Towards a Legal and Regulatory Framework for South African Domestic Remittances: Some Considerations

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This paper is an exploratory study that examines the legal and regulatory framework for domestic remittances within the South African legal context. The author makes some proposals for consideration in the review of the National Payment System Act No 78 of 1998 (NPS Act) with regards to domestic remittances as a retail, low-value payment service. To this end, the paper provides an understanding of domestic remittances, the transaction, process and channels used. It also contextualizes domestic remittances within the South African National Payment System (NPS) and finally examines the current gaps that can be remedied through the review of the NPS Act. The author argues that if financial inclusion is to be promoted, the regulatory framework pertaining to domestic remittances should enable, rather than inhibit the use of domestic remittances as a payment service.

Keywords: domestic remittances, migration, national payment system, payment service(s), financial inclusion

INTRODUCTION

In the global economy, regardless of the legality of work, migrants experience the need to send money to families they have left in their countries of origin. The same applies at the domestic level, where workers often work in other provinces and need to send money home to support their families. It is interesting to note that in a 2016 report of Technoserve, South Africa's domestic remittance market was estimated to include between US$11 billion and US$13 billion in annual transactions at an average of US$60 per transaction. This was the equivalent of four percent of the South African gross domestic product (GDP). This is more than six times as large as international remittances outflows of South Africa, driven by a far higher number of domestic over international migrants within the country. In 2016, South Africa had approximately 24,3 million domestic remittance users (Technoserve, 2016). Much has been written on the economic and development aspects of remittances, but less so on the legal and regulatory framework pertaining to remittances (Abida and Sghaier, 2014; Beyene, 2014; Adarkwa, 2015; Matuzeviciute and Butkus, 2016; Maviza et al., 2019).

In previous articles, the author dealt with international remittances and the regulatory obstacles pertaining to international remittances and implications for migrant workers and asylum seekers (Lawack, 2013, 2014). This paper is an exploratory study that aims to examine the legal and regulatory framework for domestic remittances, in order to make some proposals for consideration in the review of the National Payment System Act No 78 of 1998 (NPS Act) (RSA, 1998) with regards to domestic remittances as a retail, low-value payment service. The author uses a legal desktop analysis methodology. To this end, the paper provides an understanding of domestic remittances, the transaction, process and channels used. It also contextualizes domestic remittances within the National Payment System (NPS) and finally examines the current regulatory gaps that can be remedied through the review of the NPS Act. The author argues that if financial inclusion is to be promoted, the regulatory framework pertaining to domestic remittances should enable, rather than inhibit the use of domestic remittances as a payment service.

BACKGROUND AND MEANING OF DOMESTIC REMITTANCES

Remittances can be both domestic and international in nature. The term 'international remittance' (Lawack, 2013) does not have a solid universal definition. Different authors have assigned varying definitions to the term. The Bank for International Settlements (BIS) and the World Bank define international remittances as, "cross-border person-to-person payments of relatively low value" (CPSS and World Bank, 2007: 4). Bester et al. (2010: 2) define them as, "non-reciprocal transfers from one person to another across a distance", while Abdul Azeez and Begum (2009: 300) define them as, "that portion of migrants' earnings sent from the migration destination to the place of origin".

The latter definition is deemed more suitable for the purposes of this paper, which looks at the context of the labor migrants who send funds back to families in their countries of origin. According to statistics presented by Genesis Analytics, amounts sent by such migrants within the Southern African Development Community (SADC) region are of relatively low value (Genesis Analytics, 2005).

From the varying definitions mentioned above, two common features of international remittances can be identified, namely that (a) remittances are unrequited person-to-person payments – not made in exchange for goods or services and do not involve receipts and invoices – of relatively low value; and (b) there is a considerable geographical distance between the sender and the recipient. The same definition can be applied to domestic remittances, except that the remittances take place within the borders of a country.

Remittance transactions can be categorized as credit transfers, as payment is typically initiated when the sender instructs a remittance service provider to send funds (CPSS and World Bank, 2007). Remittance transactions are typically recurrent payments made via individual transfers as opposed to being made by standing order. The latter pre-authorizes an institution, typically a bank, to make regular payments to a specified individual or entity. Remittances may be done either in the form of cash transfers, or goods such as groceries (Dodson, 2008). However, this paper focuses on remittances of a monetary type and not those made in the form of goods.

