Governor of the SARB and the Minister of Finance on the required changes to the NPS Act and related regulatory framework.

4. Key drivers of the review

The following matters necessitated the review of the NPS Act:

- 4.1 **Emerging payment methods, technologies, services, functionalities, providers and systems**
- 4.1.1 The payments landscape is experiencing major developments in the provision of payment services and their regulation, supervision and oversight. Payment services and systems are in a period of major re-engineering and restructuring due to three main factors: (i) developments in information and communications technology (ICT); (ii) globalisation; and (iii) customer services integration. This is likely to change and redesign basic everyday payment services. Cross-border services will become common, and domestic and regional solutions will need to be aligned to international standards, systems and applications (apps). Customers, both payers and payees, will be able to integrate their devices, such as mobile devices and computers, directly with payment services. In the same way, there will be less technical differences between domestic and international telecommunications, and the differences between domestic and international payments will soon disappear.
- 4.2 **Increased focus by regulatory authorities on payment services and systems regulation, supervision and oversight**
- 4.2.1 There seems to be a growing global trend of increased focus by regulatory authorities on payment services and systems to address slow developments, insufficient competition and consumer protection needs in the payments market. Following the global financial crisis and other most recent sovereign and corporate failures, central banks and regulatory authorities are increasingly becoming 'hands-on' and assuming more regulatory, supervisory and oversight responsibilities. Typical examples are the European Commission's directives and regulations in Europe and the Australian Reserve Bank's involvement in payment developments in Australia.

4.2.2 Past experiences of economic crises and a drop in consumer trust in payment systems and services have resulted in a social need for regulating and licensing payment services. Market, system and service provider stability are required to maintain financial stability where payment systems play a major role. Licensing and regulations should support competition, and therefore measures to promote development, competition and customer services are needed in the payments industry. The payments industry is a typical network industry that requires cooperation among competitors in order to provide customer services across service providers. However, such cooperative services can also act as a barrier to further developments, as new solutions need to be adopted coherently and coordinated across all service providers. As the common payment infrastructures have become more complex and more integrated, the legacy system pressure of maintaining the status quo tends to increase in order to avoid costly changes, or at least to postpone such to the future. This may result in a situation in which the industry participants' views on the benefits of certain developments differ from the social and public authorities' views.

4.3 Section 15 of the NPS Act

4.3.1 Section 15 of the NPS Act requires the SARB to cooperate with the payment system management body (PSMB), establish a standing committee to review the NPS Act from time to time, and to make recommendations to the Minister of Finance with regard to amendments to the NPS Act which, in the opinion of that committee (i) have become advisable owing to changed circumstances; or (ii) through the administration of the NPS Act have been shown to be advisable. This review is aimed at compliance with this section by the SARB.

4.4 Twin Peaks model of financial sector regulation

4.4.1 South Africa proposed the shift toward the Twin Peaks model of financial sector regulation in 2011. The FSR Act came into effect in April 2018. The FSR Act aims to achieve a financial system that works in the interests of financial customers, and supports balanced and sustainable economic growth in the Republic of South Africa by establishing, in conjunction with other financial sector laws, a regulatory and supervisory framework that promotes the following:

- a. financial stability;
- b. safety and soundness of financial institutions;
- c. fair treatment and protection of financial customers;
- d. efficiency and integrity of the financial system;
- e. prevention of financial crime;
- f. financial inclusion;
- g. transformation of the financial sector; and
- h. confidence in the financial system.

4.4.2 The FSR Act has given the SARB an explicit financial stability oversight mandate and established the PA as a juristic person within the SARB. The PA is responsible for promoting and enhancing the safety and soundness of market infrastructures as well as financial institutions that provide financial products and securities services.

4.4.3 The FSR Act further provides for, among other things, the regulation and supervision of a 'payment service' by the FSCA in an effort to address evident conduct issues that impact customers in the payments environment. However, the FSCA is required to seek the concurrence of the SARB in respect of the issuance of conduct standards relating to PSPs. The SARB is working in close collaboration with National Treasury and the FSCA to define the scope of the FSCA in the NPS. The 'agreed' scope will be included in the relevant documentation (i.e. legislation and memorandum of understanding (MoU)), which will include the Conduct of Financial Institutions Act (COFI Act) once promulgated, the NPS Amendment Act and/or an MoU between the SARB and the FSCA.

4.4.4 This review is necessary to align the NPS Act with the relevant provisions of the FSR Act to avoid conflict and the duplication of efforts between the FSR Act and the NPS Act.

4.5 G20 and Financial Stability Board

4.5.1 The FSB has been tasked by the G20 to develop recommendations for its members on regulatory, supervisory and other financial sector policies to oversee and monitor the risks that the financial system is exposed to. This is aimed at enhancing global financial stability across all sectors of the financial system, including FMIs. Of particular interest as a driver of the review is the FSB's ongoing work to enhance the resilience, recovery planning and resolvability of FMIs. The FSB monitors and advises on market and systemic developments and their implications for regulatory policy.

4.5.2 Another matter of relevance to the review is the FSB's announcement in March 2016 of its examination of whether the growing fintech sector presents any risk to the stability of the financial system. The FSB expressed a view that technology innovations, such as blockchain, with potentially transformative implications for the financial system may have stability repercussions that should be managed.

4.5.3 Further, the G20 developed the Principles for Innovative Financial Inclusion in 2010.⁶ The principles aim to address issues related to leadership, diversity, innovation, protection, empowerment, cooperation, knowledge, proportionality and the regulatory framework.

4.5.4 The G20 and FSB are also looking specifically at providing policy direction on matters relating to shadow banking, the resolution of systemically important financial institutions (SIFIs) and over-the-counter derivatives. These policy matters are also relevant for consideration as part of this review.

4.6 Committee on Payment and Market Infrastructures (CPMI)

4.6.1 In April 2012, the Committee on Payment and Settlement Systems (CPSS – currently known as the CPMI) and IOSCO published the Principles for Financial Market Infrastructures (PFMIs).⁷ The PFMIs seek to harmonise and strengthen international risk management and associated standards applicable to systemically important payment systems (SIPSS) – also known as systemically important payment FMIs – as well as securities and derivatives FMIs, that is, central securities depositories (CSDs), securities settlement systems (SSSs) and central counterparties (CCPs). In addition, the PFMIs also outline the regulatory, supervisory and oversight responsibilities of relevant authorities in respect of FMIs, including the responsibility to clearly

6 <https://www.gpfi.org/sites/default/files/documents/G20%20Principles%20for%20Innovative%20Financial%20Inclusion%20-%20AFI%20brochure.pdf>

7 <https://www.bis.org/cpmi/publ/d101a.pdf>

define and publicly disclose the criteria used to identify FMIs that should be subject to regulation, supervision and oversight.

4.6.2 The CPMI member countries were expected to have formally adopted the PFMI by the end of 2012. However, the PFMI have not yet been adopted into the NPS Act, although in September 2013 the SARB published a position paper and a supporting information paper broadly expressing its commitment to adopting the PFMI within the NPS regulatory framework.

4.6.3 Further, the CPMI constantly issues reports, recommendations and guidelines on payment systems-related matters to guide policy and regulatory development in its member jurisdictions. These matters relate to, but are not limited to, payments aspects of financial inclusion, digital currencies, cybersecurity, recovery and the resolution of FMIs. The CPMI report released in April 2016⁸ titled 'Payment Aspects of Financial Inclusion Report' (PAFI report) provides an analysis of the payment aspects of financial inclusion as well as guiding principles designed to assist countries that are seeking to advance financial inclusion in their markets through payments. These developments have been driving the developments in the payments landscape, necessitating the review of the NPS Act to ensure that the South African payments regulatory framework is aligned with best international standards.

8 <https://www.bis.org/cpmi/publ/d144.pdf>

4.7 SADC harmonisation programmes/initiatives

4.7.1 SADC⁹ has established goals to integrate the finance and investment sectors within the region through the Protocol on Finance and Investment (FIP). The FIP was implemented on 16 April 2010 in terms of the strategic guidelines provided in the SADC Regional Indicative Strategic Development Plan (RISDP), which sets time-specific targets for regional integration.

9 The SADC Member States are: Angola, Botswana, Democratic Republic of Congo, Eswatini, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, Seychelles, South Africa, United Republic of Tanzania, Zambia and Zimbabwe.

4.7.2 Annexure 6 of the FIP endeavours to achieve, among other things, convergence across regional policies, practices, rules and procedures relating to payment systems, clearing systems and settlement systems. With a view to achieving similar legislation in the SADC region, in 2014 a study was conducted in 14 of the SADC Member States on their legal and regulatory framework for payments. Flowing from the study, the SADC Member States collaborated from 2015 to 2017 to prepare a SADC Payments Model Law (Model Law). The Model Law was approved by the Committee of Central Bank Governors in September 2017.

4.7.3 The Model Law makes provision for SADC central banks' mandates, powers and functions, including their oversight mandates; the power to conduct inspections, investigations, cooperative arrangements, consultations, access, licensing, designations and payment services; and the power to issue directives and guidelines. The principles and standards agreed to in the Model Law should be incorporated into the NPS legislation and regulatory framework.

4.7.4 In addition, SADC central bank governors approved the SADC Mobile Money Guidelines in 2016. The primary objective of the Mobile Money Guidelines is to harmonise the principles for the development of appropriate mobile money legislative and regulatory frameworks within and between the SADC Member States. This review also seeks to align the South African Mobile Money Framework with the Mobile Money Guidelines.

10 International Monetary Fund, 'South Africa Financial System Stability Assessment', *IMF Country Report No. 14/340*, December 2014, available at <https://www.imf.org/external/pubs/ft/scr/2014/cr14340.pdf>

4.8 IMF Financial Sector Assessment Program (FSAP)

- 4.8.1 During 2014, the IMF conducted a financial system stability assessment of South Africa's compliance with international standards. With regard to the NPS, the FSAP report¹⁰ found that, contrary to Principle 18 of the PFMI, access to clearing and payments was biased against new entrants and there was a lack of competition among financial institutions in the payment system.
- 4.8.2 It was recommended that more competitive behaviour by financial institutions be promoted by regulators and that entry hurdles be lowered without sacrificing a stringent fit-and-proper test for new entrants. The IMF noted that promoting more competition among financial institutions would result in a greater supply of financial services at lower intermediation costs, especially for small and medium enterprises and lower-income households.
- 4.8.3 Given the commitments that South Africa made as a G20 member country in respect of compliance with FSAP recommendations, it was necessary to, among other things, initiate processes to address identified shortcomings as well as to stimulate competition. This review is the main initiative aimed at addressing the identified shortcomings.

4.9 World Bank

- 4.9.1 The General Principles for International Remittance Services (General Principles) issued by the World Bank and the CPML, which provide best practices and guidelines for efficient remittance markets, have been endorsed by various international organisations, including the G20. In May 2014, a comprehensive review of the South African remittance market was conducted by the World Bank.
- 4.9.2 The report with outcomes on the review was finalised in August 2015. The report identified key actions that could lead to the enhanced safety and efficiency of remittance transactions to and from South Africa, and deliver other benefits associated with the implementation of the General Principles. These include the development of a consumer protection framework, financial literacy strategies, development of governance and risk management frameworks, promotion of competition, interoperability, and access in the remittance industry.
- 4.9.3 The increased focus on the development of retail payment systems as well as the need for increased financial inclusion, access to the payment system and competition necessitated a review of the current payments legislative framework to ensure appropriate alignment with general principles.

4.10 Review of the effectiveness of the PSMB model and PASA

- 4.10.1 Since the establishment of the Payments Association of South Africa (PASA) in 1996 and its subsequent recognition in terms of the NPS Act, the NPSD has exercised oversight responsibilities over PASA as provided for in section 3 of the NPS Act. Recent developments in the global and domestic payments landscape have, however, necessitated a review into the effectiveness of the PSMB model. These include issues identified in the NPSD's ongoing oversight over the affairs of PASA as well as various concerns or issues raised by payments industry stakeholders in respect of the current PASA model.

- 4.10.2 The NPSD's decision to initiate the PASA review process commenced in January 2015 with a payments industry-wide survey on the effectiveness of PASA. The survey was aimed at gathering necessary information and identifying the shortcomings of PASA as well as highlighting areas of concern. The scope of the survey included gathering information on PASA's:
- mandate and strategy;
 - governance structure;
 - regulatory model; and
 - membership.

4.10.3 Following the above survey and consideration of the comments/recommendations received, in October 2015 the NPSD published a consultation paper based on its analysis of the responses and its own insights for comment. The final report¹¹ was published in July 2016 with 19 recommendations on how to improve PASA's effectiveness. A process is underway to implement the recommendations of the final report. The first stage involved the development of relevant proposals in respect of the recommendations mentioned above on how to improve the effectiveness of PASA. The second stage involved the broader review of the PSMB model to establish its validity in the current and future payments environment. The outcome of both processes is addressed in paragraph 12.9.

11 [https://www.resbank.co.za/RegulationAndSupervision/NationalPaymentSystem\(NPS\)/Documents/Oversight/PASA%20Report.pdf](https://www.resbank.co.za/RegulationAndSupervision/NationalPaymentSystem(NPS)/Documents/Oversight/PASA%20Report.pdf)

4.11 2008 Competition Commission Banking Enquiry

4.11.1 The 2008 Banking Enquiry undertaken by the Competition Commission also made a number of recommendations specifically relating to poor practices in the NPS,¹² and recommended that access to the NPS should be given to non-bank providers of payment services, and that non-bank financial institutions and non-clearing banks should also be permitted to clear and settle in the payments system. While most recommendations have since been actioned, the enquiry highlighted the need for better oversight of all aspects of the NPS, including the ultimate impact on customers.

12 *Banking Enquiry: Report to the Competition Commissioner by the Enquiry Panel – Executive Overview*, June 2008 available at <http://www.compcom.co.za/banking-enquiry/>

4.12 Vision 2025

4.12.1 In March 2018 the NPSD published a seven-year roadmap for the NPS titled *The National Payment System Framework and Strategy Vision 2025*.¹³ The main objective of the document is to envision a future payments landscape which includes a modernised NPS. Similar to previous editions, the Vision 2025 document provides a directional framework and highlights the major developments anticipated or desired by the NPSD and the wider payments community.

13 [https://www.resbank.co.za/RegulationAndSupervision/NationalPaymentSystem\(NPS\)/Documents/Overview/Vision%202025.pdf](https://www.resbank.co.za/RegulationAndSupervision/NationalPaymentSystem(NPS)/Documents/Overview/Vision%202025.pdf)

4.12.2 The focus goals are broader than just payment infrastructure development and include strategic goals aimed at enhancing the regulatory and oversight framework, transparency and public accountability, financial stability and security, competition and innovation, cost-effectiveness, interoperability, flexibility and adaptability, regional integration, and financial inclusion. The NPS Act needs to be flexible and enable the achievement of these goals.

4.13 Stakeholder proposals and other developments

4.13.1 To initiate the review process, the NPSD sought submissions from the payments stakeholders on the required amendments to the NPS Act. The stakeholders recommended the following amendments for inclusion into the NPS Act: policy matters relating to the objectives of the NPS Act;

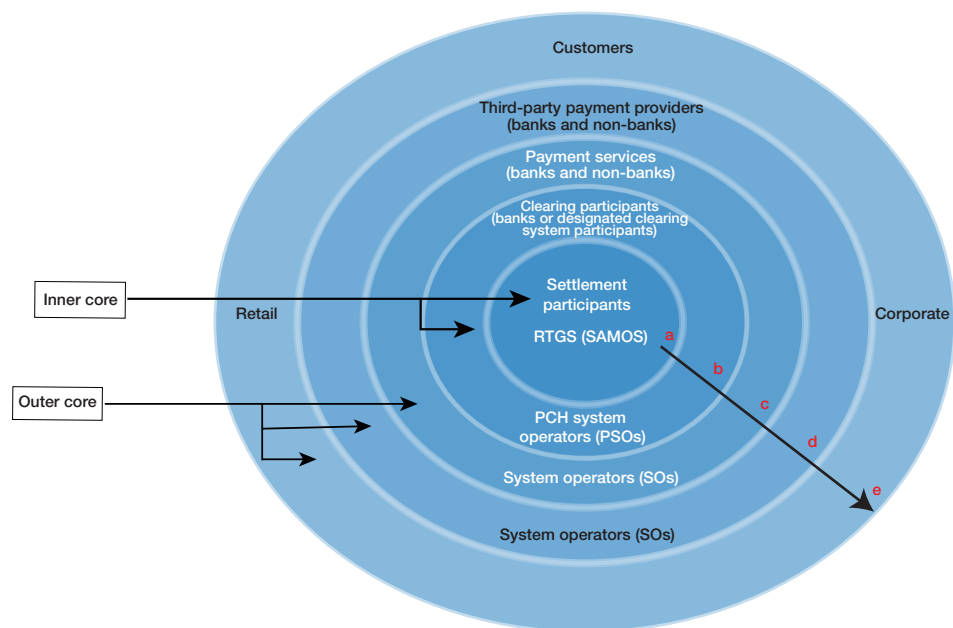
overarching regulatory principles; the adoption of the PFMLs; SARB versus PSMB mandate clarification; harmonisation with other relevant domestic legislation (e.g. FSR Act); the future role of the PSMB; and licensing and enforcement issues.

4.13.2 The NPSD has also been monitoring regulatory developments in other jurisdictions and has identified matters that need to be incorporated into South African law to make it more effective and resilient.

