

Oversight of High-value Payments Systems

Reserve Bank Information and Transfer System

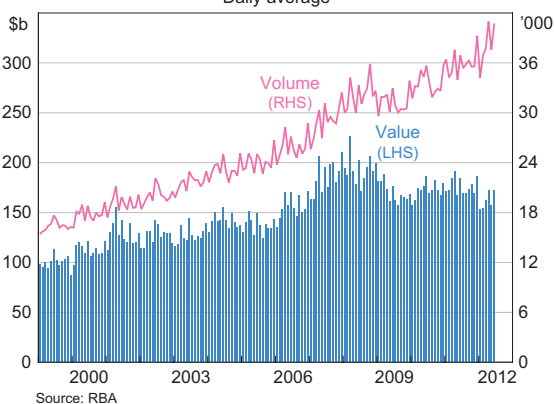
Australia's high-value payments system is the Reserve Bank Information and Transfer System (RITS), owned and operated by the Bank. RITS is a real-time gross settlement (RTGS) system that settles transactions on an individual basis, sequentially, in real time across Exchange Settlement Accounts (ESAs) held at the Bank. RITS also provides multilateral settlement functionality (where a number of linked payments settle simultaneously).

A key element of the Payments System Board's responsibility for the safety and stability of the payments system in Australia is oversight of RITS. An important part of this is for the Board to satisfy itself that RITS meets relevant international principles. To this end, the Reserve Bank periodically conducts self-assessments of RITS, which are subject to review by the Board, with any material changes occurring between assessments being reported to the Board. In April 2012, the Bank for International Settlements Committee on Payment and Settlement Systems (CPSS) and the Technical Committee of the International Organization of Securities Commissions (IOSCO) released *Principles for Financial Market Infrastructures* (the Principles). These update, harmonise and strengthen the pre-existing standards for payments, clearing and settlement systems, including the CPSS's *Core Principles for Systemically Important Payment Systems* against which self-assessments of RITS have to date been carried out. The Bank intends to adopt the Principles for future self-assessments, with a review planned in the calendar year 2013.

RTGS payments account for around 74 per cent of the value of total recorded payments in Australia.³¹ While the remaining 26 per cent of payments are settled on a deferred net basis, the interbank obligations arising from these payments are settled in RITS. Currently, this occurs in the daily 9.00 am batch. In 2011/12, the average size of this batch (i.e. the sum of credit and debit positions) was \$4 billion, slightly higher than in the previous year.

Prior to the global financial crisis, both the value and number of RTGS transactions settled in RITS grew steadily (Graph 18). Since 2007/08, the value of RTGS transactions has stabilised at a daily average of just over \$170 billion. In contrast, the number of

Graph 18
RTGS Transactions
Daily average

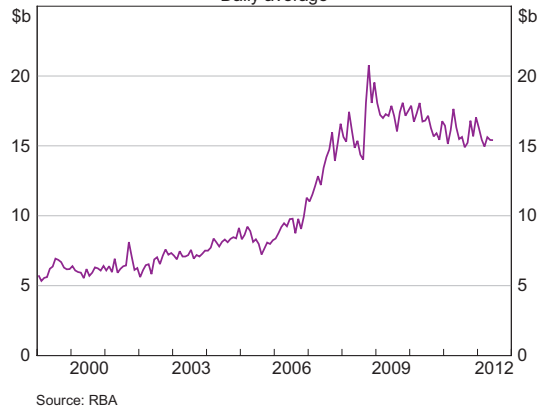


³¹ This measure of payments is broader than interbank settlements as it includes retail payments settled across the books of a commercial bank, such as payments between two customers of the same institution.

RTGS transactions have maintained a fairly steady growth rate of approximately 7 per cent per annum, interrupted only briefly in 2009/10. The decline in the average value of individual RITS transactions, from over \$6 million to around \$4.7 million, would seem to reflect a combination of factors, including a tightening of financial institutions' credit controls and the decline in asset prices.

