



South African Reserve Bank

National Payment System Department

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Notice to all stakeholders in the national payment system on sort-at-source

1. Background
 - 1.1 Section 10(1)(c)(i) of the South African Reserve Bank Act 90 of 1989, as amended (SARB Act) empowers the South African Reserve Bank (SARB) to “perform such functions, implement such rules and procedures and, in general, take such steps as may be necessary to establish, conduct, monitor, regulate and supervise the payment, clearing or settlement systems”. Furthermore, in terms of the National Payment System Act 78 of 1998 (NPS Act), the SARB is required to provide for the management, administration, operation, regulation and supervision of payment, clearing and settlement systems in the Republic of South Africa; and to provide for connected matters.
 - 1.2 The national payment system (NPS) encompasses the entire payment process, from payer to beneficiary, and includes settlement between banks. The process includes all the tools, systems, mechanisms, institutions, agreements, procedures, rules or laws applied or utilised to effect payment. The NPS enables the circulation of money, that is, it enables transacting parties to exchange value.
 - 1.3 The National Payment System Department (NPSD) within the SARB is assigned the role of overseer of the NPS. The *National Payment System Department Oversight Framework (Framework)* published in October 2016 outlines; inter alia, the legal framework, objectives, scope and approach of the oversight function of the NPSD. The *Framework* includes the enhancement of

the following objectives of oversight: safety and soundness; efficiency; reduction of systemic risk; fostering of transparency; prevention of financial crime; financial inclusion; consumer protection; building confidence in the financial system; and competition.

- 1.4 The SARB recognises the Payments Association of South Africa (PASA) as a payment system management body (PSMB) in terms of the NPS Act, with the objective of organising, managing and regulating the participation of its members in the payment system. In this regard, PASA is responsible for the regulation of its members' participation in the payment system.
- 1.5 In support of the objective of a safe, sound and efficient payment system, PASA issued the PASA Policy on Sort-at-Source (Policy no. 01/2009 – PASA Policy) to its members, namely banks and designated non-banks. In terms of the PASA Policy, sort-at-source is defined as the activity where a person (or such person's agent or outsourcing partner) submits payment instructions or transactions directly to the member holding the destination account, resulting in the bypassing of the clearing system which is undertaken through the regulated acquiring or sponsoring relationships.
- 1.6 Sort-at-source transactions may be initiated for both debit-pull and credit-push payment instructions. For debit-pull transactions, the initiator of the payment instructions bypasses clearing by sorting transactions and submitting relevant instructions directly to the paying bank for the crediting of their accounts held at that paying bank. For this process to work, the entity that needs to be paid has to hold multiple accounts at the paying banks. In the case of credit-push transactions, multiple accounts are held by the payee at different banks, thus enabling the payer to pay into the relevant account of the payee held at the same bank as the payer. These processes manipulate transactions destined to be processed as interbank off-us transactions and effectively bypass clearing as these transactions would normally have been switched through a payment clearing house (PCH).

1.7 The SARB supports the PASA Sort-at-Source Policy and is in the process of amending the regulatory framework to address sort-at-source and has deemed it necessary to issue this notice to all stakeholders in the NPS in the interim.

2. Summary of issues

2.1 The SARB is aware that certain payment system stakeholders, including retailers, users, system operators, microlenders, bureaus and paying banks are involved in the practice of sort-at-source, which results in bypassing of the regulated clearing system.

2.2 If allowed, the sort-at-source practice will, inter alia, negatively impact the following public policy objectives and principles:

2.2.1 Efficiency and interoperability

- i. Sort-at-source is inefficient as it may require a participant to have multiple devices from multiple acquirers, thus requiring a participant to sign multiple agreements and incur costs from multiple acquirers. Similarly, it may require a receiver of funds to hold multiple accounts for similar payment instructions.
- ii. If allowed to proliferate, sort-at-source will reduce the interoperability and positive network effects of the current centralised clearing system. The benefits of centralised clearing include a level playing field, common standards, and a single connection to the clearing system to enable the exchange of payment instructions with other participants.

2.2.2 Access and competition

- i. In South Africa, the largely concentrated banking sector makes sorting at source attractive due to the concentration of retail demand-deposit accounts with a few major banks. The effect of sorting at source reduces competition on the acquiring side where merchants seek to acquire

directly with larger retail account-holding institutions. This disadvantages acquirers with lower consumer retail account-holding structures. Sort-at-source forces the tight coupling of acquiring services and retail account-holding services. Sort-at-source therefore does not foster competition.

- ii. Over time, the entry for new participants accessing the NPS will become increasingly costly and cumbersome, as more transactions will be processed as on-us transactions, which will disadvantage those participating in the clearing arrangements. This will lead to a decrease in economies of scope and scale, resulting in an inefficient and expensive centralised clearing system.

2.2.3 Innovation

- i. The sort-at-source practice will encourage the proliferation of “on-us solutions” and thus impede further development of a two-sided market. This may discourage innovation at a platform-level and further reduce competition on both sides of the two-sided market.

2.2.4 Transparency

- i. The sort-at-source practice may reduce transparency of payment activities. In this arrangement, transactions are on-us and thus the real activity (growth or declining trends) within certain payment streams is not visible to regulators from a central point.

2.3 Note: With regard to multiple acquiring, where the clearing system is not bypassed, a participant is able to process different brands or card types through different acquiring banks. Each acquiring bank still processes the on-us transactions and transmits the rest of the transactions (off-us) through a payment clearing house system operator (PCH SO) such as BankservAfrica, MasterCard or Visa. In addition, multiple acquiring is normally used for business continuity purposes. In cases where multiple acquiring arrangements do not bypass the clearing system, the SARB will not have objections to such practices.

3. Notice

- 3.1 This notice serves to advise stakeholders to refrain from the practice of sort-at-source which is specifically aimed at bypassing the clearing system as it negatively impacts the public policy objectives and principles set out in clause 2.2.
- 3.2 In view of the above, the SARB is in the process of reviewing and developing a comprehensive policy position regarding the sort-at-source practice which will provide clear scope and guidance.
- 3.3 NPS stakeholders who are uncertain of any aspect relating to this practice or this notice are advised to contact the SARB. Enquiries in this regard can be directed to npsdirectives@resbank.co.za.



Mr. PMT Masela

Head: National Payment System Department