



CENTRAL BANK OF
TRINIDAD & TOBAGO

safe-tt



safe-tt is a newsletter on developments in the Payments System in Trinidad and Tobago

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If you require any further details on any aspect of the reforms process, or would like to offer any suggestions, then please contact the Payments System Department at the Central Bank of Trinidad and Tobago.

Please see our full contact details on the last page.

Now that *safe-tt* and the GSS have been launched, the *safe-tt* newsletter will now be published on a quarterly basis.

Putting the Pieces Together

Past issues of *safe-tt* newsletters have provided our readers with details of various payments system reform initiatives in Trinidad and Tobago. Terms such as the RTGS, GSS, the ACH and concepts like financial stability, efficiency and risk reduction have become common terminologies used in our articles.

This issue will focus on putting the pieces of the puzzle together by looking at the characteristics of the payments system regime, the market actors and the principles behind the operation of the Payments System in Trinidad and Tobago.

National Payments System

Our payments system can be likened to a machine. Each of its components work together to create an efficient system that facilitates daily business and commerce in Trinidad and Tobago. Did you know that the fact that you can sell a house or a car with ease and receive immediate value for it is a reflection of a healthy payments system?

The 'payments system' refers to arrangements which allow consumers, businesses and other organisations to transfer funds, usually held in one account at a financial institution, to the account of another. It includes the payment instruments – cash, cheques and electronic funds transfers which customers use to make payments – and the unseen arrangements that ensure that funds move from accounts at one financial institution to another.

Payments can be placed into two categories: high value payments



and low value payments.

High value payments are currently defined by the Central Bank of Trinidad and Tobago as those transactions over TT\$500,000 or approximately US\$80,000 in value.

Low value payments on the other hand are below TT\$500,000 and tend to be retail payments made either via cash, cheques, credit cards, debit cards or other forms of electronic transfer.



Cash

Cash is probably the most important instrument for small-retail transactions and for transfers of value between individuals in Trinidad and Tobago. In many cases, cash accounts form a dominant share of the total number of payment transactions.

The ready availability of cash through automated teller

machines (ATMs) has perhaps sustained the use of cash as well. Currently there are over 300 ATM machines distributed throughout Trinidad and Tobago. ATM transactions averaged TT\$9 billion or just under TT\$600 per citizen, per month in 2004 (source: Infolink Services Ltd.).



Credit and Debit Cards

The use of electronic payments has escalated over the years in Trinidad and Tobago. In the retail market alone, during the period 2000 to 2004, there was approximately 82% growth in ATM debit card *switch* transactions only and an 87% growth in Point of Sale (POS) transactions. Further, the number of credit cards in issue has risen by about 32% during this period. At present, four of the six commercial banks in Trinidad and Tobago issue credit cards. They are First Citizens Bank Limited, Republic Bank Limited, RBTT Bank Limited and Scotiabank Limited.

Putting the Pieces Together continued...



Cheques

Anecdotal information will suggest that the increase in usage of credit and debit cards in the retail segment would have reduced the use of cheques for retail payments. Further, with the discontinuation of the cheque guarantee in 2000, the attractiveness of personal cheques would have somewhat waned. Many retailers have refused to accept cheques for fear that they may be dishonoured. With the declining importance of cheques in the retail segment, the use of electronic payment instruments at the retail level has been becoming more popular.

Nevertheless there is still widespread use of cheques. It is estimated that over one million cheques are cleared

each month by commercial banks and a further 200,000 government cheques by the Central Bank. For the last quarter of 2004, an estimated TT\$48 billion in cheque payments was cleared by the Central Bank and the commercial banks.



The RTGS

While low-value, non-cash payments are becoming popular in the domestic market, large-value electronic payments are still slow on the increase. There is a small but growing number of large-value electronic payments being made over Trinidad and Tobago's new real-time gross settlement (RTGS) system called **safe-tt**. With the RTGS, settlement of payments is immediate, compared to the alternative cheque payment which can take up to four days to clear.

The RTGS began operations on 14 October 2004 and to date the

growth in the number of transactions is less than 10%. RTGS payments generally consist of inter-bank transactions, large corporate transactions and government securities settlement transactions.

It is the intention of the Central Bank and commercial banks to encourage the migration of large business payments from paper-based, cheque transactions to the RTGS system. Traditionally cheques have been the common form of payment for large-value payments. The use of cheques however creates an avoidable risk to the stability of the local payments system in the event of default.

Consequently, and given the low usage of the RTGS to date, the banking sector is considering options which would reflect the higher risk and costs of using cheques for large value payments and promote the use of electronic payments. It is estimated that approximately 200 high value cheques are cleared in Trinidad and Tobago each business day.

