
THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: Right morning ladies and gentlemen, we are carrying on with hearings today on the National Payment System. The roll for today, we will have PASA, Standard Bank and then Nedbank and Standard Bank later. Yes PASA then we will break for tea, Standard Bank, lunch and then Nedbank this afternoon. Right just a housekeeping matter; please can you switch off your cell phones? Yesterday we had a misfortune of a cell-phone which was on again. PASA team, I would like to welcome Mr. Pierre Coetzee...

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MR. COETZEE: Thank you Mr. Jali...

CHAIRPERSON: Mr. Johnny Piennaar...

MR. PIENNAAR: Thank you Mr. Jali.

CHAIRPERSON: Nick Altini.

MR. ALTINI: Thank you Chair.

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CHAIRPERSON: And then lastly Mondo Ntlha.

MR. NTLHA: Yes thank you.

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: Welcome, right we can start. I do not know whether you have prepared a presentation?

MR. COETZEE: We have.

CHAIRPERSON: You have prepared a presentation?

MR. COETZEE: Yes.

10 CHAIRPERSON: So we start with your presentation, thereafter we may just go on to if you got any questions, ask some questions just for clarification.

MR. COETZEE: Thank you Mr. Jali, members of the panel. We will be providing you with a few diagrams which have been simplified for understanding purposes.

PASA has provided you with our submission on 17 May and this presentation should be read in conjunction with our submission. We have also provided you with the PCH agreements and Clearing Rules under confidentiality.

20 In any payment system or a PCH, we have at least the following three factors or tensions. Firstly we have the business issue, which relates to innovation and it relates

THE NATIONAL PAYMENT SYSTEM

to competitive issues between the banks individually. You will see the overall there that is the business aspect of a payment system.

Once two or more banks have agreed to establish a PCH or payment system, it will move in the regulatory environment. The regulatory environment is the PASA environment where rules, PCH agreements are developed to govern risk and operations. PASA was established in 1996, the Act was promulgated in 1998. At that point in time, PASA and the Reserve Bank discussed the main issue and that was to govern settlement. You will see there on the board, it is not very clear that the purpose of that was... is concentrated on and focused on settlement and that was to move next day batch settlement to inter base settlement.

The drafting of PCH agreements, clearing rules and processes for BCP and DRP..., one thing that I have left out is the next day settlement to same day settlement as I said, exclusively for the purpose of governing settlement risk. At the time the NPS Act provided for entities participating in the NPS, however, with the promulgation of the amendments to the Act, this situation was clarified.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

You will now see on the screen Section 4(2)(d) which provides for a non-PASA members banks wishing to participate in the payment system through an arrangement with a PASA member. Now the crux of Section 4(2)(d) is that settlement will be the responsibility of the PASA member bank. It also provides for system operators, Section 4(2)(c) and you will clearly see the rectangular in red there. That is the regulated environment and that is the PASA environment currently.

10 Underneath you will see the non-regulated environment and that is where system operators are currently sitting but they will be governed in terms of directives and criteria to be issued by the SARB.

In addition the Act provides for Section 7, service providers. These are service providers such as the beneficiary service providers and payment service providers. These are persons who as a regular feature of their business, except money and make payment in respect of payment that is due to a person. Now we could in our further discussions relate that to perhaps the float or deposit taking.

20 This is the normal transaction flow of any PCH, very simplified but that is to understand it better. A client of B1 would definitely go to a merchant of a system

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

operator, the transactions will flow to B4 then to the PCH system operator and back to B1.

The system operator in this scenario is acquired by B4. B4 is responsible for the risks introduced by the system operator. There is clearing, inter bank clearing between B1 and the rest of the banks. In the event of any complaint, a client may go to his bank that bank will in then in terms of the PCH agreement and rules, approach his counterpart to resolve any issue the client has.

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At this scenario we have a difficult sort-at-source arrangement. Once again very simplified but once again to just explain the picture, the system operator as we call it now for convenience purposes is not acquired by B4. The system operator is also not regulated, will be when the directives are issued. There is no clearing between B4 and the rest of the banks. There is no inter-operability and the risks that may be introduced in the system will be born by the client.

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For instance, if the client has a problem, he goes to an ATM, draws money or it shows on the slip 1 000 and he only gets 500, where does he go? Now the consequence of sort-at-source, it was mentioned by some of the banks previously and

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

also by Bankserv yesterday that there will be consequences on sort-at-source. We have listed a few of those consequences: inter bank clearing; inter-operability; centralised clearing; infrastructure settlement et cetera, et cetera.

10 The view is that those consequences are not quantified at this point in time. It was also mentioned that there maybe unintended consequences. We do not know what the impact of Sort-at-source will be. I believe if a scientific study is undertaken we might get closer to the truth that is why we made a question mark on the PCH system operator representing the centralised clearing system. Just to refresh your memory, this is the normal clearing process.

Multi banking, we have explained in our submission the position about multi-banking. A bank could be multi-bank for instance in KwaZulu-Natal with Bank A and with Bank B in Gauteng. The bank is or the institution is not bypassing clearing in Gauteng it will be introduced through Bank B, KwaZulu-Natal, through Bank A. You could also per association, you could be acquired per association and that is not
20 the bypassing of clearing must be understood.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

The Reserve Bank is ultimately responsible for the NPS. Within the NPS, PASA has its role and mandate. You will see the red circle there. The mandate includes SAMOS, the PCH system operators and the banks. That is in terms of the NPS Act. However the Act also provides for the system operators as I have said, who are not regulated at this point in time but will be in the not too distant future, Mr. Jali that is our presentation, short and sweet, if you have any questions?

10 CHAIRPERSON: Right you will let us have copies of the slides and also let us have them electronically.

MR. COETZEE: We have already provided Charles with...

CHAIRPERSON: You have already provided, alright that is Exhibit UU. Right now I just want to, firstly before I give all the others an opportunity to ask questions for clarification, just about one..., couple of questions for you on issues relating to your submission then anything else. Last year there was a presentation by Mr. Pelsler, I think.

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MR. COETZEE: That is correct.

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: In which he made reference to the fact that..., it was taken as Exhibit AA, talking about clearing and said..., I do not know if you have that slide? The old presentation...

MR. COETZEE: I should have it with me, yes.

CHAIRPERSON: It was slide 12.

MR. COETZEE: Well you can proceed, I can get to my...

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CHAIRPERSON: Right, the question which you put up was “which banks may clear,” and then the very first bullet point was “any bank registered by South African Reserve Bank,” that is the member of the Banking Association.

MR. COETZEE: Yes.

CHAIRPERSON: Right now there was an issue with that. I do not know whether that was cleared with the Banking Association at a later stage. There was an issue with that as to whether it is actually a requirement for one to be able to clear and if so in terms of which provision was that a requirement.

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THE NATIONAL PAYMENT SYSTEM

MR. COETZEE: The requirement to be a member of PASA. PASA has basically four criteria to be able to become a member of PASA. The one is, you must be a bank and the second one is you must be a member of the Banking Association. That is a PASA requirement.

CHAIRPERSON: That is a PASA requirement?

MR. COETZEE: That is a PASA requirement.

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CHAIRPERSON: In terms of what?

MR. COETZEE: In terms of our PASA regulatory framework.

CHAIRPERSON: That is in terms of your own regulatory framework?

MR. COETZEE: Yes.

CHAIRPERSON: Is it a part of any legislation?

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MR. COETZEE: It is not part of any legislation.

CHAIRPERSON: So you just impose that?

MR. COETZEE: Yes.

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: Okay we get back to that. Just wanted to get clarification on that whether it is still your position because...

MR. COETZEE: Well...

CHAIRPERSON: There was uncertainty the last time you were here.

10 MR. COETZEE: We have taken cognisance of the fact that this might be perceived to be a barrier to entry and PASA is currently involved in considering whether that requirement is still required. We might adopt....and the purpose of the requirement was to force and that might sound a bit strong, to force your member banks to subscribe to a Code of Conduct. Now the way to overcome that problem is to adopt the appropriate parts of that Code of Conduct in your rules and not to impose the requirement could be a member of the Banking Association.

CHAIRPERSON: Yes because my understanding is definitely out there the Banking Association is a voluntarily association.

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MR. COETZEE: Yes.

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: Now if they are imposing that requirement it stops being a voluntary association.

MR. COETZEE: Absolutely.

CHAIRPERSON: Yes.

MR. COETZEE: Absolutely and that is...

10 CHAIRPERSON: Now that is why we had..., we took issue with it the last time.

MR. COETZEE: Yes that is why we are...

CHAIRPERSON: If you want to the Code of Conduct to be part of the requirement why can he just say "you must subscribe to a Code of Conduct?"

MR. COETZEE: That is what we are looking at in this point in time. We are in a...

20 CHAIRPERSON: You get what I mean? You have lifted the bar, basically unnecessarily when...

MR. COETZEE: Yes...

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: It is not a requirement because what you are trying to achieve is that they must have the Code of Conduct, so why can you not just say so?

MR. COETZEE: That is an actual fact with we..., are doing. We have proposed council, to PASA council resolution to approve the new structure without that requirement and with accepting appropriate parts of the Code of Conduct.

CHAIRPERSON: We will get back to that. Now there is a couple of other issues
10 that I want to raise with you relating to your additional submission dated 16 May 2005.

MR. COETZEE: Sure...

CHAIRPERSON: Sorry 2007, I am still two years behind here. Why is the PASA constitution confidential?

MR. COETZEE: Well maybe I should ask my lawyers to assist me there but it was
20 deemed at the time when we disclosed all the documents to the Competition Commission to adopt this approach to..., because at this stage we do not know exactly and we have not identified the clauses clearly, which may or may not be confidential and just as a matter of fact, we adopted that approach, yes.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: So you adopt it...the reason for adopting the approach is because you were not sure which clauses are confidential? So the entire document becomes confidential?

MR. COETZEE: That was our approach, yes.

CHAIRPERSON: Well that really without saying..., I am a bit surprised by the answer but anyway, why will a clause of a constitution be confidential?

10 MR. COETZEE: I cannot think and knowing the constitution very well that there are clauses that are confidential and we do not have a problem...

CHAIRPERSON: But why..., then what is...

MR. COETZEE: In lifting the confidentiality.

CHAIRPERSON: Yes, then why did you seek confidentiality on the entire constitution? I cannot come to terms of why any organization will say its
20 constitution is confidential, unless it was a secretive organization.

THE NATIONAL PAYMENT SYSTEM

MR. COETZEE: Yes it is definitely not a secretive organization. The constitution is available to any member bank. It is also available on our PASA intranet, so it was just from maybe legal assistance that we have received but as I said...

CHAIRPERSON: Are you saying this was legal advice to say the document is on the Internet, it is freely available, yet it's confidential?

MR. COETZEE: Yes that is what we are saying.

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CHAIRPERSON: That was legal advice?

MR. COETZEE: In respect of our disclosure to this Competition Commission...

CHAIRPERSON: No, no, no I am just trying to seek clarification so that we can understand, was that legal advice that..., although it is available on the internet to the public, it is still confidential?

MR. NTLHA: Mr. Jali if I could assist there. I think the submission that Mr.

20 Coetzee is making is that the document is not available on the Internet. It is available on the intranet which is a closed system only available to the banks. As far as confidentiality is concerned, from PASA's perspective that would have required the

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

consent of the member banks for them to make it available on the basis of that it was claimed to be confidential as at that time, no permission from the member banks had been sought and as I understand, we can take instructions as to whether PASA maintains the confidentiality.

10 CHAIRPERSON: Maybe that is what we needed to deal with that but I have got other issues as well. We will give you opportunity to take those instructions because we really find it difficult for us to...., I mean to operate under these circumstances, when people claimed confidentiality even on names of people sitting in committees? That is what is going on here, we get people saying the entire page is confidential and when you look at the page you find that it is just names of people sitting in a certain committee. But let us move on. And why is the PASA regulatory framing including the application form for membership of PASA confidential?

MR. COETZEE: Mr. Jali...

20 CHAIRPERSON: Because that is again..., confidentiality has been claimed with regard to that.

THE NATIONAL PAYMENT SYSTEM

MR. COETZEE: Well I have been assisted by Mondo in the sense that at the time of disclosing this to the Competition Commission, we did not obtain the necessary sign off from our members and we felt that it might be necessary to do it this way.

CHAIRPERSON: Well your members have been appearing before the commission and all of them have been saying they want to cooperate and then in saying we will get PASA to come here, we will get documents, we will get PCH agreements to be given to you. Now we do not understand this. That is why we do not understand how we can...,how we expected to function and to come up with recommendations which will suit the general public of South Africa, if this is happening.

MR. COETZEE: Mr. Jali yes, we take cognisance of that concern and as I indicated, we do not have a problem in removing confidentiality as far as the constitution and application form is concerned. At the time and I think you will appreciate that we have at this point in time although it was indicated that we have 21, at present we only have 20 full members and to consult with all members without knowing which impact it might have on each of those members because only a few numbers of those members appeared in front of this commission. So in consultation with our members we would not have a problem to disclose.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: Well, I know, I think Ms Nyasulu has got some questions, a follow-up question to these so I will let her ask but I am a bit surprised. I mean we started sitting ..., this was announced as early as August last year, we are now in May so it has not been possible to round up all the members to get permission? But anyway, I will leave it at that.

10 MS NYASULU: Mr. Coetzee and your team, thank you very much. Can I just say, you know as a direct follow-up to the questions that the Chairman has asked, that it has come up as a regular feature of the governance structure of PASA that to a large extent the tail wags the dog and I think if I could just really ask PASA to look at how in its..., the way it is structured itself in governance that its members are able to tell it what it can and cannot do. It should be the other way round, so if you could in looking at all of these things that we have been asking, have a look at whether the governance structure of PASA and how you relate to your members, is really a healthy relationship. They have a lot more power than members should of a

20 particular system, particularly of a regulatory nature such as yours.

But just before I ask my questions, can I just..., the document that you submitted on the 17th ..., I am going to let the Chairman finish up his line of questioning.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: Again, the same issue relates to the constitution of PASA PCH participant group, again I still do not understand why is it confidential unless you are going to give me the same answer?

MR. COETZEE: Absolutely Mr. Jali, I do not have any other response.

CHAIRPERSON: The same question with regard to entry and participation criteria for the authorization to act as the PCH system operator, again why is it confidential?

10 It looks like we have claimed to confidentiality almost everything, which we need to deal with for purpose of understanding exactly, because PASA is about the governance of the banks.

MR. COETZEE: Yes.

20 CHAIRPERSON: It is all about the governance of the banks and you seemed to be claiming confidentiality on all the documents that relate to the governance so that we clearly understand what is happening. The table contained in paragraph 7.7.2 of your submission, you have also said it is confidential. A table which contains a chronology of communications between the Reserve Bank and PASA, is just a . . . , it

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

is not even the contents just the chronology of the communication and you claim that as confidential.

MR. COETZEE: That is communications received from the Reserve Bank and we felt that it might not and we were also at some point in time approached by the Reserve Bank as far as one communication is concerned. It was a concern from the Reserve Bank that the letter addressed to PASA was leaked or was disclosed to entities out there and on that basis we deemed it necessary to be confidential.

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CHAIRPERSON: Yes but I hear what you are saying, it is not the contents of the letter, it is just the table. A table saying...

MR. COETZEE: Yes I see.

CHAIRPERSON: It is the table and claiming confidentiality on a table which says these letters were written.

MR. COETZEE: Although the...

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CHAIRPERSON: We have not asked for the contents of the letter or understanding we claimed confidentiality on the contents.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. COETZEE: I understand that Mr. Jali but if you look at the fourth row of column, it deals with a certain extent with some of the contents of that letter, that is..., and each one of those lines does not necessarily only refer to the letter dated so and so of the Reserve Bank, it deals with the message, the main message of the letter received from the SARB.

10 CHAIRPERSON: I think this letter was sent to almost the whole lot of people and evidence has been led about this letter before this commission and that is the letter which was dealing with the moratorium on sorting-at-source.

MR. COETZEE: Some of those issues were...

CHAIRPERSON: It has been discussed in this Enquiry since last year so I..., that is why I do not understand. Even if you had claimed confidentiality in respect of that, I will understand, then we will debate it but you are claiming the entire table. You could have.... because your confidentiality claim could have only been limited to the
20 March 2, 06 letter.

MR. COETZEE: Yes.

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: Not the entire table but even then it would have been debatable.

You see that is why we have difficulty about..., in the way PASA is conducting its business, which is supposed to be governance body and ensuring that is proper governance when it comes to the way banks do their business. Anyway, sometimes people say “we lead by example” but anyway, I will let Ms Nyasulu carry on with the questions.

10 MS NYASULU: Thank you Chairman, can I..., if I could refer you to the document that is dated, I think 15 May 2007 and then in the light of some of the things that we have talked about, the need in terms of your mission statement to be equitable, fair and ensure that the system is accessible.

20 Can I just refer you to the pages starting after your blue section, and I am sure it is an oversight on your part, but under the mission statement that document clearly has two pages because it is one of two and page 2 of 2 is missing and the following one which pertains to the structure, which are all the documents we need to understand the governance, clearly that one has five pages, page 2 of 5 is missing and page 4 of 5 is missing in that document.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

And then the document that relates to policies and principals of PASA, again it is a document with four pages, page 2 of 4 is missing and then finally the document on membership, which again is really critical to our understanding of what is happening, it is a document with seven pages. Page 2 of 7 is missing, page 4 of 7 is missing, and page 6 of 7 is missing. Could you explain why those pages are not in the document?

10 MR. COETZEE: Ms Nyasulu I must apologise for this situation. We have printed these pages double sided and I cannot explain how this happened and why this happened. In actual fact I am sitting with a version, which are printed double sided and I can provide you with that version. I know this will not assist you in this short period of time but it was not purposely done.

MS NYASULU: Okay.

MR. COETZEE: It was inadvertently done, I cannot explain.

20 MS NYASULU: Okay if you could make those available to us, please because as I said there are some critical questions we have on the governance and all of these things relate to governance and we need to understand those, so if we could have a complete document that would help.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

Can I then ask you specifically on areas where PASA has jurisdiction and maybe start with a question about whether is Bankserv or Visa or MasterCard are those all, are those in anyway, anyone of those members of PASA?

MR. COETZEE: They are not members of PASA, they are PCH system operators authorised in terms of the criteria approved by the Reserve Bank.

MS NYASULU: Okay and is it then feasible that someone who is not a member of
10 PASA and my understanding is in one form or another, you have to be a member of PASA to get full access to the National Payment System.

MR. COETZEE: A member of PASA is entitled to clear and settle and that deals...

MS NYASULU: Which is the...,

MR. COETZEE: With the full...

MS NYASULU: Full access...

20 MR. COETZEE: Access.

MS NYASULU: Yes that is inner core.

THE NATIONAL PAYMENT SYSTEM

MR. COETZEE: Absolutely yes then.

MS NYASULU: Okay now I need to understand because in a lot of the documentation and all the banks used that same circle and wheel what we talked about yesterday. It is all their documentation and I imagine it is well-known to PASA as well.

All of those, the Bankserv's and the MasterCards and the Visas who are the system operators, are really portrayed as sitting in the outer core but the reality is, we know that those are operating within the inner core and I would like to understand what sort of dispensation makes it possible for some operators who are sitting in the outer core as per your..., that diagram, which says that anyone in the outer core is basically kept as far away from the inner core of clearing and settlement, when in reality we know that they are in the inner core. By what dispensation are those allowed into the inner core?

MR. COETZEE: Look I appreciate that the panel is fully aware of the provisions of the Act which very clearly stipulates that only banks who are members of PASA may clear and settle...

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MS NYASULU: Exactly.

MR. COETZEE: When you enter the NPS and you provide a service, you must decide on your own business case where you want to participate. If you want to become a bank you can grow your business and you can enter the inter core at this point in time. If however, your business model only allows you and if that is your intention, to only participate in one of those onion, we called it Mr. Piennaar's onion, if one of those rings outside, and that is your business, that is where you participate.

10 There is no rule preventing you from entering the inner core.

MS NYASULU: Yes.

MR. PIENNAAR: I think just to assist the Bankserv, Visa and MasterCard is so-called PCH system operators...

MS NYASULU: Understood...

