



**The Western Hemisphere Payments &  
Securities Clearance and Settlement Initiative  
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**Status Report on the WHI: Improving  
Payments and Securities Arrangements in LAC**



**Massimo Cirasino, World Bank  
Mario Guadamillas, World Bank**



**José Antonio García, CEMLA**

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**Part A. Presentation to the LAC  
central banks Governors in their  
meeting in Seville, May 2003  
(In Spanish)**

**Part B. Recommendations for  
improving payments systems  
from WHI missions (follow-up of  
last year presentation)**

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# Content Part B



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## A.1 Origen, Pilares y Estructura Organizativa



### •Origen de la Iniciativa: 1998

### •Pilares:

OBJETIVO: Evaluar, recomendar e implementar mejoras en los sistemas de compensación y liquidación de valores



Integración pagos y valores



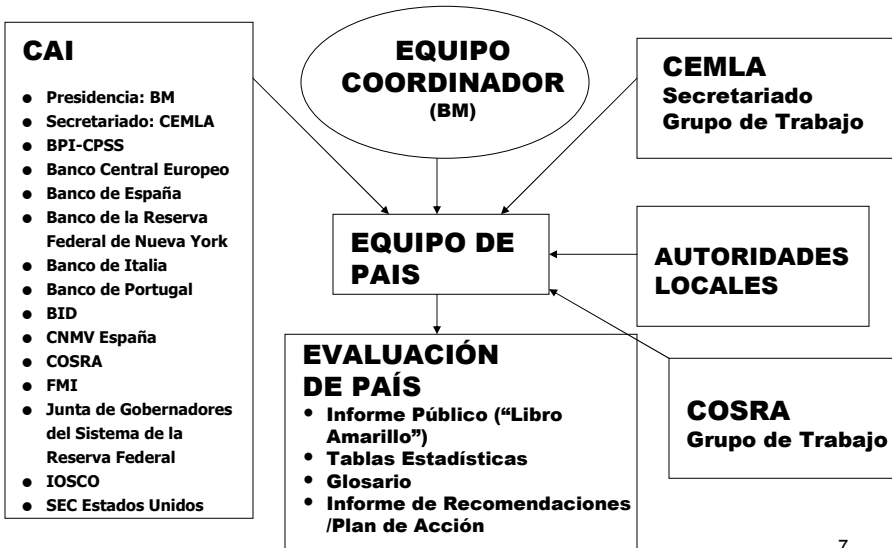
Cooperación con organismos internacionales



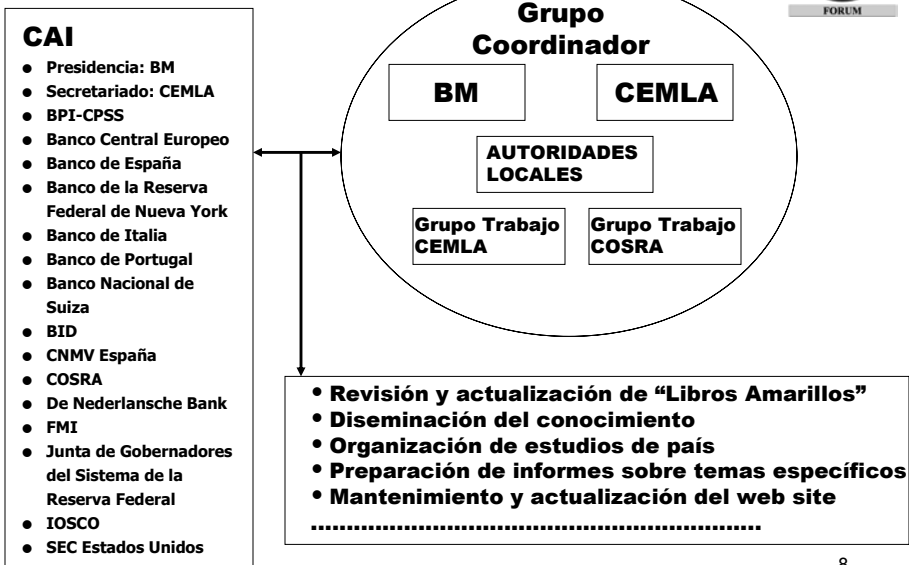
Apoyo e implicación de autoridades locales

