

Business Services

The RBA provides a range of services including banking services to the Australian Government and other customers; a registry of Commonwealth Government securities and other securities; payments and settlement services; and note issue services to banks. Where appropriate, services are provided on a commercial basis, with those services run as individual businesses which seek to recover their full costs, and earn a return on notional capital, through fees and charges.

The RBA's principal focus in carrying out these services as a central bank derives directly from the *Reserve Bank Act 1959* which says that:

- the RBA is empowered to carry on business as a central bank, and shall, in so far as the Commonwealth requires it to do so, act as banker and financial agent for the Commonwealth; and
- the RBA is empowered to print currency notes, and to issue, reissue and cancel currency notes.

Accordingly, the principal focus is:

- for banking and registry, to service the Commonwealth's requirements;
- for settlement services, to develop and operate a reliable payment and settlement system that ensures risks are well identified and controlled and that limits the spread of any problems that might arise; and
- for note issue services, to meet the community's requirements for clean, counterfeit-free currency.

These activities are carried out by the Business Services Group which comprises the Banking, Payments Settlements and Note Issue Departments. Services are delivered through Sydney, the branch in Canberra and via the National Note Processing and Distribution Centre (NNPDC) operated by the RBA's subsidiary, Note Printing Australia Limited (NPA), at Craigieburn, Victoria.

Banking

Banking services are provided to the Australian Government and to other customers, including 50 overseas official institutions and central banks.

The RBA provides a central banking facility to the Australian Government consisting of a group of bank accounts, known as the Official Public Account (OPA) Group, whose aggregate balances represent the Government's daily cash position. These banking arrangements include the provision of a term deposit facility for the investment of temporarily surplus funds, the sweeping of balances to and from agencies' accounts held with transactional bankers, and access to a strictly limited overdraft facility. To assist in monetary policy and liquidity management, this service also includes the electronic collection of forecasting data and reporting on high-

value transactions from agencies and transactional bankers. The Department of Finance and Administration (Finance) manages this facility on behalf of the Australian Government. A new Central Banking and Related Services Agreement, replacing the previous agreement dating from August 2000, was executed with Finance during the year.

The other component of government banking business is the provision of transactional banking services to government agencies.

Traditional banking services offered by the RBA include bank account facilities and the processing of transactions such as deposits, cheques and bulk direct entry. The major services provided to government agencies are described below. Access to these services is usually via a dedicated leased line connection or via the *ReserveLink* electronic desktop banking package. In recent times, access has also been broadened to include *RBAnet*, an internet-based account and transaction enquiry system.

The Government Direct Entry Service (GDES) receives and processes bulk electronic direct credit and direct debit transactions from government agencies and distributes these to financial institutions. This service makes use of an extensive communication network and warehousing capabilities and is the main transactional banking activity performed by the RBA for its government banking customers. It has incorporated same-day settlement since its inception. GDES transactions processed include government welfare pensions, salaries and vendor payments; 217 million transactions were processed in 2003/04, an increase of 1 million from the previous year.

The RBA Overseas Banking Service provides customers with the ability to send instructions electronically for overseas payments to be made via draft, telegraphic transfer, or direct entry. This service provides government agencies with a secure, timely and cost-effective delivery mechanism for their regular overseas payments. For overseas direct entry payments, the RBA has now established Automated Clearing House arrangements in 22 countries on behalf of Centrelink for the distribution of Australian pension payments to overseas bank accounts in the local currency.

The Document Printing Service enables customers to send payment details electronically to the RBA for the issue of cheques and electronic documents on their behalf. For cheques, the RBA service includes the production, enveloping and mailing of the cheque together with an attached remittance advice. For electronic payments, the service provides for the delivery (by post, email or facsimile) of a remittance advice with the actual payment occurring via direct entry. The volumes of transactions processed via this service increased by 7.5 per cent in 2003/04.

The Cheque Reconciliation and Verification System offers a full cheque reconciliation service for government agencies as well as a verification system to detect whether or not a cheque has been fraudulently altered. This service, developed in-house, uses image technology to confirm that the details of a cheque presented for payment match details of the cheque when it was originally issued. This system enables the RBA to detect changes to cheque information quickly, thereby protecting itself and its customers from losses due to fraudulent cheque alteration. The system has proven to be highly beneficial to government agencies because it minimises their exposure to cheque fraud and has been a significant factor in reducing fraudulent alteration of government cheques.

