

ICE Clear Europe Response

Questionnaire for CDS CCPs on Protection of Customer Initial Margin

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I. ICE Clear Europe Solution Development Approach

ICE Clear Europe Limited, (“**the clearing house**”) has a pre-existing legal and operational framework for providing segregation of initial margin of Customers of Clearing Members (non-members) and portability of Contracts entered into by Clearing Members with the clearing house on behalf of their Customers (the "Non-Member Framework"). In developing its framework further for credit default swap contracts ("**CDS**"), ICE Clear Europe is consulting extensively with numerous buy-side participants, its existing members, as well as with its principal regulators.

ICE Clear Europe's rulebook provisions enabling the segregation of Customer Accounts are already operating for energy contracts cleared by it and would apply equally to CDS contracts. However, the relevant provisions are currently "switched off" in the rulebook pending operational readiness. The relevant provisions comply with applicable UK statutory requirements for customer account segregation, including under the Financial Services Authority ("FSA")'s Customer asset rules and the Financial Services and Markets Act 2000 (Recognition Requirements for Investment Exchanges and Clearing Houses) Regulations 2001.

ICE Clear Europe's approach to protection of customer initial margin is subject to regulatory approval.

II. Factual Matters

A. Structure of ICE Clear Europe

ICE Clear Europe is a limited liability company established under the laws of England and Wales. It is a recognised clearing house for purposes of the Financial Services and Markets Act 2000, supervised by the FSA. It has also been designated by the FSA as a “designated system” for purposes of the Financial Markets and Insolvency (Settlement Finality) Regulations 1999 (“Settlement Finality Regulations”) and Directive 98/26/EC on Settlement Finality in Payment and Securities Settlement Systems, providing it with Europe-wide insolvency law protections. It has been given the status of a multilateral clearing organisation by the Commodity Futures Trading Commission in the United States of America. The implementation of the Non-Member Framework will require review by the FSA and may require additional exemptive relief from the Securities and Exchange Commission.

B. Clearing Members

The clearing house limits its Clearing Members (“**CM**” or “**Member**”) to persons who are able to meet the required membership criteria set out in Rule 201, some of which are outlined below. In order to attain and maintain membership as a clearing member (“Clearing Member”), including a CDS Clearing Member, a person must, at a minimum, as from the date on which it is proposed that it becomes a member, among other things:

- Hold sufficient capital;
- Be party to a Clearing Membership Agreement (as defined in the Rules);
- Hold all necessary regulatory authorisations, licenses, permissions and approvals;
- Satisfy ICE Clear Europe that it and its directors and officers satisfy requirements of an “approved person” under FSA rules;
- Have appropriate technical and operational systems and controls;
- Have appropriate business continuity procedures;
- Hold an account or accounts (as necessary) at a financial institution that is a member of ICE Clear Europe’s payment system in relation to each of which a direct debit mandate has been established in favour of ICE Clear Europe;
- Be able to meet margin requirements;
- Have contributed the minimum requested amount to the Guaranty Fund (defined in the Rules); and
- Not be subject to insolvency or other event of default.

The following additional requirements are specified in the CDS Procedures for the purposes of becoming a CDS Clearing Member:

- It has a minimum of \$5 billion of capital; provided that this requirement may, at the discretion of ICE Clear Europe, be met by a direct or indirect parent of such CDS Clearing Member that is acceptable to ICE Clear Europe (“Parent”) if such Parent provides a guarantee in accordance with the Finance Procedures.
- At the time of admission, it has a minimum long-term senior unsecured debt rating of at least the following from each of the following rating agencies (or any successor to the rating business thereof) that provides such a rating (with a

minimum of one such rating): (i) “A2” from Moody’s Investors Service (“Moody’s”), (ii) “A” from Standard & Poor’s Ratings Services (“S&P”), a division of The McGraw-Hill Companies, Inc., (iii) “A” from Fitch Ratings (“Fitch”) or (iv) the equivalent rating from any other rating agency that ICE Clear Europe designates from time to time for this purpose; provided that, if such applicant does not have such a rating from any of the foregoing rating agencies, it demonstrates to ICE Clear Europe that it otherwise satisfies, in the discretion of ICE Clear Europe, stringent credit criteria, such satisfaction to be confirmed by an examination of its books and records, then this requirement will be met; provided further that this requirement may, at the discretion of ICE Clear Europe, be met by Parent if such Parent provides a guarantee in accordance with the Finance Procedures;

- At no time after admission, does it (or, if applicable, its Parent) have a long-term senior unsecured debt rating below the following from any of the following rating agencies (or any successor to the rating business thereof) or, at the discretion of ICE Clear Europe, does any such rating agency suspend or withdraw such rating: (i) “Baa2” from Moody’s, (ii) “BBB” from S&P, (iii) “BBB” from Fitch or (iv) the equivalent rating from any other rating agency ICE Clear Europe designates from time to time for this purpose or, if applicable, it or its Parent ceases to satisfy objective criteria established by ICE Clear Europe at its discretion;
- It is a member of industry organisations related to CDS, as designated by ICE Clear Europe from time to time for this purpose, which as at the date of launch of CDS clearing by ICE Clear Europe are ISDA and Deriv/SERV;
- It has executed an agreement with ICE Clear Europe in the form set out in paragraph 10 of the CDS Procedures; and
- If it is not incorporated in England and Wales, it has appointed an agent for service of process pursuant to Rule 113(e).

These requirements are consistent with the Financial Services and Markets Act 2000 (Recognition Requirements) Regulations 2001 (as amended) and FSA rules applicable to RCH (“Recognition Requirements”).

As noted above, ICE Clear Europe does not limit CMs by jurisdiction, legal entity type or type of regulatory or supervisory authority, although each CM (either itself or as part of a holding company group) must have necessary regulatory authorisations, licences, permissions and approvals. For CMs based in the United States, regulatory and supervisory authorities generally include the Federal Reserve as supervisory authority at the holding company level and, for CMs that are banks, the OCC or another appropriate supervisor. For CMs licensed in the United Kingdom, the FSA would generally be the principal regulatory and supervisory authority. CMs organized in other jurisdictions may be subject to banking or securities regulatory authorities in those jurisdictions.

C. Structure of Custodians

1. ICE Clear Europe Custodians

Currently, ICE Clear Europe uses JPMorgan Chase, as custodian for assets transferred to it. JPMorgan Chase is regulated by the FSA, among others. ICE Clear Europe may from time to time use other custodians.

ICE Clear Europe's rules do not restrict the custodians that ICE Clear Europe may use.

2. Clearing Member Custodians

The clearing house rules require that CMs transfer the full amount of clearing house-required margin to the clearing house by title transfer pursuant to a "title transfer financial collateral arrangement" for purposes of the Directive 2002/47/EC on Financial Collateral Arrangements. As a result, Custodians do not act for the Clearing Members. The clearing house holds margin with relevant custodians at each ICSD or CDS.

D. Structure of Customers

The clearing house rules do not restrict the organisational type or jurisdiction of organisation of customers of Clearing Members. ICE Clear Europe does not monitor the various regulatory or supervisory authorities to which customers may be subject.

E. Expansion/Restriction of Permitted Entity Types

The clearing house considered netting implications, regulatory capital implications, operational impacts, adverse pass through effects, legal regime impacts and other factors in drafting its rules applicable to eligible CMs. As a general matter, the clearing house's membership criteria to ensure that firms have the resources, controls and sophistication to participate in the central clearing function. CMs are required to meet membership criteria designed to ensure each CM has sufficient operational capabilities, financial resources, risk management experience and regulatory oversight to be permitted to meet the clearing house's membership criteria. This requirement is in keeping with regulatory guidance from the Bank of International Settlements ("BIS")¹.

This approach is intended to manage counterparty exposure at the clearing house and to minimise operational disruptions in moving positions to the clearing house following an insolvency of a CM.

In accordance with its rules for admission of new CMs, ICE Clear Europe expects that it would focus on these factors, including the appropriate legal and insolvency framework, in the event that new types of CM or CMs in other jurisdictions seek to become members of ICE Clear Europe. As noted above, ICE Clear Europe would seek a legal opinion as to relevant matters under the law applicable to the new CM or type of CM, including in the event of its insolvency.

¹ The BIS Committee on Payment and Settlement Systems and Technical Committee of the International Organisation of Securities Commissions (IOSCO) published "Recommendations for Central Counterparties" Recommendation 2 states "A CCP should require participants to have sufficient financial resources and robust operational capacity to meet obligation arising from participation in the CCP. A CCP should have procedures in place to monitor that participation requirements are met on an ongoing basis. A CCP's participation requirements should be objective, publicly disclosed, and permit fair and open access."

III. Segregation and Safekeeping of Initial Margin

A. Initial Margin Held by the clearing house

1. Composition of ICE Clear Europe Margin

The clearing house's policies regarding the acceptable forms of non-cash collateral for Initial Margin and their associated haircuts are designed to provide protection for liquidity risk. In establishing acceptable collateral, the clearing house considers the liquidity of funds in the event of a CM default and evaluates how quickly funds would be available to cover CM post insolvency losses. The principal consideration in determining eligible CCP Required Margin was the protection of the clearinghouse and the clearing system as a whole. The clearing house established the following acceptable collateral for Initial Margin:

i. Acceptable Collateral

Acceptable forms of "Permitted Cover" are set out in ICE Clear Circulars from time to time.² Cash collateral is acceptable in U.S. dollars, Euros and pounds sterling. Acceptable Forms of non-cash collateral for Initial Margin include UK, French, German, US, Belgian and Netherlands government bonds

The following factors, among others, are taking into account in considering any modifications to the list of acceptable Permitted Cover:

- There must be adequate demand for acceptance of the collateral form among current Clearing Members;
- An active secondary market with reasonable sized bids must exist;
- An accurate, reliable and timely price information source must be available to ICE Clear Europe from an independent third party vendor; and
- The clearing house must be capable of obtaining a perfected security interest in the collateral type.
- Appropriate withholding tax authorisation must be completed prior to the forwarding of coupon settlements to the beneficial owner.

Additional margin will be called if the Clearing Member does not maintain the appropriate minimums by asset type (regardless of whether the total sum of Permitted Cover meets the total Margin obligation).

ii. Collateral Haircuts

To manage the risk created by the uncertainty surrounding the future value of collateral, the initial value of the collateral is discounted or in other

² Most recent circular is available at:
https://www.theice.com/publicdocs/clear_europe/circulars/C09015_att.pdf

words, a haircut is applied. If margin requirements are covered by cash in a different currency to the underlying contract a foreign exchange (FX) haircut is applied to account for fluctuations in exchange rates. In terms of Government bonds, a haircut is applied to cover movements in the price of the securities. The current Permitted Cover list with the corresponding haircuts is set out below.

The haircut is calculated based on the general risk method principles used to calculate margin, i.e. the parametric Value-at-Risk (VaR) and historical simulation approach, and should secure a potential move in collateral prices and currency rates at a confidence level, over a 2-day period, of at least 99.9%.

For eligible currencies, the haircut is derived by analysing historic dollar, euro and sterling spot rates which are collected from Bloomberg for the previous three year period. Assuming a normal distribution for the parametric approach, we calculate the standard deviation using the worst of the one or two day price move and scaling this up by 3.09 to get to a 99.9% confidence level. We also calculate in parallel to the parametric approach a historical simulation VaR covering the largest profits and losses (“fat-tail”) in the given time interval. The historical VaR of 1000 days is the worst value observed.

