[Name of Bank/Broker]

Policies and Procedures [Manual/Handbook]

for the margining of uncleared swaps under EMIR

Contents

1. About this document

1.1 This document contains the policies and procedures of [ ] (the "**[Bank/Broker]**") with respect to margining of uncleared OTC derivative transactions under the EMIR Rules.

1.2 Defined terms are set out in paragraph 14.

1.3 This version of this document is dated as of [ ] 2017 and was prepared by [ ] and was approved by [ ] on [ ].

2. Background

2.1 The EMIR Rules

2.1.1 The EMIR Rules were developed by the Joint Committee of the European Supervisory Authorities to define the risk-mitigation techniques for OTC derivative contracts not cleared by a Central Counterparty, as laid out in Article 11 of EMIR.

2.1.2 The EMIR Rules require:

(a) counterparties to exchange VM with regards to the uncleared transactions. This requirement takes effect from 1 March 2017;

(b) counterparties to exchange IM with regards to the uncleared transactions. This requirement takes effect from 4 February 2017, with transitioning (see paragraph 3.1.4 below);

(c) counterparties to have in place appropriate netting and collateral agreements and to conduct a legal review of the effectiveness thereof (see paragraph 5 below);

(d) counterparties to establish policies and procedures as to various matters (see paragraph 2.4 below).

2.1.3 This document sets out the [Bank/Broker]'s policies and procedures as to the manner in which it will comply with the EMIR Rules.

2.2 Counterparties covered

2.2.1 The requirements under the EMIR Rules apply to all EU financial counterparties (FCs) and EU non-financial counterparties (NFCs) whose OTC derivative contracts are over the clearing threshold (NFC+s).

2.2.2 EMIR does not apply to European Central Banks or the BIS (EMIR Article 1(4))).

2.2.3 Other than the transaction reporting requirements, EMIR does not apply to certain multi-lateral developments banks, certain public sector entities, the European Financial Stability Facility and the European Stability Mechanism (EMIR Article 1(5)).

2.2.4 For counterparties to whom the EMIR Rules apply, the EMIR Rules also extend to those counterparties with whom they enter into uncleared OTC derivative transactions which are:

(a) EU non-financial counterparties whose OTC derivative contracts are below the clearing threshold (NFC-s);

(b) non-EU counterparties which would be FCs or NFC+s if they were established in the EU (TCEs).

2.2.5 The EU Commission has adopted a delegated act to disapply EMIR to central banks of the US and Japan. The EU Commission has consulted on a delegated act which, when adopted, would also disapply EMIR to the following non-EU central banks:

Australia, Canada, Hong Kong, Mexico, Singapore and Switzerland.

2.2.6 All other non-EU central banks are the equivalent of NFCs and, if over the clearing threshold, would be the equivalent of NFC+s.

2.2.7 Notwithstanding paragraph 2.2.4(a) an entity to whom the EMIR Rules applies may, as a matter of policy, decide not to exchange VM or IM with NFC-s. (Art 23) – see further paragraph 12.2.

2.3 Transactions covered

2.3.1 The EMIR Rules apply to uncleared OTC derivative contracts entered into after the date when the EMIR Rules specify.

2.3.2 For VM the date of application of the EMIR Rules is 1 March 2017.

2.3.3 For IM the date of application of the EMIR Rules is phased in depending on the AANA of both counterparties – see paragraph 3.1.4 below.

2.3.4 Notwithstanding that the EMIR Rules only apply to the margining of new uncleared OTC derivative contracts, it is the [Bank/Broker]'s policy to:

(a) exchange VM in accordance with the EMIR Rules for new and legacy transactions together (save where there are commercial reasons not to do so (such exceptions to be approved on a case by case basis by [ ]);

(b) exchange IM only where required under the EMIR Rules for new transactions only save where there are commercial reasons not to do so (such exceptions to be approved on a case by case basis by [ ]).

2.3.5 Consistent with the industry position, the [Bank/Broker]'s policy is to treat the following as if a new OTC derivative contract had been entered into:

(a) Novation or assignment of an existing OTC derivative transaction to the [Bank/Broker];

(b) Any increase in the notional amount of an existing OTC derivative transaction;

(c) Any increase to the maturity date of any existing OTC derivative transaction;

(d) Any change to the terms of an existing OTC derivative transaction which is material in economic terms;

(e) Any other change to the terms of an existing OTC derivative transaction which is material in that it changes the nature of the transaction.

2.3.6 The EMIR Rules requirements with respect to VM apply to all types of uncleared OTC transactions entered into after 1 March 2017, subject to the following:

(a) With respect to physically settled FX forwards the requirements of the EMIR Rules to exchange VM are deferred until the earlier of 31 December 2018 and the date of entry

into application of certain clarifications to the definition of physically settled FX forwards under the MiFID2 framework. (Art 37(2)). This means that the [Bank/Broker] is not required under the EMIR Rules to exchange VM for such transactions entered into before such date. However, the [Bank/Broker]'s policy is to margin the transactions on an EMIR Rules basis in any event [save only for trading relationships where the only product traded is physically settled FX and there are no existing ISDA/CSA trading documents in place. In those cases, the [Bank/Broker]'s policy is to try to enter into an ISDA/CSA (on an EMIR Rule compliant basis) before the date on which such transactions are subject to the VM requirements.

