

Proposal for Reorganizing Fund Transfer Systems in Japan - Introducing a "Large Value Settlement System" (overview)

1. Background

(1) International Standards of Settlement Risk Mitigation

Bank for International Settlements (BIS) "Core Principles for Systemically Important Payment Systems (Core Principles)" January 2001

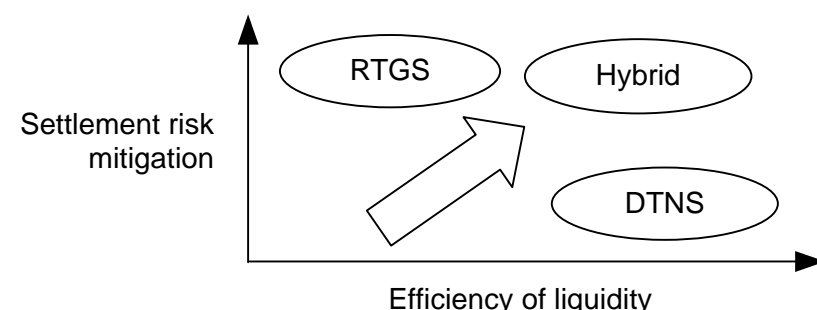
"(Real-time final settlements during the day) are particularly desirable in countries with large volumes of high-value payments and sophisticated financial markets."



Introduction of Real-Time Gross Settlement (late 1990s)
 Fedwire (US), CHAPS (UK), TBF (France), BOJ-NET, etc.
 Introduction of Hybrid Settlement (1999~)
 CHIPS (US), RTGS^{plus} (Germany), PNS (France), BIREL (Italy)

(2) New Trend: Introduction of "Hybrid Settlement"

- Combination of "Designated Time Net Settlement (DTNS)" and "Real Time Gross Settlement (RTGS)"
- Using "Queueing" and "Offsetting" functionalities
- Benefit of saving liquidity and real-time finality



(3) Other Environmental Factors

- Revised Foreign Exchange and Foreign Trade Law eliminated the necessity to distinguish "domestic" from "foreign exchange-related" transactions
- Security settlement reform
- Improving the network infrastructure of BOJ-NET (implementation in 2004)

History

- FY2001: Discussion about introducing a hybrid settlement system started
- FY2002: Feasibility study of US model, etc. (private sector system model) were conducted
- FY2003: Feasibility study of German model (central bank system model), comparison of models, impact analysis on Zengin System were conducted

2. Framework of the System

A comparison was made between the "US model (a Zengin System-based system, which deals with FXYCS transactions and large value transactions of the Zengin System)" and the "German model (a BOJ-NET-based system, which deals with FXYCS transactions, large value transactions of the Zengin System and BOJ-NET Funds Transfer System transactions)".

Although a reduction in credit risks was observed to certain extent in both models, the German model is superior to the US model in the following points:

- It can save more liquidity since it also handles BOJ-NET transactions
- From the perspective of Japanese Yen settlements as a whole, it can anticipate integration with the large-value fund settlement system in the money market, etc.

Considering that the hybrid systems have been introduced in developed countries, the introduction of such a system is necessary in Japan in a few years. If the system is developed utilizing the Zengin System, occasional system developments will be required in the middle of its system life (2003-2011). In this sense also, BOJ-NET-based German model is more practical.

3. Master Plan

JBA proposes to reorganize the fund settlement systems in Japan by introducing a BOJ-NET-based hybrid settlement system, the "Large Value Settlement System," which aims to reduce settlement risk, comply with international standards, and improve the efficiency of providing liquidity.

Note: With regard to the Zengin System, transactions of 5 billion yen or more will be dealt with in the Large Value Transaction System initially. The scope of the amount will be reviewed after assessing its operational performance.

Zengin System Large volume / Small value payments (5.3M trans., JPY9.2T, JPY1.74M/trans.) Designated Time Net Settlement at 16:15 Loss-share rule: Defaulters pay Liquidity provision scheme by 25 banks, JPY2.6T Collaterals JPY11.6T	Large value payments	Zengin System Focusing on small value payments	1. Credit Risk	Interbank exposures of large value transactions reduced (0.005% of transactions and 17.7% of value)
			2. Liquidity Risk	Necessary amounts to provide for liquidity provision scheme reduced (effectiveness limited)
			3. Collaterals	Limit for Sender Net Debit and necessary collaterals reduced (effectiveness limited)
Foreign Exchange Yen Clearing System Small volume / Large value payments (0.036M trans., JPY20.4T, JPY0.6B/trans.) Designated Time Net Settlement at 14:30 Loss-share rule: Survivors pay Liquidity provision scheme by 10 banks, JPY0.8T Collaterals JPY0.7T	Large value payments	BOJ-NET Large Value Settlement System (new)	1. Credit Risk	Cleared by introducing real time settlement
			2. Liquidity Risk	Reduced Liquidity supply scheme not needed
			3. Collaterals	Not needed Funds in the settlement account will be necessary instead.
BOJ-NET Funds Transfer System Small volume / Large value payments (0.016M trans., JPY65.4T, JPY4.0B/trans.) Real Time Gross Settlement Overdrafts supplied JPY14.7T (average peak amounts in each day) Collaterals N.A.	Large value payments	RTGS	No change	

(Transaction numbers and amounts are daily averages of 2003. M: millions, B: billions, T: trillions)

Further issues to be discussed

Based on the above Master Plan, the following issues shall be discussed. To pursue these discussions, JBA and TBA, as owners of related payment systems, shall request the cooperation of the Bank of Japan.

1. Identification of market participants' needs as a whole
2. Discussion about how to reduce the collateral burden and costs of the Zengin System
3. Identification of issues relating to market practices, which may arise due to the introduction of this System
4. Enhancement of opportunities and channels to dialogue with the Bank of Japan in regards to conveying the needs of participants