For Government securities, the haircut is derived using the same principles as for currency haircuts. However, in this instance the potential yield shift is calculated to determine how sensitive bond prices are to changes in yield. This is done by taking a 3 year history of Euro, Sterling and Dollar denominated swap rates and calculating the yield VaR for the selected maturities.

The determined yield shifts are then used with the duration of each security in issue to estimate the change in bond prices and hence the haircut. To ensure that the haircuts are sufficient a backrest of a selection of securities is carried out. In the event that the derived haircut does not cover the largest movement in price over the time period, then this value should be taken as the haircut.

Government Securities				
Description	Bloomberg Ticker	Jurisdiction	Maturity	Haircut
Belgian Treasury Bills	BGTB	Belgium	<3 years	3%
Belgian Treasury Bills	BGTB	Belgium	<11 years	5%
Belgian Treasury Bills	BGTB	Belgium	>11 years	7%
Belgian Government Bonds	BGB	Belgium	<3 years	3%
Belgian Government Bonds	BGB	Belgium	<11 years	5%
Belgian Government Bonds	BGB	Belgium	>11 years	8%
Bons du Tresor a Taux Fixe et Interet Precompte	BTF	France	< 3 years	3%
Bons du Tresor a Taux Fixe et Interet Annuel	BTNS	France	< 3 years	3%
Bons du Tresor a Taux Fixe et Interet Annuel	BTNS	France	< 7 years	4%
Bons du Tresor a Taux Fixe et Interet Annuel	BTNS	France	<11 years	5%
Bons du Tresor a Taux Fixe et Interet Annuel	BTNS	France	>11 years	7%

Obligations Assimilables du Tresor	FRTR	France	< 3 years	3%
Obligations Assimilables du Tresor	FRTR	France	< 7 years	4%
Obligations Assimilables du Tresor	FRTR	France	<11 years	5%
Obligations Assimilables du Tresor	FRTR	France	>11 years	9%
German Treasury Bill	BUBILL	Germany	< 3 years	3%
German Schatz	BKO	Germany	< 3 years	3%
German Bunds	DBR	Germany	< 3 years	3%
German Bunds	DBR	Germany	< 7 years	4%
German Bunds	DBR	Germany	<11 years	5%
German Bunds	DBR	Germany	>11 years	10%
German Bobl	OBL	Germany	< 3 years	3%
German Bobl	OBL	Germany	< 7 years	4%
German Bobl	OBL	Germany	<11 years	5%
German Bobl	OBL	Germany	>11 years	7%
German Treuhand	THA	Germany	< 3 years	3%
German Treuhand	THA	Germany	< 7 years	4%
German Treuhand	THA	Germany	<11 years	5%
German Treuhand	THA	Germany	>11 years	7%
Dutch Treasury Certificate	DTB	Netherlands	<3 years	3%
Dutch Treasury Certificate	DTB	Netherlands	<11 years	5%
Dutch Treasury Certificate	DTB	Netherlands	>11 years	7%
Dutch Government Bond	NETHER	Netherlands	<3 years	3%
Dutch Government Bond	NETHER	Netherlands	<11 years	5%
Dutch Government Bond	NETHER	Netherlands	>11 years	8%
UK Gilt	UKT	UK	< 3 years	3%
UK Gilt	UKT	UK	< 7 years	4%
UK Gilt	UKT	UK	<11 years	5%
UK Gilt	UKT	UK	>11 years	8%
UK Treasury	UKTB	UK	< 3 years	3%
United Kingdom Inflation Indexed Gilt Bond	UKTI	UK	< 3 years	3%
United Kingdom Inflation Indexed Gilt Bond	UKTI	UK	< 7 years	4%
United Kingdom Inflation Indexed Gilt Bond	UKTI	UK	<11 years	5%
United Kingdom Inflation Indexed Gilt Bond	UKTI	UK	>11 years	7%
US Treasury	B	USA	< 3 years	3%
US Bonds	T	USA	< 3 years	3%
US Bonds	T	USA	< 7 years	4%
US Bonds	T	USA	<11 years	5%
US Bonds	T	USA	>11 years	9%
US Treasury Inflation Indexed Note/Bond	TII	USA	< 3 years	3%
US Treasury Inflation Indexed Note/Bond	TII	USA	< 7 years	4%
US Treasury Inflation Indexed Note/Bond	TII	USA	<11 years	5%
US Treasury Inflation Indexed Note/Bond	TII	USA	>11 years	7%
Others				
Eligible currencies	GBP, USD, EUR			5.5%
Certificate of Deposit (CD)	Certificates of Deposit are accepted exceptionally on request for a limited range of issuers. The clearing house will assess each request individually and confirm or decline acceptance on a case by case basis			
Letter of Credit (LC)	Letters of Credit may be used to cover Margin requirements only. Not more than 50% of a Clearing Member's total Margin requirement may be covered using Letters of Credit.			

2. Relationship Between CCP, CM and Customer

CMs act as principals vis-à-vis both the clearing house and Customers. This approach is consistent with, and builds on, the existing structure of the OTC

CDS market and is also consistent with the existing rulebook structure for energy clearing. As is the case with most clearing houses, ICE Clear Europe has a direct, principal relationship only with its CMs. CMs therefore have back-to-back principal contracts with Customers in connection with any contracts with the Clearinghouse which are entered into with their customers. The clearing house does not enter into cleared contracts with customers of CMs.

The Rules do not currently contemplate that customers will be permitted to clear transactions through non-CM affiliates of CMs.

B. Proposed Clearing Structure

The basic methodology of the clearing house clearing structure is outlined in Sections 1 to 10 below.

1. Clearing of CDS

Upon acceptance of a transaction for clearing, two new contracts arise, one between the clearing house and the Clearing Member that is the protection seller and the other between the clearing house and the Clearing Member that is the protection buyer. The clearing house requires Members to post margin (i.e. collateral) to secure their obligations to the clearing house under cleared contracts.

2. Basic Non-Member Framework

Pursuant to the Rules, the clearing house is establishing a framework that provides certain protections of clearing for CDS transactions entered into by customers of Clearing Members ("Customers"), including the segregation of margin posted by CMs for positions recorded in segregated accounts and provisions to enhance the transferability, or "portability," of such transactions in the event of a Member insolvency (the "Non-Member Framework").³

Under the Non-Member Framework, the Rules generally distinguish between Customer-generated open Contracts, treated by the Rules as being for the Clearing Member's Customer Account ("Customer Positions") and proprietary Contracts, treated by the Rules as being for the Clearing Member's Proprietary Account ("Proprietary Positions") for each Clearing Member. Customer Positions are cleared CDS transactions between the clearing house and the Member that are offset or mirrored on a back-to-back basis by a CDS transaction between the Member and a Customer and are designated by the Clearing Member as Customer Account transactions (a "Customer Transaction"). Proprietary Positions are all other cleared CDS transactions between the Clearing Member and the clearing house.

Both Customer Positions and Proprietary Positions represent principal-to-principal transactions between the Clearing Member and the clearing house.

³ clearing house rules will not preclude a Customer from trading with a Member on a bilateral, non-cleared basis.

In addition, where a Clearing Member enters into Customer Transactions, it will also enter into a back-to-back principal-to-principal transaction between it and the Customer ("Customer-Member Transaction"). Pursuant to the Rules, the clearing house has no direct relationship with, or liability to, Customers, in respect of Customer Positions, Customer Transactions, Customer-Member Transactions or otherwise.

The clearing house will record each Customer Position submitted by a Clearing Member to the clearing house in the Customer Account. It will permit Clearing Members to identify and close out offsetting Customer Positions that reflect positions corresponding to the same Customer. Notwithstanding that the clearing house may in this manner retain records of "gross" Customer Positions across different Customers, the obligations of each of the clearing house and the Member to the other at any time in respect of Customer Positions (for example, to make payments under CDS) will be determined on a net basis.

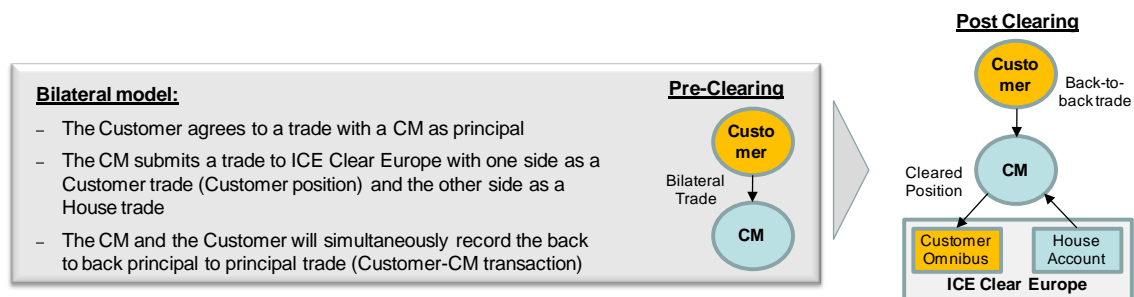
3. Submission of Customer Positions to the clearing house

Customer Positions may be submitted for clearing in two ways. In order for a cleared Contract to arise between the clearing house and a relevant Clearing Member, the Customer is required to be a customer of a Clearing Member. In each case the contractual arrangements between clearing house and Clearing Member and Clearing Member and Customer is as principal.

i. Bilateral Model

The Customer would execute a trade with a Clearing Member, each acting as principal. The Clearing Member submits a back-to-back trade to the clearing house. Upon acceptance, this would be treated by the clearing house as giving rise to two Contracts of economically opposite effect to one another. One would be recorded as a Customer Position and would mirror the Customer-Member Transaction and an exactly offsetting Contract would be recorded as a Proprietary Position.

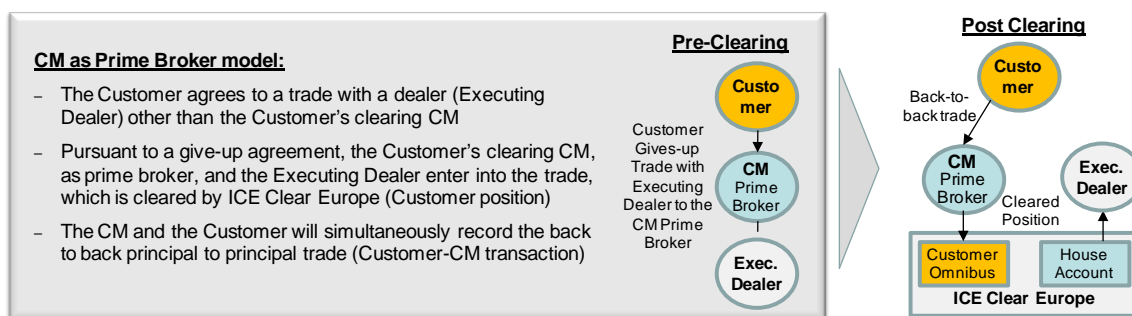
ICE Clear Europe Bilateral Model



ii. Member as a Prime Broker

The Customer agrees to a trade with a Clearing Member (the “Executing Dealer”) which is a different Clearing Member from the Clearing Member used by the Customer when submitting Customer-Member Transactions to the clearing house. Pursuant to a give-up agreement, the Customer’s Clearing Member, as prime broker, and the Executing Dealer enter into an over-the-counter trade, which is then submitted to the clearing house for clearing. The Clearing Member and the Customer would simultaneously enter into a back-to-back Customer-Member Transaction. The leg of the cleared transaction between the clearing house and the Customer’s Member would be treated as a Customer Position.⁴ The other Clearing Member that was the Customer's original counterparty would have an additional contract in its Proprietary Position.