5. Overview of the current payments industry

5.1 The NPS is comprised of a series of layers of participants, systems, operators, providers and products, as depicted by Figure 1 below:

Figure 1: South African NPS Industry



Source: Payments Association of South Africa

5.2 The South African NPS industry diagram depicts the following:

- a. Settlement banks are in the inner core of the NPS and their respective payment obligations are settled through the South African Multiple Options Settlement (SAMOS) system.
- b. The second layer consists of banks or designated clearing system participants. The clearing of payment instructions between these participants in respect of the various payment streams occurs through authorised payment clearing house system operators (PCH SOs). At present, there are four authorised PCH SOs, namely Strate, BankservAfrica, Visa and MasterCard. The clearing participants are directly regulated and managed by PASA in terms of PASA rules. PCH SOs are also authorised by PASA with no further regulatory or supervisory responsibility.
- c. The third layer consists of providers of payment services, either directly by a clearing participant or by means of a system operator (SO). SOs

may provide payment services to banks, mutual banks, registered branches of foreign banks, cooperative banks and designated clearing service providers; beneficiary service providers (BSPs); payer service providers; and clients of banks.

- d. The fourth layer consists of third-party payment providers (TPPPs), that is, BSPs and payer service providers that accept money or the proceeds of payment instructions from, or effect payments on behalf of their clients to, two or more payers/beneficiaries.
- e. The fifth layer consists of consumers, corporate customers of TPPPs and other providers of payment services.¹⁴

14 <http://www.pasa.org.za/national-payment-system/key-role-players>

5.3 In addition to the participants and systems depicted in Figure 1, the NPS also comprises the following:

5.3.1 National Payment System Department (NPSD)

The SARB's NPSD is the regulator, supervisor and overseer of the NPS. The NPSD is also the operator of the settlement systems, namely SAMOS and the SADC Integrated Regional Settlement System (SIRESS).

5.3.2 Payments Association of South Africa (PASA)

Included within the scope of domestic regulation is PASA – the PSMB recognised in the NPS Act that performs the role of a self-regulatory organisation (SRO) responsible for regulating, organising and managing its members in the clearing environment.

5.3.3 Regional settlement system

SADC has developed and extended a regional settlement system called SIRESS to most SADC countries. SIRESS provides a cross-border settlement service for SADC countries. The service is available to banks that are participants in their respective domestic payment systems. The NPSD is the lead overseer of SIRESS and has concluded a cooperative oversight agreement with other SADC central banks for purposes of SIRESS oversight.

5.3.4 International settlement system

The South African rand was officially accepted as a CLS currency on 6 December 2004. CLS uses a unique combination of payment-versus-payment settlement over CLS central bank accounts, real-time gross settlement (RTGS) systems and multilateral payment netting supported by a robust and resilient infrastructure. The NPSD participates in the cooperative oversight of CLS. The lead regulator of CLS is the United States Federal Reserve Board.

5.3.5 Critical service providers

Critical service providers, such as the Society for Worldwide Interbank Financial Telecommunication (SWIFT) that provide secure financial messaging services, will increasingly fall within the domain of oversight where participation and contributions are required.

5.3.6 Payment streams

The various payment streams that currently fall within the scope of the NPSD and PASA include real time line (RTL), code line clearing (CLC) (cheque),

electronic funds transfer (EFT) credit and debit, Saswitch (automated teller machines (ATMs)), debit card, credit card, cash, American Express, Diners Club, fleet card, authenticated early debit order (AEDO), non authenticated early debit order (NAEDO), real time clearing (RTC), derivatives, equities, money markets, and bonds. While the payment streams reflect the type of payment instruments cleared and settled, a payment system is defined in the NPS Act as a “system that enables payments to be effected or facilitates the circulation of money and includes any instruments and procedures that relate to the system.”¹⁵

5.3.7 Payment instruments and products

South Africans use various payment instruments to initiate the transfer of claims between them after having used the instruments to purchase goods and services, to make financial investments or to transfer funds from one party to another. These payment instruments include cash, cheques, debit and credit cards, and mechanisms to trigger EFTs. Non-cash payment instruments facilitate the movement of a claim on a financial institution such as a bank of the payer to the bank of the beneficiary, and the financial institutions involved need arrangements to transfer such claims, including bank-to-bank transfers.

6. Overview of the current NPS legislative and regulatory architecture and framework

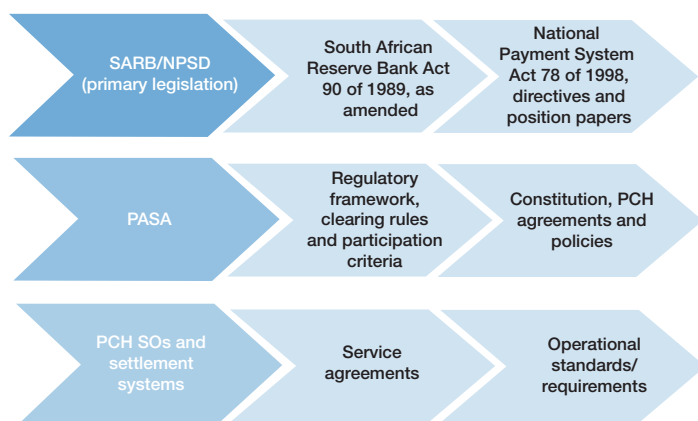
- 6.1 The SARB Act authorises the SARB to “perform such functions, implement such rules and procedures and, in general, take such steps as may be necessary to establish, conduct, monitor, regulate and supervise payment, clearing or settlement systems.” Aligned to this mandate is the enabling legislation, the NPS Act, which aims to “provide for the management, administration, operation, regulation and supervision of the payment, clearing and settlement systems in the Republic of South Africa; and to provide for connected matters.” The authority to perform these functions within the SARB has been assigned to the NPSD.
- 6.2 The NPS Act provides the NPSD with the legislative authority to issue directives, after consultation with the PSMB, to any person regarding a payment system or the application of the provisions of the NPS Act. The directives are gazetted and have a binding effect on the persons to whom they are applicable. The directives also enable the NPSD to induce change and enforce corrective action for non-compliance with the NPS Act, decisions or orders of the NPSD, or policies in the NPS.
- 6.3 The NPSD also issues non-binding (yet morally persuasive) position and information papers (or ‘soft standards’). Position papers are published in order to state the NPSD’s position in respect of specific payment system issues. These documents normally contain approaches, procedures and policy matters, which are applicable at a particular time.
- 6.4 In terms of the NPS Act, the NPSD may recognise a PSMB, established with the objectives of organising, managing and regulating the participation of its members¹⁶ in the payment system. PASA is recognised by the NPSD in this regard. PASA sets the rules, regulatory framework, agreements and policies with which its members are required to comply. PASA also authorises the participation of members in PASA, and supports the NPSD in its role as

¹⁶ Only the SARB, a commercial bank, mutual bank, cooperative bank, branch of a foreign institution and a designated clearing system participant may be members of a payment system management body.

the overseer of the payment system by ensuring compliance and imposing penalties and sanctions against non-compliant members in relation to PASA rules.

- 6.5 The SAMOS system, SIRESS, PCH SO and the outer core level (see Figure 1) participants enter into legally binding service level agreements for the provision of services or systems.
- 6.6 The current legal foundation of the NPS is outlined in Figure 2:

Figure 2: South African NPS legal foundation



7. Regulatory effectiveness

In assessing what works effectively in the current framework versus what does not, it is important to consider how effectively the NPS Act has achieved its regulatory objectives. The following were identified as critical measures used to evaluate the application of the NPS Act as well as the extent to which the NPS has achieved its objectives as set out in the NPS Act:

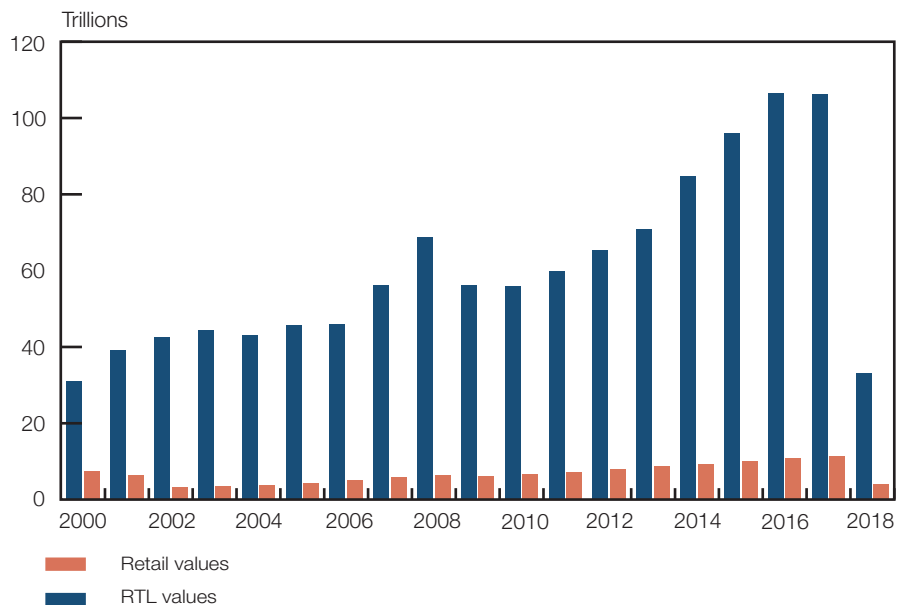
- a. extent to which the NPS Act is delivering on its objectives;
- b. level of coverage of the payment space;
- c. extent to which the NPS Act meets international standards;
- d. effectiveness and accountability of the NPSD;
- e. effectiveness of the PSMB;
- f. proportionality and efficiency of the regulatory framework;
- g. flexibility of the regulatory framework;
- h. timeliness and responsiveness of the regulatory framework;
- i. compliance and enforcement mechanisms; and
- j. redress mechanisms.

7.2 Extent to which the NPS Act is delivering on its objectives

- 7.2.1 The objectives of the NPS Act, although not explicitly provided for, are to promote the safety and efficiency of the NPS. The institutional framework established by the NPS Act has greatly contributed to meeting the objectives of the NPS Act. The NPSD has effectively exercised oversight over the NPS as evidenced by the safety and stability of the NPS and

operational efficiency of SAMOS. The availability of the SAMOS system averages over 98% per month. The retail values settled in SAMOS increased significantly from R7 trillion in 2000 to R11 trillion in 2017, and the RTL values increased from R31 trillion in 2000 to R106 trillion in 2017, as represented in Figure 3.

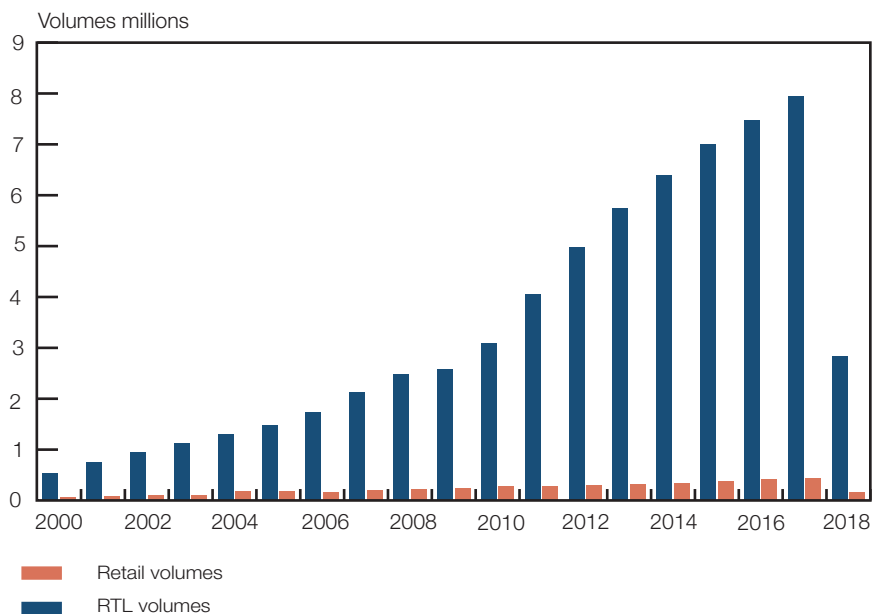
Figure 3: Values settled in the SAMOS system



1. RTL is the high-value, low-volume interbank settlement facility that is provided to the settlement banks in SAMOS to effect immediate, final and irrevocable payments.
2. Retail includes all payment streams listed in paragraph 5.3.6 above.

7.2.2 The retail volumes settled in the SAMOS system increased significantly from 76 000 in 2000 to 451 000 in 2017, and the RTL volumes increased from 543 000 in 2000 to 8 million in 2017, as represented in Figure 4 below.

Figure 4: Volumes settled in the SAMOS system



1. RTL is the high-value, low-volume interbank settlement facility that is provided to the settlement banks in SAMOS to effect immediate, final and irrevocable payments.
2. Retail includes all payment streams listed in paragraph 5.3.6 above.

- 7.2.3 Awareness and enforcement of significant payment changes were effected, including the inclusion of the rand as a CLS currency; the strengthening of the regulatory framework, such as the collection framework; the enhancement of financial integrity through the publication of the anti-money laundering and combating the financing of terrorism directive; and the inclusion of non-bank participants in the NPS (i.e. designated clearing participants, TPPPs and SOs).
- 7.2.4 PASA has also contributed to the effective regulation of the NPS as the recognised PSMB. Over the years, PASA assisted the SARB in developing the regulatory framework and led complex payment matters in relation to new payment instruments, services and incident management. As a result, PASA has built the necessary expertise, knowledge and ability to effectively implement and conduct efficient and cost-effective regulatory programmes.
- 7.2.5 In contributing to the safety and efficiency of the NPS, PASA has, over the years, demonstrated its success in several projects, for example:
- a. implementation of the Early Debit Order Project;
 - b. awareness and enforcement of the Payment Card Industry Data Security Standards;
 - c. addressing the growth of 'card not present' fraud (e.g. enforcement of 3D-Secure);
 - d. introduction of new payment systems (i.e. RTC);
 - e. capacity-building initiatives such as the PASA foundational course and Unisa module on payments;
 - f. development of a robust PCH regulatory framework (e.g. PCH constructs, PCH rules, clearing agreements); and
 - g. development of an internationally accepted biometrics standard.
- 7.2.6 As an entity operating in a dynamic industry with divergent membership and stakeholders with different commercial interests, PASA in its current form has not been without challenges. The NPSD, through its ongoing oversight of the NPS and the PASA effectiveness review survey referred to in paragraph 4.10 above, identified shortcomings with the current governance and institutional structure as well as the regulatory framework of PASA. In particular, the shortcomings were related to the restrictive mandate and membership of PASA, which limited the accessibility of PASA and the broader NPS for non-banks; the lack of independence of the governing body of PASA; and the lack of objectivity and independence in the compliance and enforcement framework of PASA.
- 7.2.7 As required by the NPSD, steps are being taken by PASA to address these shortcomings. However, full implementation of the PASA review recommendations will require legislative changes and a broader review of the PSMB model. The review of the NPS Act seeks to address some of the identified issues by proposing a revised mandate and regulatory framework for PSMBs and by ensuring activity-based regulation aimed at enhancing the access of banks and non-banks to the NPS.

7.3 Level of coverage of the payment space

- 7.3.1 For a long time, participation in the NPS was dominated by banks. Non-banks participated indirectly in the NPS through commercial arrangements with banks. From 2004, non-banks' participation in the NPS was greatly enhanced in the outer core of the NPS with the inclusion of non-banks

in the clearing environment and payment services. Since 2004, over 150 SOs have been authorised and over 100 TPPPs have been registered with PASA. However, non-bank participation in the inner-core (i.e. clearing and settlement) has been less progressive. Only two non-bank entities have been designated as clearing participants. This can mainly be attributed to the legal requirement for non-banks to be sponsored into settlement by banks and that only banks can settle in the SAMOS system.

- 7.3.2 Notwithstanding the enhanced participation of non-banks in the outer core, the type and scope of services included in the NPS Act extend to SO and TPPP services only. Payment services where money is 'not due' are excluded from the NPS Act. Participants wishing to provide other payment services involving the pooling of funds from consumers are required to partner with banks. As a result, criticism has been levelled against the NPS Act for impeding access and competition in the NPS, thereby stifling innovation.
- 7.3.3 The limited type and scope of services has also negatively impacted product-level innovation, resulting in service offerings that were directly linked to a bank account (e.g. EFTs, cheques and cards). E-money is an example of a product that can currently only be issued by a bank. Further, with the increased emergence of closed-loop payment systems, interoperability is far from being achieved. Table 1 below outlines payment system-related information collected from SAMOS participants through a Payment Information Return (PAYIR) system.

Table 1: Infrastructure access points and payment instruments

| | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | Growth 2009 to 2016 |
|---|------------|------------|------------|------------|------------|------------|------------|---------------------------|
| | Number | | | | | | | Per cent |
| No. of ATMs | 23 259 | 24 063 | 22 901 | 26 133 | 27 774 | 28 906 | 29 643 | 27 |
| No. of mini-ATMs ¹ | 3 385 | 2 335 | 2 475 | 2 706 | 2 672 | 2 004 | 2 000 | -41 |
| No. of self-service device terminals (SSTs) ² | 1 562 | 1 645 | 1 722 | 1 720 | 1 386 | 1 022 | 1 065 | -32 |
| No. of point-of-sale devices ³ ... | 273 798 | 277 478 | 254 368 | 308 824 | 393 883 | 394 309 | 402 670 | 47 |
| No. of cards | 57 827 824 | 62 211 297 | 44 796 838 | 45 010 160 | 61 303 189 | 50 236 849 | 50 935 160 | -12 |

1. A mini-ATM issues a paper voucher that may be encashed or used for the purchase of goods at a specific merchant.

2. SSTs have the same electronic features and functions as ATMs, except that they do not dispense cash.

3. These are only bank-owned devices.

Figures as at 31 December for each period (only available from 2010)

- 7.3.4 Conduct regulation is another area that is not explicitly provided for in the NPS Act. As a result, payments regulation is under constant scrutiny for not affording the necessary protection to vulnerable consumers.