MR. PIENNAAR: Provided for in the Act and that is the dispensation that they have got. It is provided for in the Act. They can only become PCH system operators provided two banks; at least two banks appoints them. Now it is free to any bank to negotiate with another bank to appoint another PCH system operator upon which

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

they will then come to PASA and ask them for authorisation of that particular PCH system operator.

MS NYASULU: Thank you Mr. Piennaar, may I just interrupt you, I do quite understand all of those rules and how they come about. What I am trying to understand is the misalignment between the criteria that are set by PASA for who operates in which part of your onion, to use your term, and I am trying to understand whether there are exceptions to some of those rules in terms of, by some special
10 dispensation you are not a bank, you are not this and you are not all of those, you are called something else but you are actually in the inner core of your onion.

And just to follow-up also on that question, we do know that those system operators do clear and settle on behalf of the banks. So in effect it is an outsourced role which allows people who do not fit all the..., if you follow the letter of your requirements for who should be in that inner circle, they do not fit that. They are service providers who do not fit all of these criteria that you have said.
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MR. PIENNAAR: But I think to be quite honest, the Act never intended to close down the inner core except in relation to clearing and settlement of banks and that

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

particular part of the Act was never intended to then say but the banks are not allowed to use a system operator to assist them. Instead the Act actually acknowledged that it may happen and therefore it provided for the PCH system operator.

10 So I am not certain if you are relating to exceptions that currently exist and if you can give us example that would obviously assist in our answers, but certainly we do not know to our mind or to my mind at least, that there is exceptions to the rule currently in the inner core outside of what the Act allows.

MS NYASULU: Okay, the point that I was making is that it seems to me that there is an exception as relates to the criteria which then allows the system operators a different kind of dispensation but we will come back to that later. Can I ask you what assistance there is for non-clearing banks that wish to become clearing banks? What is the process to assist non-clearing banks to become clearing banks?

20 MR. COETZEE: Any bank registered in South Africa may become a clearing bank and once again back to the choice of the bank in the bank's business model, whether that bank wishes to be sponsored through an arrangement with a current PASA

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

member bank to . . . , and that is Section 4(2)(d) 1 and 2 of the Act which provides and allows non PASA member banks to enter the payment system irrespective clearing and settlement.

Any other banks wishing to become a member of PASA may submit an application, become a provisional PASA membership, it is then approved by the PCH and then it obtains full PASA membership. Such a bank and that is one of the requirements, will also have to be mentored for a period of three years in that PCH and that will enable
10 the bank to grow its business until it is a fully fledged direct clearing bank.

MS NYASULU: Did you say three years or three months?

MR. COETZEE: It is definitely three years.

MS NYASULU: Three years?

MR. COETZEE: Yes.

20 MS NYASULU: Okay I was not quite sure because we were under the impression that it is a mentoring relationship for three months.

THE NATIONAL PAYMENT SYSTEM

MR. COETZEE: There is a notice period of three months but it is definitely three years...

MS NYASULU: But is definitely three years.

MR. COETZEE: Yes.

MS NYASULU: Okay, are you aware of any bank that has currently been mentored but which has had difficulties getting into clearing?

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MR. COETZEE: I am aware of new banks coming or joining PASA, who do not have the resources or the expertise to enable them to efficiently participate in the payment system, I am aware of those.

MS NYASULU: My question was whether you are aware of any bank which is currently being mentored but has no access to clearing.

MR. COETZEE: No.

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MS NYASULU: No, thank you. If we could proceed to..., in the event of one of the banks failing to cooperate in terms of allowing a proposed change to a PCH...

MR. COETZEE: Yes?

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MS NYASULU: What authority have you got to get that bank to cooperate?

MR. COETZEE: To respond to that question we need to understand the underlying structures that govern this picture. Any bank participating in a PCH has in terms of the PCH participant's group constitution, a right to participate and a right to vote. So it is a majority not volume based or value based, it is one bank one vote. The constitution also provides for a majority vote.

- 10 So should you have a scenario where one bank is outvoted, that bank will have to accept the decision of the PCH participant group but it has access to an escalation process to PASA council. It will first through..., go through a process with the PCH participant group, then to PASA council and then to the Reserve Bank who will ultimately decide whether the decision was unfairly impacting on that member.

MS NYASULU: Okay, can I just distinguish between voting because voting as on the basis of an issue and you know one would assume that there is no disagreements
20 about the rules. The example that I am talking about specifically relates to changing of the rules within a PCH. We have heard over the course of the hearings from a number of banks that certain things could not be done because they are not currently

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

in the PCH rules and it would take close to three years to get everyone to agree to a change of the rules. Now as we understand it, there is a mechanism to ensure that no one member can slow down processes. If that happens, what authority has PASA got to get to move and nudge that member along?

MR. COETZEE: Once again if I could just be allowed to put this into perspective, I..., we have showed the three impacts or tensions on any payment system. We have alluded to the fact that business and innovation sits outside where two or more banks may decide to establish a payment system or PCH and once they have agreed to establish that PCH, it moves into the PASA regulatory domain where rules and PCH agreements are drafted to govern ops and crisp issues.

If there is a slowest mover in a PCH and that slowest mover is outvoted, the slowest mover is compelled to join the rest of the banks. For instance, if we have a rule change and that rule change impacts on such a member that you will implement the certain system by such and such a time and to..., we must understand it takes place on firstly, on a consensus basis. It gives each bank a reasonable time within which to implement those systems. So we do it by consensus, we do it by project management and we ensure that all the sheep are in.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

But if that is not possible and it goes for about the last member will have to follow. PASA do have mechanisms. We do a dispute resolution process. We have PASA penalty rules in terms of which we can enforce that. We have..., never had the need to impose the penalty rules so far and that is the process that we have in place but according to my mind it is never been necessary to implement any of those measures because as I said the nature of our environment is cooperation and regulation.

10 MS NYASULU: Mr. Piennaar you want to add to that?

MR. PIENNAAR: I would just like to enlighten specifically in relation to systems because systems is difficult. Systems is difficult to change sometimes, sometimes some people take longer than other people and specifically at that points in time these PCH system operators becomes very important because in such instances you can go as fast as the fastest two players and then let the other... allow the others to catch up. Because all what you do is at system operator level, which is PCH system operator
20 level which is one entity, you then provide the old systems to carry on as well as the new systems to start running and then in time they catch up. And that is why that PCH system operator in that environment is so important.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MS NYASULU: I think I agree with you Mr. Piennaar but the system operator and the systems would really come in at the implementation stage. I am being a bit clumsy in trying to explain to you where I am getting to, so let us just maybe go back to some of the discussions that have happened on ATMs and the direct charging model for instance, where one of the issues raised by some of the banks was against a direct charging model, was that it would take so long because it would have to..., we would have to change the PCH rules and regulations and it would take close to three
10 years. Hence my question, is there a mechanism that allows PASA to intervene in the instance of there being some slow moving members within a PCH in relation to changing any of the rules?

MR. COETZEE: Well as I indicated, yes we do have our dispute process, we do have our penalty rules, but I think Mr. Piennaar has alluded to the fact that any two banks wishing to establish the PCH may do so. The other may follow. If they are not there yet, they must develop their systems and ensure inter-operability in order to be
20 able to participate with the other banks. The environment that we..., that PASA is involved in is of such a nature that it has not been necessary to nudge those banks

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

because if they do not want to participate and their business model does not allow it, then they do not participate.

MR. PIENNAAR: I think it is just also important to note that a rule change is not that difficult. You can change the rules if that rule change do impact and specifically the proposed new model of payment at ATMs will impact on all the systems of all the banks as well as the PCH system operator.

- 10 You obviously have got problems because that is huge systems, huge system impacts. The banks actually plan up to two and more years ahead with limited resources on what system changes they are going to do and by simply changing a rule to try and force them to change the system, is very, very difficult and very, very awkward.
- To then intervene into their business development for business systems which must service their customers and try and comply with a required change at the short term and I think that is where the difficulty rather come from and not so much the
- 20 changing of the rule but with the changing of the rule you will have the impact on the systems and I think that is where the lengthening of the time come into play from that perspective because there is really limited resources in that type of environments.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MS NYASULU: Thank you my final question is, it is under something which you have marked as “confidential.” So I will refer you to it and then you can tell me whether it is a question that you can ask. It is under PCH memberships Section 5 of the May 15 document and page 5 of 5, item 563. It is under the blue section or the first blue section under Section 5 PCH membership, which as I say you have claimed confidentiality on it so I am not going to read it but I will refer you to item 5.6.3.

10 I would like to find out particularly within relation to 5.6.3.2, if you are able to answer that question in public, why that particular instance would lead to that action. If you are unable to answer the question in public, please say so as you have claimed confidentiality...

MR. COETZEE: Yes I do not have a problem in discussing this in public. This deals with the participation of any bank in a PCH. The rule was introduced that if that bank is not participating for the period of six months, membership may be terminated.

20 We have had one instance since 1999, of a bank not participating in the PCH, we approached the bank and we said according to our monthly stats we noticed that you

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

do not participate, is there any sense in your participating and there was no sense, so we got a request from the bank to terminate membership.

MS NYASULU: Is it conceivable that a bank might be within a PCH but it takes a lot longer for it for instance to get started...

MR. COETZEE: Absolutely...

10 MS NYASULU: And is it quite possible that that little section could be abused by the other banks to get a competitor out of the system?

MR. COETZEE: No with that..., especially with the development of a new system, if your business model is agreed upon and it enters the PASA domain, then we have to develop a PCH agreements rules and to ensure that the systems are in place and I am referring to the RTC PCH. We have had to approach PASA council, this specific requirement was moved out and it was agreed that banks do not need to participate for a period of six months to enable them to get their systems up to speed and to
20 implement and such a date, implementation date was just moved out for another, I think it was a period of eight months.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MS NYASULU: Just..., I know I said it is my final question but this one really is my final question and I am just trying to see whether that is under anything that is confidential. It is under the document, the first document in the submission titled “Additional Submission by PASA,” page 13 of that. If you look at that page 14, article or item 4.19, “the fact that the SARB has and I think it has been said in public quite a number of times in terms of Vision 2010 has already recognised the need for greater participation by non-banks within the NPS and have included this in the 2010 Vision and the aim is to enable wider access to the NPS for participants by providing different categories for participation.” What is PASA’s understanding of what the SARB’s objective is with that?

MR. COETZEE: I think the statement that speaks for itself. The PASA environment is a very dynamic environment in the sense that it continually develops changes and so forth. This is a statement that was put as a principle. This was accepted by PASA and also accepted that whatever will follows in terms of the SARB’s strategy, will be..., will have to be accepted by PASA. Preliminary discussions have taken place with the Reserve Bank, the content of which I was not involved in my..., I cannot

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

divulge, but it is the aim of PASA to cooperate as far as this principle is concerned and to open up the payment system.

MS NYASULU: Okay thank you Chairman.

CHAIRPERSON: Yes just one question that is a follow-up to your question by Mrs. Nyasulu before this last one. You raised concern about whether member banks can interfere with whatever decision is..., she was talking about. What is the membership of PASA? Is it five big banks and the smaller ones?

MR. COETZEE: Yes, currently we have 20 member banks one of which...

CHAIRPERSON: I am talking about the council sorry, of the council...

MR. COETZEE: Of the council?

CHAIRPERSON: Yes.

MR. COETZEE: We have five big council members and then two smaller members.

CHAIRPERSON: Two smaller members?

MR. COETZEE: Yes.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: And the five big ones are based on the volume of the transactions that is what you said I think in your submission.

MR. COETZEE: The first five..., their membership is determined by their volumes and values yes.

CHAIRPERSON: Yes the volume and values of.

MR. COETZEE: Yes.

10

CHAIRPERSON: Now in going through your submission, the common thread which I sort of picked up is that you tried to say that the Reserve Bank is playing an oversight role.

MR. COETZEE: Yes.

20

CHAIRPERSON: Now I have just got a slight difficulty with the whole governance thing within PASA because in talking about in paragraph 8.25 of your submission, you say you do not have a role to play when it comes to approving the criteria that the Reserve Bank approves, but earlier on you mentioned that they are not actually a voting member of the council. So I am trying to understand as to really how does the

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

structure work *per se* because if I read your submission, you talk about this oversight role by the Reserve Bank but on the council that on vote, basically it means the five big banks who are the majority can make a number of decisions which are crucial to the industry.

10 MR. COETZEE: Mr. Chairman, yes that is in fact the structure that we have. It is five big banks and two smaller banks and the SARB is a non-voting member. We must keep in mind that if a decision was taken at council, firstly will be we operate on the basis of consensus. If an issue is taken to council for a vote it must clearly illustrate that it involves risk. The SARB attends all these meetings to guide, to observe and to ensure that its responsibility in terms of the SARB Act, Section 10 is implemented by PASA. So a decision is taken. The reason why the SARB is not voting, is in a governance structure, if the SARB is going to be approached at the last level, the SARB must not be perceived to be a participant in the voting process but they must be perceived to be sitting on top making the final decision.

20 CHAIRPERSON: But they are part of the meeting anyway?

MR. COETZEE: Well...

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: They made their contribution to what the discussion was about.

The only thing is that if there is no consensus and there is voting to be done, they did not participate.

MR. COETZEE: Well once again in the PASA environment and we need to understand...

CHAIRPERSON: I am trying to understand...

10

MR. COETZEE: It is very...

CHAIRPERSON: I am trying to understand...

MR. COETZEE: It is very seldom that an issue ever goes for a vote to council, very, very seldom, because the SARB exerts its influence. It guides PASA council members and reminds them of their role. So that is why we do not have a voting council very often and if it goes for a vote, it definitely..., the vote will be based on a risk issue.

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Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: In paragraph 7.16 you make reference to two member banks who were allowed to participate in the NPS outside of the approved rules. Would you like to elaborate on that and clarify to us whom you are referring to?

MR. COETZEE: Mr. Chairman I will ask Mr. Piennaar just to respond to that issue.

MR. PIENNAAR: Mr. Chairman in this particular instance, it is part of the PASA rules and the SARB is actually also in favour of that rules, that whenever an entity
10 becomes a bank and enters the clearing and settlement domain that they should clear all their transactions as any other bank, allowing the Reserve Bank to see the settlement figures on a daily basis of that particular bank.

In this particular two instances, the entities previously was outside of the clearing domain, they became banks and they could not due to certain system constraints at that point in time, they could not clear as any of the other member banks so therefore they acted partly as a clearing bank member and partly as a corporate customer of
20 another bank which in terms of the PASA rule, should not be allowed for risk monitoring purposes.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

PASA then specifically wanted those banks to get into line and start doing whatever they need to do but at that point in time the Reserve..., they approached the Reserve Bank and the Reserve Bank granted them allowance for a longer period of time to bank with another bank until the necessary systems were put in place which in this particular instance was the EDO systems, the AEDO and NAEDO systems.

CHAIRPERSON: Will you be free to indicate which of those two banks you are talking about?

10

MR. PIENNAAR: I maybe wrong, but as far as I know it is African Bank and Capitec.

CHAIRPERSON: African Bank and Capitec?

MR. PIENNAAR: Yes.

CHAIRPERSON: Okay so this was done in preparation for..., basically it is a transition stage to get them into a full banking status?

20

MR. PIENNAAR: Yes it was a transition stage.

THE NATIONAL PAYMENT SYSTEM

MS NYASULU: Chairman just before someone else proceeds, I just want to put on record that I have gone through the documentation and I am satisfied that there was no..., that Mr. Coetzee's explanation seems to make sense, that it is only where there was the other side of the page that was missing that what has not come on, so it is a feasible explanation. I just wanted to put on record...

MR. COETZEE: I still apologise, we will provide you with proper...

10 MS NYASULU: Absolutely...

CHAIRPERSON: You will provide us with the necessary pages?

MS NYASULU: Yes...

MR. COETZEE: Yes.

CHAIRPERSON: Okay dealing with that which is a housekeeping matter as well, the other issue relating to confidentiality, can you come back to us when...

20 MR. COETZEE: We will.

CHAIRPERSON: So that we can..., that can be lifted and we can deal with it properly.

THE NATIONAL PAYMENT SYSTEM

MR. COETZEE: Yes.

MR. BODIBE: Good morning Mr. Coetzee and your team. First question, the NPS Act does not make reference to PASA in name, is that correct?

MR. COETZEE: Yes.

MR. BODIBE: So how, can you explain to me the process through which the SARB went about to appoint PASA as the deemed manager of the payment system.

10

MR. COETZEE: Mr. Bodibe you will recall that I stated in my presentation that PASA was established in 1996. The NPS Act was promulgated in 1998. The Act provides for the payment system management body that must enable the SARB to fulfill its obligations. The SARB and PASA cooperated at that point in time in..., especially in settlements because a payment system already existed before the Act was promulgated. Unfortunately I cannot say because I was..., simply because I was not there, but PASA was recognised in 1999 as a payment system management body having appropriate rules, constitutions and agreements in place to enable the SARB to fulfill its obligations in terms of the Act.

20

MR. BODIBE: And do you know whether that was in writing?

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. COETZEE: That was in writing, yes.

MR. BODIBE: And is that possible to have access to that?

MR. COETZEE: Yes I will provide you with a copy of that later.

MR. BODIBE: Okay so how does the Reserve Bank fulfill its oversight over PASA?

10 MR. COETZEE: The Reserve Bank and we have already dealt with this requirement or did this issue. The Reserve Bank is a non-voting member of PASA and ultimately any decision based on risk and which may have an impact on the system is discussed at PASA council and the Reserve Bank is a participant on that PASA council committee. Quarterly National Payment System strategy meetings are also scheduled to discuss issues of pertinence between the Reserve Bank and PASA.

20 MR. PIENNAAR: Yes I think what is also important in the SARB, SARB's armory but really they should be answering the question is that they fulfill oversight over each and every member of the PASA. So they actually visit each and every member of PASA to see that the bank operates in a proposed way which they measure it in certain items and logically any misconduct of the PASA/EXCO and the PASA

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

council obviously would then be raised by those particular banks to the Reserve Bank.

The Reserve Bank has also entered into a process of oversight over the payment clearing house system operators so they also now entering that phase where they can again have feedback straight from the ground level up on whether whatever they require and what the Act requires of PASA, is actually fulfilled on it.

10 MR. BODIBE: Are you required to report regularly to the SARB and what is the content of those reports?

MR. COETZEE: We are not required, we do it on ad-hoc basis. Any developments and changes and so forth are communicated to the SARB. There is an open line of discussion and communication with the Reserve Bank.

MR. BODIBE: So ultimately you are answerable to your council?

20 MR. COETZEE: We..., yes. In fact so the only..., if there is an official escalation or reporting mechanism that might be seen as the council meetings every second month that we have and we provide the SARB with the full report of all issues, progress on systems, changes of clearing rules, agreements and anything new that is

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

in the system. So the SARB is the recipient of a pack this thick to enable it to monitor what progress has been made on issues at PASA.

MR. BODIBE: But you still say that there is no official requirement for PASA to report to the SARB to enable the SARB to make a judgement as to whether PASA is still fulfilling its mandate and still capable of fulfilling that mandate...

MR. COETZEE: I should perhaps rephrase myself and say it is..., there is an official
10 requirement, yes, but there is no official process. We escalate issues when and as they happen.

MR. BODIBE: Thank you and where is this to be found, this requirement to report.

MR. COETZEE: Look as I have said, it is a requirement, the PASA executive office responsibility and it is one of our admin requirements to report those issues so we are the central point and from there we escalate any issue in any event the Reserve Bank is included in all those communications.

20 MR. BODIBE: Would it be in the memorandum of understanding between yourself and the Reserve Bank or would it be in the legislation?

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. COETZEE: There is and not to signed memorandum of understanding but in terms of the NPS strategy sessions that we have, scheduled by the SARB on a regular basis as well as the PASA council meetings that we have. So the bottom line is there is an official communication going to the SARB at least once a month, in terms of our processes that we have adopted for council and in terms of the processes that the SARB has adopted for PASA.

10 MR. BODIBE: Okay thank you, now PASA is governed by its constitution.

MR. COETZEE: That is correct.

MR. BODIBE: And to what extent, I mean you have to appreciate that we have not sight of the constitution, to what extent is that constitution consistent with the law, the NPS Act?

20 MR. COETZEE: I must admit I think from a governance perspective, the constitution does address all the sound governance issues, but I have not given a proper consideration as to where it might not be consistent with any law and if you would allow me, we could revert on this issue.