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## A.1 Antigua Estructura Organizativa: La Iniciativa



## A.1 Nueva Estructura Organizativa: El Foro



## A.2 Actividades/Fase I



### • Fase I (Preparatoria), Marzo 1998 a Marzo 1999:

- **Contactos con países y miembros del CAI**
- **Elaboración de herramientas metodológicas (índice, estadísticas, metodologías de evaluación, etc.)**
- **Taller de lanzamiento, Enero 1999**
- **Primera Reunión del CAI, Marzo 1999**

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## A.2 Actividades/Fase II



### • Fase II, Marzo 1999 a Junio 2001:

- **Semana Pagos y Reuniones del CAI, Noviembre 1999 y Enero 2001**
- **Formación Grupo Trabajo de Valores, Diciembre 1999**
- **Formación Grupo de Trabajo Pagos, Enero 2001**
- **Evaluaciones 10 Países Iniciales: Perú (Junio 1999), Argentina (Julio 1999), Chile (Diciembre 1999), Trinidad y Tobago (Febrero 2000), El Salvador (Junio 1999), OECS (Abril 2000), Brasil (Noviembre 2000), Colombia (Febrero 2001), México (Marzo 2001), y Costa Rica (Junio 2001)**
- **Talleres específicos: Argentina (Julio 1999 junto con CPSS Task Force), Trinidad y Tobago (Febrero 2000), ECCB (Abril 2000), Brasil (Noviembre 2000), CEMLA-WB (Enero 2001)**
- **Herramientas: web site ([www.ipho-whpi.org](http://www.ipho-whpi.org)), matrices de evaluación, documentos de trabajo 1 a 4, grupos de trabajo TOR**

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## A.2 Actividades/Fase III



### • Fase III, Junio 2001 a Junio 2003:

- **Semana de Pagos y Reuniones del CAI, Abril 2002 y Junio 2003**
- **Grupo Trabajo de Valores, Octubre 2001, Febrero 2002, Marzo 2003**
- **Grupo de Trabajo Pagos, Noviembre 2001, Abril 2002, Noviembre 2002, Junio 2003**
- **Evaluaciones solicitadas por países: Bahamas (Marzo 2002), Jamaica (Junio 2002), Ecuador (Agosto 2002), Venezuela (Noviembre 2002), Antillas Holandesas (Diciembre 2002), República Dominicana (Enero 2003)**
- **Otras actividades relacionadas: Barbados (2002), Nicaragua (Octubre 2002), Honduras (Marzo 2003)**
- **Talleres específicos: Bahamas (Marzo 2002), Cartagena (Noviembre 2001), CEMLA-WB (Abril 2002)**
- **Herramientas: adaptación a estándares internacionales, uso del BM-FMI *Guidance Note*, serie de artículos de investigación**

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## A.2 Actividades Futuras/El Foro



- **Demanda de países adicionales: Uruguay, Guatemala, Paraguay, Nicaragua, Bolivia, etc.**
- **Tareas grupo de trabajo de pagos**
  - **Actualización “Libros Amarillos”**
  - **Ejercicio de autoevaluación de los Principios Básicos**
  - **Creación y actualización de estadísticas**
  - **Estudio de temas específicos relevantes para la Región**
  - **Coordinación con grupo de trabajo de valores**
- **Reuniones del CAI**
- **Potenciaamiento de actividades de formación e investigación**

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### A.3 Disponibilidad “Libros Amarillos”