The clearing house Prime Broker Model



If a Customer-Member Transaction is terminated because of a default by the Customer or otherwise, the related Customer Position would by its terms remain in place. However, the Clearing Member could enter into an offsetting trade with another Clearing Member and submit that for clearing in order to come out of the position. In order to do so, the Member may need to change the relevant Customer Position into a Proprietary Position. If this were to take place, margin requirements would automatically change as between the Customer Account and the Proprietary Account, so the Clearing Member would be able to do so only in accordance with applicable laws applicable to it relating to segregation.

4. Customer Accounts

The clearing house maintains separate margin accounts for each Member for Proprietary Positions and Customer Positions. Initial margin for Proprietary

⁴ In this scenario, the opposite leg between the clearing house and the Executing Dealer would be a Proprietary Position. If the executing dealer were clearing through another Clearing Member, the leg between the clearing house and the executing dealer’s Clearing Member would be a Customer Position as regards the executing dealer’s Clearing Member. If the executing dealer is the same legal entity as the prime broker, the result would be the same as in the bilateral model above.

Positions is posted to the proprietary account (the “Proprietary Account”) on a net basis and held as under the current Rules. Initial margin for Customer Positions of a Member is posted to a segregated Customer Account (the “Customer Account”) for that Clearing Member. The Customer Account is segregated from any other assets transferred to the clearing house by a Clearing Member, including assets transferred to the clearing house for credit to the Proprietary Account.⁵

For purposes of the Rules, the Customer Account includes a cash collateral account for cash margin and a custody account for securities collateral (if any). The cash collateral account is that through which all Customer-related cash payments are made. It will include in it all initial margin posted as cash by the Member in respect of Customer Positions (including cash posted to the Member by the Member’s Customers in respect of related Customer Transactions and transferred by the Member to the clearing house in respect of such Customer Positions). Clearing Members may use the same Customer Account for both energy and CDS customer payments, or may alternatively use two Customer Accounts, one for CDS and one for energy.

Cash in the cash collateral account may be applied by the clearing house to the obligations of the Member in respect of Customer Positions. The custody account linked to the Customer Account will hold any non-cash assets transferred to the clearing house by the Member in respect of Customer Positions. This may include non-cash assets received by a Clearing Member from that Clearing Member’s Customers as collateral for Customer-Member Transactions and passed on to the clearing house in respect of related Customer Transactions. The clearing house uses outside financial institutions as custodians (currently, JPMorgan) and records the name of the Clearing Member on each account for administrative convenience. The assets transferred to the clearing house and credited to the Customer Account will secure the Clearing Member’s obligations to the clearing house in respect of Customer Positions.

Pursuant to the Rules and Clearing Membership Agreement, both cash and non-cash collateral transferred to the clearing house becomes the property of the clearing house pursuant to a “title transfer financial collateral arrangement” for purposes of the Directive 2002/47/EC on Financial Collateral Arrangements. As a result, all Customer Account assets transferred to ICE Clear Europe must be held as proprietary assets of the CM or under some other arrangement pursuant to which the CM has a right to rehypothecate and transfer the assets to ICE Clear Europe outright. Although ICE Clear Europe receives an outright transfer of the assets, it passes interest payments to the Clearing Member.

⁵ In the circumstance where a Clearing Member collects margin from a Customer and posts different margin to the clearing house in respect of the related Customer Position, the Clearing Member would retain an interest in such margin. Clearing Members will be required under the Rules to maintain records of any such interest.

5. Clearing house Margining and Excess Account

For purposes of margining Customers, however, each Member will collect margin on a “gross” basis (that is, the Member will be permitted to net across multiple Customer Transactions of the same Customer, but not across different Customers). However, each Member will be required to post to the clearing house in the Customer Account initial margin on a “net” basis across all Customer Positions held in that account (“ICE Net”), whether for the same or different Customers, in the same manner as generally required for Proprietary Positions.⁶ The Rules do not specifically limit the clearing house's ability to demand additional, special margin at any time from a CM.

The clearing house will enable each Clearing Member, at the Customer's request to transfer to an Excess Margin Account the difference between the aggregate “gross” margin required from Customers and the net margin required by the clearing house to be posted to the Customer Account (such excess, the “ICE Excess”).

The CM will be required to maintain records showing the amount and form of excess margin held in the Excess Margin Account in respect of positions of each relevant Customer (the “Customer Excess Margin Amount”).⁷

The Customer Excess Margin Amount would be held in a separate account from the Customer Account and pursuant to separate legal entitlements. Excess collateral would be held by ICE Clear Europe effectively as banker (in relation to cash) and effectively as custodian (in relation to non-cash assets) for the benefit of the Clearing Member. The Clearing Member would hold its rights to return of such assets on trust for Customers such that such assets would fall outside its insolvency estate.

In the event of a default by a Customer under a Customer Transaction, the CM will be permitted to withdraw up to the Customer Excess Margin Amount for that Customer and apply it to amounts owed by the Customer under the Customer Transaction. Only the defaulting Customer's Customer Excess Margin Amount may be so used; margin posted by other Customers may not be used by the CM. The CM will also be permitted to withdraw amounts from the Excess Margin Account (not to exceed the Customer Excess Margin Amount) when required to be returned to the Customer under the Customer Transaction. The CM may transfer amounts in the Excess Margin Account (taken from Customer Excess Margin Amounts of different Customers on a pro rata basis (determined excluding any CP Excess held in the Excess Margin

⁶ We note in this regard that the clearing house's exposure to the Member, and the Member's exposure to the clearing house, in respect of Customer Positions will also be determined on a net basis across all Customer Positions in aggregate by Customer Account.

⁷ CMs will be required to provide reports or otherwise make information available as to such amounts to both ICE Clear Europe and the relevant Customers.

Account)) to the Customer Account as necessary to satisfy the ICE Net margin requirement for Customer Positions. It would also be able to transfer the assets recorded in the Excess Margin Account together with contracts and margin following an event of default. The CM will not otherwise be permitted to use or rehypothecate amounts in the Excess Margin Account.

6. Customer Transaction Documentation

Customer Transactions will be documented pursuant to a separate ISDA Master Agreement between the Customer and Clearing Member dealing only with ICE Clear Europe cleared contracts (and not with any other derivatives). In order for a Customer Transaction to be eligible for clearing, the relevant Customer-Member Transaction will be required to include a standard annex in the form approved by the clearing house under the Rules (the “Standard Annex”).

Under the Standard Annex, Customer-Member Transactions will for certain purposes be treated separately from other derivatives between the Customer and the Member (“Other Trades”). Specifically, Customer-Member Transactions will be subject to the separate clearing house margin requirements discussed below. In addition, the Standard Annex will include a standard definition of Clearing Member default, which will be based on a determination by the clearing house under the Rules that a Clearing Member is subject to an Event of Default.⁸

The Standard Annex will also specify procedures for the exercise of remedies in case of a Clearing Member default. If Default Portability Rules are to apply, the Standard Annex will include an agreement and consent on the part of the Customer, for the benefit of ICE Clear Europe, for ICE Clear Europe to transfer Customer-Member Transactions to a new Clearing Member following default. The Customer will also agree not to exercise termination rights during the Transfer Period (as defined below). In the event the Customer-Member Transaction is terminated as a result of a Clearing Member default, the termination value will be equal to the termination value of the related Customer Position as determined by ICE Clear Europe. To facilitate portability, in the event of a Member default, termination amounts owed in respect of Customer Transactions will not be netted against termination amounts owed in respect of Other Trades.

⁸ The Standard Annex would not have a standard definition for Customer defaults, which would be subject to bilateral agreement between the parties, as is current practice for OTC derivatives.

The Standard Annex will also provide that a failure by the CM to perform a payment or delivery obligation under a Customer-Member Transaction will constitute an event of default with respect to the CM, regardless of whether the CM is otherwise determined to be in default under the ICE Clear Europe Rules. Such a failure would, however, permit ICE Clear Europe to declare the CM in default under the ICE Clear Europe Rules. If ICE Clear Europe makes such a declaration, the default procedures described herein would apply. If ICE Clear Europe does not declare the CM to be in Default, the Customer will be permitted to exercise its bilateral contractual termination remedies against the CM, although the default procedures of the Rules would not apply. In any event, the Customer would not have any direct remedy against the clearing house.

7. Customer Transaction Margining

Under the Standard Annex, each Member must obtain initial, variation and any special margin from its Customer for Customer-Member Transactions in an amount at least equal to the clearing house requirement for the related Customer Positions (determined on a gross basis).

In the case of initial and any special margin, the Member will be required to transfer such margin to the clearing house for credit to the Customer Account.

The Rules do not limit a CM's ability to require additional margin from a customer beyond the CCP requirement ("CP Excess"). Treatment of any CP Excess required of the Customer by the Member beyond Clearinghouse requirements would be as agreed between the Customer and Member.⁹

Variation margin posted by a Customer may be transferred freely, and it would be expected that such margin may be used to satisfy the Member's variation margin requirements at the clearing house in respect of Customer Positions.

The clearing house would make available to Clearing Members information sufficient for Members to determine their Customers' minimum margin requirements in respect of Customer-Member Transactions.

The Member will be required under the Rules to maintain accurate records concerning the identity of Customers, the margin assets posted by its Customers and the transfer of such assets to the clearing house.

8. Default Rules

The Rules provide for separate treatment of Customer and Proprietary Positions at all times, including following an Event of Default¹⁰ being declared in relation to a Clearing Member. The determination of whether a Clearing Member is subject to an Event of Default is not affected by the existence or use of Customer Accounts. However, the clearing house is required by law and by the Rules to undertake the close-out process under the Rules separately in respect of Proprietary Positions and Customer Positions, such that a separate "net amount" for purposes of the Companies Act 1989 is calculated in respect of Customer Positions and Proprietary Positions.

The relevant events of default under ICE Clear Europe Rules are as follows:

⁹ CP Excess could be held in the Excess Margin Account if agreed by Member and Customer. As noted below, there may be limitations on the ability of the clearing house to effect a transfer of margin not held at the clearing house.

¹⁰ See Rule 905(c).

- (i) any breach by that Clearing Member of these Rules, the Procedures, the Clearing Membership Agreement, any other agreement with the Clearing House or Market Rules;
- (ii) that Clearing Member being unable, or likely to be unable, to meet its obligations under these Rules or in respect of any Contract;
- (iii) a Monetary Default occurring with respect to that Clearing Member;
- (iv) any Financial Indebtedness of that Clearing Member or any of its Affiliated Persons: (A) not being paid when due or within any originally applicable grace period; or (B) being declared to be or otherwise becoming due and payable prior to its specified maturity as a result of an event of default (however described);
- (v) any commitment for any Financial Indebtedness of that Clearing Member or any of its Affiliated Persons being cancelled or suspended by a creditor as a result of an event of default (however described);
- (vi) any creditor of that Clearing Member or any of its Affiliated Persons becoming entitled to declare any Financial Indebtedness due and payable prior to its specified maturity as a result of an event of default (however described);
- (vii) an Insolvency in relation to that Clearing Member or any of its Affiliated Persons;
- (viii) any material action being taken against that Clearing Member (including, without limitation, any declaration of default, material adverse notice or finding, material fine, suspension or expulsion or withdrawal of, revocation of or failure to renew any permission, licence or authorisation) by any Governmental Authority, Regulatory Authority, Exchange, Clearing Organisation or Delivery Facility; or
- (ix) breach by that Clearing Member of any Applicable Law relevant to its business as a Clearing Member.