THE REMITTANCE TRANSACTION

Participants

The key participants in a typical remittance transaction are the sender, the recipient, the capturing remittance service provider (RSP) and the disbursing remittance service provider. The sender, in the context of this paper, refers to the migrant worker seeking to send funds to their home of origin. The recipient is the person to whom the migrant seeks to send funds to. Often, but not necessarily, the person is a family member of the migrant such as a spouse, sibling or parent. A remittance service provider facilitates the transfer of funds from the sender to the recipient in exchange for a fee, which is usually a percentage of the amount being sent (World Bank, 2015). Different types of remittance service providers exist within the South African remittance industry. The nature of these RSPs differs depending on the type of remittance channel that is utilized. The 'capturing RSP' is the RSP to whom the sender hands over the funds to be sent to the recipient. The 'disbursing RSP', on the other hand, is the RSP that pays out the funds to the recipient. Depending on the type of remittance network in place, the capturing and disbursing RSP may be one and the same entity or, alternatively, agents of a single RSP, albeit located in different countries.

Regardless of whether or not a remittance is channeled via formal or informal means, some form of network needs to be in place in order for the service to function. Access points at which consumers can hand over funds and conversely receive funds need to be in place and interlinked (Biller, 2007). In regard to the nature of a remittance network, four types can be distinguished, namely unilateral, franchised, negotiated and open networks.

Unilateral remittance networks involve a single RSP and do not utilize the services of any other entities for the purpose of capturing and disbursement. Such networks can only be implemented if the RSP has physical access points in both the sending and recipient countries or if the network is a virtual one. Access points are not physical agents but electronic devices such as computers or mobile phones (see CPSS, 2005:9; Biller, 2007). Unilateral remittance networks are rare due to scarcity of physical access points and lack of access to electronic communications and banking in general.

In a franchised remittance network, an RSP creates a remittance network without owning any of the physical access points. The RSP provides the infrastructure for the messaging and settlement aspects of the remittance transaction and acquires physical access points by inviting institutions in both the sending and recipient countries to offer services as agents of the RSP on standardized terms (CPSS, 2005: 9). This type of network is typically associated with global money transfer organizations (MTOs) such as Western Union which utilize, inter alia, banks and post offices as agents (IMF, 2009: 9).

In a negotiated remittance service network, an RSP negotiates and establishes a network with an institution or institutions, or even individuals, in other countries and by doing so creates an adequate network of access points (CPSS and World Bank, 2007). It is typical for funds to be paid out to the recipient before the disbursing RSP actually receives funds from the capturing RSP with no guarantee of payment aside from the expectation that the capturing agent will settle the amount in future (Biller, 2007).

In an open remittance network, an RSP is able to offer remittance services to customers without owning any access points in the recipient country. It obtains access points by using an open network which any RSP can access (CPSS and World Bank, 2007). These networks are not pre-negotiated and usually, as a consequence, the messaging and settlement aspects of a transaction occur simultaneously. RSPs that are not banks can access the network via banks that they hold accounts with.

The remittance process

A variety of activities transpire within the process of making a remittance transaction. Of these activities, the capturing and disbursement aspects are the most visible to the end user. Messaging and settlement, which transpire between capturing and disbursement, are not as apparent.

Capturing involves the sender paying funds to be sent, as well as the applicable transaction fees, to the RSP or its agent. Payment can be effected by any means acceptable to the sender and RSP and may be done via cash, cheque or account transfer. The mode of payment may be influenced by the nature of the RSP. For instance, if the RSP is a bank, payment is more likely to be effected via an account transfer. Transactions are typically carried out at a physical location such as a bank branch, post office and so forth. However, with technological advancements it is now possible for transactions to be concluded in a virtual location by means of a computer or mobile phone (CPSS, 2005: 40). In South Africa such practice is possible through, for instance, ABSA Bank and Western Union's internet and mobile remittance services. It is usually necessary for the sender to identify themselves and to verify such identity using documents that are prescribed by regulatory authorities. In contrast, minimal information in regard to the identity of the recipient is usually required, with specification of their name being the basic minimum requirement.

