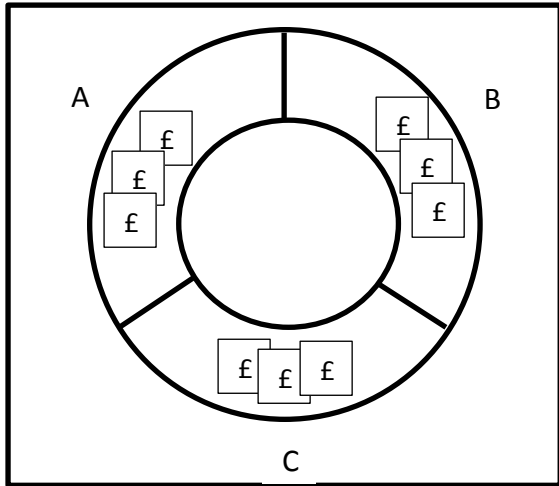
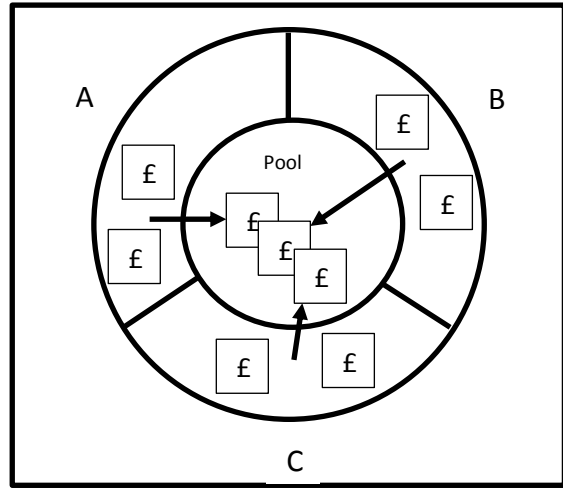


BOX 1

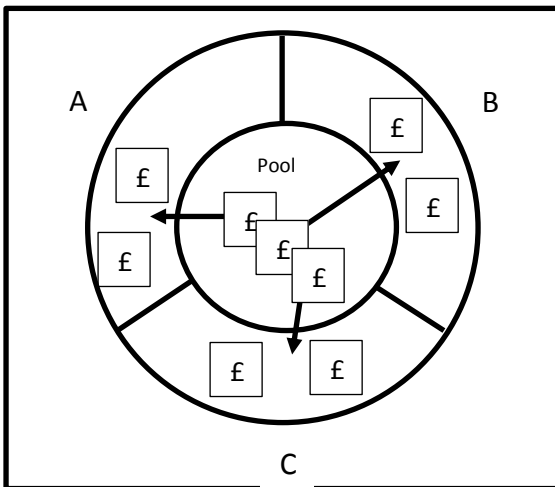
1. In a simple RTGS system, each bank has liquidity only on its own account from which to make its payments.



2. Let us suppose that there is a liquidity pool to which the banks contribute some of their liquidity (say £1 each). Any of A, B or C can now use the £3 units of liquidity in the pool to make payments to each other.



3. In normal circumstances, the pooled liquidity would be returned to A, B and C and the end of the day.

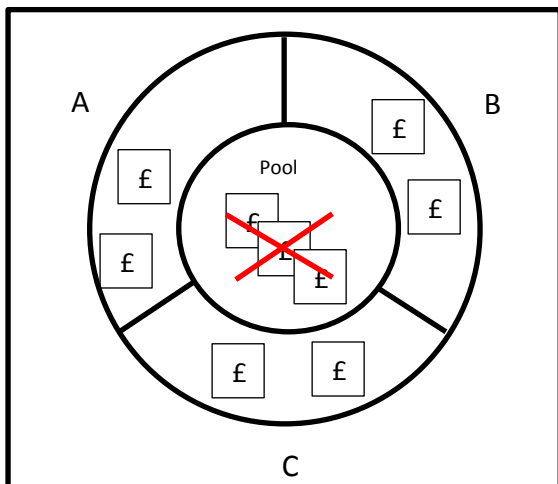


4. Say, during the day, A uses the pool to pay £3 to B. At that point A's net debit position (NDP) is also £3 (n.b. the maximum it can be in this example).

	Contribution to pool (£)	Net debit position (£)	Change in NDP
A	1	3	0 + 3
B	1	0	n/a
C	1	0	n/a

Memo: A pays £3 to B.

5. If A were to enter insolvency at this point, it would lose its £1 contribution to the pool; so too B and C – to extinguish the £3 NDP A created making its payment to B.



6. As members of the liquidity pool, how can B and C protect themselves from losing their contributions if A fails? The answer is: by themselves making payments using the pool. Let's say that (after step 4. above) B then pays £½ to A, and C pays £1½ to A.

	Contribution to pool (£)	Net debit position (£)	Change in NDP
A	1	1	3 - ½ - 1½
B	1	½	0 + ½
C	1	1½	0 + 1½

Memo: A first pays £3 to B. Then B pays £½ to A; and C pays £1½ to A.

7. If A failed at this latter point, it would lose its £1 contribution to the pool. But no further contribution from the pool would be needed to extinguish its NDP. So B and C would both have made their payments and not lost their contributions to the pool.