Depending on the type of event, different levels of management approval may be required before determining that a Member is in default. It is a requirement that ICE Clear Europe notify the FSA of any event of default.

The Rules and applicable laws (Financial Services and Markets Act 2000 (Recognition Requirements) Regulations 2001, Schedule, paragraph 28) require the Clearing House's default rules to prohibit any netting between Customer Positions and Proprietary Positions. Rule 905 gives effect to this requirement. If a net amount was owed to the Member in respect of Customer Positions, the clearing house would not offset that amount against any amount

owed by the Member to the clearing house in respect of Proprietary Positions. However, as from 15 June 2009 following a change in law, if a net amount is owed by the Clearing Member in respect of Customer Positions, the clearing house would be entitled to offset against that obligation any amount owed to the Clearing Member in respect of Proprietary Positions.

Thus, the clearing house only will be permitted to apply margin in a Customer Account to satisfy obligations of the Clearing Member in respect of Customer Positions. Such margin could not be used to satisfy obligations in respect of Proprietary Positions.

9. Certain Rules Regarding Portability of Positions and Margin

i. Pre-Default Portability

Rule 406 allows a Clearing Member to transfer Customer Positions to another Member, subject to the agreement of both Clearing Members and the consent of the clearing house. In practice, the Clearing Members will only agree to such a transfer if the Customer also agrees to the transfer and appropriate novation agreements in respect of Customer-Member Transactions are entered into.

The clearing house is considering supplementing this requirement with procedures pursuant to which the old Clearing Member, Customer and new Clearing Member must enter into a written novation agreement concerning the Customer-Member Transactions to be transferred, the date and time the transfer is to be effective, the amount of margin held in the old Member's Customer Account that relates to the related Customer Positions to be transferred.

Upon submission of such agreement to the clearing house and acceptance of it by the clearing house, the provisions of Rule 406 would be effective. In addition, under such a structure, the clearing house could transfer the appropriate amount of margin from the Customer Account of the old Member to the Customer Account of the new Member. Each of the old Clearing Member, new Clearing Member and Customer will be responsible for ensuring that their respective margin requirements remain satisfied upon the transfer of positions.

ICE Clear Europe's Rules do not permit it to mandate that a CM transfer any or all of its customer positions or related initial and variation margin (and any associated contractual relationships) to another clearing member, if such CM is not in default, regardless of whether ICE Clear Europe perceives that the CM is in a state of impending financial distress.

ii. Post-Default Portability

The Rules include certain procedures to enhance portability of Customer Positions, Customer Transactions and margin in the case of a Member default (“Default Portability Rules”). The clearing house is considering supplementing these rules with additional Default Portability Rules. As a general matter, pursuant to Rule 902(a), the clearing house is able to sell or transfer any contracts of a defaulting Clearing Member the “Defaulting Member”) to another Member (the “New Member”), including any Customer Positions.¹¹ Clearing Members would not be obliged to accept a transfer of Customer Transactions but would be entitled to effectively purchase or bid for the portfolio. Under a power of attorney executed by Clearing Members in Clearing Membership Agreements, the clearing house is able to deal with any other assets of the Clearing Member that is a defaulter, which would include Customer-Member Transactions.

The Customer would consent to such procedures in the Standard Annex for the Customer-Member Transactions. The result of these actions (collectively, the “clearing house Transfer Procedures”), in effect, would be to allow the clearing house to transfer the Customer Transactions and Customer-Member Transactions from the Defaulting Member to the New Member. The Clearing House's power of attorney would enable it to execute such agreements in the name of a defaulting Clearing Member. The Clearing House is considering further supplementing its powers under this power of attorney for CDS customer clearing.

If such a transfer were effected at present, the clearing house would transfer the appropriate initial margin for the related Customer Positions back to the Defaulting Member and the new Member would need to provide fresh Margin. Under applicable insolvency laws, assets posted in the Customer Accounts, if received by a Defaulting Member, would be held on trust for its Customers and therefore would not be available to the insolvency practitioner. The clearing house is considering introducing new procedures that would enable such assets instead to be transferred directly from the defaulting Member's Customer Account to the New Member's Customer Account.

Alternatively, the clearing house would have the right under the Rules to achieve effectively the same result through procedures for the termination of existing transactions and establishment of new positions with the New Member as opposed to a transfer (“clearing house Termination/Replacement Procedures”).

If the clearing house did not effect a transfer or termination and replacement under the Default Portability Rules within the Transfer Period

¹¹ These procedures would only apply in situations where the Defaulting Member's regulator, administrator, liquidator or other applicable insolvency practitioner did not otherwise transfer or arrange the transfer of the relevant positions.

(including because no Member was willing to accept transfer or enter into replacement transactions), the Standard Annex would permit the Customer to terminate the relevant Customer-Member Transactions in accordance with their terms. In that case, remaining assets in the Customer Account would be returned to the defaulting Clearing Member's administrator or liquidator, who would receive the same in the Clearing Member's capacity as trustee on trust for distribution to Customers.

ICE Clear Europe will determine the close-out price for Customer Positions pursuant to its close-out procedures, which may involve auction or allocation of the relevant Customer Positions. Under the Standard Annex, the same close-out price will apply to the related Customer-Member Transaction. Because the close-out process for Customer Positions is conducted separately from the close-out process for Proprietary Positions, the same close-out price will not necessarily apply to Customer and Proprietary Positions.

The Rules permit the clearing house to use the Default Portability Rules for some or all of the relevant Customer Transactions. In addition, the Standard Annex will permit Customers to elect, at the time they enter into the Standard Annex, whether they want their Customer Transactions to be subject to the Default Portability Rules.¹² The clearing house may, but will not be obligated to, take into account requests from Customers to have positions transferred to, or not to, specific Members and any prearrangements among Members and Customers as to the transfer of positions. Depending on the circumstances, such elections and arrangements may facilitate or complicate any attempt by the clearing house to move Customer Transactions. In addition, it is not clear that the clearing house will be able to move, or cause the relevant Member to move, additional margin that may be required by the CM which is not held in the Excess Margin Account. This may affect the willingness of a Member to accept transfer of Customer Transactions.

With respect to documentation, if the New Member and Customer have entered into an ISDA Master Agreement, the transferred or replaced Customer Transactions will be subject to that agreement, together with the Standard Annex. If those parties have not entered into an ISDA Master Agreement, the transferred or replaced Customer Transactions will be subject to the terms of the ISDA Master Agreement in effect between the Customer and the Defaulting Member, subject to any amendments agreed between the Customer and the New Member. A New Member may be less willing to accept transferred or replaced Customer Transactions if it has not entered into an ISDA Master Agreement with the Customer.

¹² Customers or CMs in jurisdictions requiring automatic termination or providing for automatic setoff upon insolvency (currently for ICE Clear Europe, only Switzerland) may be limited in their ability to elect that default portability rules apply.

In order to implement the Default Portability Procedures, ICE Clear Europe will rely on information provided by Members as to the identity, positions and margin of Customers, although ICE Clear Europe will not have a direct relationship with those Customers other than through any rights which it may enforce pursuant to the ISDA Supplement. Members will be required to provide such information to ICE Clear Europe on a daily basis.

10. Investment of Excess Margin Account

Subject to regulatory approvals, excess margin assets could potentially be invested in a broader range of assets than required margin assets in the Customer Margin Account (which the clearing house may need to access in the event of a Member default). This issue is being considered further.

C. Transfer of Margin from Clearing Members to ICE Clear Europe

CMs are required to post margin to ICE Clear Europe for the Customer Account within the timelines set forth in the Finance Procedures, whether they are on-posting margin provided to them by Customers or using their own assets. Failure to provide margin within such timelines will constitute a default by the CM under the Rules. While there is no specific requirement about how quickly a CM must transfer margin posted by customers, to the extent a CM does not do so within the required margin timeframe it will be required to transfer its own assets.

To the extent a CM has received customer margin and not transferred it to ICE Clear Europe, the margin must be held by the CM in segregation from the CM's assets.

ICE Clear Europe has considered having Customers post margin directly to ICE Clear Europe. To ICE Clear Europe's knowledge, it would be unusual for a clearing organisation for futures, securities or other derivatives to accept CCP Margin directly from, or otherwise have a direct contractual relationship with, customers that are not themselves CMs. Such an approach could expose the clearing house to additional liability to customers, result in additional compliance obligations and could raise various operational considerations, including as to margin timing.

D. Economic Effects of Proposed Clearing Structure for CCP Margin

In evaluating the proposed clearing structure, ICE Clear Europe analysed the economic costs/benefits of the segregation model.

1. Return on Investment

If initial margin is held at ICE Clear Europe, the clearing house will pass through the return (yield) on that property. However, as noted above, there are limitations on the types of Permitted Cover for ICE Clear Europe, and the return may be correspondingly limited. ICE Clear Europe is considering permitting a wider range of investments to be accepted as excess Customer Account margin.

2. Allocation of Risk and Returns

The risk and return on investment of customer margin would be allocated by agreement between the CM and its Customer. ICE Clear Europe rules would not prevent the risk and return from being passed through to Customers.

E. Determination of Required Margin and Related Considerations

1. Required Margin Collection for Customer Segregation

ICE Clear Europe will determine ICE Gross Margin to be collected by Members from Customers based on a single Customer portfolio (gross exposure) and will not net multiple customer portfolios. Positions within the single Customer's portfolio will be netted for margining purposes providing offsets for a particular Customer portfolio.

2. Protection Against Collecting Insufficient or Excess Margin

The ICE Clear Europe Risk Management Framework ensures that the clearing house has sufficient funds to cover potential Clearing Participant default losses under distressed market conditions. ICE Clear Europe collects conservative, but not excessive, margins to collateralise risk.

i. Potential Impact of Collecting Insufficient or Excess Margin

Collection of excess margin could result in loss of liquidity and investment return for customers and CMs, as compared to other potential uses for those assets. Collection of insufficient margin may increase the risk of a CM or customer default and/or result in a shortfall in the event of such a default. Because customer margin will be held on an omnibus basis, customers are exposed to the risk of a shortfall in customer funds, even if caused by the default of another customer. Collection of insufficient margin may also increase the likelihood that losses from a default would be charged against guaranty fund contributions, which could cause other CMs to share in losses from another CM's default.

3. Addition of New Products to Clearing

Prior to accepting a new product type for clearing, ICE Clear Europe must consult with the Risk Committee and may consult with the non-member Advisory Committee to evaluate the acceptability of the new product. The ultimate decision to add a new product lies with the ICE Clear Europe Board. ICE Clear Europe must also gain approval from its regulators prior to clearing a new product.

4. Margin Methodology

ICE Clear Europe employs a robust methodology that accounts for instrument risk, hedging benefits and concentration charges. The methodology identifies all risk factors, generates plausible market scenarios for all risk factors, allows for a wide range of portfolio strategies and financial instruments and estimates portfolio replacement value in response to generated scenarios.