Messaging encompasses the sending of information in regard to the transaction from the capturing RSP to the disbursing RSP (Biller, 2007) and is predominantly carried out through the message transmission of the Society for Worldwide Interbank Financial Telecommunication (SWIFT) (BIS, 1999: 158). SWIFT acts as a carrier of financial messages between financial institutions. Depending on the nature of the remittance service, for instance whether it is an open or franchised service, funds and information in regard to the transaction can be sent either simultaneously or independently. In an open service remittance network, funds are usually sent simultaneously with information about the transaction, whereas in other networks, funds are sent separately from the information pertaining to the transaction (CPSS, 2005: 41).

Settlement provides for the actual movement of funds between the capturing RSP and the disbursing RSP (Biller, 2007). The settlement process, depending on the arrangements in place, can be of varying speed and complexity (CPSS and World Bank, 2007). Settlement usually occurs in a 'settlement chain' – a series of separate payments each of which can be made differently – by way of a credit transfer from the payer to the payee's bank. In South Africa, this takes place through the usual process of settlement of obligations between the banks as settlement system participants. In South Africa, RSPs that are not banks cannot directly access the settlement system. They can only access the settlement system indirectly via the banks that they hold accounts with. Unlike payments between end users and agents, which are paid on an individual basis, payments between the agents and RSPs can be batched and possibly netted (CPSS, 2005: 41). In order for netting arrangements to function, it is necessary for a fairly even two-way flow of remittances between the sender and recipient to be in place (CPSS and World Bank, 2007).

Despite the fact that settlement occurs in a chain, it is not always necessary for the disbursing agent to wait for the actual receipt of funds that have been sent in order to pay the recipient. It is possible for liquidity arrangements to be in place, allowing for the disbursing RSP to pay the recipient before actual receipt of funds from the capturing RSP (CPSS, 2005: 41). Liquidity arrangements are more commonplace within franchised networks provided by global MTOs such as Western Union, whereby the recipient may collect funds from anywhere and the RSP will not be aware of which disbursing agent to pay until the funds are actually collected. Liquidity arrangements entail a greater credit risk on the part of the RSP and make it necessary for the disbursing agent to retain greater liquidity. Provision of greater liquidity coupled with the increased credit risk that the RSP is exposed to, are likely to raise the overall transaction costs (CPSS, 2005: 41).

Disbursement entails the payment of funds by the disbursing agent to the recipient. As with capturing, payment can occur via any means acceptable to the recipient and the disbursing agent. Where money is sent via an MTO, the sender is typically required to provide a Multi Transfer Control Number (MTCN) and answer a test question set by the sender. Failure to provide the correct MTCN or answer the set question correctly, prevents the recipient from obtaining the funds from the disbursing agent.

REMITTANCE CHANNELS

When migrants decide to send funds beyond the host country's borders, they have the option of channeling such funds through either formal or informal mechanisms.

Formal channels

In formulating a description of formal channels, reference can be made to the financial department of the International Monetary Fund (IMF), which defines a formal RSP as, "a provider that is regulated and overseen by competent government agencies for its remittance services" (IMF, 2005: 10). Based on this definition, formal remittance channels can be described as being those that are operated within the legal and regulatory framework and that are subject to the supervision of a superior regulatory authority. In the case of South Africa, the South African Reserve Bank (SARB) is the latter authority.

Banks are traditionally an important means of effecting remittance transactions, which can be attributed to their extensive networks in the country and their participation in the National Payment System (NPS). Banks also offer internet as well as mobile transfer services. Previously, in South Africa such services were only available for domestic transfers. All major banks have now introduced such services to their internet and cell phone banking clients, allowing them to send as well as receive remittances electronically (TechCentral, n.d.).

Mobile payments (m-payments) can be described as transactions whereby customers are able to give payment instructions by means of their cell phones, to either a merchant, payment service provider, or, as in the case of South Africa, a bank. Upon being given the instruction, the institution proceeds to pay the specified amount towards the beneficiary (Bester et al., 2010: 6). Transactions, reportedly, take between 2-3 minutes to execute (Rasool, 2010), thereby offering much convenience and appeal.

