Reserve Bank of Australia Corporate Plan

2016/17

1. Introduction

This corporate plan is prepared for 2016/17 in accordance with section 35(1)(b) of the *Public Governance, Performance and Accountability Act 2013* and also covers the reporting periods from 1 July 2017 to 30 June 2020.

The accountable authority of the Reserve Bank is the Governor.

This corporate plan outlines the key functions and purposes of the Bank and, in relation to each of those functions and purposes, sets out:

- the Bank's assessment of the relevant environment in which those functions and purposes will be carried out
- how the Bank plans to achieve the relevant purposes and how it will measure and assess its performance in the achievement of those purposes
- the key strategies and plans that the Bank proposes to implement with a view to achieving the relevant purposes.

The plan also outlines the purposes and performance measures in relation to the Bank's financial position. The penultimate section of the plan outlines the Bank's approach to managing and overseeing the main risks it faces, including a reference to the Bank's published *Risk Appetite Statement*, which also indicates the Bank's attitude towards its key strategic, financial, people and operational risks. A final section highlights the important role that other factors play in the Bank achieving its various functions and purposes, including in particular its high-quality staff, in which the Bank invests heavily, the information technology underpinning its activities, as well as a range of support services provided by other areas of the Bank.

2. Monetary Policy

2.1 Purpose

It is the duty of the Reserve Bank Board to ensure that the monetary and banking policy of the Bank is directed to the greatest advantage of the people of Australia and that the powers of the Bank are exercised in a way that, in the Board's opinion, will best contribute to:

(a) the stability of the currency of Australia;

(b) the maintenance of full employment in Australia; and

(c) the economic prosperity and welfare of the people of Australia.

In support of the above duties, the most recent *Statement on the Conduct of Monetary Policy* between the Treasurer and the Governor, dated 24 October 2013, confirms the Bank's continuing commitment to keeping consumer price inflation between 2 and 3 per cent, on average, over the cycle, consistent with its duties under the *Reserve Bank Act 1959*. Ensuring low and stable inflation preserves the value of money and facilitates strong and sustainable growth in the economy over the longer term. Low inflation assists businesses and households in making sound investment decisions and underpins the creation of jobs, protects the savings of Australians and preserves the purchasing power of money. The *Statement on the Conduct of Monetary Policy* also recognises the importance of financial stability for a stable macroeconomic environment.

2.2 Environment

There have been considerable challenges in the conduct of monetary policy globally. There is no reason to expect that this will not remain the case over the years ahead. The global environment remains uncertain and the nature of the global economy is invariably changing. Global interest rates are extremely low at present and inflation is generally subdued. Both are likely to rise at some point, but there is significant uncertainty around when and by how much this is likely to occur. Globally, the current persistent period of highly accommodative monetary policies is unprecedented. These global influences partly condition the environment in which monetary policy in Australia is conducted.

The structure of the Australian economy is likely to continue to change and economic shocks – which, by definition, are not forecastable – are likely to occur. Movements in asset values and leverage may be more important for the economy than previously and different policies may be more or less able to sustain growth. With interest rates in Australia already low, and a good deal of debt already on household balance sheets, the trade-offs for monetary policy have become more complex. On the one hand, policymakers are wary of fostering a further substantial build-up in debt. At the same time, high debt levels mean that monetary policy's ability to stimulate growth in the short term may be more limited than in the past. While domestic cost pressures are subdued, inflation is forecast to increase gradually and remain consistent with the medium-term inflation target. The risks around the Bank's inflation forecasts are assessed to be balanced.

2.3 Performance

The Reserve Bank will seek to ensure that monetary policy is appropriately configured, by means of the level of the overnight cash rate in the domestic money market, to produce inflation outcomes in Australia that are consistent with the inflation target of between 2 and 3 per cent, on average, over the cycle, which allows the Bank to foster sustainable economic growth and financial stability. Assessing performance on inflation is relatively straightforward – inflation outcomes in 2016/17 and subsequent years will be measured by annual percentage changes in the consumer price index and assessed in the context of achieving inflation between 2 and 3 per cent on average over the medium term. As always, it may be necessary to allow for one-off effects on prices arising from government policies and economic shocks.

