

9 September 1996,

The Secretary  
Financial System Inquiry  
Treasury Building  
Parkes Place  
PARKES ACT 2600

Dear Sir,

## **Submission by Austraclear Ltd to Financial System Enquiry - September 1996**

### **THE COMPANY**

During the late 1970's and early 1980's extreme volatility in Australian short term domestic interest rates led to significant trading in the main money market instruments of the day viz. Bank Accepted Bills of Exchange and Certificates of Deposit issued by licensed Australian banks.

Settlement of these transactions was by physical delivery of negotiable paper in exchange for cleared funds, normally a bank cheque. The capacity to trade outstripped the capacities of back offices to settle these transactions in a timely manner and consequently market inefficiencies and settlement risks developed. Market needs dictated that a solution be found to this problem. A group of major market participants commissioned a study and out of this study arose the concept for Austraclear Limited.

Austraclear was formed by 70 of the leading participants in the Australian money market and was charged with developing and operating a Central Securities Depository (CSD) for money market securities and providing for the electronic settlement and clearing of trades for the market.

The system which began operation in September 1984 now has in excess of 500 participants, including all licensed banks, merchant and international banks, major life insurance, superannuation and trust companies, Federal and State Government bodies, securities dealers and brokers. Securities lodged at the CSD by these participants are either in paper or registered form and include Bills of Exchange, Negotiable Certificates of Deposit (NCD's), State Government Securities (and those of their agencies), Corporate Paper and all types of interest bearing securities such as Bonds, Notes, Pass-Through and Variable Rate Securities. Corporations wishing to use these facilities are required to apply to become participants in the system, establish a special clearing bank account and abide by a set of regulations (business rules) which are established and controlled by Austraclear.

The system software has been updated regularly to include new capabilities. Today, the system (known as FINTRACS) complies with all the Group of 30 recommendations for clearing and settlement.

Austraclear not only operates the CSD in Australia for all non-Australian Government money market securities but has also used its software development team to build customised versions of Fintracs for the clearing and settlement of Commonwealth Government Securities by the Reserve Bank of Australia. An enhanced range of securities settlement options and facilities have been provided in a customised version of Fintracs which is operated under licence in New Zealand by the Reserve Bank of New Zealand. This system settles both debt and equity securities.

### **Austraclear in the Australian Money Market**

The following summarises Austraclear Ltd's role in the Australian Money Market:

Number of Participating Entities/Members	-	770
Value of Securities held on behalf of members:-		
Bearer	-	\$ 85.5 Billion
Registered	-	<u>\$ 69.0 Billion</u>
Total	-	\$154.5 Billion
Average Daily Turnover	-	\$ 25.0 Billion
Average Transaction Size	-	\$ 5.3 Million
Number of Transactions in a year	-	900,000

Transactions settled by the Austraclear system between its participant members are:-

- Trades in securities held by the depository on behalf of members;
- Pledges in these securities;
- Repurchase agreements in these securities;
- Forward recording of transactions in
  - Fixed Interest Trades
  - Foreign Exchange Transactions
  - Forward Rate Agreements
  - \$AUD Interest Rate Swaps (from October 96);
- Settlement of the above transactions;
- Cash payments between member participants;
- Deposit and margin payments to and from settlement members of both the Sydney Futures Exchange and Options Clearing House.

The Austraclear system interfaces into the payments system through a direct interface to the banking systems and the Reserve Bank of Australia to achieve the delivery versus payment on a net end of day basis.

The Austraclear system has received very high levels of support from the Australian Market. Over 95% of wholesale money market settlements take place through the system. Due to this acceptance it is able to offer additional facilities to improve settlement efficiencies. These include the operation of an electronics registry system for book entry securities and Issuing and Paying facilities for paper securities which are transferable by delivery. These securities are highly negotiable and in the Australian Market they are Bills of Exchange, Certificates of Deposit and Promissory Notes. Austraclear and its members feel that they should be dematerialised in the interest of creating safer and more efficient settlement procedures.

### **Dematerialisation of Physical Securities**

The introduction of the CHESS system to the Australian Stock Market has given that equities market the ability to become scripless. The trend worldwide is to move away from physical paper based securities to book entry recording and transfer of ownership of securities. There is widespread industry support for this approach including the Reserve Bank of Australia, Australian Financial Markets Association, Australian Treasury Operations Association, Australian Society of Corporate Treasurers, International Banks and Securities Association and issuers of securities. Austraclear as the holder of these securities as nominee for the beneficial owners as recorded in its settlement system would also point out that the continuation of this practice of physically issuing securities which are immediately delivered to its central depository and held there until maturity, makes no commercial sense in this age of electronic advances. We would also point out that the Federal Government dematerialised Treasury Notes and Treasury Bonds in the 1980s.

Austraclear endorses the need for a review of the Bills of Exchange Act to allow Bills of Exchange to be recorded in the books of a Central Depository and facilitate the change of ownership within that depository without the need to actually draw up the securities as a physical document. As the Central Securities Depository to the Australian Money Market Austraclear is well placed to perform this role.

Austraclear Ltd would welcome the opportunity to discuss with the Committee the issue of dematerialisation of paper based securities and to expand on the benefits that would accrue to the Australian Money Market as a result.

### **Securities Systems by Austraclear Limited**

#### **Other Securities Markets Products provided by Austraclear Limited**

The Software developed by Austraclear Limited to facilitate the electronic settlement of the Australian money market has been licensed to the following organisations:-

Reserve Bank of Australia - to enable the RBA to provide electronic settlement to holders of Australian Government Securities.

Reserve Ban of NewZealand - to enable the RBNZ to provide electronic settlement to holders of New Zealand debt and equity securities.

In both these licensing arrangements, Austraclear maintains and enhances the software. Recently, market initiatives have been undertaken to enhance both systems to facilitate the implementation of Real Time Gross Settlement.

Austraclear Ltd's relationship with the RBA is particularly close as membership by organisations are common to both systems.

Hardware and network backup arrangements are formally in place between the RBA and Austraclear systems and from November 1996 Austraclear will operate under contract to the RBA, the network production and disaster recovery systems for the RBA System and the future Real Time Gross Settlement. Money Market participants see advantages in the merging of these two systems from both a business efficiency point of view as well as the potential to achieve considerable cost savings.

Enclosed is background material describing in greater detail the operation of the Austraclear System and its customised version. Also enclosed is the latest annual report.

We would appreciate the opportunity to expand on the issues raised in this submission. The contact person for this submission is;

Mr John Hall  
Managing Director  
Austraclear Ltd  
GPO Box 4606  
SYDNEY NSW 2001  
Phone (02) 9321-8400  
Fax (02) 9221-1945

**JOHN A HALL**  
**Managing Director**