This represents at minimum a TT\$100 million risk exposure of default each business day!

The government is the issuer of a considerable number of large-value cheques in Trinidad and Tobago. Approximately one sixth of all local cheques in the system are written by government. However there is a move on the government's part to make use of the electronic forms of payment being introduced in Trinidad and Tobago such as the RTGS and ACH. The government is automating a number of its systems and making internal arrangements to facilitate the use of electronic payments.

With the RTGS on board and the ACH to soon join the cadre of payment options, the consumer in Trinidad and Tobago now has a wider choice when making his/her payments. Electronic payments are safe, fast and an efficient way to make payments. ■

Payments Clearance and Settlement in Trinidad and Tobago



While a cash payment effects immediate transfer of value, other forms of retail payment require some form of "back office" processing in a procedure known as "clearings", which is the process of validating and netting all payment instructions. Most payment systems involve two or more financial institutions, requiring payments to be "cleared" between them.

Cheque Clearings

Details of a cheque drawn on one financial institution (drawee bank) and deposited at another must be returned to the first financial institution so that it can verify that its customer has sufficient funds to debit the customer's account.

Arrangements for clearing payment instruments in Trinidad and Tobago are done by the Central Bank for TT-dollar cheques and by commercial banks for US-dollar cheques drawn on local banks.

The Central Bank is mandated under the Central Bank Act to operate the clearing house for cheque payments. The commercial banks and the Central Bank meet on a daily basis to clear TT-dollar cheques. Here, each bank tallies the cheques presented for payment at its institution and offsets this amount against the tallies of other banks. The net value for each bank is agreed upon and confirmed by the Central Bank for final settlement on the RTGS. This is referred to as multilateral net settlement.

The commercial banks meet to clear US-dollar cheques, drawn locally, in a similar fashion to the process conducted at the Central Bank.

Other Clearings

Other payments clearing systems independent of the two mentioned include credit cards and the LINX© switch for electronic transactions.

Settlement

When payments are cleared between institutions, they accrue obligations which must be settled. In Trinidad and Tobago, final settlement of obligations occurs at the Central Bank.

Large-value payments made through **safe-tt** are settled one-by-one on a real time basis. Here, the reserve accounts held by

commercial banks at the Central bank are debited and/or credited. When the Automated Clearing House, called TTIPS, begins operations, its electronic payments will also be settled on a deferred net settlement basis at the Central Bank via the RTGS.

There are **two** securities clearance and settlement systems in Trinidad and Tobago: the Government Securities Settlement (GSS) system (owned by the Central Bank) which settles trades in government securities; and the Trinidad and Tobago Central Depository (TTCD) which clears and settles equity and secondary market government bond trades. The TTCD forwards net funds settlement values to the Central Bank for settlement on the RTGS. ■

The Role of the Central Bank in the Payments System

A safe and efficient payments system is essential to support the day-to-day business of the local economy and to settle transactions in its financial markets. Accordingly, the Central Bank has important regulatory responsibilities for the payments system and plays a key role in monitoring its operations.

This responsibility is reflected in the Bank's introduction of the RTGS system for large-value and time-critical payments. The RTGS minimises systemic risk within the financial system. It offers a safe, quick and guaranteed means of making payments.

Oversight of payment systems falls under the Bank's financial stability obligations. The Payments System Oversight Department of the Central Bank will oversee

payment systems in Trinidad and Tobago. The Department will be responsible for promoting safety, confidence and efficiency within the payments system.

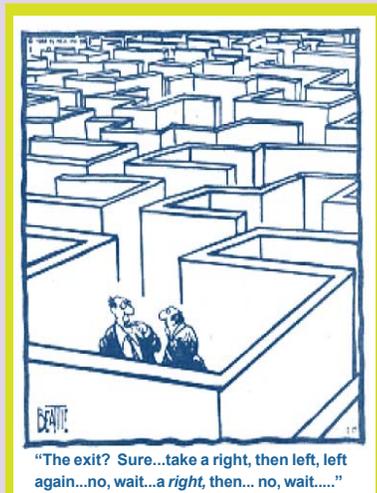
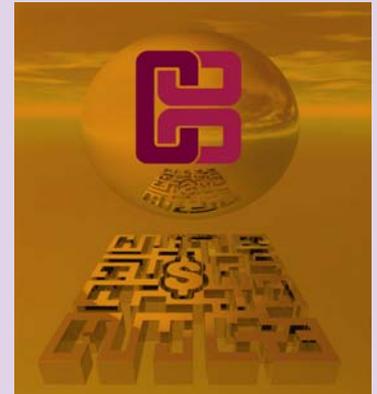
Trinidad and Tobago is among the first countries in the Caribbean to adapt an integrated approach to reform of the payments system. This is part of the wider financial sector reform as outlined in the White Paper on the Financial System of Trinidad and Tobago, 2004.