Migrants who are unbanked have the option of engaging the services of money transfer operators. MTOs are financial companies that provide services in regard to cross-border transfer of funds using either their own internal network or another cross-border banking network (IMF, 2009: 9) The services of Money Gram and Western Union are currently available in South Africa. According to Bradford (2008: 2) these MTOs are two of the worldwide leaders in this field of the formal remittance market.

As an alternative to banks and MTOs, remitters have the option of engaging the services of the post office, which is empowered to remit funds within South Africa, in accordance with Section 46 of the Post Office Act 44 of 1958 (RSA, 1958). In comparison to other formal RSPs, post offices have been identified as having the largest outreach network (IMF, 2009: 9), which encompass remote locations and can prove useful within developing countries that lack adequate financial infrastructure. Post offices either provide their own services for international money transfers or may act as agents of other money transfer agents. They provide remittance products in the form of ordinary money orders and telegraphic money orders, the latter being speedier than ordinary money orders (Genesis Analytics, 2003).

The post office's position within the remittance market is unique in that, unlike its counterparts, it is not subject to the Exchange Control Regulations. This anomaly is attributed to the fact that its services were initiated prior to the passage of the Exchange Control laws (Bester et al., 2010). It is able to offer its services at a much cheaper price, which is partially a circumstance of the fact that it faces no regulatory compliance costs. The post office, despite its unique situation, is not immune from deficiencies. For instance, transactions via the post office take a longer time period and, unlike the services of MTOs such as Money Gram, receipt of funds is not immediate.

In April 2006, Shoprite launched a money transfer service at its money market counters. This transformed the domestic remittance market and set the scene for innovation in the sector. On the retail side, the post office (Post Bank), Shoprite Money Market, Spar Instant Money Pep (various partnerships) and Pick 'n Pay Money Transfer and Mobile Money partnership are amongst the most-used remittance channels. All four big banks have domestic remittance products as well, such as ABSA CashSend, FNB eWallet, Standard Bank Instant Money and Nedbank Send-iMali. Digital or mobile money products include Vodacom M-Pesa, MTN Mobile Money, WeChat Wallet, MobiCash and even Facebook Messenger. Interestingly enough, the Technoserve Report (2016) indicates that approximately 50 percent of all domestic remittance transfers are initiated through bank services, while at least 25 percent of transfers are still cash-based.

Informal remittance channels

The IMF (2005: 10) defines an informal RSP as, "a provider functioning without regulation or oversight of financial supervisors for its remittance services". Taking into account this definition, informal remittance channels can be described as those that are operated outside the legal and regulatory framework. Such remittance channels are often, but not necessarily, illegal (IMF, 2009: 7).

Informal transfers are based on informal relationships and involve a high level of trust between the sender and the RSP. These channels entail a high level of risk, on the part of the sender, as there is no guarantee of delivery and the sender has no legal recourse should the RSP fail to deliver. In the South African remittance market, common providers of informal remittance services are long distance taxi drivers and friends (Genesis Analytics, 2003). When sending funds via taxi drivers, the procedure appears to vary dependent on whether the remitter is a friend or stranger to the taxi driver (Genesis Analytics, 2005). If the remitter is familiar with the driver, transaction costs are lower or even foregone. No record of the transaction is maintained, making trust an essential component. Unlike with a familiar remitter, if the remitter is a stranger, the procedure is more formalized. The sender approaches a taxi association office and together with the driver, who will be entrusted with the funds, counts the amount to be sent. The value of the amount entrusted to the driver is recorded in a book kept at the office specifically for such purposes. The recipient collects the funds from the taxi association office in the destination city or country and is required to know the number-plate of the taxi as well as the name of the driver who delivered the money. Senders are often not insured against losses incurred due to theft or accidents. Taxi drivers, on the other hand, are at times insured against such losses, more specifically in cases where transactions have been recorded in books at the taxi association office (Genesis Analytics, 2005).

Remittances via friends or family are similar to those channeled via taxi drivers and are also highly trust-based. Remittances via these people are favorable as they allow for funds to be sent to recipients located in remote areas where infrastructural facilities may be inadequate or non-existent. Furthermore, transaction costs are low or may be foregone where the relationship between the sender and person entrusted with the funds is close (Genesis Analytics, 2005).