Although the value of RTGS payments is a little below earlier peaks, liquidity in RITS – as measured by the sum of opening ESA balances and intraday repurchase agreements – remains substantially above pre-crisis levels (Graph 19). This has contributed to a greater proportion of transactions being settled earlier in the day. During the last three years, on average at least 50 per cent of payments by value have been settled by 1.30 pm, more than an hour earlier than in 2006/07.

Graph 19
Liquidity in RITS
Daily average



Exchange Settlement Accounts

The Board has ongoing responsibility for the Reserve Bank's policy on access to ESAs. These accounts provide a means for ultimate settlement of interbank obligations via the exchange of a settlement asset – a deposit held with the Bank – that carries no credit risk.

Under current policy, to be eligible to hold an ESA, an institution must be a provider of third-party (customer) payment services with a need to settle clearing obligations with other providers. An institution should also be able to demonstrate that it has the liquidity to meet its settlement obligations under routine conditions, during seasonal peaks and under periods of stress. In general, applicants must be current or prospective members of a payments clearing arrangement. At present, all banks that are licensed by the Australian Prudential Regulation Authority (APRA) are required to have an ESA. Other authorised deposit-taking institutions can apply to have an ESA under the general policy outlined above. However, any entity that accounts for 0.25 per cent or more of all RTGS payments must use its own ESA to settle its high-value transactions, whereas smaller entities may elect to settle using another ESA holder as an agent. A full list of ESA holders, which also includes a number of financial market infrastructures (FMI)s, is available on the Reserve Bank's website.³²

Shortly after the financial year under review, the Reserve Bank announced an amendment to its ESA policy creating a specific category of ESA for central counterparties (CCPs) for which Australian-licensed CCPs with Australian dollar obligations are eligible.³³ In addition, any Australian-licensed CCP determined by the Bank to be systemically important will be required to operate an ESA to assist in the management of its Australian dollar obligations. Australian-licensed securities settlement facilities with payment arrangements that require Australian dollar settlement are also eligible to hold an ESA.

³² Available at <<http://www.rba.gov.au/payments-system/rits/membership/membership-list.html>>.

³³ For more information, see RBA (2012), 'Payments System Issues: Exchange Settlement Account Policy for Central Counterparties', Media Release 2012-17, 31 July 2012. Available at <<http://www.rba.gov.au/media-releases/2012/mr-12-17.html>>.

An institution may be subject to collateral requirements as a condition of holding an ESA; this will typically depend on several factors, such as whether it is subject to supervision by APRA, the nature of its operations, and the extent of its payments experience.

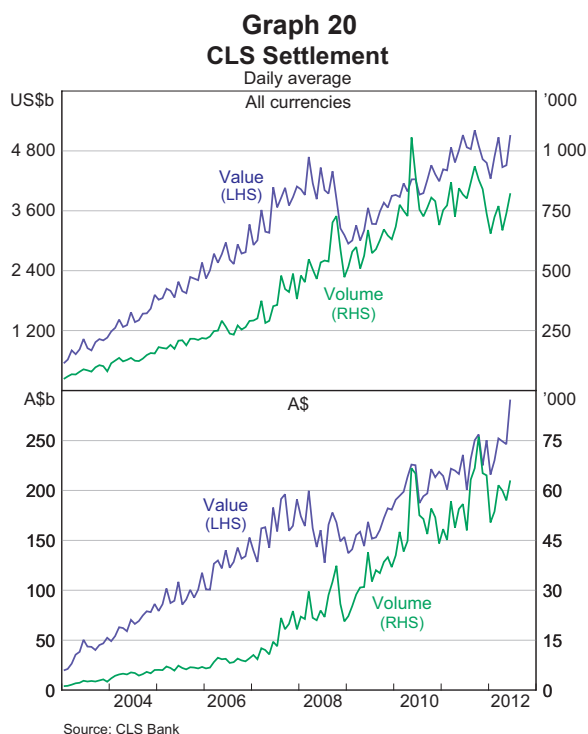
Oversight of Continuous Linked Settlement (CLS) Bank