7.4 Extent to which the NPS Act meets international standards

- 7.4.1 The NPS Act came into effect in 1998 prior to the 2001 CPSS Core Principles for Systemically Important Payment Systems and the subsequent PFMI. While certain changes were effected to the NPS Act to address specific shortcomings and limitations, certain definitions and provisions are not aligned with best international standards (e.g. the definition of 'clearing')

and ‘payment clearing house’). Further, other internationally accepted definitions such as oversight and the FMI framework are not included in the NPS Act. In this regard, the NPS Act falls short of compliance with international standards.

7.5 Accountability of the NPSD and PSMB

7.5.1 The NPSD, as the regulator of the NPS, is accountable to the SARB’s Governors’ Executive Committee (GEC) and the Minister of Finance for the effective administration of the NPS Act. The operations of the NPSD are subject to the NPS Act and SARB Act, and the NPSD complies with both Acts. The PSMB is accountable to the NPSD for the effective performance of its functions as set out in the NPS Act. The NPS Act empowers the NPSD to withdraw the recognition of the PSMB should the PSMB fail to effectively perform its functions. The NPSD has regular engagements with the GEC and National Treasury on policy and other NPS-related matters, and with the PSMB on payments-related matters.

7.6 Proportionality and efficiency of the regulatory framework

7.6.1 In light of the scope and systemic nature of the NPS, the NPS Act seems to be proportional to the risks it addresses as well as other broader economic or social needs. The NPSD has engaged with the industry to ensure that the interchange calculation in the industry is fair and transparent in order to enhance interoperability in the NPS and efficiencies to users and customers. While the NPSD supports the provision of payment services to customers at the lowest cost, this has not been the major focus of the NPSD under the current regulatory framework. However, it is envisaged that the FSCA will address this issue now that the FSR Act has become effective.

7.6.2 The PSMB model is a cost-efficient model that utilises available regulatory resources optimally. Compliance costs are also fairly reasonable. Fees and levies charged by the PSMB are calculated on volumes and values as well as time spent on regulation. To date, no industry participants have refused to pay fees or argued that fees are not commensurate with the regulatory functions of the PSMB. However, the PASA effectiveness review process raised questions with regard to the adequacy of the funding for PASA.

7.6.3 In addition, concerns have been raised with regard to the cost of the RTC payment stream to consumers as well as the broader payments value chain. A process has been implemented to address these cost inefficiencies in this system.

7.6.4 The SARB has also commissioned a research project on payment fees to obtain more insight on end-to-end fees charged to consumers, merchants and users, and for inter-bank transfers. This is aimed at informing the necessary regulatory response, which may include enhancing transparency through disclosure, promoting access, financial inclusion and consumer protection.

7.7 Flexibility and simplicity of the regulatory framework

7.7.1 The NPS Act is designed as an enabling legislation. The subordinate legislative authority afforded to the NPSD (in the form of directives) and the rule-making authority afforded to the PSMB is sufficiently flexible and simple to accommodate certain changes in the financial system while still achieving its objectives. However, the NPS Act revision is necessary to make the NPS Act more flexible and enabling to address new and emerging payment

methods and risks, and to adequately regulate the less regulated aspects of the NPS.

7.8 Timeliness and responsiveness of the regulatory framework

7.8.1 The subordinate legislative authority afforded to the NPSD and the rule-making authority afforded to the PSMB allows for a timely and responsive reaction to the rapid pace and complexity of innovation in the financial sector. The revised NPS Act should continue to support this regulatory architecture. However, more flexibility of the NPS Act is required to create an environment that will swiftly respond to innovation without compromising the safety, stability and efficiency of the NPS.

7.9 Compliance and enforcement mechanisms

7.9.1 The NPS Act does not provide the NPSD with effective compliance and enforcement mechanisms. While the NPS Act provides for criminal and civil enforcement mechanisms, comprehensive administrative powers are not provided for. Although the NPSD may issue directives, it does not have specific powers to impose financial penalties. Other compliance or enforcement mechanisms available to the NPSD include the power to withdraw licences/recognition, apply for curatorship, apply for other court orders, and prescribe matters.

7.9.2 The NPSD has, over the years, applied moral suasion in ensuring compliance with the NPS Act. Although this has been effective in correcting behaviour in the NPS, stringent administrative powers are required. This review seeks, among other things, to codify compliance and enforcement matters in order to provide the NPSD with comprehensive administrative sanctions, in addition to the current powers in the NPS Act.

7.10 Effective dispute resolution

7.10.1 Decisions of the NPSD and PSMB are subject to the Promotion of Administrative Justice Act 3 of 2000. The decisions of the NPSD may also be taken on appeal/review to the High Court, and the decisions of the PSMB are also, or in addition, subject to appeal by the NPSD. Administrative penalties imposed by the PSMB are also appealable to the High Court. There is, however, no independent tribunal to hear appeals from the affected participants or PSMB. The NPS Act review seeks to address this by providing a dispute resolution and an appeal mechanism.

8. Current PSMB model

8.1 The NPS Act makes provision for the PSMB model. Section 3 of the NPS Act authorises the NPSD to recognise a PSMB established with the objective of organising, managing and regulating the participation of its members in the payment system if the NPSD is satisfied that:

8.1.1 “the payment system management body, as constituted, fairly represents the interests of its members;

8.1.2 the deed of establishment or constitution, as the case may be, and the rules of the payment system management body, including the rules relating to admission as members of that body, are fair, equitable and transparent; and

8.1.3 the payment system management body will enable the Reserve Bank to adequately oversee the affairs of the payment system management body and its members and will assist the Reserve Bank in the discharge of the Reserve Bank’s responsibilities, specified in section 10(1)(c)(i) of the SARB



Act, regarding the monitoring, regulation and supervision of payment, clearing and settlement systems.”¹⁷

- 8.2 The PSMB mandate as currently defined in section 4(1) of the NPS Act is to organise, manage and regulate its members; provide a platform for the consideration of matters of policy and act as a medium of communication between its members and policymakers, regulatory bodies, and other specified public and private institutions; and to promote matters of interest to its members and foster cooperation between them.
- 8.3 In addition, the PSMB is empowered in terms of the NPS Act to:
- a. admit, regulate and control members and, with the NPSD’s approval, terminate membership;
 - b. establish committees, forums or bodies comprising its members;
 - c. recommend membership, including SO and PCH SO authorisation criteria for approval by the NPSD;
 - d. recommend clearing authorisation criteria for approval by the SARB, and authorise SOs and PCH SOs; and
 - e. register TPPPs.
- 8.4 The NPS Act restricts the membership of a PSMB to the SARB, a bank, a mutual bank, a cooperative bank or branch of a foreign institution, and a designated clearing system participant that complies with the entrance and other applicable requirements laid down in the rules of the PSMB. Except for designated clearing system participants that may be non-banks, the NPS Act excludes non-banks from the PSMB membership.
- 8.5 Where the SARB is no longer satisfied that the PSMB complies with the above-mentioned requirements, and after it has consulted with the members of the PSMB, the NPSD may withdraw its recognition of the PSMB.

9. Applicable international standards, principles and recommendations

- 9.1 In developing the regulatory and legislative framework, the NPSD endeavours to align the domestic framework with international best practices and standards. These include standards issued by the G20, FSB, CPMI, IOSCO, Financial Action Task Force (FATF) and International Organization for Standardization (ISO) as well as best practice recommendations from other jurisdictions, the World Bank, IMF and similar organisations. This is aimed at ensuring the development of a robust regulatory and legislative framework that is largely consistent with best international standards and practices.
- 9.2 However, the NPSD is equally mindful of the unique landscape, circumstances and challenges of South Africa as an emerging market economy, and ensures that these are taken into account in developing the NPS policy and regulatory framework.

10. Jurisdictional comparative analysis

- 10.1 The NPSD conducted an assessment of payments regulation, supervision and oversight in other comparable jurisdictions to determine how the South African regulatory framework equates. Box 1 provides a summary of the analysis.

Box 1: Summary of jurisdictional comparative analysis

United States

- The United States (US) Federal Reserve Board, as the supervisor and regulator of certain financial institutions, is the primary federal banking regulator for several payment, clearing and settlement systems. In addition, the Federal Reserve Board, by statute, supervises the Federal Reserve banks and their provision of payment and settlement services, such as Fedwire funds. The Federal Reserve Policy on Payment System Risk (PSR policy) addresses the risks that payment and settlement activities present to the US financial system and to the Federal Reserve banks. Through the PSR policy, the Federal Reserve Board establishes standards for financial system participants to reduce and control settlement and systemic risk arising in payment and settlement systems.
- The Federal Reserve Board is also responsible for the supervision of the Federal Reserve-operated financial markets utility (FMU) and other FMUs, pursuant to its general supervisory authority over the Federal Reserve banks on which it applies the Principles for Financial Market Infrastructures (PFMIs). It is the supervisory agency for CLS Bank, the Clearing House Interbank Payments System and the Clearing Payments Company. It also exercises oversight over the Fedwire Funds Service through the application of the PSR policy. Title VIII of the Dodd-Frank Act (DFA) strengthens the supervisory and regulatory framework related to payment, clearing and settlement systems in the US and gives the Federal Reserve Board additional authority to assess systemic risks arising from these systems. Section 805(a) of the DFA authorises the Federal Reserve Board to prescribe risk management standards governing the operations of FMUs that have been designated as systemically important.
- Regarding retail payments regulation and oversight, the US Federal Reserve has a more limited role. It has issued a limited set of regulations for retail payment systems but it does not oversee those systems. Nevertheless, it is worth noting that the US Federal Reserve itself is the operator of a major retail payment system (i.e. FedACH) and it also provides cheque clearing services.
- NACHA is a private rule-setting body for the Automated Clearing House (ACH) Network, FedACH, and the Electronic Payments Network. It does not operate a system. Rules are approved by members but the two ACH operators have to incorporate them into their agreements.

European Union

- The Eurosystem (comprising the European Central Bank (ECB) and national central banks) plays three complementary roles in payments: operator, overseer and catalyst. Its general objectives include (i) the smooth implementation of a single monetary policy; (ii) the maintenance of public confidence in the currency and financial stability; and (iii) the safety and efficiency of payments. The Eurosystem does not play a role in anti-money laundering and terrorist funding, data protection or consumer protection. It exercises oversight over payment systems, payment instruments/schemes, and critical service providers.
- The PFMIs have been adopted as the Eurosystem's oversight standards for all types of financial market infrastructures (FMIs). The ECB has issued regulations on oversight requirements for systemically important payment systems (SIPs) as well as oversight standards for non-systemically important retail payment systems and for retail payments instruments. The Eurosystem is currently conducting assessments on national and international card payment systems (Visa, MasterCard and America Express).
- The Eurosystem is revising its SIPS regulation which implements the PFMIs for SIPS in the euro area to substantially improve the mitigation of liquidity risk generated in deferred net settlement systems. The mitigation is to be achieved by ensuring effective liquidity risk mitigation for all settlement cycles from the moment a transfer order has been included in the calculation of net settlement positions and the position is visible to the receiving participant. The revised regulation will require SIPS to establish obligations which then trigger the covered requirements.
- Other amendments being introduced to the SIPS regulation include the implementation of the CPMI-IOSCO guidance on cyber-resilience and strengthening the powers of competent authorities (e.g. the right to conduct on-site inspections and to mandate an independent review on certain aspects of SIPS). To promote efficiency and innovation in financial markets in Europe, the Eurosystem has launched an investigation to identify how it can best support the emergence of instant payments. TARGET Instant Payment Settlement (TIPS) is a service that makes it possible to settle payments in central bank money in real time, around the clock, 365 days a year.

- The revised Payment Services Directive (PSD2) is now effective. It introduces new players, namely third-party payment providers aimed at enhancing competition. It is aimed at regulating payment services (i.e. in addition to payment systems and payment instruments, which are the responsibility of the Eurosystem). Each country has to designate a 'Competent Authority' for the prudential supervision of payment institutions and monitor compliance with business conduct rules, as transposed into national legislation.

United Kingdom

- The United Kingdom (UK) has adopted the Twin Peaks regulatory model. The Bank of England (BOE) is responsible for monetary and financial stability in the UK, while the Prudential Authority (PA UK) is responsible for microprudential regulation; the Financial Conduct Authority is responsible for protecting consumers and market integrity, while the Payment System Regulator (PSR) is responsible for competition and innovation in the payments industry. The BOE supervises FMIs to ensure that FMIs are managed in a manner that contributes to the delivery of the financial stability objective. It applies the PFMI framework to UK-recognised payment systems. The BOE authorised SIPSs as FMIs and supervises FMIs' compliance with standards. Although the PFMIs have not been translated into law, they are acknowledged as standards for recognised FMIs.
- The PSR regulates and supervises the conduct of members for consumer protection, and promotes market integrity through the regulation and supervision of payment systems, infrastructures and payment institutions/members. The PSR recognises and regulates non-SIPSs. Payments UK is a trade association. It used to have a quasi-regulatory role; however, this role was shifted to the PSR. The Minister of Finance designates payment systems. At present, there are eight designated payment systems, including SIPS, ACHs and payment card processing systems. E-money is currently open to banks; however, the BOE is considering opening it to non-banks.
- Key regulatory developments in the UK include the consolidation of retail payments into Bacs Payment Schemes Limited (Bacs) and the consolidation of wholesale high-value payments into the BOE. The UK's Payments Strategy Forum – a group of 22 payments industry stakeholders with bank, business, consumer and government representation – published its strategy for the UK payments industry in November 2016. The strategy proposed a range of measures, including significant changes to the UK's retail payments infrastructure and merging the three companies responsible for operating the UK's instant payments system, ACH and cheque clearing system. In November 2017 the high-value payment scheme was consolidated into the BOE. As a result of this change, Clearing House Automated Payment System (CHAPS) was derecognised as a recognised payment system operator under the Banking Act 2009. Responsibility for the operation of the CHAPS system now lies with the BOE. Further, non-banks are now allowed to settle in the BOE's real-time gross settlement (RTGS) system.

Canada

- The Bank of Canada (BOC) is responsible for the reduction of systemic risk and payment risk. It also has a mandate for the safety and efficiency of the payment system. The Governor of the BOC has the power to designate FMIs, with the Minister of Finance's approval. The BOC oversees the system and not the operator. The Minister is responsible for oversight of Payments Canada, which operates two payment systems and makes rules for the systems that it operates. It also makes by-laws which are reviewed by the BOC and approved by the Minister of Finance. Final settlement in Canada happens in the books of the BOC.
- The PFMIs are applied as standards for SIPSs and prominent payment systems (PPSs). Application of the PFMIs differs slightly, based on the Risk Management Standards for SIPS and the Risk Management Standards for PPSs. While the BOC designates PPSs and FMIs, the BOC and Payments Canada are currently undertaking a project aimed at modernising the wholesale and retail payments systems, as these have become outdated and non-adaptive to accommodating access. Other pillars of the project include the need to align with ISO 20022 and modernising the rules framework.
- The Canadian authorities are also working together to develop an oversight framework for Canada's national retail payment systems. These are relatively small systems that have not been designated for oversight by the BOC. A new retail payments oversight framework was issued for comment in October 2017.
- The Payment Clearing and Settlement Act was recently amended to strengthen the BOC's ability to identify and respond to risks of an FMI in a proactive and timely manner. Two main changes were made to support this objective: (i) broadening the Governor's power to issue a directive; and (ii) explicitly allowing the Governor to approve or disapprove significant changes made by a designated FMI.

11. Key policy developments in the NPS

11.1 The NPSD, in collaboration with PASA (as the PSMB) and the payments industry, continually issues relevant measures to strengthen the NPS regulatory framework and regularise industry conduct. The NPS Act review should take these initiatives into account and provide supportive enabling provisions. The key initiatives underway are discussed below.

11.2 PASA review implementation plan

11.2.1 A review into the effectiveness of PASA was launched in January 2015. The review was initiated through a stakeholder survey, which culminated in the 'PASA/Payment System Management Body (PSMB) Model Review Consultation Paper' (consultation paper), published in October 2015. The consultation paper was followed by the publication, of the 'Final Report on the Review of the Effectiveness of PASA' in July 2016 (final report). The final report contained recommendations for execution/implementation relating to the governance, mandate, membership and regulatory framework of PASA.

11.2.2 Subsequent to the publication of the final report, the PASA Review Implementation Project was initiated to implement the recommendations of the final report and included the broader review of the PSMB model. It is envisaged that the implementation process will be completed by the end of 2019. The proposals relating to the future regulatory model have been included in paragraph 12.9 below.

11.3 Domestic remittances

11.3.1 In 2011 the Minister of Finance announced that measures would be taken to reduce the costs of cross-border remittances. A new framework was established for this through the dispensation provided by the SARB's Financial Surveillance Department. The Exchange Control Rulings were amended by eliminating the requirement for money transfer operators (MTOs) to partner with existing Authorised Dealers. This permitted MTOs to operate independently and encouraged greater competition relating to cross-border remittances.

11.3.2 For domestic remittances (i.e. remittances within South Africa) the current policy is that domestic MTOs are required to partner with registered banks to be able to provide such services. The activity of domestic remittances is deemed a deposit-taking activity as it involves the pooling of funds from the public, which element falls within the realm of the Banks Act 94 of 1990 (Banks Act).

11.3.3 In terms of section 7 of the NPS Act, a person may, as a regular feature of that person's business, accept money or payment instructions from any other person for purposes of making a payment on behalf of that person to a third person to whom that payment is due. This does not provide sufficient regulatory power to address domestic remittances or money transfers provided by MTOs, as most remittance payments to third parties are not always classified as 'payments due'.

11.3.4 In view of the above, the players in this industry have cited these regulatory restrictions as one of the main contributors to the collapse of mobile money products such as M-Pesa and MTN Mobile products in South Africa. In this regard, the NPSD has, in the interest of deepening financial inclusion, competition and improving access to the NPS for non-banks, taken a decision to review the regulatory policy framework for domestic remittances.

