

Oversight of High-value Payment Systems

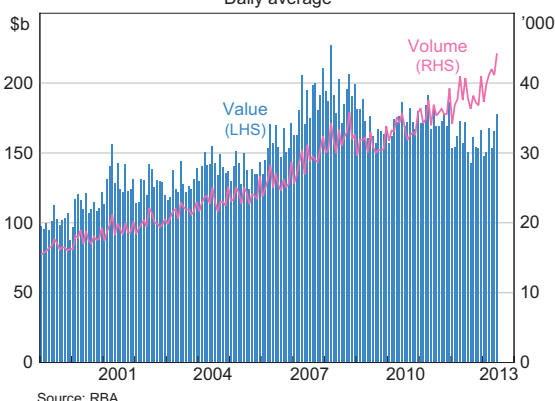
Reserve Bank Information and Transfer System

A key element of the Payments System Board's responsibility for the safety and stability of payment systems in Australia is oversight of the Reserve Bank Information and Transfer System (RITS). RITS is primarily a real-time gross settlement (RTGS) system, which settles transactions on an individual basis in real time across Exchange Settlement Accounts (ESAs) held at the Bank. Consistent with RITS being the principal domestic payment system in Australia, around 70 per cent of the value of non-cash payments in Australia is settled on an RTGS basis in RITS.²² In 2012/13, an average of over 39 000 RTGS transactions were settled each day, with an aggregate daily value of around \$158 billion (Graph 14). Since the global financial crisis, the volume of RTGS transactions has continued to grow steadily, while the value has remained fairly stable.

The interbank obligations arising from the remaining 30 per cent of non-cash payments are also settled in RITS, but on a deferred net basis. Currently, this occurs in a batch settlement process at 9.00 am on the next business day after a payment is made. As discussed in the context of the Strategic Review of Innovation in the Payments System, by the end of 2013 it is expected that arrangements will be in place to settle Direct Entry (DE) payments – the largest component of the current 9.00 am batch settlement – on a same-day basis.

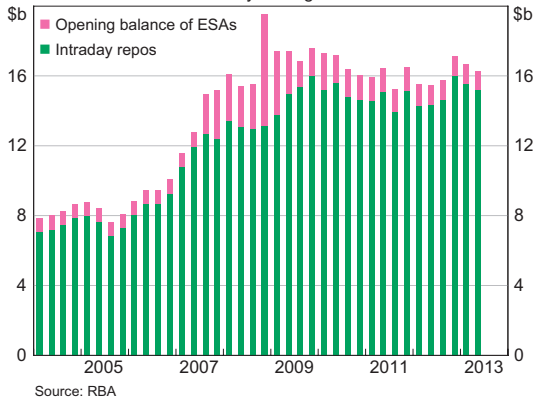
At present, liquidity in RITS is sourced from overnight balances in participants' ESA and interest-free intraday repurchase agreements (repos). However, the proposed same-day settlement of DE payments will require settlement late in the day, after intraday repos have been unwound and the interbank cash market has closed. To facilitate same-day settlement, from November 2013, ESA holders will be able to engage in repos on an 'open' basis; that is, without a maturity date. To ensure RITS participants are not penalised for holding higher overnight balances for this purpose, the Bank has made arrangements to pay RITS participants the target cash rate on a proportion of their balances (rather than 25 basis points below the target cash rate for overnight ESA balances at present). In aggregate, it is anticipated that ESA holders will hold open repos of between

Graph 14
RTGS Transactions
Daily average



²² This measure of payments is broader than interbank settlements, since it includes retail payments settled across the books of a commercial bank, such as payments between two customers of the same institution.

Graph 15
Liquidity in RITS
Daily average



\$20 and \$30 billion, which is substantially above existing liquidity levels (Graph 15).²³ The overall effect of these changes may be to facilitate earlier settlement of other transactions in RITS.

