

Enhancing Cross-border Payments

Stage 1 report to the G20

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Stage 1 assessment report to the G20

The G20 has made enhancing cross-border payments a priority during the Saudi Arabian Presidency. Faster, cheaper, more transparent and more inclusive cross-border payment services, including remittances, would have widespread benefits for citizens and economies worldwide, supporting economic growth, international trade, global development and financial inclusion.

Cross-border payments are often perceived to face challenges of high costs, low speed, limited access and insufficient transparency. The challenges with cross-border payments affect end-users and service providers, but they do not affect all in the same way. Individuals and small companies face particular challenges with retail cross-border payments, and financial inclusion remains a challenge for many. Low-value payments may incur high fees as a percentage of the amount sent and face cumbersome processes. The unbanked and individuals and firms from fragile states are amongst those who may not be able to access payment services at all.

Enhancing cross-border payments requires addressing frictions in existing cross-border payment processes. These frictions include: fragmented data standards or lack of interoperability; complexities in meeting compliance requirements, including for anti-money laundering and countering the financing of terrorism (AML/CFT), and data protection purposes; different operating hours across different time zones; and outdated legacy technology platforms.¹ Additionally, the frictions increase the need for intermediaries involved in cross-border payments to hold precautionary funding – often in multiple currencies. Furthermore, depending on the country corridor and payment process, the length of the transaction chain can add to costs and delays. These frictions create cost barriers to entry that may weaken competition in providing cross-border payments services.

A number of public sector initiatives have sought to address these challenges and frictions by enhancing existing payment arrangements. On the retail side, the G20 and UN have set targets to reduce the cost of sending international remittances and launched workstreams to achieve this. On the wholesale side, central banks have undertaken interlinking projects between individual national payment systems or, for instance in the case of the euro, established a regional payment system. The FSB has undertaken action plans to address the decline in correspondent banking relationships and remittance firms' access to banking services.

Financial innovation is creating opportunities to make payments more efficient. Innovation in technology and business models in payments has put the focus on further enhancements in payments systems. New technologies have the potential to facilitate fast, low cost, transparent and scalable payments for a broad range of users through the banking system.

¹ This list of frictions is broadly consistent with those identified by market participants via outreach through the CPMI Cross-border Payments Task Force.

And the use of internet-based infrastructures for payments has created opportunities for new business models and for new providers including nonbanks to offer payment services.

Technological innovation could build on existing cross-border and domestic payment arrangements or take the form of new structures and ecosystems. There is a range of identifiable improvements to current correspondent banking and other cross-border payment arrangements that are in train or could be implemented.

The use of new technologies and business models in cross-border payments also involves challenges and risks. Innovation in the provision of financial services should always be accompanied by measures to address all relevant risks and to ensure that proper consumer protection is in place. To address this requires a detailed analysis of the operational soundness of solutions (including to promote interoperability of payment systems), legal certainty and consistency (including issues related to legal enforceability in a cross-border context and avoiding jurisdictional conflicts) and whether additional regulation and oversight is needed (including to ensure meeting AML/CFT requirements and addressing financial stability risks). For instance, recent private sector proposals to create so-called “stablecoins” for payment purposes have highlighted the possibility of new digital payments gaining scale quickly, potentially globally. Therefore, these mechanisms raise questions which are being examined by the FSB and the public sector more broadly about how to ensure appropriate regulation, supervision and oversight, but also wider macroeconomic and monetary policy issues. The FSB is publishing this month a consultation paper on financial regulatory issues associated with these mechanisms.

Public authorities have an important role to play, working with the private sector to leverage opportunities and address challenges. As regulators, supervisors and overseers, public authorities seek to achieve the public policy goals of cross-border payment services safety and efficiency, through consistent implementation of international standards; however, they face challenges with cross-border access to information and international coordination in the regulation and supervision of the various entities in the cross-border payments ecosystem. As operators of payment infrastructures, central banks provide services primarily designed to settle transactions between domestic participants in their home currency; as they evaluate how to modernise systems or improve payments processes in their jurisdiction, they also need to consider how to address challenges associated with cross-border and cross-currency payments. As catalysts and facilitators of improvements by the private sector, public authorities can encourage interoperability of private sector improvements to payment systems.

The Saudi Arabian G20 Presidency has asked the FSB to coordinate amongst the relevant stakeholders on a three-stage process to develop a roadmap to enhance cross-border payments:

- **Assessment (Stage 1):** The FSB, in coordination with relevant international organisations and standard-setting bodies has considered the existing practice of cross-border payment arrangements through conducting an assessment of existing arrangements and challenges, and accordingly is providing this update to the G20 Finance Ministers and Central Bank Governors (FMCBGs) meeting in April 2020.
- **Building Blocks (Stage 2):** The Committee on Payments and Market Infrastructures (CPMI) is leading the work on creating building blocks of a response to improve the current global cross-border payment arrangements. This will set out areas where further

public sector work could assist in moving to an improved cross-border payments system and in public goods or removing unnecessary barriers, and accordingly provide an update to the G20 FMCBGs meeting in July 2020.