- 11.3.5 A payment services engagement paper has been developed in consultation with the FSCA to review the current payment services landscape and propose possible regulatory options. The options explored include an exemption in the Banks Act from the definition of deposit taking or the business of a bank for the pooling of funds for purposes of providing domestic remittances, as well as the development of a regulatory framework for the domestic remittance activity and for all domestic MTOs. This should enable non-bank MTOs to operate independently from banks and allow for fair, non-discriminatory entry into the NPS, with improved efficiencies and increased competition. Section 7 of the NPS Act will also require an amendment to broaden its scope to include payment services where money is not 'due'.
- 11.3.6 Discussions are ongoing between the NPSD and the PA on the possible exemption, structure and extent of the regulatory framework. A detailed policy paper is also being developed to clarify the key policy drivers and objectives of domestic remittances. It is envisaged that an enabling provision will be included in the NPS Act to allow the provision of domestic remittances by non-banks independently of banks. The detailed framework will then be issued as standards in terms of the NPS Act.

11.4 Payroll deductions

- 11.4.1 The NPSD has become aware of the growing practice of voluntary payroll deductions, where parties (third parties and employers) use the payroll system as a general purpose payment system or collection mechanism, instead of using the available NPS collection systems (i.e. early debit order (EDO) or EFT). The NPSD has identified potential policy issues that motivate the review of payroll deductions, such as preference and the ineffectiveness of the debit collection system. In July 2016, the NPSD issued a payroll deductions notice to the industry highlighting the potential negative connotation of non-statutory payroll deductions and advising the industry of the decision taken by both National Treasury and the NPSD to review the voluntary payroll deductions system.
- 11.4.2 The objective of the initiative is to develop a position on voluntary payroll deductions with justifiable principles. The NPSD met with other affected regulators and government departments to discuss the various policy options for payroll deductions. These include National Treasury, the FSCA, National Credit Regulator, Department of Trade and Industry, Department of Labour and the National Consumer Commissioner. As a result, several regulators and government representatives were selected to form a working group to deliberate and formulate a policy option with justifiable principles. This led to the development of a joint consultation paper by the SARB and National Treasury which was published for comment in March 2018. The outcome of the consultation process will inform any amendments to the relevant existing laws currently administered by the respective regulators or government departments. The NPS Act should therefore enable the intervention of the NPSD in the payroll deductions system and similar payment systems, where necessary.

11.5 Sort-at-source

- 11.5.1 In March 2017 the NPSD issued a notice to all stakeholders in the NPS on sort-at-source. The sort-at-source notice was issued in response to the practice of users bypassing the central clearing system and submitting files

directly to the paying banks, thus processing these transactions as 'on-us' transactions. This practice negatively impacts public policy objectives and principles. The notice served to advise stakeholders to refrain from the practice of sort-at-source, specifically with the aim of bypassing the clearing system. In the notice, the SARB stated that it was reviewing and developing a comprehensive policy position which would provide clear scope and guidance. This position should be clearly articulated in the NPS Act, through the review of the definition of clearing.

11.6 Domestic issuing and acquiring

11.6.1 Instances exist where card transactions are concluded domestically between local buyers and sellers, but the services to effect the payment, such as the issuing and/or acquiring and settlement of these card transactions, are provided by foreign entities in foreign jurisdictions. Although the transactions occur domestically as a result of the foreign issuing or acquiring of entities, such transactions are processed as international/cross-border transactions. This results in the circumvention of the domestic legislative and regulatory framework.

11.6.2 The NPSD took a decision to address these circumventions through the issuance of a directive prohibiting the acquiring of domestic card transactions or domestic merchant transactions by foreign acquirers. All domestic card transactions are to be acquired domestically and be subjected to South African legislation, rules and standards in terms of clearing, settlement and processing. The directive will be published by the end of 2018. Once finalised, the directive will be published and gazetted, and assume the status of subordinate legislation.

11.7 Authenticated collections

11.7.1 The Authenticated Collections (AC) Project was prompted by a review of the early debit order collection environment as a result of increased complaints by customers regarding unauthorised debits from their bank accounts as well as an increase in the number of disputes on early debit orders. This led to growing mistrust in the existing EDO systems, namely the AEDO and NAEDO systems.

11.7.2 The main objective of AC is to protect both the payers (customers) and users (collectors) of the debit order collection systems by strengthening debit order mandates and ensuring a secure debit is approved and authenticated by the paying customers upfront for future-dated early debit orders.

11.7.3 The approach taken was to address this behaviour through the issuance of a directive that will require all participants involved in the collection of payment instructions in the EDO environment to design, develop and fully implement AC through a phased approach by 31 October 2019. PASA will be required to monitor compliance by the participants with the NPSD's approved implementation plan, and apply an appropriate enforcement action through its existing compliance and enforcement framework.

11.7.4 The directive for conduct within the NPS in respect of the collection of payment instructions for ACs was issued and published in May 2017. The SARB is closely monitoring the project to track the implementation and monitor compliance with the directive.

11.8 Interchange determination

- 11.8.1 Interchange is a critical enabler of the payment infrastructure and the interoperability within the NPS. South African banks have been charging each other interchange fees for several years, but it was uncertain how these rates were determined. In 2006, the Competition Commission of South Africa commissioned a banking enquiry to review the conduct of retail banking in South Africa. One of the recommendations of this inquiry was to provide an independent, objective and transparent regulatory process for determining interchange in the payment streams in the South African NPS. As a neutral and trusted party, the NPSD assumed the responsibility to facilitate the determination of interchange rates for the various payment streams in the NPS.
- 11.8.2 The NPSD launched the Interchange Determination Project (IDP) in 2011 to assess the relevance of interchange for specific payment streams in the South African NPS. Since then, three phases of the IDP have been completed during which an IDP model was built to determine the interchange rates for ATMs and card transactions, and a secure web browser – known as the PAYIR system – used to collect data was developed and implemented. Every year, the NPSD collects interchange and other payment system-related data from the participating banks via the PAYIR system. The data is used, among other things, to calculate the interchange rates.
- 11.8.3 The first interchange rates for the ATM and card payment streams were determined and published on the SARB's website. The interchange rates for ATMs were implemented in the NPS on 1 April 2014, while the card interchange rates were implemented on 17 March 2015. From 2013 to 2015, there were no changes in the rates as the implemented rates remained relevant. In 2016 the rates for ATMs and cashback at point-of-sale devices remained unchanged. However, in the card payment stream, rates for card-present transactions remained unchanged while that of the card-not-present transactions were changed and implemented on 14 November 2016. This change was implemented to encourage secured online payment activities.
- 11.8.4 Future activities of the IDP include the issuing of the interchange position paper, and the review and determination of interchange rates for other retail payment streams which include RTC, EFT credits and EFT debits.

11.9 Virtual currencies/distributed ledger technology/fintech

- 11.9.1 The NPSD participates in ongoing engagements between National Treasury, the FIC, FSCA, South African Revenue Service (SARS) and other departments in the SARB on the appropriate regulatory approach to virtual currencies (VC). During September 2014, National Treasury, the FIC, FSCA, SARB and SARS together issued an investor and consumer alert notice highlighting the risks associated with VCs. As a subset of VCs, digital currencies are also covered in the notice.
- 11.9.2 Furthermore, the NPSD participated and contributed to the development and issuance of the SARB's position paper on VCs. The position paper was issued in December 2014 and mainly highlights several risks associated with the VC landscape, particularly digital currencies, and provides a cautionary note to users thereof. The position paper further highlights that, given the market size of VCs to date, VCs pose no significant risks to financial stability, price stability or the NPS. However, the continuous monitoring of VCs was

deemed necessary and the SARB reserved the right to change its position should the situation warrant regulatory intervention. Accordingly, the NPSD continually monitors developments relating to VCs for this purpose as well as the potential impact on the NPS.

- 11.9.3 In March 2016, the SARB established an internal Virtual Currencies and Distributed Ledgers Working Group to research and review international and domestic regulatory, supervisory and technological opportunities as well as risks linked to financial stability. This was aimed at formulating policy responses pertaining to VCs and distributed ledger technology (DLT) from a central banking perspective.
- 11.9.4 The developments relating to VCs and DLTs occur under the umbrella of the broader fintech innovations. Fintech is defined by the FSB as “technologically enabled financial innovation that could result in new business models, applications, processes, or products with an associated material effect on financial markets and institutions and the provision of financial services”.
- 11.9.5 A Fintech Unit and related programme was established in July 2017 within the SARB to, among other things, monitor fintech-related developments and advise the SARB on the appropriate policy interventions to be taken in this regard.
- 11.10 Anti-money laundering and combating the financing of terrorism: EFT directive in respect of FATF Recommendation 16 on wire transfers**
- 11.10.1 In 2008 South Africa was evaluated in terms of its compliance with the FATF Recommendations on anti-money laundering (AML) and combating the financing of terrorism (CFT). The FAFT report¹⁸ issued in 2009 found South Africa to be partially compliant with Recommendation 16, as the regulatory framework required accountable institutions to collect and verify originator information, but did not provide for the necessary legal requirement for EFT transactions to be accompanied by full originator and beneficiary information.
- 11.10.2 In June 2015 the NPSD issued Directive 1 of 2015¹⁹ titled ‘Directive for conduct within the NPS in respect of the FATF Recommendations for Electronic Funds Transfers (EFT Directive)’. Following the issuance of the EFT Directive, the payments industry approached the NPSD and raised specific interpretation and implementation concerns with regard thereto; the FIC Amendment Act 1 of 2017 has since been promulgated and is now effective. The NPSD has decided to amend the EFT Directive, and has also developed a guidance note to assist in achieving a common interpretation of the EFT directive. It is envisaged that the revised EFT Directive and guidance note will be finalised and published in 2018.

18 <http://www.fatf-gafi.org/media/fatf/documents/reports/mer/MER%20South%20Africa%20full.pdf>

19 [http://www.resbank.co.za/RegulationAndSupervision/NationalPaymentSystem\(NPS\)/Legal/Pages/DirectivesForConductWithinTheNPS.aspx](http://www.resbank.co.za/RegulationAndSupervision/NationalPaymentSystem(NPS)/Legal/Pages/DirectivesForConductWithinTheNPS.aspx)

12. Main policy issues, proposals and recommendations

12.1 Overarching principles

- 12.1.1 The regulatory, supervisory and oversight frameworks proposed herein aim to achieve the following principles which have been clearly set out in the Twin Peaks Roadmap document:
- Transparency:** Appropriate information regarding the regulators’ decisions, actions and approaches will be made available to the regulators’ governance structures, regulated entities and necessary confidentiality safeguards.



- b. **Comprehensiveness and consistency:** The regulatory, supervisory and oversight frameworks will identify and address inappropriate risks and gaps in the regulatory coverage of financial services activities to limit regulatory arbitrage.
- c. **Appropriate, intensive and intrusive:** The supervisory and oversight frameworks will empower the regulators to gain meaningful and timely insight into the risks arising from supervised entities' activities.
- d. **Outcomes-based:** The regulatory, supervisory and oversight frameworks will adopt a blend of principles- and rules-based regulation to achieve the desired regulatory outcomes. Where principles-based regulation is used, the framework will ensure the principles are legally binding and enforceable.
- e. **Risk-based and proportional:** The regulatory, supervisory and oversight frameworks will enable the regulators to assess the risks associated with different regulated activities, systems, entities or group of entities. The frameworks will be sufficiently flexible to ensure that the regulatory, supervisory, oversight or enforcement approaches are proportionate to the risks.
- f. **Pre-emptive and proactive:** The frameworks will enable the regulators to identify emerging risks to financial stability and to consumers as early as possible, and grant them the authority to intervene to reduce the likelihood of these risks materialising.
- g. **A credible deterrent to non-compliance with prescribed standards:** To achieve the desired outcomes, regulated entities must be aware that regulators have the authority to enforce adherence to prescribed principles and rules, and will not hesitate to do so.
- h. **Aligned with the FSR Act and applicable international standards:** The frameworks must adhere to relevant provisions of the FSR Act and applicable standards set by relevant international standard-setting bodies. The NPSD will continue to play an active role in shaping such international standards.
- i. **Activity-based:** The regulatory framework should be focused on the activities related to payments, clearing and settlement within the NPS, in line with the spirit and intent of the FSR Act.

12.1.2 The NPS Act should reflect these principles in line with the FSR Act.

Recommendation 1

- 1.1 The proposed regulatory, supervisory and oversight frameworks to be provided for in the NPS Act should be transparent, comprehensive, certain, consistent, appropriate, intensive, intrusive, outcomes-based, risk-based, proportional, pre-emptive, proactive, a credible deterrence, and aligned with relevant provisions of the FSR Act and applicable international standards.
- 1.2 In support of a level regulatory playing field, the proposed regulatory, supervisory and oversight frameworks should be focused on the activities related to payments, clearing and settlement within the NPS.

12.2 Adoption of international and domestic financial sector regulatory standards

12.2.1 The requirement for the NPSD to consider and adopt relevant international standards in regulating, supervising and overseeing the NPS is not provided for in the NPS Act. This is crucial in ensuring proper alignment of South African payments law with relevant international standards or best practices. The revised NPS Act should be developed as an enabling legislation for other applicable international and domestic financial sector regulatory standards, to ensure that these can be effected through relevant subordinate legislation. In addition, the revised NPS Act must be flexible and broad to adopt other standards as required by relevant standard-setting bodies or as the market evolves.

12.2.2 In 2013 the NPSD expressed its commitment to adopting the PFMLs through the publication of a position paper and an information paper on the PFMLs.²⁰ Position and information papers are policy documents that express the NPSD's views on a particular payments matter and have no legal force and effect. The CPML expected its member jurisdictions to have adopted the PFMLs into domestic law by the end of 2012. The NPSD is in the process of reviewing both the position and information papers. The review is aimed at identifying FMLs in the NPS and clarifying the role of the respective authorities in relation to all FMLs. The NPSD, as the authority of payment FMLs, will further clarify its role in the revised position paper. This process will be finalised in 2018. As an initial step to adopting the PFMLs, the NPSD has currently recognised five payment systems as systemically important (i.e. systemically important FMLs), namely (i) SAMOS; (ii) SIRESS; (iii) the clearing system operated by BankservAfrica; (iv) the payment clearing system operated by Strate; and (v) the CLS system.

12.2.3 However, other than the publication of the position and information papers and the identification of FMLs using the PFML FMI criteria, the PFMLs have not been formally adopted into the domestic legislative framework. Therefore, no legislative FMI designation criterion has been translated into law by the NPSD. To address this, the NPSD will incorporate relevant/applicable provisions of the PFMLs in the NPS Act or relevant subordinate legislation in consultation with other relevant regulatory authorities. Once adopted, appropriate supervision and oversight controls and processes will be introduced to ensure effective implementation and compliance with the PFMLs by relevant FMLs.

Recommendation 2

- 2.1 The NPS Act should enable the ability to consider and adopt, where appropriate, international standards and principles to the extent that it is appropriate to South Africa and does not stifle innovation.
- 2.2 The adoption of international and domestic standards should be done in consultation with relevant regulatory authorities.

12.3 Public policy objectives

12.3.1 Unlike most financial sector legislation, the NPS Act has no objects clause that explicitly sets out the public policy objectives to be achieved through its implementation. These objects are, however, currently arbitrarily included in

20 [https://www.resbank.co.za/RegulationAndSupervision/NationalPaymentSystem\(NPS\)/Legal/Pages/Legal-Home.aspx](https://www.resbank.co.za/RegulationAndSupervision/NationalPaymentSystem(NPS)/Legal/Pages/Legal-Home.aspx)

various sections of the NPS Act and include the safety, efficiency, integrity and effectiveness of the NPS. The absence of an objects clause creates uncertainty with regard to the aim, objectives and scope of application of the NPS Act. The NPS Act should therefore make provision for the objects clause for clarity purposes, and specify both the primary and secondary objects listed in Recommendation 3 below.

Recommendation 3

- 3.1 The objects of the NPS Act should be explicitly stated in the NPS Act, and be aligned with the FSR Act, PFMLs and other relevant international standards.
- 3.2 The primary objects should be stated as promoting the financial stability, safety, efficiency (including interoperability), transparency and integrity of the NPS; the safety and soundness of payment institutions and activities; and confidence in the NPS.
- 3.3 The secondary objects should be stated as the prevention of financial crime, promotion of financial inclusion, and support of the FSCA in its consumer protection objective.

12.4 Payments regulator, supervisor and overseer

- 12.4.1 Currently, the SARB performs three roles in respect of the NPS, namely (i) the regulator, overseer and supervisor of the NPS through the NPSD; (ii) the operator of SAMOS and SIRESS through the NPSD; and (iii) a participant in the NPS through the Financial Services Department of the SARB. Two areas that flow from these roles need to be addressed: first, the conflict of interest that arises from the SARB's role as operator, participant and regulator; and second, the original and adequate powers that are required for the NPSD to effectively fulfil its envisaged new mandate and functions, matched with good governance and accountability.
- 12.4.2 It is crucial to clarify and separate these roles and establish an institutional and governance framework that would assist in avoiding a conflict of interest in the fulfilment of these roles. Of importance is the need to ensure operational independence of the regulatory, supervisory and oversight functions from the operator and participant roles, as well as from other key functions of the SARB.
- 12.4.3 In addition, the NPS Act should provide the SARB with clear original powers to act as the regulator, supervisor and overseer of the NPS. Currently, the powers of the SARB in respect of the NPS have been delegated from the SARB Board of Directors in accordance with section 2(2)(a) of the NPS Act. This presents a challenge as the SARB Board of Directors is an oversight board, with no operational role. Further, as part of the SARB's structural reforms of the NPS, certain powers previously delegated to the PSMB will be transferred back to the SARB, which necessitates an enabling legal environment for the effective execution of those functions by the SARB. These include the access and authorisation functions.
- 12.4.4 To ensure regulatory effectiveness, transparency, proper role clarification and accountability of the SARB as the regulator, overseer and supervisor of payments, it is important that the powers derived directly from the NPS Act are given to the SARB as represented by the executive. These powers should include licensing, the regulatory framework and standards, supervision, oversight and enforcement. As a regulator with extensive powers and reach, it must be subject to appropriate standards of good governance, operational independence and accountability.