The ICE Clear Europe margining approach:

- Configured to assess risk requirements (margin) to meet replacement costs
- Risk quantile of 99% over a 5-day position replacement time horizon
- Assuming a heavy (fat) tailed and skewed distribution with dynamic volatility forecasting for daily changes in log credit spreads
 - Significant heavy-tailed for log credit spread increases
 - Almost normally distributed log credit spread decreases
 - No hedge offset among 'Risk Factors' (e.g., NA.IG, NA.HY)
 - Limited (conservative) offset among long-short positions on products in same risk factor (e.g., different series)
 - Concentration charges are applied by product when losses exceed a threshold of position size relative to the market depth
- Independent expert review validated the ICE Clear Europe risk methodology and models

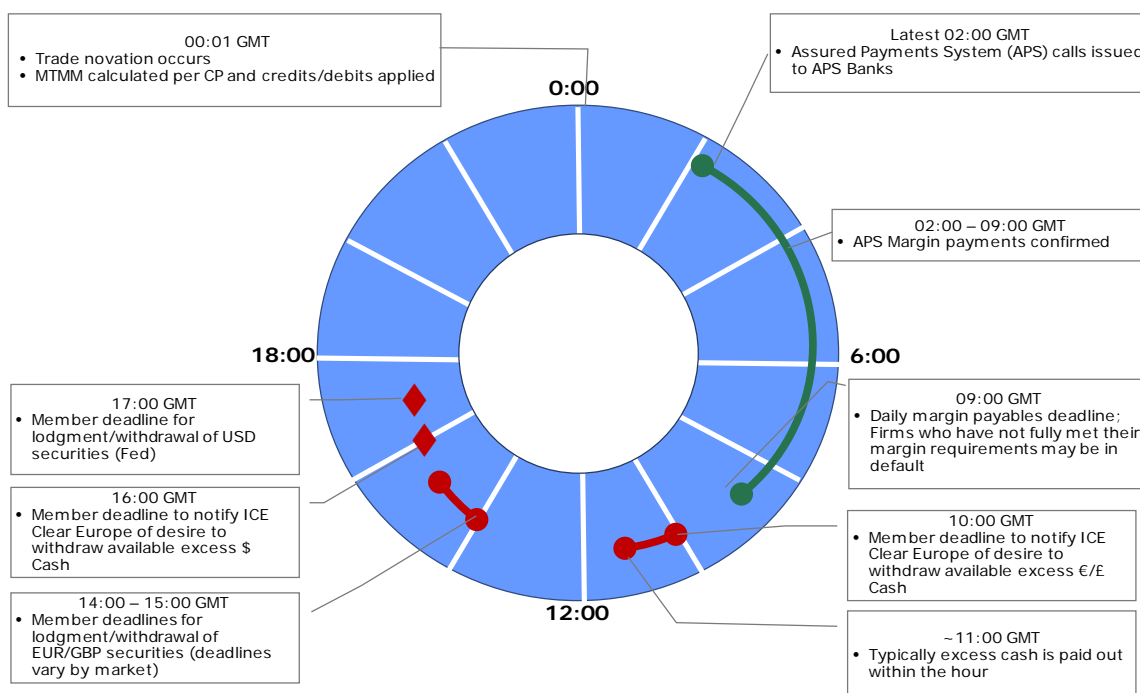
ICE Clear Europe provides robust margin reporting to CMs through a web report distribution system.

To enable customer segregation, ICE Clear Europe is in the process of developing a margin calculation tool for CMs and Customers that provides access to ICE Clear Europe margin requirement determination. CMs will be able to enter Customer portfolios into the tool to establish margin requirements. Customers will be able to view margin requirements upon demand.

5. Margin Calls/Collection

In the normal course of business, ICE Clear Europe will publish margin requirements by 2:00 AM GMT (via SWIFT Messaging). Payments are due no later than 9:00 AM GMT. Clearing Participants will be considered in default if full payment is not received by 9:00 AM GMT (barring technical difficulties). The daily settlement cycle is outlined in the figure below.

ICE Clear Europe Direct Settlement Process



6. Mark-to-Market

ICE Clear Europe utilises a dynamic price collection and settlement price calculation process to determine the mark-to-market. On a daily basis, each clearing member must submit a bid/offer for each instrument for which it has an open position. ICE Clear Europe uses a pricing algorithm to calculate an End of Day (EOD) Settlement Price per product. To ensure accuracy of bid/offers submitted by CMs, ICE Clear Europe requires CMs, on a frequent basis, to trade at the calculated EOD Settlement Price.

ICE Clear Europe monitors intra-day pricing to evaluate market conditions and manage its risk. ICE Clear Europe does not anticipate providing intra-day pricing to its CMs or CM's Customers.

7. Guaranty Fund Contributions

While CM Guaranty Fund requirements will take into account both Customer and Proprietary Positions, ICE Clear Europe does not anticipate that Customer funds will be applied to Guaranty Fund contributions for the CM. Therefore, portability of Customer Guaranty Funds is not relevant.

F. Amendments to Clearing Structure

Pursuant to its Rules, ICE Clear Europe is required to consult with its Risk Committees and more generally with all Clearing Members prior to making certain material modifications to its Rules and/or clearing structure (Rule 109). All consultations are made public as circulars on ICE Clear Europe's website. Various examples of past circulars are available on ICE's website. The Risk Committees include representatives appointed by CMs. ICE Clear Europe is in the process of establishing a non-member

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advisory committee, which will include representatives of buy-side firms. ICE Clear Europe expects that it would consult with the non-member advisory committee as well in connection with material modifications to the Rules and/or the clearing structure that would affect buy-side firms.

IV. Legal Considerations

The following discussion is based principally on English law. The legal structures for implementing client segregation are currently under consideration. However, the key intended outcome from a Customer perspective is that Customer Account margin (including ICE Excess Margin) would not form part of the Clearing Member's insolvent estate. This would be achieved by the Clearing Member holding its right to return of assets on trust for Customers.

A. Segregation Requirements under Applicable Law

The Client Asset Rules apply to Clearing Members that are regulated by the FSA, including when they deposit client assets or money with a third party such as ICE Clear. The Client Asset Rules are only relevant to Clearing Members regulated by the FSA. However, they are based upon the Markets in Financial Instruments Directive (Directive 2004/39/EC), so similar rules are likely to apply to Clearing Members that are regulated elsewhere in the European Economic Area.

A Clearing Member to which the Client Asset Rules apply, that transfers client assets as Margin to ICE Clear, is required, before a client transaction account is first opened with ICE Clear, to: (a) notify ICE Clear that the Clearing Member is under an obligation to keep client assets separate from the Clearing Member's own assets, by placing client assets in a client account; (b) instruct ICE Clear that any assets paid to ICE Clear in respect of client transactions are to be credited to the Clearing Member's client transaction account. A written acknowledgement of the requirement of Clearing Members to segregate client assets must be given by ICE Clear and has indeed been given on these terms to all Clearing Members.

To the extent that the client asset rules apply, any amounts payable to a Clearing Member following an Event of Default would be received by the relevant insolvency practitioner in a separate account and fall outside the insolvency estate of the Clearing Member. ICE Clear Europe is considering a possible alternative legal construct under which the client asset rules would not apply due to the Clearing Member receiving assets from Customers by way of title transfer or security collateral under the Financial Collateral Regulations. In this situation, the Clearing Member would be required under the Rules to enter into an express declaration of trust by deed poll over its receivables in relation to its Customer Account and ICE Excess Margin account with ICE for the benefit of its CDS clearing customers. The Clearing House's membership department would ensure that such documentation were in place prior to customer account launch. The Clearing House would itself separately enter into a waiver of set off in similar form to that required under client asset rules. This would achieve a similar result in terms of ensuring that Customer Account and Customer Margin Excess account assets fell outside the Clearing Member's insolvency estate and that the same could be passed on to Customers if necessary.

There is no formal U.S. regulatory or governmental segregation requirement applicable to ICE Clear or its U.S. Clearing Members with respect to cleared CDS transactions. To the extent ICE Clear, any Clearing Member or any custodian accepts margin in a custodial

capacity and such arrangements are governed by U.S. federal or state law, it will be subject to the requirements applicable to such custodial property under applicable U.S. federal or state law, including the Uniform Commercial Code in effect under the relevant state law.

B. Customer Rights to CCP Margin

The clearing house will not directly have a contractual or legal relationship with the customers of a CM, so any rights to margin of Customers would be only as against the Clearing Member. However, the Clearing Member will hold its interests in Customer collateral, including rights to repayment owed by the clearing house, on trust for its Customers including on insolvency, pursuant to the client asset rules or express declarations of trust.

Considerations:

- With respect to cash initial margin held at the CCP, the CCP will have a contractual obligation to return such initial margin as provided in the Rules. The CM's rights to repayment from ICE Clear (and any proceeds resulting from that right) will be held by the CM as trustee for its CDS clearing Customers. Accordingly, as between any Customer and the CM, the Customer (jointly with all other Customers of the CM who are interested in Customer Account assets held by ICE Clear) would have proprietary rights in the CM's claim against the CCP.
- As a result of Customers having such proprietary rights, initial margin would not be subject to the insolvency estate of the defaulting CM, and accordingly, assuming that the CM has properly maintained its books and records in relation to its Customer Account, would not be subject to the claims of general creditors of the defaulting CM.
- Under ICE Clear Europe rules and the Standard Annex, a shortfall in CCP margin in the Customer Accounts will be shared among customers on a pro rata basis.

C. Customer Rights to CM Margin

The CM would need to transfer all initial margin (other than any CM Excess) to the clearing house. As a result, such margin would not be held by the Clearing Member unless the margin was returned, for example following the close out of positions or a default. The Clearing House is required under the Companies Act 1989 and Financial Services and Markets Act 2000 (Recognition Requirements) Regulations 2001 to declare net sums separately in respect of a defaulter's client account and customer account (see Rule 905). A customer's rights to CP Excess will depend on the manner in which the customer and CM agree that such CP Excess is to be held.

D. Legal Enforceability of Portability and Netting Framework

In summary, three separate pieces of legislation provide clearing houses with a series of protections against the effects of insolvency:

- (a) Part VII of the Companies Act 1989, which provides protections for 'market contracts' to which a clearing house is party, certain collateral taken by a clearing house and the default rules and default procedures of a clearing house;

- (b) Settlement Finality Directive (Directive 98/26/EC) as implemented in the UK by the Financial Markets and Insolvency (Settlement Finality) Regulations 1999 (S.I. 1999/2979), which provide protections for payment transfer orders, security transfer orders, collateral security and the default rules of 'designated systems'; and
- (c) Financial Collateral Directive (2002/47/EC) as implemented in the UK by the Financial Collateral Arrangements (No. 2) Regulations 2003 (S.I. 2003/3226), which provides protections to persons who take certain kinds of financial collateral.

ICE Clear Europe is a "recognised clearing house" for purposes of the Companies Act 1989 and a "designated system" for purposes of the Settlement Finality Regulations. As a result, all relevant customer margin protections applicable under such legislation apply to ICE Clear Europe.

In the event of a Clearing Member's default, ICE Clear Europe's ability to use collateral and transfer or sell the defaulting CM's contracts and Customer-Member Transactions should be protected by such legislation. ICE Clear Europe's rules would not however contemplate portability of positions of a customer that itself is insolvent.

In the case of the insolvency of a U.S. Clearing Member, insolvency laws applicable in the United States (including FDICIA, the FDIA and the Bankruptcy Code) generally uphold the enforceability of a clearing organization's rights to terminate and net contracts with, and apply security of, an insolvent Clearing Member. By contrast, these laws do not specifically address the enforceability of rights of a clearinghouse to transfer positions (and related collateral). Accordingly, there are uncertainties as to the enforceability of a general right of a clearinghouse to transfer positions (including a Clearing Member's Customer-Member Transactions) on default.

