



Default handling procedure

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Introduction

This documents includes the version for publication of the EuroCCP Default Handling procedure for the Risk Management, Middle & Back Office, Finance, Legal & Compliance and Relationship Management departments and the Breach and Default Management Team of European Central Counterparty N.V. – further “EuroCCP”.

The purpose and scope of this document is to describe:

- Definitions
- Procedure description
- Roles & responsibilities

This procedure will be reviewed on a quarterly basis or if this is required by the respective situation.

European Central Counterparty N.V.

Definitions

The following capitalised terms shall, unless specifically defined otherwise, have the respective meanings set out below:

“**BDMT**” means Breach and Default Management Team, which is part of the Crisis Management Team “**CMT**”;

“**Clearing Participant**” means the written agreement entered into between EuroCCP and a Clearing Participants pursuant to article 4.4.1. in EuroCCPs’ Clearing rule book;

“**Client**” means any Person, which has opened accounts with respect to the trading of Securities in the Books of Clearing Participants, other than a Trading Participant;

“**Collateral**” means cash or such approved Financial Instruments as set out in the Regulation Collateral deposited in a Collateral Account or transferred to EuroCCP by way a title transfer financial collateral arrangement in accordance with the Regulation Collateral;

“**Collateral Account**” means a House Collateral Account, an Omnibus Client Collateral Account, or an Individual Client Collateral Account opened by a Credit Institution, CSD and/or central bank which is approved by EuroCCP, or by EuroCCP, in the name of the Clearing Participant in order to hold Collateral provided by the Clearing Participant by way of depositing approved Financial Instruments and/or cash to cover the Margin for the corresponding Position Account;

“**Competent Authority**” means anybody by which the Clearing Participant, a Co-operating Clearing House of EuroCCP is supervised

“**Co-operating Clearing House**” means a Person, which entered into a Link Agreement with EuroCCP with approval from the Competent Authority of EuroCCP;

“**EuroCCP**” means EUROPEAN CENTRAL COUNTERPARTY N.V.;

“**House Collateral Account**” means the Collateral Account holding Collateral to cover the Margin for the House Position Account;

“**Omnibus Client Collateral account**” means the Collateral Account holding Collateral to cover the Margin for the Omnibus Client Position Account;

“**Open Position**” means the net aggregated balance of the Trade Legs of a Clearing Participant, per ISIN code, per Position Account, per CSD account, per currency and per Settlement Date;

“**Statement of Authority**” means a statement of a Clearing Participants to EuroCCP that it authorises a specific Trading Participants to conclude Trades in the name of Clearing Participants, in the form as set out in the Regulation Statement of Authority;

“**Trading Participant**” means any Person which has been and is admitted by an Exchange as a participant of that Exchange as a broker and/or dealer;

Procedure Objective

The objective of this procedure is to ensure proper handling of a Clearing Participant default situation. *Note: a default situation can apply to a Clearing Participant as well as a Co-operating Clearing House¹.*

Proper handling of a default situation requires a structured approach:

- to ensure observance of the defaulting party's obligations towards EuroCCP;
- to minimize impact on the financial markets, Clearing Participants and EuroCCPs services and;
- to prevent losses for EuroCCP.

This procedure is tested and reviewed at least each quarter.

This procedure is also tested annually through a simulation exercise, based on a default scenario to assess its effectiveness.

Procedure Description

Crisis Management Team

This procedure starts when the decision to declare a default is already taken. The procedure to declare a Clearing Participant in default is described in "Breach of Rulebook procedure v1.6".

EuroCCP's Breach and Default Management Team (BDMT²), which is part of EuroCCP's Crisis Management Team (CMT), handles any default. The CMT is therefore responsible for taking appropriate measures in close cooperation with the relevant stakeholders, especially the Risk Management and Legal & Compliance departments.

Default Handling

The Crisis Management Team manages the default in four steps, through its CMT meetings:

CMT Meeting 1: define crisis management objectives and agree actions to achieve these.