The Bank has formed a Payments System Council to support the achievement of sound and efficient payments and securities clearance and settlement systems in the country. Through the Council, the Bank consults closely with participants in the payments industry. Additionally, the Central

Bank participates in a number of international groups focusing on payment systems.

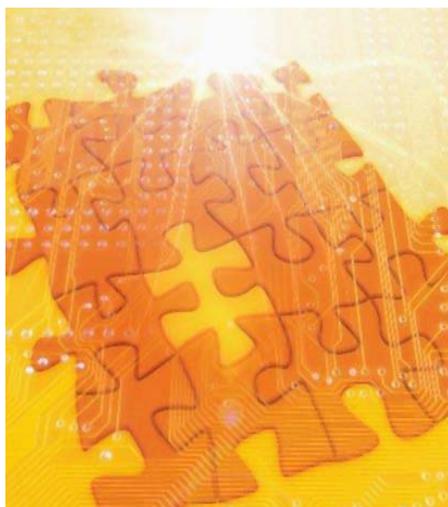
Apart from being the issuer of currency notes and coins, the Central Bank has three roles in the domestic payments system:

- 1) responsibility for oversight of payments clearance and settlement systems, with the objectives of controlling risk, and promoting efficiency and competition;
- 2) the provision of facilities for final settlement payments system obligations; and
- 3) participation in the payments system as banker to the government of Trinidad and Tobago. ■



The *safe-tt* and GSS Volume Meter

The actual volumes of payment transactions to date are as follows:-



Date	Safe-tt	GSS
October 2004	860	—
November 2004	1527	—
December 2004	1751	275
January 2005	1681	563
February 2005	1345	329
March 2005	1784	541
April 2005	1671	437
May 2005	1639	376
June 2005	1734	330
July 2005	1877	710
August 2005	1731	229

Economic Impact of the Reform of the National Payments System in Trinidad and Tobago - Part 1



It is acknowledged that the establishment of a Real Time Gross Settlement (RTGS) system, called **safe-tt**, and other elements of the payments system reform – the Government Securities Settlement (GSS) system and Automated Clearing House (ACH) – will have a number of benefits for the financial system and for the economy as a whole. The move from an essential manual clearing and settlement system to an electronically-based one is expected to significantly reduce systemic, credit and liquidity risks. At the same time, the efficiency of the payment services provided by the commercial banks to their customers and by the Central Bank to the commercial banks would be greatly improved, and should generate cost savings in the long term.¹

In the manual paper-based system that obtained in Trinidad and Tobago until September 2004, settlement of large-value inter-bank payments was done on a deferred net basis. Under this arrangement, an accurate assessment of liquidity levels of the commercial banks could not be done on a real-time basis. Consequently, the system as a whole was made more vulnerable to credit and liquidity risks if the payer were found to be temporarily illiquid. However the maintenance of a relatively high reserve requirement provided a buffer against risks of this nature. One of the major advantages of the establishment of **safe-tt** is the reduction in settlement risk. For real-time settlement to take place, the funds must be available for the successful completion of the

transaction. In this way, credit and liquidity risks are virtually eliminated. The settlement is safe and secure.

In September 2003, the Central Bank announced a phased reduction of the reserve requirement of commercial banks from 18 per cent to 9 per cent of prescribed liabilities, in order to bring the ratio in line with that of the non-bank financial institutions. This represents the partial removal of the buffer against settlement risk in the payment system. However this risk has effectively been eliminated with the establishment of the RTGS system.

The conduct of monetary policy by the Central Bank should be greatly enhanced. In the old system, real-time data on liquidity was not

available as the Bank operated a net deferred settlement system which meant that the impact of a day's transactions, particularly the large-value payments on liquidity levels was not known until the end of day. With the establishment of **safe-tt** and imminent start-up of the ACH, the liquidity levels of the commercial banks should be available on an ongoing basis. Early warning signals of potential systemic risk would now be available to the Central Bank and its ability to take appropriate action should be enhanced.² An efficient payment system is essential to the health of the financial system and of the economy. ■

Part 2 in next issue...

¹ Regrettably, quantitative data are not available to adequately measure the economic impact of the payments system reform in Trinidad and Tobago.
² A systemic risk may arise if a commercial bank cannot meet its payment obligations in the payment system, which may cause difficulties for the other commercial banks and for the entire system.



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