In the case of an insolvency of a U.S. Clearing Member, the application of ICE Clear Europe's default rules would be subject to any rights of the Clearing Member's receiver or other insolvency trustee or similar party under applicable U.S. law to transfer positions. With respect to Clearing Members that are insured U.S. banks, the Federal Deposit Insurance Corporation ("FDIC") would generally have the power within the one-business-day period following its appointment as receiver to transfer derivative contracts of the Clearing Member to a new financial institution, which may be an existing institution or a "bridge bank". During the one-business-day period, the clearinghouse would not be able to exercise remedies. In making any such transfer, the FDIC is required to transfer all derivative transactions of the defaulting Clearing Member (whether cleared or uncleared) with a particular counterparty or its affiliate, or transfer none of such transactions. This requirement could in some circumstances hinder the FDIC's ability to transfer positions.

E. Legislative Reforms

ICE Clear Europe is not at present lobbying for UK legislative reforms specific to customer clearing of CDS. We note that the Financial Markets and Insolvency Regulations 2009 come into force on 15 June 2009 and make various improvements to

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the UK insolvency legislation applicable to recognised clearing houses. US legal issues are discussed in ICE Trust's submission.

V. Appendix - Questionnaire

Please see the references in the questionnaire below for links to specific answers in the response.

Questionnaire for CDS CCPs on Protection of Customer Initial Margin

This questionnaire has been prepared by an ad hoc group (comprising both buy-side and sell-side constituents)¹³ to more fully understand the rights of “customers” – i.e., buy-side and other market participants proposing to clear CDS transactions through clearing members (“CM”) of a central CDS counterparty (“CCP”) – to initial margin (“IM”) posted in connection with the central clearing of certain CDS transactions.

The questions are divided into two sections. The first part solicits responses to several factual matters regarding the clearing structure of the CCP, the precise means by which IM is held by the CCP and CMs (and their custodians, if applicable), and the CCP’s proposals as to segregation and portability of customer positions and initial and variation margin (and any associated contractual relationships).¹⁴ The second part solicits responses as to the legal treatment of the CCP’s proposed clearing structure. As the latter inquiry is largely dependent on the legal and contractual framework governing the CCP, the CMs and the customers (and the relationships between them), the questions in the second part should be considered under the laws of all jurisdictions relevant to the CCP (and its custodian, if applicable), the CMs (and their custodians, if applicable) and the customers. We note that although similar or identical questions are posed throughout certain portions of the questionnaire, this repetition arises from the need to consider the questions for each level at which IM is held: (i) IM held at the CCP (or the CCP’s custodian) – referred to in this questionnaire as “CCP Margin”, and (ii) IM held at a CM (or the CM’s custodian) – referred to in this questionnaire as “Dealer Margin”.

I. Factual Matters

A. Composition and Structure of the CCP, CMs, Custodians and Customers

Structure of the CCP

1. Please describe the legal structure (e.g., entity type, jurisdiction, governing structure, etc.) of the CCP. Include references to any required licenses or registration orders obtained in connection with the establishment of the CCP.

¹³ This group was formed at the behest of the Federal Reserve Bank of New York, and consists of buy-side members Alliance Bernstein, Barclays Global Investors, Blue Mountain, Brevan Howard, D.E. Shaw, Goldman Sachs Asset Management, King Street and PIMCO, and sell-side members Barclays Capital, Citigroup, Credit Suisse, Deutsche Bank, Goldman Sachs, JPMorgan Chase, Morgan Stanley and UBS. ISDA, the Asset Managers Group of SIFMA, and Managed Funds Association are facilitating and observing the group’s activities.

¹⁴ If the CCP is envisioning a multi-step approach to implementation, please detail both the interim and final phases, and an approximate time frame for achievement of the latter. If customers or CMs may elect one of multiple options with respect to any aspect of the clearing structure, please describe all such options.

2. Please list all relevant regulatory and supervisory authorities of the CCP.
3. Please detail any legal or regulatory segregation requirements applicable to customer IM held at the CCP.

[See Section II, A.](#)

Structure of CMs

4. Please describe the legal structures applicable to the CMs.
 - a. Does the CCP restrict either the (i) organisational type (e.g., banks, broker-dealers, futures commission merchants, unregulated entities, etc.) or (ii) jurisdictions of organisation of CMs? (Note: This will be key, as much of the legal analysis will depend on the insolvency laws applicable to the CMs.)
5. Please list all relevant regulatory and supervisory authorities applicable to the CMs.
6. Please detail any legal or regulatory segregation requirements applicable to customer IM held at the CM.

[See Section II, B.](#)

Structure of Custodians (If Applicable)

7. Please describe the legal structures applicable to the custodians used by the CCP and CMs to hold IM.
 - a. Does the CCP restrict either the (i) organisational type or (ii) jurisdictions of organisation of entities that may serve as custodians of the CCP or CMs to hold IM? Are there any restrictions on whether such custodians may be affiliated with the CCP or CMs? (Note: This will be key, as much of the legal analysis will depend on the insolvency laws applicable to the respective custodians, to the extent IM is held by custodians.)
8. Please list all relevant regulatory and supervisory authorities applicable to the custodians.
9. Please detail any legal or regulatory segregation requirements applicable to customer IM held at the custodians.

[See Section II, C.](#)

Structure of the Customers

10. Please describe the legal structures applicable to the customers.
- a. Does the CCP restrict either the (i) organisational type or (ii) jurisdictions of organisation of customers? (Note: This may be important, as some of the legal analysis may depend on the insolvency laws applicable to the customers.)
11. Please list all relevant regulatory and supervisory authorities applicable to the customers.

[See Section II, D.](#)

Expansion/Restriction of Permitted Entity Types

12. In weighing the relative benefits and drawbacks of expanding or restricting the entity types and jurisdictions of the CMs, customers and custodians, what factors did the CCP consider in its analysis? For example, to what extent did the CCP consider the following issues in reaching its proposed structure?
- a. Netting implications for CMs and their affiliates (from a credit, accounting and capital perspective);
 - b. Regulatory capital implications for CMs and their affiliates;
 - c. Operational efficiencies or inefficiencies, and other business implications of operating through the permitted entity types;
 - d. Adverse pass-through effects (e.g., unfavourable pricing) flowing from the CMs to customers as a result of the foregoing; and
 - e. The legal regime applicable to the proposed clearing framework upon an insolvency of a CM, customer or custodian.
13. What is the process for approval and consideration of risks presented by additional CM or custodian entity types (by way of inclusion of new CMs or custodians or mergers of existing CMs or custodians in a manner that changes the applicable legal structure)?

[See Section II.E](#)

B. Segregation and Safekeeping of IM

IM Held at or for the CCP (“CCP Margin”)¹⁵

Composition of CCP Margin

1. Please describe the types of assets (e.g., Treasury securities, US dollars, non-US currencies, etc.) that may be deposited as CCP Margin to satisfy IM requirements imposed by the CCP (“Required Margin”). To what extent did customer protection considerations affect the CCP's determination in this regard?

[See Section III, A, 1.](#)

Nature of Relationship Between CCP, CMs, Custodians and Customers

2. Please describe the nature of the legal and contractual relationship between the CCP, the CMs, custodians, the customers and any other relevant parties, specifically addressing the following:

[See Section III, A, 2.](#)

- a. Are CMs acting as agents or principals (or operating with aspects of both) vis-à-vis (i) the CCP and (ii) customers? Please elaborate.
- b. If customers are permitted to clear transactions through non-CM affiliates of the CM, who in turn clear through the affiliated CM, please describe in detail the mechanics of such an arrangement.

[See Section III, B.](#)

Description of Proposed Clearing Structure¹⁶

3. Please detail the manner in which customers will post CCP Margin.
 - a. Will the CCP Margin be posted pursuant to pledge or title transfer arrangements?
 - b. May the CCP Margin consist of property posted by customers and pledged or transferred to the CCP, or must it consist of the proprietary assets of the CM?

¹⁵ Please also answer the questions below with respect to excess variation margin (i.e., mark-to-market margin posted by customers in excess of the CCP's requirements), to the extent excess variation margin is treated differently from CCP Excess Margin.

¹⁶ Please address the relevant questions with respect to each proposed clearing structure. For instance, if the CCP has one clearing structure for transactions entered into directly between a customer and its CM / prime broker, and another for transactions originally entered into between a customer and an executing broker that are subsequently given up to the customer's CM / prime broker, please respond to the questions with respect to each proposed clearing structure.

4. Please detail the manner in which CCP Margin will be held (noting any circumstances in which the default clearing structure may be modified by elections available to CMs or customers), distinguishing between various categories of margin to the extent appropriate – e.g., (i) Required Margin, (ii) margin in excess of that required by the CCP to secure performance obligations in connection with cleared transactions (“CCP Excess Margin”), (iii) margin posted in respect of requirements imposed by CMs on their customers in excess of the CCP’s margin requirements (“Dealer Excess Margin”), etc. – and specifically addressing the following:
 - a. CCP Margin Held Directly at a CCP (or at a Custodian Holding Solely for the Benefit of the CCP) – If the CCP will hold CCP Margin directly (without a custodian), or the custodian will hold CCP Margin only for the CCP (rather than for individual CMs or customers (individually or as a group)), please detail all aspects of the arrangement that are relevant from a customer protection standpoint, specifically addressing the following:
 - i. The manner in which the CCP holds the CCP Margin, distinguishing to the extent relevant between various categories and types of CCP Margin (e.g., securities or cash), and identifying in particular:
 1. On behalf of whom the CCP is holding the property – itself, the CMs or the customers (as a group or individually);
 2. Whether CCP Margin securing the positions of a particular CDS customer will be segregated from (i) the CCP Margin posted by other CDS customers and (ii) the property of other custodial claimants of the CCP or instead, commingled in a single omnibus account (either for CDS customers or custodial claimants of the CCP generally);
 - a. In whose name(s) has/have the account(s) been established?
 3. Whether CCP Margin securing customer positions will be segregated from the CCP Margin securing proprietary positions of CMs;
 4. Any operational practices (whether voluntary or mandated by regulators) relevant to the analysis of customer protection and the sharing of any shortfalls in custodial property;¹⁷

¹⁷ See clause (ii) of note 6.

5. Under what circumstances CCP Excess Margin held at the CCP may be (i) withdrawn by the CM or customers or (ii) applied by CMs or the CCP.
 - ii. Whether the CCP has the right to rehypothecate or cause liens to be placed on the CCP Margin – e.g., to potential lenders or liquidity providers to the CCP – and if so, whether any such liens have been subordinated or waived; and
 - iii. Whether investment of CCP Margin in interest-bearing instruments or vehicles (e.g., overnight sweeps into repos) is permitted or required, and if so, in what types of instruments or vehicles.
 1. Who obtains the economic benefit of investment of CCP Margin in permitted instruments? Who bears the risk of loss?
 2. How does the above response differ as between Required Margin and CCP Excess Margin posted to the CCP?
- b. CCP Margin Held at a Custodian (Whether the Custodian is Holding for the CCP, Individual CMs or Customers) – If the CCP will hold CCP Margin at a custodian, please detail all aspects of the custodial arrangement that are relevant from a customer protection standpoint, specifically addressing the following:
 - i. The manner in which the custodian holds the CCP Margin, distinguishing to the extent applicable between various types of CCP Margin (e.g., securities or cash), and identifying in particular:
 1. On whose behalf the custodian is holding the property – the CCP, the CMs or the customers (as a group or individually);
 2. Whether CCP Margin securing the positions of a particular CDS customer will be segregated from (i) the CCP Margin posted by other CDS customers and (ii) the property of other custodial claimants of the custodian, or instead, commingled in a single omnibus account (either for CDS customers or custodial claimants of the custodian generally);
 - a. In whose name(s) has/have the account(s) been established?