(b) Under the EMIR Rules there is no requirement to exchange VM with respect to single-stock equity options and index options until 4 January 2020. The [Bank/Broker]'s policy is to margin these transactions on an EMIR Rules basis in any event.

2.3.7 The requirements with respect to IM apply to all types of uncleared OTC transactions entered into with IM in-scope Entities after the applicable phase in date (see paragraph 3.1.4 below), provided that an FC or NFC+ may provide in its risk management procedures that IM is not collected with respect to the following:

(a) physically settled FX forwards;

(b) FX swaps; and

(c) the exchange of principal of uncleared currency swaps (Art 27).

2.3.8 [It is anticipated that the][The [Bank/Broker]'s policy [will be][is] not to apply IM with respect to such transactions.

2.4 Policies and Procedures

2.4.1 Under the EMIR Rules (Art 2(2)), counterparties are under an obligation to establish, apply and document risk management procedures for the exchange of collateral for uncleared OTC derivatives which provide for or specify:

(a) the eligibility of collateral for uncleared OTC derivatives in accordance with Section 2 of the EMIR Rules – these are contained in paragraph 6;

(b) the calculation and collection of margin for uncleared OTC derivatives in accordance with Section 3 of the EMIR Rules – these are contained in paragraph 8 and 9;

(c) the management and segregation of IM for uncleared OTC derivatives in accordance with Section 5 of the EMIR Rules – [these will be developed before the [Bank/Broker] is subject to the requirement to exchange IM];

(d) the calculation of the adjusted value of collateral in accordance with Section 6 of the EMIR Rules – these are contained in paragraph 7;

(e) the exchange of information between counterparties and the authorisation and recording of any exceptions to its risk management procedures – these are contained in paragraph 13.1;

(f) the reporting of the exceptions set out in Chapter II of the EMIR Rules to senior management - these are contained in paragraph 13.2;

(g) the terms of all necessary agreements to be entered into by counterparties, at the latest, at the moment in which an uncleared OTC derivative contract is concluded, including the terms of the netting agreement and the terms of the exchange of collateral agreement in accordance with Article 3 of the EMIR Rules - these are contained in paragraph 4;

(h) the periodic verification of the liquidity of the collateral to be exchanged - these are referred to in paragraph 7.3 and are not required by the [Bank/Broker] for the reason stated;

(i) the timely re-appropriation of the collateral in the event of default by the posting counterparty from the collecting counterparty - these [are/will be] contained in paragraph 9.5 and are only applicable to IM; and

(j) the regular monitoring of the exposures arising from OTC derivative contracts that are intragroup transactions and the timely settlement of the obligations resulting from those contracts - these are contained in paragraph 12.6.5 and apply where the intragroup exemption is granted or applied for.

2.4.2 These risk management procedures should be tested, reviewed and updated as necessary and at least annually (Art 2(5)).

2.4.3 Additionally where FCs and NFC+s enter into a netting agreement or an exchange of collateral agreement, they shall perform an independent legal review of the enforceability of those agreements. That review may be conducted by an internal independent unit or by an independent third party. However, the requirement to perform the review referred to in the first subparagraph shall be considered to be satisfied in relation to the netting agreement where that agreement is recognised in accordance with Article 296 of CRR (Art 2(3)).

2.4.4 FCs and NFC+s are also required to establish policies to assess on a continuous basis the enforceability of the netting and the exchange of collateral agreements that they enter into (Art 2(4).

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14. Defined Terms

14.1.1 **AANA** means the aggregate average notional amount of uncleared OTC derivatives determined in accordance with Art 36 of the EMIR Rules as described in paragraph 3.1.4.

14.1.2 **Central Counterparty** means a legal person that interposes itself between the counterparties to the contracts traded on one or more financial markets, becoming the buyer to every seller and the seller to every buyer. A Central Counterparty need not be a CCP authorised under EMIR.

14.1.3 **Credit Support Annex** means a 1995 ISDA Credit Support Annex (English law – transfer) or a 1994 ISDA Credit Support Annex (New York law) or a 2016 ISDA VM Credit Support Annex (English law – transfer) or a 2016 ISDA VM Credit Support Annex (New York law).

14.1.4 **CRR** means Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms.

14.1.5 **EMIR** means Regulation (EU) No 648/2012 of the European Parliament and of the Council of July 2012 on OTC derivatives, central counterparties and trade repositories.

14.1.6 **EMIR Rules** means Commission Delegated Regulation of 4 October 2016 supplementing EMIR with regard to regulatory technical standards for risk-mitigation techniques for OTC derivatives not cleared by a central counterparty.

