

Consultative Report – Principles for Financial Market Infrastructures

Comments by the South African Reserve Bank

Introduction

The National Payment System Department of the South African Reserve Bank (the Bank) has reviewed the consultative report and has consulted with the Johannesburg Securities Exchange (JSE) and STRATE (the operator for securities and bond market transactions) in South Africa. The JSE and STRATE will be channelling their comments to the Financial Services Board (the securities regulator in South Africa) for submission via IOSCO in a separate document. The Bank will, therefore, focus on the payment system issues rather than securities.

The Bank has also requested comment from the Southern Africa Development Community (SADC) central banks and has received comment from two banks. These are attached separately.

Comment

We would like to start by complimenting the workgroup and editing team responsible for compiling the consultative report on a comprehensive and thorough document. We find the principles relating to the payment system comprehensive and relevant. Our comments and questions, as a result, are limited.

1. General comment on principles 4 (Credit risk) and 7 (Liquidity Risk) including aspects related to principle 5 (Collateral):

In South Africa, participants in the payment system are held responsible for the risk that they introduce into the system. In terms of the RTGS several options for settlement are provided of which the major ones are:

- i. Real-time line catering for single settlement instructions (immediate settlement),
- ii. Continuous Processing line (CPL) and Continuous batch processing line (CBPL) which allow for gross settlement using net funding.

These options all work on a pre-funded settlement principle. Intraday liquidity is boosted by allowing the use of the cash reserve and the Liquid Asset Requirement holdings to be used for intra-day liquidity. Furthermore, risk reduction initiatives introduced over the years, including the placing of item limits on retail instruments, has reduced the retail settlement to between 7 and 8 percent of daily settlement. The “cover 2” principle was contemplated prior to the risk reduction measures but is no longer considered necessary in the retail settlement environment. In the high-value environment the measures to provide

liquidity boosting intra-day measures has proved extremely effective and the Cover 1 or 2 principle is not being contemplated.

Finally, in the provision of central bank assistance to the settlement system and its participants (e.g. LOLR), this will be considered on an individual participant basis. In this regard assistance would be provided to one, two or more participants depending on circumstances rather than to the system itself. To further explain this concept, for example, a bank participating in the CLS environment requiring assistance from the central bank would (depending on circumstances), receive that assistance as a participant in the settlement system rather than the Bank considering assistance to CLS directly.

2. "Public disclosure" – Key consideration 3 in principle 13 and 2 in principle 18:

These two considerations speak of "public" disclosure relating to participation and default. What is meant by "public"? Is it the general public? Or does it mean to disclose to those participants that "need to know"? For example, we have certain participation and procedural rules etc. published on a restricted web site available to participants in the settlement system. Is this perhaps what is being implied?

3. General comment on principle 19 – Tiered participation:

Tiered participation in the settlement system is allowed in South Africa in terms of sponsorship arrangements where a qualifying large settlement bank may sponsor a smaller bank in clearing and settlement. The sponsoring bank is held responsible for any risk that the sponsored bank may bring into the system.

An option exists where the sponsored bank may clear in its own name with settlement still the responsibility of the sponsoring bank.

Legislation also allows for non-banks to be designated as clearing participants in the system with settlement occurring via the sponsoring bank. Preference is given to clearing in own name as this enables the sponsored bank to be visible in the system.

Such sponsorship and designation takes place in terms of criteria approved by the Bank.

4. Adoption and implementation of principles

The Bank uses the current CPSS SIPS as a fundamental basis in its oversight process and will continue to do so. The Bank is confident that its current legislation relating to the National Payment System will remain relevant and cover the new principles that apply to the payment system. Furthermore, rules, participation criteria etc are generally approved for implementation by the Bank allowing adjustment to be made when the new principles are published. Certain criteria, for example, entry of payment clearing house operators into the system,

may have to be modified in South Africa to cater for principles such as principle 15 (General Business Risk).

5. Assessment methodology

The Bank looks forward to viewing the results of the work of the Assessment Methodology Workgroup as we believe that this will have a significant impact on how the principles will be interpreted (in, for example, an FSAP process).

Once the assessment methodology is available the Bank will initiate a process to do a self-assessment on the payment and settlement system in South Africa. The Bank, in its role as the SADC payment system project leader, will also encourage the SADC central banks to undertake similar reviews which may include peer-reviews, as done in the past.