

# Faster, faster... safer!

Our need for near-instant transfers and settlements is the force behind efforts to modernise national payment infrastructures the world over. Gerry Gaetz looks at Canada's modernisation programme, as well as global trends



Around the globe, technology has conditioned us to expect instant access to the things we want. And payments are no exception. In a world where Google can retrieve thousands of search results in the blink of an eye, getting a payment safely from sender to recipient is no longer enough.

Consumers and merchants also want faster access to funds, security and privacy – all at a low cost. Businesses, on the other hand, want richer payment data and operating environments that promote efficiencies like straight-through processing (STP). Industry players must evolve to remain current and relevant. In response to changing user needs, regulatory and technological drivers, more than 30 countries around the world, including Canada, have launched major initiatives to modernise their national payments infrastructure.

**The impetus for global modernisation**  
Together with new customer expectations, a number of

connected factors are driving modernisation around the world. Coming out of the global financial crisis, and given the rapid evolution of the retail payments space, regulators want to ensure that evolving payment services offer greater protection, transparency and reduced risk for consumers and businesses. As a result, they're holding financial market infrastructures to more stringent risk management standards. This is true for credit and liquidity risk, but also operational risks, such as cyber and data security.

In Canada, there is a new and tangible example of this – legislation has given the Bank of Canada the power to oversee retail payment systems that could cause disruption and impact to the economy if not functioning properly.

At the same time, globalisation is driving modernisation and spurring the adoption of the payment standard ISO 20022 around the world. This international standard for the development of payment messages

IMAGE SOURCE

allows richer payment data (remittance information, such as invoice details) to travel along with a payment. This creates the opportunity for businesses to automate their accounts payable/accounts receivable functions and more fully enjoy the benefits of electronic payments, such as STP and automated error correction. The enhanced remittance information also provides greater transparency, enabling easier payment tracking, issue resolution and system reconciliation for financial institutions and their customers. Since ISO 20022

operates independently of any specific technology platform, it promotes interoperability and will enhance the efficiency of cross-border payments.

## Faster and real-time payments

In most countries, payment system modernisation has concentrated on the development of faster or real-time payment systems. The focus has been on retail (in particular, customer-initiated electronic and mobile) transactions.

It's important to distinguish here between payment

## GLOBAL DEVELOPMENTS

- CANADA CPA modernisation
- MEXICO SPEI® payment system
- BRAZIL STR RTGS system
- US The Clearing House faster payments
- UK Faster Payments Service
- FINLAND Finvoice
- POLAND Express Elixir system
- EUROPE EBA Clearing pan-European instant payment infrastructure solution
- SINGAPORE Fast and Secure Transfers payments
- AUSTRALIA New Payments Platform
- SOUTH AFRICA Real-time clearing system

SOURCE: McKinsey Literature Review

speed and settlement speed. Customers want payment speed – the ability to see transactions reflected in their accounts within a few seconds – and immediate access to funds. The popularity of these characteristics is reflected in the success of the UK's Faster Payments Service (FPS), which has experienced solid growth since its launch (a compound annual growth rate of 34.6% during 2009-13)<sup>1</sup>. Although that growth has slowed somewhat, FPS is expected to drive the continued growth of non-cash payments in the UK well into the future and provide a platform for further innovation. However, immediate access to funds for customers doesn't necessarily mean that settlement between payment system participants has to be immediate. Faster settlement isn't driven by customer demand – it's more about reducing credit and liquidity risk in a payments system, which is of primary importance to regulators.

Similar to the way the government drove the agenda that led to the development of the FPS, modernisation

a UK-based international payment systems provider, to develop a real-time payments network that will enable individuals and businesses in the US to make immediate payments. It will also include data, such as invoices for business payments.

### The Canadian approach

In Canada, the Department of Finance and the Bank of Canada have expressed strong support for payment system modernisation, and system participants are aligning on ISO 20022, faster payments and other possible enhancements.

The Canadian Payments Association (CPA), Canada's financial market infrastructure for payments, is leading a holistic, collaborative initiative to modernise the payments system for the benefit of the overall financial system.

In September, the CPA and the Bank of Canada released joint research<sup>2</sup> outlining the most critical issues the industry must investigate to improve the payment system. The research translates the government's public policy

systems. A disruption or failure in the CPA's retail payments system has the potential to adversely affect Canadian economic activity and general confidence in the payments system. Therefore, under the new legislation, this system is expected to be designated for oversight by the Bank of Canada, and will need to meet new and higher standards.

In line with other countries further along the path to payment system modernisation, the CPA is bringing the ISO 20022 standard for payment messages to Canada and actively promoting harmonisation at the international level. In August of 2015, as part of its modernisation initiative, it launched a consultation on its ISO 20022 message standard for direct debits and credits. In early 2016, the new ISO 20022-enabled messages for Automated Funds Transfers will be made available for use in the market.

While the global focus on real-time payments is very important, the CPA is taking a broader, more holistic look at the future of payments

## Regulators want to ensure that evolving payment services offer greater protection and reduced risk

in many countries has been initiated by government or central banks. In Australia, for example, financial institutions are collaborating to develop a New Payments Platform in response to the central bank's strategic objectives on payments innovation. In the US, the Federal Reserve has formed a Faster Payments Task Force to help determine the way forward for more than 12,000 financial institutions of all sizes and business models.

Market forces are also spurring the development of faster payment services in the US. Recently, The Clearing House announced that it will work with VocaLink,

objectives (PPOs) for the broad payments ecosystem into desired outcomes for CPA payment systems. Then it develops a taxonomy for clearly describing the defining attributes of a payment system: access, functionality, interoperability, timeliness of payments and risk management. Lastly, it develops an analytic framework to consider the trade-offs of the various attributes to achieve the PPOs for the Canadian payments ecosystem and recommends the most critical issues for the CPA to investigate as it considers the modernisation of its own

in Canada. Working with McKinsey & Company, the CPA is conducting interviews and interactive workshops with industry participants and stakeholders – another key component of its modernisation initiative.

Finding common ground and aligning industry players from across the payments ecosystem is not without its challenges. Many of these organisations are highly focused on regulatory compliance, and subject to varying levels of oversight. Consistent oversight and/or collateral requirements to ensure Canadians' funds are safely stewarded are of

### GLOBAL DRIVERS

**Changing user needs and expectations**, including near real-time payments with availability beyond traditional hours of operation, and a growing demand for mobile and electronic channels, giving rise to new entrants

**Convergence towards global payments standards**, including cross-border consumer and corporate needs

**Accelerating advancement in technology**, including cloud, agile development, data analytics and hosted services viability

**Growing regulatory requirements and demands for enhanced risk management** both inside and outside government (for example, risk management, payment security, etc)

SOURCE: McKinsey Payments Practice

primary importance to payment system users. Access rules for clearing and settlement systems that support innovation and maintain trust are also a priority.

In 2016, once the shared vision has been established, the CPA will turn its attention to developing proposals for its core clearing and settlement systems to support the vision.

Through research, engagement and collaboration, the CPA will find the best opportunities to modernise for the benefit of payment system participants, businesses and all Canadians. 🍀



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- <sup>1</sup> *World Payments Report 2015* by Capgemini and the Royal Bank of Scotland
- <sup>2</sup> *Public Policy Objectives and the Next Generation of CPA Systems: An Analytical Framework*, available on the CPA website, [www.cdnppay.ca](http://www.cdnppay.ca)