

Banking and Payments

The Reserve Bank provides a range of banking, registry and payment settlement services to Australian financial system participants, the Australian Government, and other central banks and international bodies. These include the provision of central banking services to the Australian Government for the public accounts operated by the Department of Finance and Deregulation (DoFD); transactional banking services to government agencies; custodial, registry and associated services; and the operation of a real-time gross settlement (RTGS) system for Australian dollar high-value payments.

While the majority of these services fall within the scope of central banks' core activities, some, such as the transactional banking and registry services provided to Australian Government agencies, do not. Accordingly, these services are provided on a commercial basis in line with the Australian Government's competitive neutrality guidelines.

Banking

The Reserve Bank provides central banking and related services to DoFD on behalf of the Australian Government, the Australian Office of Financial Management (AOFM), the Australian Reinsurance Pool Corporation and 46 overseas central banks and other official institutions. It also provides contestable transactional banking services to around 90 government agencies on a commercial basis.

One aspect of the Reserve Bank's central banking activities is the role it plays as core banker to the Australian Government. Among other things, this requires the Bank to manage the consolidation of all Australian Government agency account balances, irrespective of the financial institution that provides transactional services to an Australian Government agency. These balances are transferred at the end of the operational day into a group of accounts at the Reserve Bank, known as the Official Public Accounts (OPA) Group. This is where the Commonwealth's overnight at-call cash balances are held. The Bank also provides the Government with a term deposit facility for investment of its excess cash reserves, as well as a short-term overdraft facility to cater for occasions where there is an unexpected demand on Commonwealth cash balances. These broad arrangements have been established under an agreement with DoFD.

The AOFM has day-to-day responsibility for ensuring there are sufficient cash balances in the OPA Group and for investing excess Commonwealth funds in approved investments, including term deposits at the Reserve Bank. The Bank also offers term deposit investment facilities to other government entities, including the Australian Reinsurance Pool Corporation.

The Reserve Bank's transactional banking activities involve the delivery of payment and related banking services. The provision of these services is contestable, and the Bank competes against other commercial financial institutions to deliver these services to government agencies. These agencies can require service features that are common to government but not routinely requested by other users of payment and collection services. Because of its particular focus on the government sector, the Bank is able to provide facilities tailored to their specific requirements. These include features such as extremely high standards of system reliability and availability, purpose-built overnight reporting and the flexibility to react quickly when changes in government policy require consequent changes to systems and processes.

The delivery of direct entry payments from government agencies to recipients' accounts is a significant part of the Reserve Bank's transactional banking activities. In 2009/10, approximately 277 million payments totalling \$276 billion were delivered through this payment stream by the Bank.

During the course of the year, the Reserve Bank continued to work closely with industry on replacing the outdated bilateral communication links that support the exchange of direct entry and other low-value payments between payment service providers in Australia. In February 2010, the industry formally established a new communication 'network cloud', called the Community of Interest Network (COIN), to facilitate the exchange of these low-value payments. An industry management committee has been established under the auspices of the Australian Payments Clearing Association to oversee the operation of this network. The Bank is represented on this committee.

By end June 2010, the Reserve Bank's Banking Department had migrated its cheque and direct entry payment exchanges with four financial institutions – including two of the four major banks – to the COIN infrastructure. It anticipates migrating all of its low-value payment exchanges by end September 2010.

In addition, one major bank has chosen to exchange its direct entry and cheque payments via SWIFT. Banking Department has also migrated its payments exchanges with this institution, using the Low Value Clearing Service (LVCS) established by the Reserve Bank's Payments Settlements Department. Additional detail on the LVCS is set out in the 'Settlement Services' section of this chapter.

Over the past year, the Reserve Bank has also been working actively with its larger government agency customers to upgrade their legacy bilateral communication links with the Bank, which had been based on similar technology to that used by payments service providers. These links are used by agencies to send payment request files to the Bank and receive end of day reports and other data from the Bank. By end June 2010, the Bank and its government agency customers had replaced all bilateral links reaching the end of their technology life cycle.

The Reserve Bank also provides its government agency customers with access to a number of bill collection services, including BPAY®, over-the-counter, phone and internet-based collection services. The range of services provided in this area has continued to expand over the past year and the Bank has worked closely with government agencies to make sure that they have the payments options most suited to their business needs. As part of this process, the Bank worked with an external service provider to introduce a purpose built internet and phone-based card collection facility for the Australian Taxation Office. Since its introduction, other agencies have also begun to use this enhanced service.

The Reserve Bank has also introduced a new service that allows frequent within-day submission of RTGS payment files to the Bank on an automated basis. Agencies are able to submit RTGS payments promptly using their own business systems once they have identified a need to send an urgent, or time critical, payment. In October 2009, the Bank also responded to an industry discussion paper released by the Minister for Human Services on *Better Dealings with Government: Innovation in Payments and Information Services*. The response outlined various ways in which the Department of Human Services could enhance its customer service options and processing efficiency, including by making greater use of internet and phone-based payment collection services to reduce manual processing.

Earnings after tax in 2009/10 for the Reserve Bank's transactional banking services were \$3.8 million, compared with \$3.5 million in the previous year.

