Enhancing Competition and Reducing Costs in the Remittance Industry: The General Principles for International Remittance Services

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Overview

- Remittances as payments
- The CPSS-WB general principles
- Implementing the General Principles

Remittances as payments

Remittances as a payment system issue

- *KEY IDEA: Remittance services are part of the broader retail payment systems - both domestic and cross-border*
  - Remittances are cross-border retail payments with particular access requirements (on both the demand and supply sides)
- An efficient domestic payment system infrastructure is key to reduce costs of remittance services, especially in receiving countries
- The development of payment system oversight is fundamental to enhance transparency and improve efficiency in the retail payment sector

Additional key ideas

- Remittances are part of an individual's access to financial services
- A good remittance product improves value to the user in the short term and access to other financial products in the long term
- A good remittance product increases competition and could move transactions to the formal sector
- There are no standard solutions

Definition

An international remittance is a cross-border, person-to-person payment of relatively low value

- Typically by migrant workers to their families. Especially from developed to developing countries
- Person-to person, low value - ie not commercial or wholesale
- Domestic remittances also exist
- Recurrent - but typically made by individual transfers (eg not by standing order)
- Typically credit transfers
- For remittance service providers (RSPs), often indistinguishable from any other retail cross-border transfers

Key problems

Focus here is on *payment system* aspects (not developmental, immigration, balance-of-payments or other aspects)

- Usually expensive
- Sometimes slow
- Sometimes inconvenient
- Occasionally unreliable

As part of the 2004 “Sea Island” remittance initiative, the G8 Finance Ministers and Central Bank Governors called for work toward developing prudential standards or guidelines for remittance services.

The General Principles

The thinking behind the principles

- Premise is that best way to reduce cost is to have competition as far as possible
- The principles are *not* a call for remittances to be regulated. Sometimes it may be more important to remove existing regulation
- They do *not* aim to set specific service levels. Low price may often be more important than high level of service
- Purpose is to tackle weaknesses in the market that inhibit competition (including poor regulation)

GP1: Transparency and consumer protection

The market for remittances should be transparent and have adequate consumer protection

- Transparency means information about the service (price, speed etc). Transparency promotes competition and should drive down prices
- Specially important for remittances:
  - "Access" problems for users
  - Complex to work out price
- What is appropriate consumer protection? Most important are probably "error resolution" procedures (RSPs' own or national schemes). Beware of the cost of some possibilities!

Some possible actions re GP1

- Transparency requirements for individual RSPs *where feasible*?
- Encourage information in key foreign language?
- Encourage use of reference exchange rate?
- Publish comparative price information?
- Background understanding: financial literacy campaigns?

GP2: Payment system infrastructure

Improvements to payment system infrastructure that have the potential to increase the efficiency of remittance services should be encouraged

Domestic payment infrastructure.

- Remittance services usually depend to some extent on this. But the infrastructure may not always be very efficient, especially in receiving countries.

Cross-border payment infrastructure.

- Greater standardisation to help STP in correspondent banking?
- Direct links between domestic systems as an alternative to correspondent banking?

Some possible actions re GP2

- Overall development of domestic payment infrastructure: central banks can facilitate?
- Encourage increased interoperability of electronic networks?
- Postal services to play bigger role?
- Link domestic ACHs across borders?

GP3: Legal regulatory environment

Remittance services should be supported by a sound, predictable, non-discriminatory and proportionate legal and regulatory framework

- Does *not* mean special laws/regulations for remittances
- Sound, predictable, non-discriminatory ...
- ... and proportionate! Avoid danger of over-regulation. What is the problem regulation is meant to cure? Is regulation the best way to cure it?
- For key corridors, sending and receiving countries may want to cooperate if there seem to be legal obstacles

Some possible actions re GP3

- Check what is really necessary and useful
- Check in particular:
  - Different types of RSPs treated equivalently?
  - Do you need prudential requirements?
  - Nature of registration/licensing requirements?
  - Nature of reporting requirements?
  - What sort of customer ID is acceptable?
- Consult RSPs before changing!

GP4: Market structure and competition

Competitive market conditions, including appropriate access to domestic payments infrastructures, should be fostered in the remittance service industry

- Importance of contestability and removing barriers to entry
- Avoid exclusivity *conditions* (as opposed to an agent *choosing* to offer only one remittance service)
- Are there problems with direct or indirect access to domestic payment systems?

Some possible actions re GP4

- Central banks, supervisors etc could work with competition authorities to ensure consistent approaches?
- Discourage exclusivity conditions?
- Help improve potential RSPs' awareness of the market?
- Check whether direct and indirect access conditions are consistent with safety requirements and not unnecessarily anti-competitive?