It is less straightforward to assess the extent to which the Bank has succeeded in fostering sustainable growth in the economy, partly because the levels of output and unemployment that are consistent with stable inflation and maintaining financial stability risks at manageable levels cannot be directly observed and must be inferred from other data. Over the short term, monetary policy can affect cyclical deviations of output and unemployment from their equilibrium levels, but over the long term, the Bank's contribution to sustainable growth will mainly come through preserving low inflation and financial stability. The assessment of financial stability is discussed in section 3.3.

Assessing the conduct of monetary policy will, as always, involve judging whether the policy decisions taken were prudent and consistent with the objectives of monetary policy, based on the information available at the time.

2.4 Capability

The flexible inflation target is the centrepiece of the monetary policy framework in Australia and has been well established for more than two decades. It has provided the foundation for the Reserve Bank to achieve its monetary policy objectives by providing an anchor for inflation expectations. The Bank will remain alert to new developments that may have a bearing on the framework for monetary policy. It will continue to pursue and monitor relevant research and evaluate overseas experience, engaging with other relevant public institutions and the academic community, both domestically and internationally. The Bank will also continue to carefully communicate its views on relevant economic developments, the economic outlook and monetary policy decisions.

3. Financial Stability

3.1 Purpose

The Reserve Bank's responsibility for fostering overall financial stability rests on the duties noted in section 2.1 above requiring that the powers of the Bank are exercised in a way that will best contribute to 'the maintenance of full employment in Australia' and 'the economic prosperity and welfare of the people of Australia'. Given the serious damage to employment and economic prosperity that can occur in times of financial instability, the *Reserve Bank Act 1959* has long been interpreted to imply a mandate to pursue financial stability. This implicit goal has been made more explicit by successive governments. In 1998, the then Treasurer explicitly referred to financial stability being the regulatory focus for the Bank in the Second Reading Speech in support of the *Australian Prudential Regulation Authority Act 1998*. More recently, the Treasurer and the Governor recorded their common understanding of the Bank's longstanding responsibility for financial system stability, as part of the periodically updated *Statement on the Conduct of Monetary Policy*.

The Bank works with other regulatory bodies in Australia to foster financial stability. The Governor chairs the Council of Financial Regulators (CFR) – comprising the Bank, Australian Prudential Regulation Authority (APRA), Australian Securities and Investments Commission (ASIC) and Australian Treasury – whose role is to contribute to the efficiency and effectiveness of regulation and the stability of the financial system. The Bank's responsibility to promote financial stability does not, however, equate to a guarantee of solvency for financial institutions, nor is its balance sheet available to support insolvent institutions. Nevertheless, the Bank's central position in the financial system – and its position as the ultimate provider of liquidity to the system – gives it a key role in financial crisis management, in conjunction with the other members of the CFR.

3.2 Environment

Financial stability in Australia has been assisted by the sustained strong financial performance of the domestic banking system. Australian banks have improved their resilience to future financial and economic shocks by increasing their capital ratios, as well as strengthening their lending standards, particularly for their mortgage business. But some of the factors that have helped increase banks' profits in recent years, such as the downward trend in credit losses, may not persist and, internationally, there is a trend to higher capital requirements. The global financial environment may change in unpredictable ways over the next four years. The financial system is also facing a period of significant regulatory change, both domestically and abroad. In addition, risks to financial stability will continue to evolve in ways that may not easily be predicted.

3.3 Performance

The ultimate test of performance in financial stability policy remains the stability of the financial system itself as it performs its proper functions. The Reserve Bank will use its powers, influence and communications to ensure so far as possible that the Australian financial system remains stable. This entails the assessment and, together with the other CFR agencies, management of domestic sources of systemic risk, as well as enhancing the resilience of the financial system to any shocks that might come from abroad. The Bank's liquidity operations would be available as needed, but most of the tools that bear directly on financial stability outcomes are under the control of other agencies. The Bank also contributes to financial stability in Australia through its published assessments, especially the half-yearly *Financial Stability Review*, and through its role on the CFR and in various international regulatory bodies, including the Financial Stability Board (FSB), the Basel Committee on Banking Supervision (BCBS) and the Trans-Tasman Council on Banking Supervision.

