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RECENT DEVELOPMENTS IN AUSTRALIA IN CURRENCY NOTE PROCESSING AND DISTRIBUTION ARRANGEMENTS

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Introduction

Since early 1998 the Reserve Bank of Australia has worked with commercial banks and armoured car companies in Australia to significantly re-engineer currency note processing and distribution arrangements. Catalysts for this work were:

- an Australian Government requirement that government enterprises operate within a “competitively neutral” framework when providing services in competition with the private sector. Within such a framework the Reserve Bank was unable to compete for some distribution services it was providing. There was also the realisation that some distribution services were no longer efficient; and
- recognition that, following the introduction of polymer currency notes in Australia, the level of currency note processing by the Reserve Bank was excessive.

Some background

The Reserve Bank of Australia is responsible for the manufacture, distribution, processing and destruction of Australian currency notes. It is also responsible for the distribution of coin. This paper concentrates on currency note (herein referred to as “note”) processing and distribution re-engineering as the Reserve Bank has had little more than oversight of coin distribution since the mid-1980s.

Up until the mid-1990s the Reserve Bank operated a note processing and distribution centre in each of Australia’s eight capital cities. These centres provided a “retail” note service whereby consignments of notes were despatched to/received from commercial bank branches in metropolitan and near country areas. The Reserve Bank centres also provided a “wholesale” note service to armoured car companies for the servicing of their commercial customers. Large regional centres in Australia were serviced by Note Issue Agencies operated by armoured car companies in conjunction with commercial banks. Other country areas were serviced by a number of different arrangements, ie mail, courier, mobile cash services. Initially the cost of many of these arrangements was met by the Reserve Bank but over time the cost was passed to the commercial banks and others.

Such arrangements resulted in a significant flow back of notes to Reserve Bank processing and distribution centres. From the early 1980s the Reserve Bank’s policy was to process through high speed note processing equipment all notes received by it. To facilitate this policy the Reserve Bank installed 21 Currency Verification Counting and Sorting (CVCS) systems in its processing and distribution centres during the period 1981 to 1986. These systems were subsequently upgraded in 1991

through the installation by Currency Systems International of improved detectors and data processing technology.

By the mid-1980s some 1.8 billion notes were being returned to the Reserve Bank each year - nearly 4 times the number of notes in circulation. The processing and distribution centres employed some 500 staff. In 1990 restrictions were placed on the return of notes to the Reserve Bank under the “wholesale” arrangements for armoured car companies; as a result, the number of notes returned fell to around 1.5 billion each year.

From 1992 to 1996 the Reserve Bank replaced Australia’s paper notes with polymer notes. It quickly became apparent that polymer notes were much more secure and considerably more durable than their paper counterparts and did not require the level of processing being undertaken by the Reserve Bank. There was also evidence of considerable “churning” of notes whereby the same denomination of notes was being delivered to/collected from some commercial banks in the one visit. Experience was that despite the Reserve Bank’s very high note sorting standards, some 98% of polymer notes returned to its processing and distribution centres were being returned to circulation after processing.

It therefore became apparent that changes were needed to make processing and distribution arrangements in Australia more efficient.

The re-engineering process

The first step in the re-engineering process was for the Reserve Bank to withdraw from the “retail” note service it had provided to commercial banks since the mid-1960s. It did this in June 1998 after a period of consultation with commercial banks and the armoured car companies. The armoured car companies subsequently provided a “retail” service to the commercial banks.

At the same time, the Reserve Bank agreed to the establishment of Bank Note Pools - holdings of Reserve Bank owned notes by armoured car companies at some 80 sites Australia-wide. The purpose of these holdings was to enable armoured car companies to service the needs of commercial banks without notes having to be transported to/from the Reserve Bank. Rules were agreed with the commercial banks which saw them receiving same day credit for notes returned to Bank Note Pools by 5.00pm each business day. Same day payment for notes drawn also occurred. Conditions applied for the sorting/presentation of notes lodged to Bank Note Pools. Limits were set on the maximum amount to be held in Bank Note Pools. The basic operating concept for Bank Note Pools was that notes lodged today were to be used to make up deliveries for the day after tomorrow with surplus and unfit notes returned to the Reserve Bank once each week. Additional supplies of notes, if required, were also to be sourced once each week.

The effect of this change was that the number of notes returned to the Reserve Bank dropped to some 1.2 billion over the next 12 months, 1998/9. With the establishment of Bank Note Pools, the Reserve Bank closed three of its smaller processing and distribution centres.