MR. BODIBE: Please, I would appreciate that.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. COETZEE: Okay.

MR. BODIBE: In the event that there is a dispute between the PCH rules and the PASA constitution and the spirit of the law or the letter of the law in this particular case, which will prevail?

MR. COETZEE: The constitution and the law of course...

MR. BODIBE: Yes.

10

MR. COETZEE: Ultimately the law will prevail in all instances thereafter the PASA constitution and then lastly the rules.

MR. BODIBE: But what happens in instances where you have interpreted the law so widely in your rules as to impose new conditions in that kind of situation what will prevail?

MR. COETZEE: The law would prevail.

20

MR. BODIBE: Okay.

MR. COETZEE: So it boils down to the first step, the law will prevail.

THE NATIONAL PAYMENT SYSTEM

MR. BODIBE: Okay so on what ground can members therefore reject participation by new entrant?

MR. COETZEE: Any bank wishing to join a PCH must comply with certain entry and participation criteria. The most important of which is, once you are a member of PASA I think on a high level you are a bank you can participate in terms of the National Payment System Act, but then you have to comply with operational issues and if you are not...

10

MR. BODIBE: Operational?

MR. COETZEE: Operational requirements, standards and rules, if you do not comply, you do not have access. That is the most important point that I can think of from a PCH perspective. PASA council will look at it from a risk perspective and the risk perspective has been dealt with on a high level if you are a bank and you have a banking license then you can participate.

20

MR. BODIBE: So is it feasible therefore that you could meet the Reserve Bank requirement but still be rejected on the basis of..., by a PCH?

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. COETZEE: Mr. Bodibe I have alluded to this fact in our submission and since the inception of PASA we have not had one rejection. So I cannot think of any instance where..., if that member is operationally able to link with other banks, that bank would be allowed to participate.

MR. BODIBE: Okay in the event that that happens, what do the rules provide? What is the recourse for that new entrant who has met the Reserve Bank requirements but has an objection in the PCH?

10

MR. COETZEE: Well the process is as follows. We would for instance get an application, we would refer it to the PCH participant group and if there is not consensus, typically this is the constitutional process that we will follow and voting has to take place, then if the majority votes against it and the vote has to be on sound reasons, you have to illustrate very clearly that the bank is not complying with the following requirements and that is why I am voting.

20

If you cannot do that then you are you as a member and participant of the PCH are at risk. You have to explain to council, you have to explain to the SARB. So I do not think banks would want to venture there.

THE NATIONAL PAYMENT SYSTEM

MR. PIENNAAR: Yes but I..., sorry can I just jump in? I think the normal approach rules there also. If that bank feels aggrieved due to the..., to not being allowed to enter and it is mainly based on the risk reasons, if it should happen even in the future, then he can approach, he can inform council about his intent to approach the SARB and he can directly approach the SARB for a final decision in that regard.

MR. BODIBE: And can the SARB override...

10 MR. PIENNAAR: Obviously...

MR. BODIBE: Council decisions?

MR. PIENNAAR: Obviously yes.

MR. BODIBE: And then what happens when the SARB has?

MR. PIENNAAR: Then you will have to come into the system and you have to play. The point is that at that point in time that the risk reason for which he was declined
20 will then have to be obviously taken into account by the SARB and to an extent by allowing the person to enter the system, the SARB to an extent and I may be stand to

THE NATIONAL PAYMENT SYSTEM

be wrong saying or be showed wrongly to an extent the SARB then become a risk for that particular participant.

MR. BODIBE: And this entrant and participation criteria is it publicly available, the PASA?

MR. COETZEE: It is available on our Intranet, yes.

MR. BODIBE: Intranet?

10

MR. COETZEE: Intranet.

MR. BODIBE: So if I am a new member, I am not part of the network. What..., how would I get that information?

20

MR. COETZEE: On our Internet we have provided any person wishing to join with the contact details of myself and of the personnel of PASA/ECSA and what we do in terms of our process is, we set up a meeting, we provide the applicant bank with all the appropriate documentation and processes and we assist that bank through the process. We facilitate final compliance and membership of that bank.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. BODIBE: Is there any reason why the entrant requirements are not on your internet?

MR. COETZEE: There could be and I am not in a position from a legal perspective to address whether there is from a fraud perspective any grounds not to disclose some of these criteria. You might provide this information to fraudsters so to speak and they might obtain some advantage but..., and I do not want to speculate. It is possible to provide it subject to being not being any of these possibilities.

10

MR. BODIBE: Okay and then if I am a new entrant, what business information must I submit to PASA and its members?

MR. COETZEE: Any PASA member bank is required to confirm a number of issues. The one of which is to provide your model as a bank and if you for instance your business model relating to the PCH, you are going to participate in. So if you say because in your application form you will have to provide estimated volumes and values. So it is expected of any bank coming in that there will be volumes and values in the PCH, EFT environment then you will have an EFT business model, ATM, are

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Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

you going to issue only or acquire only and that is the type of information that we would want.

MR. BODIBE: Okay and also your systems?

MR. COETZEE: And the systems, the one requirement also deals with the DR requirements, system requirements, if you are going to outsource, do you subscribe to the SARB principles as far as outsourcing is concerned, yes.

10

MR. BODIBE: And if I am introducing an entirely new system?

MR. COETZEE: If you want to introduce a new system, there must be at least another bank wishing to participate in that system. It moves down to the business level with another bank you introduce that new system, it will enter the PASA environment where we will look at it from a regulatory perspective and develop rules around ops and risk.

20

MR. BODIBE: And that will then establish a new PCH or can that be accommodated in any new...., existing PCH?

THE NATIONAL PAYMENT SYSTEM

MR. COETZEE: If it is totally a new model then a new PCH could be established, yes. If it relates, closely relates, to existing infrastructure that we have, it could be introduced once again through your business model, banks must be together and say this closely relates to ATM or debit card or so, let us introduce it as a new transaction type in this PCH.

MR. BODIBE: Okay what are the voting powers of each member in the council?

10 MR. COETZEE: There are seven members of council and it is one bank one vote for each of those members.

MR. BODIBE: And criteria for membership of council?

MR. COETZEE: As I have stated, the big five are determined by their volumes and values and thereafter for the smaller banks to agree on their two representatives on council.

20 MR. BODIBE: Can you explain why the criteria for volume and value?

MR. COETZEE: I think..., well just my view is that when this happened and the constitution was drafted, it..., we must keep in mind that the volumes and values of

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

the big five are more..... represent more than 90% of the volumes and values in the payment system and they are risk based. The decision to..., for this specific provision was based on a risk issue.

MR. BODIBE: But you are a governance structure delegated.

MR. COETZEE: Yes and that is why the constitution allows for any member that feels that he..., a decision that impacting on it that member has a right to escalate to
10 the Reserve Bank. So...

MR. BODIBE: It is not a..., yes?

MR. COETZEE: We make provision for the fact and we make provision for the..., we have to govern the risk issue. PASA's domain is the risk domain and that is why that decision was taken to allow the five members on council.

But you cannot allow those members to determine the future and the participation of
20 other members if you do not allow them to have access in terms of an escalation process at least to the Res...the SARB who has the final say.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. BODIBE: But their power is entrenched in perpetuity unless their values and volumes decline.

MR. COETZEE: Yes.

MR. BODIBE: Okay thank you.

10 MR. PIENNAAR: Sorry, can I just assist there? The five is actually established every year based on values and volumes. So you always look at the past year's values and volumes. So you may find that Bank Number 5 to an extent may alternate in some instances depending on the growth of the smaller players or not.

20 ADV PETERSEN: My turn. In regard to the payment clearing house agreements and on the clearing rules, thank you by the way for providing them to us, once again we are confronted with the difficulty of claims of confidentiality, covering the entire document and I must therefore proceed with caution here but I have propose to ask questions and you can stop me if there are serious confidentiality issues which you wish to assert.

I may just mention that on Friday when I raised questions concerning the clearing rules and the PCH agreements with ABSA, they had no difficulty in the afternoon

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

accessing the intranet for us right here in this room and pulling up the rules to which I referred. So those particular rules if I happen to address them today are no longer confidential because the cat is out of the bag.

Now my understanding of the structure and I appreciate the difficulties involved here. From a legal point of view it seems to me that the structure of the PCH agreement is that first of all there are what I might call founding participants when that agreement was first drawn up, there were the basic participants who all signed Schedule 1. And then any new participant added after that has to first reach agreement individually with every other.....every existing participant, and has to then satisfy PASA that in fact such an agreement has been reached and may then sign Schedule 1 and thereupon all the members become bound to each other including the new entrant, have I got it right?

MR. COETZEE: Yes.

ADV PETERSEN: Okay so that theoretically and I know you have shown that it has not happened in practice but theoretically one existing participant could refuse, am I right so far?

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. COETZEE: Yes.

ADV PETERSEN: And that would be..., keep the door closed to the new participant.

MR. COETZEE: Well not necessarily, as I stated in terms of the PCH participant group constitution, if a decision is taken by the majority to allow that participant..., new participant in the PCH, the membership or application will be successful.

10 ADV PETERSEN: Are you saying that that remedy, that rule, is powerful enough to force every existing participant to agree to accept the new participant into the PCH?

MR. COETZEE: Well yes, we provide within that PCH participant group constitution, it happens on a regular basis to refer membership applications to the PCH participant group and if there is a majority decision, I have not had any decision otherwise then it must go through. And once again the PCH participant group operates in the operational realm.

20 ADV PETERSEN: Reference has been made to it, but I think just to for ease of future reference when we read the transcript, perhaps you would like to just read for

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

us the first sentence of your paragraph 4.7 of your latest submission that starts with the word “since 2002,” just the first sentence would be sufficient for me.

MR. COETZEE: “Since 2002 PASA has received six applications for membership of PASA, three applications for sponsored participation through a member bank of PASA and more than 80 applications for membership of a PCH.”

ADV PETERSEN: And the..., sorry and then the next sentence?

10 MR. COETZEE: “None of these applications were turned down by PASA council of the PCH participant group.” One bank...

ADV PETERSEN: Sorry does that mean that they all got into the PCH?

MR. COETZEE: Yes.

ADV PETERSEN: Now just for a way of follow-up to some questions that Mrs. Nyasulu asked about mentoring. I have looked at the Reserve Bank Position Paper
20 on bank models. I think it is Position Paper 2 of 2000 and if I am understanding that Position Paper correctly and PASA followed up with its own Position Paper on the

THE NATIONAL PAYMENT SYSTEM

same subject, if I am understanding that Position Paper correctly, mentorship is only provided for banks, which have already become clearing banks.

MR. COETZEE: Mentorship is a requirement introduced for any new applicant bank, which has not been involved in clearing. It applies for membership, it has to then enter into a mentorship agreement and only then will it participate as a mentored clearing bank.

10 ADV PETERSEN: Well with great respect and I do not want to quibble on small things, but we are looking here at whether there is a process of assistance, which is given to non clearing banks to help them to get to the point where they can become clearing banks. My understanding is that there is at the moment no such process because in the Reserve Bank Position Paper there is a fundamental division into two categories, clearing banks and non-clearing banks. Now it is once you are in the category of a clearing bank that you then fall into one or other category, subcategory
20 within the clearing bank category and one of those is a mentored clearing bank. That is what the Position Paper provides for..., Mr. Coetzee is shaking his head so can you help us to straighten that out?

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. PIENAAR: Yes Mr. Petersen I think it is important to understand why the Position Paper was put out. A bank only becomes a clearing bank at the moment when it provides a payment mechanism into the hands of its customers. Until that point, it is not a clearing bank and that was the intent of the Reserve Bank Position Paper to clarify to banks because there is many banks, I mean there is probably about forty four banks operative in the system and only roundabout 20 is clearing banks because only those 20 decided to provide to their clients a payment mechanism, and at that point in time the Reserve Bank Position Paper was to make it clear that should you take such a decision, better look at this and then see I am now entering the carder of clearing bank environment in which case you need to go to the Re..., to PASA and you need to do the necessary applications et cetera, et cetera.

So the Reserve Bank only clarified when do you cross the line and become a clearing bank and from that point onward you then go to PASA, you required to become a member of PASA, you start-up your systems, you prove that you can run the necessary systems and on a very limited basis probably at first, you issue the particular payment instrument to your clients so that in time you can grow your

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

knowledge of doing that and understand the particular payment mechanisms and how to handle that from that perspective.

MR. COETZEE: If I may?

MR. PIENNAAR: From that perspective yes it is true that only at that point in time from there onwards you can provide membership to the bank. Should you decide not to become a settlement system participant, in other words not to settle but rather to be
10 sponsored, then the mentorship is obviously included in the sponsorship arrangement on that perspective.

ADV PETERSEN: Yes I am not sure if we are missing each other here but the definition of “mentored clearing” in the SARB Position Paper, includes this “that the bank will participate as a direct clearer.” In other words, it does its own clearing and I might add and I think this is what you have been explaining that if it is not also
20 sponsored for settlement purposes then it will undertake its own settlement obligation.

MR. PIENNAAR: That is correct.

THE NATIONAL PAYMENT SYSTEM

ADV PETERSEN: So it participates directly but it has the assistance guidance, if you like, of a mentoring relationship. So to get into mentoring you have to first get into the category of a clearing bank.

MR. PIENNAAR: Yes.

ADV PETERSEN: Right that was what I was getting at.

MR. PIENNAAR: Yes.

10

ADV PETERSEN: So there is no, at least to as far as this Position Paper is concerned, there appears to be no provision for the education of a non-clearing bank to prepare it for that entry into the clearing bank category. Now is that correct?

MR. PIENNAAR: No you are quite right, but there are obviously informal relationships between banks. I mean most of the banks that is not clearing banks has got a corporate client relationship with another clearing bank. It has got to have it, so the relationship is already there with a clearing bank so should he wants to...pick up knowledge, he probably discuss it with his bank on the how to what to et cetera, et cetera. So the informal relationships certainly will be there.

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Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. COETZEE: Mr. Petersen if I may just clarify one issue as far as this is concerned, in 5.3 of the SARB Position Paper it states clearly that mentored clearing, this is the model from an entrant bank into a particular PCH. So firstly your first step is on your base and your business model, am I a non-clearing bank or a clearing bank? If I am going to clear and enter a PCH, I have to do so as a mentored clearing bank. So there is..., if there is the perception that there was first clearing then mentoring that is not correct. It is at the moment when clearing starts; you start out as a mentored clearing bank.

ADV PETERSEN: The point is however that there is no mentoring before clearing.

MR. COETZEE: Well before joining PASA then as a member, yes.

(Caucus)

CHAIRPERSON: Excuse us...

(Caucus)

ADV PETERSEN: We are under constraint of time. It is already past 11:00. I am afraid I do have several more questions which will..., several more topics and so we

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

have just been conferring, you got my back turned about how that might be handled.

Chairman do you..., would you want to indicate to us?

CHAIRPERSON: Yes, every..., almost everyone of the panel has got so many questions for you because the entire issue relates to governance and it looks like all the questions we have been asking, all point to PASA at the end of the day amongst others. There are other people as well all the questions point to, so I do not know whether..., there is also the issue of confidentiality which you had raised and needs..., still needs to be sorted out so will it be possible for us to arrange for another day?

10

MR. COETZEE: Absolutely.

CHAIRPERSON: The Enquiry Manager will liaise with you to fix another day and maybe we will have more than the two hours which was original allocated for this particular matter then we can..., go into detail on the issues relating to PASA.

20

MR. COETZEE: We will do so.

MR. PIENNAAR: Can I just in relation to the last topic just clarify that PASA obviously never thought about formalising the informal relationship of a corporate

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

bank to its banker but should that be a wish, we can always look at that in formalising, it is not a big problem. So it is not that it is not there at all, I am quite certain knowing banks and having come from banks, that those two banks do discuss issues before a bank becomes a clearing bank and if necessary it can be formalised.

CHAIRPERSON: Thank you then, we will adjourn and resume at 11:30.

(Adjourns)

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On Resumption:

CHAIRPERSON: Good morning ladies and gentlemen once again and welcome to the Standard Bank team. Welcome to Mr. Sinton.

MR. SINTON: Thank you Chair.

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CHAIRPERSON: Mr. Brian Le Sar, Mr. Ravi Shunmugam and a..., I have got something wrong. I do not have all the names, would you introduce the rest of the people, Mr. Schlebusch, yes. Welcome and we will let you take the floor with your presentation if you do have a presentation. Before I let Standard Bank carry on, let

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

me just remind everybody to switch off your cell phones please. You may then proceed.

MR. SINTON: Thank you Mr. Chairman. Chair may I say that undoubted yes we do have a brief presentation which we would try and confine to the problem areas as we see it and some recommendations that we wish to make.

I would also like to mention that we have invited Ravi Shunmugam here, he is Head
10 of Payments in Standard Bank to do the presentation and really be available to answer question that pertain to Standard Bank. We also thought it might be useful for you if we asked Brian Le Sar to attend, Brian is now head of our Global Payment Strategies but he also have been an active participant in the National Payment System for many years and he is in fact an advisor to the SARB on many issues so we asked him to join us so that we could actually help you answer questions that affect the industry as a whole rather than just Standard Bank so we..., but obviously he will
20 chip in when he thinks he can add value.

CHAIRPERSON: Whatever he thinks can add value.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. SINTON: Peter Schlebush is the Head of the Business of Standard Bank where all of this takes place, so he is here really to represent Standard Bank in that capacity.

CHAIRPERSON: Okay, so another housekeeping matter...

MR. SINTON: Yes?

CHAIRPERSON: We will have this of course electronically...

10 MR. SINTON: Absolutely.

CHAIRPERSON: And then this will be Exhibit VV.

MR. SINTON: Thank you Mr. Chairman.

CHAIRPERSON: Right you may proceed.

MR. SINTON: On that base can I ask Ravi to proceed?

20 MR. SHUNMUGAM: Yes thank you. Thank you Chair, good morning to you and the rest of the members of the panel. I think at the outset before we kick-off with the presentation, I just want to say that the Standard Bank supports the participation of all players be it banks or non-banks within the NPS however this participation needs to

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

be premised on the mitigation of all risks to ensure that the integrity and functionality of the National Payment System is not jeopardised in any way.

This would require a balanced approach among all stakeholders and the application of the principles of adequate competition, credit competition and the protection of consumer interest. I think our presentation this morning is in line according to the guidelines of the technical committee and needs to be read in conjunction with our submission.

10

And really the presentation is going to cover the mechanisms that exist for new banks and small banks to gain access into the NPS. It gives you an understanding of the current existence of non-banks within the NPS, some of the current governance and regulatory oversight that exists. It were given...oversight non-bank participation in the payments value chain. We will talk a little about the phenomenon of sorting-at-source and multiple acquiring and some of the potential consequences for the NPS.

20

Although Bankserv was not a specific requirement, we will touch on it, given its focus during the course of this hearings and we will talk a little bit about innovation

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

in the National Payment System and conclude with some of our recommendations for access and regulation.

I think access to the current National Payment System by new banks or small banks can be easily facilitated within the current regulatory and risk management framework that exists. The payments clearing and settlement environment is a specialised environment which requires specific knowledge, expertise and skills to ensure that the stability and integrity of the National Payment System is maintained.

10

For new entrants that do not want to clear and settle in their own right, participation can still be facilitated through a sponsorship arrangement which could either be technical, financial including settlement or both. Sponsorship enables new entrants to access the National Payment System at a lower cost and the current entry requirements do not create unnecessarily barriers to entry but merely exist to safeguard the soundness of the National Payment System and the contained counterparty risks to acceptable levels.

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Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

Standard Bank further supports the introduction of dedicated banks and corporative banks via an appropriate Act and believes that this will facilitate the entry of new participants with appropriate governance and oversight.

This is the infamous onion diagram that we have been alluding to during the course of the hearings and on the left as you would see is the inner core of the National Payment System, which really consists of the settlement system of the SARB at the

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core. The clearing banks are present either as direct clearers, mentored clearers or sponsored clearers. We also have exempted, excluded entities such as the Post Bank and Ithala and really enter this fray as sponsored entities into the clearing settlement space. And obviously the last piece of the either called the National Payment System is really the National Payment System operators who play a pivotal role in the clearing and settlement of payment instructions and obligations.

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The inner core of the National Payment System is a highly regulated environment whose threads lie in its governance, compliance for the bank of international

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

settlement principals, risk reduction measures and a high level corporation to maintain very high standards.