3.4 Capability

The Reserve Bank will continue to devote appropriate resources to the processes of identifying and assessing risks to financial stability and engaging on these matters through international groups such as the FSB, BCBS and the Bank for International Settlements.

The Bank will also work with the other CFR agencies on financial stability related matters. These include conducting domestic (2016/17) and trans-Tasman (2017/18) crisis simulation exercises, and beginning initial preparations ahead of the next Financial Sector Assessment Program review of Australia by the International Monetary Fund. The Bank expects to continue working with other regulators to assess and contain risks that may arise from the domestic housing and other property markets.

4. Financial Market Operations

4.1 Purpose

The Reserve Bank has a sizeable balance sheet, which is managed in support of the Bank's policy objectives. Part of the balance sheet is used to ensure that there is sufficient liquidity in the domestic money market on a daily basis. This promotes the stable functioning of the financial system, in particular the payments system, and the objectives of monetary policy. The Bank's regular transactions in the foreign exchange market are conducted to manage Australia's foreign currency reserves, which are held on the balance sheet of the Bank, and also to provide foreign exchange services to the Bank's clients, the largest of which is the Australian Government.[1] On occasion, the Bank may intervene in the foreign exchange market, consistent with the objectives of monetary policy.

4.2 Environment

The general model that the Reserve Bank uses to implement monetary policy is well established and understood by market participants. The present nature of the Bank's financial market operations continues to be influenced by the regulatory regimes that are imposed on financial markets in which the Bank transacts and/or the counterparties with which it deals, both domestically and internationally. With these regulations undergoing a period of substantial reform, market functioning and structure is evolving significantly and this is likely to continue. The Bank is adapting its processes accordingly. The historically extremely low level of global interest rates has provided challenges for the Bank in managing its holdings of foreign reserves and this is likely to remain the case for some time to come.

4.3 Performance

The Reserve Bank's operations in financial markets support its monetary policy objectives through the specification of an operational target for the overnight cash rate in the domestic money market, which is a decision of the Reserve Bank Board. When supplying liquidity to the domestic money market, the Bank seeks to ensure that the overnight cash rate is maintained at the prevailing cash rate target each day. The Bank collects information on each participant's activity in the money market in order to make this assessment and it publishes the outcome daily.

The Bank manages its foreign reserves portfolio relative to a benchmark. Managers' discretionary positions are limited. A measure of performance in managing the portfolio is provided by the close adherence to the asset and duration benchmarks.

4.4 Capability

The Reserve Bank's ability to manage 'system liquidity' is based on its capacity to lend cash to, or withdraw cash from, the interbank settlement system. It does this by undertaking transactions on behalf of the Bank's customers and/or transacting with other financial institutions. The Bank will continue to adjust its systems for domestic market operations to cater for extended hours and out-of-hours liquidity provision. It is in the process of undertaking a periodic upgrade to its trading system for both its domestic and foreign operations. The Bank will continue to evaluate its domestic market operations framework and make any adjustments necessary to address 24/7 processing of payments through the New Payments Platform.

1 Section 8 covers the Bank's financial position and capital, and outlines the effect of the Bank's operations on its profits and capital.

5. Payments and Infrastructure

5.1 Purpose

There are several distinct aspects to the Reserve Bank's role in the payments system, involving those of policymaker, overseer and supervisor, and owner and operator of key national payments infrastructure.

In relation to the policymaking role, it is the duty of the Payments System Board to ensure that the Bank's payments system policy is directed to the greatest advantage of the people of Australia, to ensure that the powers of the Bank under the *Payment Systems (Regulation) Act 1998* and the *Payment Systems and Netting Act 1998* are exercised in a way that, in the Board's opinion, will best contribute to:

(a) controlling risk in the financial system;

(b) promoting the efficiency of the payments system; and

(c) promoting competition in the market for payment services, consistent with the overall stability of the financial system.

In addition, it is the Payments System Board's duty to ensure that the powers and functions of the Bank under Part 7.3 of the *Corporations Act 2001* are exercised in a way that, in the Board's opinion, will best contribute to the overall stability of the financial system. These powers and functions relate to the supervision of central counterparties (CCPs) and securities settlement facilities, which are key components of the central infrastructure that supports financial markets. The Bank's payments policy area also acts as independent overseer of Australia's high-value payment system, the Reserve Bank Information and Transfer System (RITS), which is another key part of Australia's financial market infrastructure.

