

BANK OF NAMIBIA

No. 4

6 January 2009

DIRECTIVE UNDER THE PAYMENT SYSTEM MANAGEMENT ACT, 2003 (ACT NO. 18 OF 2003)

In my capacity as Governor of the Bank of Namibia (the Bank), and under the powers vested in the Bank by virtue of section 13 of the Payment System Management Act, 2003 (Act No.18 of 2003), I hereby issue the Directive on the conduct of Early Square-Off within the National Payment System in Namibia (PSDIR-4), which Directive shall become effective on 31 December 2009.

T.K. ALWEENDO
GOVERNOR

Windhoek, 6 January 2009

DIRECTIVE ON EARLY SQUARE-OFF WITHIN THE NAMIBIA INTER-BANK SETTLEMENT SYSTEM

Overview

Currently, the Bank considers Payment Clearing House (PCH) batches as systemically important because in total they represent a significant proportion of the daily settlement in NISS. Retail PCH batches form an unacceptably high proportion of the daily settlement undertaken late in the day when NISS participants' treasury operations are closed therefore precluding participants entering the inter-bank market should they be short at settlement time and resorting to the automatic overnight repo facility provided by the Bank. With the implementation of 7-day repo on 1 July 2008, the usage of overnight repo has been considerably reduced, although the inter-bank market activity still remains low.

The failure of a NISS participant to honour its obligations in PCH batches late in the evening, when inter-bank financial markets are closed may contribute to systemic disturbances and risk in the payment system together with potential to affect statutory requirements. The current arrangement is regarded as unsatisfactory. The Bank prefers that participants, who are short, first enter the inter-bank market to secure funds prior to approaching the Bank to request an overnight facility that must be settled at the commencement of business on the following day.

Consequently, early and multiple clearing and settlement operations during the day will contribute to the reduction of the overall risk profile of the NPS to the benefit of the Bank and participants.

On 10 July 2008, the Bank issued a position paper (1/2008) on the early square-off in Namibia Inter-bank settlement System (NISS). The position paper outlines the Bank's position on the earlier closure¹ of NISS. Early Square-off in NISS is intended to align the opening and closing of the NISS settlement schedule with the start/close of the participants' business hours and treasury operations.

¹ Early closing of NISS is aim at aligning NISS Settlement Schedule with the treasury operations' and business hours of NISS participants.

1. The position of the Bank

- 1.1 The Bank of Namibia views the current clearing and settlement arrangements for PCH batches to be unsatisfactory.
- 1.2 Current late closure of NISS introduces both operational and settlement risks. While operational risk is the risk that NISS could malfunction, settlement risk is a result of failed settlement due to lack of funds in participant's settlement account. Such risks contribute to systemic disturbances and risk when extended operational arrangements are in place.
- 1.3 NISS settlement schedule shall be changed to enable early square-off. The preferred square-off time in NISS shall be 17h00.

2. Purpose

- 2.1 The purpose of this directive is to notify Namclear and banking institutions participating in the PCHs to implement the necessary system, operational and infrastructure changes and re-align their clearing, settlement arrangements and business processes to facilitate early square-off in NISS by 31 December 2009.

3. Definitions

In this Directive, unless the context indicates otherwise, the words and expressions used herein shall have same meaning assigned to them in the Payment System Management Act, 2003 (Act No. 18 of 2003) and cognate expressions shall have corresponding meanings.

- 3.1 'Bank' means the Bank of Namibia as referred to in section 2 of the Bank of Namibia Act, 1997 (Act No.15 of 1997);
- 3.2 'Banking institution' means a company established to conduct banking business in terms of the Banking Institutions Act, 1998 (Act No. 2 of 1998).
- 3.3 'CLC PCH' means a payment clearing house arrangements for Code Line Clearing of Cheque payment transactions;
- 3.4 'Card PCH' means a payment clearing house arrangements for Card (ATM, Debit and Credit) payment transactions;
- 3.5 'Day of value' means day at which funds are debited from one participant and credited to another participant within NISS at the Bank.
- 3.6 'Clear' or 'clearing' means the exchange of payment instructions between system participants with a view to reconciling and confirming payment instructions;