CLS Bank (CLS) is primarily a settlement system for foreign exchange transactions that involve an exchange of currencies. Since CLS operates on a payment-versus-payment basis (PvP, i.e. settlement of one side of the transaction occurs simultaneously with the other), it eliminates the principal risk that would arise if one party settled its obligation while the other did not. CLS also settles some one-sided payments related to non-deliverable forwards and credit derivatives, and offers an aggregation service that compresses large volumes of low-value foreign exchange trades for settlement.³⁴

CLS is chartered in the United States and is regulated and supervised by the Federal Reserve System. The Federal Reserve also coordinates the CLS Oversight Committee, which provides for cooperative oversight by the central banks of issue of the currencies that settle in CLS. Currently, 17 currencies are eligible for settlement in CLS, including the Australian dollar.

The Reserve Bank is represented on the CLS Oversight Committee and through this contributes to discussions and assessment as to how well CLS meets the requirements of the relevant international principles – currently, the CPSS Core Principles for Systemically Important Payment Systems – including the ongoing adequacy and robustness of its risk controls, processes and settlement arrangements. Settlements in CLS give rise to significant flows in Australian dollars. Any potential disruption to these flows, or to its PvP arrangements, could have implications for the smooth functioning of RITS, and indeed the wider Australian financial system. Accordingly, CLS constitutes an important component of the Australian financial market infrastructure.

CLS settled an average of \$241 billion of foreign exchange transactions involving the Australian dollar per day in 2011/12 (bottom panel of Graph 20). These settle on a PvP basis across accounts in CLS. Under this process, settlement members either receive or pay a net settlement amount vis-à-vis CLS in each currency. Members meet any Australian dollar settlement obligation by paying into CLS’s ESA in RITS. These funds are then paid out to those settlement members with long positions in Australian dollars. The value of these payments in RITS is a fraction of the gross value of transactions involving the Australian dollar settled by CLS.



³⁴ The aggregation service works by bundling together into one transaction all buy sides and sell sides in a particular currency pair between two counterparties over an agreed period of time.

Having experienced an extended phase of growth due to the addition of new currencies, settlement members and services, as well as the progressive migration of settlements away from traditional settlement arrangements, CLS is now a relatively mature system. Across all currencies, the average daily value of foreign exchange trades settled in CLS in 2011/12 was US\$4.8 trillion.

Oversight of SWIFT

During the period, the Reserve Bank accepted an invitation to participate in a new cooperative oversight arrangement for SWIFT, a Belgian-headquartered member-owned cooperative that provides a communications platform and secure messaging standard to facilitate the global exchange of information on financial transactions. SWIFT messaging is employed by more than 9 500 financial institutions globally, including many financial market infrastructures such as RITS. Given the prominent role played by SWIFT, including in the domestic market, participation in this oversight arrangement was seen as an important complement to the Board's direct oversight of RITS.

To date, SWIFT has been overseen by a Cooperative Oversight Group chaired by the National Bank of Belgium (NBB) and comprising senior level central bank overseers from each of the G-10 countries. This Group oversees SWIFT on an ongoing basis against a set of High Level Expectations spanning risk identification and management; information security; reliability and resilience; technology planning; and communication with users.

In part, in response to the increasing economic influence of countries outside of the G-10, the NBB has sought to broaden the reach of its oversight framework by establishing an additional tier to its structure. This new tier – the SWIFT Oversight Forum – comprises representatives from 25 central banks and monetary authorities, plus the chair of the CPSS secretariat. A key function of the SWIFT Oversight Forum will be to facilitate the sharing of oversight information relevant to this broader group of stakeholders by both the existing G-10 Oversight Group and SWIFT. It is anticipated that the Forum will meet in person once a year, with ad hoc meetings organised as necessary and occasional conference calls. The SWIFT Oversight Forum met for the first time in May 2012.