The Bank's operational role in the payments system is effected through its ownership and management of RITS, which is used by banks and other approved financial institutions to settle their payment obligations on a real-time, gross settlement basis. Extinguishing settlement obligations in a safe and efficient manner ensures that there is no build-up of settlement obligations associated with high-value transactions and thereby promotes the stability of Australia's financial system.

5.2 Environment

The payments environment is changing rapidly. Usage of cash and cheques is declining relative to other payment instruments, use of electronic payments is increasing and there is significant innovation in customer-facing technology. User and industry expectations concerning the speed of payments, and the capacity to combine information with payments, have been increasing. The Reserve Bank has encouraged a major upgrade of Australia's retail payments infrastructure through its *Strategic Review of Innovation in the Payments System*. It is also contributing to the process of innovation by participating in the New Payments Platform, including by developing the Fast Settlement Service (FSS), which will act as the settlements hub for the new industry platform. For card payments, the Financial System Inquiry broadly endorsed the existing regulatory approach, although it recommended that the Bank consider some changes with respect to interchange regulation and surcharging. The Bank has since conducted a review of the regulatory framework, with the Payments System Board determining three new standards in May 2016.

In the area of financial market infrastructure, there is a strong international push towards greater use of CCPs in derivatives markets. This has resulted in increased cross-border provision of CCP services, which in recent years has led to the licensing of two overseas-based CCPs in Australia, bringing them under the supervision of the Bank and ASIC. With greater use of CCPs, there is a strong focus among policymakers internationally on regulatory policies to ensure their resilience.

Globally, there is significant interest in the use of block-chain or distributed ledger technologies in payments, clearing and settlement. There is also a strong focus among operators of payments infrastructure globally on cyber resilience.

5.3 Performance

As the owner and operator of RITS, the Reserve Bank seeks to ensure that this system operates with extremely high levels of reliability and security, while also adapting to the needs of a 24/7 payments world. A broad range of operational metrics are tracked in real time and documented. These include measures of system availability, system liquidity, participants' transaction values and volumes, and system throughput and performance. The system availability target is 99.95 per cent for RITS during core system hours. The Bank will work to maintain this operational target for each reporting period covered by this plan.

The Reserve Bank is committed to ensuring that RITS is well protected from cyber attack and work is ongoing to ensure that RITS's cyber resilience continues to be at a very high standard.

Reflecting its responsibility to promote competition and efficiency in the payments system, the Bank has recently concluded a wide-ranging review of card payments regulation, which addressed issues raised in the recommendations of the Financial System Inquiry. At the conclusion of the review, the Payments System Board determined three new standards, two dealing with interchange payments in debit and credit card systems and one relating to merchant surcharging. Over the coming year, the Bank will monitor the impact of the new standards, which will be implemented in a staged manner, beginning with a new framework for surcharging by large merchants effective 1 September 2016.

In the area of financial market infrastructure, the Bank will continue to execute its responsibilities as overseer of high-value payment systems and supervisor of Australian-licensed clearing and settlement facilities. As part of this function, the Bank will continue to conduct and publish annual assessments of RITS and licensed clearing and settlement facilities, against relevant standards. The Bank will also continue to contribute actively to international policy work on CCP resilience and crisis management of financial market infrastructures, adapting domestic regulatory standards and frameworks as needed in response to international policy developments.

5.4 Capability

Reflecting the critical importance of RITS to the Australian financial system, the Reserve Bank invests significantly in its technical and business infrastructure and in operational resourcing to ensure that RITS continues to operate to appropriately high standards of availability and resilience, and that it meets the changing needs of the Australian payments system.

The Bank will develop new systems and functionality, including the FSS, which will facilitate 24/7 real-time settlement of payments exchanged by households, businesses and government agencies across the New Payments Platform. Development of the FSS will be completed by mid 2017. Live operations are expected to commence in the fourth quarter of 2017.