- 3.7 'Early Square-Off' means the final settlement within NISS of all PCH batches prior to 17:00 during weekdays and 12:00 on Saturdays. No settlement shall occur on Sundays.
- 3.8 'EFT PCH' means a payment clearing house arrangements for Electronic Funds Transfer (EFT) payment transactions;
- 3.9 'Funds Settlement Value Date (FSVD)' means settlement cycle date on which the settlement takes place.
- 3.10 'National Payment System (NPS)' means the payment system as a whole as defined in the Payment System Management Act, 2003 (Act No. 18 of 2003);
- 3.11 'Namclear' means Namibian Clearing Services Company;
- 3.12 'NISS' shall mean Namibia Inter-bank Settlement System (implemented on 10 June 2002), an automated interbank settlement system provided to NISS participants by the Bank, including all the technical infrastructure and business components thereof;
- 3.13 'Payment Clearing House (PCH)' means an arrangement between two or more system participants governing the clearing of payment instructions between those system participants;
- 3.14 'Payment obligation' means the indebtedness that is owed by one system participant to another system participant as a result of the clearing of one or more payment instructions in a payment system;
- 3.15 'Payment system arrangement' means procedures and services for the processing of payment transactions;
- 3.1 'Systemic risk' is the risk that should one or more participant in the payment system fail to settle its obligations, other participants may also be unable to settle their obligations.
- 3.16 'Settlement' means payment or discharge of outstanding obligation that a system participant owes to another system participant;
- 3.17 'Intraday settlement' means prompt and final settlement on the day of value, preferably during the day and at a minimum at the end of the day. When the intraday settlement objective is implemented as envisaged, CLC, EFT will have more than one settlement window in NISS. It will enable Namclear to provide intraday payment finality through NISS and thereby reduction of payment-related risks in the financial system.

4. Implementation of Directive

- 4.1 This directive shall be effective from 31 December 2009.
- 4.2 Namclear and banking institutions participating in the PCHs shall implement the necessary system, operational and infrastructure changes and re-align their clearing, settlement arrangements and business processes to facilitate early square-off in NISS by 31 December 2009.
- 4.3 Namclear and banking institutions participating in the PCHs shall implement intra-day settlement for PCH batches to enable multiple settlements of EFT and CLC PCH batches, in two settlement cycles, at 10h00 and 16h40.
- 4.4 The banking institutions participating in the PCHs shall continuously send as much possible their retail payments to Namclear before 15h00 to ensure that the values that are left after 17h00 are low. Wherever possible, retail batches shall be settled as soon as the obligations of the parties involved have been determined.
- 4.5 The banking institutions participating in the PCH batches shall adhere to Namclear's Service Level Agreements. Namclear shall enforce improved delivery and processing flows in order to meet the earlier closure in NISS.
- 4.6 In its role as overseer of the NPS, the Bank shall ensure that cut-off times in all PCHs are continuously observed and banking institutions are expected to comply with delivery and collection times to Namclear.
- 4.7 The following clearing and settlement arrangements shall be implemented for PCH batches:
 - 4.7.1 The EFT dated services shall be settled at 10h00, while same-day and one-day services shall be settled prior to 16h40. This would entail splitting of the Electronic Funds Transfer (EFT) batches into dated transactions, one-day and same-day transactions. Dated transactions would then be settled early in the settlement cycle day, with same-day and one-day batches being settled at agreed times throughout the day, thus decreasing the value in the batch streams not settled at end of day.
 - 4.7.2 The CLC PCH batches shall be settled more than once a day at least twice (at 10h00 and 16h40) and as much as possible prior to 17h00.
 - 4.7.3 The Card PCH batches shall settle once a day prior to 16h40. Sunday's² processing shall be settled under Monday's FSVD prior to 16h40.
 - 4.7.4 Settlement shall not be allowed on Sundays or public holidays and any transactions processed by Namclear on these days would only be submitted to NISS under the next valid FSVD.

² Currently Sunday's processing is settled under Monday's FSVD at 18h30 in NISS.

5. General

- 5.1 This directive is not exhaustive and may be supplemented and/or amended from time to time.
- 5.2 In order to maintain the cost-effective, efficiency of the National Payment System all participant banking institutions and Namclear are obliged to act in accordance with this directive.
- 5.3 Contravention of this directive is an offence in terms of section 13 of the Payment System Management Act, 2003 (Act No. 18 of 2003) and is subject to penalties under section 17 of the Payment System Management Act, 2003 (Act No. 18 of 2003).

6. Enquiries

Any enquiries or clarification concerning the directive may be address to:

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