As you see on the right-hand side, our current non-bank players who participate in or influence the National Payment System with no regulatory oversight in governance.

I think if you look at the categories of non-banks that currently exist, they extend from retailers all the way through to money transfers systems including beneficiary service providers, Bureaus that we alluded to earlier, system operators and mobile
10 phone operators.

Now to illustrate the Activities of some of the non-banks, I will use an example. I am not going to go through all of them. If you take a retailer and some of his activities in the payment space, retailers are issuing payment instruments on the basis of credit granting. Now where customers used these instruments as pre-funded payment mechanisms, this could equate to the holding of deposits. If the payment instrument issuer was utilised outside of a retailer and a typical example of this would be an in-
20 store-card that can be used out of that store.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

If you look at the current governance on regulatory oversight of banks, sorry, the current governance of regulatory oversight of banks, although intensive and costly are absolutely necessary to ensure a safe, sound and stable National Payment System.

If you look at banks on the inner core, they are closely monitored for capital adequacy, liquidity which is secured by cash reserves with the SARB, disaster recovery plans and all of these ensure that the confidence in the National Payment System is maintained and promoted.

10

Now South Africa follows the Bank of International Settlements Principles regarding clearing and settlement models and in South Africa we have a “survivor pays model” and this compliance with the international best practice is necessary for South African banks to participate in the global economy and that has been illustrated by the inclusion of the Rand as one of the 15 currencies settled via the continuous link settlement system.

20

Nevertheless the NPS is only as strong as its weakest link and the participation of non-banks in the National Payment System should introduce no more risk than banks

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

do, and therefore non-banks must be subject to capital adequacy, liquid reserves, governance and regulation that is appropriate to the risk that they introduce.

I think the lack of appropriate regulation oversight of non-bank activities such as introduction of payment transactions, deposit taking, multiple acquiring, sorting-at-source, float holding, adequate DRP and PCP, introduces risk which needs to be regulated and overseen. Now the slide shows you some of the risks that are regu...,
10 that are introduced by non-banks, they not an exhaustive list but I think it is worthwhile just going through a couple just to illustrate how these risk actually play out in terms of non-banks.

If you look at reputational risk, if you take a beneficiary service provider that is collecting payments on behalf of a beneficiary, if the beneficiary service provider does not clearly indicate to customers that they are merely acting as agents on behalf of beneficiaries and not actually the bank and should something go wrong or they
20 abscond in the process, then the banking industry faces those reputational risks with..., where something has gone wrong. That is one example of how the risks do play out. There are many other examples which we can explore at a later stage.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

Inadequate regulatory oversight of non-banks in the National Payment System could result in increased processing costs which, is due to process inefficiencies. Non-optional clearing between banks and one such an example is direct clearing which is costly.

10 And because of the cost, this could lead to consequently lower volumes and lower economies of scale through the National Payment System operator, which would lead to higher costs for smaller banks resulting in higher barriers to entry. Further to that is that there would be an inconvenient, inefficient payments transactional capability for customers who will be limited to their own banks infrastructure leading to reduced inter-operability. Therefore non-banks need to be subject to appropriate governance and regulation.

20 Non-banks are already active in the payments system, performing many technical functions relating to acquiring. They are present either as technical outsource providers such as ATM Solutions, switches such as Easy Pay or consolidators such as Bureaus. The key acquiring functions of clearing, settlement and reversal if required should only be performed by clearing banks, there are strictly regulated limited risk adequately.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

For non-banks that are active in the payment system, there is a need for regulatory oversight under the auspices of the SARB, which would include tighter controls through the issuing of directives and rules in this regard. We are going to touch on the principals or the phenomenon of sorting-at-source and multiple acquiring. What we have done in the slide is actually defined it to kind of make clearer and I am not going to go through the definitions of both but from the Standard Bank's perspective, essentially these practices are the same.

10

Sorting-at-source is applicable within the electronic funds transfer environment and multiple acquiring within the card environment. Historically the primary driver of the wanting sorting-at-source was for preferential payments. It is where corporate would get first hit of the funds. With the introduction of the AEDO system and the NEADO system and consequently the National Credit Act which is due soon, all preference from systems has been removed and replaced with randomization.

20

And within Standard Bank we are not seeing a massive demand for sorting-at-source. The primary drive of multiple acquiring as been indicated during the course of this hearings, is the perception that interchange will be avoided. In overall we do not see any benefits of either of these practices.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

So in conclusion I think Standard Bank supports restricted multiple acquiring by card associations, which exists for a..., the purposes of PCP and DRP. Standard Bank does not support unrestricted multiple acquiring and sorting-at-source because of the consequences that it has and really these consequences have been echoed by the other banks during the course of this hearings and these involve a reduction in the volumes through the existing operator which will lead to decrease economies of scale.

10 The consequence of that is higher processing cost which would because of the higher processing cost cause larger volume players to move to alternative such as direct clearing and that would leave the smaller volume banks to incur higher processing cost and jeopardise the inter-operability of the system that currently exists.

I think moving on to Bankserv and although this was not a specific requirement, we decided to cover it. Bankserv was created by the banks for the banks to achieve greater efficiencies and switching and to maintain the safety and soundness of the clearing and settlement system. The move to..., of Bankserv becoming a commercial
20 vehicle, undermines this and therefore Standard Bank believes that Bankserv should be managed as a national utility on a self-funding non-profit basis.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

I think some of the unintended consequences of the commercialisation of Bankserv, may lead to increased cost of the consumer, cause banks to take its eye off its core function within the NPS of clearing and settlement, thereby jeopardising integrity of the NPS and could drive and may drive behavior that potentially introduces more risk into the system.

10 Bankserv is a near monopoly in relation to the provision of domestic clearing switching services. Clearly the alternatives for the banks include direct clearing or switching off shore. However this comes at incurring massive risk in cost. So the banks in South Africa have no viable alternatives to Bankserv on the short to medium term especially in EFT as you have heard from the CEO's presentation yesterday that it covers more than 50% of Bankserv's volumes.

20 We will now turn our attention to innovation in the NPS and I think from that slide you can see that from the 80's all the way through to current day there has been quite extensive innovation in the National Payment System with particular focus on risk management initiatives in terms of the reform of the payment system as well as new payment instruments and mechanisms.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

In some respects, South Africa has been leaders in innovation. However it is critically important that innovation in the National Payment System is not done at the expense of ignoring International Risk Management standards.

So Chair in conclusion I think some of our recommendations from a Standard Bank's perspective is that all participants that introduce risk into the National Payment System must be regulated and subject to appropriate oversight. Legislation governing dedicated banks and corporate banks should be promulgated and exempted entities should fall under the legislation relating to dedicated banks. Appropriate directives and underlined rules on non-bank participation in the NPS should be issued to ensure clarity and reduce risks. The SARB should establish appropriate structures to regulate non-banks and finally Bankserv should operate as a national utility.

Thank you.

CHAIRPERSON: Thank you, before I ask the rest of the panel members to whether they have any questions, I just got one question relating to Bankserv. You say it should operate as a national utility, can you just clarify that for me?

MR. SHUNMUGAM: Chair...

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: I think I heard views to the contrary yesterday from the CEO yesterday when it came to the issue of national... of making it a national utility, maybe you can clarify what you mean?

MR. SHUNMUGAM: Chair I think Bankserv was originally setup as an NPS operator to focus on the core clearing and settlement services for the banks and as I have indicated, was created by the banks for the banks for that particular purpose and some of the functions was really economies of scale and reducing costs of processing
10 but I think where Bankserv is gone in terms of commercialisation is going to ultimately start focusing its intention outside of the formal clearing and settlement functions.

CHAIRPERSON: You were concerned about them moving out of South Africa or is it something else, I am trying to understand this.

MR. SHUNMUGAM: Well I will handover to Brian, he is more au fait with this.

MR. LE SAR: Mr. Chairman I think there is a multitude of things that we would
20 need to look at. A utility clearly speaks to national good in terms of driving that. As you heard yesterday from the CEO of Bankserv where Bankserv currently accounts

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

to for 90 plus percent of inter bank clearing in the South African context. To overnight move this vehicle to a commercial operation speaks basically to a near if not type of monopoly but it is more round the management thereof and the focus of the company.

10 A utility that is driven on a self funding type basis would clearly be there for a specific need and a specific role to fulfill namely clearing and settlement which is tantamount or sacrosanct to the National Payment System. Clearing and settlement does not occur, this country would incur severe ramifications.

If you now moving to a profit driven motive which speaks to the fiduciary role of your board et cetera being now driven for profit that starts to speak to a whole different focus in terms of how the company is managed and would not necessary constraint anyway to continue to focus on the national good of the NPS industry.

20 So you start moving through that as you talk to the focus of management, the fiduciary role of the Board and the like and how that changes some of the dynamics, I think it needs to be carefully thought through and you know while there is multiple

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

examples we could give you, I do not think we have time in this hearing to explore them all.

But I think it needs to be thought through of what does this actually mean by taking something that has been tantamount to “the clearing house” within the South African context of more than 90% the volumes and has clearly led to an efficient operation being driven to now moving it to the commercial operation where it already carries 90% the volume and in a short to medium term, there is no viable alternative for 10 banks to turn to bar Bankserv. So you start talking to near monopolistic things. I think those are all hypothesis that could come out, but I think a person Mr. Shunmugam could just talk to around some of the customer things that you necessarily seen start emerging in the space since Bankserv has moved to the commercial route.

MR. SHUNMUGAM: Yes I think Chair, if I mean in terms of where we stand and using purely my customer hat, I think currently one of the examples and there is 20 numerous examples as Mr. Le Sar alluded to, one of them is that in the current environment we have been compelled as customers to sign agreements for pricing

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

and services that lock me in based on the old paradigm of utility, when in fact they have actually become a commercial vehicle.

So my sense of going commercial is that as a customer I should be able to negotiate my fees and my prices with Bankserv, but that is not the case. I am being locked into old agreements and old pricing clauses and that is just one of the examples. There are many other examples which we can explore.

10 CHAIRPERSON: Yesterday there was also, I think reference to the restructuring of the Board, and do you think that will also affect the manner in which Bankserv works?

MR. LE SAR: Mr. Chair...

CHAIRPERSON: Or operates in?

20 MR. LE SAR: Mr. Chairman exactly to my point earlier that the Board will now have one, a fiduciary role to focus purely on the good of Bankserv, as opposed to if you were under the utility focus that we are looking at the broader domain, so it is merely..., it is purely on a profit motive. To now be appointing members to the Board who have little if no payments related knowledge to be driving the company

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

and making decisions on its behalf, I shudder to think where that could possibly impact on this industry relevant to the risk and stability and efficiency of the clearing and settlement type services it provides.

CHAIRPERSON: I maybe wrong but it was my understanding that the talk was about appointing people who have got no payments knowledge.

MR. LE SAR: Mr. Chairman I stand corrected, as far as I remember from the
10 presentation, banks who makeup more than 5% of the volume will be assigned each a chair, up to a maximum of five, the remaining five board members will be independence which necessary talks to where would you find those type of...

CHAIRPERSON: It does not necessarily mean that they do not have payments knowledge if they are independent.

MR. LE SAR: No, no that is why I said they may have little or not...

CHAIRPERSON: That is why I am raising the concerns that it was not my
20 understanding that it would be people without any payments knowledge.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. LE SAR: Correct, but what we are saying is that, hypothetically, where you are sitting is that you could be appointing anybody to that Board which would not necessarily bring in payments knowledge, you driving for profit maxim and hence that could take you down on a different route.

CHAIRPERSON: Okay there is also reference to, in Slide 12, there is that the commercial profit maximum motive is made drive behavior that potentially introduces more risk into the system. Can you maybe expand on that?

10

MR. LE SAR: Mr. Chair I think the short answer to that is if you are now starting to drive services potentially utilising the same infrastructure that you used for clearing and settlement or not, but your focus is on driving profit type related services which now start expanding your services which may not even necessarily be constrained to anything to do with payments, you start running the risk that the lack of focus which we have had to date on ensuring clearing and settlement and sound systems, could come apart.

20

CHAIRPERSON: Right, then moving away from Bankserv, in your second submission you talked about tiered settlement, there is reference to tiered settlement,

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

I think it is pages 18 in reply to Question 7. I just want to get clarification as to... just to get clarification on your opinion, if you could just clarify and let us understand what you mean by “tiered settlement?”

MR. LE SAR: Sorry Mr. Chairman, could you just refer me to the page here?

CHAIRPERSON: It is your second submission 207, page 18, Reply to Question 7. Access and inter-operability, sorry, that is the...

10 MR. LE SAR: Mr. Chairman we responded, this question is in answer to a question from the panel in which we allude to in our response that we were actually a little bit confused as to what was being suggested or requested.

I think in the course of this hearing it has come up, Mr. Petersen was talk..., referring to and I think yesterday, relevant to, is there any benefit in having some form tiered settlement type arrangements that move forward. So I will answer the question based on that.

20 If we talk to settlement occurring on a tiered basis as opposed to the current unlimited if you really want to call it, that type of settlement that currently occurs between banks, to impose a settlement limit on a member for example, Petersen ATM

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

Solutions now Bank has a limit of ten million in terms of settlement. The..., first of all just the system constraints in terms of putting that in place would be quite onerous but yes, technology enables us to overcome anything.

10 The main part of it is that how do we ensure that Petersen ATM Solutions Bank restrains itself to that limit because most of these exposures are built up during the day, which means that whilst Petersen Bank has this limit, tonight when they come to settle, they suddenly put through to the banks that they have been acting on behalf of or dealing with or clearing with an amount of 50 million. It is too late to stop. That means fundamentally settlement cannot occur which results in settlement failure which obviously has other catastrophic effects throughout the economy.

20 So when we talk to tiered settlement, I think we need to be very careful of unpacking what it is we are trying to achieve and understand that before we can actually start exploring any of these in a future realm to find is there any other suitable alternatives, but on that premise we would put to you that it would be extremely difficult.

CHAIRPERSON: Alright I will have the others carry on, I will ask my questions later.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. BODIBE: Thank you.

CHAIRPERSON: Do you have any questions?

MR. BODIBE: Yes thank you Chair, good morning. My questions are in relation to homing fees and that is where you answer to Question 17 in your second submission, the one that the Chair was referring to now. Again the justification of homing fees is now based on two-sided market, in what way are these from an EFT perspective to
10 have a two-sided market.

MR. SHUNMUGAM: Mr. Bodibe I think EFT..., in the EFT debit and credit environment is, I mean the homing fees is no different to the interchange fees and the rationale for the interchange fees as in the debit card and credit card environment. In EFT debits and credits you have an issuer and an acquirer. They referred to as the collecting participant and the paying participant and obviously there is work done on one another's behalf and obviously it is a balancing mechanism in the market. So
20 homing fees is no different and we are happy to explore it but I think we have given detailed submission around card interchange and the reasons for its existence, so the similar reasons would apply for EFT homing.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. BODIBE: Is it the same for credit and debit transactions?

MR. SHUNMUGAM: I just need to clarify, are you talking about the quantum or the flow?

MR. BODIBE: Yes, the quantum.

MR. SHUNMUGAM: The quantum is different for credits and debits.

10 Unfortunately I cannot share what the quantum is because there are bilateral agreements with various banks but in principle, I think the quantum for credits is a little higher than debits.

MR. BODIBE: And how do you determine these fees?

MR. SHUNMUGAM: Sorry how do we?

MR. BODIBE: Determine them, so how are they set?

20 MR. SHUNMUGAM: Yes sir, I mean the homing fees were previously determined on a multilateral basis but since the signing of the PCH agreements we had to move to bilateral and we have bilateral agreements with the various other participants in EFT.

THE NATIONAL PAYMENT SYSTEM

MR. BODIBE: Okay my final question related to that is, why cannot the fee be recovered, I think you heard Mercantile yesterday saying that you already collecting fees from customers and now you are collecting a homing fee, why could the fee not be collected from the customer.

10 MR. SHUNMUGAM: No I think you got to separate both debits and credits because in the credit environment for EFT, the only fee flow is the homing fee and there is no recovery from customer, for example salary credits. On the other side in terms of debits, there are in terms of debit card pricing, it is part of the pricing regime of EFT credits and if you look at the quantum of the homing fee, it is in terms of its quantum it is pretty small and its there to recover some of the work done on behalf of the other bank. In terms of the pricing to customer, there is a lot of other functionality and work that is done on behalf of the customer that is being recovered for.

20 MR. BODIBE: Sorry if it is small, what will be the effect of recovering it from the customer?

MR. SHUNMUGAM: Sorry from the customer?

MR. BODIBE: Yes.

THE NATIONAL PAYMENT SYSTEM

MR. SHUNMUGAM: What...

MR. BODIBE: In this relationship now somebody issues a payment instruction and who pays the homing fee?

MR. SHUNMUGAM: In terms of debits and credits the EFT, the homing fee is recovered from the customer. It is one of the components that goes into recovery from the corporate customer in terms of the sponsorship fee.

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MR. BODIBE: So it is not paid by the..., now what is it, the collecting bank.

MR. SHUNMUGAM: It is paid by the collecting bank to the paying bank but it is recovered...

MR. BODIBE: Is it?

MR. SHUNMUGAM: From the customer, yes.

20

MR. BODIBE: Okay now my last question, what do you actually mean when you are talking about Bankserv as a utility? Are you implying: (a) retaining the old model or (b) state ownership.

THE NATIONAL PAYMENT SYSTEM

MR. LE SAR: Mr. Bodibe what we are referring to, I mean how you achieve the governance I think is one thing and there are opportunities to explore that. What we are referring to is that the company is run in a manner that is for the national good which could be and as Hawkins referred to in her previous investigation into this, that potentially you bring somebody like the Central Bank to sit on the board to make sure that these things are driven out in the right manner that there is no potential collusion et cetera that would run with it.

10

So there is many ways to run the governance structure around it but it is fundamentally referring to running the company in a way that is purely self-funding. It is not driven by a profit maxim beyond the means to keep itself going and to ensure that it is able to provide the services in appropriate manner and that basically your governance structure ensures that it is not capable of misusing its position.

MR. BODIBE: Thank you Chair.

20

MS NYASULU: I have a very few questions for Standard Bank but perhaps you could bring up your diagram of the onion and in real life I actually hate onions but I have an appetite for this one.

THE NATIONAL PAYMENT SYSTEM

MR. LE SAR: Well consider it an orange.

MS NYASULU: I just need to understand because in terms of that onion and you have covered the same kind of diagram in your written submissions, at all times the NPS operators are always shown to be on the outer core and yet we know and as I have raised with the PASA, we know that they do on behalf of the banks the settlement and the clearing. Now how accurate is this drawing? Does it really show the situation as it is because if you were just looking at this, you would understand why the banks are so adamant that only the people who are banks and members of PASA should be in the inner circle. So I battle with what this onion is really showing us.

MR. SHUNMUGAM: I think from an NPS operative perspective, we got to separate normal operators from NPS operators and I think purely from an operator perspective, if you look at the function of what NPS operators perform, it is really for the national good of the country in terms of clearing and settlement.

If you look at normal operators and that is why if you look on your right-hand side, you get system operators or payment service providers. Those operators are a normal

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

extension of your business. So in terms of enabling technical ability or in extension of your business so as a bank I would vet them as an extension of my business, so whereas operators form a natural part of the inner core of the National Payment System, I think that is where the clear distinction is coming.

MS NYASULU: Mr. Shunmugam, I really do understand the distinction, my question really relates to the fact that although the banks and PASA and everyone will tell us over and over again what criteria you have to fulfill before you are
10 allowed to participate within the inner circle, we know that the NPS operators and I understand the greater good for the country that they fulfill. We know they are not banks, we know that they are not members of PASA and we have asked the questions directly and we have been told that, so I am trying to understand what makes them special but also contiguous to that question is I am trying to understand whether it is possible then, to use the same regulations because they still are non-banks, the NPS operators, whether it is possible to use the same regulations and I understand why
20 they need to be regulated, to apply to the others and to regulate the others using the same regulations to then allow them into the inner core of that onion.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. SHUNMUGAM: I think it is, if you look at, I think the entire premise of the inner core and the criteria that is used to basically rate the NPS operators, if the same rating criteria were to apply to other operators, then we principally would not have a problem as long as the risks that are brought into the NPS are mitigated, that would be the premise on which we go.

