

V Meeting of Central Bank Legal Advisers

Banco Central de Bolivia and CEMLA

La Paz, Bolivia 23rd to 25th August 2000.

English and Spanish, simultaneous translation.



OBJECTIVE: To analyze legal aspects of the payment systems in participating countries, in particular, those that have introduced electronic systems.

PARTICIPANTS: Central Banks' members of CEMLA

METHODOLOGY OF THE MEETING: The meeting will be held in plenary sessions and working groups. In plenary session, national cases related to the participation of the central bank (operative and regulatory aspects) in payment systems will be presented. In working groups, these cases will be discussed; conclusions and recommendations will be formulated in order to be presented in plenary session during the third day.

DEADLINE FOR INSCRIPTION: Name of the participants and the title of the papers (or at least the theme of interest) should be received by CEMLA and by the Central Bank of Bolivia June 30th, at the latest.

DEADLINE FOR PAPERS: Papers must be delivered to the host and to CEMLA before July 31st, 2000. The text must be 25 pages long (maximum), double spaced, preferably written in English and Spanish, and formatted in WORD for Windows 98 or earlier versions. By the time this information is sent, specifications of the visual equipment and time needed for the presentation must be notified to the host.

In order to ease the selection of the papers to be presented at the meeting, as well as to prepare an adequate program, it is requested that an outline of the content of the paper (no longer than a page), in Spanish and English, be delivered before next July 24th.

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Agenda

I. The central bank as regulator entity of the payment systems

- The financial system liquidity
- Relationship between the role of lender of last resort and monetary regulation
- Private sector participation in the management of clearing mechanisms. Compared analysis

II. Transformation of the electronic clearing system

- Changes in payment systems functionality. Restrictions and risks faced with the traditional checks clearing
- Legal changes
- Compared experiences
- Advantages and disadvantages

III. The payments electronic clearing regime

- Functionality and legal framework
- Means of payment
- Technological requirements
- High-value clearing vs. Low-value clearing
- Checks truncation
 - Electronic clearing perspectives
- Dematerialization of means of payments
- Advantages and disadvantages

IV. Payment Systems Regulation and legal risk for central banking

- Regulation of cash payments
- Regulation of banking transfer payments
- Regulation of electronic card payments
- Regulation of electronic payment orders

GROUP 1: LEGAL PERSPECTIVES OF PAYMENT REGIONALIZATION AND GLOBALIZATION

INITIAL OBSERVATIONS

- Private sector institutions regularly establish payment systems on their own including cross border systems.
- Central banks may have an interest in individual payment systems:
 - Solely for monetary policy purposes;
 - To promote the efficiency and safety of payments to carry out economic transactions; and/or
 - Because they have been assigned responsibility for payment systems by their government.
- Final settlement guaranteed by a central bank provides the highest assurance of payment and cannot be duplicated by the private sector, but may not be necessary in any particular payment system.
- Central banks are best able to support payment systems in their own currencies.
- Central banks can support payment systems in a variety of ways:
 - For example, settlement for transactions can be done directly or indirectly.

REASONS FOR REGIONALIZATION OR GLOBALIZATION OF PAYMENT SYSTEMS WITH CENTRAL BANK ASSISTANCE

- Monetary policy purpose
 - For example, TARGET;
- To promote the efficiency and safety of payments to carry out economic transactions on a regional or global basis;
- A regional or global payment system supported by central banks will require some sort of intergovernmental agreement or interaction between central banks.

HARMONIZATION OF NORMS

- Some limited harmonization may be necessary for different systems to work together but it may be limited to a core or backbone system and need not extend to all aspects of the payment transactions handled;
 - For example, harmonization need not address relations between banks and their customers.
 - Systems must be harmonized sufficiently to complete the payment.
- While harmonization may be viewed as promoting efficiency it may also be difficult to achieve due to conflicting local laws or practices.

FORMULATION OF POLICIES

- The degree of harmonization depends on the purposes of the payment systems.
- Other factors bearing on the degree of harmonization may include:
 - The urgency of payment transactions;
 - The volume of the transactions;
 - The costs of the transactions;
 - The liquidity available to support the transactions.

NEED FOR A REGIONAL CENTRAL BANK FOR REGIONAL PAYMENT SYSTEMS

- Not necessary.
- The use of multiple currencies may complicate settlement.
- The use of a single currency may limit the support that individual central banks may provide to participants in the system.

Conclusions and Recommendations

Group 2: Principal Aspects of Payment System Norms

Considering that:

1. The fundamental objective of the central bank is to preserve monetary and the financial system stability. To this end the central bank regulates the liquidity of the economy through monetary policy and its participation in the money market. Moreover the central bank regulates the performance of financial intermediaries through the conditions and norms it issues in accordance with current legislation.
2. The participation of the central bank in the regulation and performance of payment systems can be important to monetary policy and financial stability. The payment system is in fact the channel for the implementation of monetary policy. The safe and efficient operation of the payment system helps the central bank to implement its monetary policy adequately.
3. Along with the operating and technological factors, the legal framework help to ensure that the payment system functions adequately. The operations therein involve diverse risks that may endanger its operation and eventually monetary and financial stability.
4. The payment system risk reviewed with the most attention was systemic risk, that is, the possibility that the negative results of the operations of some of the participants in the system spread to the rest of the institutions, putting at risk the functioning of the system as a whole and favoring the break of payments in the economy.
5. For these reasons it is of the utmost importance to the central bank that payment systems be equipped with adequate operative regulations and a precise and well-structured legal framework. In the case where legislation does not eliminate the operative risks of payment systems, it brings certainty and legal security to participants.
6. The central bank may participate in payment systems as user, administrator, regulator and/or supervisor and as such:
 - Carries out a variety of operations throughout the system.