<b>Perú (Inglés y Español)</b>	<b>2000</b>
<b>Argentina (Inglés y Español)</b>	<b>2000</b>
<b>Trinidad y Tobago (Inglés y Español)</b>	<b>2000</b>
<b>El Salvador (Inglés)</b>	<b>2000</b>
<b>Chile (Inglés y Español)</b>	<b>2001</b>
<b>Colombia (Inglés y Español)</b>	<b>2001</b>
<b>Costa Rica (Inglés y Español)</b>	<b>2002</b>
<b>Brasil (Inglés y Portugués)</b>	<b>2003</b>
<b>México (Inglés y Español)</b>	<b>2003</b>
<b>OECS (Inglés y Español)</b>	<b>2003</b>
<b>Ecuador (Inglés y Español)</b>	<b>2003</b>
<b>Venezuela (Inglés y Español)</b>	<b>2003</b>
<b>República Dominicana (Inglés y Español)</b>	<b>2003</b>

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### A.3 Participación miembros del CAI



<b>Peru</b>	<b>Banco de España, CNMV España, BID</b>
<b>Argentina</b>	<b>Banco de Italia, Fed NY, CNMV España, BID</b>
<b>Chile</b>	<b>CNMV España, BID</b>
<b>El Salvador*</b>	<b>COSRA (CONASEV Peru)</b>
<b>Trinidad &amp; Tobago</b>	<b>Banco de Italia, CEMLA (Banco de las Antillas Holandesas) COSRA (CMV Argentina), Fed, SEC EE.UU.</b>
<b>OECS</b>	<b>Banco de Italia, CEMLA (Banco de las Antillas Holandesas), Banco Nacional de Suiza</b>
<b>Brazil</b>	<b>Banco de Italia, Banco de Portugal, Junta Gobernadores Fed, SEC EE.UU.</b>
<b>Colombia</b>	<b>Banco de Italia, CEMLA, CNMV España</b>
<b>Mexico*</b>	<b>Banco de España, CNMV España</b>
<b>Costa Rica</b>	<b>de Nederlansche Bank, Banco Nacional de Suiza</b>
<b>Jamaica</b>	<b>Banco Nacional de Suiza, SEC EE.UU.</b>
<b>Ecuador</b>	<b>de Nederlansche Bank</b>
<b>Venezuela</b>	<b>Banco de España, CNMV España</b>
<b>Antillas Holandesas</b>	<b>de Nederlansche Bank</b>
<b>República Dominicana</b>	<b>Banco Nacional de Suiza</b>

\* Coordinado con el FSAP

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## A.4 Resultados



- **Impulso a la implementación de reformas**
- **Mejora en la información sobre la infraestructura financiera de la Región (“Libros Amarillos”)**
- **Foro anual para debatir los temas de sistema de pagos (“Semana de Pagos”)**
- **Creación de una base común para un proceso potencial de armonización futura**
- **En definitiva, mejoras en:**
  - **Seguridad (reducción de riesgos de principal, liquidez, sistémicos y operativos) y eficiencia de los sistemas**
  - **Marco legal y regulatorio**
  - **Función de vigilancia**
  - **Arreglos de cooperación**

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## A.4 Resultados



- **Diagnósticos precisos a un coste reducido por acceso a expertos internacionales**
- **Fortalecimiento del Secretariado**
- **Establecimiento de los grupos de trabajo para dar continuidad al proyecto**
- **Coordinación con FSAPs (México, Costa Rica, Brasil, Ecuador, Bolivia)**
- **Coordinación con asistencia técnica del Banco Mundial (Barbados, Bahamas, El Salvador, Trinidad y Tobago, Venezuela, Honduras y Ecuador)**
- **Desarrollo de herramientas metodológicas**

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## A.4 Factores de éxito



- **Mandato de alto nivel**
- **Estructura organizativa basada en la cooperación que ha permitido la conjunción de esfuerzos**
- **Enfoque coordinado de pagos y valores**
- **Implicación e iniciativa de las autoridades locales y regionales**
- **Trabajo en base a demanda y orientado hacia las reformas**

