

Oversight of High-value Payment Systems

A key element of the Payments System Board's responsibility for the safety and stability of payment systems in Australia is the oversight of systemically important payment systems.

In November 2013, this role was described in detail in the *Self-assessment of the Reserve Bank of Australia – Systemically Important Payment Systems*.¹² This report assesses how the Bank meets international expectations for regulatory authorities set by the Committee on Payment and Settlement Systems (CPSS; recently renamed the Committee on Payments and Market Infrastructures (CPMI))¹³ and the International Organization of Securities Commissions (IOSCO) as part of the *Principles for Financial Market Infrastructures* (PFMIs).¹⁴

To date, the Reserve Bank Information and Transfer System (RITS) and CLS Bank International (CLS) are the only payment systems identified by the Bank as warranting oversight as systemically important systems. This reflects the fact that the majority of Australian dollar-denominated (AUD) payments, by value, are settled in these two systems and that both systems primarily settle high-value or time-critical payments (Table 8). RITS is also used to effect interbank AUD settlements arising in retail payment systems and other financial market infrastructures (FMIs), including AUD payments to CLS. The Bank has also identified SWIFT as a provider of critical services to both RITS and CLS, since both systems depend on SWIFT's communications platform and other services to process payments and exchange information with their participants. SWIFT also provides critical services to other FMIs and many other market participants.

In the report, the Bank concluded that it observed all relevant responsibilities. However, in the spirit of continuous improvement, the Bank identified some specific actions to further enhance its oversight. In particular, the Bank committed to: continuing to monitor developments in the payments landscape periodically to consider whether any other payment systems should also be subject to ongoing oversight and assessments against the international standards; and considering additional mechanisms to enhance coordination and consistency in its oversight of FMIs, which have since been implemented (see 'FMI Oversight Committee' under 'Oversight of Clearing and Settlement Facilities').

12 RBA (2013) *Self-assessment of the Reserve Bank of Australia – Systemically Important Payment Systems*, available at <<http://www.rba.gov.au/payments-system/policy-framework/principles-fmi/assessments/systemically-important/2013/pdf/2013-self-assess-sys-imp-pay-sys.pdf>>.

13 The change in name, which took effect on 1 September, reflects the evolution of the Committee's work since it was established in 1990. It reflects, in particular, the gradual shift in emphasis from payments issues towards clearing and settlement issues. The CPMI has issued a refreshed Mandate and Charter which highlight its role in promoting the safety and efficiency of payment, clearing and settlement arrangements, fostering central bank cooperation in related matters, and setting standards.

14 The international expectations are set out in the Responsibilities of Central Banks, Market Regulators, and other Relevant Authorities for Financial Market Infrastructures that form part of the PFMIs, available at <<http://www.bis.org/publ/cpss101a.pdf>>.

Table 8: Payments in Australia
2013/14, daily averages^(a)

	Number ^(b) '000s	Value ^(b) \$ billion	Growth since 2012/13 Per cent	Interbank settlement value in RITS \$ billion
Domestic				
RITS	42	162.7	3.1	162.7
<i>SWIFT payments (HVCS)</i>	38.7	100.5	3.5	100.5
<i>Debt securities (Austraclear)^(c)</i>	3.1	50.3	3.8	50.3
<i>RITS cash transfers</i>	0.2	11.9	-3.6	11.9
Retail payment systems	34 816.3	62.9	5.5	2.9 ^(d)
Equity settlements	718.8	4.0 ^(e)	-3.9	0.5
International				
CLS	56.8	246.2	-2.2	2.2

(a) Business days

(b) Includes payments between customers of the same financial institution

(c) Excludes intraday and open RBA repurchase agreements, and multilaterally netted interbank settlements arising from the retail payment systems and the equity market

(d) Average prior to (post) the implementation same-day settlement of direct entry payments was \$1.9 billion (\$3.6 billion)

(e) Gross value of equity trades

Sources: ASX; CLS; RBA

Reserve Bank Information and Transfer System

RITS is primarily a real-time gross settlement system, which settles transactions on an individual basis in real time across Exchange Settlement Accounts (ESAs) held at the Bank.¹⁵ RITS is owned and operated by the Reserve Bank.

Self-assessment against international standards

As part of its oversight of RITS, the Bank periodically conducts self-assessments of RITS against relevant international standards. These self-assessments are reviewed by the Payments System Board and published on the Bank's website. Following the finalisation of the PFMs in April 2012, the Bank announced that from 2013 it would conduct self-assessments of RITS against the principles within the PFMs (the Principles) on an annual basis.

In the first of these self-assessments, published in December 2013, the Bank concluded that RITS observed all of the relevant Principles.¹⁶ Nevertheless, the Bank noted a number of existing plans, the completion of which would further enhance RITS's compliance with the Principles. Two of these actions have since been completed. In June 2014, the Bank successfully upgraded RITS's core infrastructure and, in December 2013, enhancements to network monitoring were implemented.