An important domestic policy focus in recent years has been the development of a special resolution regime for financial market infrastructures. The Australian Government consulted on the design of such a regime in 2015, including the proposal that the Bank be the resolution authority for CCPs and securities settlement facilities. The Bank will continue to work with the government and other domestic financial regulators to develop legislation to underpin the proposed regime as well as operational plans to execute powers granted under the regime.

6. Banking

6.1 Purpose

Insofar as the Commonwealth requires it to do so, the Reserve Bank must act as banker for the Commonwealth. In common with many other central banks, the Bank also provides banking and custody services to a number of overseas central banks and official institutions. These services include payments and collections as well as general account maintenance and reporting.

6.2 Environment

There are substantial changes under way in transactional banking, particularly in the area of payment services. The broader community is embracing new technology and demanding digital services at a rapid pace. As the largest provider of transactional banking services to the Australian Government, the Reserve Bank must be in a position to respond appropriately with convenient, secure, reliable and cost-effective services.

The Australian Government is seeking to implement more modern electronic payment services when interacting with its customers. It is expected that the government's banking requirements will continue to evolve in response to broad policy requirements, improvements in payments technology and general changes in the way government agencies interact with the public. The Bank expects that the government and its agencies will require banking services that facilitate a range of options for making and receiving payments on digital platforms that are convenient and cost effective for the public to use.

6.3 Performance

The Reserve Bank competes with commercial organisations to provide banking services to Australian government agencies. It must cost and price the services separately from its other activities as well as meet an externally prescribed minimum rate of return on capital over a business cycle. At present, the return on capital is the Bank's principal measure of financial performance for its transactional banking business.

The Bank will continue to implement several important banking projects over the next few years, including the renovation of its banking applications and systems and building the capabilities to participate in the payments industry's New Payments Platform.

The renovation of the Bank's banking applications and systems is made up of a number of projects, which will be completed progressively over the next several years. Work on renovating key components of the systems used to process bulk electronic payments and the final components of systems used to collect payments for the government will be completed during 2016/17. Effort is also under way to replace the Bank's core account maintenance system. This work began in 2015/16 and is scheduled for completion in late 2018.

By the end of 2019, the Bank is seeking to have migrated all of its banking applications and systems to more contemporary technologies, enabling it to continue providing convenient, secure, reliable and cost-effective banking services to the Australian Government and its agencies over the subsequent decade. The Bank's work to build capabilities to participate in the New Payments Platform is planned to proceed in line with the payment industry's timeline.

6.4 Capability

The Reserve Bank will continue to develop its services with the intention of accommodating the government's likely banking needs, while at the same time meeting the objectives of security, reliability and cost-effectiveness.

The Bank has several strategic projects either under way or at the planning stage that will enable it to meet its banking purposes, including those projects mentioned in section 6.3 above.

7. Banknotes

7.1 Purpose

The Reserve Bank is responsible for the issue, reissue and cancellation of Australian banknotes. Its primary purpose in carrying out this role is to maintain public confidence in the supply, security and quality of Australian banknotes. The Bank works with its wholly owned subsidiary, Note Printing Australia Limited (NPA), to design the banknotes and arranges for their production through NPA. The Bank distributes the banknotes to financial institutions, monitors and maintains their quality in circulation and withdraws unfit banknotes from circulation. It also monitors and analyses counterfeiting and carries out research into banknote security technology.

7.2 Environment

While the proportion of payments made using banknotes is declining relative to electronic payments, the number and value of banknotes on issue continues to rise, highlighting their continued importance as a payment mechanism and a store of value. At the same time, the number and value of banknotes on issue in several countries has fallen in absolute terms in recent years. As well, it remains the case that counterfeiting in Australia, while still low by international standards, has risen over the past decade as advances in technology have made it easier and cheaper to produce and distribute counterfeit banknotes.

7.3 Performance

Public confidence in Australian banknotes is measured directly by a Reserve Bank survey on perceptions of Australian banknotes that is conducted every two years, with the next survey to be conducted in late 2016. This survey asks a number of questions about the public's attitude to, and awareness of, banknotes, including the level of concern about counterfeiting.

In addition, for each reporting period covered by this plan, the Bank will continue to monitor a number of indicators that could affect the public's confidence in the supply, security and quality of Australian banknotes, as discussed below.