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## A.5 Réplica del Modelo



- **Importancia del *partnership* y cooperación entre instituciones**
- **Otras áreas en la Región (CEMLA)**
  - **Información crediticia**
  - **Estándarización contable**
  - **Desarrollo de mercados de títulos públicos**
- **Contactos en el Banco Mundial para otras Regiones**
  - **MENA**
  - **ECA**
- **Fuentes alternativas de recursos a explorar (FIRST, etc.)**

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## **B.1 Payments: Overall Reform**



- Status: Many countries in the region have implemented or are in the process of implementing reforms of the payments system. However, in many cases the reform has not been conducted or designed following a strategic approach
- Public authorities, in cooperation with all stakeholders, should formulate a medium-long term vision strategy for a payments and securities settlement system reform, incorporating improvements in all aspects (legal, regulatory, operational, oversight, etc.)
- In conducting a reform the logical sequencing process would be: i) diagnostic, stocktaking, situational analysis; ii) vision development; iii) conceptual design and implementation planning; iv) user requirement specifications; v) acquisition, procurement development, testing, implementation

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## **B.1 Payments: legal framework**



- Status: In many countries, the legal framework for payments and securities settlement still presents important deficiencies.
- Pending legal issues should be addressed as a priority by the authorities. Typical shortfalls include: the definition of finality, protection of the systems against bankruptcy procedures, improvement of the legal basis for custody arrangements, legal basis for netting arrangements, and the regulation of oversight powers of the central bank.
- In many countries, external assistance might be considered to determine the scope of the reform of the legal framework.

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## **B.1 Payments: systemically important payments systems (SIPS)**



### Status

- In many countries, SIPS have been designed following the CPSS Core Principles for SIPS.
- However, in some cases, some important issues have not been assessed properly
- Apart from the legal issues presented above, other typical shortfalls include:
  - Risk control management are weak: no sufficient provision of intra-day liquidity; no optimal integration with securities settlement systems; no or insufficient guarantee schemes for systems based on netting

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## **B.1 Payments: systemically important payments systems (SIPS)**



### Status

- Operational reliability and business continuity measures might be insufficient in light of recent debate on the issue
- Too many large value payments are still processed in relatively risky systems (especially cheque systems)
- Access is restricted to few participants without disclosure of risk considerations. Exit criteria are uncertain
- Governance arrangements are not transparent and system participants do not have appropriate fora to express their needs

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## **B.1 Payments: systemically important payments systems (SIPS)**



**The central bank and other authorities should push to achieve full observance with the Core Principles of their SIPS**

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## **B.1 Payments: retail systems**



### Status

- Despite the existence of an electronic funds transfer system, cheques are still often used as an instrument for the exchange of large value interbank payments.
- In some cases, cheques are not standardized and are, therefore, processed with cumbersome procedures
- In many countries retail systems are characterized by a low degree of interoperability
- In most of the countries, payment instruments are used in a sub-optimal way, from the efficiency point of view

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## **B.1 Payments: retail systems**



- Authorities and stakeholders should assess all pending issues in the retail sector as a matter of urgency and move rapidly toward the implementation of more efficient arrangements and create incentive for the use of more efficient payment instruments
- From the central bank's perspective, many central banks do not fully perform all the minimum actions indicated in the CPSS Report "Policy Issues for Central Banks in Retail Payments". Therefore, it is recommended that they address as a matter of urgency all policy implications for the safety and efficiency of the retail system in their countries, including the possibility to perform some of the additional actions indicated in the Report

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## **B.1 Payments: government payments**



- Status: In many countries government payments are processed in a less than efficient way and have several negative implications for the payments system as a whole
- It is strongly recommended that collection and disbursements of the public sector be processed electronically and timely through current and envisaged automated systems. This is to ensure that all the benefits of the on going payments reform be accrued by all segments in the country. It must be noted that, in many cases, the gains in efficiency and cost reductions for government payments have been the main result of the reform effort, being able to recover the initial investment in a very short time-span