It is submitted that from a risk perspective, on the part of the consumer, formal channels are a safer remittance channel in terms of guaranteeing the delivery of funds to the recipient. Despite this, informal channels, which commonly do not offer a consumer any form of recourse in the event of non-delivery, are sometimes the preferred means of sending remittances. In this regard, one also has to be mindful of the challenges that the remittance payment system encounters as it operates within the National Payment System (NPS). In addition, when formal channels are used, a key consideration should be how financial inclusion can be improved, whilst ensuring that financial integrity is maintained.

DOMESTIC REMITTANCES AND THE SOUTH AFRICAN NATIONAL PAYMENT SYSTEM (NPS)

Background on the NPS

A national payment system (NPS), as defined by the BIS, encompasses a set of instruments, banking procedures, and typically a funds transfer system that allows for the circulation of funds (CPSS, 2005). Aside from the payments between banks, a payment system includes the entire payment process, systems, mechanisms, institutions, agreements as well as laws that are in place and have an impact upon the movement of funds (SARB, 2008).

Before the National Payment System Act 78 of 1998 (RSA, 1998) came into effect, there was no legislation that specifically governed the NPS. The NPS was established, regulated by either common law or in terms of certain provisions contained in selected South African legislation (Lawack-Davids, 2008). The NPS Act, which came into effect on 28 October 2008, is currently the principal piece of legislation that regulates the NPS.

Over the past years, the South African NPS has developed into a complex environment which, for clarity, can be broken down into various inter-linking payment networks. These networks are:

- the customer network;
- the payment network;
- the clearing network;
- the settlement network; and
- the continuous linked settlement network (SARB, 2008).

The customer network encompasses the payment networks that have been put in place by business customers of commercial banks such as supermarkets and public utilities (SARB, 2008). The customer network allows these businesses to partake in the payment system and provide payment services to their clients. The business customers of banks cannot, however, directly access the settlement network and must therefore use the payment networks of participating banks.

The payment network consists of the systems and communications mechanisms put in place by commercial banks in order to provide their customers with facilities and channels to effect payments (SARB, 2008). It encompasses bank-owned automated teller machines (ATMs), internet banking services, branch networks and payment instruments such as cheques, debit cards, credit cards and so forth.

Clearing refers to the exchange of payment instructions, in line with Section 1(iv) of the NPS Act (RSA, 1998). The clearing network provides a forum for payment system participants to exchange payment instructions. Previously only banking institutions were granted access to the clearing network. As the payment system evolved, more non-banking institutions began to participate in the payment system. The Reserve Bank decided to re-evaluate the criteria for participation in the clearing network and as a consequence, non-banking institutions are now able to access the network and clear in their own name (SARB, 2008).

Payment clearing house (PCH) system operators are other participants of the clearing network. These are also referred to as “clearing houses”. The NPS Act defines a PCH system operator as, “a person authorised by the payment system management body to provide clearing processing services on behalf of two or more system participants or a payment clearing house – as per Section 1(xx) (RSA, 1998). In South Africa, one such PCH system operator is Bankserv. Bankserv, which is owned by the South African clearing and settlement banks, is responsible for clearing and determining interbank obligations stemming from the retail payments environment.

A settlement system is defined by the NPS Act as, “a system established and operated by the Reserve Bank for the discharge of payment and settlement obligations between system participants” As per Section 1(xvii) (RSA, 1998). The core of South Africa’s payment system is the South African Multiple Option Settlement (SAMOS) system, which is owned and operated by the South African Reserve Bank. The SAMOS is a real-time gross settlement (RTGS) system and enables settlement participants to settle their interbank payment obligations finally and irrevocably. RTGS systems allow for funds as well as securities transfers to be continuously settled in ‘real time’. Transfers are settled individually at the time that they are received as opposed to them being settled collectively with other transfers at a later stage (see CPSS definition of ‘real time’ and ‘RTGS systems’ in CPSS, 2005: 40-41. Only banking institutions and designated settlement operators have access to the settlement system (see Sections 3 and 4 of the NPS Act, 1998).