GP5: Governance and risk management

Remittance services should be supported by appropriate governance and risk management practices

- RSPs face financial risk (eg if liquidity is supplied to disbursing agents), legal risk, operational risk, risk of fraud, reputational risk
- Good governance and risk management practices by RSPs make remittance services safer and help protect consumers ...
- ... but there is unlikely to be any systemic risk so protection measures should be proportionate to the risks

Some possible actions re GP5

- Remittance industry to develop guidelines for good governance and risk management?
- Authorities to give guidance on how to meet AML/CFT requirements in an effective and appropriate way?

Who should take action?

Many people may need to take action. But RSPs and the authorities have particularly important roles:

- Role A: RSPs should participate actively in the application of the general principles
- Role B: Public authorities should evaluate what action to take to achieve the public policy objectives through implementation of the general principles

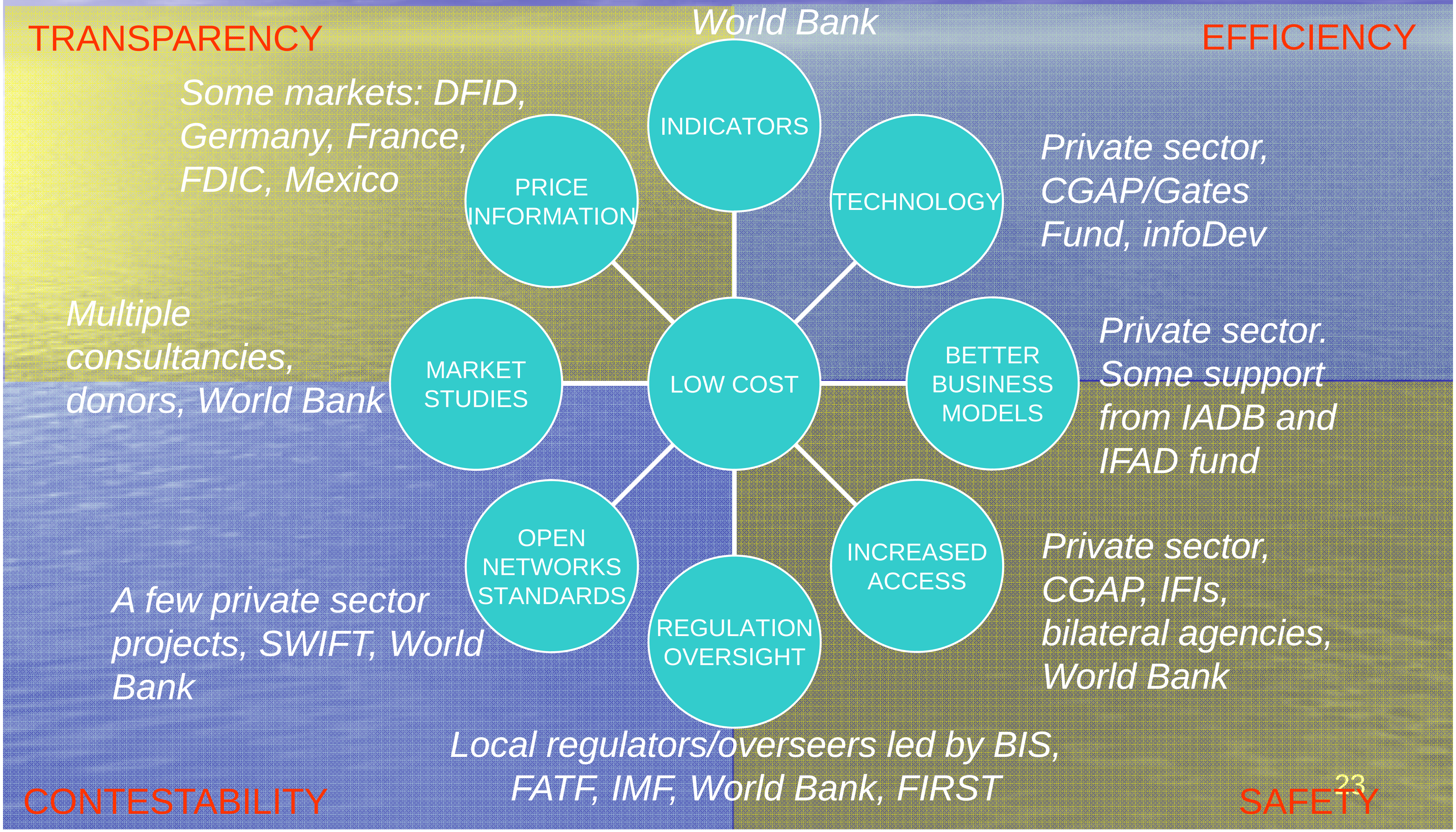
Implementing the GPs

Remittances and development

- If $250 bn of remittances have an average cost of 10 percent, cutting this cost in half means savings of $12.5 billion a year (the equivalent of a People's IDA)
- Remittances are a key element to reach higher levels of bankarization (e.g., Bansefi in Mexico) and obtain access to other financial services (e.g. credit)
- Remittances can be a vehicle to develop innovative services and payment instruments
- May ensure integrity of the financial system channeling transactions through the formal financial system
- Instrument for capital markets development?