Government Easy pay is a telephone and internet collection service that allows government agencies, which would not normally have the volumes for a stand-alone service, to receive payments from clients using major credit cards. During 2003/04, the volume of collections via this service increased by 35 per cent as additional agencies commenced using this product.

Earnings after tax from transactional banking activities were \$3.0 million in 2003/04, compared with \$3.2 million in the previous year.

Business Developments

Activities during the past year focused on improving existing banking products and services and on working with major customers – including Centrelink, the Health Insurance Commission, and the Australian Taxation Office – on projects designed to improve processes and better satisfy their banking needs.

Work continued during the year on providing secure banking services via the internet, through *RBA net*, which is now available to customers. This facility provides enquiry functions to assist customers with all their account, cheque and trace requirements. All information relating to banking transactions and cheque presentations is available on-line. For customers, a major feature of this system is the availability of high-resolution images of deposit transactions (and supporting cheques) and presented cheques (both the front and reverse sides). Given the often sensitive nature and high value of government payments, *RBA net* does not provide for value payments to be effected via the internet. The RBA will continue to monitor internet security technologies and Australian Government guidelines in this regard. In the meantime *ReserveLink*, which offers a secure closed network environment for both data and value payment files, remains the main method for the transmission of files for the majority of government agencies.

Risk management practices and procedures for banking services are continually under review. This year, particular attention was given to the privacy and protection of customer data and to the standardisation of the methodologies used to identify and manage risks, in conjunction with the RBA's new Risk Management Unit.

During the past year, the RBA worked with a number of government agencies to help them meet their business continuity requirements in relation to payments. As a consequence of this initiative, government agencies are now offered a generic service which will, should an agency suffer a loss of key systems or personnel, allow that agency to continue making payments pending re-establishment of their internal operations and systems.

Arrangements for the provision of banking and safe custody services to overseas official institutions and central banks were also the subject of a detailed review during the year. The review resulted in the RBA adopting a consistent approach to the services offered, as arrangements for individual organisations had evolved separately over many years.

Registry

Registry services are provided to the Australian Government and a number of official foreign institutions which have Australian dollar debt programs. Services provided to all clients include the issue, transfer and registration of securities, the maintenance of ownership records, the distribution of interest payments and the redemption of securities at maturity. Additional services

which are specific to the Commonwealth Registry include the management and encashment of physical securities; the maintenance of records relating to unclaimed Commonwealth Government securities (CGS) monies; the undertaking of historical searches; and the provision of a small investor facility which enables retail investors to access CGS.

Traditional paper-based registry activity remains low as in other recent years. This type of activity is now predominantly related to retail-based holdings as large institutional holdings of CGS are held and traded electronically outside the Commonwealth Registry in Austraclear.

Earnings after tax for the CGS registry business in 2003/04 were \$0.1 million, the same as in the previous year.

Settlement Services

RTGS and Other Settlement Services

About 90 per cent of the value of interbank payments is settled on a real-time gross settlement (RTGS) basis; this includes all wholesale debt and money market settlements, a range of time-critical customer payments and Australian dollar foreign exchange settlements (including those settled by CLS Bank for which a net settlement is made daily on an RTGS basis).

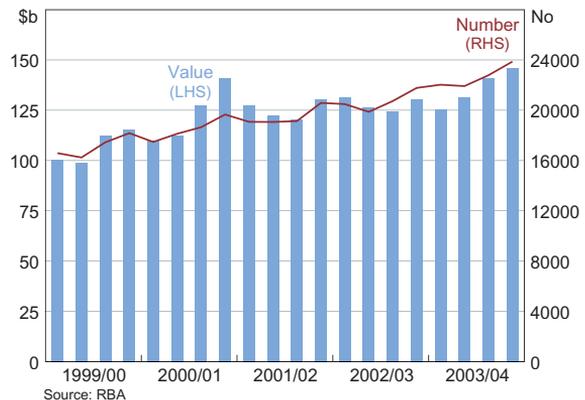
The Reserve Bank Information and Transfer System (RITS) is the means by which banks and other approved institutions settle these RTGS and other interbank payments across their Exchange Settlement Accounts (ESAs) conducted with the RBA.

RTGS turnover through RITS grew strongly in 2003/04 in terms of both value and number of payments settled. On average, around 22 600 payments totalling \$136 billion were settled across RITS each day. This represented growth of 9.3 per cent and 6.0 per cent, respectively, on the corresponding figures for the previous financial year. The percentage increase in value settled was the largest annual increase since 2000/01; the increase for volume was the highest recorded since the commencement of RTGS in June 1998. The end of financial year on 30 June 2004 saw a daily volume of 35 512 transactions, a record for any single day.

