INSTANT PAYMENTS: REALLY A REAL-TIME REALITY?

Oddly, speed is not the chief attraction of instant payments, according to Adrian Lovney, CEO of the New Payments Platform (NPP) in Australia. He thinks round-the-clock availability, the ability to enrich a payments message with additional data and the operational simplicity of settling continuously rather than in batches are more important. Nearly eight months on from launch, the CEO of NPP is now looking to grow its network, settlement volumes and services. MI Forum magazine asked him what lessons the story of NPP holds for other market infrastructures pondering a transition to instant payments.

The New Payments Platform (NPP) in Australia has set a new standard in instant payments. Every single transaction is settled in real-time, in central bank money, round-the-clock, all-year-round. “There is no delayed settlement,” says Adrian Lovney, CEO of NPP Australia Limited. “There is no netting. It is instant payment. There is no value limit set by the central system. Though sending and receiving banks can set their own limits, we have seen a payment of A$28 million go through the NPP.”

Though NPP has no floor either – paying a cent through the system is a trick Lovney plays on sceptical visitors to his office – the figure of $28 million is a vivid reminder that instant payment is especially attractive to counterparties exchanging significant value. “Instant payment drives credit and settlement risk out of the system,” explains Lovney. “We expect people to get comfortable with using NPP to buy and sell houses, for the same reason.”

Initially, however, Australian banks have focused on shifting low value, free-of-charge, person-to-person payments, primarily in the retail channel, to NPP. These do not require the fastest speeds. The Service Level Agreement (SLA) NPP signs with the banks defines “real-time” as clearing and settling a transaction in less than 12 seconds, though the system is capable of settling much faster than that.

But the Osko person-to-person instant payment service now running on NPP aims to post money in the account of the payee within 60 seconds – five times as long as the SLA target, and with added time to allow banks to run fraud checks and sanctions screening. “Generally, Australians will see money in their account in significantly less than 60 seconds,” says Lovney.

Speed is a feature not a benefit of instant payments

But he thinks the focus on speed is misplaced. In his view, NPP offers more important capabilities than instant settlement. An obvious one is round-the-clock availability 24 hours a day, 365 days a year. A less obvious one is openness to smaller banks and non-banks. Another is the flexibility to address a payment either through the familiar combination of a sort code and account number, or by using a so-called PayID.

PayIDs are memorable identifiers, such as a telephone number or email address or company registration number, that can be linked to a particular account. “A benefit of PayID is that it provides confirmation of the legal account name of the beneficiary, before the payment is executed,” says Lovney.

But the most valuable service enhancement offered by Osko is the ability to enrich payment instructions with additional information of up to 280 characters in length (including emojis). This represents a considerable advance on the 18 characters available in the old batch processing system. In addition, the Osko service will soon enable requests for payment, as well as allowing business senders to attach documents, explaining what the payment is for.

Banks are staggering the migration to instant payment

The amount of data a payments message can carry will become steadily more important as the payments banks choose to process via NPP shift from person-to-person payments to unattended and bulk transactions. Early candidates include interest and dividend payments, insurance pay-outs, payroll, superannuation contributions and benefits, and electronic invoicing and payments by corporates. The most data-light, least time-sensitive payments will probably be the last to move to NPP.

“The banks have taken a slow and steady approach to shifting payment channels to NPP,” explains Lovney. “They start with a relatively small set of customers through one channel first, or start in a particular state, in order to get comfortable with the process before rolling it out to other client groups or geographies. They may apply transaction value limits to manage the risk, starting as low as A$500 or A$1,000 before lifting or removing these as their confidence grows.

> **“Retail customers appreciate the cautious approach taken by Australian financial institutions”**
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> **- Adrian Lovney, CEO**
> **New Payments Platform (NPP)**
> **Australia**

In some instances, they might also hold back the first real-time payment customers make to facilitate fraud, Know Your Client (KYC) and Anti-Money Laundering (AML) checks.”

Evidence from social media suggests that retail customers appreciate the cautious approach taken by Australian financial institutions. In fact, it is ironic that such a bold initiative has benefited since its inception from a safety-first approach. But then taking NPP from a blueprint to going live with the back offices of 60 institutions representing more than 80 per cent of bank accounts in Australia was a risky enterprise.

Lovney pays handsome tribute to SWIFT, which nursed the project through the design, elaboration, building and testing stages to go-live. “The support, the attention to detail, and the diligence and the quality of the build from SWIFT has been absolutely exceptional,” he says. “There is clear acknowledgement from the industry, as well as from our own organization, that SWIFT provided an exceptional level of service delivery throughout the process.”

But he also argues that designing, building, testing and launching the central infrastructure was the least complicated aspect of the delivery of NPP. “Integrating with the kit supplied by SWIFT was a relatively small part of the overall effort,” says Lovney. “The real challenge was back office integration, and it was under-estimated by some participants.”

Migration means integration with multiple back office systems

The gain from of accomplishing it is one of the least-noticed benefits of NPP. Batch processing systems require banks to net and bundle instructions into packages of payments, not all of which will be processed in the next available cycle, leading to delays in payments that can extend for as long as 48 hours if sent over a weekend. NPP simply processes a continuous stream of payments on a gross basis in real-time.