In the self-assessment, the Bank also reiterated its commitment to monitor RITS participants' compliance with new business continuity standards, which set minimum standards for participants in the area of business continuity planning, system resilience, incident management, testing and recovery time frames. These standards, introduced in May 2013, acknowledge that, while the Bank devotes significant operational and financial resources to ensuring the resilience of RITS, the efficient operation of RITS is also dependent on the operational reliability of RITS participants. All participants are expected to fully comply with the new standards by September 2015.

¹⁵ The Board has responsibility for the Bank's policy on access to ESAs. This policy is available at <<http://www.rba.gov.au/payments-system/esa/>>.

¹⁶ The 2013 *Self-assessment of the Reserve Bank Information and Transfer System* is available at <<http://www.rba.gov.au/payments-system/rits/self-assessments/2013/index.html>>.

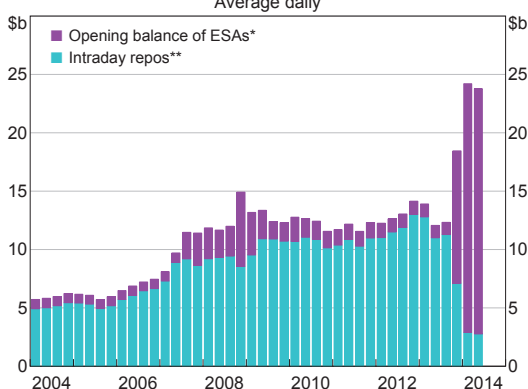
Additionally, the Bank has committed to conducting a comprehensive review of the regulations that govern participation in RITS, with the aim of identifying any areas in which the clarity of these regulations could usefully be improved. Finally, the Bank will review any supplementary guidance that may be issued in the future by the CPMI and IOSCO on quantitative disclosure requirements for payment systems.

Open repos and same-day settlement of direct entry

The Board maintains a keen interest in material changes to the operational arrangements for RITS. One such recent change was the change to liquidity arrangements required to accommodate the settlement of direct entry (DE) obligations exchanged after the interbank cash market has closed. As discussed in the ‘Strategic Review of Innovation’ chapter, the same-day settlement of obligations arising from DE payments – the largest component, by value, of retail payments – commenced in November 2013.¹⁷ Since participants do not know the size of their net DE obligations (which can be quite large relative to end-of-day ESA balances) prior to the close of the interbank cash market, the Bank has increased the amount of overnight liquidity provided to participants, from around \$1 billion to around \$21 billion to ensure that after-hours DE obligations are able to settle without active liquidity management by participants. The new liquidity arrangements were introduced in November 2013, ahead of the introduction of same-day settlement of DE. The Bank provides this additional liquidity through repurchase agreements with no specified maturity (open repos). These are capped at a predetermined amount for each DE participant.

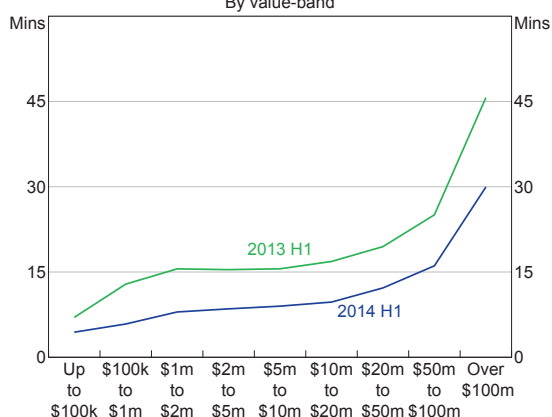
The introduction of open repos has resulted in a significant increase in the average intraday liquidity available in RITS, from \$13 billion in the first half of 2013 to \$24 billion in the first half of 2014 (Graph 13). As well as facilitating the settlement of evening DE payments, the additional liquidity has resulted in earlier settlement of payment instructions submitted to RITS. Since the introduction of the new arrangements, the average length of time a payment instruction has been held on the queue awaiting settlement has declined from 46 minutes to 30 minutes (for submitted payments over \$100 million) (Graph 14).

Graph 13
Liquidity in RITS



* Includes open repos
** Average value of intraday repos during the daily settlement session
Source: RBA

Graph 14
RITS Payments Time to Settle*



* Average time payments eligible for settlement spend on the queue; does not include interbank settlements arising from retail payment systems or the equity market
Source: RBA

17 For more detail on the implementation of same-day settlement of DE payments, see Fraser S and A Gatty (2014), ‘The Introduction of Same-day Settlement of Direct Entry Obligations in Australia’, RBA Bulletin, June, pp 55–64.