The Bank aims to ensure that the public's demand for banknotes is met. Fulfilment of banknote orders by commercial banks provides an indication that this demand is being met. Fulfilment of 99.5 per cent of banknote orders on the day requested indicates the Bank has been timely in meeting demand. The Bank will work to maintain this operational target for each reporting period covered by this plan.

The Bank's key initiative to enhance banknote security is the Next Generation Banknote (NGB) program for the issuance of a new series of banknotes. Issuance of the first new banknotes is scheduled to commence in September 2016, when the new $5 banknote will be issued. It is planned that the new $10 banknote will be launched in late 2017. The intention for subsequent issuance is that one denomination will be issued each year. Wide acceptance and distribution of these banknotes over subsequent years will be important to this strategy and the Bank will monitor progress via the survey conducted every two years. The Bank will also monitor counterfeiting rates of the existing and the new series, as well as overseas trends in counterfeiting, to identify possible threats to public confidence in banknotes.

It is generally easier for the public to detect counterfeits if the quality of genuine banknotes in circulation is high. The Bank accepts banknotes only of sufficiently high quality for issuance to the public. It works closely with NPA to ensure that high-quality Australian banknotes are produced that meet the Bank's specifications and requirements. The Bank also has arrangements in place whereby the private sector is encouraged to sort banknotes to minimum standards. The Bank will continue to collect information on the quality of banknotes in circulation to measure the success of this program.

NPA is required to meet the Bank's Australian banknote order in full and on time, and to the required quality standard. Quality is measured relative to agreed specifications and compliance with those specifications is monitored through reports provided by NPA to the Bank after each production run.

7.4 Capability

The Reserve Bank's key strategy in this area over the next four years is to develop a new series of banknotes, incorporating improved security features.

NPA is supporting the Bank's strategy by working with it on the design of the new series, investing in the equipment required to produce the new series and printing the new banknotes as required by the Bank. During the period of production of the new banknotes, NPA will be required to operate at full capacity, with some, albeit limited, ability to meet any orders from longstanding export customers. This is in line with NPA's five-year strategy, which involves maintaining relationships with existing central bank customers and seeking to re-establish relationships with some previous central bank customers to keep open the possibility of export business after production of the NGB series eases off.

To facilitate a smooth transition between issuance of the new series and withdrawal of the existing series, and to ensure this occurs in the most cost-effective manner, the Bank has negotiated modifications to the distribution agreement with the relevant commercial banks.

The Bank has developed a communication strategy to assist with public recognition of the new series. This involves engaging business stakeholders, such as banks, retailers and relevant machine manufacturers. It also involves an ongoing multi-channel public awareness campaign providing information to many groups across the community, including the vision-impaired, older generation and people from culturally and linguistically diverse backgrounds.

Construction is progressing on the new banknote storage, processing and distribution facility at Craigieburn, in Victoria. This new National Banknote Site will facilitate the effective issuance of the new series and is designed to meet Australia's estimated needs for the next 25 years. Construction is due to be completed by the end of 2016. Upgraded banknote-processing equipment will be installed in the new facility in 2017 and the facility is expected to be commissioned in the second half of 2017.

Overseas central banks and organisations provide essential information and intelligence on world best practices for banknote security and functionality. As part of its strategy to maintain public confidence in banknotes, the Bank will continue to be involved in organisations such as the Central Bank Counterfeit Deterrence Group, which examines emerging threats in counterfeiting technologies, and the Reproduction Research Centre, which provides facilities to test new security features. Additionally, the Bank will share information and participate in joint work on banknote distribution and research and development into banknote security with the Four Nations Group of central banks.[2]

2 Members of the Four Nations Group are the Reserve Bank of Australia, Bank of Canada, Bank of England, Bank of Mexico and Federal Reserve Board. These central banks collaborate on banknote security research, testing and development.