The meeting starts as any crisis management meeting and follows the agreed crisis management methodology (see Crisis Management & Crisis Communications Plan). The BCM will hand out the Default Handling work instructions. The CMT then identifies the situation in clear terms so that all parties involved will have a single view of the situation at hand. The CMT defines the objectives that need to be achieved during the management of the crisis. Based on the situation and the objectives the CMT will agree the actions that need to be taken. The default handling work instructions provide detailed guidance that can be used to support the default management.

After each CMT meeting the Loggers or the Business Continuity Manager (BCM) produce a situational report (Sitrep). The Crisis Manager will approve the Sitrep and use that to inform the Supervisory Board and the Risk Committee.

The BCM also produces the Regulatory Sitrep. The Crisis Manager will approve the Regulatory Sitrep and Legal & Compliance sends it to the regulator.

Also after each meeting, the Corporate Secretary will record formal MB decisions.

These last three recurring tasks will be mentioned further in the document as "the standard CMT logging and communication tasks".

¹ For reasons of readability, we will only refer to Clearing Participants below but any reference to a Clearing Participant is also meant as a reference to a Co-operating Clearing House.

² The role of the BDMT is described in the "Breach of Rulebook procedure".

CMT Meeting 2: CMT declares or confirms a default for relevant CP's

At this point, it is known which CP or CP's are involved in the default and if any other entities are involved, like e.g. groups, mother companies, subsidiaries, daughters, etc.

In addition, it is known what the accounts and account structures are that are impacted and if portability agreements exist.

Last, it is known what the financial impact for EuroCCP might be of the defaulting CP's.

With this information the CMT will either declare or confirm the default(s).

Technical measures to be taken:

- Legal & Compliance to deliver declaration of default to defaulting CP's;
- Client Services to request Trading Platforms to revoke Statements of Authority;
- IT to revoke CP(s) Trade link in TVS.

Further, the CMT checks if any EuroCCP business processes are impacted by the default(s) and if the Liquidity Measures procedure needs to be activated.

Risk Management will inform the CMT about the expected financial result of close out after application of collateral against "Skin in the game" and delivers its advice for the Liquidation Strategy.

With this knowledge CMT then informs all staff by email and the stakeholders by Newsflash.

The standard CMT logging and communication tasks will be performed by OR&C, L&C and the Corporate Secretary.

CMT meeting 3: CMT decides on liquidation strategy

The CMT decides the liquidation strategy based on the advice received from Risk Management.

There are four possibilities, which can be used in combination:

1. Continue to settle (as in BaU);
2. Porting (see Portability work instruction);
3. Liquidate (see Liquidation work instruction);
4. Auctioning (see Auction work instruction).

Risk Management, together with Middle & Back Office, executes the liquidation strategy and keeps the CMT informed.

The standard CMT logging and communication tasks will be performed by OR&C, L&C and the Corporate Secretary.

CMT meeting 4: CMT evaluates financial results and decides on one of the below options.

Risk Management, together with Middle & Back Office checks the financial result of close out after application of collateral against "Skin in the game" and informs the CMT.

Based on the information the CMT applies one of the following four options:

1. No financial impact: Clearing Fund is sufficient;
2. Financial impact: SIG is sufficient; Clearing Fund is not used;
3. Financial impact: SIG is not sufficient; Clearing Fund is used.
4. Financial impact: SIG + Clearing Fund is not sufficient.

1. No financial impact: Clearing Fund is sufficient

The CMT agrees that following actions will be taken:

- The CMT informs the customers (i) and other relevant stakeholders that there is no financial impact and therefore the Clearing Fund is not being used;
- Middle & Back Office returns collateral and results of close out activities;
- Legal & Compliance terminates (j) the Clearing Agreement(s) with the defaulting parties.

