

**BANK OF JAMAICA (BOJ)**

**VISION OF THE FUTURE NATIONAL  
PAYMENT SYSTEMS**

**EXECUTIVE SUMMARY**

**MARCH 2006**

## EXECUTIVE SUMMARY

1. The Bank of Jamaica (BOJ) has embarked on a process of payment system reform to enhance the safety and efficiency of these systems in order to reduce systemic risks, as well as minimize BOJ credit risk. The BOJ has assumed a leadership role in order to coordinate the necessary actions to achieve an overall upgrade of the payment systems. Due to the growth in use of cashless instruments in Jamaica, emphasis must be placed on enhancing the safety and efficiency of the payments system. The rapid growth in importance of the money and securities markets in the payment system and their associated systemic risks have also demanded that greater attention be paid by the Bank to the interface between payment and securities settlement arrangements. It is against this background that the BOJ considers it critical to embark on a process of comprehensive reform of the payment and settlement systems including the legal and regulatory framework, the modernization and integration of payment systems, and the establishment of the oversight function for payments and securities settlement systems.

2. The BOJ is responsible for the oversight of the payment and settlement systems in Jamaica. The BOJ believes that a cooperative approach must be taken in formulating the strategy for successful payment system reform. All stakeholders in the payment system including financial regulators, financial institutions, telecommunications providers, and private sector bodies must be involved in the reform process. Constant dialogue among participants must be maintained through the National Payments Council (NPC), which consists of senior level representatives of stakeholders. At the helm of the reform process, the BOJ presides over the maintenance of confidence in the currency, as well as, the viability of the financial system, which will provide the essential infrastructure for economic growth and development. The BOJ also provides the Chair and secretariat functions for the NPC.

3. This is the executive summary of the document: **“Vision on the Future National Payments System”**, the general purpose of which is to state an agreed vision by all stakeholders on the future of the National Payments System in Jamaica. The specific purpose of the current version of the report is to stimulate local interest and provide a basis for discussion with key Jamaican stakeholders during the next months as agreement on a number of policy, organizational, technical and operational issues will be required before next steps are undertaken. The BOJ recognizes that a successful initiative requires active participation from key stakeholders at both the policy and operational level. In addition the BOJ also recognizes the need to increase the payments system knowledge of key stakeholders and thus ensure that they have an opportunity to influence the specifics of the national payments system strategy to satisfy the needs of their institutions and customers. To this end, the BOJ conducted a **Sensitization Workshop** in August 2005 at which critical policy, organizational, technical, and operational issues were discussed by experienced payments systems practitioners and participants. World Bank advisors brought their experience in payment systems reforms in other countries to this Workshop.

4. The BOJ is adopting a strategic approach for the reform of the payments system of Jamaica. The experience of several other countries has proven, in fact, that the lack of a coordinated approach to payments system issues not only impacts on the success of individual projects underway but also affects the overall financial infrastructure and, in the end, the economy. If a National Payments System (NPS) strategy is not defined and agreed as a matter of urgency, the future of the payments system in Jamaica will be the uncertain result of separate efforts by stakeholders trying to improve their systems without a view of the overall national interest. In defining the vision for the Jamaican payments system, the BOJ is also considering the outputs of the report, “Guidance for Payment System Development” of The Committee of Payment and Settlement Systems (CPSS, May 2005).

5. A national payments system architecture should consider as an important element the safety and stability of the financial system. A consensus on a strategic and collaborative approach is crucial in that it would take a holistic view of all aspects of the nation’s payment system needs and satisfy them in an orderly and cost-efficient manner. A collaborative approach, with the active participation of all stakeholders, is highly desirable because of the complexity of the required changes which will involve inputs relating to service providers, users, technology, legal and regulatory matters, and contributions from several professional disciplines. A well-structured collaborative approach will create synergy, stimulate learning and provide a basis for optimizing benefits through cooperation and consensus building. Finally, the strategic approach will be able to address all the critical issues present in the current payments arrangements.

6. The BOJ is taking the lead role in formulating and implementing the strategy for payment systems modernization. The BOJ will act in the interest of the system as a whole. As a neutral agent, the BOJ is less likely to trigger competitive concerns that could slow progress and is better able to support the creation of a comprehensive vision for the national payment system.

7. The scope and difficulty of developing and carrying out a strategy for payment systems modernization successfully should not be underestimated. This will be a new process, and the projects that will be designed and carried out under the umbrella of the overall strategy will present new challenges to all parties involved. The major risks are: (i) the systems developed could not be used (ii) the resulting system changes will not satisfy the needs of all users, and (iii) the systems will not be cost efficient and affordable. However, a collaborative and cooperative approach is the only way in which these risks can be minimized. In order to have an efficient cooperative approach appropriate human resources, in number and expertise, should be made available by the different stakeholders.