Registry

The Reserve Bank provides registry services to the Australian Government, under an agreement with the AOFM, and a number of official foreign institutions that have Australian dollar debt programs. In common with other registry operators, the services provided to clients include registration of new issuance, ongoing maintenance of ownership records, distribution of interest payments and redemption of securities at maturity.

The Reserve Bank also provides a small-investor facility that enables retail investors to buy or sell CGS. The number of small-parcel transactions has dropped noticeably over the past 12 months as a result of the more stable economic environment. Information relating to the small-investor facility, including indicative buying/selling prices, is available on the Bank's website.

As in past years, the level of transactional activity in the Reserve Bank's registry remained quite low because wholesale financial market participants settle their CGS trades electronically in Austraclear. Earnings after tax for the CGS registry business in 2009/10 were \$0.1 million, the same as in the previous year.

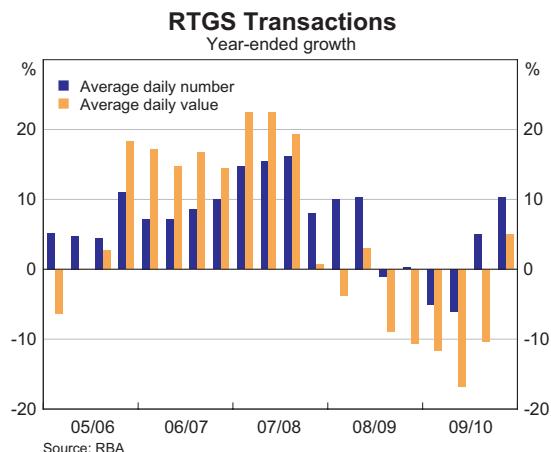
Settlement Services

The Reserve Bank owns and operates the Reserve Bank Information and Transfer System (RITS), which is a critical piece of infrastructure of the Australian financial system. It is used for real-time payments and settlements by 58 institutions – mainly APRA-licensed ADIs – that have been approved by the Bank to operate an Exchange Settlement Account (ESA). A further 10 institutions that hold ESAs have appointed another ESA holder to act as a settlement agent in RITS.

Payments between institutions are settled in RITS across their respective ESAs. By value, about 90 per cent of all payments settled in RITS are settled individually on an RTGS basis. These include time-critical customer payments, all wholesale debt and money market transactions and the Australian dollar legs of foreign exchange transactions. The latter includes Australian dollar trades involved in continuous linked settlement (CLS), for which net amounts are paid to and received from CLS Bank each day.

In addition to RTGS payments, RITS settles batches of netted payments. One batch is a dedicated multilateral settlement at 9.00 am each day for payments arising from cheque, direct entry and retail card transactions that are cleared through low-value systems prior to settlement the next business morning across RITS. A batch settlement facility in RITS also allows approved parties to submit batches of netted payments to RITS at any time during the business day. This facility is used once each day by the Australian Securities Exchange for settlement of payments arising from equity transactions. It has also been used to settle some property-related transactions to prove the capability for electronic conveyancing and settlement.

The average daily value and number of RTGS transactions in 2009/10 were \$168 billion and 32 400, respectively. The value of transactions was well below annual averages recorded prior to the onset of the global financial crisis. RTGS transaction figures continued to be relatively low through 2009/10, particularly in the first half of the year. Some recovery was experienced in the June quarter, with transaction values and numbers both higher than in the June quarter 2009. In 2009/10, the highest daily value of transactions settled in RITS was \$254 billion, on 15 June 2010, a decrease from the previous year's peak day of \$289 billion, which in turn was down from the peak day of \$312 billion recorded in 2007/08.



The Reserve Bank continues to invest significant resources in maintaining and enhancing RITS to ensure it operates to the highest standards of availability and resilience and keeps pace with international best practice for RTGS systems.

One new piece of functionality implemented in RITS in July 2009 is a targeted bilateral offset facility. This functionality allows any two RITS members to offset selected transactions against each other to improve the efficient use of system liquidity and to assist in client credit management.

As foreshadowed in last year's Annual Report, the Reserve Bank is making use of its significant public policy investment in RITS to assist the industry to make improvements in the infrastructure for low-value clearing systems. This major RITS initiative – the Low Value Feeder (LVF) project – comprises three main parts:

- Establishment of RITS network connectivity with members utilising the COIN infrastructure. This work has been completed.
- Provision of the LVCS, which facilitates interconnectivity between the COIN and SWIFT so that RITS members can exchange clearing files across their preferred network rather than having to use both SWIFT and the COIN industry infrastructure. The LVCS became operational in June.
- Provision of a Low Value Settlement Service, which facilitates more timely settlement of low-value clearings. RITS members will be able to provide settlement instructions to RITS for these low-value clearings by either SWIFT or the COIN. This service is expected to be available in the first half of 2011.

Together, the three components represent a new settlement infrastructure for low-value payments that will improve timeliness and efficiency. This infrastructure modernisation aims to provide a platform to support product innovation and customer service, as well as reducing the risk associated with the current net deferred settlement arrangements.

The Reserve Bank also provides settlement services for banknote lodgements and withdrawals by commercial banks and for high-value transactions undertaken by the Bank and its customers, including the Australian Government, overseas central banks and official institutions. At the end of June 2010, 41 central banks and official institutions overseas were using the settlement and safe custody services provided by the Bank to settle their Australian dollar transactions.