But the level of change required to banking platforms, operational processes and customer channels to make that stream possible was enormous. Every stage had to be scoped accurately and planned meticulously if the industry was to shift from a batch environment to a real-time environment without any allowance for down-time. Major banks had upwards of 50 systems impacted by NPP, including fraud detection, anti-money laundering and sanctions screening systems as well as core banking and back office technologies.

Financial crime and customer due diligence rapidly became a major focus of the integration process. Lovney recalls that in the run-up to the launch of NPP, technology vendors lost no opportunity to remind Australian banks that the transition to the Faster Payments system in the United Kingdom in 2008 was accompanied by a surge in fraudulent transactions. Significantly, the NPP planners did not suffer the same fate.

Good planning makes for a trouble-free transition

“We are not complacent about fraud, but those predictions have not eventuated,” says Lovney. “True, a lot has changed in terms of the technology since 2008. It now provides much greater security in both mobile and Internet payments channels than it did back then. But the Australian banks were also very focused on denying fraudsters any opportunities as NPP went live. They have continued to do a good job since in detecting and preventing fraud in real-time payments. The levels of fraud in NPP are very similar to those we see in the old batch system.”

The old batch system has continued to run in parallel with NPP. There are no plans to retire the legacy system, though its volumes will gradually be cannibalized by NPP as banks transition more and more channels and payment types to NPP. “We foresee the batch system continuing to operate for many years to come,” says Lovney. “Some banks are more focused than others on the opportunities created by NPP to cut the costs of running multiple legacy clearing streams.”

So keeping the batch processing system operational is not a risk management decision. Lovney says NPP does not need to be backed up by an alternative payments market infrastructure. While a handful of banks have had to suspend real-time payments briefly since launch, their problems were specific to the banks concerned. NPP has experienced no system-wide outages at all. “We are very happy with the overall performance of the entire eco-system over the last six months,” says Lovney.

He thinks this trouble-free transition also reflects careful planning. “An important focus for us in late 2017 and early 2018 was transitioning from programme to operational mode,” he says. “Obviously, you need one set of people to plan, design, build, test and prove a system, and a different set of people to run it. We spent time planning that transition over a four-month period prior to going live.”

Domestic market growth is the priority

Since going live, the management of NPP has concentrated on bedding the system down. But it is now switching its attention to extending the size of the network (by getting the remaining 20 per cent of Australian bank accounts connected) and growing transaction volumes (to enable NPP to lower the price of transactions). But extending coverage and growing volume is inevitably also a function of the capabilities of the platform.

NPP has just launched an API framework for banks to extend real-time payment services to FinTechs and corporates. It is actively exploring a central consent-and-mandate service as an alternative to direct debits, and Osko will soon roll out the planned request-to-pay capability. NPP is also talking to both international payments FinTechs and to SWIFT about how it can support inbound payments from overseas, whether they are intermediated by correspondent banks or other digital intermediaries. One obvious option is to feed real-time data into the SWIFT gpi service.

Naturally, the company continues to work closely with SWIFT, whose follow-the-sun network of data centres guarantees the NPP is open for business round-the-clock. The plan is to publish two upgrades to the centralized infrastructure a year, one minor and one major. SWIFT is also helping NPP encourage its users

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to communicate with the platform using the ISO 20022 standard. Adopting ISO 20022 will in time make it easier for NPP to provide cash settlement services to the new distributed ledger technology (DLT) settlement platform now being built by ASX, which has also adopted the standard.

Once the ASX platform is live, it will drive settlement traffic to NPP. This fits the NPP strategy of giving priority to growing its domestic franchise. When NPP went live on 1 February 2018, the 60 institutions connected to it included some of the smallest customer-owned banks and credit unions in Australia. But there are over 100 authorized deposit-taking institutions (APIs) in Australia, and 10 more have joined since February. All APIs are free to join NPP directly and submit clearing and settlement messages, but so far only 13 have done so, with the remainder choosing to connect indirectly through another participant.

Non-banks were always free to develop products – the platform separates products from infrastructure, so that companies can build products that make use of different aspects and features of the infrastructure - that are hosted by NPP and used by banks. But corporates and FinTechs will be able to connect directly or indirectly to NPP, in order to submit payment initiation messages to banks and to pass other non-value messages to banks, through a graduated set of admission criteria. "We want the system to be accessible to a wide range of organizations, only some of which will be banks," explains Lovney.

Six valuable lessons of NPP for other market infrastructures

What NPP will not be doing is developing a consulting service for payments market infrastructures planning a transition to real-time payments. "We would not seek to tell other people how to run their businesses," says Lovney. "Every jurisdiction is different. And we are focused on opportunities in Australia, principally."

But he is happy to share with other market infrastructures the knowledge gleaned from the six-year journey of NPP from concept to reality. Let the regulators set goals and features, he says, but free the payments industry to determine the best way to deliver them. Specify the scope of the system and its budget at the outset, to prevent mission-creep and contain costs. Ensure that the platform is extensible, so it can support multiple use-cases. Run the organization to cover its costs, not maximize its profits. Cut fees instead of paying dividends. Above all, argues Lovney, put the right governance structure in place, to ensure that banks which ordinarily compete fiercely with each other are able to collaborate successfully to deliver the project.

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