8. A National Payments System (NPS) consists of a defined group of institutions and a set of instruments and procedures, used to facilitate the circulation of money within the country and internationally. The NPS is therefore a core component of the broader financial system and can be viewed as the infrastructure that provides the economy with the channels or circuits for processing the payments resulting from the many different types of economic transactions that take place on a daily basis. A well functioning NPS

requires a delicate balance between market-driven competition, cooperation and public good considerations. Taking account of the previous points, it is clear that a comprehensive NPS comprises not just the funds transfer mechanisms - payment processing organizations, communications networks, and computer systems – but includes all of the following: institutions providing financial intermediation; a legal and statutory framework; rules, regulations and agreements; appropriate payment instruments; processing systems and procedures; a cost effective technological infrastructure; clearing and settlement mechanisms that adequately balance risk and efficiency requirements; providers of access to payment-related services; and a carefully selected range of payment-service providers and products that satisfy market needs at acceptable costs.

9. The **Vision Document** presents the main elements which will characterize the future payment arrangements in Jamaica. The vision has been agreed with all stakeholders, and the BOJ is in the process of preparing a detailed action plan for the implementation of all the main objectives stated in the document. The BOJ will work with all market participants to achieve these objectives. The NPS in Jamaica will be based upon the following Pillars:

**Pillar I: Payment Systems in Jamaica work in a sound and robust legal environment which supports settlement finality**

10. *The BOJ supports a robust legal framework for payments and securities settlement and is proactively seeking to strengthen the legal and regulatory environment in Jamaica. A legal team has been formed within the BOJ to address all pending issues and make proposals for the provisions to be included in draft legislation, including the rules and regulations of all systems which will be discussed with all stakeholders.*

**Pillar II: Systemically Important Payment Systems (SIPS) in Jamaica are safe and efficient and comply fully with the CPSS Core Principles for SIPS**

11. *All systemically important payment systems in Jamaica will comply with the CPSS Core Principles for Systemically Important Payment Systems.<sup>1</sup>*

12. *The BOJ will issue a risk control policy document, the main implications of which will be discussed with all stakeholders. All systems and their participants will be required to adhere to this policy document. Stakeholders will commit to observe the agreed policies.*

---

<sup>1</sup> The CPSS established a Task Force on Payment System Principles and Practices in May 1998. International consensus on these principles resulted in the BIS development and publication of Ten (10) Core Principles for SIPS.

13. *The BOJ will operate a modern Real Time Gross Settlement (RTGS) System, which will represent the backbone of the payments system in Jamaica. To this end, the BOJ will initiate the launch of a large-value transfer system (LVTS) with a Real-Time Gross Settlement (RTGS) function that will replace the current CIFTS. The RTGS system will have clear rules and procedures, which will specify all the tools for managing legal, financial and operational risks. The design of the system will include the provision of management tools to handle liquidity risks. These include: the provision of queuing mechanisms by introducing optimization mechanisms; agreeing with system participants efficient operating hours and establishing sound and efficient interconnections among the systems; creating routines for channeling government payments early in the operating day and providing collateralized intraday liquidity in accordance with predetermined criteria.*
14. *The design of the payment system will include: 1) the strengthening of a robust and efficient communication network between the Bank and system participants, which could reduce and eventually eliminate the use of manual and paper-based procedures. 2) The strengthening and enforcement of strict security measures both for physical and electronic access to the system. 3) Implementation of contingency plans and disaster recovery mechanisms, including secondary sites. 4) Implementation of measures for business continuity and resilience across the NPS.*
15. *Pricing policies will be consistent with the overall objectives. The BOJ will establish a cost recovery pricing policy consistent with the general policy objectives defined, and intends that the obtained benefits be passed to the final users.*
16. *Access criteria (entry, exit and exclusion) will be clearly defined. Tiered arrangements through indirect participation will be considered to allow the reduction of manual procedures.*
17. *User Groups (i.e. groups of system participants to discuss system development issues) will be introduced and new participants will be incorporated. The BOJ in the context of its transparency policy will publish the operating rules of the system.*
18. *The RTGS system will be integrated safely and efficiently with straight through processing with other systems. The RTGS system will be used for settlement of retail systems and appropriate interfaces will be implemented. The RTGS system will be integrated with all securities settlement systems to achieve DVP. Some interfaces with trading platforms both for the securities market and the interbank market will be designed to guarantee efficient liquidity management for financial institutions.*
19. *The BOJ will adopt the necessary measures to reduce the systemic importance of the cheque clearinghouse. Other systemically important payment systems could*

