Case study

LCH.Clearnet implements ISO 20022 standards for collateral management

> "The choice of ISO 20022 standards on our SWIFT infrastructure will accelerate clearing member on-boarding."
>
> Gerard Smith, Director – Collateral Services, LCH.Clearnet

Business background

Regulatory changes to increase financial stability have prompted a rise in central clearing and led central counterparty clearing houses such as LCH.Clearnet Group, and clearing members, to adopt new methods to address the subsequent increase in collateral movements. LCH. Clearnet Group currently receives approximately 200 instructions per day to move collateral through its Graphic User Interface (GUI) deployed with clearing members. Over the next year, collateral movements are anticipated to increase drastically with the uptake of individual segregated accounts (ISAs) and the continued extension of central clearing mandates. As a result of increasing levels of collateral, clearing members are seeking to optimise collateral efficiency and velocity with more frequent and intra-day movements.

The industry faces three key challenges:

— Increasing volumes of collateral instructions

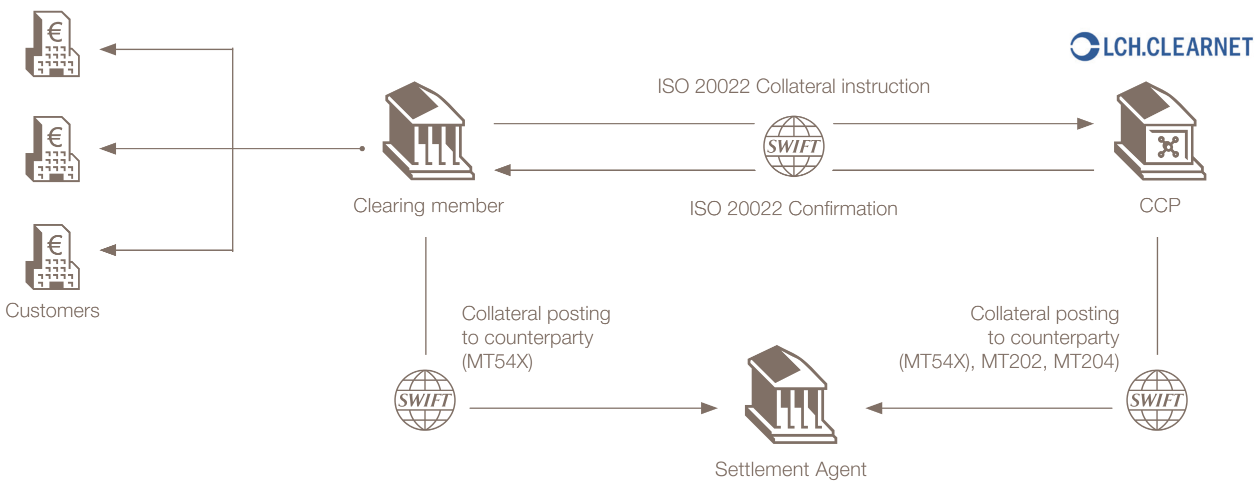
— Lack of standardisation of the process and communication

— Constant pressure to reduce costs and operational risks

Key benefits

In 2013, LCH.Clearnet began an initiative to provide clearing members with a SWIFT interface based on the ISO 20022 standards, which are recognised as international standards for the financial community. This allows clearing members to instruct multiple collateral movements in a single message e.g. multiple cash deposits and also securities substitutions.

This feature reduces the manual processes, increases efficiency and scalability for LCH.Clearnet and its clearing members. In addition, the solution aims to provide sufficient scalability to support the increased number of market participants looking to set up individual segregated accounts ISAs. It is cost efficient as the SWIFT infrastructure already supports ISO 20022 standards and can be re-used for collateral management. It also uses the existing integration mechanism to the back-office to streamline operations and reduce operational risks.



ISO 20022 standards for collateral management

The solution

With the ability to communicate collateral movements to a CCP using ISO 20022 standards, clearing members can re-use their middleware to generate ISO 20022 XML instructions. The instruction, once received and validated by LCH. Clearnet's Collateral Management System (CMS), is then confirmed to the clearing member. This confirmation informs the clearing member that the instruction will be processed, or in other words, will generate a payment or securities settlement.

ISO 20022 standard components enable the clearing member to instruct all types of collateral, designate the specific account at the CCP in question detailing the amount, value and settlement dates. Importantly, through the use of supplementary data, clearing members can also provide details of the settlement location. The design of the ISO 20022 messages supports the various EMIR and Dodd-Frank compliant account segregation models.

Most importantly, the solution allows for real-time collateral transfer, typically from receipt of the message by LCH.Clearnet to the point of actual account credit or debit within 60 seconds, without manual intervention.

Market adoption

LCH.Clearnet's solution is beginning to gain momentum in the market. "We have successfully connected one clearing member and are in discussions with several others" says Gerard Smith, Director – Collateral Services at LCH. Clearnet. "Leveraging our SWIFT connectivity to ensure full straight-through processing (STP) of collateral instructions will benefit our customers that are looking for a solution to streamline collateral movements."

"Our solution is a step towards a more efficient collateral management service for clearing members."

Gerard Smith, Director – Collateral Services, LCH. Clearnet

New opportunities

LCH.Clearnet manages 60 billion EUR of margin liabilities for its clearing members. With the interface live, additional clearing members are set to realise the benefits in the coming months. There are plans to introduce further enhancements, such as leveraging the messaging as part of the clearing member collateral affirmation process. This will support any new client protection models that will be introduced in 2015.

About LCH.Clearnet

LCH.Clearnet is a leading clearing house, serving major international exchanges and platforms, as well as a range of OTC markets. It clears a broad range of asset classes including: securities, exchange traded derivatives, energy, freight, interest rate swaps, credit default swaps, foreign exchange derivatives and euro and sterling denominated bonds and repos. LCH.Clearnet works closely with market participants to identify and develop innovative clearing solutions.

About SWIFT

SWIFT is a member-owned cooperative through which the financial world conducts its business operations with speed, certainty and confidence. More than 10,500 financial institutions and corporations in 215 countries trust us every day to exchange millions of standardised financial messages. This activity involves the secure exchange of proprietary data while ensuring its confidentiality and integrity. SWIFT enables its customers to automate and standardise financial transactions, thereby lowering costs, reducing operational risk and eliminating inefficiencies from their operations.

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