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## **B.1 Payments: government payments**



- It is suggested that the Ministries of Finance and the central banks coordinate more closely in the field, especially in this moment of reform in the payments system infrastructure in the country. Among other things, enhanced cooperation could lead to a higher level in the use of banking services for the public in general. The afore mentioned cooperation efforts should also focus in a level playing field in the treatment of the different payment instruments, specially avoiding any measure promoting the use of cash and cheques
- A plan of government disbursements and government securities related payments is announced weekly. Timely and efficient enforcement of announced payments by the government should occur early in the operating day. This would have a very positive impact on the intra-day liquidity management of financial institutions, especially in absence of alternative liquidity facilities provided by the central bank

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## **B.1 Payments: transparency**



- Status: In many cases, conditions applied to payment services are not transparent nor is it clear to the stakeholders and the public the policies pursued by authorities
- In performing the oversight function and as system operator, the central bank should ensure that transparency of policies and conditions for payment services offered be available to the population at all times. Banks and other financial institutions should be forced to provide information to the public on the services they offer in the payments system and the general public should be able to resort to a bank's Ombudsman and/or to the central bank and/or the consumers' protection agencies for resolution of conflicts related to payment services.
- In performing the oversight function, the central bank should ensure its policies are transparent and publicly disclosed

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## **B.1 Payments: FX and cross-border settlement**



- Status: Financial risks are present in foreign exchange trading and settlement in the Region. In particular, in some countries, true PvP is not achieved in the vast majority of foreign exchange transactions
- The central bank should investigate the possibility of introducing some measures to mitigate the risks associated to these operations when PvP is not possible. The central bank might consider evaluating the risks in this market taking as a reference the reports and questionnaires published by the CPSS of the BIS. Also, central banks might want to investigate emerging models of clearinghouses for domestic foreign exchange transactions (e.g. in Brazil)
- Status: In many countries, cross-border retail payments are costly and not adequately regulated
- Authorities should take action in this field as a matter of urgency

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## **B.1 Payments: interbank money market**



- Status: In many countries, interbank money markets are not deep since they are characterized by the heavy use of bilateral and OTC unregulated arrangements
- The interbank money market is an important element for the liquidity management and improvements in some elements of the payment systems could further strengthen this market. Procedures, settlement cycles, and operating hours might have to be modified in order to obtain maximum gains from development of the systems at the central bank. The legal, regulatory and oversight framework should be strengthened in order to create the conditions for interbank money market development that is crucial for liquidity management

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## **B.1 Payments: Oversight**



- Status: Many central banks are in the process of strengthening their oversight function. Typical open issues to be addressed include:
- The central bank should seek clear legislative authority for the oversight of clearance and settlement systems. Secondary legislation (bylaws, circulars, etc.) should be implemented to ensure that this oversight function is done in such a way that contributes to the development and operation of payment mechanisms that effectively contribute to the integrity, efficiency and safety of all financial markets and the operation of monetary policy

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## **B.1 Payments: Oversight**



- In the context of establishing the oversight function, the central bank should disclose publicly its implementation strategies to achieve its objectives relating to all significant payment system matters. With regard to policy objectives, it is suggested that consideration be given to a broadening of scope beyond the two traditional main objectives of efficiency and reliability to a wider set of issues including the promotion of competition in the payment services market and the protection of consumer interests. These objectives might be pursued by the central bank, as overseer on the payment system, especially in those cases not embraced by other regulatory or supervisory authorities

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## **B.1 Payments: Oversight**



- With regard to the scope of its oversight role, it is recommended to that the central bank oversight authority be applied over both systemically important and retail systems (both handling domestic and cross-border transactions), since the latter are especially important in supporting economic activity and the public trust in money
- The central bank in exercising its oversight role should have the ability to carry out this function effectively. To this end, the BCV should:
  - i) establish appropriate organizational arrangements and staffing. This includes forming a small unit of people in charge of payments system oversight to be separated to the extent possible from the units in charge of operating the systems offered by the central bank. Skills of human resources involved in the function should be as wide as possible and include legal, operational and technical expertise as well as policy and economics.

