Innovative Buy-Side access models for central clearing

July 2019
Central clearing – A core element to ensure stability and resilience of financial markets

“... Improving over-the-counter derivatives markets: All standardized OTC derivative contracts should be traded on exchanges or electronic trading platforms, where appropriate, and cleared through central counterparties by end-2012 at the latest. ....”
Quoted from the G20 Pittsburgh Summit Leaders’ Statement, September 2009

<table>
<thead>
<tr>
<th>Identified issues related to traditional client clearing models</th>
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<tr>
<td><strong>OTC Derivatives</strong></td>
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<td>❖ Strong concentration of client risk on a few clearing members</td>
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<td>❖ Limitation in terms of porting of positions and collateral in case of clearing member default</td>
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<td>❖ High costs for both clearing members and its clients due to balance sheet constraints</td>
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<th>Solution:</th>
<th>Challenge:</th>
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<tr>
<td>➢ Allow buy-side to directly access CCP Clearing</td>
<td>➢ Address specifics of client types and transaction types to make CCP clearing feasible and relative to bilateral business attractive</td>
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## Buy-side service offering overview and client penetration

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<th>Product/Service</th>
<th>Direct and Specific Clearing Member types for the buy-side</th>
<th>Model</th>
<th>Status</th>
<th>Client examples</th>
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<td>Securities Lending</td>
<td>• <strong>Buy-Side as Lenders can directly participate in the CCP model</strong> where beneficial owners interact with banks on a centrally cleared basis through their Lending Agent</td>
<td><strong>Specific Lender License (SLL)</strong></td>
<td><strong>1</strong></td>
<td><strong>SLL Member</strong>&lt;br&gt;• PGGM (Beneficial owner)&lt;br&gt;Agent lender&lt;br&gt;• BNY Mellon</td>
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<tr>
<td>Special / GC Repo / GC Pooling</td>
<td>• <strong>Specific Direct Membership for Repo and GC as direct participation model for non-banks place and/or take cash on a secured and centrally cleared basis</strong>&lt;br&gt;• cash investment (reverse repo)&lt;br&gt;• cash investment and –taking (reverse repo and repo)</td>
<td><strong>Specific Repo License (SRL)</strong></td>
<td><strong>2</strong></td>
<td><strong>SRL Member</strong>&lt;br&gt;• HDI (Cash provider)&lt;br&gt;• Airbus (Cash provider)</td>
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<td></td>
<td></td>
<td><strong>ISA Direct</strong></td>
<td><strong>3</strong></td>
<td><strong>ISA Direct Member</strong>&lt;br&gt;• PGGM Treasury B.V.&lt;br&gt;• Ronin Trading Europe LLP</td>
</tr>
<tr>
<td>OTC Derivatives</td>
<td>• Expansion of scope of eligible participants for full direct clearing membership&lt;br&gt;• <em>The ISA Direct model combines a direct clearing membership with elements of the traditional service relationship in client clearing</em></td>
<td><strong>ISA Direct</strong></td>
<td><strong>3</strong></td>
<td><strong>ISA Direct Member</strong>&lt;br&gt;• Swiss Life&lt;br&gt;• Bq. Cantonale Vaudoise</td>
</tr>
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<td></td>
<td><strong>Clearing Agent</strong>&lt;br&gt;• ABN AMRO Clearing&lt;br&gt;• Zürcher Kantonalbank</td>
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</tbody>
</table>
Specific Lender License / Specific Repo License tailored to risk profile of underlying transactions

1. Specific Lender License
   - Agent Lender (Beneficial Owner, Specific Lender License Holder) to Loan negotiation (Eurex Clearing)
   - Collateral Pledge or Transfer of Title/Pledge-back*
   - Loan securities
   - Pledge to Lender
   - Pledge to the CCP
   - Transfer of Title

2. Specific Repo License
   - Select Invest participant (Beneficial Owner, Specific Repo License Holder)
   - Cash (GC Pooling basket collateral)
   - Trade negotiation via Eurex Repo F7 (MTF)
   - Eurex Clearing AG (CCP)
   - Cash (GC Pooling basket collateral)
   - Margin Collateral

CCP has no credit risk towards
(a) Beneficial owner as lender in a securities lending transaction
(b) Cash Provider / Cash Investor
as in both models provided collateral remains with the CCP

*Beneficial Owner receives Non-cash Principal Collateral via Transfer of Title with a Pledge-back to the CCP

Therefore
- No initial margin (IM) requirement
- No default fund (DF) requirement
- No default management (DMP) obligation
The ISA Direct model combines a direct clearing membership with elements of a traditional service relationship in client clearing.

Direct contractual relationship between ISA Direct Client and CCP with a Clearing Agent providing mandatory and optional service functions.

**Initial focus on**
- Insurance and financial services companies
- Pension funds
- Asset Managers

Initially in following jurisdictions:
NL, UK, IE, CH, GER, LU, ES

**Access type characterized by a principal relationship between buy-side clients and the CCP**

**Existing Clearing Member acts as Clearing Agent**

**ISA Direct Member has to meet admission criteria equivalent to regular Clearing Members with extended servicing functions by the Clearing Agent**

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**Provision of operational services by Clearing Agent to ISA Direct Member**
- Default Fund contribution
- DMP obligation

**Transaction Management**
**Cash Management**
**Collateral Management**

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**Direct contractual relationship**
Core benefits of direct buy-side CCP access models

**Improved safety & resilience**

- Better protection of client assets
- Reduction of concentration in client clearing
- Improved portability in default scenarios
- Broadening of scope of general CCP benefits in regards to safety and resilience
- Access for non-banks to CCP cleared (reverse) repo in particular in stressed market conditions

**Economic perspective**

- Reduction of capital requirements and potentially improved return of capital for banks
- Consequently improved conditions for the buy-side firms
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