Recommendation 4

- 4.1 The SARB should be given clear and original legal regulatory, supervisory and oversight powers in respect of the NPS in the NPS Act.
- 4.2 A department with no separate legal personality should be established within the SARB to which the regulation, supervision and oversight functions of the SARB should be delegated. The department should be accountable to the SARB executive, and through the SARB executive to the Minister of Finance on payments policy-related matters.
- 4.3 The department may be funded through industry levies and fees, combined with financial support from the SARB.
- 4.4 The role of the SARB in regulating, supervising and overseeing the NPS should be separated from the SARB's settlement SO and participant roles.
- 4.5 MoUs should govern the relationship between the SARB and other regulatory authorities, or international or regional bodies.

12.5 Mandate and objectives of the SARB

- 12.5.1 The mandate of the SARB in its current form is derived from section 10(1)(c) of the SARB Act which stipulates that the SARB may “perform such functions, implement such rules and procedures and, in general, take such steps as may be necessary to establish, conduct, monitor, regulate and supervise payment, clearing or settlement systems.” The mandate was subsequently incorporated in the preamble of the NPS Act as “provide for the management, administration, operation, regulation and supervision of payment, clearing and settlement systems in South Africa; and to provide for connected matters”.
- 12.5.2 However, regardless of this broad preamble, there is no clear alignment between the preamble and the actual mandate of the SARB in the NPS Act. This has resulted in uncertainty on the role, scope and extent of the mandate of the SARB. For instance, the oversight mandate of the NPSD is not explicitly provided for in the NPS Act, which causes uncertainty about the powers of the NPSD with regard to oversight.
- 12.5.3 Nevertheless, the SARB, through the NPSD, has executed the regulatory, supervisory and oversight mandates in respect of the broader NPS over the years through the application of the NPS Act, subordinate legislation, standards from the CPMI, and other applicable laws and standards. To provide clarity, it is crucial that the SARB should become the primary regulator, supervisor and overseer of the NPS, and that the NPS Act is explicit and provides sufficient guidance in this regard.
- 12.5.4 The mandate of the SARB should be to regulate, supervise and oversee the NPS, including licensing and enforcement and other related and ancillary mandates. In fulfilling the mandate, the SARB should seek to achieve the objects of the NPS Act listed in Recommendation 3. These include the promotion of the safety and efficiency, transparency, integrity and effectiveness of the NPS. In addition, the regulation, supervision and oversight of the NPS should aim to prevent financial crime, promote financial inclusion and competition, and support the mandates of relevant authorities such as the FSCA.
- 12.5.5 The NPS Act should also clarify the mandate of the SARB in relation to matters of mutual interest with other financial sector regulators.

12.5.6 The NPS Act should allow the SARB to delegate its mandate to an appropriate body or structure within the SARB or to another regulatory authority. Two possible structures are proposed in Box 2.

Box 2: Proposed establishment of the payment regulator, supervisor and overseer

a. Option 1

- A Payment System Authority (PSA) must be established as a separate juristic person within the administration of the South African Reserve Bank (SARB) to regulate, supervise and oversee the national payment system (NPS). As a separate juristic person, the governance and accountability requirements imposed on the Prudential Authority (PA) will *mutatis mutandis* apply to the PSA. The PSA will have a Chief Executive Officer responsible for the day-to-day management and administration of the PSA.
- New powers should be given to the PSA in line with those granted to the PA as described in the Financial Sector Regulation Act (FSR Act).
- The funding model will resemble that of the PA (i.e. through fees and levies imposed on regulated persons).
- The benefits of this model include leveraging off existing models from which lessons can be drawn. The model provides clarity with regard to the accountable officer to the Minister of Finance, and reserves the SARB's oversight over the structure as it still remains within the administration of the SARB. The disadvantage of this model relates to the transfer of the core function of the SARB relating to payments regulation, supervision and oversight to a separate legal entity. This is not ideal considering that this function supports the SARB's mandate of promoting financial stability and of implementing monetary policy.

b. Option 2

- The SARB must establish an internal department dedicated to regulating, supervising and overseeing payments, with no separate juristic or legal personality. The powers to regulate, supervise and oversee the NPS should be derived from the NPS Act and delegated by the SARB executive to the relevant department within the SARB, and not from SARB Board of Directors as is currently stated in the NPS Act. The Head of the established department will be accountable to the Deputy Governor responsible for the day-to-day management and administration of the department. The Deputy Governor will be accountable to the Governor, and the Governor to the Minister of Finance/National Treasury in respect of payments policy matters.
- Owing to its regulatory role, the funding model will resemble that of the PA (i.e. funded through fees and levies imposed on regulated persons as well as through any financial support provided by the SARB).
- The advantage of this model is the removal of the administrative and logistical burden of establishing a separate legal structure. The established department will be an internal structure of the SARB and will have the SARB's resources at its disposal. Further, the model will ensure that the payment system regulation, supervision and oversight, which is one of the core functions of the SARB in promoting financial stability, is not legally separated from the SARB. The model will also ensure that the original powers are appropriately derived from the SARB executive, as well as preserve the independence of the SARB. The disadvantage of this model is that it may result in the blurring of roles, resulting in the SARB executives' direct involvement in operational matters.

12.5.7 With both options, the role of the payments regulator, supervisor and overseer should be clearly distinguished from the SARB's role as a participant in the NPS and as the operator of the settlement systems to avoid perceived conflicts of interest and ensure the clarity of roles.

12.5.8 Having considered the two options, option 2 is preferred. The payment system regulation, supervision and oversight is a core function of the central bank from a financial stability perspective, and thus should remain with the SARB.

- 12.5.9 The SARB should also have cooperation arrangements, including MoUs with other financial sector regulatory authorities to ensure cooperation and the exchange of relevant information between it and other regulatory authorities.

Recommendation 5

- 5.1 The mandate of the SARB, namely to regulate, supervise and oversee the NPS, should be explicitly included in the NPS Act. Ancillary and related mandates should be included.
- 5.2 The NPS Act should enable the delegation of the regulatory, supervisory and oversight mandate as well as the related and ancillary mandate of the SARB to a department within the SARB or any other regulatory authority.
- 5.3 The primary and secondary objectives of the SARB should be included in the NPS Act, and should be fulfilled in alignment with the objects of the NPS Act and, where applicable, the FSR Act. These objectives include to promote safety and efficiency, transparency, integrity and effectiveness, financial inclusion and competition; and to prevent financial crime.
- 5.4 The SARB's objective to support the mandates of relevant authorities such as the FSCA should also be provided for in the NPS Act.
- 5.5 The NPS Act should clarify the role of the SARB in relation to matters of mutual interest with other financial sector regulators and other relevant authorities.

12.6 Powers and functions of the SARB

12.6.1 General powers and functions

- a. In executing its mandate to achieve its objectives, the SARB should have the following powers or perform the following functions: issue standards, directives, interpretation rulings/notes; conduct on-site and off-site inspections, FMI assessments, reviews and investigations; request any information; request reports, including annual reports with audited financial statements; attend meetings; approve rules applicable to any activity regulated under the NPS Act; impose administrative sanctions, including financial penalties; delegate any of its power and function/duty to a department within the SARB or another regulatory authority; delegate or outsource its non-core function/duty to a third party; consistently review the perimeter of regulation to identify new payment methods and risks; and conclude MoUs with other domestic or international regulatory bodies to enhance cooperation and the exchange of information.

12.6.2 Licensing

- a. In addition, the NPS Act should explicitly vest the responsibility for the licensing of entities performing any activity within the NPS in relation to payments, clearing or settlement with the SARB, after consultation with relevant regulatory authorities such as the FSCA and the PA, where necessary. It should be within the discretion of the SARB to waive any licensing requirement if it is deemed not to be appropriate under the circumstances, taking into consideration the relevant risk the activity poses to the NPS or an equivalent regulatory framework. The principles and criteria for exemption from licensing are to be determined within the NPS Act, in line with the provisions in the FSR Act regarding licensing.
- b. While the licensing requirement will not apply to the SARB-owned settlement systems, provision should also be made for the oversight

and supervision of these settlement systems, and what the continuing obligations of the SARB should be in this regard.

- c. The licensing requirements for other payment entities should include the requirements relating to legal and institutional forms (e.g. juristic persons, utilities versus for-profit entities and ownership restrictions), business activities, financial resources, fitness and propriety of key persons, operational management, technical capability, security, governance, risk management arrangements, and so on. They should also be aligned with the FSR Act and Financial Markets Act licensing requirements, as well as other applicable best international standards or best practices such as the PFMI and the King Code governance principles. The SARB should be satisfied that licensed institutions are compliant with applicable licensing requirements at the time of licensing or authorisation as well as on a continuous basis.
- d. As a general rule, the NPS Act should also require domestic presence for foreign licensed/authorised applicants who wish to participate in the NPS. This means that registration as a local/external company registration with the Companies and Intellectual Property Commission and the establishment of a local branch/office should be required. Additional requirements may also be imposed based on the applicant's size and risk profile. These functions and powers would enable effective supervision and enforcement by the SARB.
- e. However, notwithstanding (d) above, an equivalence framework requirement should be provided for in the NPS Act in terms of which the SARB may consider licensing/authorising foreign applicants on condition that the applicants are authorised in terms of an equivalent regulatory framework for the provision of similar services in their home jurisdiction. The equivalence regulatory framework is necessary to lessen the regulatory burden on the participants through possible exemption, and to ensure that only appropriately regulated foreign participants are allowed in the NPS. Additional requirements, including security or collateral prudential requirements, may also be imposed on the applicant.

12.6.3 Declaration of payment, clearing and settlement systems and payment instruments, services and participants

- a. The current designation framework in the NPS Act is too restrictive and unclear. The Minister of Finance should have declaration powers, which should extend to the declaration of any system, service, participant, operator and product, and not only clearing participants and settlement systems. The declaration referred to herein should be distinguished from the functions referred to in paragraphs 12.7 and 12.8 below, relating to the designation of systemically important payment systems (SIPs), prominent payment systems (PPSs) and critical service providers (CSPs).
- b. The requirements, conditions and processes for all declarations should be aligned with the minimum licensing requirements and processes as contained in the FSR Act. Where the applicant for declaration is a foreigner and is subject to an equivalent regulatory framework, such applicant may be exempted from satisfying some of the requirements. The designation should also meet the public policy objectives of the

NPS Act, and the reasons for the designation should be specified. The SARB should impose additional industry-specific requirements as well as ongoing licensing conditions to ensure continued compliance with designation conditions.

Recommendation 6

- 6.1 The general powers and functions of the SARB relating to regulation, supervision and oversight should be clearly outlined in the NPS Act. These should include the powers and functions relating to exemptions, enforcement action, ongoing monitoring of the risks in the NPS and the delegation of powers; issuing of standards, directives, interpretation rulings/notes and public warnings; powers to conduct on-site and off-site visits, FMI assessments, reviews, investigations and inspections; powers to request any information and reports, including annual reports with audited financial statements; powers to attend meetings, approve rules, impose administrative sanctions, including financial penalties; delegate any of its power or function/duty to a department within the SARB or another regulatory authority; delegate or outsource any of its non-core functions (excluding licensing, oversight and standard-setting functions) to any third party; and conclude memorandums of understanding with other domestic or international regulatory bodies to enhance cooperation and the exchange of information.
- 6.2 The SARB should be responsible for licensing all entities that provide payment services and operate payment systems, after consultation with the FSCA. The licensing and designation powers and functions as well as the requirements should be provided for in the NPS Act.
- 6.3 The Minister of Finance should have the power to declare services, activities, entities, systems and operators as payment services, activities, entities, systems and operators.

12.7 Designation, regulation, supervision and oversight of systemically important financial institutions (SIFIs), systemically important payment systems (SIPs – also known as systemically important FMIs) and non-systemically important payment systems (also known as prominent payment systems – PPSs)

12.7.1 Designation of SIFIs, SIPs and PPSs

- a. The NPS comprises payment participants and systems that may be classified as SIFIs, SIPs as contemplated in the PFMI, and other payment systems that are not systemically important but are prominent enough to lead to disruptions and the loss of confidence in the NPS should they fail (i.e. PPSs). The NPS Act should provide legislative authority to designate payment institutions and systems (including clearing and settlement systems) as SIFIs, SIPs or PPSs. In line with the FSR Act, the designation of SIFIs and SIPs should be the responsibility of the Governor of the SARB. The SARB should also have the responsibility to designate the PPSs and this should be included in the NPS Act.
- b. However, the institutions and the operators of these systems should first be licensed to provide a payment system or operate a payment system for the clearing or settlement of payments prior to designation. The designation criteria for SIFIs, SIPs and PPSs should be aligned with the FSR Act and PFMI, and should consider the following:
 - i. the size of the payment institution or payment system in respect of the number and value of transactions processed, the number and type of participants, market share, etc.;

- ii. the complexity of the payment institution or payment system and its business affairs;
- iii. the interlinkages/interdependencies of the payment institution or payment system with other payment institutions or payment systems, both within and outside of South Africa; and
- iv. whether there are substitutes readily available for the payment institution or payment system and/or services that the payment institution or payment system provides.

12.7.2 Regulation, supervision and oversight of SIFIs and PPSs by the SARB

- a. Once designated, the SIFIs, SIFIs and PPSs should be required to comply with the ongoing licensing requirements and general requirements applicable to payment, clearing or settlement institutions/systems/operators. For SOs, these should include the requirement to provide a technical infrastructure, the development of rules, and the monitoring and enforcement of compliance with those rules by authorised participants.
- b. In addition, SIFIs and SIFIs should be required to fully comply with the applicable PFMIs and other relevant international standards and domestic laws, such as the FSR Act. SIFIs should therefore be able to satisfy all the key considerations in respect of each applicable PFMI principle when being assessed against the PFMIs. The SIFIs and operators of SIFIs should also be required to comply with any financial stability requirements that may be imposed by the SARB in respect of SIFIs. These would also be given effect as payment standards in line with the FSR Act. Standards for PPSs, although somewhat aligned with the PFMIs applicable to SIFIs, might not be equivalent to the standards for SIFIs. Applicable principles in the PFMIs should be adopted into domestic NPS law or be included in subordinate legislation.

Recommendation 7

7.1 Provision must be included in the NPS Act for the:

- a. designation, regulation, supervision and oversight of SIFIs and PPSs, in line with the FSR Act, FMI identification criteria of the PFMIs and taking into account international best practices;
- b. designation of SIFIs and SIFIs, which should be the responsibility of the Governor, in line with the FSR Act; and
- c. designation of PPSs, which should be the responsibility of the SARB.

7.2 A designation as a SIFI, SIFIs or PPS may result in additional regulatory requirements being imposed on such SIFI, SIFIs or PPS by the SARB.

7.3 Applicable PFMIs will apply to SIFIs and PPSs, although the standards for PPSs might not be equivalent to the standards for SIFIs.

7.4 The SARB may not delegate any of its functions relating to SIFIs, SIFIs or PPSs to any person.

7.5 The NPS Act should also require home jurisdiction licensing and authorisation, and a domestic presence and/or equivalence home jurisdiction framework for foreign licensed/authorised applicants who wish to participate in the NPS.

12.8 Designation of critical service providers

- 12.8.1 CSPs provide services that are vital for the continuous and adequate operational functioning of SIPSs or PPSs. These include information technology and messaging providers such as telecom providers and SWIFT. Usually, these services are not payment services, but are services that are critical for the provision of payment services or the provision of infrastructure services. The providers of these critical services usually operate under a licence or some form of authorisation from their responsible authorities (who are not payment system authorities) to provide the critical services. However, owing to the critical nature of their services with regard to the operation of payment infrastructures and the provision of payment services, it is important for critical service providers to be subjected to designation standards that will ensure their safety and efficiency. To provide the SARB with authority over designated service providers, the critical service providers require designation as such by the SARB, and the designated critical service providers will be required to comply with the applicable standards. Licensing by the SARB is not required as the service provided is not a payment service, but an essential basic but critical service, already licensed/authorised by the responsible regulator. Cooperation arrangements are, however, required between the SARB and the licensing authorities to ensure effective designation of critical service providers.
- 12.8.2 In terms of the PFMLs, this should help ensure that the operations of a critical service provider are held to the same standards as those of the SIPS operators. The regulatory requirements are provided for in Annexure F of the PFMLs and cover risk identification and management, robust information security management, reliability and resilience, effective technology planning, and strong communication with users.
- 12.8.3 The SARB should be responsible for the designation of critical service providers in line with the PFMLs. Where a critical service provider provides services to SIPSs across jurisdictions, the SARB may enter into cooperative arrangements to ensure effective regulation, supervision and oversight of such critical service provider.

Recommendation 8

- 8.1 The SARB should be responsible for the designation of critical service providers that provide critical services to the SIPSs and PPPs.
- 8.2 Critical service providers will be required to comply with operational, risk, information, resilience, technology and communication requirements as provided for in the PFMLs.
- 8.3 Cooperation arrangements should be concluded between the SARB and the licensing and regulatory authority of the critical service provider, and between the SARB and other regulatory bodies where the critical service provider provides services to SIPSs and PPPs across jurisdictions.

12.9 Regulatory approach, including the consideration of delegation and outsourcing

- 12.9.1 As stated in paragraph 4.10, the SARB adopts a PSMB model, similar to an SRO model, in terms of which a PSMB is recognised to regulate, manage and organise its members. While the PSMB model has been in existence since 1998 and has greatly contributed to the safety and efficiency of the NPS, new

payment systems, participants, services, methods and developments have emerged which necessitated its review to determine whether the model is still optimal in the constantly changing payments landscape and, if so, how the future regulatory model should be designed. NPSs need to integrate and adapt to these development trends, and the national regulations need to be updated accordingly. National supervision and oversight functions and policies also need to be developed accordingly.