*be introduced in Jamaica by the private sector, provided that they meet fully the CPSS Core Principles and have been authorized by the BOJ in the context of the payment system oversight function (see Pillar VII).*

**Pillar III: Interbank Money Markets are fully developed and closely integrated with settlement systems**

20. *The interbank money market is an important element for liquidity management and enhancements of these systems should run in parallel with those of settlement systems. Procedures, settlement cycles, and operating hours will be designed to maximize the benefits. The legal, regulatory and oversight framework will be strengthened in order to create the conditions for interbank money market development. The BOJ has adopted and will continue to adopt the necessary measures to strengthen the interbank money market.*

**Pillar IV: Retail payment systems are efficient, sound and interoperable and support the offer of a wide range of payment instruments and services**

21. *The BOJ will continue to play a role in retail systems as settlement agent, participant, overseer and as catalyst for change. The overall objective is to provide the Jamaican economy with a wide range of safe and efficient payment services.*
22. *The existing ACH is designed to operate efficiently and facilitate the move towards electronic credit and debit instruments and will thereby reduce the systemic importance of cheques.*
23. *Financial risks in the ACH will be minimized by removing proactively all large value items from the cheque clearinghouse and, eventually some forms of guarantee will be introduced. The establishment of settlement assurance procedures and its associated costs should be evaluated in terms of the level of “systemic importance” of the ACH. These procedures can also be used as an incentive mechanism to move large value payments out of the cheque clearing system.*
24. *The BOJ has co-ordinated the establishment of the rules and regulations for the ACH. In particular, the following items are covered: i) definition and characteristics of the system(s); ii) operational instructions; iii) responsibilities of the clearinghouse and system participants; iv) controls to be performed, v) message structures; vi) contingency arrangements; vii) interchange commissions; viii) conflict resolution procedures, etc.*
25. *The system operator is required to maintain dialogue with the major stakeholders, through the creation of User Groups.*

26. *Other financial or non-financial entities may operate retail systems or provide retail payment services. All retail systems will be overseen by the BOJ (see Pillar VII) in terms of their safety and efficiency, with appropriate instruments depending on the level of risk they introduce in the financial system.*
27. *All retail circuits must be characterized by a high degree of interoperability (e.g. EFTPOS) and high efficiency in terms of their clearing cycles. The BOJ supports the use of central bank money<sup>2</sup> for the settlement not only of large value systems, but also of retail systems.*
28. *Pricing policies for retail circuits are formulated in a way that takes into account the principle that costs are borne in proportion to the benefits accrued, and in keeping with efficiency enhancement objectives. The BOJ will review the cost recovery pricing policy to make it consistent with the general policy objectives defined and intends that the obtained benefits be passed to the final users.*
29. *Effective fraud prevention and detection measures are in place for all retail systems and fraud occurrences in all payment flows are acceptably low. An important objective will be to establish appropriate mechanisms for customer protection for all the systems.*

**Pillar V: Government collections and disbursements are fully and efficiently integrated with the National Payment System and support its smooth functioning**

30. *The current system for government payments will be strengthened. The bulk of collections and disbursements by the government sector will be executed electronically using the current and envisaged systems. This is to ensure that all the benefits of the payments reform accrue to all segments of the economy through increased efficiency in the payments flow as lower idle resources will be maintained in bank accounts. The cost reduction and efficiency gains for government payments are a significant objective of the reform effort, that itself facilitates cost recovery in a shorter time frame.*

**Pillar VI: Securities Clearance, Settlement and Depository Systems are safe and efficient, fully comply with international standards, and contribute to support the development of capital markets**

---

<sup>2</sup> This includes funds and assets held in accounts at the Bank of Jamaica.

31. *Securities Settlement Systems in Jamaica will comply with the CPSS-IOSCO Recommendations for Securities Settlement Systems.<sup>3</sup> The BOJ and FSC are committed to this objective.*
32. *The settlement of securities and funds will be linked to allow securities transactions to be settled on a DVP basis, thus eliminating principal risk.*
33. *The BOJ strongly favors the use of central bank money for settlement of securities transactions as the most effective way to eliminate risk. Instruments used to settle the cash leg of securities transactions between CSD members will carry little or no credit or liquidity risk. Cheques will be eliminated as a method for settlement of securities markets transactions.*
34. *All securities will be issued in book-entry form.*
35. *Improvement of custody arrangements will be a key objective of the reform in order to enhance the development of a secondary market for public debt. The BOJ, FSC and the Ministry of Finance and Planning will make sure that these efforts are accompanied by an adequate legal, regulatory and supervisory framework. **The operations of the depository will be subject to the regulatory and supervisory powers of the FSC in exercise of its functions under the Securities Act.***
36. *The regulatory and oversight framework for securities settlement **systems** will be integrated and strengthened. The BOJ and FSC will cooperate in the oversight of the securities settlement systems. This will be done through a framework for cooperation (e.g. a Memorandum of Understanding) or other formal agreement between the parties. (see Pillar VII below)..*
37. *Governance arrangements for depositories need to permit fair open access, provide market participants with sufficient information for them to accurately identify and evaluate the associated risks and costs. A strong, capitalized, autonomous and independent depository, with reliable and flexible systems to expedite settlement of transactions and accessory rights is crucial for the development of the secondary market.*