3. Whether CCP Margin securing customer positions will be segregated from the CCP Margin securing proprietary positions of CMs;
 4. Any operational practices (whether voluntary or mandated by regulators) relevant to the analysis of customer protection and the sharing of any shortfalls in custodial property;¹⁸ and
 5. Under what circumstances CCP Excess Margin held at the custodian may be (i) withdrawn by the CM or customers or (ii) applied by CMs or the CCP.
- ii. Whether the custodian has the right to rehypothecate or cause liens to be placed on the CCP Margin, and if so, whether any such liens have been subordinated or waived;
 - iii. Whether investment of CCP Margin in interest-bearing instruments or vehicles (e.g., overnight sweeps into repos) is permitted or required, and if so, in what types of instruments or vehicles; and
 1. Who obtains the economic benefit of investment of CCP Margin in permitted instruments? Who bears the risk of loss?
 2. How does the above response differ as between Required Margin and CCP Excess Margin posted to the CCP?
 - iv. How the risk of the custodian's insolvency is allocated among the CCP, the CMs and the customers (as a group and individually).

[See Section III, B.](#)

Transfer of CCP Margin from CMs to the CCP

5. If CCP Margin will be deposited by customers at their respective CMs, and subsequently transferred to the CCP, please address the following (distinguishing between various categories of CCP Margin (e.g., Required Margin, CCP Excess Margin, Dealer Excess Margin, etc.) and types of CCP Margin (e.g., securities or cash) to the extent relevant):

¹⁸ For example, please consider, to the extent relevant, (i) whether the intermediary is a UCC securities intermediary that credits securities to a securities account in the name of a particular customer or customers generally, and whether the securities intermediary debits securities from the securities accounts of its customers upon any rehypothecation of such securities, and (ii) whether any cash held by the intermediary is maintained as a segregated "special deposit" that remains property of a particular customer or customers generally under applicable law (as distinguished from a "general deposit" in which legal title to the cash passes to the intermediary).

- a. How long will it typically take for a CM to transfer CCP Margin posted by customers to the CCP?
- b. In the intervening period, where at a CM will the CCP Margin be held?
- c. At what point is the CM deemed to be in default for failing to transfer CCP Margin to the CCP?
- d. What considerations militate in favour of, or against, allowing customers to deposit CCP Margin directly with the CCP?

[See Section III, C.](#)

Economic Effects of Proposed Clearing Structure for CCP Margin

6. Please describe the economic benefits or disadvantages (from the perspective of CMs and their customers) of the proposed clearing structure for holding IM at the CCP or its custodian (as opposed to at CMs or their custodians).
 - a. Do CMs have the ability to generate returns on customer property under the proposed structure?
 - b. To what extent do the benefits or disadvantages of the proposed structure flow through from CMs to their customers?

[See Section III, D](#)

Determination of Required Margin and Related Considerations

7. Is Required Margin determined on the basis of net exposures (i.e., by netting offsetting positions across different customers) or gross exposures? Are offsetting positions within a particular customer-CM relationship netted for this purpose?
8. Please describe whether margin requirements will be reported and published, and whether calculations are replicable by the CCP upon demand from a CM or customer.
9. Are there any restrictions on the ability of the CCP to demand additional margin from a CM or customer?
10. Are there any restrictions on the ability of a CM to demand additional margin from its customer?
11. Is the required amount of CM guarantee fund contributions relating to customer positions at the CCP determined on the basis of net or gross clearing exposures? Are offsetting positions of a single customer netted for this purpose?

12. Please discuss the approximate timeline for trade execution, submission to the CCP and novation, and how the CCP's structure in this regard (together with any other operational efficiencies) affects the customer protection analysis.

[See Section III, E](#)

Allocation of Risk upon CM Default

13. In the event of a CM default to the CCP, please detail the risk waterfall among guarantee fund contributions, Required Margin securing CM proprietary positions, Required Margin securing customer positions, and any other applicable source of funds (e.g., CCP Excess Margin, to the extent accessible by the clearing house), drawing distinctions between defaulting and non-defaulting parties where relevant.
- a. How does the applicable risk waterfall vary (if at all) depending upon whether the default arises from an insolvency event, as opposed to a non-insolvency event?
 - b. How does the applicable risk waterfall vary (if at all) depending upon the nature of the IM being applied – i.e., is IM securing customer positions applied in a different manner from IM securing proprietary CM positions?
 - c. In the event of a CM default arising from a failure to post sufficient margin, how does the applicable risk waterfall vary (if at all) depending upon whether the failure to post sufficient margin arose in respect of customer positions, rather than proprietary positions?
 - i. Please explain (to the extent applicable) how the CCP's methodology for isolating the origins of the CM default permits the CCP to identify, in a sufficiently precise manner, which risk waterfall applies in any particular instance (especially in circumstances under which the CM default may have arisen from multiple complex and interlocking factors).

[See Section III, B, 8.](#)

14. If a CM has defaulted on an obligation to its customer in respect of a cleared transaction (or a transaction related to a cleared transaction), but is not otherwise in default to the CCP, what are the customer's remedies against the CCP?

[See Section III, B, 6.](#)

IM Held at or for the CM ("Dealer Margin")

Permitted Asset Types for Customer Margin

15. Do the types of assets that may be deposited as margin with the CM differ from the types of assets that qualify as Required Margin?

[ICE Clear does not prescribe margin taken by CMs.](#)

Description of Proposed Clearing Structure for Dealer Margin¹⁹

[See Section III, B, 4, See Section III, B, 5 and Section III, B, 7.](#)

16. Please detail the manner in which customers will post Dealer Margin.
- a. Will Dealer Margin be posted pursuant to pledge or title transfer arrangements?
17. Please detail the manner in which Dealer Margin will be held (noting any circumstances in which the default clearing structure may be modified by elections available to customers), specifically addressing the following and distinguishing between different types of margin (e.g., cash versus securities) and categories of margin (e.g., Required Margin, CCP Excess Margin, Dealer Excess Margin and any other applicable categories of margin) where appropriate:
- a. Dealer Margin Held Directly at a CM (or at a Custodian Holding Solely for the Benefit of the CM) – If the CM will hold Dealer Margin directly (without a custodian), or the custodian will hold Dealer Margin only for the CM (rather than for customers (individually or as a group)), please detail all aspects of the arrangement that are relevant from a customer protection standpoint, specifically addressing the following:
 - i. The manner in which the CM holds the Dealer Margin, distinguishing to the extent applicable between various types of Dealer Margin (e.g., securities or cash), and identifying in particular:
 1. Whether Dealer Margin securing the positions of a particular CDS customer will be segregated from (i) the Dealer Margin posted by other CDS customers and (ii) the property of other custodial claimants of the CM, or instead, commingled in a single omnibus account (either for CDS customers or custodial claimants of the CM generally);
 - a. In whose name(s) has/have the account(s) been established?
 2. Whether Dealer Margin securing customer positions will be segregated from the margin securing proprietary positions of CMs;

¹⁹ See note 4.

3. Any operational practices (whether voluntary or mandated by regulators) relevant to the analysis of customer protection and the sharing of any shortfalls in custodial property;²⁰ and
 4. Under what circumstances Dealer Margin may be (i) withdrawn by customers or (ii) applied by CMs or the CCP.
- ii. Whether the CM has the right to rehypothecate or cause liens to be placed on Dealer Margin, and if so, whether any such liens have been subordinated or waived; and
 - iii. Whether investment of Dealer Margin in interest-bearing instruments or vehicles (e.g., overnight sweeps into repos) is permitted or required, and if so, in what types of instruments or vehicles.
 1. Who obtains the economic benefit of investment of Dealer Margin in permitted instruments? Who bears the risk of loss?
- b. Dealer Margin Held at a Custodian (Whether the Custodian is Holding for the CM or the Customers) – If the CM will hold Dealer Margin at a custodian, please detail all aspects of the custodial arrangement that are relevant from a customer protection standpoint, specifically addressing the following:
- i. The manner in which the custodian holds the Dealer Margin, distinguishing to the extent applicable between various types of Dealer Margin (e.g., securities or cash), and identifying in particular:
 1. On whose behalf the custodian is holding the property – the CM or the customers;
 2. Whether Dealer Margin securing the positions of a particular CDS customer will be segregated from (i) the Dealer Margin posted by other CDS customers, and (ii) the property of other custodial claimants of the custodian or instead, commingled in a single omnibus account (either for CDS customers or custodial claimants of the custodian generally);
 - a. In whose name(s) has/have the account(s) been established?

²⁰ See note 6.

3. Whether Dealer Margin securing customer positions will be segregated from Dealer Margin securing the proprietary positions of CMs; and
 4. Any operational practices (whether voluntary or mandated by regulators) relevant to the analysis of customer protection and the sharing of any shortfalls in custodial property;²¹
- ii. Whether the custodian has the right to rehypothecate or cause liens to be placed on the Dealer Margin that is not posted to the CCP, and if so, whether any such liens have been subordinated or waived;
 - iii. Whether investment of Dealer Margin that is not posted to the CCP in interest-bearing instruments or vehicles (e.g., overnight sweeps into repos) is permitted or required, and if so, in what types of instruments or vehicles;
 1. Who obtains the economic benefit of investment of Dealer Margin in permitted instruments? Who bears the risk of loss?
 - iv. Under what circumstances Dealer Margin may be (i) withdrawn by customers or (ii) applied by CMs or the CCP; and
 - v. How the risk of the custodian's insolvency is allocated among the CMs and the customers (as a group and individually).

C. Portability

1. Please consider whether a customer's positions and initial and variation margin (and any associated contractual relationships) can be ported to another CM, under each of the following scenarios.

[See Section III, B, 9.](#)

- a. Can a customer effect a voluntary, pre-CM default transfer of its positions and margin (and any associated contractual relationships)? From which entities must the customer obtain consent before effecting such a transfer?
- b. Does the CCP have the authority to mandate that a CM transfer any or all of its customer positions and initial and variation margin (and any associated contractual relationships) to another clearing member, if such CM is not in "default" (as defined in the CCP's rules)?

²¹ See note 6.

- i. Does the answer change if the CM, although not in default, is perceived by the CCP to be in a state of impending financial distress?
 - ii. To what extent is a default under the CCP's rules the product of the CCP's subjective determination, rather than being determined by reference to objectively verifiable events?
- c. How does the CCP intend to transfer customer positions and initial and variation margin (and any associated contractual relationships) from a defaulting CM to a non-defaulting CM? Please elaborate on the following details (distinguishing between Required Margin, CCP Excess Margin, Dealer Excess Margin and any other categories of margin where relevant):
- i. The expected timeline from CM default to re-establishment of customer positions and initial and variation margin (and any associated contractual relationships) at a non-defaulting CM;
 - ii. The mechanism for transferring customer positions and initial and variation margin (and any associated contractual relationships) to a non-defaulting CM, including a description of:
 - 1. How customer positions and initial and variation margin (and any associated contractual relationships) are allocated and how transferee CMs are selected (including whether a non-defaulting CM and its customers can be forced by the CCP to accept a transfer of positions through auction, assignment or other allocation procedures);
 - 2. Whether customer positions and initial and variation margin (and any associated contractual relationships) in respect of cleared transactions can be effectively transferred separately from non-cleared transactions between the defaulting CM and its customers;
 - 3. Whether the treatment of CCP Margin differs from the treatment of Dealer Margin, from a portability perspective; and
 - 4. Any pledge or other arrangements designed to facilitate transfer of customer positions and initial and variation margin (and any associated contractual relationships).
 - iii. Any procedures designed to control the effect of market movements on the value of customer positions during the pendency of the transfer – e.g., institution of hedge positions subsequent to the CM default, or assigned allocation of customer

margin deficits to non-defaulting CMs – and the allocation of losses if the customer positions cannot be assigned to a non-defaulting CM.