By the middle of 1999, the Reserve Bank had decided to include the “wholesale” distribution arrangements for armoured car companies in the Note Pool arrangements in an effort to further reduce the number of notes being returned to its note processing and distribution centres. This had the effect of significantly reducing the inflow of notes to those centres. During the period July 1999 to June 2000 less than 0.5 billion notes were received at Reserve Bank centres.

With such processing levels it became difficult to sustain operations at the Reserve Bank’s then smaller processing and distribution centres and following a further review of arrangements the Reserve Bank decided to close its remaining note processing and distribution centres and centralise such activities to its note printing site in Craigieburn, Victoria.

By the middle of 2000 all but the Sydney note processing and distribution centre had closed. Supply of notes and the return of unfit and surplus notes for all of Australia has occurred at the Sydney centre since. The centre is equipped with five CVCS systems and has a staff complement of around 20 people. The pre-dominant processing function of the centre is the processing of unfit notes. Surplus fit notes are, in the main, returned to the Sydney centre in tamper evident packets and are stored and re-issued into circulation without processing.

Future arrangements

Around the middle of 2001, the new National Note Processing Centre operated by Note Printing Australia (a wholly owned subsidiary of the Reserve Bank) will take over the processing and distribution role for the Reserve Bank. From that time the Sydney processing and distribution centre will close.

The National Note Processing Centre will accept and distribute notes on a wholesale basis. Its primary functions will be the despatch of new/reissue notes, the receipt and processing of unfit notes, the receipt and storage of surplus fit notes post peak periods and the receipt and processing for quality/authenticity purposes of notes returned from circulation at the Reserve Bank’s request. The Centre will have a similar complement of CVCS systems and staff as the Sydney centre and is expected to process around 250 million notes each year. Rules for accessing/returning notes will apply. Minimum quantities for receipt/despatch are still being discussed with commercial banks and armoured car companies but the Reserve Bank is looking for notes to be returned/despatched in minimum quantities of 200 000 notes of the one denomination and quality type. Unfit notes returned will be already prepared ready for CVCS processing.

With the establishment of the National Note Processing Centre, the Reserve Bank is also re-engineering its processing methods and practices. A significant change will be the introduction of note processing under single control supported by sophisticated CCTV monitoring and other security control measures.

The Reserve Bank has also announced plans for further changes to cash distribution arrangements which seek further efficiencies. The Reserve Bank believes that arrangements under which those who need stocks of notes and coin for their ongoing business also own those stocks would facilitate the development of more efficient distribution practices and inventory management. Under present arrangements no direct links exist between net receivers and net payers of notes and coin. The Reserve Bank also believes that such links are unlikely to develop while the Reserve Bank provides depository facilities through its ownership of external stocks of notes and coin, ie Note and Coin Pools.

Accordingly, the Reserve Bank has proposed that from 1 July 2001:

- commercial banks own stocks of notes and coin presently held in Note and Coin Pools;
- the Reserve Bank pay compensation to commercial banks for interest foregone on those stocks;
- cash centres become the centrepiece of the arrangements. These will be similar to existing Note and Coin Pools but will undertake automated processing of notes for fitness. The payment of compensation will be dependent upon effective sorting of notes by the various holders. The cost of operating cash centres would be for others;
- commercial banks/others meet the cost of obtaining stocks of notes from the new National Note Processing Centre and returning surpluses;
- the Reserve Bank pay a premium for the return to the National Note Processing Centre of unfit notes and other notes which the Reserve Bank directs be returned for quality/authentication sampling.

At the date of publication of this paper, the Reserve Bank, the commercial banks, the armoured car companies and other interested parties are still involved in negotiation of the finer details of the proposed new arrangements. It is, however, expected that new arrangements will commence in July 2001, the minimum change being that the Reserve Bank will cease its ownership of working stocks of notes and coin stored outside its premises.

Summary

The last three years or so has seen significant re-engineering of note processing and distribution arrangements in Australia with a considerable reduction in the Reserve Bank's involvement in those arrangements. The primary catalyst for that re-engineering was the introduction of polymer notes in Australia and the resultant increase in security and durability which occurred.

The re-engineering has delivered considerable cost savings and has enabled the Reserve Bank, commercial banks and armoured car companies in Australia to introduce efficiencies into processing and distribution arrangements. With the changes already made and those to be implemented later in 2001, a sound platform has been established for participants to seek further efficiencies in note processing and currency distribution and inventory management.