CPSS principles for effective oversight

José Antonio Marciano
GTSP – ALC

Annual Payments Week – 2008

Vienna

September 9-12, 2008
Agenda

- The case of Brazil
- Comentarios realizados por la Región de América Latina y el Caribe
The Case of Brazil

- Introduction
- Systemically Important Payment Systems
- Oversight Tools
- Current developments
Introduction

Oversight objectives

• The BCB has an interest in the smooth functioning of payment systems and instruments
• Oversight aims at
  – preventing systemic risk
  – promoting efficiency of payment systems and instruments
  – safeguarding the transmission channel for monetary policy
• Scopus
  – SIPS
  – Settlements systems
  – Retail payments systems
Brazilian Payment and Settlement Systems
Systemically Important Payment Systems (SIPS)

• Use of Core Principles for Systemically Important Payment Systems as a guide for national payment system development
• Quantitative criteria for classification of SIPS
  – Value of individual transaction
  – Value of daily turnover
• Legislation and facilities for mitigating risk

<table>
<thead>
<tr>
<th>Risk</th>
<th>Legislation and devices</th>
</tr>
</thead>
<tbody>
<tr>
<td>Legal risk</td>
<td>Specific legislation supporting: finality, netting, collateralized transaction etc</td>
</tr>
<tr>
<td>Liquidity risk</td>
<td>Intraday repurchase agreements (government bonds)</td>
</tr>
<tr>
<td>Credit risk</td>
<td>Use of central bank money</td>
</tr>
<tr>
<td>Intraday finality</td>
<td>Real-time gross settlement system (STR)</td>
</tr>
</tbody>
</table>
Oversight Tools – Overview

Tools

- Authorizations
- On-site inspections
- Backtests
- Quantitative data
Oversight Tools – Authorizations

Must be submitted for the authorization of the Banco Central do Brasil

<table>
<thead>
<tr>
<th>• The creation of new payment and settlement systems</th>
<th>• Any change in existing payment and settlement systems involving the following aspects:</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>– The safety and integrity of the payment and settlement system</td>
</tr>
<tr>
<td></td>
<td>– The procedures for settling securities and derivatives operations or fund's transfer</td>
</tr>
<tr>
<td></td>
<td>– The credit and liquidity risk management</td>
</tr>
</tbody>
</table>

Objective:

*Verify the compliance with principles and the legal framework of payment and settlement systems*
Oversight Tools – On-site Inspection

• Partnership with the banking supervision team (BCB)
• Focused on the IT systems responsible for the risk management, clearing and settlement processes
• Auditing of:
  – Internal controls
  – Information security procedures
  – Business continuity planning
  – Third-party services providers
Oversight Tools – Backtests – Objectives

• Assessment of credit and liquidity risk management procedures for the central counterparties

**Counterparty credit risk**

• Risk of loss from a participant’s default

**Liquidity risk**

• Risk faced by clearing as it must fulfill its payment obligations to non-defaulting participants on schedule
Oversight Tools – Backtests – Description

**Backtest Credit Risk**
- Simulate the costs associated with the close-out of default participant’s portfolio at prevailing market prices
- Calculate the risk (cost) not covered by the default participant collateral
- Compare this risk with the total CCP’s financial resources

**Backtest Liquidity Risk**
- Calculate the total amount of CCP´s liquid financial resources and credit lines
- Calculate the highest debit position among the participants
- Compare the highest debit position against CCP’s liquid resources and credit lines
Oversight Tools – Backtests – Examples

**Backtest Counterparty Credit Risk**

- **X-axis:** Months (13-nov to 8-mai)
- **Y-axis:** Reais milhões (0 to 75)

**Backtest Liquidity Risk**

- **X-axis:** Months (3-mai to 2-abr)
- **Y-axis:** Reais bilhões (0 to 150)

**Legend:**
- Black: Dois Maiores Saldos Devedores
- Green: Maior RFL
- Yellow: Maior Saldo Devedor
- Orange: Linhas de Assist. de Liquidez

**R$/USD:** 1.73
Oversight Tools – Quantitative Data

- **General data**: volume and value of payments and operations, intraday payments profile, etc
- **Efficiency**: netting ratio, average queue time of payments (RTGS), etc
- **Operational risk**: ratios of operational reliability, operational failures statistics, etc.
Oversight Tools – Oversight Report – Example

• Bulletin – Monthly Report

• Financial Stability Report – Half-year (in BCB – Website)
Current developments

• Operational Risk – Business Continuity Management
  – Development of an assessment framework for Business Continuity Plans
  – Tests results review
• Operational Reliability
  – Development of operational reliability ratios for the main macro processes of a deferred net settlement system
    • acceptance
    • clearing
    • settlement
• Improvement of regulatory framework
Principios para una supervisión efectiva

• Temas críticos para la Región:
  – Fundamento legal para la vigilancia.
  – Alcance institucional de la vigilancia.
  – Colaboración entre las distintas autoridades.
  – Alcance de la función de vigilancia.
    • Sistemas de pago de importancia sistémica o mas amplio para incluir al pagos de bajo valor
Principios para una supervisión efectiva

• Solicitud de la región:
  – Colaboración del BIS a través de la publicación de un documento que dicte pautas específicas sobre la implementación de la función de vigilancia, el alcance institucional del Banco Central y la coordinación entre los distintos organismos reguladores.
Gracias

jose.marciano@bcb.gov.br