12.9.2 Further, there is a growing global trend of increased focus by regulatory authorities' regulations on payment services as a reaction to address slow developments, insufficient competition and consumer protection needs in the payments market. Following the global financial crisis and other most recent sovereign and corporate failures, central banks and regulatory authorities are increasingly becoming 'hands-on' and assuming more regulatory, supervisory and oversight responsibilities. Typical examples are the European Commission's directives and regulations in Europe and the Australian Reserve Bank's involvement in payment developments in Australia.

12.9.3 In 2015 the SARB also conducted a payments industry-wide survey of the effectiveness of PASA. The survey was aimed at gathering necessary information and identifying the shortcomings and areas of concern relating to PASA. Some of the key shortcomings highlighted by the survey include:

- a. **Mandate:** restrictive and biased mandate in favour of banks; conflicts of interest between regulatory and commercial interests as well as when executing the regulatory mandate as banks were the rule-makers and compliance monitors and were also involved in enforcement actions.
- b. **Governance:** lack of independence, skills and adequate representation at the PASA Council.
- c. **Membership:** non-bank exclusion from membership; non-bank views not adequately represented; inadequate representation and skills; and unfair representation between small and big banks.
- d. **Strategy:** failure of the strategy function.
- e. **Regulatory framework:** unclear, outdated, inconsistently applied and non-transparent regulatory and enforcement framework.

12.9.4 To address the issues associated with the PSMB model and PASA, the SARB published a report titled 'Review of the Effectiveness of the Payments Association of South Africa' (PASA Review final report) in July 2016.²¹ The report recommended the measures to be undertaken, the organisation(s) responsible for addressing the shortcomings as well as the timelines in which the review was to be conducted.

21 [https://www.resbank.co.za/RegulationAndSupervision/NationalPaymentSystem\(NPS\)/Documents/Oversight/PASA%20Report.pdf](https://www.resbank.co.za/RegulationAndSupervision/NationalPaymentSystem(NPS)/Documents/Oversight/PASA%20Report.pdf)

12.9.5 During 2017, the NPSD initiated the review of the broader PSMB model in parallel with the PASA review, which revealed certain shortcomings and some benefits of the current PSMB model. The main challenge of the PSMB model relates to the conflict between two competing interests that emanate from the dual mandate, namely (i) ensuring fair representation of the interest of its members and promoting cooperation between its members; and (ii) the regulation and management of participation of its members in the payment system in the interest of the system as a whole. Other challenges include a lack of clarity in the NPS Act on the appropriate legal and governance structures;

lack of a clear definition of recognition requirements; restrictive membership; a prescriptive mandate; and potential anti-competitive situations where the PSMB may act in an exclusionary, unfair or inequitable manner when governing access to the PSMB or when taking action with respect to the enforcement or when applying or interpreting PSMB rules and procedures in a way that is not fair and equitable to all members alike. Protection of legacy systems of the long-standing financial services providers negatively impacts the operational efficiency and effectiveness of PASA and its members, slows down regulatory reforms, stifles innovation and introduces inefficiencies in the NPS. Lack of collaboration and cooperation between PSPs may prove to be a huge impediment to interoperable systems and innovation. This necessitated the SARB's intervention through legally binding directives and sanctions to ensure (or coerce) collaboration and cooperation.

12.9.6 The review of the PSMB model included a study of the SRO or payment association models of other jurisdictions to determine which model would be appropriate for South Africa. Five jurisdictions were studied, as summarised in Box 3:

Box 3: Jurisdictional comparison of payments associations and their mandates

Australia

The payments association in Australia is known as the Australian Payments Network (previously the Australian Payments Clearing Association or APCA). Its objectives are: (i) to enable competition and innovation, promote efficiency, and control and manage risk in the Australian payments system, and to generate and collate ideas and information to support that objective; and (ii) to facilitate industry collaboration, self-regulation and system-wide standards, and to coordinate the operation of effective payment systems. The association is a **non-statutory voluntary association** not recognised in law. It facilitates **industry collaboration**, self-regulation and system-wide standards.

Canada

The Canadian Payments Association (Payments Canada) is a **not-for-profit statutory organisation** that was established in terms of an Act of Parliament in 1980 under the Canadian Payments Association Act. Membership in Payments Canada includes the Bank of Canada (BOC), Canadian domestic banks, and authorised foreign banks, other deposit-taking institutions (credit union centrals, trust and loan companies, and provincial savings offices), life insurance companies, securities dealers, and money market mutual funds. Payments Canada is governed by a 13-person Board of Directors, composed of 7 independent directors, 3 directors from Payments Canada members who are direct participants in Payments Canada systems, 2 directors from other Payments Canada members, and the President of Payments Canada.

The objectives of Payments Canada as provided for in the Canadian Payments Act, 1985 are to: (i) establish and operate national systems for the clearing and settlement of payments and other arrangements for the making or exchange of payments; (ii) facilitate the interaction of its clearing and settlement systems and related arrangements with other systems or arrangements involved in the exchange, clearing or settlement of payments; and (iii) facilitate the development of new payment methods and technologies.

In terms of section 5(2) of the Canadian Payments Act, 1985, the duty of Payments Canada is to **promote the efficiency, safety and soundness of its clearing and settlement systems and to take into account the interest of users**. Section 16 (1) states that the directors of Payments

Canada act honestly and in good faith with a view to the **best interests of the association**. Payment Canada issues **by-laws and rules** for participation in those systems. The Minister of Finance has authority over Payments Canada, while the BOC oversees the system operated by Payments Canada.

United Kingdom

The UK Payments Association (Payments UK) has been integrated into UK Finance (with the exception of the Design and Delivery and the Standards teams) from 1 July 2017. UK Finance is **now the new trade association** representing the finance and banking industry operating in the UK. Its objectives relate to policy, advocacy and delivering expertise to its members – the mandate previously executed by Payments UK. UK Finance is not recognised in law and is neither regulated nor overseen by the Bank of England (BOE) or the Payment System Regulator (PSR). During the benchmarking visit to the UK, the BOE highlighted that Payments UK was previously a quasi-regulatory body responsible for the promotion of innovation and competition in the UK payment system. However, the role was recently transferred to the PSR, a subsidiary of the Financial Conduct Authority after the association was unsuccessful in advancing competition and innovation in the payment system.

Netherlands

The Dutch Payments Association is a **voluntary trade association** responsible for the collective tasks that are important for the smooth functioning of payment transactions in the Netherlands. These common tasks relate to the infrastructure, standards, regulations and joint product characteristics of payment traffic. The Dutch Payments Association **operates in the interest of all its members and stakeholders**. The Payments Association works closely with its members and periodically consults with them on developments and activities. It also consults proactively with representatives of end users.

Analysis of the jurisdictional comparative analysis

- a. With the exception of Canada, none of the other jurisdictions provide for the legal recognition of payments association in law. In most jurisdictions, payments associations are voluntary or trade associations that organise the activities and set the code of conduct for their respective members. These associations do not exercise regulatory functions although they influence the regulatory reforms.
- b. In some jurisdictions, the payments associations were also operators of technical infrastructures or had outsourced the infrastructure to an infrastructure provider.
- c. Payments regulation was either split between the central bank (i.e. authority regulations) and the payment association (industry rules/agreements) or between the central bank and the conduct of another regulatory authority.
- d. The payment associations recognised in law had a regulatory, operator and catalyst mandate, as opposed to member interest.
- e. Collaboration challenges hampering competition and innovation in the payment system resulted in a payment association being divested of its regulatory mandate and transferred to a primary regulatory authority (see, for example, the UK).

12.9.7 The following future regulatory model is proposed for payment regulation (including licensing and enforcement) in South Africa, with implications for PASA or the PSMB model.

- a. **Legal certainty:** The future legislative framework of the NPS will provide legal certainty in relation to the model for the regulation, oversight and supervision of the NPS. The NPS encompasses the entire payment process, from payer to beneficiary, and includes settlement between participants. The process includes all the tools, systems, mechanisms, institutions, agreements, procedures, rules or laws applied or utilised to effect payment. The regulatory model, in particular, will explicitly provide for the SARB as the primary regulator, supervisor and overseer of the NPS. As a result, the revised NPS Act will no longer prescribe a PSMB

or SRO type of regulatory model. This will be in line with international best practice.

- b. **Mandate and functions:** The revised NPS Act will clearly stipulate the mandate of the SARB as the primary regulator, overseer and supervisor of the NPS. The powers and functions of the SARB in executing this mandate will also be specified in law. Of importance to note is the distinction between core functions (which will be prescribed in the NPS Act) and non-core functions which may or may not be made explicit in the NPS Act. The core functions include:

i. **Regulation of the entire NPS**

- Setting of NPS regulations and frameworks, including the issuing of regulatory instruments such as the NPS Act, directives, standards, notices, guidance notes, information papers and position papers, and frameworks such as regulatory, licensing, governance frameworks, etc., in collaboration with FSCA, where required.
- Licensing, authorisation and registration authority within the entire NPS, in collaboration with the FSCA, where required.
- Setting general entry and participation criteria for participation in the NPS.
- Setting entry and participation criteria (including rules) for settlement systems and their participants.

ii. **Oversight of the entire NPS**

- Continuous monitoring of open, interoperable, closed and stand-alone payment systems to ensure compliance with the NPS Act and regulatory instruments.
- Development of processes to identify, manage and mitigate risks in the payment system.
- Management of systemic crises in the payment system.

iii. **Supervision of the entire NPS**

- Supervise compliance with the NPS Act and relevant regulatory instruments and frameworks.
- Enforcement of compliance to the NPS Act and other regulatory instruments (such as standards, directives, etc.)

The non-core or supporting functions include, but are not limited to, the development of the NPS infrastructure; approval of industry rules that establish legal certainty and monitor the enforcement thereof; financial education; enhancing collaboration and competition; and commissioning and monitoring the implementation of industry projects and innovation.

- c. **Power to delegate:** In addition, the revised NPS Act will empower the SARB to delegate its powers and functions relating to its mandate, where necessary. The SARB will have the power to delegate some of its core functions to another regulatory authority such as the FSCA

or PA. Delegation to another regulatory authority would be useful in coordinating regulatory responsibilities under the FSR Act, the proposed COFI Act and the NPS Act among the SARB, FSCA and/or PA. Non-core functions may be delegated to a third party such as an industry body or an operator of a payment system. This will be the case where the SARB may wish to leverage off existing industry capacity and skills, and where the SARB is experiencing capacity constraints to develop and enforce system standards, and to promote ongoing innovation, competition and cooperation within the industry.

d. Responsibility of the SARB in respect of delegated functions:

- i. Depending on the delegated functions, the third party may be required to meet appropriate governance, financial, transparency, coordination, human resources, and fit and proper requirements. These may be set out in the general standard or in the delegation document.
- ii. Delegation of functions by the SARB will not amount to abdication of its responsibilities in relation to the delegated functions. The SARB will remain accountable for and oversee the overall execution of the delegated functions.
- iii. Delegation of functions will further not result in the complete transfer of delegated functions and the SARB may elect to also execute an element of the delegated function.
- iv. Moreover, the SARB will have the power to amend, suspend, cancel or withdraw the delegation within a reasonable time period, in the interest of the NPS.

e. Outsourcing: In addition to the power to delegate, the SARB will have the power to outsource specific, non-core and time-based NPS development, innovation and interoperability tasks to a third party with sufficient knowledge of, and experience in, the development of a payment ecosystem and rules, for example in the areas of payment modernisation, remittances or e-money. Paragraphs (a) to (d) above also apply with regard to the outsourcing of functions by the SARB.

f. Role of the NPS industry participants:

- i. This model has a clear separation of industry rules/standards and authority standards and regulatory instruments, which implies abolishing the application of dual mandates. The SARB would be responsible for the regulatory mandate, while the PSMB (i.e. PASA) would become a pure industry organisation which sets and enforces industry rules and standards, based on member mandates.
- ii. The industry, which includes PASA and other industry participants that do not fall under the ambit of PASA (e.g. non-banks and operators), will be required to align their goals to the SARB's public policy objectives and strategy (including Vision 2025 goals) of the NPS. In essence, the role of the industry in supporting the SARB's objectives will include the following:
 - Collaborate and cooperate to achieve the SARB's objectives and strategy of the NPS.

- Collaborate and cooperate to develop shared interoperable systems/infrastructures and ensure the benefit of the network effect.
- Collaborate and cooperate to develop industry rules and enforcement measures that establish legal certainty to support the SARB's objectives and strategy of the NPS, including interoperability.
- Collaborate and cooperate to implement industry projects.
- Contribute towards an inclusive, innovative and competitive payments landscape that will also contribute to enhanced access and financial inclusion.
- Drive capacity building and payment system education.
- Drive consumer financial education.
- Contribute to the development of, and assist with, the implementation of the NPS strategy.

c. Implications for the SARB, PASA, other stakeholders and the NPS

- i. **Discontinuation of the PSMB model:** The PSMB model will cease to exist and the PSMB's regulatory functions would be transferred to the SARB or relevant authority or delegated to a third party, where necessary. The PSMB model will no longer be recognised in the NPS Act, in line with international practice. PASA may become an industry body with a member mandate only responsible for member rules and the enforcement of such rules.
- ii. **Full regulatory responsibility lies with the authority(ies):** The SARB (and other relevant regulatory authorities such as the FSCA and PA) will assume full regulatory, supervisory, oversight and enforcement responsibility, with the SARB having the discretion to delegate or outsource non-core functions to a third party. The regulation, supervision and oversight of SOs, PCH SOs and TPPPs will also fall within the remit of the SARB (and, where applicable, the FSCA and/or the PA).
- iii. **Authorisation, licensing and access criteria:** The SARB (and other regulatory authorities such as the FSCA) will become the licensing authority(ies) and develop access, licensing and authorisation criteria for all payment providers/participants in the NPS. The current PSMB responsibility for access or authorisation criteria and the authorisation of SOs and PCH SOs will thus be transferred to the SARB (and/or FSCA). The SARB (and/or FSCA) will also develop authorisation criteria for TPPPs.
- iv. **Split of authority regulations/rules, industry/member rules and operator rules:** Any authority rules or regulations that are currently with the PSMB will be transferred to the SARB. The SARB (and/or FSCA) will set overarching payment services as well as clearing and settlement standards. Member-based or industry rules (excluding settlement rules) may be developed and enforced by industry bodies or a third party delegated by the SARB. Operator-participant rules will become the responsibility of the respective operators, for example

the SAMOS system will set settlement rules for approval by the SARB, while the other operators will set the rules for their respective systems, also subject to the SARB's approval. The industry or operator rules will require alignment with the payment, clearing and settlement standards set by the authorities.

- v. **Organisational implications:** Enhanced capacity would be required and capability would need to be built in the SARB (and FSCA) to execute some of the new responsibilities. Rule-making and enforcement capacity would also be required at the operator level, where necessary.

Recommendation 9

- 9.1 The SARB should become the primary regulator, supervisor and overseer of the NPS.
- 9.2 The PSMB model should be discontinued, removed from the NPS Act and replaced with the proposed future regulatory model.
- 9.3 There should be clear separation between authority or public regulation and self-regulation.
- 9.4 The SARB may decide to delegate or outsource some of its non-core functions to a third party.

12.10 Functions of operators of payment, clearing and settlement systems (including SIPS and PPSs operators)

12.10.1 In terms of Principle 1 of the PFMI, an FMI should have a well-founded, clear, transparent and enforceable legal basis for each material aspect of its activities in all relevant jurisdictions. In addition, Principle 23 requires an FMI to have clear and comprehensive rules and procedures, and to provide sufficient information to enable participants to have an accurate understanding of the risks, fees and other material costs they incur by participating in the FMI. All relevant rules and key procedures should thus be publicly disclosed.

12.10.2 Currently, the operators of payment, clearing and settlement systems (including the SIPSs and PPSs, or the PCH SOs) do not have the power to set and enforce technical and operating rules pertaining to the participation in their respective infrastructures. While the rules governing the clearing and settlement relationship between the participants are set by the PSMB, the relationship between the operators and the participants is governed by the service agreements.

12.10.3 Internationally, operators of clearing and settlement systems are also responsible for setting technical and operational rules for their respective systems, whether those systems are provided in-house or outsourced to a technical infrastructure provider. These rules include criteria for the authorisation of participants in their respective infrastructures.

12.10.4 In order to strengthen the regulatory, supervisory and oversight framework for the operators and participants, the operators should also make technical and operational rules relating to the payment activities and infrastructures provided by them. The technical and operational rules should be approved by the SARB. The operators should supervise and enforce compliance with their respective rules.

- 12.10.5 The operators should allow fair and open access to their respective systems in the interest of the NPS and public policy objectives, taking into account the required risk mitigation measures in the NPS and alignment with Principle 18 of the PFMLs. Where a participant is not satisfied with the decision of the operators in respect of access, the participants should be in a position to approach the SARB and/or the tribunal for relief.
- 12.10.6 The supervision and enforcement function of the operators as well as the function of the SARB in respect of the operators should be clearly articulated in the NPS Act.

Recommendation 10

- 10.1 The payment, clearing and settlement SOs should be required to adhere to standards set by the SARB.
- 10.2 The operators should develop technical and operational rules relating to the activities and infrastructures they provide.
- 10.3 The operators should monitor and enforce compliance with those rules by their respective participants.
- 10.4 The technical and operating rules should be approved by the SARB and be disclosed for transparency purposes.
- 10.5 The operators should be subject to the licensing, regulation, supervision and oversight of the SARB.
- 10.6 The operators should allow fair and open access to their respective systems in the interest of the NPS and public policy objectives.