1. Who determines the close-out price applicable to terminated positions? If the CCP, does the CCP's close-out price flow through to the customer? How is the close-out price determined? Does the same close-out price apply to CM-customer positions and offsetting CM-CCP proprietary positions?
 2. How does the CCP account for any unpaid variation margin obligations that may have accrued subsequent to the default of the CM?
- iv. Any limitations on the rights of customers to (a) terminate non-cleared transactions with CMs upon a CM default, or (b) set off their obligations under non-cleared transactions against obligations to CMs under cleared transactions;
 - v. Whether affiliate and third-party liens or cross-margining and netting arrangements in respect of non-cleared transactions affect the portability analysis;
 - vi. Whether the defaulting CM's contractual agreements with the customer are binding upon the transferee CM and such customer upon any transfer of the customer's positions and initial and variation margin, or whether the transferee CM and such customer can (or must) execute a new set of documentation;
 - vii. In connection with a transfer of customer positions and initial and variation margin (and any associated contractual relationships) to a non-defaulting CM, any rights of customers to elect not to transfer the associated margin, and instead, to apply such margin as a setoff against other amounts that may be payable to the defaulting CM (while separately posting new IM to the transferee CM); and
 - viii. The effects on the portability analysis of (a) IM at the CCP for customer positions being posted on a gross or net basis (as applicable), (b) the existence of Dealer Margin held at the defaulting CM, and (c) non-cleared trades between the defaulting CM and its customers being "in-the-money" or "out-of-the-money" (as applicable) to the CM.

D. Documentation

Required Documentation

1. What trading documentation will CMs (and their custodians, if applicable) and customers need to execute with the CCP (and its custodian, if applicable) in order to have customer transactions cleared?
 - a. Please discuss the extent to which the CCP “knows” the customers under the required documentation, and how this affects the customer protection analysis.
2. What trading documentation will customers need to execute with CMs (and their custodians, if applicable) in order to have their transactions cleared?
3. Please describe any legal, operational or other issues arising from the adoption by CMs and customers of a pledge arrangement (from an existing title transfer structure), or of a title transfer arrangement (from an existing pledge structure), for the provision of collateral security.

[See Section III, B, 6.](#)

Key Terms of Standardised Documentation

4. Please describe the material terms of any documentation standardised by the CCP, including (but not limited to) terms relating to:
 - a. Circumstances under which posted margin may be returned to customers, and all related conditions and requirements;
 - b. Specification of events of default and termination events with respect to the CM (noting any distinctions drawn between insolvency and non-insolvency events) or customer;
 - c. Standstill upon the occurrence of a CM default;
 - d. Advance elections to liquidate or transfer cleared contracts;
 - e. Advance consents (particularly those obtained to enhance portability of cleared contracts);
 - f. Limitations on rehypothecation;
 - g. Limitations on setoff against non-cleared bilateral transactions between customers and their CMs; and
 - h. Close-out calculations.

[See Section III, B, 6.](#)

Modification of Proposed Clearing Structure

5. Please state the circumstances in which the CCP has the ability to amend by rule or order any aspect of its proposed clearing structure.

[See Section III.9.](#)

II. Legal Considerations

As stated in the introductory note to this questionnaire, the following questions should be considered under the laws of all jurisdictions relevant to the CCP (and its custodian, if applicable), the CMs (and their custodians, if applicable) and the customers. In the responses below, please highlight any areas of legal uncertainty. For matters requiring reasoned legal judgment, please state the level of legal comfort associated with the relevant response.

[See Section IV.](#)

Customer Rights to CCP Margin

1. Please detail the ability of customers to recover IM held at the CCP (or the CCP's custodian) upon the insolvency of the CCP (or the CCP's custodian) – distinguishing between Required Margin, CCP Excess Margin, Dealer Excess Margin and any other categories of margin where relevant – in the event their positions are liquidated rather than transferred. Consider all relevant facts, including: (i) the manner in which the IM is held at the CCP or its custodian; (ii) the nature of the customer obligations secured by liens on the IM; (iii) the composition of the IM (e.g., whether the IM consists of securities or cash); (iv) in the event of the insolvency of the CCP's custodian, any restrictions (legal or otherwise) on the ability of the CCP to recover IM from the insolvent custodian; and (v) any other matters described in your responses to the questions above that are relevant to this analysis. Analyse how these facts ultimately affect the conclusions reached.
 - a. What is the legal nature of the customers' rights in the IM held at the CCP (or the CCP's custodian)?
 - i. To the extent relevant to this analysis, please consider whether customers hold proprietary (i.e., ownership) rights in the IM held at the CCP (or the CCP's custodian), or merely contractual rights to recovery of the IM vis-à-vis the defaulted CCP (or the CCP's custodian).
 1. How does the selection of pledge versus title transfer for the provision of collateral security affect this determination?

2. What are the relevant legal standards with respect to tracing or other requirements necessary to demonstrate proprietary rights in the IM?
3. What is the practical effect of maintaining proprietary versus contractual rights?
 - ii. If the distinction between proprietary versus contractual rights to the IM held at the CCP (or the CCP's custodian) is irrelevant as a legal matter, please describe the legal framework that is relevant to the analysis.
- b. How is a shortfall in CCP Margin and other custodial property (i.e., property held in a custodial capacity for purposes unrelated to the clearing of CDS) held by the CCP (or its custodian) allocated as between the CCP (or the CCP's custodian), the CMs, the customers (as a group and individually) and other custodial claimants? Distinguish where relevant between Required Margin, CCP Excess Margin, Dealer Excess Margin and any other categories of margin.
 - i. With what other types of custodial claimants may the customers potentially be required to share with in the event of a shortfall in custodial property?
 1. Are there any applicable regulatory regimes that limit the claims of those who may share in CCP Margin?
 - ii. Is it possible to contractually vary the sharing regime that would otherwise apply in any particular instance (e.g., by holding CCP Margin at a third party custodian)?

Customer Rights to Dealer Margin

2. Please detail the ability of customers to recover IM held at the CM (or the CM's custodian) upon the insolvency of the CM (or the CM's custodian) – distinguishing between Required Margin, CCP Excess Margin, Dealer Excess Margin and any other categories of margin where relevant – in the event their positions are liquidated rather than transferred. Consider all relevant facts, including: (i) the manner in which the IM is held at the CM or its custodian; (ii) the nature of the customer obligations secured by liens on the IM; (iii) the composition of the IM (e.g., whether IM consists of securities or cash); (iv) in the event of the insolvency of the CM's custodian, any restrictions (legal or otherwise) on the ability of the CM to recover IM from the insolvent custodian; and (v) any other matters described in your responses to the questions above that are relevant to this analysis. Analyse how these facts ultimately affect the conclusions reached.

- a. What is the legal nature of the customers' rights in the IM held at the CM (or the CM's custodian)?
 - iii. To the extent relevant to this analysis, please consider whether customers hold proprietary (i.e., ownership) rights in the IM held at the CM (or the CM's custodian), or merely contractual rights to recovery of the IM vis-à-vis the CM (or the CM's custodian).
 1. How does the selection of pledge versus title transfer for the provision of collateral security affect this determination?
 2. What are the relevant legal standards with respect to tracing or other requirements necessary to demonstrate proprietary rights in the IM?
 3. What is the practical effect of maintaining proprietary versus contractual rights?
 - iv. If the distinction between proprietary versus contractual rights to the IM held at the CM (or the CM's custodian) is irrelevant as a legal matter, please discuss the legal framework that is relevant to the analysis.
- b. How is a shortfall in Dealer Margin and other custodial property (i.e., property held in a custodial capacity for purposes unrelated to cleared CDS) held by the CM (or its custodian) allocated as between the CMs, the customers (as a group and individually) and other custodial claimants? Distinguish where applicable between Required Margin, CCP Excess Margin, Dealer Excess Margin and any other categories of margin where relevant.
 - v. Are there any applicable regulatory regimes that limit the claims of those who may share in Dealer Margin?
 - vi. Is it possible to contractually vary the sharing regime that would otherwise apply in any particular instance (e.g., by holding Dealer Margin at a third party custodian)?

Legal Enforceability of Portability Framework

3. Please discuss the legal enforceability of the CCP's portability framework in the event of either or both (i) a CM insolvency (or the insolvency of the CM's custodian) and/or (ii) a customer insolvency. In particular, consider how the enforceability of the portability framework is affected by the following:

- a. Whether, if either the CCP or insolvency trustee/receiver of the CM transfers any cleared positions and margin (and any associated contractual relationships) of the defaulted CM with the CCP, it must also transfer the defaulting CM's (i) other cleared positions and margin (and any associated contractual relationships) with the CCP, and (ii) non-cleared positions (and associated margin and contractual relationships) with customers of the defaulting CM;
- b. The effect of any standstill provisions upon default, and the interplay of such provisions with any statutorily protected termination rights;
- c. Any affiliate and third-party liens or cross-margining and netting arrangements;
- d. Any setoff rights or limitations between cleared and non-cleared trades;
- e. Any mandatory setoff requirements for CMs or customers under applicable law;
- f. Any pledge arrangements or other provisions for collateral security between CMs and customers related to cleared transactions; and
- g. Whether the CM is acting as principal (rather than as agent) vis-à-vis the CCP in respect of customer transactions.

Legal Enforceability of Novation/Netting Framework

4. Please discuss the legal enforceability of the CCP's novation and netting framework in the event of either or both (i) a CM insolvency (or the insolvency of the CM's custodian) or (ii) a customer insolvency, giving due regard to the CCP's ability (and, in the event of a customer insolvency, a CM's ability) to exercise its legal and contractual remedies on (a) IM held at the CCP (or the CCP's custodian) and (b) IM held at the CM (or the CM's custodian).
 - a. How would challenges to the validity or enforceability to an underlying bilateral transaction (prior to novation) – e.g., if a transaction was entered into in bad faith, fraudulently, or in contemplation of insolvency – affect the enforceability of the novated transaction, in the event of either or both (i) a CM insolvency or (ii) a customer insolvency?

Considerations Relating to Netting vis-à-vis the CCP

5. Please evaluate, from an accounting and regulatory capital perspective, the ability of CMs to net (i) proprietary positions against other proprietary positions and (ii) customer positions against proprietary positions, in each case vis-à-vis the CCP, upon a CCP default or insolvency.

Enforcement and Monitoring Mechanisms

6. Please describe any enforcement or monitoring mechanisms (imposed by the CCP, applicable regulatory authorities or otherwise) designed to ensure that CMs (and their custodians, to the extent applicable) comply with their obligations in respect of any legal or contractual requirements described in your response above.

Legislative or Regulatory Reforms

7. As requested above, please identify in your responses above any areas of legal uncertainty and the level of legal comfort provided on various aspects of the proposed framework. Please consider whether there are any legislative or regulatory reforms that would be helpful to clarify or improve the legal framework governing any of the foregoing issues and areas of legal uncertainty identified above. If so, describe any such proposed reforms in detail.

Other Considerations

8. Please feel free to elaborate on any topic you deem to be relevant to the analysis of customer protection or systemic risk issues.