The continuous linked settlement (CLS) system interlinks with the SAMOS for purposes of settling the rand leg of high-value cross-border foreign exchange transactions (Lawack-Davids, 2008). Low-value payments such as remittances are not settled within the CLS system. Such cross-border transactions are settled through cross-border banking relationships. (BIS, 1999: 147, 158).

Oversight of the National Payment System (NPS)

The South African Reserve Bank describes the function of overseeing the national payment system as being inclusive of the entire process that is initiated when an end-user issues a payment instruction to pay another person or business, up until the point when the beneficiary receives the payment (SARB, 2006: 11). It covers all the arrangements and procedures that exist to cater for clearing as well as settlement of the payment instruction, and payment towards the intended beneficiary (SARB, 2006).

The efficiency, as well as safety, of an NPS plays a crucial part in ensuring overall stability of the country’s financial sector (SARB, 2008). It is therefore necessary for some form of oversight to be put in place. In South Africa, the South African Reserve Bank Act (SARB, 1989) provides for such oversight. This Act was amended in 1996 in order to clarify the role of the SARB in regard to the national payment system. Section 10(1)(c) of the Act expressly empowers the SARB to, inter alia, perform functions that allow it to regulate as well as oversee the payment system. In turn, the SARB has established a National Payment System Department which bears the responsibility of overseeing the NPS. The BIS has defined the function of overseeing the NPS as being:

> [A] central bank task, principally intended to protect the smooth functioning of a payment system and to protect the financial system from possible 'domino effects' which may occur when one or more participants in the payment system incur credit risk or liquidity risk (BIS, 1999: 37).

The BIS definition of 'oversight' gives a notion of why it is necessary for an NPS to be overseen. Payment systems are subject to a number of risks. These include: credit risks – when a participant will not be able to fully meet its financial obligations within the system; liquidity risks – when a participant within the system will have insufficient funds to fulfil financial obligations within the system as, and when, they become due; legal risks – when a poor legal framework will cause or exacerbate credit or liquidity risks; and operational risks – when operational factors such as technical malfunctions or operational mistakes will cause or exacerbate credit or liquidity risks. A participant who incurs either credit or liquidity risks, may compromise other system participants' capacity, or financial institutions in other parts of the financial system, to fulfil their financial obligations as they become due; hence the need for oversight to prevent this potential 'domino effect'. The risk of detrimental effects being imposed on other participants due to, amongst others, credit or liquidity problems faced by another participant in the system, is known as systemic risk, as outlined in Section 12(1) of the NPS Act (see RSA, 1998, and also CPSS, 2005: 48). It is submitted that the potential threat of systemic failure makes it necessary to control access to the NPS, as well as to monitor the activities of participants.

Remittances, as stated by Bester et al. (2010: 2), are a payment system phenomenon. Providers of remittance services fall within the payment system, albeit at a lower level of the entire system or the 'outer layer', as the author previously described the layers of the NPS (Lawack-Davids, 2008). Remittance transactions can be categorized within the retail payment system of the NPS. The latter systems primarily deal with consumer payments of relatively low value and, in contrast to systematically important payment systems, are generally not viewed as being a threat to systemic stability. These systemically important payment systems service participants with high value transactions and can, in the event of risk exposure, trigger systematic disruptions amongst other system participants or financial institutions in other financial areas (see CPSS, 2005: 5; CPSS, 2003: 48; Competition Commission, 2006). The BIS and World Bank have stated that, taking into account that remittances are low value payments, credit or liquidity failure by an RSP is unlikely to cause systemic risk in the NPS (CPSS, 2005: 18).

The SARB has, however, stated that retail payment systems can collectively form a systematically important payment system (SARB, 2008: 15). Taking the latter into account, this paper maintains that it is necessary for retail payment systems to be overseen. This oversight is also necessary taking into account that these systems facilitate day-to-day consumer transactions and can, in the event of inefficiency and failure, compromise public confidence in, as well as the integrity of, the NPS (Competition Commission, 2006; SARB, 2006: 11).

Given the above, if the SARB oversees formal, as opposed to informal remittances, it would be preferred that formal remittance channels be used. As seen above, it is clear that the preference is for informal remittance channels. One therefore needs to understand the factors that influence the use of informal remittance channels.

