

Payment systems in the Republic of Armenia

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Introduction

The collapse of the Soviet Union was followed by the dismantling of the unified banking system in Armenia. Consequently, the Central Bank of Armenia had to solve a number of problems, related in particular to the existence of an enormous amount of non-payments on settlements between enterprises and organisations operating within Armenia, the lack of a legal framework regulating interbank settlements, the inadequate infrastructure of the banking system, an energy crisis and a paralysed postal delivery system.

During 1993–97 the Central Bank of Armenia took active steps to tackle these problems, to establish new settlement relationships and to improve interbank settlements. New projects have been undertaken not only to resolve the present-day issues relating to the payment and settlement system, but also to define the future system.

Let me first give a brief account of the current situation in our payment and settlement system and then describe the steps that the Central Bank of Armenia is taking to develop the system and all the associated problems.

Payment and settlement system reform

In the Republic of Armenia there are 29 commercial banks with 173 branches; of these, 28 banks and 42 branches are located in the capital Yerevan.

At present, banking activity is regulated by the following laws:

- the Law on the Central Bank of Armenia (30th June 1996);
- the Law on Banks and Banking (30th June 1996);
- the Law on Bank Bankruptcy (29th June 1996); and
- the Law on Banking Secrecy (14th October 1996).

Payment and settlement relationships are governed by:

- the Law on Funds Transmission by Payment Order (30th June 1996) as well as a number of other laws;
- the resolutions, instructions and regulations issued by the central bank; and
- interbank agreements.

To coordinate the work of developing the payment and settlement system in Armenia, an interbank Committee on Payment System Development was established in April 1994 with the participation of representatives from the central bank and commercial banks.

The development of the domestic payment system has been carried out in the following phases, reflecting the concentration of payment activity in Yerevan and difficulties with physical delivery at the inter-regional level:

- the introduction of new payment procedures in Yerevan;
- the introduction of new payment procedures for intra-regional payments; and
- the introduction of new payment procedures for inter-regional payments.

All licensed banks hold one correspondent (settlement) account at the Central Bank of Armenia. Compulsory reserves are held in the same accounts. The number of correspondent accounts that commercial banks may hold at domestic and foreign banks is unlimited.

Settlement on the accounts at the central bank is same-day, final and irrevocable. In order to reduce risks, all settlements are on a gross basis.

In individual cases anticipated shortfalls in funds can be covered by loans from the central bank using government securities as collateral.

At present, there are no separate large-value and low-value interbank systems. Essentially, all payments are effected by two basic interbank settlement mechanisms operated by the Central Bank of Armenia – gross (electronic and paper-based) systems and a clearing system (in operation since 1994).

Since February 1995, Armenia has been operating an intra-regional payment system.

The central bank has introduced uniform codes for banks, their branches and customer account numbers based on EBS200 as well as national formats for electronic messages based on ISO and S.W.I.F.T. standards.

In March 1997, the central bank (where the main terminal is located) and eight commercial banks (with a shared connection through the main terminal) were linked to S.W.I.F.T. The work of linking up another four banks is in progress.

Also in March 1997, the central bank issued a special resolution setting a time-limit for the execution of interbank transfers in Armenia. Penalties are imposed if transfers are delayed. The procedure and the level of penalties and fines for delays and incorrect payments are defined by an interbank agreement on payment deadlines and the establishment of interbank arbitration, according to which the party at fault must pay a penalty in respect of a delayed payment equivalent to twice the refinancing rate for the whole period of delay.

As part of the development of the interbank payment system, the central bank is implementing an interbank wide area network (called CBANet) and an electronic funds transfer system (called BANKMAIL) for all banks, their branches and the Treasury. In November 1997, 20 bank head offices, 14 bank branches and 34 Treasury branches were connected to CBANet, while 15 commercial banks are making electronic payments using BANKMAIL. The extension of BANKMAIL to other commercial banks is in progress.

The central bank has started work on setting up a securities accounting and book-entry settlement system using the delivery-versus-payment principle. This work will be completed in 1998.

In the area of retail payments, the central bank plans to set up a National Interbank Card System in the Republic of Armenia and implement new payment instruments using the CBANet.

Problem areas

In the process of developing the payment and settlement system the central bank encountered a number of problems that hampered progress, namely:

- poor cooperation between commercial banks;
- a lack of commercial bank staff sufficiently qualified in the area of payment systems;
- inadequate equipment and a lack of reliable communication links at the commercial banks;

- the absence of a tradition of providing banking services and inadequate bank structures;
- a population unaccustomed to using banking services;
- commercial banks' lack of experience in the area of security and protection of information;
- the large volume of cash in M1 (52%). Individuals and business entities generally make payments by cash, without using the banking sector; and
- the limited number of payment instruments (89% of non-cash payments are made by payment order).

Conclusions

One of the basic objectives of the Central Bank of Armenia is the creation and development of a modern payment and settlement system. The Bank is therefore playing an active role. During the reform process we have learnt some important lessons concerning the functions that the Bank must perform. These include:

- the redefinition and regulation of payment and settlement relationships;
- the establishment and improvement of payment and settlement systems;
- the supervision of their operations;
- the provision of payment and settlement system services and, on the basis of experience, other functions such as training of commercial bank specialists and the consolidation of banks' resources in order to implement interbank projects (S.W.I.F.T., National Interbank Card System, interbank arbitrage).

Experience has shown that sometimes the central bank has to take initiatives, as was the case with the implementation of S.W.I.F.T., CBANet and BANKMAIL. Otherwise, as with plastic cards, the banking sector may not achieve satisfactory results and may consequently turn to the central bank to take the lead.

During the planning and introduction of innovations in the banking sector the central bank needs the advice of the commercial banks, but sometimes it has to issue strict instructions within the limits of its rights to oblige the banks to follow its payment system policy (as was the case

with uniform customer account numbers, the setting of a time-limit for the execution of interbank transfers, etc.).

We have greatly benefited from learning from international experience, the cooperation and coordination of our work with international organisations (IMF, BIS, TACIS, USAID), and the technical assistance received from them and, especially, from central banks.