10 So I think and I think going forward if you look at other operators, in terms of going through the regulation and all of this risk criteria that stipulated for NPS operators, it is onerous and as indicated by PASA as well as Bankserv, that there is a two yearly audit and it is quite an intensive audit in terms of how they carried out those functions of the inner core.

20 So we principally would not have a problem with any other operator and as indicated earlier on that PASA is that those operators are appointed by the PCH and it takes two banks to agree who that operator is and obviously then they would need to go to the similar stringent criteria and regulatory requirements as NPS operators.

MS NYASULU: Okay I think that answers my questions because essentially what I am trying to understand is when we speak about regulating these other entities that

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

we are not speaking about them becoming banks. That is the only distinction that I was seeking to the extent that we have NPS operators who are not banks, non-members of PASA and to the extent that I do accept fully that they need to be regulated, what are the regulations that should apply to them, was the only question that I was seeking and if we were agreed that we would be comfortable with those regulations being the same ones that relate to the NPS operators rather than the ones that turn you into a bank, then I have got the answer to my question.

10

MR. LE SAR: Madam if we just look and I would just like to clarify in this diagram and if you referred to Annexure “K” in our submission, most certainly the NPS operator forms part of the inner core.

It is..., the NPS operator is tantamount... as a technological provider to enable switching to occur as in the clearing of the transactions and then the determination of the settlement obligations which will then passed on to the..., in our case the South African Reserve Bank.

20

If we talk to the risks inherent, if we look at the model, the different players on the right-hand side and included NPS operators in terms of non-banks, what is clear is

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

there is many different functions that can be performed from purely providing a technical outsource relationship to I think you are referring to in the previous presentation with PASA where some members are just merely providing certain services for bank, to players actually enabling certain provision of information switching through to the likes of the provision of ATM infrastructure et cetera.

10 So there is operational capabilities, moving all the way up to the thing we refer to as float Bureaus to moving up to basically carrying the risk on behalf of and trying to enter the clearing stream.

Unfortunately there is no clear answer, each player's model needs to be broken down in terms of understanding exactly what they are performing, exactly what risks they are bringing to the system and based on that they would need to move from anything from something that hinges around ensuring good sound disaster recovery and business continuity plans all the way up to basically becoming banks.

20 So where they are carrying the value and accessing and holding stores of value similar to what could be construed as deposit taking or the like hence our recommendation that we need to bring the Dedicated Banks Act and Corporate Banks

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

into play. So the ranges of services varies from regulation to just do you conform to certain standards, all the way through to actually you look like and therefore should act like and hence should be a bank.

MS NYASULU: A bank, I think we at idem on that one so I will not pursue it. If we could just again helping me with my understanding, I would liken the role of banks in that whole environment to one where and that is based on the understanding that the
10
PSOs really do their actual function of clearing and settling on behalf of the banks. So my analogy would be that when banks say that you have to be a bank to work..., to operate in that space it is really synonymous to an analogy where you say, “marrying people is the preserve of the priest” but the actual fact is that it is not the priest and the priest is able to appoint Hixonia to marry you because my understanding is that settlement and clearing has actually been outsourced to the PSOs, is my understanding incorrect?

MR. LE SAR: The clearing as in the mere switching technological capability to
20
determine the obligations, 100% correct, in the South African model as been outsourced primarily to Bankserv. The settlement however always remains the preserve of the Central Bank hence the figures are then passed to the Central Bank

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

via extremely tight secure pipelines who would then ensure, in terms of settling, each and every PCH, goes through that motion. Then similarly the Central Bank could choose to outsource the technical side of that operation to a different player. That always remains, but you cannot abdicate your accountability and the responsibility and the risks that you carry.

10 MS NYASULU: Okay that is understood and I am separating accountability from the actual functions of what happens. Just to understand also and I am not quite sure where it was raised but quite a few of the banks raised as a main objection to allowing non-banks into doing certain functions, the fact that you know the whole survivor pays principle, may I ask, we have had numerous bank failures in South Africa, what has been the role of the surviving banks when we have had the failures that we have had? I am just trying to understand the extent to which the survivor really pays.

20 MR. LE SAR: Flippantly obviously it has been to try and survive and I do not mean that in a funny way. If you take the likes of Saambou and the ramifications that had..., knock on it had on to BOE, so BOE was sitting as a very sound bank because of public perception et cetera, ended up feeling the ramifications of a bank falling

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

down and hence public trust if you want to call it that, diminished within that basis and led to the demise of BOE Bank as we knew it. So just when you are creating good mezzanine level banks good middle scale banks, they disappeared.

10 From a surviving bank point of view, the extremities are there, part of the question I think is best posed to the Central Bank because they reserve the right to exactly how they would play out the failure of a bank but it can result in the bank..., the surviving banks been called upon to make good for the settlement shortfall within that and hence basically extend forms of loans and generally non interest bearing et cetera into that space or to the point of BOE to the point where actually they feel the contingent effect and get taken out themselves.

20 So it is extremely onerous sitting in that space plus obviously the thing around foreign direct investment, the rating of the country et cetera and the smaller the country is obviously the more we will feel the effects in terms of bank failure. So I cannot answer you directly but it ranges from anything from just having to throw operational resources at it to basically having to fund it.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MS NYASULU: Okay and I understand the run on the bank and I understand how would affect the BOE and affected others, what I was trying to illicit is whether in and I think we have had something close to five, six or three to four failures to date whether any of the surviving banks to date has had to make good in the settlement particularly arena some of the failures of that bank.

10 MR. LE SAR: Unfortunately I would not have the specifics so I think that is best a question you best put to the Central Bank, we could only speak for ourselves and we would need to consult with our Treasury. So I think it is best to put that to the Central Bank.

MS NYASULU: Can I just say we could I am sure asked the Central Bank but to the extent that it is the survivor who pays, surely all the banks would know because the Central Bank would have called upon the existing and surviving banks. So there is no ways they would have access to your money to settle all of this without asking.

20 MR. LE SAR: Sure I think we need to look at it and come back to you with a more relevant answer...

MS NYASULU: Accepted.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. SINTON: Mrs. Nyasulu can I mention we earlier mentioned CLS Bank is the International Settlement System...

MS NYASULU: Right...

MR. SINTON: I know for a fact that in term of rules of CLS Bank if within a day there is a default by any one member bank, then all the other banks in the settlement system have to chip in, their pro rata share of the shortfall to make sure that
10 settlement occurs in the day and my understanding of that is sort of international best practice. I understand your question to be “do we have a similar systems actually legislated in South Africa, can the Reserve Bank call upon all the other banks to chip in to make up a shortfall to ensure settlement occurs rather than have the whole country come to a standstill should one bank fail.”

MS NYASULU: Yes...

MR. SINTON: I will certainly research that and come back to you.

20

MS NYASULU: It is that Mr. Sinton but it is trying to also access how real this risk is to...

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. SINTON: Sure yes I understand it...

MS NYASULU: The surviving banks...

MR. SINTON: I understand.

MS NYASULU: Because we have already had the situation. I think that covers generally my questions Chairman.

10 CHAIRPERSON: I will give you an opportunity.

ADV PETERSEN: Firstly I would just like to register appreciation for the work that went into this document on access and inter-operability. This is very comprehensive and very enlightening. Incidentally it is not my view that Standard Bank has ever adopted a confrontational tone or as I think a businesslike tone and sometimes the two get confused.

20 But I did get the impression from this document that you have the most conservative attitude to access of all the banks that we have had assistance from to the broadening of access but today I am getting a slightly different impression. The impression I am getting today is that it is not a resistance to access but that you are identifying and

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

these are my words, the inadequacy of the present regulatory framework. Before I go further, would you care to comment on that?

MR. SINTON: Mr. Petersen I think it is fair to say, we do think that the regulatory framework currently does not easily allow non-banks access. Our point being that if the regulations were more comprehensive and clearer so to permit of non-banks to easily gain access i.e. clearly prescribe what the capital adequacy requirements would be and what the rules would be for them to participate, it would be like easier for non-banks to gain access. We really saying as a principle, if it is uncertain about the rules of the game then they should not be playing in the game that is..., but I hesitate to criticize our Regulator.

ADV PETERSEN: Yes our restraints in that regard might not be as severe as yours.

MR. SINTON: Yes Mr. Petersen.

ADV PETERSEN: But you have taken the trouble to set out quite fully at least the headings under which regulation would have been developed to ensure that risk was properly managed. Do you think that the Regulators currently have any appreciation

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

of the extent and sophistication of the regulatory oversight that would be necessary to open up these avenues to more competitive access?

MR. SINTON: That is a subjective...requires subjective ..., we believe they have the...

ADV PETERSEN: Answer are entirely voluntarily.

10 MR. SINTON: We believe they certainly have the expertise and the competence whether they have thought through what is required I think they have in terms of Dedicated Bank's Act and the Corporative Bank's Act they certainly have gone a long way towards understanding what is needed to participate and I think those Acts are intended to certainly open up the access to an number of players who currently cannot participate, so in that context they certainly have thought things through. I would..., I do not..., we do not want to venture an opinion about whether they have really understood all the risks.

20 MR. LE SAR: But Mr. Petersen, if I may, I think if you talk specifically to the NPS as you have seen under the innovation slide and from the PASA presentation, the

THE NATIONAL PAYMENT SYSTEM

focus bearing in mind this is almost still an industry in its infancy if we took the regulatory regime where basically and I think it...

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...put in place around risk management driving at the item limits and then new payment instruments in a very short space of time. I think a lot has been done but the focus has been on the core to date from the original Blue Book of focusing on the
10 inner core and getting that right.

If we look at the Vision 2010, clearly speaks to the remaining areas, the outer core which is now in the process of being addressed and we are very grateful that that is where we are going but we had to get the right regime in place, perhaps wrong word, but the right regulations and the right kind of rigger in place in the inner core before I think we could necessarily understand what would be required on the outer core.

ADV. PETERSEN: Mr Le Sar, thank you, I think you have been present everyday so
20 far during this part of the hearings, if I am not mistaken and incidentally if there is anything that was raised with other participants previously that you..., your bank wants to comment on, please do so. We have not got time to cover all the same

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

questions with everybody but you would have heard questions addressed to the problem of float Bureaus for example. Whatever word you may use for it and that..., in that connection I think I put question to several people whether they had looked at the proposed directive relating to payments to third persons and whether the contents of that draft considered adequate to deal with the risk issues that are posed by such Bureaus. It will be a pity to have to deal with it ex post, if it is inadequate. I do not know if you are able or wish at this point to say anything on that?

10

MR. LE SAR: Mr. Petersen and I stand out.. a legal correction, but I am led to believe that directives are merely there to state high-level policies in terms of intentions. So to..., on that basis, no directive would clearly cover all the risks that are inherent. What is required is a rule set underpinning those directives which to date I have personally I stand corrected, I do not think I have seen sight of but the directives at least move in the step of the intention to start to regulate that specific area.

20

ADV. PETERSEN: Without wanting to get bogged down on the legal side, you might just like to consider that answer further in due course...

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. LE SAR: Will do.

ADV PETERSEN: Because it maybe and that is my impression of it that the directives would, if they are approved be issued under Section 12 of the National Payment System Act.

You see Section 7 of the same Act permits a person as a regular feature of that persons business to accept money or payment instructions et cetera for purposes of making payment on behalf of that other person to a third person to whom payment is due if, and then there is A and B and then C, the money is accepted or payment made in accordance with directives issued by the Reserve Bank from time to time in terms of Section 12.

So it may well be, you might wish to consider whether in fact the intention of the legislation is not that the directive should be comprehensive in addressing the issues that are raised.

20 MR. SINTON: Mr. Petersen, sorry do I understand that you are inviting us to comment whether we think the directive would address our concerns regarding floats, the risk in float holding et cetera.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

ADV. PETERSEN: Yes indeed and whether you wish to answer us on that or not...

MR. SINTON: No we are happy to...

ADV. PETERSEN: I am drawing your attention that it is an important step in the pipeline here and we are raising..., you are raising very important questions about the regulatory framework needed to mitigate risk and here is an instance, it is a narrow one because payment to third persons no..., by no means exhausts the access field
10 where..., I mean if scrutiny is not given to that timeously, it may be very unfortunate.

MR. LE SAR: And we will come back to you.

ADV. PETERSEN: Thank you.

MR. SINTON: Thank you Mr. Petersen.

ADV. PETERSEN: I am sorry I have to cover some of the ground that is been covered already with you. Bankserv and the utility idea, again this is my turn, what
20 do you say to the “dinosaur danger?”

MR. SINTON: Mr. Petersen...

THE NATIONAL PAYMENT SYSTEM

ADV. PETERSEN: That freed from the pressure of competition, in this highly dynamic and technologically innovative field that a public utility could become a dinosaur and in that way retard all the players in the National Payment System?

MR. SINTON: May I start perhaps to explain that our perception is that some of the difficulties around Bankserv arise out of the competition issues in this context in the sense that the four major banks, created Bankserv and they were the..., they were and still are the owners of Bankserv and realising that is was really a utility to facilitate clearing between the banks, the initial shareholder agreement put a cap on what revenues could be produced by Bankserv in terms of earnings that the banks said we are claiming this for ourselves.

There is no purpose in making it profitable entity. We just wanted to run it at effectively the cost of capital and they also reserved themselves the ability to dictate pricing that the banks could charge so they could keep the price at a level which was reasonable and was an accessory in the circumstances.

With the advent of the competition laws we currently are seeking to apply it, the advise given as I understand it was that the ability of the shareholders, being

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

competitors, to actually influence pricing at Bankserv, was anticompetitive and therefore the decision was taken that the shareholders should relinquish all control they had over the company which they proceeded to do and Standard Bank's view is really is well, we have as a shareholder given up all influence over the management of the company.

10 The management are now free to do as they please and that same management as you heard yesterday have said well they feel that they ought to be free to embark upon profit ventures, say for example as hypothetical they may want to offer switching services to the medical aid industry or whatever using the platform which they have which is probably the right thing for the Board of Bankserv to do, if they are going to pursue that growth of that company.

20 What we are saying is taking off our shareholder hat, we are a customer now, we are saying as a customer our concern is, you are vital to the existence of this payment system. You are an essential cog in the whole economy. We are very concerned that if you start diverting your management expertise, your resources, your systems to pursuing revenues in other industries you may neglect us and our systems to our prejudice and for that reason we have said as a principle we think you should rather

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

stick to your knitting, remain a utility for the National Payment System and do not think to embark upon other ventures and that is the issue.

We have not thought through really what you mean by utility, the question from Mr. Bodibe should have be state owned or not, it is certainly not a valuable asset in the hand of the banks in the sense that we put store by what we have invested there. For us it is part of our infrastructure so we are not looking to reap returns as a shareholder and so it is important I think that we have not had that debate yet but we are looking
10 for..., we are proposing that this entity that we have created that is a near monopoly, not be allowed as a really dominant firm to go off into other sectors and compete. We would prefer to keep it as it is so that does not answer your question I am sure but it gives a bit of a background, our sentiment on the issue.

ADV. PETERSEN: I do understand that but the problem is that we may be expected to think it through.

20 MR. SINTON: Yes.

ADV PETERSEN: And I am sure it is the same in business as it is in politics, if you say A, B and C, you are compelled to go on and say here are D, E and F.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. SINTON: Well I will hand you over to Brian Le Sar who can give you more detail. We in fact did deal with it to a degree. What we are saying is that the innovation that has occurred in Bankserv over most of its life has been innovation inspired by its customers who then passed the opportunity through to Bankserv. It is very..., very seldom that Bankserv itself actually innovated anything and..., but he will give you more of that.

10 ADV. PETERSEN: Perhaps I do not know if Mr. Le Sar, you are very welcome to speak immediately but you may wish to just let me raise a couple of sub questions so that you can address it comprehensively. Is that alright, can I...?

MR. LE SAR: Yes.

ADV. PETERSEN: We were..., it was explained to us that volume is all-important so that unit transaction costs are kept to a minimum. Now we were also given a picture of the development of global competition in this regard.

20 Now if it is to be treated as a utility, I use the word in a broad sense without trying to give it precise definition, would it not go with that that use of it, should be compulsory so as to keep its volumes up? Surely could not have your cake and eat it,

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

you use the utility if it suits you and use the cheaper competitive alternative if it does not. So that is the one thing.

And then in relation to that if volume is all important and of course volume has been used as the main argument and maybe a good argument against omitting sorting-at-source to keep up the volume of switching, should one not take that to its logical conclusion and say that for example, these disincentives applied by banks to prevent their customers from using others banks ATMs or discourage them, which also keeps
10 down switching, should be prohibited.

So that is what I mean when I say if you say A, B and C maybe you has to go on and say D, E and F. That is not intended to be exhaustive but those are some of the related questions, which seem to come into the frame.

MR. LE SAR: If I could try and answer you, some of your questions and if I may reserve the right to come back to you later on, it would be great.

20 Just to talk to the dinosaur issue as Mr. Sinton has mentioned, most innovation and one of the reasons why Bankserv initially was changed from moving from COO to CEO, was to insure that they were closer to their customer in terms of understanding

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

their customer needs and various other things that needed to be put in place to insure that the customer's requirements were being met, but I would not necessarily say the innovative ideas come out of the switch, which lies in the middle when it is actually what you are trying to do is to provide to the markets, be it two sided market or one sided market.

10 So the innovation primarily comes from the provider of the service to the customer with Bankserv sitting in the middle and enabling switches. So I think there is many ways around that and if you look at the innovation it has been done, with Bankserv as providing the service certainly not being driven primarily by Bankserv and there are many other facets which could still be explored there.

20 So if you mentioned that then, if as a utility this should then, the volume should not be compulsory, in some sense in the old paradigm, there was that of locking in and finding means of locking in that people got benefit from the utilisation of Bankserv and that is exactly my point. You know I have this lock in and as you have heard from Mr. Shunmugam, this previous lock in of volumes through various mechanisms, which is now still being applied in the commercial sense, which almost talks to strange type of behavior.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

So there is many ways to that and we would concede potentially and have put it to them at the time in terms of many discussions that that would certainly be something we would be willing to explore subject to certain things, i.e. do not come and start competing directly with myself because that would clearly be out of it.

10 So on that volume, if we then talk to the volume being all-important, I just like to clarify perhaps a misconception, I believe a misconception, that was put to you yesterday. The introduction or the increase in Saswitch fee as in the client fee to... the banks fee to their client customers was purported to be 98, 99 and that resulted as put by Mr. Cilliers in this flat volume that eroded out of it. Reality is that fee was put in back in 89 and has been there, it is just been the level that has been increased and the volume we were looking at, the ATM makes up 20 percent of that. So it is clearly cannot be the reason for reducing the volume, but that being said, I think if volume is all important it talks to saying how you be innovative in this space to grow your volume.

20 And as you have seen Bankserv in..., I think 2004/2005 suddenly doubled, almost doubled their volume through clearing and clearing related things by being innovative in terms of saying we could provide fraud services. We could do other

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

things so there is many ways to skin the cat bar just purely looking at banks in terms of who would clearly want on-us first because it is the most cheapest way to provide service to your customers but in the true inter bank world, yes you would want to be driving a common vehicle to be getting economies of scale. I do know.... that does not quite answer your question but it is along those veins and we would welcome to come back to you with some more appropriate answers.

10 ADV. PETERSEN: Thank you, the..., you have referred to it as a monopoly or near monopoly and of course coming from the competition policy and competition law perspective, we have to check that and having done that look at whether there is any abuse of market power and that is so far arisen mainly in relation to differential pricing and what the effects might be on smaller players.

20 But defining the relevant market can be quite a tricky exercise. In certain payment streams there is a fair bit of switching done through Visa Net and MasterCard instead of through Bankserv that is my understanding of it. If the participants in PCHs were to permit other payment system operators, would the entry of existing potential competitors into actual competition with Bankserv not be quite feasible? Are you...,

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

in other words are you stuck with the monopoly or is there the potential for competitive entry?

MR. LE SAR: I do not think anyone is ever stuck. What we are highlighting is that the initial reaction and specifically EFT, there is no viable alternative right now. So Visa and MasterCard are clearly in the card world. VOCA in the UK, well look at the price differentials when you are paying pounds and brochure(?).