The legal and regulatory environment

Like most financial services, remittance services are subject to legislation governing anti-money laundering and combating financing of terrorism. These laws impose obligations to know the customer or customer due diligence, that require financial institutions to gather, what at times can be extensive, information from their clients as well as to report on suspicious transactions (CPSS, 2005: 16). These regulatory requisites may impose compliance costs which can have an impact upon remittance transaction fees.

Regulatory requirements can also bear significant implications for the competition within the remittance industry, especially in circumstances where RSPs are required to be in possession of a license or registered to provide remittance services. A potential effect of the latter would be the limitation of competition within the remittance market by excluding potential RSPs from entering into the remittance industry. That would be the more so, if the fees for licensing and registration are expensive (CPSS, 2005: 17) or where only certain financial institutions are awarded such licenses or are entitled to registration. Economic theory suggests that the less competitive a market is, the higher the price of products and services in the market will be (Neuhoff et al., 2006: 46).

The regulatory environment also potentially constrains competition in circumstances where licensing is a pre-requisite for an individual or institution to deal in foreign currency. Such pre-requisites can compromise a potential RSP's ability to enter into a remittance market.

In providing remittance services, RSPs face a variety of financial, legal, operational, fraud and reputational risks (CPSS, 2005: 18). A mutual concern for all participants in a remittance transaction is the risk that funds will be lost whilst in transition. The question of who bears the risk depends on the nature of the remittance service (CPSS, 2005: 18). In regard to unilateral and franchised networks, the RSP usually bears the risk (CPSS, 2005: 18). This paper argues that the exposure to such risk is inevitably taken into account when providing remittance services and plays a role in determining the costs of a transaction.

Whilst the discussion above gives an insight into the factors that contribute towards the preference for informal remittance channels, it is evident that the government needs to strengthen the risk-based approach with an explicit framework for oversight of international remittances, as the benefits of international remittances for the poor cannot be under-estimated. This can only be achieved if the conditions are conductive and the legal and regulatory framework is sufficiently robust and sound to enable the increased use of formal remittance channels. A stratified approach could be used; that means that the particular payment system should be overseen bearing in mind the risks posed by the product and not only the institution which provides the payment system.

Regulatory gaps and recommendations

The National Payment System Department of the SARB issued a Review of the NPS Act Report (SARB, 2018) which has various objectives, of which strengthening the regulatory framework for domestic remittances is but one. Amongst other things, the review seeks to align the South African Mobile Framework with the Mobile Money Guidelines and the General Principles for International Remittances issued by the World Bank (SARB, 2018). A comprehensive review of the South African remittance market was conducted by the World Bank and finalized in August 2015. The report identified key actions that could lead to enhanced safety and efficiency of remittance transactions within South Africa. This includes the development of a consumer protection framework, financial literacy strategies, the development of governance and risk management frameworks, promotion of competition, interoperability and access in the remittance market (World Bank, 2015). There has been an increased focus on retail payment systems, increased financial inclusion through access to the payment system and coupled with the competition issues, necessitated a review of the NPS Act in alignment with the General Principles for International Remittance Services. With the Financial Surveillance Department of the SARB having made Exchange Control Rulings to enable alignment in respect of international remittances, some regulatory gaps still remain in respect of domestic remittances. Most noteworthy, is that domestic remittances are essentially low-value retail payment services. However, in terms of Section 7 of the NPS Act, these payment services cannot fall within the ambit of payments to third parties, as the payments are ‘not due’ to the beneficiary. Consequently, the SARB does not have the necessary regulatory authority to address remittances as services to third parties. The SARB has developed a payment services engagement paper in consultation with the Financial Sector Conduct Authority (FSCA), established in terms of the Financial Sector Regulation (FSR) Act of the South African Reserve Bank (SARB, 2016).

The aim of this paper is to review the current payment services landscape and to present possible regulatory options. The first option is to issue an exemption in terms of the Banks Act in relation to the definition of deposit-taking or the business of a bank for pooling of funds for purposes of providing domestic remittances. The second option is the development of a regulatory framework for domestic remittances activities and for all domestic MTOs. This should enable MTOs to operate independently from banks. The third option is for Section 7 of the NPS Act to be amended to include payment services where money is 'not due' to a recipient. The enabling provision will be included in the NPS Act to allow for the provision of domestic remittances by non-banks independently of banks.