Previous annual reports have discussed the introduction of the Continuous Linked Settlement (CLS) initiative to reduce foreign exchange settlement risk. To the extent that Australian dollar foreign exchange settlements take place across CLS Bank rather than direct gross payments across RITS, CLS was expected to reduce, over time, the number and value of transactions settled by RITS. To date, however, there has been no discernible impact on the continued growth of RITS settlements.

Graph 9

RTGS Transactions
Average daily value and number



In addition to RTGS payments, RITS settles two batches of netted interbank payments each day. The 9.00am batch consists of positions collated by the RBA on behalf of the Australian Payments Clearing Association arising from the previous day's "low value" clearings (paper, and bulk and retail electronic). The second batch settles net positions for equity transactions in CHES, the electronic settlement system operated by the Australian Stock Exchange.

RITS also provides a facility for members to participate in electronic tenders for Commonwealth Government securities (CGS). Since February 2002, settlement of successful tender bids has occurred in the Austraclear System, owned by SFE Corporation Limited.

The RBA is working on two major initiatives to improve the functionality provided by RITS to its ESA holders.

The first is the redevelopment of the user interface for on-line access to RITS, used for management of ESAs and RTGS payments, and for participating in CGS tenders (the latter facility is available to all members of RITS).

The objective is to provide a modern windows-based interface that will be simpler for users to learn and operate, provide improved access to account information and provide a better footing for future system development and support. At this stage, the RBA is planning for members to be able to use the new interface by around the middle of 2005.

The other major project under way is the development of improved facilities for the net settlement of batches of related low-value payments at any time during the main RITS business day. These batches could be submitted by any entity approved by the RBA to act as a batch administrator for a particular business stream. One potential use for this new facility, also expected to be available around the middle of 2005, is an initiative in various States to move towards electronic conveyancing and settlement of property transactions, to replace the current use of bank cheques.

Settlement services are also provided for financial market transactions undertaken by the RBA in the domestic securities and foreign exchange markets, and other transactions such as those relating to currency note lodgments and withdrawals. Settlement services are also provided for the Government for their high-value transactions including, for example, the settlement of tenders in CGS. Twenty-eight overseas central banks and official institutions have settlement and safe custody facilities through which the RBA settles their Australian dollar investment transactions.

Note Issue

The note issue functions include the issue and redemption of notes; the machine processing of notes returned from circulation for checking quality and authentication and the destruction of notes no longer fit for further use; organising the production of new notes; general oversight of cash distribution arrangements; and research into counterfeiting activity, new note designs and security features.

Notes on Issue

The value of Australian notes on issue rose by \$1.85 billion or 5.7 per cent over 2003/04 to \$34.0 billion. The increase occurred relatively evenly across all denominations, except the

Value of Notes on Issue (\$ million)									
At end June	\$1(a)	\$2(b)	\$5	\$10	\$20	\$50	\$100	Total	Increase (Per cent)
1998	19	47	361	617	1 804	9 523	9 280	21 651	7.9
1999	0(c)	46	379	639	1 850	10 356	10 282	23 552	8.8
2000	0(c)	46	397	646	1 917	11 188	11 240	25 434	8.0
2001	0(c)	45	431	662	2 014	12 055	11 961	27 168	6.8
2002	0(c)	45	530	791	2 789	14 718	13 057	31 930	17.5
2003	0(c)	45	515	759	2 510	14 918	13 426	32 173	0.8
2004	0(c)	0(c)	533	791	2 533	15 941	14 224	34 022	5.7

(a) Last issued May 1984
(b) Last issued June 1988
(c) See Notes To and Forming Part of the Financial Statements, Note 1(k)

\$20 which experienced a smaller increase than other denominations. Numbers of the higher denomination notes continued to grow somewhat more quickly in 2003/04 than the smaller denominations.

Note Processing

Centralised processing of redeemed notes is performed at the National Note Printing and Distribution Centre (NNPDC) at Craigieburn, Victoria. Armoured car companies transport notes to and from the NNPDC on behalf of the commercial banks. Under agreements between the RBA and the commercial banks, unfit notes, surplus fit notes (following seasonal peaks in demand), and notes requested by the RBA for quality sampling purposes are returned to the NNPDC. As surplus fit notes have already been sorted by banks, they are not resorted by the NNPDC. Commercial banks also draw notes from the NNPDC to meet demand when they cannot meet their requirements from their own holdings or by obtaining them from other banks with note surpluses. Notes that have been previously lodged by banks as surplus fit are used first in meeting banks' orders.