8. Financial Position and Capital

8.1 Purpose

The Reserve Bank is not a profit-maximising institution. Profits are incidental to its policy outcomes. As noted in section 4.1, the Bank holds assets primarily to conduct operations in financial markets to achieve its central banking policy objectives – specifically, to implement monetary policy, to support the Bank's role in the Australian foreign exchange market and to manage the country's international reserves. Although carried out largely for policy purposes, these activities have been profitable in most years in the past. The Bank seeks to ensure that its retained profits and other capital reserves are sufficient over time to absorb losses to which the Bank may be exposed.

8.2 Performance

The Reserve Bank's operations in financial markets earn a profit in most years even though they are carried out predominantly for policy purposes. The Reserve Bank Reserve Fund (RBRF) is the Bank's permanent capital reserve, whose primary purpose is to provide sufficient capacity to absorb losses when it is necessary to do so. The Reserve Bank Board has a policy of holding sufficient capital against the risks that the Bank faces and regards a target for capital of 15 per cent of assets at risk as broadly appropriate for the risks that the Bank currently faces. The distribution of profits – essentially determination of the dividend payable to the Australian Government, the Bank's owner – is governed by section 30 of the *Reserve Bank Act 1959*. This legislation determines that underlying earnings and realised gains are to be made available for distribution, while unrealised gains are retained and transferred to the Unrealised Profits Reserve. The legislation also determines the process for approving transfers to the RBRF. The decision on these transfers is the Treasurer's, following consultation with the Reserve Bank Board.

9. Risk Oversight and Management

This section outlines the approach to managing and overseeing the risks faced by the Reserve Bank.

9.1 Risk Appetite

The Reserve Bank faces a broad range of risks reflecting its responsibilities as a central bank. These risks include those resulting from its responsibilities in the areas of monetary, financial stability and payments system policy as well as its day-to-day operational activities.

The risks arising from the Bank's policy and regulatory responsibilities can be significant. These risks are managed through rigorous processes that emphasise the importance of integrity, intelligent inquiry, maintaining high-quality staff and public accountability.

The Bank faces significant financial risks, largely because it manages Australia's foreign exchange reserves. It accepts that the balance sheet risks are large, and manages these risks carefully but not at the expense of its policy responsibilities. It accepts very little credit risk.

The Bank recognises that it is not possible or necessarily desirable to eliminate all the risks inherent in its activities. Acceptance of some degree of risk is often necessary to foster innovation in business practices. Nonetheless, the Bank has a low appetite for most types of operational risk and makes resources available to limit operational risk to acceptable levels.

9.2 Risk Management Framework

The Reserve Bank's risk management framework establishes an effective process to manage risk across the Bank.[3] Managers have a responsibility to evaluate their risk environment, put in place appropriate controls and monitor the effectiveness of those controls. The risk management culture emphasises careful analysis and management of risk in all business processes.

Risks are identified, assessed and managed at both an enterprise level ('top-down') and business level ('bottom-up'). The Risk Management Committee, which is chaired by the Deputy Governor, has oversight of these processes. This Committee meets at least six times a year and provides a report on its activities to both the Executive Committee (chaired by the Governor) and the Reserve Bank Board Audit Committee.

The Bank's attitude towards its key strategic, financial, people and operational risks is described in the *Risk Appetite Statement* (RAS)[4], which is reviewed at least annually and published on the Bank's website.

All Heads of Department are responsible for the implementation of risk controls consistent with the Bank's RAS, and these are also published in the RAS. The RAS is reviewed annually or whenever there is a significant change to the Bank's operating environment.

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3 The Bank publishes its *Risk Management Policy* on its website. This policy seeks to ensure the implementation of an effective risk management framework that is consistent with the Bank achieving its policy and operating objectives. In doing so, it follows accepted standards and guidelines for managing risk, particularly those used by public and financial institutions.

4 For further details, see <http://www.rba.gov.au/about-rba/risk-appetite-statement.html>.

10. Other Influences

To facilitate the achievement of these objectives, the Reserve Bank also relies on its high-quality staff, the information technology underpinning its activities and a range of supporting services provided by other parts of the Bank. These services include:

- carrying out independent appraisals of the Bank's internal control framework
- managing the Bank's properties, security, information assets and facility services
- preparing the Bank's financial and management accounts
- preparing and publishing Bank information using a range of publications, the Bank's website and other media
- supporting the consistent and effective application across the Bank of the Bank's framework for managing risk.