10 The other aspect, we have to remember is that South African based on payments law, the rules et cetera, is slightly different necessarily to how switching is happening in other places. So, if I refer to EFT, just take things such as mandate rules are very different and how where the risk resides first what you would have elsewhere.

So it is not quite that easy just to chop and change. So the first new jerk reaction could be the big four become moving to a direct clearing model, which means basically you just skip it and you would swap directly. Clearly that would have
20 catastrophic effects for the smaller players and lead to the wrong kind of decisions been made for the industry as a whole and it fundamentally take us backwards. There are other things that we would give up but new entrants would always come in.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

It is because of the criticality of clearing and settlement to move operators is not something you would do lightly. It is certainly something that would take months, if not years of extensive testing ensuring you have the right banner, they would need to go through the criteria plus you obviously satisfy the Reserve Bank and PASA that they meet those criteria provide the records at standards so yes, anything is possible.

10 What we purporting is that potentially overnight where you are sitting, is that you may have a near monopoly type position in the short to more medium term. I will use another simple standards example, South Africa in the credit card world is the only place..., one of the few countries you can use a budget facility. How would you now switch that through a Visa MasterCard does not necessarily has not been explored, so there is many risks associated with doing it.

20 ADV. PETERSEN: So if..., for a bank as big as yours, if the alternatives are so limited from a practical point of view you would presumably accept that for a small bank, alternatives are quite unrealistic.

MR. LE SAR: Well firstly we need to understand, I would need to move with another bank and to move with a small player would be unrealistic. So I would need

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

to at least get another large volume player to move. So I could not even make that decision on my own and then yes to your point for a smaller bank to try and move to something else, well in some cases could be more *feta foot* because has less legacy systems, less pipes, maybe he is in less PCHs, but if he is in the same amount PCH, yes potentially it could be harder for them.

ADV. PETERSEN: It will need to switch with you anyway.

10 MR. LE SAR: Correct.

ADV PETERSEN: So should we not then be very concerned about any predicament, if it is a genuine predicament, that a small player is placed in by differential pricing in Bankserv.

MR. LE SAR: I think the differential pricing is maybe a bit..., yes there is many ways to look at it. If you took Mr. Cilliers presentation where 60 to 80% of Bankserv costs are fixed, if you went the flat fee route then the fair way would be to say divide
20 that 80% of the fixed cost by how many participants.

ADV. PETERSEN: So that is not the only alternative?

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. LE SAR: Correct.

ADV. PETERSEN: The alternative would be a smoothing or narrowing of the further narrowing of the tier structure and of the differences per transaction within each tier, would it not?

MR. LE SAR: Which I believe they have done in certain elements but by that, yes we can talk as a customer and I am sure that Mr. Shunmugam can bring further light
10 to that, but in terms of where the players sit is it exponentially correct or incorrect, I think you would rather pick that up with Bankserv and evaluate it for yourself.

ADV. PETERSEN: Mr. Shunmugam you want to add?

MR. SHUNMUGAM: Yes I think Bankserv in terms of their pricing tiers have..., I mean they have taken both fixed and variable cost into account and over the years they have smoothed the curve to a certain extent, but I think in the first five tiers, if you look at smaller volume players, they potentially play a smaller percentage in
20 terms of fixed fees and the bigger players obviously pick up..., bigger portion of the fixed cost. So going forward I think there is potential for them to smooth that further

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

for obviously how they determine that curve and how the players fit on to that curve would need to be explored with Bankserv themselves.

MR. LE SAR: But I think it just talks to the nature what Mr. Shunmugam was mentioning earlier around, if you...everything is based on curves and you are truly a competitive player, surely there is a negotiation as opposed to here is your fee.

ADV. PETERSEN: Even you are chaffing under the power, your lack of bargaining
10 power in this situation. I can only just imagine what the smaller players must feel.

I suggested..., was it yesterday that to some extent these hearings on access and regulation are Hamlet without the prince and I am wondering whether it is also not Hamlet without Rosencrantz and Guildenstern because for example Post Bank, something very close to your experience, we have had no input whatsoever and perhaps we will have to take further steps to try to get input from Post Bank, but I raise it with you because you are the sponsoring bank.

20 You have dealt with some of the difficulties that arise out of the... of that function in your submission and it is quite clear, I do not propose to go into that aspect of it, but it has struck me from the beginning that particularly in terms of providing banking

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

services to those least able to afford banking is a potential responsibility for an entity like Post Bank, which we need to explore with them. You have indicated that their volumes have grown to the point where agreed limits within the current regulation of the system or being challenged if not exceeded, do you foresee major further growth on the part of Post Bank? Should we be taking Post Bank seriously as a banking player?

10 MR. LE SAR: I would not like to get into the details and I like to keep, retain the confidentially of what we have put there, but most certainly if we look at all indications from government and from other players, Post Bank most definitely has a role to fulfill in that arena and so just based on that pure premise, yes it will continue to grow and quite clearly we would welcome a clarification of rules visa via all of these sort of areas where there is potentially some grey.

ADV. PETERSEN: Now you sponsor Post Bank into clearing and settlement, is that correct?

20 MR. LE SAR: The arrangement is like.... we stand in front of Post Bank so Post Bank does not nes... we would introduce their transactions under our banner into the

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

clearing regime and we would be the settlement with other banks on their behalf, which is in relation to the sponsorship agreement.

ADV. PETERSEN: I think Post Bank is specifically referred to in one of the sections of the NPS Act for access purposes. Ithala we have been told is sponsored in, not by your bank. Now fortunately you have got the onion diagram up, which just for record purposes, can... does it have a slide number, and I think it is five?

10 MR. LE SAR: Yes.

ADV PETERSEN: Is that right?

MR. LE SAR: That is correct.

ADV. PETERSEN: Now you have on the right-hand side of the central core, sponsored clearing. Now as I mentioned, I think it was this morning, that my reading of the SARB position paper is that it makes provision for sponsorship of a clearing bank.

20

Let my find it... actually I did not mention that this morning because I was dealing only as Mrs. Nyasulu was with mentoring but in 5.2 of that SARB position paper

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

sponsored clearing, this the model for a bank that in a specific PCH provides some of the payment services defined above by version and agreement with the direct clearing bank in terms of which agreement the sponsored clearing bank settlement obligation within the PCH is fulfilled by the sponsoring bank on behalf of the sponsored clearing bank. But if one reads it together with the rest of that document it..., the..., what is stated is that the sponsored clearing bank does its own clearing, it is only sponsored for the settlement obligation, have I got that correct?

10

MR. LE SAR: I think if I can just refer you back to slide 4, where we just... we do talk specifically about new banks, small banks, new entrants. A new bank that does not wish to participate fully i.e. I would like to join potentially I would like to come into ATMs but I do not necessarily want to have a settlement account with the central bank, could utilise a settlement sponsorship arrangement with another bank.

Similarly I might also choose that I would not like to put in the necessarily infrastructure to move my transactions between myself and to the operator, would refer to technical sponsorship.

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Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

So, as I come back to it, it goes back to it and it is similar to the EFT world where you got the types of user codes and do you see the bank or do you see another participant. In these particular cases for the settlement part, it could vary from for example, if I was sponsoring in another bank, the other banks would be worried about me. They would not be worried about the other bank and hence they would see my user code coming up. For reporting purposes, we would keep the other banks codes behind so that we can report to the requisite regulatory bodies of what
10 percentage of our makeup that would be or and then they can choose technical. So there are variations of the theme.

ADV. PETERSEN: Yes I hear you if you are describing what would be entirely feasible and perhaps to some extent would actually occur. The bone that I am gnawing on at the moment arises from the very narrow approach to sponsorship, which is adopted in the SARB position paper on bank modules, Position Paper 2 of
20 2000.

Because in dividing banks into, on the one hand, clearing banks, who then participate in the clearing system and settlement system, a non-clearing bank it is specifically stated in connection with non-clearing banks. First of all, as is obvious it is not a

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

system participant as defined in the NPS Act and therefore may not provide to its clients any of the payment services defined hereunder, under payment services.

And we get in conjunction with that that clearing banks may not provide clearing and settlement services for those banks, for non-clearing banks and that is followed up in a paper that you will be familiar with, the position paper from PASA, which I cannot quote because it is under a claim of confidentiality although it has gone out to practically all on sundry, but you might like to have a look at paragraph 4.1.5 of that position paper and indeed while you are about to look 4.1.2.

10

So you see this is why I am struggling with the problem that I understand there can be a special arrangement for Post Bank. We have been told that an oversight in the drafting of the NPS Act led to the omission of provision for a special arrangement for Ithala Limited but nevertheless that omission has for now for three years since the Act was amended, been filled in by discretion of the part of the decision makers not by correcting the legislation where in due course we will find out why the legislation has not been corrected.

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Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

So I can fit into my head that you have got a special arrangement for Post Bank and Ithala in the system which allows them to be sponsored into the clearing and the settlement space but for non-clearing banks otherwise, I cannot find at the moment any legal avenue for them to get in by way of sponsorship. So I am trying to identify whether there is actually a deficiency in what the system allows for sponsorship by clearing banks of non-clearing banks.

10 MR. LE SAR: Mr. Petersen I will certain warrant coming back to you, I think that the issue ...lies in the fact of what is clearing and is Post Bank and Ithala truly clearing? but I will take it under advisement and come back to you with an answer.

ADV. PETERSEN: You appreciate that the focus of my question is not to say there is anything wrong...

MR. LE SAR: Sure...

20 ADV PETERSEN: With these services being provided for Post Bank and Ithala. That is a fact that they did not do something wrong there, the question is what is the possibility for non-clearing banks generally...

MR. LE SAR: Correct...

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

ADV PETERSEN: To provide more services by way of sponsorship arrangements into the clearing space.

MR. LE SAR: Correct but you will need to take it one step further of is there any reason they would want to and we will comment on that.

ADV. PETERSEN: Thank you, now my questions on homing fees has been covered with the exception of this question. You have, and to me very clearly dealt with this
10 as an instance of interchange and suggested that similar principles applied including the balancing of demand on the two sides of the two-sided market. Should we when we sit down to write our recommendations, be adopting a similar approach to the setting of that form of interchange that we might be considering in relation to interchange for example in the card payment sphere?

MR. LE SAR: Yes.

ADV PETERSEN: Thank you very much.

20

MR. LE SAR: Thank you Mr. Petersen.

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: Okay I have just got one question, going through my notes I noticed that you... there is one bank you sponsored and also one bank you ment....sorry, sorry, well one bank you mentor, two banks you sponsor, one of the banks which you also mentor it is also on the sponsorship side of the equation. Am I correct thus far? Maybe I can mention the bank if you do not mind. Do you mind if I just mention, it is Rennies from what I gather.

10

MR. LE SAR: I am just trying to get... there is technical sponsorship...

CHAIRPERSON: Right.

MR. LE SAR: Of them...

CHAIRPERSON: And?

MR. SHUMMUGAN: Chair...

20

CHAIRPERSON: Are you in mentorship, are you doing any mentorship on Rennies?

MR. SHUNMUGAM: Chair, just to qualify, we actually mentor Rennies...

CHAIRPERSON: Right.

THE NATIONAL PAYMENT SYSTEM

MR. SHUNMUGAM: In the technical capacity.

CHAIRPERSON: Right.

MR. SHUNMUGAM: And..., sorry and it is stipulated in our..., on page 22 of our submission but it is under confidentiality in terms of which payments..., payment mechanism we do that.

CHAIRPERSON: Right.

10

MR. SHUNMUGAM: And they only sponsorship arrangement that we have is with Post Bank.

CHAIRPERSON: It is only Post Bank, not Rennie's? Okay then I got...

MR. LE SAR: But if I could just Mr. Chair, it is quite feasible to be sponsoring a bank in one stream and be mentoring them in another.

CHAIRPERSON: It is feasible?

20

MR. LE SAR: It is feasible...

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: Actually my question was going there...because I just wanted to find out whether are you finding any difficulty in doing that are there not areas of over..., do they overlap or is it different roles?

MR. LE SAR: I think it is very different roles and mentoring really is just providing almost kind of..., it is advice to the other bank when and if they require it. So it would be purely in their hands. The sponsorship however is a very different role where you are picking up the credit and financial obligations or risk on behalf of that player for the good of the industry so you would stand good in event of a failure.

CHAIRPERSON: So it does not create any problems playing the two roles?

MR. LE SAR: Not playing the two roles, no.

CHAIRPERSON: Okay, fine and in your submission, I think page 16 thereof, you make reference to the fact that there will be sponsorship agreements. What I wanted to find out, when you enter into a sponsorship agreement, are there any guidelines for those particular agreements or you can put whatever in the agreement, which suits you in negotiation with...

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. LE SAR: There are..., there is certainly guidelines relevant to..., you would need to ensure that the person you are sponsoring at least conforms to what you are obliged to conform to. So as an example whatever PASA or the Central Bank requires me to conform to, be it from disaster recovery, BCP et cetera, anything that may be relevant, I would be required to put the same thing into my sponsorship agreement but the reality is, the sponsorship agreement remains a commercial agreement.

10

So it is like any commercial arrangement, it would be subject to negotiation in the light but..., sorry..., yes, the terms are not prescribed but we certainly do have a Performa that we would utilise in terms of looking and ensuring that we would be covering ourselves in relation to our obligations to the rest of the industry.

CHAIRPERSON: Okay I just want to establish whether there were some prescribed terms as to what needs to be done. Okay thank you that brings us to the end of the session with the Standard Bank. Oh you have got a question, sorry.

20

MR. BODIBE: Thank you.

CHAIRPERSON: I am sorry about that.

THE NATIONAL PAYMENT SYSTEM

MR. BODIBE: Thank you Chair for that indulgence, can you solve for me a puzzle in your answer to question ten?

MR. SHUNMUGAM: What page is that?

MR. BODIBE: Page 26, the question was whether you have any relationship with Bureau or payment system operators. Now in your answer at 10.3 you confirm you do have a relationship and that at the same time you say you do not support in your...,
10 in at 10.4 so how..., that seems to be a contradiction in terms where you have a relationship but you do not support these relationships.

MR. SHUNMUGAM: Sir I think in terms of what is written in the submission, they are obviously, they are under confidentiality, but I think those relationships that were grown out is..., is exactly out of..., it is obviously these Bureaus fall under the auspices of the bank. So any risks that they would obviously introduce into the system would be under the auspices of the Standard Bank.

20 But I think where you are referring to is 10.4, and I think it qualifies it in the brackets and I think the piece that we are more interested in, is Bureau operations which submit payment on behalf of the third party, which obviously the risk is more in

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

terms of that we cannot see the clients that they are introducing into the system and hence we cannot regulate it or mitigate those risks, I think...

MR. LE SAR: Normal Bureaus are.

MR. SHUNMUGAM: But normal Bureaus are.

MR. BODIBE: And these are not the Bureaus that you already have relationships are not those types of Bureaus that you would not support.

10

MR. SHUNMUGAM: No, not that I am aware of, no.

MR. BODIBE: Thank you.

CHAIRPERSON: Right, then thank you Mr. Sinton and the team. Thank you for presentation, I know we are trying to arrange for another date for a hearing to take care of the other issues, which were left out the last time.

MR. SINTON: It has been arranged.

20

CHAIRPERSON: It has been arranged?

MR. SINTON: Yes Mr. Chairman.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: Okay now thank you then, so we will deal with those in due course. We will adjourn until 14:00, then we will resume please, yes till 14:00.

(Adjourns)

On Resumption:

10 CHAIRPERSON: Good afternoon ladies and gentlemen and welcome to Mr. Rob Shuter and Carmen Whateley. Once again you are on the floor to deal with the National Payment System and just one housekeeping issue again cell phones, if please you could switch them off. Right, you are on the floor; I see you have given us a copy of the slides. They have been sent electronically to the Enquiry Manager. I hope if not it could be sent afterwards and then this would Exhibit WW. You may proceed.

20 MR. SHUTER: Thank you Chair. We have a short presentation, nine slides, some of the material has been covered, so we are going to go through it reasonably briskly so that we can focus on the Q&A.

THE NATIONAL PAYMENT SYSTEM

In terms of page 2, some background I think we have heard this over and over again, just how important trust and confidence in the NPS is for it to function efficiently.

We will explain a little bit on that.

The NPS is dynamic and evolving. I think that we have seen quite a lot of commentary on that as well and essentially what we have seen in this environment over many years is that regulation follows innovation and I think we going to be drawing your attention to few items there as well.

10

What we were asked to cover particularly because this submission was fairly detailed was, sorting-at-source and non-bank acquiring, payment innovation, we have got some general perspectives on the NPS and at the end. Page 3, we really dealing with trust and confidence in the NPS at the end, there are obviously a lot of players in the system, companies, merchants, banks, end users, issuing banks, acquiring banks, the Reserve Bank.

20

There has been quite a lot of talk around confidence, stability and integrity. I think the only slight nuance we would like to bring into the discussion is that obviously what the system really requires is trust, faith for end users to be comfortable that if

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

they present a card at a merchant that their confidential information will not be stored, they will be settled that if they provide payment details to somebody else that only those in amounts will be drawn off their account.

So trust is very, very important for this system to operate effectively and I think the point is that the existing regulatory framework has accommodated that. We certainly do have active participation in the NPS.

- 10 This slide really is attempting to describe some of the evolution of the NPS. It starts off here with a fairly basic framework of acquiring banks, issuing banks using a PCH system operator like Bankserv, the Reserve Bank being involved in settlement and at the bottom we have both clients making payments and people receiving payments and the entities that are regulated are really the ones that are shown in there in yellow.

- 20 What we have see more recently is a whole array of different participants wanting to use the NPS or access the NPS, dedicated or corporative banks, payment service providers, system operators and then obviously merchants as well and the point we

THE NATIONAL PAYMENT SYSTEM

make is that we operate at the moment in somewhat of a regulatory vacuum as to how these new entities will be accommodated in the National Payment System.

But if we move to the next slide, we certainly believe that the Regulator is well aware of this and if we look at the Vision 2010, if we look at comments made in by the Governor in address in November, it is very clear that there are plans well in place to put this in place and if you look at those particular items, if you look at the previous slide, looking at increased accessibility, meeting with the payment needs, enhanced structures, clear development paths, different tiers of banks, criteria for these various operators.

So whilst the formal regulatory framework is not in place, I think we have a very clear indication from the Regulator that this framework will be put in place and that non-banks will be accommodated in any framework. It is very specific in that regard. If you can turn very briefly to single acquiring versus sorting-at-source, what the slide is presenting is that in single acquiring you have an acquiring bank, you have an issuing bank, you have a switch and essentially what happens is the merchants put their transactions into the system via the acquiring bank. I think we have covered that

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

in some detail. They do on occasion use the payment system provider or system operator but the transactions go through the acquiring bank.

A few comments there, clearly the clients are entrusting the banks with their funds, as issuing banks we need to be comfortable that the transactions that will be hitting our clients accounts are valid, authenticated and have integrity and we receive those transactions currently from an acquiring bank and we all know that there is a very complex regulatory framework for banks.

10

So we have faith that the acquiring bank who went us that transaction, if there is an error or an overcharge or whatever that we will be able to reverse that transaction and be settled and essentially the payment instruction here is between two regulated entities, two banks.

If we move to sorting-at-source, essentially what is contemplated in sorting in source is that a merchant, a sophisticated merchant either through the payment system provide or system operator, could directly access the end user's account. So we have sketched that up there, it would be an exchange between the merchant sometimes acting through payment service provider and the issuing bank.

20

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

We make the point again that the regulatory framework does not cater for this right now. That it would need to be adapted and that that adaptation requires careful consideration. I think for example the regulatory environment in which banks operate, Mrs. Nyasulu would as an ex bank director would be quite familiar with the capital adequacy, prudential, trilateral, bilateral, draft presentations.

10 That framework is not going to suite particularly well a retailer. So I do not think it is simple as... it is not a simple as saying that in order for a retailer to access directly the NPS and send transactions directly to the end users account but they would need to comply with the existing framework. Essentially a new framework is going to have to be developed to cater for these very particular entities. So discussion on capital adequacy with the retailer is going to be bit of an absurd discussion because they do not operate in the same way that banks operate. So our essential point is that it is the framework that is not in place that is the core issue here.