Property settlements

Another material operational change to RITS will be required to facilitate the settlement of the cash leg of property transactions settled through the national electronic conveyancing system being developed by Property Exchange Australia Ltd (PEXA). PEXA aims to remove the manual processes and paperwork associated with the exchange of property by allowing land registries, financial institutions, solicitors and conveyancers, and other industry participants to transact on an electronic platform. In parallel with this, the Bank is developing functionality in RITS to receive and settle payment instructions originating from PEXA. Settling the cash leg of property transactions in RITS reduces reliance on less efficient payment methods such as bank cheques. The functionality is expected to be available by November 2014, to coincide with the deployment of PEXA transfer and settlement functionality in New South Wales and Victoria.¹⁸

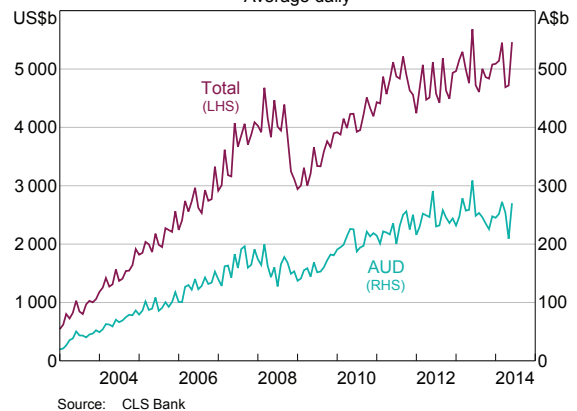
CLS Bank

CLS is an international payment system for settling foreign exchange trades in 17 currencies, including the Australian dollar. By operating a payment-versus-payment settlement mechanism, CLS allows participants to mitigate foreign exchange settlement risk (the risk that one party settles its obligation in one currency, but its counterparty subsequently does not settle its obligation in the other currency). As Graph 15 demonstrates, CLS settles a significant value of Australian dollar-denominated foreign exchange-related payments. Consequently, the Bank has identified CLS as a systemically important international payment system. In CLS, settlement members either receive or pay a net amount vis-à-vis CLS in each currency. These net amounts are settled in RITS and are typically around 1 per cent of the gross value of Australian dollar trades settled in CLS.

CLS is regulated, supervised and overseen by the Federal Reserve, in cooperation with an Oversight Committee that includes the Reserve Bank and the other issuing central banks of CLS-settled currencies. Through this forum, the Bank is involved in overseeing how well CLS meets relevant international standards.

The Oversight Committee has monitored closely a number of developments in CLS during 2013/14. CLS is currently finalising a self-assessment of its practices against the Principles. In part to meet new capital requirements in the Principles, CLS raised an additional £160 million in equity capital in late 2013. CLS is also examining options to further enhance its liquidity risk management. At the same time, CLS continues to develop its service offering. In September 2013 CLS launched a same-day settlement service to facilitate the settlement of certain payments that are required to be settled on a same-day basis. Previously, these payments were unable to be settled by CLS due to restrictions in the hours it accepts settlement instructions. Currently the service is available in the United States and Canada for the USD/CAD currency pair. CLS is working with its participants to explore the feasibility of establishing similar arrangements in other geographical regions.

Graph 15
CLS Settlement Value
Average daily



¹⁸ This is the second stage of the PEXA release schedule. In the first stage, PEXA has facilitated certain transactions, such as mortgage discharges and refinancing transactions, to be conducted on its system. This stage has been in operation since June 2013.

Finally, CLS is progressing ongoing projects to develop a settlement solution for centrally-cleared foreign exchange products and to expand the range of currencies it settles.

SWIFT

The Bank also participates in the international cooperative oversight of SWIFT, a member-owned cooperative company registered in Belgium that, amongst other services, provides communications services to facilitate the transfer of payment and other information between participants in the financial system. While SWIFT is not a payment system, it provides critical services to both RITS and CLS, as well as other FMIs and market participants.

SWIFT is primarily overseen by the SWIFT Oversight Group (OG), a cooperative body comprising the G10 central banks and chaired by the National Bank of Belgium (NBB). In 2012, the NBB set up the SWIFT Oversight Forum to provide information on SWIFT to a broader group of central banks, including the Bank, and to give these central banks an opportunity to provide input into the setting of the OG's oversight priorities. Oversight of SWIFT is supported by a set of standards – the High-level Expectations – which are consistent with standards for critical service providers in the PFMLs. One of the focuses of the OG in 2013 was a major review of the functioning of SWIFT's governance arrangements. The OG has also increased its monitoring of cyber security initiatives at SWIFT.

SWIFT's recent activities include two substantial multi-year projects. Its 'distributed architecture' project aims to further enhance the security, resilience and reliability of SWIFT's services, including through the implementation of regional processing zones, a new European operating centre, and additional disaster recovery arrangements. A separate 'FIN-renewal' project aims to refresh the technology underpinning SWIFT's main messaging service, FIN. The distributed architecture project was successfully completed in 2014 and the FIN renewal project will extend into 2016.