2. Financial impact: SIG is sufficient; Clearing Fund is not used

The CMT agrees that following actions will be taken:

- The CMT informs (k) the customers and other relevant stakeholders that there is financial impact and therefore the Clearing Fund will be used;
- Legal & Compliance files a claim (l) with the administrator;
- Legal & Compliance terminates (j) the Clearing Agreement(s) with the defaulting parties.

3. Financial impact: SIG is not sufficient; Clearing Fund is used

The CMT agrees that following actions will be taken:

- The CMT decides that replenishment of the Skin In the Game is needed;
- Risk Management activates the Maintenance own resources default waterfall procedure;
- The CMT informs (m) the customers and other relevant stakeholders that there is financial impact and therefore the Clearing Fund and the SIG will be used;
- Client Services prepare and send individual assessments (n) to the clients informing them of their financial impact;
- Legal & Compliance files a claim (l) with the administrator;
- Legal & Compliance terminates (j) the Clearing Agreement(s) with the defaulting parties.

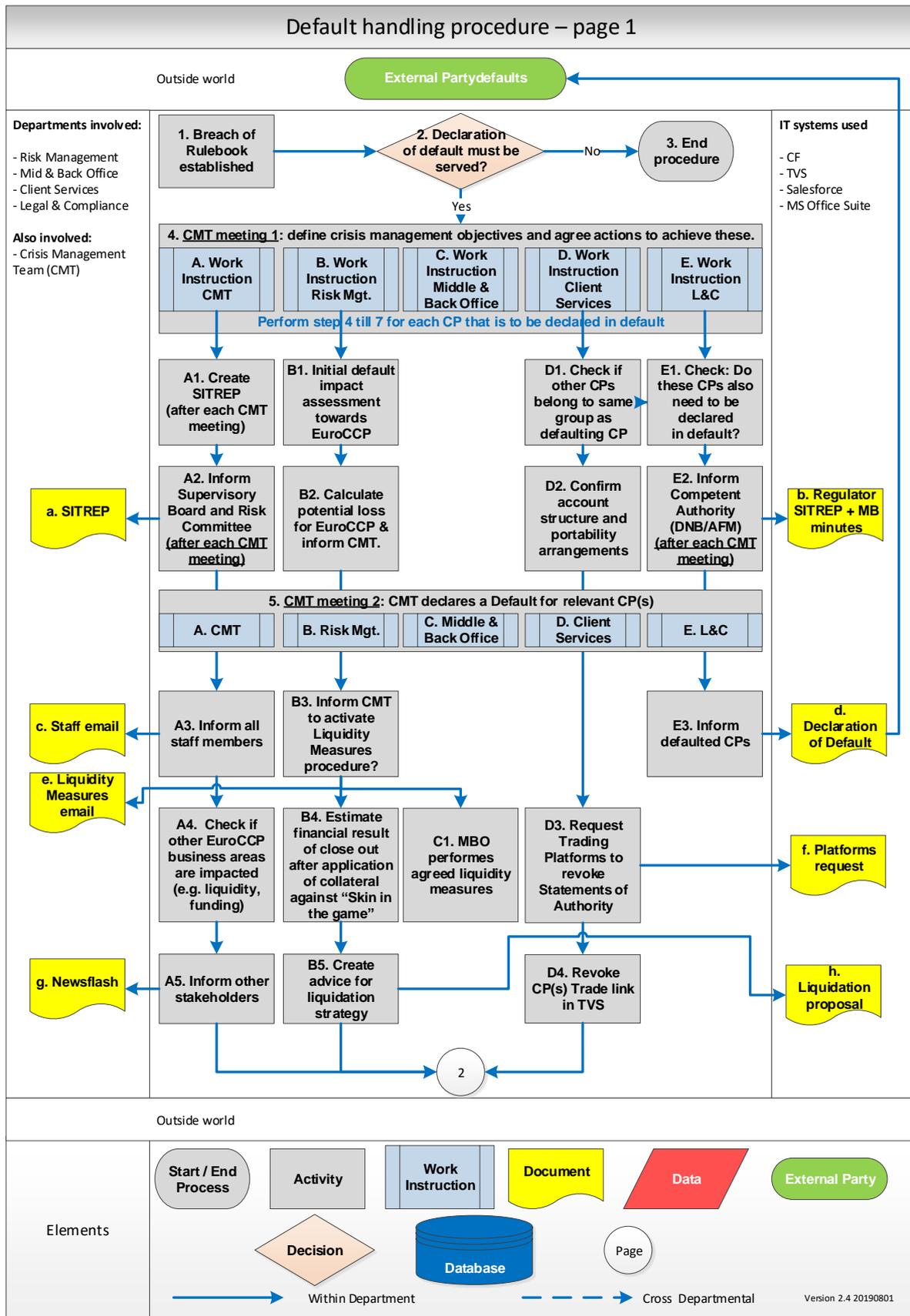
4. Financial impact: SIG + Clearing Fund is not sufficient