12.11 Settlement in central bank money

- 12.11.1 The NPSD is supportive of Principle 9 of the PFMLs which requires money settlements to be conducted in central bank money to ensure the finality of settlements in the books of the central bank. In this regard, the SARB settlement system should be the sole settlement system in South Africa. However, it is recognised that settlement in other currencies in the future might be necessary, such as VCs, and that settlement by other settlement systems may be required owing to the increased growth in innovation and in emerging payment instruments and providers.
- 12.11.2 The NPS Act should therefore enable the settlement of central bank digital currencies and other currencies as well as the designation of other settlement systems subject to specific requirements being provided for in subordinate legislation, which may include requirements on the type of currencies to be allowed and how or whether these systems should link into or connect to the SARB settlement system for settlement finality purposes.

Recommendation 11

- 11.1 Settlement should be conducted only in central bank money to ensure the finality of settlements in the books of the SARB settlement system (i.e. SAMOS system).
- 11.2 It is, however, recognised that in future the SARB may wish to allow or require settlement of other emerging currencies, such as central bank digital currencies and VCs, or designate other settlement systems, and the NPS Act should be enabling in this regard, with specific requirements being provided for in subordinate legislation.

12.12 Conduct regulation

- 12.12.1 The regulatory scope of the NPSD has been historically limited to wholesale and interbank relationships (i.e. back-end conduct of the system) with minimal focus on customer-facing (front-end) conduct. Regulation of the NPS to date has been aimed at achieving the safety, integrity and efficiency objectives for the regulation of the NPS. As a result, specific regulatory provisions aimed at consumer protection were not included in the current NPS Act. This potentially exposed the consumers in the payments industry to risks and abuse by unscrupulous product and service providers.
- 12.12.2 The PSPs are currently authorised and regulated by the PSMB as clearing members or as designated clearing system participants or settlement participants in respect of, among other things, the clearing and settlement of transactions flowing from the payment instruments that they issue. The PCH SOs and SOs are authorised, while the TPPP are registered by the PSMB. However, no specific regulatory framework exists on the issuance of those payment instruments and how the PSP should conduct itself towards its retail/front-end customers.
- 12.12.3 The FSR Act, among other things, provides for the conduct, regulation and supervision of PSPs by the FSCA to address the conduct issues impacting customers in the NPS. The FSCA is, however, required to seek the concurrence of the SARB in respect of the issuance of conduct standards for PSPs.
- 12.12.4 The discussion regarding the role and scope of the FSCA in the NPS has been ongoing since the initiation of the drafting of the FSR Bill, and subsequently the review of the NPS Act. These discussions were between the SARB, National Treasury and FSCA. The understanding was that the agreed scope would be included in the relevant legislation, including the CoFI Bill, the NPS Amendment Act or the FSR Act through consequential amendments. Furthermore, an MoU would also be concluded between the SARB and FSCA for purposes of exchanging information and collaboration on relevant payment services-related matters.
- 12.12.5 To understand the respective roles of the FSCA and the SARB in relation to conduct, it is important to distinguish between retail and wholesale conduct. The FSCA has the primary responsibility for all conduct, ensuring fair customer treatment, and intervening where there are poor outcomes identified for customers. In the payments environment, for the front end of the system (i.e. where the NPS interfaces directly with a customer), the role and mandate of the FSCA is straightforward – the FSCA may set conduct standards on matters such as disclosure and on fair and transparent costs. For the back end and interbank/wholesale relationships, the arrangement between the FSCA and the SARB is more complicated. This is because any conduct standard that may be required to respond to back-end conduct will also have an integrity and efficiency impact. For this reason, these matters should be addressed jointly between the SARB and the FSCA, through joint standards.
- 12.12.6 The licensing of the PSPs will remain the responsibility of the SARB in terms of the FSR Act.
- 12.12.7 Section 111 of the FSR Act further places the responsibility for the licensing of PSPs that fall outside the remit of the NPS Act on the FSCA, which means that the SARB retains the responsibility for the licensing of the PSPs covered under the NPS Act.

- 12.12.8 In terms of section 126 of the FSR Act, the FSCA is required to seek the concurrence of other financial sector regulators prior to licensing financial services providers. However, owing to the general exclusion of the SARB in its role as the NPS regulator from the scope of the FSR Act, and specifically the definition of the financial sector regulator, the concurrence of the SARB as the regulator of the NPS was not explicitly provided for in the FSR Act, although it can be implicitly inferred.
- 12.12.9 Although the role of licensing PSPs is the subject of ongoing discussion between the SARB and FSCA under this review and the COFI Bill process, the licensing of the PSPs should remain with the SARB and be done after consultation with the FSCA. While it is acknowledged that the FSCA has an important role to play in protecting consumers in the NPS, the FSCA has no integrity, safety and efficiency mandate in the NPS in terms of the FSR Act. Owing to the direct interrelation between licensing and fair access to the NPS, which is core to the mandate of the SARB relating to the integrity, safety and efficiency of the NPS, licensing should vest in the SARB as the primary regulator, supervisor and overseer of the NPS. This approach is supported by the international experts and the World Bank (engaged by the SARB) who confirmed that at the global level, with very few exceptions, the central bank as the NPS overseer should be the licensing authority.
- 12.12.10 Further, the NPS is a network of systems and participants connected to form a value chain. It is an open two-sided market where payment instructions are exchanged and obligations are settled in central bank money in the SAMOS system. In respect of the open-loop payment systems, the PSPs will also be participants in the clearing and/or settlement payment systems and require licensing by the SARB.
- 12.12.11 Settlement finality and irrevocability is core to reducing systemic risk and ensuring the safety and efficiency of the NPS. Once transactions are entered into the payment system, there is a point at which the transaction cannot be unwound as this might have a knock-on effect on other participants in the NPS and pose systemic risk in the financial system. As a result, there may be instances where, despite 'conduct failure' of a PSP, the SARB may wish to retain the licence of a PSP (who is also a participant) until such time that all obligations have been discharged in order to maintain the safety and stability of the NPS, or where the retention would achieve other public policy objectives. Settlement finality provisions bind third parties, including the curators, liquidators and so on, and in this case will also bind the FSCA as the conduct authority. Therefore, to have two licences and licensing authorities in the payment system may cause systemic risk where the FSCA decides to withdraw the licence of a PSP that is also a participant in the payment system regulated by the SARB, and the SARB is of a different view; hence, the recommendation is for only one licence to be issued by the SARB after consultation with the FSCA. The FSCA does not need to license any activity, system, operator or provider in the wholesale domain; these persons would be licensed only by the SARB, in consultation with the FSCA.

Recommendation 12

12.1 The NPS Act and, if required, the FSR Act, should empower the SARB to support the conduct mandate of the FSCA in relation to PSPs.

12.2 Specifically, the following is confirmed and recommended:

- a. As per the FSR Act, the FSCA will issue conduct standards for PSPs with the concurrence of the SARB.
- b. There is a need for conduct to be considered in the wholesale/back-end operations (clearing and settlement domain) insofar as arrangements can have an impact on customer outcomes.
- c. Where standards may need to be set on 'back-end' operations to ensure that conduct outcomes are met, these can be set only as joint standards between the FSCA and the SARB.
- d. The SARB should remain the licensing authority in the NPS and license the PSPs after consultation with the FSCA.
- e. The SARB should retain the licensing or authorisation responsibility in respect of wholesale/back-end services, operators or providers.

12.3 This approach effectively defines the scope of the FSCA in the NPS and should be reflected in the relevant provisions of the NPS Act, the FSR Act and in the COFI Act.

12.13 Transformation: payment, clearing and settlement services

12.13.1 Payment services by non-banks

- a. Over the years, increased attention has been given to address the restrictiveness of payments legislation to include the participation of non-banks, in the spirit of promoting financial inclusion/access, competition and innovation in the payments environment. Reference can be made to the findings and recommendations in various reports and documents such as:
 - i. The World Bank report titled 'Achieving Effective Financial Inclusion in South Africa: A Payment System Perspective', wherein it was recommended that the South African authorities pay attention to the following: "(i) enhancing the opportunities for non-banks to participate and compete fairly in the NPS".
 - ii. The 2008 Banking Enquiry undertaken by the Competition Commission which has also made a number of recommendations, specifically relating to poor practices in the NPS. The Commission recommended that access should be given to the NPS for non-banks and other unregulated PSPs. Further, non-bank financial institutions and non-clearing banks should be permitted to clear and settle. While most recommendations have since been actioned, the inquiry highlighted the need for better oversight of all aspects of the NPS, including the ultimate impact on customers.
 - iii. During 2014, the IMF conducted an assessment of South Africa's compliance with international standards. With regard to the NPS, the FSAP report²² found that, contrary to CPSS-IOSCO Principle 18 of the PFMI, access to clearing and payments is biased against new entrants and that there is less competition among financial institutions in the payment system. It was recommended that more competitive

²² International Monetary Fund, 'South Africa Financial System Stability Assessment', *IMF Country Report No. 14/340*, December 2014.

behaviour by financial institutions be promoted by regulators, and that entry hurdles be lowered without sacrificing a stringent fit-and-proper test for new entrants. The IMF noted that promoting more competition among financial institutions would result in a greater supply of financial services at lower intermediation costs, especially for small and medium enterprises and lower-income households.

- iv. As stated in the SARB *Vision 2025*, with new providers of payment services entering the market for payment activities and services, it is essential that all system participants are governed by clear and transparent regulatory and governance frameworks. A level playing field must be maintained by ensuring that the same rules apply to similar payment activities and services, irrespective of whether the participant is a bank or a non-bank.
- b. In addition, section 7 of the NPS Act makes provision for payments to be made or accepted on behalf of third persons to whom money is 'due'. The services envisaged here include services offered by the BSPs and the PSPs (also referred to as TPPPs) where a payment obligation exists. Payments without any underlying obligation such as money remittances and e-money payments (including mobile money/payments) are thus generally excluded from the ambit of the NPS Act. Reference to 'payment due' in this section thus limits the types of payment services that may be provided in terms of the NPS Act, and should thus be reviewed. Caution should, however, be exercised so as not to capture services that should not fall under the regulatory sphere of the SARB.
- c. As a result of the limitation in section 7 of the NPS Act, provision of payment systems or services in South Africa such as e-money, mobile money, remittances, pre-paid services, quick response (QR) codes, pay by proxy, wallets and so on, has been restricted to banks. Except as provided for in section 7 of the NPS Act, there is currently no enabling framework for the provision of payment services by non-banks independently of banks. This means that for a non-bank to issue mobile money or to provide a remittance service in South Africa, the non-bank is required to partner with a bank. The e-money position paper²³ that was issued by the NPSD also restricts the issuance of e-money to banks. The main restriction, however, stems from the Banks Act which prohibits deposit taking by non-banks unless exempted by the Registrar of Banks. Most of these payment services involve the pooling of funds, which usually triggers the deposit-taking element and the resultant requirement for a banking licence.
- d. Recent developments in the payments industry, including the increased innovation in the domestic, regional and global payments industry around new payments methods and services, as well as the need to enhance financial inclusion and accessibility of the NPS to non-banks, have necessitated the creation of an enabling environment for the provision of payment services independently of banks. A description of payment services that is aligned to best international standards and practices is required in the NPS Act to enable the development of the domestic low-value retail payments, including faster payments, as well as the appropriate regulatory framework for the provision of these services.

23 [https://www.resbank.co.za/RegulationAndSupervision/NationalPaymentSystem\(NPS\)/Legal/Documents/Position%20Paper/PP2009_01.pdf](https://www.resbank.co.za/RegulationAndSupervision/NationalPaymentSystem(NPS)/Legal/Documents/Position%20Paper/PP2009_01.pdf)

- e. The FSR Act defines a ‘payment service’ as a service provided to a financial customer to facilitate payments to or from the financial customer. The objective for including this definition in the FSR Act was to provide for conduct regulation of PSPs to promote consumer protection in the NPS. However, the definition is too broad and captures other services that are provided in the closed loops and wholesale or back-end wherein the NPSD has the primary responsibility to enhance the efficiency, integrity and stability of the wholesale domain.
- f. To ensure alignment with international practices while catering for the unique domestic circumstances, a new definition of payment services should be provided for in the NPS Act, which should include the provision of services by non-banks relating to, among other things, mobile money, e-money and remittances, but exclude the services in the clearing and settlement domain that are provided for separately. The FSCA’s role in respect of such payment services should be aimed at affording the necessary protection to the front-end customers of the PSPs. Consumer issues arising from services provided in the wholesale domain should be dealt with by means of a joint standard between the SARB and FSCA.
- g. Section 7 of the NPS Act should thus be amended to enable other payment services to be provided in the NPS. The requirement for non-banks to partner with banks in providing payment services should be optional rather than mandatory. To achieve this, the following is proposed:
 - i. The definition of the business of a bank in the Banks Act should be amended to exclude activities in the NPS that entail the pooling of funds for purposes of making payments and transferring funds (e.g. remittances).
 - ii. Regulated payment activities should be exempted from the pooling of funds or the business of a bank provision in the Banks Act.
 - iii. An appropriate regulatory framework should be developed for payment services, which should include prudential and conduct regulation.
- h. The regulatory framework should be aligned with the regulatory framework issued by the SARB’s Financial Surveillance Department with regard to cross-border money remittances and the PAFI report. Specifically, the regulatory framework should cover the clear description of services, the threshold in respect of transactions (e.g. low-value person-to-person transactions), the protection of funds, capital/prudential requirements, how the system should be operated and its time criticality, interoperability, interest accrued, clearing and settlement of transactions, and AML/CFT supervision, among other things.

12.13.2 Clearing services: clearing by non-banks

- a. In 2004, 2007 and 2009 the NPSD allowed non-bank financial institutions that were excluded or exempt from the Banks Act, Co-operatives Banks Act and Mutual Banks Act to clear transactions, subject to certain conditions. Two institutions have been designated as clearing participants in terms of section 6(3)(a) of the NPS Act, namely Postbank and Diners Club. However, section 4(2)(d) and section 6(1)(b) of the NPS Act make access to clearing by non-bank participants dependent on

a settlement participant (bank), allowing such non-bank participants to clear. This is seen as restrictive and limits the non-bank participation in the clearing domain. The NPS Act should thus allow non-bank clearing participants to provide clearing services independently of banks and be provided the option to either settle directly in the SARB's settlement system or through another settlement participant.

12.13.3 Settlement services by non-banks

- a. Currently, only banks are allowed to open accounts and settle in the SAMOS system in South Africa. Non-banks are thus compelled to use banks to settle their transactions in SAMOS.
- b. However, recent developments in other jurisdictions have witnessed a shift from this policy to policies allowing non-banks to open accounts directly and settle transactions in the RTGS system owned by the central bank. Recently, in July 2018, the BOE published a revised Settlement Account Policy that includes non-bank PSPs. The Settlement Account Policy articulates eligibility criteria for a BOE settlement account. The applicant may include a bank or a non-bank PSP, namely a building society, broker dealer, CCP, FMI, authorised e-money institution or an authorised payment institution. It also contains which applicant qualifies for reserve accounts and intraday liquidity, and stipulates other requirements. The policy change is designed to ensure that the UK's payments infrastructure keeps pace with the changing structure of the financial system.
- c. It is important to create a level playing field between banks and non-banks settling in the SAMOS system. Allowing non-banks to settle in the SAMOS system will enhance the access of non-banks into the core of the NPS, and address issues raised by the FSAP and the 2008 Banking Enquiry.
- d. As a result, non-banks should be allowed to settle directly in the SAMOS system, subject to applicable requirements, particularly the risk-reduction measures (i.e. capital, liquidity and collateral or pre-funding requirements). Essentially, the NPS Act must contain an empowering provision to designate non-banks in settlement, the specific details of which must be contained in the subordinate legislation.

Recommendation 13

- 13.1 The following should be adopted in support of transformation and financial inclusion, to enhance access and competition, and to reduce payment services costs in the NPS:
- a. The provision of retail payment services/activities (e.g. remittance services, e-money, mobile money) where money is not due to a third party should be allowed, whether the entities providing such services are banks or non-banks. Such entities should be exempted from the definition of the business of a bank in the Banks Act and be subject to a risk-based and proportionate regulatory, supervisory and oversight framework. This could also be effected through an amendment to the Banks Act and necessary provisions in the NPS Act, while at the same time maintaining financial stability.
 - b. Any entity (including non-banks) should be allowed to provide clearing services, provided they make the necessary arrangements for the settlement of their transactions, either through another settlement participant or by settling in their own name.
 - c. Any entity (bank or non-bank) should be allowed to settle in the SARB settlement system, provided the applicable requirements (i.e. risk-reduction measures, including capital, liquidity and collateral or pre-funding requirements) are met by such entity.
 - d. The NPS Act must contain empowering provisions to designate non-banks in settlement. Thereafter, the details must be contained in the subordinate legislation.
- 13.2 The NPS Act should enable (a), (b), (c) and (d) above, with a view to maintain the stability of the NPS.

12.14 Regional or international payment, clearing and settlement services

- 12.14.1 Where any of the domestically licensed or authorised, designated or recognised payment, clearing or settlement systems provide services to entities/bodies outside of South Africa, prior approval of the SARB should be sought by the operator of such system, and relevant South African law, including the NPS Act, will apply. Where any of the domestically licensed operators/providers wish to participate in a regional or international payment, clearing or settlement system, it should ensure that such system is subject to a regulatory framework equivalent to that in South Africa prior to participation therein. This is aimed at reducing possible systemic risks that may be introduced domestically from the provision of cross-border services/systems or from participation in external systems.

Recommendation 14

- 14.1 Prior approval of the SARB should be sought where a domestically licensed operator of a payment, clearing or settlement system provides payment activities/services, functions or systems to regional or international users/customers/entities or where such operator wishes to participate in a regional or international system (e.g. as a regulatory body participant or user).
- 14.2 South African law and/or an equivalent regulatory framework will apply in this regard.