- Coordinates its operations by itself or by district, facilitating relations between participants.
 - Formulates the norms and dispositions which regulate payment system operations, and in accordance with the legislation in force in each country, may exercise its supervision.
7. Depending on the operations attributed to the central bank to regulate the payment system, in its aspects of high and low value, it may regulate the payment system through norms or via contract.
 8. The Committee of Payment Systems and Liquidation based in Basel has put forward basic principles for important payment systems at a systemic level. These principles assert that the objective of policy is to guarantee the security and efficiency of transactions made within these systems of payment, for which it makes recommendations from legal and operational points of view.
 9. Among the situations that must be identified to establish if they require public legislation beyond that of the private contracts agreed on by the participants of the payment system, is principally the utilization of electronic means, whose legal validity and mandatory effect shall be defined.

Because of the above stated it is recommended:

1. To establish the sphere of influence of the central bank in the payment system in the applicable legal arrangement clearly, defining where the borderline should be between the central bank's regulatory actions and its role as facilitator and likely supervisor of operations.
2. To define the range of terms used in the payment system regulation in order to make them consistent with international practice.
3. To simplify the system of guarantees that ensure compliance with the obligations stemming from the payment system, so that they may be formulated and rendered easily and swiftly.
4. To foster, with basis in the central bank's role as facilitator, the celebration of agreements between the participants that tend to organize the functional mechanisms of payment systems (provided that they do not infringe upon norms of public order). Likewise, to further the legislative modifications considered pertinent so as to

provide adequate legal cover to the functioning of payment systems. In particular the endorsement of legislative norms that confer full legal value on the use of electronic forms and signatures is considered to be of special importance. The endorsed legislative norms must encourage the trust of those taking part in the payment system, thus they must possess transparency and disclosure.

5. To isolate payment system from legal consequences that may arise as a result of discrepancies in underlying relations that give way to payments effected, so it is not seen to be implicated in aspects that do not concern it.
6. To reiterate the necessity that the applicable norms ensure, where appropriate, the irrevocability of transactions and constancy of liquidations effected by the system along with the validity of compensations in net systems.
7. To adopt the criteria dictated by the Committee of Payment Systems and Bank Liquidation of International Payments according to which payment systems are those that allow the transfer of funds between financial institutions be it for their own gain or that of their clients.

GROUP 3

DEGREE OF INCORPORATION OF THE MODEL LAW FOR ELECTRONIC COMMERCE OF THE UNITCAL

The United Nations Commission for International Trade Law (UNITCAL), having observed that a growing number of commercial transactions are made by means of the electronic exchange of data known as “electronic commerce”, issued the Model Law of the UN commission for the Unification of International Trade Law for Electronic Commerce. This was with the mandate of fostering harmonization and the progressive unification of International Trade Law. The scope of the Model Law covers all forms of information in the form of data messages that are utilized in the context of commercial activities.

THE APPROVAL OF NATIONAL LAWS ON THE BASIS OF THE MODEL LAW

With reference to analysis carried out within the countries represented in the working groups, it was shown that Peru, Colombia and Mexico have taken to important aspects contained in the Model Law. They have, however, extended its application not only to commercial transactions but also to all types of declarations of will.

In the case of Colombia a plan was followed to issue a sole law that would incorporate dispositions about electronic documents, following for this purpose the model law recommended by the aforementioned commission.

In the cases of Peru and Mexico the plan was followed to modify the pertinent legal bodies, observing the objectives contained in the Model Law.

In the three countries three principles were recognized, that of “Technological Neutrality” which dictates that legislation not mention specific means in the form of taxation allowing new technologies that arise in the future to be used; “Functional Equivalent”, which establishes that data messages have the same legal standing as written documents and that digital signatures have the same legal efficacy as handwritten; and “Express Acknowledgement of Electronic Means” which decrees

that legal validity will not be denied to data messages simply for having that form.

Ecuador and Bolivia have prepared law projects destined to regulate electronic legal relations, considering the principles laid down in the Model Law.

Brazil has law projects about this matter. However they do not strictly follow the recommendations of the Model Law. On the other hand current legislation is extensive, so it permits data messages to be endowed with legal validity, subject to judicial interpretation.

Paraguay, Guatemala and Costa Rica are in the analysis and study of the Model Law stage, for the future implementation of its principles in legislation.

RECOMMENDATIONS

The development of payment systems, involving more and more the use of electronic means, requires a sound and efficient legal framework that allows their implementation and use in conditions of legal security.

It is recommended, therefore, that all countries adopt legislation that recognizes the legal value of data messages and electronic signatures. In this context it is suggested that any such legislation follow the principles contained in the Model Law so as to achieve a uniform treatment of data messages in payment systems. This would facilitate the future integration of payment systems.

Until pertinent legislation is adopted, in those countries where the norms allow, it would be expedient to endorse agreements in which they recognize the legal value of data messages.

It is suggested that suitable Institutions, in terms of trustworthiness and operation, be created to undertake activities pertaining to the certification of the integrity of documents, authentication, filing and their conservation.

It is necessary to highlight the leading role that central banks can play as entities that govern the payment systems of the different countries to urge the adoption of norms and infrastructure, making the utilization of electronic means possible in conditions of security and efficiency.

It is recommended to make a consultation that allows the visualization of advances in the approval of national laws on the basis of this Model Law, among the member countries of the CITRAL that were not represented in the working groups of this assembly.

Finally, It is suggested that seminars and courses be carried out, principally to judicial administrators, to broadcast and explain the principles of the Model Law incorporated in the corresponding legislation, with the objective of achieving the correct and efficient administration of justice in the application of said norms.