The CMT activates the Recovery Plan.

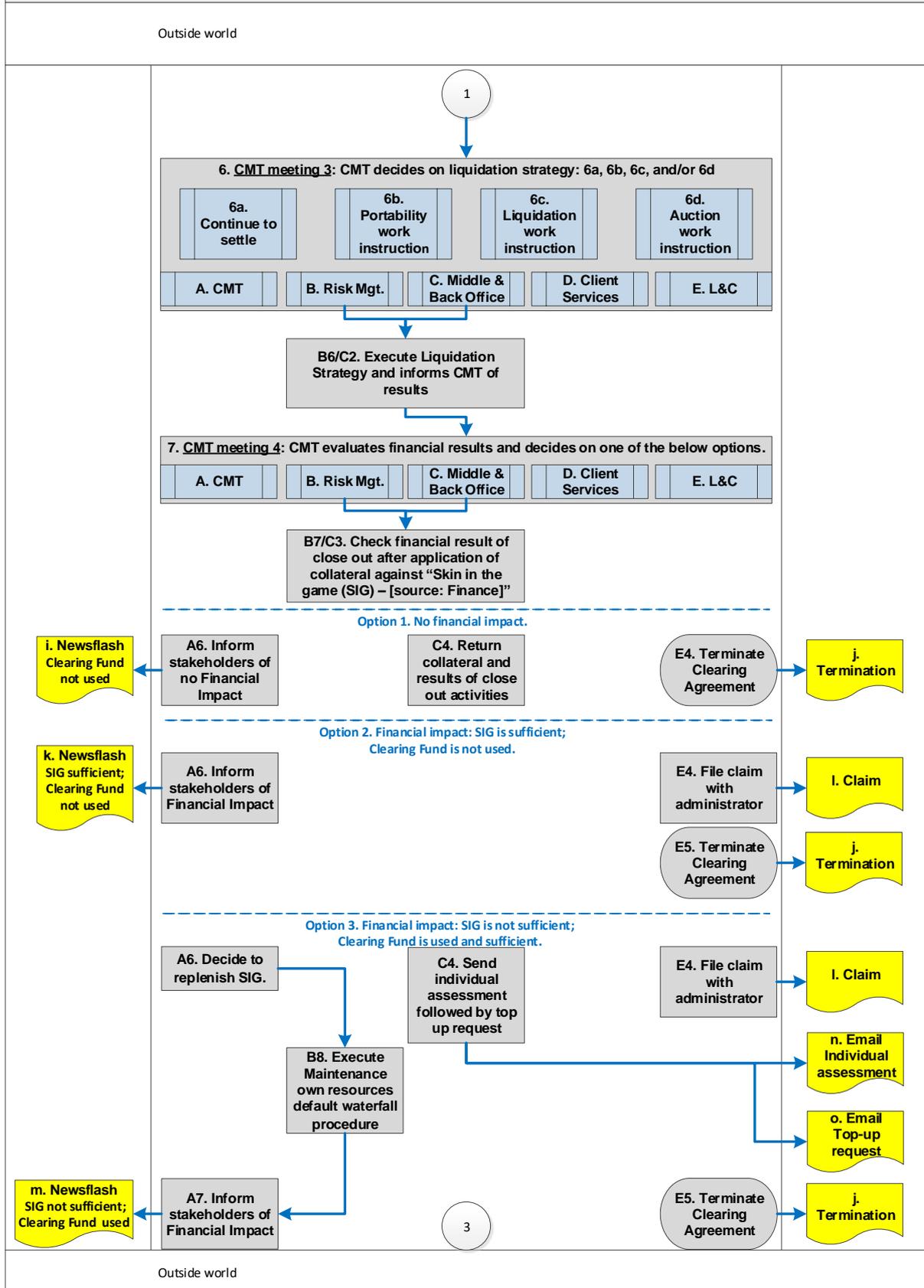
The standard CMT logging and communication tasks will be performed by OR&C, L&C and the Corporate Secretary.