20 You did ask or the technical committee asked that we focus a little bit on payment innovation,..... has not come up that much I think and certainly in the one or two presentations I have attended, but if you look at the diagram there we have the fairly standards of for four party model, acquirer, issuer, clients and payment beneficiaries.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

We have the payment platform in the middle. We used this slide before. All the things that sit on the payment, on the platform to facilitate inter-operability, infrastructure technology standards, messaging formats, clearing rules et cetera, et cetera.

10 And the point we want to make is that there are really two types of innovation that can take place here. In the first instance there is innovation that has to take place on the platform and for it to take place on platform you really need the consensus of all the participants and quite a lot of that has taken place. More recently cell-phone top ups and cash back at cause(?) are technical innovations on the payment platform.

20 But that is not the only type of innovation and participants such as ourselves do not always have to beg and implore all the banks or all the participants to agree. There is a variety of innovations that can be done without the consent of everybody so there are some PCHs, real time clearing that is a PCH that as an example Nedbank has not participated in parts of early debit order. We in NAEDOS, we are not in AEDOS. So it is not essential that everybody participates and then there is a lot of functionality that various banks have developed for their own cardholders and their own merchants

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

which is not needed to be done on a platform, so we just thought that might be a useful distinction.

So whistling through it, the last few comments are really that you all understand that the SARB is the Regulator of the NPS, I think that much is clear, that regulation aims to provide risk management and trust required for robust efficient adoptable NPS, we comply with the national, with the regulatory framework. We do support extension of access, the framework as we have said needs to be adapted and then, you know, we welcome competition.

MS NYASULU: I think we should let Rob start.

ADV. PETERSEN: Me?

MS NYASULU: Yes.

ADV PETERSEN: Mr. Shuter either you or colleagues of yours, I think have been present throughout this set of hearings and just as you did not try to recover all the grounds that has been covered by others and I would not try to cover it either with questions but obviously this is your opportunity also to comment on any of the issues, which have been raised earlier.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

So let me confine myself then to things that specifically struck me from your very helpful second volume of submissions. Some of them quite technical points, which I would like to explore. I assume you have that volume with you?

MR. SHUTER: Yes we do.

ADV PETERSEN: Could you go to the section on acquiring which in my file is yellow, has a yellow tag, to pages 2 to 3 and I would like to read that together with
10 page 12, where you have given your answer to question 27 and I... it seems to me there is not a confidentiality problem here so I can go straight into it. When Nedbank accepts by Nedbank's acquiring infrastructure by aid cards such as for example those of Pretorium Trust, how is clearing and settlement effected? Right you participate on the acquiring side, what is the participation on the paying side?

MR. SHUTER: I think what I like to do with your indulgence is ask our Head of
Card to join the panel because we were not expecting to much focus on the card side
20 but fortunately he is here, Sydney Gericke for the record and I think he is best equipped to answer question particularly on the buy aids. Sydney, are you good to...

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

ADV. PETERSEN: Perhaps just before Mister... thank you, Mr. Gericke, perhaps just before you answer, the reason that I am asking that today is because I just want to understand whether there is some access taking place here, which is not simply a clearing bank access.

10 MR. GERICKE: Good afternoon, I did not plan to sit here but I am just supposed to answer this question. In fact for the buy aids there is no clearing and settlement, as we would understand it in the context of the NPS. What we do for buy aids, we issue the cards, the plastic to the cardholders and then we do two additional things, we host an authorisation file which affectively is a credit balance or “the open to buyers” as it is known, of the member. So whenever they go and transact, the transaction would come through to us, we would look at “the open to buyer”, the credit limit available, the line available and approve or decline it.

20 What we would do at the end of the day, we would provide a summary of the purchased transactions for each member to the respective buy aid and they in turn would independently settle the merchant. The relationship is also between the buy aids and the merchant, not between the bank acquiring business and the merchant for the buy aids business.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

Where our green machine or our..., (indistinct)infrastructure is used, the card will be accepted, the buy aids card on that machine, but we would only hold the Visa/MasterCard acquiring relationship with the merchant. We simply act in this instance as a processor and authorisation agent for the buy aids.

ADV. PETERSEN: Speaking for myself, it is going to...

MS NYASULU: I did not understand that one bit...

10

ADV PETERSEN: Require reading the transcript before I fully can...

MS NYASULU: Yes.

ADV PETERSEN: Unpick that answer for which..., thank you very much. Is this not the exchange of payment instructions?

20

MR. GERICKE: Not through the payment system as described in this presentation or the so-called four party model. This is an independent arrangement that we have with the buy aids and it is very closed loop in the sense that we can only accept those transactions where they have signed up the merchant and we are the acquirer of that merchant for the Visa/Master transactions.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. SHUTER: Carmen just wanted to add some comment sir.

MS WHATELEY: If I may, just to clarify, I think the key distinction that we would make would be the difference between a closed user group and participation in a fully inter-operable payment platform and that is the key distinction in this case. In this case it is a closed user group, imagine the fact that you..., it is not quite a buy aid but I think it is sort of similar illustration using if you have an Edgars card and that you can use it at Jets and the Sales House, it is a similar type of concept. Those are store cards but it is a similar concept, it has limited use.

10

ADV. PETERSEN: And if , correct me if I am wrong, it is a credit instrument in the sense that the... that the store or the Pretorium Trust whoever it is, is extending credit to the card user, is that right? There is no deposit sitting with the card issuer in that case.

MR. GERICKE: That is correct. The credit is extended by the buy aid and managed by the buy aid.

20

ADV. PETERSEN: Now moving on to ATMs, I cannot predict whether it is safe for Mr. Gericke to retire at this point but moving on to ATMs you will be well aware of

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

the issues that have been raised concerning the requirement in the ATM PCH agreement and the clearing rules, if I have interpreted them correctly, which confines participants to processing transactions only from devices owned by or contracted to a participating bank.

Now before I go further perhaps I should ask you whether you have any comment on that issue which we may or may not but we may consider it to be some kind of restriction or exclusion introduced by agreement between the participating banks, 10 which is not actually required by the regulatory framework. So I am just putting that up to you without any prejudgement of the issue, I put that up to you for comment if you wish to add anything to what others have said early in the hearings.

MR. SHUTER: I think we have discussed it internally and just a few comments.

Clearly under the existing framework, it requires a bank to introduce transactions into the NPS and so maybe it is useful to make a distinction between the acquiring bank and the device owner. So if we look at it in a point of sale context, the device that is 20 actually accepting the transaction can be owned by the bank, it can be owned by the retailer, it can utilise the retailers point of sale infrastructure but that transaction needs to go through an acquiring bank to be introduced into the NPS.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

That is similarly what is happening in ATM, the device can be owned by the bank, it can be owned by a device owner, provided it is contracted to a bank. We understand that contracting to be similarly that there needs to an acquiring relationship with those transactions need to flow through an acquiring bank into the system.

10 ADV. PETERSEN: Well thank you, let me just say that I have seen in what I have read, a difference with point of sale devices and that it is in fact not necessary that the point of sale device to be contracted to the bank and so I have seen the requirement in the ATM PCH agreement and Clearing Rules as an additional restriction, are you saying that is not the case?

20 MR. SHUTER: I think we are focusing on the operational reality of it that neither the device owner of a point of sale or of an ATM can introduce transactions into the NPS other than through an acquiring bank. Now how that is expressed in the PCHs practically on the ground, we know that the device only is either the bank or someone who has a relationship with them.

ADV. PETERSEN: Bear with me a second, if you would?

THE NATIONAL PAYMENT SYSTEM

MR. SHUTER: We did attempt to come up with a description of the device owner; the point of origination was what Carmen came up with but we thought it had a rather unfortunate acronym so we decided to leave it.

(Laughter)

ADV. PETERSEN: But in fact, as I understand it, some ATM transactions are the electronic payment instructions generated at the ATM, are delivered directly into
10 Bankserv.

MR. SHUTER: In all cases the ATM is sponsored by a bank and all the recourse is to a bank who sits in this regulatory framework that we have. So let say for example, that an erroneous instruction is delivered to a Nedbank account holder and the account is over debited, in that example our recourse as the issuing bank, is to that sponsoring bank and that is really where we draw comfort from in terms of them operating with the NPS.

20 ADV. PETERSEN: Or the acquiring bank, which would be the same as sponsoring bank in this situation.

MR. SHUTER: And the critical thing is that they are a bank?

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

ADV. PETERSEN: Yes that I understand but in seeking as we obviously exploring the possibilities of doing, in seeking to open up access to more players including non-bank players, we obviously try to analyse to what extent functions can be performed, which do not entail participation in clearing, in settlement but which could perhaps be performed directly without having to be approved by a particular bank.

10 I am not suggesting they would not have to meet objective standards and be regulated but it seems to me that there is a difference between having to contract one's service to a bank not only to find an acquiring bank for the purposes of the service, but to contract the entire service to the bank, in order to be able to get in. There is a difference between that and being able to get in technically or meeting objectives and transparent standards, and then having of course had an acquiring bank to sponsor the transaction and the clearing and settlement. I do not know whether that distinction, which I have in my mind, makes any sense to you?

20 MR. SHUTER: I think it does make sense and I think what we need to be clear on our position, which is perhaps slightly different to what you have heard all along. We think that the core issue here is that the regulatory framework does not exist for non-banks, and as an issuing bank the counterparty for us is always an acquiring bank and

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

we know that we can rely on the regulation that surrounds banks. Capital adequacy, disaster recovery, prudential limits, solvency et cetera, et cetera.

We have a very clear understanding from the Regulator that this framework is going to be constructed for non-banks, that have been said in as many words, and we think that's absolutely fine and once that framework exists, we are very happy that that competition takes place.

- 10 So we are not raising a whole lot of concerns that even if the framework was in place, we would be worried about this or that. We are not in the second part of the debate. We are really in the first part of the debate.

ADV. PETERSEN: So then as a matter of detail within that framework, you deal with integrators in various parts of your submission. For example again within the acquiring section on page 11 in your answer to Section... into Question 25A, you say if I may quote you:

- 20 *“Nedbank currently has the ability to acquire transactions through most of the local third party integrators. Integrators are entities that switch transactions on behalf of merchants to acquiring banks and provide merchants with*

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

integrated tool systems and back office reconciliation facilities. Where the merchant uses an integrator, Nedbank will facilitate the implementation of an integrated link and offer both technical and project management resources.”

That is an example of where you deal with integrators. Now what I want to explore in relation to that using this as another example to test whether we could have the possibility of a more direct access.

- 10 Let us conceive of the acquiring function remaining with the bank and on the other side the issuing function being that of a bank. At the moment the integrator must get in through a bank's infrastructure. The question again is whether one could not by development of the regulatory framework with proper standards, risk management, disaster recovery and all the things that might go with that, have an objective and transparent basis upon which an integrator could qualify to be able to deliver those transactions directly into the clearing system. In other words deliver them to the payment system operator, who after all is going to carry out the functions connected
- 20 with clearing or most of them on behalf of the participating banks. Would that again be an instance where you would be open to a properly regulated development of access?

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. SHUTER: If I could just make a few comments, introductory, and then I will answer it. You made the comment I think in the last presentation that its a bit like Hamlet without the prince and so the analogy we felt was perhaps more appropriate, is its a bit like a tournament without the referee.

You know we would love a situation where only banks with a green logo can issue credit cards. That would be fantastic for us but clearly that is not the space we are in and so it is not... we have a competitive interest in the field in which we play and we are a concerned citizen of the National Payment System but it is not really up to us, you know, on what basis other competitors come in.

So if the regulatory framework is intact and no risk is being... no more risk is being introduced into the system and then what will be will be, I think is generally the philosophy we have.

ADV. PETERSEN: Thank you. Another point where in your submission where integrators come up, is on page 29 of the same section, the acquiring section. In your answer to Question 48B on that page, okay here you are dealing with internet transactions, same principles?

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. SHUTER: Sir, in many instances our corporate clients deal with integrators.

They get a whole range of value added services from them and the transactions are delivered to us as acquiring bank via the integrator. If the regulatory framework is expanded on a basis that an integrator can access directly on the same way we do as acquiring banks within the regulatory domain, then that is what will happen and we will compete with them in a slightly different way than we compete now.

10 ADV. PETERSEN: Thank you. Let me move then to sorting-at-source. Would you mind bringing up slide 7 again? Now here you have me a bit puzzled and so I would appreciate it if you could clear this up. You say in the first bullet point on the right-hand side of the slide “the payment instruction in sorting-at-source” that is where the merchant sorts, “would be exchanged between the merchant/payment service provider and the issuing bank.” Now the... to the extent that the NPS Act defines clearing as the exchange of payment instructions, are you saying that sorting-at-source involves clearing?

20 MR. SHUTER: I want to ask Carmen to answer that.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MS WHATELEY: I think the approach that we have taken in describing specifically how we would understand sort-at-source to work, because clearly it does not... it is not practiced as it is today, is that as practitioners as business people in the payment environment, we would describe the transaction as a transaction coming from a payment service provider or to a merchant on to the issuing bank in the same way if one looks at our previous slide, we understand from a business perspective that without sorting-at-source the transaction moves between the acquirer and the issuer.

10 So it was not a legal statement. It was a descriptive from a payment business perspective.

ADV. PETERSEN: See I heard Standard Bank to say this morning that they see sorting-at-source as an extended form of multiple acquiring. But within the way that you describe it, you seem to have removed the acquiring element. So that is what I am wanting to test out because in the way that I have seen it up to now, it has seemed to me that the issuing bank is also has to be the acquiring bank for purposes of the transactions sorted to it and that therefore you have issuing and acquiring residing in the same bank as in any on-us transaction and so that is why I am having difficulty with this idea that sorting-at-source really introduces some strange different process.

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Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MS WHATELEY: I guess the one question for me would be that multiple acquiring, despite its definition, refers to the fact that there is more than one acquirer and that one... as I recall it was in the PASA presentation, they did not refer to multiple acquiring, they refer to multiple banking.

That I think is just one point so the difference... that we would see between multiple acquiring and sorting-at-source and that sorted sources essentially splitting one's transactions according to its destination and..

10

ADV. PETERSEN: Yes you will appreciate that I am in no way expressing a view to whether sort-at-source is a good thing or a bad thing. I am merely looking at it from the point of view of what goes on.

Okay now if I am the merchant and I want to sort-at-source, what I imagine I would be doing is establishing an acquiring relationship and having an account with several banks. I could have it with all issuing banks but that would probably be too many since there are so many issuers. So let us say I want to do this with the four major banks and assuming that they were amenable to it, I would have an acquiring relationship and hold an account with each of those banks. What I would then do is

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Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

sort my transactions with customers according to which of those four was the issuing bank in respect of that particular card transaction and I would then just see to the delivery of the payment instructions, assuming that there is no direct access to Bankserv or any other switch. I would simply be delivering the sort..., that parcel of payment instructions to the issuing bank which is also my acquiring bank for purposes of those transactions. So I cannot see that the acquiring is removed from it or that I am entering into clearing in my own name.

10

MR. SHUTER: Yes and I think that as we have described it there is not how you described it and I am not so sure one is right or wrong. I mean nothing..., I think sorting-at-source is a little bit in the realm of speculation because we do not have a model currently of sorting-at-source. I think what our slide contemplated was that the merchant would have their existing banking accounts and they would be able to go through an entity like Bankserv and extract money from whichever issuing bank the particular account holder had.

20

ADV. PETERSEN: That is a more radical concept.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. SHUTER: And that is really what we described, your alternative is that the merchant opens accounts with each bank and essentially has a four acquiring relationship...

ADV. PETERSEN: That is multiple acquiring.

MR. SHUTER: That we would describe as multiple acquiring.

10 ADV. PETERSEN: A more developed multiple acquiring than is currently permitted.

MR. SHUTER: Yes because currently multiple acquiring is really between the associations.

ADV. PETERSEN: Well that is how it is..., that is the extent to which it is permitted.

20 MR. SHUTER: I think obviously what is also slightly awkward in sorting-at-source is that there are you know, very many more issuing banks than acquiring banks and that introduces a layer of complexity. I think maybe if I can just say from our perspective, we have no particularly issue with sorting-at-source. We think if the

THE NATIONAL PAYMENT SYSTEM

regulatory framework is amended then rather let you know, there be a competitive playing field.

ADV. PETERSEN: But do you not agree with the observation that has been made to us that almost inevitably the implication of this would be a big reduction in switching volumes and that that would have attendant consequences upon the unit cost per switching transaction, which we would have to take into account in any recommendation that we might make.

10

MR. SHUTER: We would not make that argument, I think as vociferously as it has been made. In essence if we have..., I mean Nedbank is a large player in acquiring. I think as you know.

If we had a particular merchant to desperately wanted to do it this way, we have other options available in terms of persuading them to keep their business with us and looking at how things are priced, perhaps letting them operate in this way for a while and seeing just how easy it is because I do not think it is going to be simple. You know to the extent that there is a drop of volume through Bankserv which as we all

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Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

know essentially is processing off-us transactions. You know, it may be possible that our unit cost goes up a bit, and you know, so be it.

ADV. PETERSEN: Would you think that it could intensify competition in the acquiring market that is to say as between the acquirers for merchant business and sir and perhaps bring down merchant service charges.

MR. SHUTER: Obviously we would have to speculate on that but I do believe that if
10 it was clearly possible that the framework is in place for it, that large merchants would use it in their negotiating discussions with their acquiring banks. I think practically very few merchants would have the technical ability, or in fact have the appetite to do it because the vast bulk of our merchants are quite happy with the service being provided and they got other things on their minds. You know if there are fashion retailers in Menlyn Park with 30% margins, they really not particularly focused on the acquiring side.

20 ADV. PETERSEN: You have said in your submission that sort-at-source is currently not permissible in the debit and credit card PCH rules. Would you agree that there is no statutory ground of exclusion in existence at the moment?

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. SHUTER: Have we prepared an answer on that? I will have to go through this whole pile of papers, Carmen can you pick it up the...

MS WHATELEY: I think that the..., what I will share with you is our understanding of the manner in which we arrived at the position where it was stated in the PCH agreements and that would be at the time when the moratorium was placed on this practice by the Reserve Bank and for..., with concerns around the risks and issues of that.

10

We are currently in a process of still discussing the issue with the Reserve Bank and because there are some areas of potential unattended consequences that as responsible participants we feel we need to confirm with the Reserve Bank that we have the same understanding of the issues and the potential way in which they could be managed prior to lifting it from a PCH agreement. So it is really, it is work in progress.

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ADV. PETERSEN: Now if I were to say to you I am imposing a moratorium on some practice, you tell me to get lost, quite correctly. When the Reserve Bank says to

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

you we are imposing a moratorium on some practice, what power do you regard them as exercising when they do that?

MR. SHUTER: I think that practically operationally we would desist from that practice, the Regulator is the primary regulator of the banking industry.

ADV. PETERSEN: You would not explore whether there was a power been lawfully invoked there?

10

MR. SHUTER: It is a difficult question to answer.

ADV. PETERSEN: I appreciate that. I was somewhat puzzled when Mr. Volker of ABSA said that he regards on us transactions as also involving clearing, is that your view?

MR. SHUTER: I did not attend the ABSA hearing.

MS WHATELEY: I did attend and I think again it would depend on looking at it from a business perspective and I am not to sure from which perspective Mr. Volker he was you know, referring to the legal definition but from a business

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

perspective a technical description would be as an exchange of a payment instruction from one side of the bank to the other.

ADV. PETERSEN: Within the same bank, not an exchange between different participants?

MS WHATELEY: But it is still an exchange between two functions but I think that is also the point to understand perhaps from a business perspective, payments and
10 exchange between two functions, the person who asks for the money and the person who gives it.

ADV. PETERSEN: On the Bankserv policy issues and here I am addressing, yes this is also in the section on acquiring, let me just see that you have not asserted confidentiality here, page 6. I just want to make sure that I do not overstep the mark. Yes okay I am in the clear. In answer to question 16 you indicated that you mainly use Bankserv for domestic transactions switching but you do use Visa and
20 MasterCard, I quote: “for selected local card transaction switching due to specific value added services they provide,” unquote.

MR. SHUTER: Question 17?

THE NATIONAL PAYMENT SYSTEM

ADV. PETERSEN: Yes I beg your pardon. I beg your pardon answer to question 17. So would you be prepared to indicate just so we can get a mental grasp on it what the value added services would be that would persuade you to use a different switch than Bankserv?