**Pillar VII: The oversight and supervisory framework for payments and securities settlement systems is clearly defined, and the BOJ exercises effectively its oversight authority in cooperation with other regulators and supervisors**

---

<sup>3</sup> 30 core principles of securities regulation are set out in the IOSCO Objectives and Principles of Securities Regulation.

38. *The BOJ will function as payment system overseer in Jamaica.*
39. *The BOJ will have clear legislative authority for the oversight of clearance and settlement systems. The law will provide the BOJ with the legal authority to ensure the development and operation of payment mechanisms that effectively contribute to the integrity, efficiency and safety of the financial system and the effective implementation of monetary policy.*
40. *The BOJ will disclose publicly its objectives and policies relating to all significant payment system matters along with its implementation strategies.*
41. *With regard to policy objectives, the BOJ will seek to achieve efficiency and reliability for all systems. The BOJ will also promote competition in the payment services market and the protection of consumer interests in coordination with other regulators (such as the FSC). The BOJ supports the establishment of an Ombudsman<sup>4</sup> for the financial services industry.*
42. *With regard to the scope of BOJ oversight, the Bank's role will encompass both systemically important and retail systems, since the latter are especially important in supporting economic activity and the public trust in money.*
43. *The BOJ in exercising its oversight role will have the ability to carry out this function effectively. To this end, the BOJ will :*
- i) establish appropriate organizational arrangements and staffing; The oversight function will be assigned to a Department within the BOJ separated from the Departments in charge of operating the systems;*
  - ii) ensure that an adequate degree of participant co-operation exists and is sufficient to promote and realize the desired organizational and operational arrangements;*
  - iii) verify that individual payment systems satisfy user needs as well as risk and efficiency requirements through appropriate interventions both at the development stage and during the on-going system implementation and operational phases;*
  - iv) define and implement appropriate actions should participants not comply with published rules and regulations (e.g. the application of pre-determined penalties and sanctions for compliance failures);*
  - v) collect and distribute relevant statistical information to demonstrate the use being made of each system and the extent to which the systems are satisfying end-user and other market needs. Information and public policy statements relating to all substantial payment system matters will be disclosed in a manner that assures wide dissemination among payment system stakeholders.*

---

<sup>4</sup> The Ombudsman will act as an advocate for the citizenry by investigating and addressing complaints against the financial services industry.

44. *The BOJ will continue to be a direct provider of clearing and settlement services. In regard to such services, care will be taken to ensure that appropriate service and performance levels are routinely achieved and adequately cover all critical safety and efficiency requirements. To this end, the BOJ will continuously review and seek to improve the design and operation of the systems it operates.*
45. *The BOJ and the FSC will evaluate, identify, and implement procedure and process changes to address any weaknesses or inconsistencies in the regulatory arrangements and ensure a high level of co-operation in the way that policies are implemented. Joint task forces will be created to address problems of common interest and appropriate memoranda of understanding between regulators and supervisors will be prepared and observed.*

**Pillar VIII: Effective and structured cooperation is in place within the NPS**

46. *In light of the above considerations, a Payments Council has been created in Jamaica under the leadership of the BOJ. This body includes representatives from all major stakeholders with an interest in payments and securities clearance and settlement systems improvements and will be an extremely useful tool to secure constructive dialogue between regulators and market participants. Terms of Reference for the Payments Council have been agreed with its members.*
47. *The Communication Strategy for the reform objectives and policies and for any issues related to the payments and securities settlement systems, as well as the different roles to be played by Council members in this effort, are being defined cooperatively.*

## **GLOSSARY**

<b>Term</b>	<b>Definition</b>
BIS	Bank for International Settlements, an international organization which fosters cooperation among central banks and other agencies in pursuit of monetary and financial stability.
CIFTS	Customer Inquiry and Funds Transfer System, a funds transfer system owned and operated by the Bank of Jamaica.
CPSS	Committee on Payment and Settlement Systems, made up of the central banks of the Group of Ten Countries.
DVP	Delivery versus Payment, simultaneous book-entry transfer of securities and cash.
EFTPOS	Electric Funds Transfer at Point of Sale
FSC	Financial Services Commission, regulates securities, insurance and pension industries.
IOSCO	International Organization of Securities Commissions