

APPENDIX TO THE TARGET USER REQUIREMENTS OF 6 NOVEMBER 2002

Complementary Business Needs of the Banking Community

24 April 2003

INTRODUCTION

Since our original TARGET2 User Requirements document issued on November 6th 2002, the TARGET Working Group acting in the name of credit institutions has made further analysis from the perspective of establishing an answer to the ECB consultation on TARGET2.

Thanks to some clarifications which appeared in the Public Consultation and from this analysis, the following important topics are now included for consideration. These complement the initial "TARGET User Requirements" (URs) which remain the fundamental basis of our needs.

1. Liquidity Management: (see 2.1 in URs)

Credit Institutions are increasingly reliant on Central Bank intraday liquidity. Users' payment-liquidity is becoming increasingly fragmented, with the existence of many pots and no effective way to bridge intraday liquidity. There is much greater demand for time specific payments. As a consequence, rapid liquidity shocks may occur with increased interdependencies between financial markets. Liquidity Management should be at the forefront of a system like TARGET.

Need for "Cash Management" services from TARGET2:

Why?

The Eurosystem has decided to keep the management of central bank accounts at the level of NCBs. As a consequence, in the Single Euro Payment Area, numerous credit institutions are dealing with several accounts in one or more NCBs. Each credit institution willing to do so should be able to steer and consolidate its liquidity (payment capacity) and the related cash and collateral management processes.

Each user should have the right to:

- Settle the balance of any ancillary system at a pre-defined account in a pre-defined country. Direct debit could be a tool used for this solution.
- Manage all his accounts held within the participating Central Banks from a centralised location in the European Union.

What content?

A. Access to centralised information:

In the framework of TARGET2, credit institutions need to have permanent real time access to their cash positions in the Eurosystem, namely:

- Information on their global position. The intra-day global euro position of a credit institution corresponds to the addition of all its balances (master account + other NCB accounts).
- Details of the balances composing their global positions. This global position comprehends numbers and global amount in the sending and receiving queues.

To meet intraday management requirements, this information should automatically be updated by each transaction in real time, whatever the push or pull data solution chosen.

B. Pooling facility:

A global credit position should be usable from any entity of the credit institution owning one of the accounts, even when its account shows a debit position (under certain limits and conditions to be defined contractually by the mother credit institution, which will require specific tools to be put in place).¹

C. Netting optimisation facility:

Credit institutions need netting optimisation facilities within the same RTGS and at the level of the Eurosystem.

At the end of the day, the credit institution handling the master account will have to square its debit and if needed its credit positions at all NCB levels from its master account in one NCB². This process should be more or less automatic, depending on contractual relationships between the mother credit institution and NCBs involved in the process.

D. Other facilities:

Use of **direct debit facility** for wholesale purposes only (for banks willing to use this facility) should be part of the TARGET2 cash management offer.

Use of this direct debit facility should, in any case, be subject to a triangular pre-agreed contract involving: the mother credit institution, its branches and subsidiaries and related NCBs.

This tool could also be applied in the single shareable platform for the settlement of local ancillary systems.

These processes will obviously imply the respect of legal constraints in terms of monetary reserves at each country level.

2. Add-ons to Core Services (see 2, 2.1 and 2.2 in URs)

The purpose of the present add-ons is to enhance the same part in the original User Requirements.

- The above cash management services
- Pooling facilities as mentioned above.
- Single standardisation to organise prioritisation facility³.
- Inquiries facilities on the account balances and the status of payments.
- Action facilities to change the priorities or to cancel the payments
- Facilities to manage the reserve requirements.
- Issuing inquiries on own waiting list of outgoing and incoming payments
- Tools facilitating decreases in the need for intra-day liquidity

¹ The (mother) credit institution, defined by the bank willing to use this concept, could also decide to pool all NCB accounts or to leave some NCB accounts outside e.g. for special needs of branches.

² The master NCB account will be clearly defined.

³ The transaction format should not be a concern (SWIFT standards will remain unchanged and therefore used without adding supplementary specification) e.g. SWIFT message fields 13c and 72 containing time sensitive STP coded information should be a driver (depending on the used format).

3. Harmonisation of the settlement of ancillary systems (see 2.1 in URs)

Liquidity is indeed the primary driving factor to be taken into account when considering settlement of ancillary systems. A credit institution should be able to settle the balance of any ancillary system, wherever it is located, at a predefined account in a pre-defined country. Current settlement modes for the ancillary systems oblige multi-country banks to keep an account with each NCB. Settlement of any ancillary system should also be able to be handled through the single shareable platform from the beginning as part of the core service. Therefore, the whole process will only be manageable if settlement of the ancillary systems are modelled on a same time window by type (e.g. cash, securities..).

4. Business continuity - Crisis Management (2.3 in URs)

A standardised help desk service, a single contact point for each user with the necessary knowledge and authority to deliver the same information for all at the same time and make immediate decisions on the problems referred to it is needed.

Each user needs an accountable contact entry point able to answer in his/her language, whatever the type of problem. This single entry point must not necessarily be the same for all users as long as a level playing field is guaranteed: i.e. the same query always gets the same response

Plan, resilience & processing of critical payments in contingency mode:

Except in an extreme case⁴, TARGET2 will ensure the banking community receives prompt and accurate processing of 100% of TARGET payments.

As far as cash and collateral management are concerned, a local disruption could be very damaging in the overall process.

Provision of the best information available in a timely manner is expected. In this context, it is recognised that in the midst of a crisis this may change on an ongoing basis.

It is important that organisational procedures are put in place and regularly tested to avoid confusion when a crisis occurs.

5. SLA: (see 3 in URs)

A single SLA between credit institutions (users) and TARGET2 including the ECB and NCBs should be included in the core services list, the whole composing the “Core Services”. The object of a single SLA is to meet users’ requirements and avoid discrepancies between banks from different EU countries. Therefore, it should cover at the minimum a clear definition of:

- Each service level,
- The contingency measures/plan,
- The resilience constraints,
- ECB & NCBs operating standards & rules.

This global SLA should be the same for domestic and intra-European payments.

⁴ Extreme case or ‘force majeure’ (e.g. SWIFTNet failure).

6. Efficiency, Costs and pricing (see 4.1 in URs)

The TARGET2 single shareable platform should be built as simply and efficiently as expected. This will be facilitated by the architecture, which should not need complicated interfaces or translators:

- Same standards /rules,
- Same functions,
- Same process, etc.

As traffic will be concentrated on the single shareable platform, pricing should decrease, compared to the 15 current RTGS prices, whilst efficiency should increase. Investments and costs in new services should be discussed with users.

Cost reduction research

Every credit institution wants to benefit from the implementation of the single shareable platform in order to reduce its internal costs:

- One shot: credit institutions want a **one-time** investment (i.e. adaptation of their internal software, hardware and procedures) instead of multiple ones for each Euro RTGS. This is also the case in the implementation phase if endorsement, test and training are done at once for all platforms. The migration cost to the single shareable platform for the credit institutions should also be kept in mind.
- Recurrent: the recurrent cost should decrease as well, by managing the maintenance, test and training from a central and co-ordinated point instead of having to deal within each NCB process separately.