During 2003/04, 280 million notes (\$9 billion) were issued (despatched from the NNPDC) and 244 million (\$7 billion) were redeemed (returned to the NNPDC). This level of activity is some 32 per cent higher than the previous year.

Of the 280 million notes issued in 2003/04, 123 million were new notes and 157 million were previously circulated notes that were reissued after they had been returned to the NNPDC, processed and judged fit for reissue.

Of the 244 million notes returned to the NNPDC, 196 million notes were processed through high-speed note processing equipment for verification, authentication and quality control compared to 199 million notes processed during 2002/03. Notes deemed fit for reissue represented 47 per cent of notes processed compared to 41 per cent last year. The remaining 48 million notes were surplus fit notes returned to the NNPDC by commercial banks after Christmas or Easter.

Over the past couple of years, the RBA has noticed a decline in the quality of the lower denomination notes received in its sampling program. In order to improve the general quality of notes in circulation, new procedures have been developed with commercial banks and armoured car companies to improve note sorting standards and remove greater volumes of unfit notes from circulation for return to the NNPDC for destruction. As part of this process, commercial banks and armoured car companies have been provided with a revised version of the RBA's Note Sorting Guide.

The RBA has continued the process of evaluating a replacement for its high-speed note processing machines with new machines incorporating improved detectors to identify unfit notes. The new machines should enable a further expansion of the sampling program and better monitoring of compliance with sorting standards by commercial banks and armoured car companies.

The NNPDC also assesses the value of mutilated notes that are difficult for commercial banks to assess accurately and confirms the value of those assessed by commercial banks. During the year the NNPDC assessed 11 200 mutilated note claims with a total value of \$2.5 million. The volume of claims assessed was slightly higher than last year but the value was slightly less. During the year, a revised policy for mutilated notes was introduced. Among other changes, it is now necessary to have more than 80 per cent of a note to receive full value. If less than 20 per cent of a note is present (previously less than 50 per cent) no value is given. If between 20 and 80 per cent, value is paid on the percentage of the note present. The new policy is available on the RBA's website.

New Note Orders

The RBA ordered a total of 78 million new Australian notes in 2003/04 from Note Printing Australia. This was made up of 18 million \$5 notes, 9 million \$20 notes, and 51 million \$50 notes.

Distribution

Under arrangements for note and coin distribution introduced in November 2001, the commercial banks own the working stocks of notes and coin required to operate the cash distribution system and are encouraged to deal directly with each other to manage any short-term surplus or deficit in their holdings of currency. Under previous arrangements, the RBA owned the working stocks and commercial banks dealt directly with the RBA for their individual note and coin requirements.

During 2003/04, commercial bank holdings of working stocks were on average some \$370 million lower than during the previous year, due to increased efficiencies in cash management procedures.

The RBA pays commercial banks interest forgone on banks' working stocks of notes and coin up to a specified amount, provided the stocks are held in approved cash centres and notes are sorted for quality. The sorting standard is set and monitored by the RBA. As commercial banks gain more experience with these arrangements and further progress is made in developing

more efficient distribution and exchange arrangements between them, it is expected that working stock levels will continue to decline.

The RBA bears the cost of producing new notes, costs associated with the return of unfit and sampling notes, and the holding costs of the working stocks up to a specified limit. All other costs associated with the distribution of cash are met by others, including commercial banks, retailers and the public.

Counterfeiting Activity

Counterfeiting activity declined in 2003/04, with around five counterfeits passed per million notes in circulation, compared to around nine counterfeits per million in the previous year. Around 3 600 relatively low-quality counterfeits were passed, with a face value of about \$187 500. Much of the fall was attributable to a reduced level of counterfeiting of the \$50 note. However, the majority of counterfeits was still of the \$50 note; the remainder was largely \$100 counterfeits. Counterfeiting activity remains low and Australia's experience compares favourably with that of most other countries. Almost all counterfeits (95 per cent) were paper reproductions of polymer series notes, and were easily detected by visual inspection, as well as by feel.

Notwithstanding the low level of counterfeiting activity, the RBA has an active research and development program aimed at continually improving the security of polymer notes by using features that are not easily reproducible by technology available to counterfeiters.

Graph 10

Counterfeits Passed
Per million notes in circulation