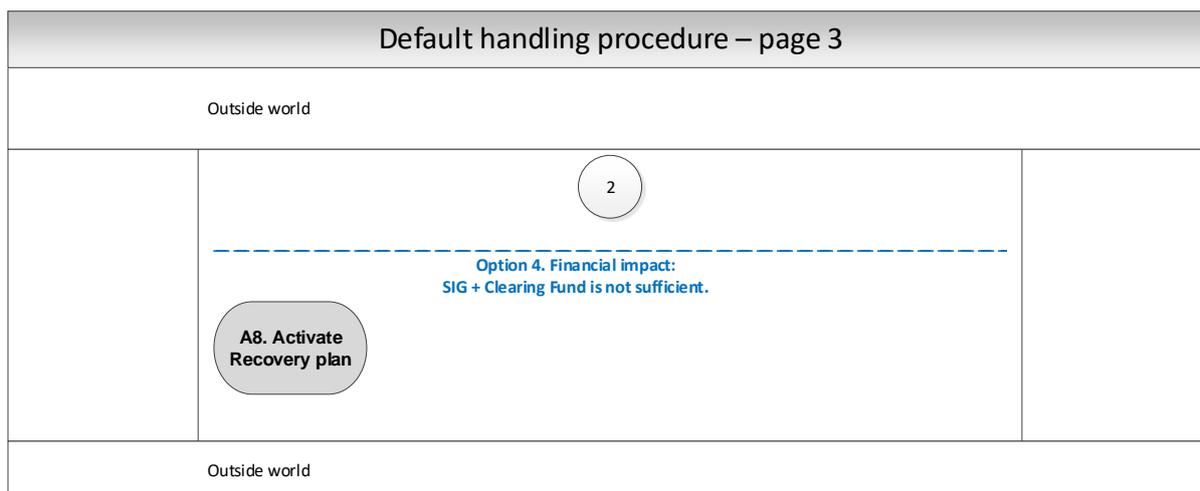
This ends the procedure.

Flowchart



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Roles and responsibilities

RACI ³ .	Role	Responsibility	3LoD
R	Middle & Back Office	Monitoring Clearing Rulebook breaches by CP's, performing Middle & Back Office Default Handling work instruction	1LoD
R	Client Services	Performing Client Services Default Handling work instruction	1LoD
R	Risk Management	Monitoring Clearing Rulebook breaches by CP's, activating the Default Handling procedure, performing Risk Management Default Handling work instruction	2LoD
R	Legal & Compliance	Performing Legal & Compliance Default Handling work instruction	2LoD
A	CMT	Manages the default handling process	1LoD
C	OR&C	Provide Crisis Management process guidance to CMT when needed for this procedure	2LoD
I	Internal Audit	Monitor how the procedure was dealt with	3LoD

³ Responsible / Accountable / Consulted / Informed