10 MR. GERICKE: What we see is that innovation on these payment platforms are not necessarily always in step and some of the management information that Visa and MasterCard can provide you about cardholder transactions over their infrastructure is well beyond what Bankserv can today do. So we are using on specific bins and specific products a choice of Visa and MasterCard where we want to access that information and understand the cardholder spend better than what we today get out of Bankserv and that drives our choice. It is really the innovation on the respective payments.

20 ADV. PETERSEN: Thank you and answer to question 19 on the next page you say Nedbank would consider switching more of its present volume through Visa and MasterCard if the commercial arrangement and value added services for this option proves to be better than that offered by Bankserv. In other words you approach it from a business point of view. Now you have heard the discussion about whether

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

Bankserv should be treated as a utility or treated as a purely commercial competitive enterprise in swimming in the big ocean, have you got a view on that?

MR. SHUTER: We do...,my teammate is telling me to stop shaking my legs... I think what we see in the Bankserv debate is that often what is presented are two extremes of the spectrum. So on one side what is presented is a state owned utility doing only one thing, regulated pricing et cetera, et cetera?

10 On the other side what is presented is a commercial enterprise, diversifying, could be buying casinos or operating the lottery or getting into chains of hamburger stations whatever and these thing are often described in you know some of the conversations between the banks as being the utility versus the commercial enterprise and I think the..., you know the painting them as extremes is not always helpful.

Our perspective is that the right solution for Bankserv is somewhere in the middle. So we do not believe it should be state owned. We think that there is a lot of merit in
20 operating this as part of private enterprise. We believe it should be operated as a for-profit organization. We think that brings disciplines around cost control, cap-ex, just the disciplines of managing a business.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

We believe that its....one of its primary objectives always will be to operate as this payment system operator in the South African context and that there is a huge commercial rationale for them to never put that at risk and on top of that we think sensible diversification is quite acceptable so not to be the casinos and the hamburgers but possibly to switch other transaction types, look at other markets.

10 So we are in sort of sensible diversification from where they are without putting the core business at risk and I think the only other thing I can add into the pot is that we really are not attached to our shareholding in Bankserv. Most important thing for us is our relationship with Bankserv as a service provider to Nedbank. So that is really not a big thing in our lives either.

ADV. PETERSEN: And maintaining this happy medium should be achieved how?

MR. SHUTER: I think that is a challenge for all businesses. I think we really would rely on the rational economic imperative for them to protect their core business.

20 ADV. PETERSEN: You have dealt quite extensively with the competitive threats to Bankserv. The implications of those threats, the crucial dependence on volume and so forth. Presumably you say that is really for Bankserv to make sensible decisions,

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

presumably big customers of Bankserv also have to make sensible decisions in order for this happy medium to be sustained because at the moment one of the threats is that the big players move their business, switching business elsewhere, which it appears, could be done without too much disruption.

MR. SHUTER: I think we are obviously a relatively small player in all of this. I mean we are the smallest of the big four banks. I think we continually ask the panel not to view us as homogenous, we are a net payer of interchange both in ATM and
10 card. We directionally would far rather see lower interchange that higher interchange, just to give you one example, and you know I think our essential ideology really is that they are doing a good job. It makes sense for us to use them.

To set up our own infrastructure would be much more costly. We want a sound economic agreement with them and we leave ourselves flexible depending on what happens in the industry. Clearly whatever other payment system operator comes in
20 would also be regulated, would also have to comply with all the framework that they would have to comply with, so there are lots of checks and balances in the system.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

ADV. PETERSEN: Now a more technical point again, if I may, you indicate I think that a cash settlement payment-clearing house is under development. Those are... is that correct and the access and inter-operability section, page 5, yes in that table it is the third row from the bottom, could you just explain to us what that is about?

MR. SHUTER: I am unsighted on that.

MS WHATELEY: I also do not know the technical detail but quite happy to come
10 back to you later on that.

ADV. PETERSEN: Thank you that would be helpful and then what is the difference essentially between RTC and immediate settlement, PC... because there is two different PCH's?

MS WHATELEY: I think that looking at the names is instructive, immediate settlement is the PCH that looks after the real-time line as the system operating. In other words that is the system across which settlement occurs. So for example the
20 kinds of things that they would look at will be item limits over to manage certain risks.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

RTC is real-time clearing, which is a payment stream, which envisages that if I were to make a payment to a client of another bank that that process would occur within... I think it is within a minute is the time. So that would be clearing and then there would be settlement rules associated with that clearing that that PCH is essentially about this service of clearing within a specific amount of time and whereas the other is more about the settlement process.

10 ADV. PETERSEN: But that... but they are distinct payment streams presumably?

MS WHATELEY: That is correct.

ADV. PETERSEN: Is that... does it have anything to do with the five million Rand limit on RTC?

20 MS WHATELEY: The correct... let me answer that more broadly, is that one of the..., if one has read, there is quite a lot of material available from the Reserve Bank on the different measures that have been put in place to mitigate settlement risk to try and reduce overnight exposures and exposures that the industry may face over the time. One of those measures that was deemed necessary was around the item limits that could be processed within any payment stream. So one has similar item limits in

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

the EFT payment stream and it is really around trying to limit the values that can be processed within that. So from a RTC perspective it is a similar construct.

ADV. PETERSEN: And then the immediate settlement PCH, are they similarly limits?

MS WHATELEY: Sir, the immediate settlement PCH is about the settlement process. So for example RTC transactions are settled via the immediate settlement
10 PCH.

ADV. PETERSEN: Oh I see. So that the PCH is interlinked at that point, thank you. Thank you very much.

MR. BODIBE: Good afternoon. I just have one question that is related to question 2 on page 28 on access and inter-operability. Okay I am not going to ask about which organizations you have relationship but just for you to confirm that you have relationships with Bureaus or payment system operators.
20

MR. SHUTER: Yes we do.

MR. BODIBE: Even in the context of this regulatory vacuum?

THE NATIONAL PAYMENT SYSTEM

MR. SHUTER: I think the point is that the way the Bureaus operate, we do not necessarily regard as being in a vacuum in the sense that there is no regulatory framework for retailers or other operators to access the NPS directly.

MR. BODIBE: So you do not have the same kind of concern that you have for the other type of players?

MR. SHUTER: No, we do not.

10 MR. BODIBE: And related to that case of, this is my second question. Sorry I said I have one question. If I want to enter the banking space, okay, we already now accepted Petersen ATM's and I do not want to have inter-operability with any bank, do I go through the same system or same process of acceptance.

MR. SHUTER: Sorry, let me just clarify...

20 MR. BODIBE: I know it may not be realistic to try to enter as a bank that has own relationship with its clients and no relationship with other banks but I just want to understand the legal and the process point and the processes that I would have to follow in gaining partici..., entry into the banking space.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. SHUTER: So I suppose the first question is for clarity, so is it your intention to become the bank?

MR. BODIBE: Yes.

MR. SHUTER: Okay so the question is what is the process to become a bank or is it, what is the process once I am a bank to participate in these various payment streams?

10 MR. BODIBE: Will I have to follow the same processes as another bank that wants to have the kind of...that wants to participate fully in the system when all I want to be is to be a bank that has a relationship with its clients and nobody else.

MS WHATELEY: I have a..., I am sorry perhaps it has been a long day, I just have to check that I get the question correctly, are you asking “I would like to offer payment services...”

MR. BODIBE: No.

20 MS WHATELEY: No? What services do I want to...?

MR. BODIBE: Deposit taking, I just want to be a bank.

THE NATIONAL PAYMENT SYSTEM

MR. SHUTER: It is either a very simple question or a very complex question. I think the answer is that to become a bank you need to comply with the Banks Act. It is when you want to participate in the National Payment System that you have to decide which PCHs you want to participate, do you want to just paid in debit card or credit card or EFT and then you will follow a process. So your example of just being a very simple savings bank, you would follow a very different process to somebody who wants to participated in all the different payment streams of the NPS.

10

MR. BODIBE: So the only hurdle that I have got to cross is the Reserve Bank Act in this example?

MR. SHUTER: Well you have to comply with the Banks Act...

MR. BODIBE: Yes.

MR. SHUTER: Which I would submit is a very large hurdle.

20

MR. BODIBE: Okay thank you, thank you Chairman.

MS NYASULU: Mr. Shuter and team, just first of all just a frustration because I feel stymied... because just before lunch all my questions disappeared when you replaced

THE NATIONAL PAYMENT SYSTEM

pages 18 to 25 which had been open suddenly claimed confidentially on them. So I am just going to go with the two questions that are left after those have disappeared and this one relates to the question that Mr. Bodibe just asked you recently and it is on your concerns regarding what you have to referred to as Bureaus that work on a third party basis and I think our technical team referred to them as float, float Bureaus.

10 Now your biggest worry clearly is around the fact that they sign up clients and that you have no visibility and you have no way of knowing, you know what risk those clients would introduce. Now, what confuses me is you obviously would have given them a user code, you have given them a credit limit and so you have done some form of due diligence on the Bureau itself. Why would it worry you who lies behind that if you have set a credit limit for them and you have actually given them a user code?

20 MS WHATELEY: At the time that we would sign up the Bureau and assign them a credit limit, clearly we take it on good faith and an explanation from them on what their business model entails. I do not think that at the time that we sign the Bureau up, they are in any position to tell us who or they would be signing up underneath.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

So it is really just that in the nature of their business and a competitive environment where they want to get as many transactions as they would like, Nedbank has no way of knowing who they are signing up and through the course of debts.

MS NYASULU: So just to follow-up, what risk would that actually introduce because I understand that you do not know who they have signed up? Let us just assume that you have given them a credit limit of say 600 million, I do not knowwould you give 20 million? Let us make it 20 million, they are obviously very
10 small, but let us say they sign up 20 clients, that does not change the credit limit that you have given them. You still have control on how far they can go in their activities, so why is that a risk?

MR. SHUTER: What I can say Mrs Nyasulu is that Nedbank has a policy for example that we do not bank clients in the escort industry that...

MS NYASULU: Wonder why but that is...

20 MR. SHUTER: We can debate that?

MS NYASULU: Yeah, we would not.

THE NATIONAL PAYMENT SYSTEM

MR. SHUTER: But that is the banks policy.

MS NYASULU: Right.

MR. SHUTER: The danger with the Bureau is that we do not actually know who we are banking.

MS NYASULU: Okay but that is a separate risk...

10 MR. SHUTER: And it is from a policy perspective...

MS NYASULU: It more a reputational risk that you are talking about rather than what I understood to be a risk because just to read a little bit further you then say, you know, the bank which is you yourselves, would then be liable for fraudulent transactions. So that is a completely different risk and that is the one I could not understand, reputational I understand completely specifically with the example that you have given.

20 MR. SHUTER: I think just the other point to raise is that whilst we as banks are liable for the settlement, we in turn then would attempt to recover from our client

THE NATIONAL PAYMENT SYSTEM

through the Bureau and that is also why it is important because we are reliant on that eventual client to effect our recovery.

MS NYASULU: Absolutely whereas I have said to one of the other banks, I see that as no different to if you knew the corporate and if you had actually had a relationship directly with the corporate because you, yourselves in the end would have no guarantee that if they were fraudulent transactions and you wanted to collect that you would always be able to.

10

MR. SHUTER: There is no guarantee you will be settled but when we know the corporate, we know what our risk is and we have signed up for that risk. When you have got blind banking, like you have had with this example it is just more awkward.

MS NYASULU: And may I ask then and I see Ms Whateley wants to add something, I am not going to stop you, so go for it.

MS WHATELEY: I wanted to really use an example because I think that examples are definitely more instructive. There recently has been a case and if I am not mistaken one of the other banks also alluded to in May hearing, where a Bureau as described here introduced a user who did fraudulent collections of our some public

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Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

service employees and disappeared with those funds so there clearly is a fraudulent risk. Those parties are now without money and the party has absconded. We did not know who the party was.

MS NYASULU: So in that case it will be, supposing this Bureau was one of your clients, you would have to pick up the mess.

MS WHATELEY: Absolutely.

10 MS NYASULU: Okay, understood. If we could go to, I am now trying to find where my questions are, the ones that can ask.

MR. SHUTER: Can I just comment on the confidentiality just while you are searching, we have certainly attempted to keep us much of our submission not confidential. I think we one of the few in last two, the particular section you are referring to was that we realised that the information was not really ours to disclose, it related as you know, to Bankserv and so unfortunately we had to withdraw it.

20 MS NYASULU: Okay, yes. Okay I think I will now go back to your presentation and maybe ask you to call up slide 6 and I was trying to understand this slide because as I look at it although it is headed "Single Acquiring," it really is a slide that I would

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

use against non-banks acquiring because if I follow your logic around the fact that you would be getting an instruction from an acquiring bank and therefore you essentially trust them. What you are talking about is really the integrity of the request for payment.

MR. SHUTER: So I think it did come up, I think yesterday that non-bank acquiring is a bit of an oxymoron I suppose, currently you actually cannot practically have a non-bank acquirer. I think the thing here is that we can rely on the acquiring bank for many things, not just that the transaction is valid. It has been authenticated that if there is a dispute, we can get the money back, that acquiring bank will have the capital, that they got a whole lot of safeguards in place and that there will be disaster recovering, they would not fall over, they will keep records for five years, so it is much broader than simply that it is a valid transaction.

Clearly what happened, if the regulatory framework was created for perhaps are more extreme version of sorting-at-source, we would be able to write here that the non-bank acquirer complies with multiple regulations to guarantee this trust and they could all proceed quite happily to the future.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MS NYASULU: Okay granted. My other question would be whether or to what extent some of that trust in another bank is really misplaced because I would argue that there must be occasions where despite the fact that the acquirer was a bank who had gone through all of these hoops and have been registered and bank sacked and all of those things that they have failed and left you or left the surviving banks to pick up particularly in their acquiring space. I mean I have asked the question about survivor paying within the greater NPS, but in this instance where the acquirer was no longer around even if they were a bank and had been registered and regulated, is that trust not misplaced? Just the fact that they are a bank does not mean you guaranteed they will be around next year.

MR. SHUTER: So this is what banks refer to as counterparty risk. We would have counterparty risk against that particular bank. I think the history in South African experience is that banks have gone into curatorship, they have not simply on the next day stop trading and generally settlement has proceeded and deposits have been frozen and in an orderly process has been gone through. I think that is the experience for at least probably since the 70's that that is the process that has been gone through.

MS NYASULU: Okay...

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

MR. SHUTER: So...

MS NYASULU: So it is really the regulatory framework around banks that gives you comfort rather than a bank itself and so if you replace that acquirer space with an entity that had the same regulatory framework that would give you comfort, you would have not problem with that.

MR. SHUTER: Absolutely, I think the point we are making is that it cannot be
10 exactly the same framework because the way you regulate a retailer is going to be different in the example...

MS NYASULU: Absolutely...

MR. SHUTER: But we are quite happy for that to happen.

MS NYASULU: Okay and if we go to your slide 7, your second bullet point, which
20 says “the current regulatory framework does not cater for merchants and payment services providers acting in this capacity,” I think it is absolutely valid. You would have been in the previous discussions where we were talking about how that group of entities would be regulated. Would you agree and be comfortable that if the

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

regulatory framework that is used to regulate payment system operators, would be sufficient to regulate that same group of entities?

MR. SHUTER: Difficult to answer, we would want to see a regulatory framework that gave us a similar level of comfort for a merchant or payment service provider as we have from another bank and until we see that it is difficult to comment on what would be enough or appropriate.

10 MS NYASULU: Can I just ask why you would want it from another bank and it is a term bank that I would question and the reason that I am asking that is, as I have indicated in the earlier hearings, the payment system operators that have access to clearing and settlement are not banks and..., but they are regulated which is what gives you comfort and all I am asking is if we took that kind of regulatory framework and used it for these groups of people and entities, would that suffice?

20 MR. SHUTER: Sorry just to clarify my answer, what I am saying is that we would want a similar comfort with this new entity that we have in the existing arrangement for a bank. What a payment system operator like Bankserv does is potentially quite

THE NATIONAL PAYMENT SYSTEM

different to what a retailer may do and it is not clear that the one framework will be suitable for the other.

MS NYASULU: Okay that is all Chairman thank you.

CHAIRPERSON: Is that all?

MS NYASULU: Yes.

10 CHAIRPERSON: In the last three days most of my questions have been sort of addressed but I just got a couple of queries I have and maybe you will assist me to understand a couple of things.

Going back to your slide number 5, you talk about regulation which follows innovation. Earlier on this morning we had PASA, I was just wondering what will be your views, would you say the same applies to PASA when it comes to regulation?

20 MS WHATELEY: We would and in fact this is a principle that is one of the principles in the Vision 2010 that it is always been a principle with the National Payment System that regulation follows innovation to prevent a stifling of innovation and an example would be..., my interpretation of the role of PASA would be that if a

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

new transaction were to be desired to input into the system, their evaluation of that transaction would be on the basis of the additional risk it may or may not introduce as opposed to anything else and that those matters of risk are actually clearly defined in the regulatory framework within which PASA has its devolved authority, so yes I would.

10 MR. SHUTER: So it is a phrase that it is used in the industry and it is really saying that if your regulatory framework is static, it would be very difficult to introduce new innovations. So it is essentially saying that as the innovations come, the regulatory framework must be amended to cater for the innovation on a sustainable and sensible basis.

CHAIRPERSON: So one can anticipate that in whatever innovations will come through would be accordingly addressed by PASA in their..., within their regulatory framework.

20 MR. SHUTER: PASA and the Reserve Bank.

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: And the Reserve Bank of course, alright the other one, I just want to ask you when it comes to sponsorship and mentorship, do banks have a say as to whether they want to participate or not?

MR. SHUTER: Sadly Mr. Chair, Nedbank has never been approached to either sponsor or mentor a bank.

CHAIRPERSON: Well I just, that was my next question.

10 MR. SHUTER: We are the wallflower of the banking industry. I am not sure we would be able to shed a whole lot of light on that.

CHAIRPERSON: Okay...

MS NYASULU: I will give you Petersen's ATM.

20 CHAIRPERSON: You can mentor Petersen's ATM. Well, right fine, that was going to be my next question but lastly page 19 and 20. I just want to deal with that but it is sort of confidential so I am going to tread carefully, if you think..., are you battling to see that? You can imagine I have to read this in the middle of the night.

THE NATIONAL PAYMENT SYSTEM

MR. SHUTER: I think they are trying to keep it confidential from me. I mean it is really a section on...

CHAIRPERSON: On Bankserv...

MR. SHUTER: Bankserv pricing model and then...

10 CHAIRPERSON: I just want to ask you about the pricing model. If you would think I am treading on confidential ground just let me know. The pricing model, you make a reference at page 19, to the fact that your costs increase as a result of the change in the pricing model but then in the other page, if you look at line 208 on page 20, I am not going to read it out. Now I just..., maybe if you could expand if you feel free to talk about just so us to..., you can read it if you feel it is not confidential, it is up to you, 208, line 208.

MR. SHUTER: Sir is your question trying to reconcile and open this to the model with the fact of (indistinct)...

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CHAIRPERSON: Yes I am trying to reconcile the two statements.

THE NATIONAL PAYMENT SYSTEM

MR. SHUTER: I mean I think we will answer it fairly straight forwardly, the amount by which our cost went up was about 800 thousand Rand on a banking cost base of some..11 or 12 billion, so it was not a significant amount.

CHAIRPERSON: It was not a significant amount because I sort of tried to reconcile the two statements and I was wondering why would anybody support it, if it had those consequences but I understand that now.

10 MR. SHUTER: We had bigger battles to fight at the time as well. I think...

CHAIRPERSON: There were bigger battles to fight.

MR. SHUTER: Yes.

CHAIRPERSON: Okay I have got no further questions unless anybody else got another question.

MS NYASULU: No, not for me.

20 CHAIRPERSON: Okay thank you Mr. Shuter, Ms Whateley and Mr. Gericke for coming. We will adjourn today's hearings until....,

MS NYASULU: We do not know.

Pretoria
29 MAY 2007

THE NATIONAL PAYMENT SYSTEM

CHAIRPERSON: I am not sure of when we are sitting again. It will be on the website though, oh yes, Dr Hawkins has her hand up.

MR. SHUTER: 5 June.

CHAIRPERSON: 5 June, we will adjourn until 5 June when we will sit again to deal with the other issues.

MR. SHUTER: Thank you.

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CHAIRPERSON: Thank you for coming.

(End)

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