What are the different institutions doing?

PRIMARY ACTORS: Who are at the front line of making remittances cheap through safety, efficiency, contestability, and transparency?



Implementation of the General Principles

- The Multilaterals (ADB, AMF, EBRD, IADB, and IMF), under the leadership of the World Bank, have developed detailed Guidelines for the application of the GPs and a stocktaking methodology
- Available tools will be used for the stocktaking and to foster the dialogue within the country and among countries (e.g. regional initiatives in payment systems, e.g. WHF, CISPI, API, FSAPs, etc.)
- Two new regional initiatives are being launched with special focus on remittances (South Asia Payments Initiative and Africa Payments and Remittance Initiative)

Implementation of the General Principles

- In 2006, the World Bank carried out two pilots of the assessment of the GPs in El Salvador (September 2006) and Morocco (November 2006)
- **In 2007, a Remittance program in LAC has been launched in cooperation with CEMLA and with financial support from IADB-MIF (missions to Honduras and Haiti in 2007)**
- The World Bank is launching a project to create a remittance price database worldwide to provide a benchmark to measure improvements in transparency, efficiency, and competition within remittance corridors.

Remittance Price Database: Goals

- Benchmark to measure improvements in transparency, efficiency, and competition within remittance corridors.
- Comparisons of markets across countries and regions.
- Price reductions through a “name and shame” approach. An example of this has been the case of LAC, where publication of remittance fees was a factor in their reduction from 15%, on average, in the region in 2000, to 5.6% in 2006.
- Better understanding of local remittance market for consumers. This will be improved by increasing the frequency of updates after the first year.

Project Methodology

Consist of finding a simple average price from country X to country Y.

Country Sampling methodology

- A matrix has been constructed that selects thirteen important remittance sending countries and identifies the volumes of remittances in the most important corridors for each country.

Company Sampling Methodology

- The population of remittance firms in sending countries can be identified using information from regulators where registration/ licensing/oversight mechanisms exist. The sample is split between the most important non-bank RSPs and the most important banks/credit unions/MFIs in each corridor. The sample will not include transfer mechanisms such as hawala, couriers, and post.

Amount and Speed

- The project will collect data on two different price levels: the local currency equivalent of US$250, and the average amount (US$) for each corridor.

Project Methodology

Data acquisition

- Firms will be contacted to obtain the sending fees and exchange rates charged to transfer the local currency equivalent of US$250, and the average transaction amount (funds to be received in the currency of the recipient country). The day and time of the request will be recorded, as will the interbank exchange rate at that day/time. The researcher will also ask if there are any known fees for the recipient. When possible, the quote requested will be for next day service.

Data Verification

- Actual transactions should be undertaken through a random selection of firms in the corridor, including firms that cannot or will not give customers price information before a transaction has taken place. ("mystery shopping")

Publication

- Once finalized, the database will be published online within the Payment System's section of the World Bank website. The website will consist of a world map with average price information on sending and receiving countries, and each country studied will also have a page outlining the individual firms studied and the factors that make up the average price.
- It is intended that the website be updated annually.
- The project team will proactively raise awareness on the existence of the database.

Implementation of the General Principles

- So far, authorities showed great interest in the content and the scope of the Principles, and in the concrete actions and benefits that can be drawn from their implementation
- The World Bank has expressed its willingness to support the implementation of action points after the assessments (e.g. Payment system development projects can be a good vehicle to address the issue)

Possible Difficulties in implementation

- Large number of “systems”; many are small and informal

  - Even for banks, each may have its own “system”

- In many countries, the authorities may not have the powers to assess or implement

  - With the possible exception of AML/CFT provisions, many remittance markets and RSPs lack any form of regulation/control

- Implementation will typically involve multiple authorities: it may be difficult to coordinate actions and/or to determine what agency should take the lead
- Some of the problems identified may not be fully addressed unless the GPs are implemented on both the sending and receiving country (e.g. improving global systems)

YET, WE MUST TRY. A DAY SHOULD COME WHEN TRANSFERRING MONEY IS AS CHEAP AND FAST AS TRANSFERRING OUR FILES, OUR PICTURES AND OUR VOICES IS TODAY