As part of its oversight of RITS, the Reserve Bank conducts periodic self-assessments of RITS against the relevant international standards. Following the finalisation of the Committee on Payment and Settlement Systems (CPSS) and the International Organization of Securities Commissions (IOSCO) *Principles for Financial Market Infrastructures* (the Principles) in April 2012, the Bank announced that from 2013 it will conduct self-assessments of RITS against the Principles on an annual basis.²⁴ These

self-assessments are reviewed by the Payments System Board and published on the Bank's website. The Board also reviews any material developments occurring between assessments.

As part of this ongoing oversight process, the Board was briefed on the details of the 14 September 2012 operational incident, during which members' access to RITS was disrupted for around 50 minutes. This outage resulted in RITS availability falling to 99.948 per cent in 2012, the first time it has fallen below the target of 99.95 per cent in 5 years. In response to internal and external reviews of the circumstances surrounding the outage, the Bank has refined its incident management procedures.

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. To ensure RITS participants manage their operational risk effectively, the Bank recently introduced business continuity standards for RITS members. These complement existing Australian Payments Clearing Association (APCA) and Australian Prudential Regulation Authority (APRA) standards. The standards cover business continuity planning, system resilience, incident management, recovery time frames and testing. RITS members were required to complete their initial self-assessments against the standards by July 2013.

CLS Bank

Continuous Linked Settlement (CLS) provides a mechanism for settling foreign exchange transactions in 17 currencies, including the Australian dollar. These transactions are settled on a payment-versus-payment (PvP) basis, thereby eliminating foreign exchange settlement risk (the risk that one party settles its obligation, while the other subsequently does not). Members meet any Australian dollar settlement obligation by making payments into a CLS's ESA via 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 small fraction of the gross value of transactions involving the Australian dollar settled by CLS. CLS also settles some one-sided payments related

²³ These arrangements were discussed in Debelle G (2013), 'The Impact of Payments System and Prudential Reforms on the RBA's Provision of Liquidity', Address to the Australian Financial Markets Association and Reserve Bank of Australia Briefing, 16 August. Available at <<http://www.rba.gov.au/speeches/2013/sp-ag-160813.html>>.

²⁴ *Implementing the CPSS-IOSCO Principles for Financial Market Infrastructures in Australia*, available at <<http://www.rba.gov.au/payments-system/policy-framework/principles-fmi/implementing-principles-australia.html>>. See also CPSS-IOSCO (2012), *Principles for Financial Market Infrastructures*, available at <<http://www.bis.org/publ/cpss101a.pdf>>.

to non-deliverable forwards and credit derivatives, and offers an aggregation service that compresses large volumes of low-value foreign exchange transactions for settlement.

Across all currencies, CLS settled US\$4.8 trillion on average each day in 2012/13 (Graph 16, top panel). This figure includes an average of \$247 billion of foreign exchange transactions involving the Australian dollar per day in 2012/13 (Graph 16, bottom panel). Because of the large value of Australian dollar settlements in CLS, any disruption to CLS or members' payments to CLS could have implications for the smooth functioning of RITS, and indeed the wider Australian financial system.

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 in the currencies that settle in CLS. As a member of the Oversight Committee, the Bank is

able to contribute to the assessment of the ongoing adequacy and robustness of CLS's risk controls, and its processes and settlement arrangements. In addition, through this forum the Bank is involved in overseeing how well CLS meets the requirements of the relevant international principles, against which CLS is required to submit annual self-assessments.