- 12.15 New or unregulated service providers, services, systems and instruments (e.g. virtual currencies, distributed ledger technologies and fintech companies)
- 12.15.1 The NPSD is aware of payment systems, payment services, instruments, products, functionalities and service providers operating in the unregulated domain. These include closed-loop systems such as the social grants payment system, payroll deduction system, mobile money systems/providers, remittance products and operators, VCs, fintech, cloud computing, artificial intelligence, open banking, and so on. In certain instances, some of these systems, services, instruments, functionalities, products and service providers are mainly provided as an alternative to regulated systems, instruments, services and providers, or to circumvent the existing NPS regulatory framework in contravention of the applicable public policy objectives.
- 12.15.2 These include the objectives of safety and efficiency, transparency, financial inclusion, consumer protection, integrity and competition, and principles such as interoperability, access and no preference. While direct regulation of all payment systems, instruments, technologies, functionality, services and service providers may be practically impossible, the SARB should have the authority to intervene in the unregulated domain where necessary to promote adherence to the public policy objectives and other applicable principles.
- 12.15.3 The SARB should be required to, on an ongoing basis, scan the regulatory perimeter to identify and respond to emerging risks. The NPS Act should therefore provide for this and have an enabling provision empowering the SARB to intervene through the issuing of standards, conditions, authorisation criteria or directives in respect of these services, systems or entities, and to take the necessary enforcement for non-compliance with these regulatory instruments.
- 12.15.4 The NPS Act should also have a prohibitions clause for the outright prohibition of provision of regulated services, instruments and systems without the required authorisation. In addition, the SARB should have the power, where necessary, to prohibit undesirable activities that might impact the efficiency, stability, safety, efficiency, transparency and integrity of the NPS.
- 12.15.5 In the future, the SARB should consider other methods of payment that could impact the efficiency and stability of the NPS, especially transfers of value other than money (e.g. the transfer of airtime and bitcoin). These activities may bring immediate risks to the consumer as well as longer-term risk to effective monetary policy, and may require appropriate regulation.

Recommendation 15

- 15.1 The SARB should be required to, on an ongoing basis, scan the regulatory perimeter to identify and respond to emerging risks through appropriate regulatory intervention.
- 15.2 The NPS Act should have an enabling provision for the SARB to intervene in all activities in the NPS and, where necessary, to bring new or unregulated activities into the regulated environment to set standards for such activities and to assist in developing the NPS, where necessary.

Other key issues, proposals and recommendations

12.16 Settlement finality and value date

12.16.1 Principle 8 of the PFMLs stipulates that the legal framework for FMIs should, as a minimum, define the point at which the settlement of a payment is final and irrevocable, and that the settlement process should be completed no later than the end of the value date. Further, the point at which unsettled payments may not be revoked by a participant should also be specified.

Recommendation 16

- 16.1 The NPS Act or settlement standards should explicitly state that settlement is final and irrevocable, and the point at which settlement is final and irrevocable cannot be unwound.
- 16.2 It should also be prescribed that the settlement should be completed no later than the value date in line with the PFMLs. Section 8 of the NPS Act should be amended to be aligned with Principle 8 of the PFMLs.

12.17 Risk management provisions

12.17.1 The current risk reduction measures in the SARB's settlement system are contained in the 'Position paper on risk reduction', published by the NPSD. Given the non-binding nature of position papers, it is recommended that these risk reduction measures be included either in the NPS Act or in the legally binding standards to be issued by the NPSD. They should also be aligned with the risk management standards in the PFMLs, including the management of collateral, cyberattacks, liquidity, credit, and settlement/participant failure risks.

Recommendation 17

- 17.1 General risk reduction measures should be included in the NPS Act.
- 17.2 Details of the risk reduction measures should be included in the standards issued by the SARB. The measures should also be aligned with the risk management principles in the PFMLs, including the management of collateral, cyberattacks, liquidity, credit, and settlement/participant failure risks.

12.18 Clearing provisions

12.18.1 Clearing definition

- a. The definition of clearing needs to be revised to align with the BIS CPMI definition. The current definition does not provide clarity with regard to the scope of clearing. The uncertainty has resulted in certain users in the financial system bypassing the central clearing system and submitting files directly to the paying banks, thus processing these transactions as 'on-us' transactions (i.e. sort-at-source).
- b. The BIS defines clearing as "the process of transmitting, reconciling and, in some cases, confirming transactions prior to settlement, potentially including the netting of transactions and the establishment of final positions for settlement". Sometimes this term is also used (imprecisely) to cover

settlement. The definition in the NPS Act should be aligned with the BIS definition to bring clarity on the types of activities which would qualify as clearing.

Recommendation 18

18.1 The definition of clearing should be aligned with the BIS CPMI definition of clearing to provide legal certainty that clearing entails the process of transmitting, reconciling and, in some cases, confirming transactions prior to settlement, potentially including the netting of transactions and the establishment of final positions for settlement. This should avoid the bypassing of the system by users submitting files directly to the paying banks, thus processing these transactions as 'on-us' transactions.

12.19 Enforcement/dispute resolution

12.19.1 Enforcement

- a. The NPS Act currently explicitly provides for criminal and civil enforcement action to remedy non-compliance therewith. Other than the powers to issue directives (section 12), withdraw/revoke recognition/designation (sections 3 (2A) and 6(3)(b)), and the power to request any form of information from any person, comprehensive administrative enforcement powers are not provided for in the NPS Act. In terms of section 13A of the NPS Act, the NPSD may approach a High Court to direct a person to comply with the NPS Act or a directive issued in terms of the NPS Act, while section 14 deals with criminal offences and penalties applicable in the event of non-compliance with certain specified sections of the NPS Act.
- b. Administrative sanctions/powers are always necessary to enable the regulator, after consideration of relevant factors, to either reprimand, impose financial penalties or even order compensation orders, and are often quicker to implement than criminal and civil actions. To ensure an efficient response to non-compliance, it is thus necessary for the NPS Act to contain administrative enforcement actions/powers. These should also be aligned with the relevant administrative penalties and enforcement action provisions in the FSR Act.
- c. In addition, empowering provision for directives in the NPS Act should be aligned with the FSR Act. Essentially, the issuance of subordinate legislation through directives should be replaced with the power to issue standards. Thus, the directives that the SARB will be issuing in the future would be specific to individual institutions, and not of a general nature. In accordance with the FSR Act, the SARB should be required to notify the payment institution of the intention to issue a directive, and provide the payment institution the opportunity to make submissions prior to the issuance of the directive.
- d. Currently, only criminal or civil actions are applicable in respect of the non-compliance of directives, which is not ideal as criminal and civil proceedings tend to be lengthy and time consuming, which negatively impacts the efficiency of the NPS. Thus, administrative sanctions should be imposed where there is non-compliance with the directive.
- e. In addition, the application of funds received from penalties should be clearly specified in the NPS Act. Penalties should be applied for the costs and expenses reasonably incurred by the SARB in connection

with the contravention as well as the development of the NPS through training and capacity-building initiatives, and the remaining balance should be deposited in the National Revenue Fund. These requirements should be applicable to the SARB as well as the payment, clearing and settlement SOs.

12.19.2 Dispute resolution

- a. Section 11 of the NPS Act is restrictive as it provides dispute resolution recourse only to the SARB settlement system participants aggrieved by a decision taken by the NPSD. In practice, the decisions of the NPSD are not only restricted to SARB settlement system participants, but to other participants and operators in the NPS, including the PSMB, designated settlement systems, designated settlement participants and other systems/participants/payment institutions within the NPS. The dispute resolution mechanism provided in section 11 of the NPS Act should thus be extended and be availed to other participants in the NPS that are aggrieved by the decisions of the SARB.
- b. The FSR Act established the Financial Services Tribunal (Tribunal) which is responsible for the reconsideration of the decisions of, among others, the financial sector regulators, ombuds and market infrastructures. Specifically, the FSR Act provides that a reconsideration of a decision by the Tribunal constitutes an internal remedy as contemplated in section 7(2) of the Promotion of Administrative Justice Act 3 of 2000.
- c. Although the NPS has been excluded from the FSR Act, it is recommended that the dispute resolution mechanisms, particularly the Tribunal, be availed to participants and the payment, clearing and settlement SOs in the NPS. In this regard, the necessity of section 11 should be reconsidered, given that the aggrieved party may choose to approach the Tribunal directly instead of following the section 11 dispute procedure. It is therefore recommended that the NPS Act be aligned with the provisions of the FSR Act relating to access to the Tribunal. Essentially, the Tribunal should also have the power to reconsider the decisions of the SARB and the payment, clearing and settlement SOs in the NPS, and provide an avenue to persons aggrieved by the decisions of these entities to resolve their disputes.
- d. While the above is necessary to ensure administrative justice, it is equally necessary to ensure that financial customers have dispute resolution avenues to lodge complaints against PSPs. The FSR Act provides for the recognition of industry ombud schemes for this purpose. Where there is no industry ombud scheme, the Ombud Council will have the power to designate the scheme for that particular industry. Consumers in the NPS who are dissatisfied with the products, services or conduct of PSPs should have access to an ombud for recourse, although there is currently no dedicated ombud for payment services consumers. Consumers in the payments industry have been approaching the banking ombud for assistance.
- e. However, while there are efforts to consolidate ombud schemes in South Africa under the FSR Act, an ombud for payment services should be considered in this context, given the acknowledgement that there are many non-bank PSPs that offer payment instruments to financial customers. This may be included in the NPS Act or FSR Act through consequential amendments.

Recommendation 19

- 19.1 The NPS Act should contain administrative enforcement actions/powers, including the power to reprimand, impose financial penalties or even order compensation orders. These should also be aligned with the relevant administrative penalties and enforcement action provisions in the FSR Act.
- 19.2 Financial penalties should be applied to defray the costs and expenses reasonably incurred by the SARB in connection with the contravention as well as the development of the NPS through training and capacity-building initiatives, and the remaining balance should be deposited in the National Revenue Fund.
- 19.3 A dedicated payment services ombud should be established and recognised in terms of the FSR Act.

12.20 Resolution, recovery, curatorship, judicial management or liquidation (section 8 of the NPS Act)

- 12.20.1 Section 8 of the NPS Act only applies in respect of the curatorship, judicial management or liquidation of clearing system participants and settlement system participants, to the exclusion of other key participants in the NPS. Following the release of the PFMI, the main focus has shifted to SIPSs and the shocks they could potentially cause to the NPS and the broader economy should they fail. Thus, the resolution and recovery provisions should also apply to SIFIs, SIPSs, PPSs and other retail payment systems. In addition, the framework needs to be aligned with the relevant FSB as well as the CPMI recovery and resolution standards, principles and guidelines. The section should include powers to transfer some or all of the FMI's operations to one or more third party or statutory management/ administration, or to require the curator to continue with critical operations until they can be transferred or wound down in an orderly manner. Alignment with the Companies Act with regard to, among other things, business rescue provision is also required.
- 12.20.2 The SARB, in collaboration with National Treasury, has developed a resolution framework for SIFIs. It is important for the framework to include the resolution of SIPSs and SIFIs in the NPS. The SARB should develop a resolution and recovery framework for non-SIFIs and non-SIPSs in the NPS. It is important for the settlement finality rules to be included in the relevant resolution legislation and in the NPS Act, and to bind the Resolution Authority, curator, business rescue practitioner and liquidator. The NPS Act should also provide clarity with regard to these issues.

Recommendation 20

- 20.1 Provision should be made for the recovery and resolution of SIPSs, SIFIs and PPSs in the relevant resolution legislation and/or NPS Act.
- 20.2 However, recovery and resolution proceedings should be subject to the settlement finality, irrevocability provisions and settlement assurance provisions in the NPS Act to avoid the unwinding of transactions in the settlement system.

12.21 Regulatory instruments

12.21.1 Standards

- a. The FSR Act has introduced the power to issue subordinate legislation in the form of standards by financial sector regulators for their respective industries. Although the NPSD is not listed as a financial sector regulator in the FSR Act, as the regulator of the NPS, the SARB should be empowered to issue standards to regulate the NPS and/or guide the development of rules at the operator level, where required. The power to issue standards and the consultation process should be included in the NPS Act (with appropriate amendments to the FSR Act). The standards should replace the current directives that require gazetting.

12.21.2 Regulatory instruments (administrative actions)

- a. The FSR Act also makes provision for the issuance of regulatory instruments by financial sector regulators. Likewise, the NPS Act should make provision for regulatory instruments with the necessary consultation process as contained in the FSR Act.

12.21.3 Guidance/guidelines/interpretation rulings

- a. Given the principle nature of the NPS Act, it is necessary for the SARB to have the power to issue guidelines on the application and interpretation of the NPS Act, where necessary. This is currently not expressly provided for in the NPS Act. Section 6(3)(k) of the Financial Markets Act gives the Registrar of Securities Services the power to issue guidelines for this purpose.

12.21.4 Consultation (regulatory process)

- a. The FSR Act seeks to strengthen the regulatory processes of the financial sector regulators by prescribing a process for the issuing of regulatory instruments, which includes the consultation and submission of standards and regulatory instruments to Parliament. Alignment with the FSR Act in developing the above-mentioned legislative and regulatory framework is recommended to ensure broader consultation, which is the cornerstone of robust and inclusive regulatory and legislative frameworks.

Recommendation 21

- 21.1 The SARB should be empowered to issue standards and interpretation ruling notices, and take regulatory and enforcement actions against other regulatory instruments in line with the FSR Act in its regulation of the NPS.

13. Consequential amendments

13.1 Consequential amendments to the following legislation are envisaged:

13.1.1 FSR Act

- a. The FSR Act should be amended to, inter alia:
 - i. align the definition of payment services to define the scope of the FSCA within the NPS;
 - ii. enable the resolution of SIPSs and SIFIs by the Resolution Authority;
 - iii. enable the issuance of financial stability standards by the SARB;
 - iv. extend the application of the Tribunal and ombuds to the NPS;
 - iv. extend the power of the Governor to designate SIFIs, SIPSs and PPSs in the NPS; and
 - vi. cater for any other amendment required that is established during the process of crafting the NPS Act.

13.1.2 Banks Act

- a. The Banks Act should be amended to exclude payment services regulated under the NPS Act from the definition of the business of a bank.

13.1.3 Consumer Protection Act 68 of 2008 (CPA)

- a. In terms of section 10 of the FSR Act, the CPA does not apply a function, act, transaction, financial product or financial service that is subject to the NPS Act.
- b. In this regard, attention must be given to the following provisions in the CPA:
 - i. dealing with fraudulent schemes and pyramid schemes (sections 42 and 43) insofar as these relate to financial crime; and
 - ii. dealing with prepaid cards or other devices, insofar as these relate to payment services (sections 63 and 65).
- c. Consideration must be given to whether these should be regulated under the NPS Act. This will prevent fragmentation in the different laws. The CPA is not regarded as a financial sector law, and all such matters should rather be dealt with in appropriate legislation.

Abbreviations

| | |
|-----------|--|
| AC | authenticated collections |
| ACH | automated clearing house |
| AEDO | authenticated early debit order |
| AML | anti-money laundering |
| ATM | automated teller machine |
| Banks Act | Banks Act 94 of 1990 |
| BIS | Bank for International Settlements |
| BOC | Bank of Canada |
| BOE | Bank of England |
| BSP | beneficiary service provider |
| CCP | central counterparty |
| CDS | central securities depository |
| CFT | combating the financing of terrorism |
| CHAPS | Clearing House Automated Payment System |
| CLS | continuous linked settlement |
| COFI Act | Conduct of Financial Institutions Act |
| CPA | Consumer Protection Act 68 of 2008 |
| CPMI | Committee on Payments and Market Infrastructures |
| CPSS | Committee on Payment and Settlement Systems |
| DLT | distributed ledger technology |
| ECB | European Central Bank |
| EDO | early debit order |
| EFT | electronic funds transfer |
| FATF | Financial Action Task Force |
| FIC | Financial Intelligence Centre |
| FSB | Financial Stability Board |
| fintech | financial technology |
| FIP | Protocol on Finance and Investment |
| FMI | financial market infrastructure |
| FMU | financial markets utility |
| FSAP | Financial Sector Assessment Program |
| FSCA | Financial Sector Conduct Authority |
| FSR Act | Financial Sector Regulation Act 9 of 2017 |
| G20 | Group of Twenty |
| GEC | Governors' Executive Committee |
| IDP | Interchange Determination Project |
| IMF | International Monetary Fund |
| IOSCO | International Organization of Securities Commissions |
| ISO | International Organization for Standardization |
| Model Law | SADC Payments Model Law |
| MoU | memorandum of understanding |
| MTO | money transfer operator |
| NAEDO | non-authenticated early debit order |

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|------------|---|
| NPS Act | National Payment System Act 78 of 1998 |
| NPS | national payment system |
| NPSD | National Payment System Department |
| PA | Prudential Authority |
| PAFI | Payment Aspects of Financial Inclusion |
| PASA | Payments Association of South Africa |
| PAYIR | Payment Information Return |
| PCH | payment clearing house |
| PFMIs | Principles for Financial Market Infrastructures |
| PPS | prominent payment system |
| PSA | Payment System Authority |
| PSMB | payment system management body |
| PSP | payment service provider |
| PSR policy | Federal Reserve Policy on Payment System Risk |
| PSR | payment system regulator |
| RTC | real-time clearing |
| RTGS | real-time gross settlement |
| RTL | real-time line |
| SADC | Southern African Development Community |
| SAMOS | South African Multiple Options Settlement [system] |
| SARB Act | South African Reserve Bank Act 90 of 1989, as amended |
| SARB | South African Reserve Bank |
| SARS | South African Revenue Service |
| SIFI | systemically important financial institution |
| SIPS | systemically important payment system |
| SIRESS | SADC Integrated Regional Settlement System |
| SO | system operator |
| SRO | self-regulatory organisation |
| SWIFT | Society for Worldwide Interbank Financial Telecommunication |
| TPPP | third-party payment provider |
| UK | United Kingdom |
| US | United States |
| VC | virtual currency |