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## **B.1 Payments: Oversight**



- ii) ensuring that an adequate degree of participant co-operation exists and is sufficient to promote and realize the desired organizational and operational arrangements (see below);
- iii) verifying 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) defining and implementing appropriate actions should participants not comply with published rules and regulations (e.g. the application of pre-determined penalties and sanctions for compliance failures)

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## **B.1 Payments: Oversight**



v) collecting and distributing 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 could be disclosed in a manner that assures wide dissemination among payment system stakeholders (for example in a payment system chapter of the annual report or other appropriate publication)

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## **B.1 Payments: Cooperation**



- Status: In many countries cooperation (among authorities, between authorities and stakeholders, and among stakeholders) is largely insufficient
- Authorities should evaluate, identify, and implement procedure and process changes to address any weaknesses or inconsistencies in the regulatory arrangements and assure a high level of co-operation in the way that policies are implemented. Consideration should be given to the need for joint task forces to address problems of common interest and/or the preparation of appropriate memoranda of understanding
- In absence of cooperative arrangements, it is recommended that the central bank take the lead in forming a formal Payment System Council. This body should include representatives from all major stakeholders with an interest in payments and securities clearance and settlement systems improvements and should be used as the main tool also to secure a constructive dialogue between regulators and market participants

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## **B.2 Securities: legal issues**



- Finality must be integrated in the legal framework
- Systems with more advance legal frameworks still present a potential impact on settlement finality because of bankruptcy procedures that apply the cancellation of fraudulent transactions up to certain days before the participant is declared failed. Initiatives to engage the judicial system in this debate is worth pursuing to clarify the issue
- The fragmentation of regulations of wide legal rank and hierarchy relating to securities and capital markets is common in the Region. A unified payments system law, which systematizes all existing provisions in the field might help resolving the potential conflicts of interpretation on issues such as finality and oversight
- Introduce legal basis for multilateral netting schemes

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## **B.2 Securities: legal issues**



- Establish clearly the priority of securities settlement systems over assets corresponding to the principal of the transaction
- Repos definition (normally only sell and buy back) makes difficult to implement margin calls. Define in the SML the scope of repos so that it is clear that this implies not only sell and buy backs but a much broader range of instruments in line with best market practices
- Decrees, resolutions and releases must develop the timing of the dematerialization and immobilization procedures
- Many countries laws do not contain explicit conflicts of law rules. This could hamper the development of interregional financial markets and international co-operation in the area of trading, custody and clearing and settlement

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## **B.2 Securities: clearing and settlement processes**



- Confirmation of trades between securities markets and SSSs or CSDs must take place not later than T+0
- Blocking of transactions previous to matching avoid arbitration. More orthodox risk management tools should be used in order to avoid the rigidity introduced by this mechanism
- Standardization of settlement cycles for same type of securities
- Extensions of the established settlement cycle should be avoided

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## **B.2 Securities: clearing and settlement processes**



- A gradual implementation of Straight Through Processing (STP) in order to reduce operational risk
- The efficiency of the several current ways to cope with securities shortages should be evaluated vis-à-vis standardized forms of securities lending
- If short selling is permitted, the securities regulator must be alert against market manipulation

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## B.2 Securities: settlement risk



- Still some systems do not settle on a DvP basis, implement it as a matter of urgency
- Imperfection of Delivery versus Payment procedures. One reason behind these settlement arrangements is lack of standardization
- Currently in some of the net settlement systems risk management mechanisms are not in place in order to achieve timely settlement under all circumstances. Sometimes there is only a symbolic guarantee fund and neither a system for securities lending and borrowing is in place, nor are sufficient credit lines contracted by the Stock Exchange in order to deal with liquidity risk on the securities side as well as on the cash side. Upgrade risk management tools
- Brokers act as clearance and settlement institutions without enough capital requirements. Apply and enforce adequate capital requirements