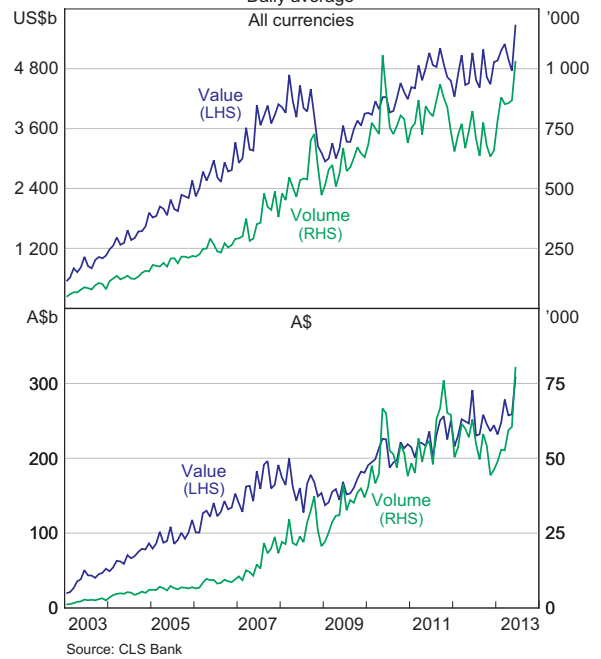
The Oversight Committee has also kept a close watch on developments in the CLS system over 2012/13. These include: the development of a same-day settlement service across a limited number of jurisdictions (currently not including Australia); continued expansion of the range of currencies settled via CLS; and efforts to assist in the settlement of foreign exchange transactions cleared by central counterparties (CCPs).

SWIFT

While the Society for Worldwide Interbank Financial Telecommunication (SWIFT) is not a payment system, many systemically important payment systems depend on SWIFT's communications platform and other services. In Australia, SWIFT is a core component for communication between important payment and settlement systems (i.e. RITS, CLS, the Low Value Settlement Service (LVSS) and Austraclear) and those systems' participants.

SWIFT is a member-owned cooperative company, which is chartered in Belgium and is primarily overseen by the SWIFT Oversight Group (OG), comprising the G10 central banks and chaired by the National Bank of Belgium. In 2012, the OG set up the SWIFT Oversight Forum (SOF) to include additional central banks, including the Reserve Bank, in the oversight process. Through its membership of the SOF, the Bank is able to contribute to discussions on oversight priorities and policies. In addition, the SOF facilitates information sharing about SWIFT oversight and considers system interdependencies arising from the common use of SWIFT.

Graph 16
CLS Settlement
Daily average



Source: CLS Bank

To support its oversight activities, the OG has set proprietary minimum standards – the High-level Expectations (HLEs) – against which SWIFT is assessed. In its capacity as a member of the SOF, the Bank receives SWIFT’s annual self-assessment against the HLEs. SWIFT also has a number of strategic projects underway, including the construction of a third operating centre and a technology refresh of its main messaging service, FIN. The OG monitors closely these projects to ensure that they do not adversely affect SWIFT’s core services, and keeps SOF members updated on its work in this area.

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.

In July 2012, the Bank announced the creation of a specific category of ESA for which Australian-licensed CCPs with Australian dollar obligations are eligible.²⁵ At the same time, the Bank took the opportunity to consolidate its policy statements on ESA eligibility into a single statement.²⁶ This statement clarifies that the following types of institutions may hold an ESA:

- an authorised deposit-taking institution (ADI) or other institution that is an actual or prospective provider of third-party (customer) payment services with a need to settle clearing obligations with other providers
- an Australian-licensed CCP or securities settlement facility (SSF) (or a related body corporate acceptable to the Bank) with payment arrangements that require Australian dollar settlement.

The statement further clarifies that all banks licensed by APRA are required to have an ESA, and that any Australian-licensed CCP determined by the Bank to be systemically important is required to settle its Australian dollar margin and other securities- and derivatives-related obligations using its own ESA. Any entity that accounts for 0.25 per cent or more of the value of total 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 is available on the Bank’s website.²⁷

In addition to meeting the eligibility requirements listed above, any institution applying for an ESA must be able to demonstrate that it has access to sufficient liquidity to meet its settlement obligations under routine conditions, during seasonal peaks and under periods of stress. Depending on whether it is subject to supervision by APRA, the nature of its operations and the extent of its payments experience, collateral requirements may be imposed on an ESA holder.

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

26 The statement on ESA policy is available at <<http://www.rba.gov.au/payments-system/esa/index.html>>.

27 The full list of ESA holders is available at <<http://www.rba.gov.au/payments-system/rits/membership/membership-list.html>>.