In the author's view, the combination of a detailed framework for domestic remittances, coupled with an amendment of Section 7 of the NPS Act to cater for the oversight of payment services that are 'not due', would be better. The framework could provide the key policy drivers, such as financial inclusion and financial integrity, the risk-based approach which could be stratified, as well as standards for the provision of domestic remittances. This paper proposes that the amendment of Section 7 of the NPS Act should include the deletion of "to whom payment is due" and the following insertion in Section 7:

> A person may, as a regular feature of that person's business, accept money or payment instructions from any other person for purposes of making payment on behalf of that person to a third person.

In addition, some of the standards for domestic remittances could be included as part of the detailed domestic remittances framework or as directives issued in terms of the NPS Act, as is the case for the practice of third-party payment service providers where payments are due. Furthermore, requirements for licensing of payment services can be provided in the amendment of the Act and a new definition of payment services could be inserted that would make it clear that these would fall under the SARB and offer the necessary protection to the front-end customers of payment service providers, as is currently the case with back-end wholesale customers. This should be aligned with the framework issued by the Financial Surveillance Department with regard to cross-border money remittances, as well as the Payment Aspects of Financial Inclusion (PAFI) Report, issued by the World Bank and the Payment and Financial Market Infrastructure Committee of the Bank for International Settlements (BIS and World Bank, 2016).

The regulatory framework should provide a clear description of payment services, a threshold in respect of low-value transactions, the consumer protection of the funds, capital/prudential requirements, how the system would operate timeously, interoperability, interest accrued, clearing and settlement of transactions, provisions for anti-money laundering and combatting financing of terrorism, supervision, amongst other things.

The opportunity exists to more fully capture the use of remittances as a channel for financial inclusion. This can be done if market participants build more seamless connections between remittance transfer products and other financial services. This could include:

- evolving offerings for interoperability;
- increasing flexible send-options (whether mobile, retail, ATM/bank branch);
- enabling choice of most convenient and comfortable channels and receipt options to make digital payments using remittances received, etc.

If providers of remittance services were to partner with merchant payment solutions on merchant networks, opportunities exist for remittance beneficiaries to make electronic payments directly with money transfers, rather than simply cashing out. Currently, since non-bank providers have to partner with banks, these opportunities cannot be leveraged. This paper proposes that the NPS Act should be amended to allow non-banks to settle transactions in SAMOS, subject to applicable requirements, particularly risk mitigation measures, capital, liquidity, collateral or pre-funding requirements, and so on. In this regard, the NPS Act should have an enabling provision in order to designate non-banks as settlement system participants.

CONCLUSION

This paper has presented an exposition of the various arrangements commonly put in place by RSPs to allow for funds to be transferred from a sender to a recipient across the country, outlining the payment system aspects of the domestic remittance industry. In doing so, it described the various RSPs as well the different channels through which remittances are sent. The paper further examined domestic remittances within the context of the regulatory framework of the NPS in South Africa, delineated the current regulatory gaps and made recommendations for inclusion in a regulatory framework and subsequent revision of the NPS Act. These recommendations pertain to the inadequacy of Section 7 of the NPS Act and put forward suggestions relating to the licensing of remittance services as payment services. Once the amendment to Section 7 is effected, the SARB would be able to license and lay down standards for the prudential and market conduct of the remittance service operators and subject remittances to oversight. This paper should broaden the understanding of the regulatory gaps in the regulation of the South African remittance industry, for those operating in this industry as well as the regulators.

The author argues that unless the risk-based approach is complemented by a framework for the oversight of international remittances, a proper balance between the priorities of financial inclusion and financial integrity will not be reached. The government appears to be serious about promoting financial inclusion as one of its key priorities. Domestic remittances can be a contributor towards this priority if the obstacles highlighted in this paper can be overcome.

In conclusion, it is worth noting Guiding Principle 2 of the Payment Aspects of Financial Inclusion (PAFI) Report as follows:

The legal and regulatory framework underpins financial inclusion by effectively addressing all relevant risks and by protecting consumers, while at the same time fostering innovation and competition (BIS and World Bank, 2016: 60).

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