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## B.2 Securities: settlement risk



- Lack of a specific supervision of the settlement bank. In addition, lack of coordination between regulators on this aspect increases the concern. The authorities should explore different alternatives in terms of the assets used to settle and, if the current situation is maintained, the adequate regulatory and supervisory mechanisms should be in place
- Avoid the use of cheques for funds settlement, still use in some cases although with a clear downward trend
- Improve liquidity distribution for the securities transactions cash settlement leg as normally securities intermediaries do not have easy access to liquidity or they have it at a very high cost

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## **B.2 Securities: operational risk**



- In many cases back-ups are missing or in the process of being implemented. They should be in place the earliest possible in order to cover any contingency in the system
- External auditing of the services provided should be considered in order to assess the cost- efficiency of the systems
- The efficiency of the present infrastructure is insufficient and needs to be improved

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## **B.2 Securities: custody risk**



- For securities represented by means of title, in case of a bankruptcy, realization of the pledged securities cannot take place without a court order. Eliminate handling of physical securities
- The securities regulator must ensure that all customer assets are appropriately accounted for, and that customer's holdings of securities are actually being registered in the client's omnibus accounts at the depository
- Although on an operational basis segregation is used, customer's assets might not be clearly protected, from a legal point of view, against the claims of depositor's creditors. In this context is even more important an adequate supervision of participant's registers in which final beneficiaries are identified

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## **B.2 Securities: regulatory and oversight issues**



- Although there have been efforts in order to harmonize the regulations, there is overlap in relation to different markets for the same jurisdiction
- Potential conflicts between the roles of the central banks as operators and overseers of securities settlement systems should be addressed by appropriate internal organizational arrangements
- The capacity of the securities regulators of the Region should be strengthened as a matter of urgency
- The securities regulator must oversee more closely the SRO role of the stock exchange. For example, make sure that necessary modifications of the Stock Exchange and depository internal rules and regulations are introduced, and that such regulations are timely updated

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## **B.2 Securities: regulatory and oversight issues**



- The oversight empowerment for securities settlement systems is missing in some cases. It should be implemented as a matter of urgency
- A forum should be established in order to institutionalize the cooperation in securities settlement and payment systems.
- Securities regulators should in co-operation with central banks develop a policy framework for the oversight of clearing and settlement systems for securities and disclose this to the market in order to guide the development of proper risk management measures by the stock exchange. The securities regulators should build up knowledge and skills to assess clearing and settlement systems

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## **B.2 Securities: CSDs organizational arrangements**



- In general, governance structure are adequate. However, in some cases it is not clear whether it prevents any potential conflict of interests between the clearinghouse and the exchange. This issue should be addressed by the oversight authorities
- Some legal and governance arrangements introduce monopolistic situations that impede the adequate development of some markets (e.g., money market) The authorities should address this issue as a matter of urgency and agree with the private sector a cooperative solution
- The authorities should consider whether the current capital requirements for brokerage houses are in line with their activities

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## **B.2 Securities: CSDs organizational arrangements**



- 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. This is particularly important if new issues of public debt are to be deposited
- The depository should provide participants with a meaningful opportunity to participate in the organization's decision making process for system design and settlement procedures, among others
- The depository should publicly disclose its procedures and access criteria, in order to permit a fair and open access

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## **B.2 Securities: cross-border settlement**



- Normally, not significant involvement on cross-border settlement
- The main improvement in this area is related to the international law governing the cross-border pledge of securities as collateral. Some depositories have been participating in the Hague Convention efforts in order to build a consensual internationally accepted principle on this issue but they believe that market participants and mainly clearing and settlement systems were not yet involved the way it would be advisable. Some securities regulators are already involved in this discussion