- **Roadmap (Stage 3):** Building on the previous stages, the FSB will coordinate, with CPMI and other relevant international organisations and standard-setting bodies, the development of a roadmap to pave the way forward. In particular, the FSB will report to the G20 on practical steps and indicative timeframes needed to do so. The three-stage process will be submitted as a combined report to the G20 FMCBGs meeting in October 2020.

Global cross-border payments, in reality, are carried through a diverse multi-layered set of networks. These include more traditional arrangements such as correspondent banking, interlinked domestic payment systems, card networks, remittance services such as money transfer operators and innovations based on new financial technology, to name just some arrangements. These networks are based on distinct models, for instance correspondent banking arrangements settle across the ledgers of the various correspondent banks, while some other arrangements settle across the single ledger of the central operating platform. These can have quite different implications for the severity and type of frictions, such as the number of counterparties that need to conduct compliance checks on a given transaction.

A roadmap for enhancing cross-border payments, therefore, will need to encompass a variety of approaches and time horizons. Some building blocks that form part of the roadmap, which may be shorter-term actions, should benefit a number of different types of existing arrangements, such as improvements in interoperability among payment arrangements and the standardisation of payment messages, effectiveness of due diligence, enhanced interconnectedness between payment systems and improved currency conversion mechanisms. Other building blocks, which may be more medium-term, may go beyond adjustments to existing arrangements by proposing actions that should eventually improve the structure of the system and cover all identified frictions, but would take longer and face greater uncertainties in their development. Some actions would need to be taken at the national level and others at the international level. Moreover, the roadmap should recognise that, while greater consistency and a more efficient interlinking are important goals, these do not imply a “one size fits all” approach for the diverse set of users of the different payment system networks and their differing needs.

While the roadmap may indicate different possible routes, all need to meet minimum standards of safety and soundness. For instance, there should be no compromise in meeting minimum international standards for safe and sound payment systems, prudential supervision and AML/CFT compliance.

The roadmap will need to involve a variety of actors in the public and private sectors. In the public sector, payment system overseers, central banks (including as operators of payment systems), banking supervisors and AML/CFT regulators are among those with roles to play. In the private sector, banks and other financial institutions, payment systems, technical service providers and new FinTech solution providers all will have roles.

This report concludes with some preliminary thoughts on areas to consider when developing the eventual roadmap, which will include practical steps and indicative

timeframes. These include questions to explore a range of topics that fall under four broad categories:

Operational improvement of payment infrastructures

Improvements to the operational aspects of cross-border payments could improve the efficiency and speed by which these payments are processed. Building block analysis will examine ways in which the public and private sectors can catalyse operational improvements to address these constraints. Questions to be explored further include:

- How can the public and private sectors help to catalyse improvements in technology that help to better satisfy user needs?
- Are there initiatives that public authorities could take to enhance key payment infrastructures (cf. real-time gross settlement systems, automated clearing houses, fast payment systems), including to enhance interoperability?
- Are there areas where operational improvements can reduce the burden of maintaining liquidity in multiple currencies while meeting prudential liquidity requirements?
- Could operational improvements reduce the length of payment chains and, as a result, reduce complexities and risks?

Standardisation of data and market practice

Frictions arise from the lack of use of standardised payment messages and the data they contain and from divergent market practices in processing payments. Questions to be explored further include:

- What steps could the public or private sector take to increase overlaps in operating hours across payment systems in different time zones?
- What steps could the public or private sector take to increase the use of standard message format protocols or other mechanisms to ensure interoperability?
- What other steps could be taken to address and handle other operational aspects such as data quality, transparency of fees and status of processing, etc?

Legal, regulatory and oversight framework

This report sets out how the need to transmit cross-border payments across multiple jurisdictions with diverse legal and regulatory practices can create frictions. Current arrangements can delay payments and increase the cost of offering services across many currency corridors. To improve the efficacy and efficiency of regulation and supervision, enhancements may need to be considered. Questions to be explored further include:

- Which initiatives could be taken to improve the efficiency and reduce costs of AML/CFT and other compliance processes without compromising on the quality of compliance and to ensure adequate oversight? This could include facilitating improved customer due diligence mechanisms for AML/CFT, greater use of the Legal Entity Identifier (LEI) for firms and digital IDs for individuals and stronger regulatory frameworks that reduce unnecessary barriers to cross-border data sharing when implementing the FATF standards and other regulatory and supervisory requirements. What further steps in cross-border cooperation in regulation, supervision or oversight could help to reduce frictions?

- What further steps can authorities take to enable appropriate access to cross-border payment services?

Progress monitoring and information sharing

Progress monitoring and information sharing will be essential for successful implementation of the roadmap. Questions to be explored further include:

- What data would it be useful to collect going forward to enhance understanding and monitoring of cross-border trends and costs (while taking account of the need to avoid undue burden on firms from data collection)?
- What steps can be taken to share good practices in areas such as regulation/supervision/oversight?
- How can authorities share experiences in facilitating FinTech development while maintaining a sound financial system and a level playing field?
- Are there opportunities for providing technical assistance to improve jurisdictions' supervisory and regulatory frameworks and thereby enhancing their ability to access cross-border payment markets?