14.1.7 **FC** means a financial counterparty under EMIR being a credit institution, investment firm, pension scheme, UCITS, an alternative investment firm management by an AIFM.

14.1.8 **group** means, with respect to an entity, that entity and the other entities in the world-wide accounting group of which it forms part.

14.1.9 **IM** means collateral calculated in accordance with the EMIR Rules that is collected or posted in respect of an uncleared OTC derivative transaction in order to cover the potential future exposure in the interval between the last exchange of VM and the liquidation of positions following a default.

14.1.10 **IM Credit Support Documents** means a 1995 ISDA Credit Support Deed or an 1994 ISDA Credit Support Annex (New York law), in each case, adapted for the provision only of IM or a 2016 ISDA Credit Support Deed (IM) or a 2016 ISDA Credit Support Annex (New York law) (IM), in all cases together with the relevant account control agreement(s), however described, between the parties thereto the their applicable custodian(s).

14.1.11 **IM In-Scope Entity** means, at any time, an entity which is subject to the requirement to exchange IM under the EMIR Rules at that time.

14.1.12 **IM Model** means a model to determine the amount of IM required to be exchanged under the EMIR Rules.

14.1.13 **ISDA** means The International Swap & Derivatives Association, Inc.

14.1.14 **ISDA Master Agreement** means a 1992 ISDA Master Agreement or a 2002 ISDA Master Agreement.

14.1.15 **NFC** means an undertaking established in the European Union other than a financial counterparty or a Central Counterparty

14.1.16 **NFC+** means an NFC which has crossed the clearing threshold and is subject to the clearing obligations pursuant to Article 10(1)(b) of EMIR

14.1.17 **NFC-** means an NFC which has not exceeded the clearing thresholds in EMIR

14.1.18 **OTC derivative transaction or contract** means a derivative contract the execution of which does not take place on a regulated market as within the meaning of Article 4(1)(14) of Directive 2004/36/EC or on a third-country market considered as equivalent to a regulated market in accordance with Article 19(6) of Directive 2004/39/EC.

14.1.19 **TCE** means non-EU counterparties which would be FCs or NFC+s if they were established in the EU.

14.1.20 **uncleared OTC derivative transaction or contract** means an OTC derivative transaction or contract which is not cleared through a Central Counterparty.

14.1.21 **VM** means collateral provided by one party to its counterparty to meet the performance of its obligations under one or more OTC derivative transactions between the parties as a result of a change in value of such obligations since the last time such collateral was provided.

Appendix 1

Eligible Collateral (Art 4)

The following assets are eligible as collateral under the EMIR Rules

(a) cash in the form of money credited to an account in any currency, or similar claims for the repayment of money, such as money market deposits;

(b) gold in the form of allocated pure gold bullion of recognised good delivery;

(c) debt securities issued by Member States' central governments or central banks;

(d) debt securities issued by Member States' regional governments or local authorities whose exposures are treated as exposures to the central government of that Member State in accordance with Article 115(2) of CRR;

(e) debt securities issued by Member States' public sector entities whose exposures are treated as exposures to the central government, regional government or local authority of that Member State in accordance with Article 116(4) of CRR

(f) debt securities issued by Member States' regional governments or local authorities other than those referred to in point (d);

(g) debt securities issued by Member States' public sector entities other than those referred to in point (e);

(h) debt securities issued by multilateral development banks listed in Article 117(2) of CRR;

(i) debt securities issued by the international organisations listed in Article 118 of CRR;

(j) debt securities issued by third countries' governments or central banks;

(k) debt securities issued by third countries' regional governments or local authorities that meet the requirements of points (d) and (e);

(l) debt securities issued by third countries' regional governments or local authorities other than those referred to in points (d) and (e);

(m) debt securities issued by credit institutions or investment firms including bonds referred to in Article 52(4) of Directive 2009/65/EC of the European Parliament and of the Council(1);

(n) corporate bonds;

(o) the most senior tranche of a securitisation, as defined in Article 4(61) of CRR, that is not a re-securitisation as defined in Article 4(63) of CRR;

(p) convertible bonds provided that they can be converted only into equities which are included in an index specified pursuant to point (a) of Article 197(8) of CRR;

(q) equities included in an index specified pursuant to point (a) of Article 197(8) of CRR;

(r) shares or units in undertakings for collective investments in transferable securities (UCITS), provided that the conditions set out in Article 5 are met.

A counterparty shall only collect collateral from the asset classes referred to in points (f), (g) and (k) to (r) where all the following conditions apply:

(i) the assets are not issued by the posting counterparty;

(ii) the assets are not issued by entities which are part of the group to which the posting counterparty belongs;

(iii) the assets are not otherwise subject to any significant wrong way risk, as defined in points (a) and (b) of paragraph 1 of Article 291 of CRR.

(1)Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) (OJ L 302, 17.11.2009, p. 32).

Appendix 2

Annex II to the EMIR Rules

Methodology to adjust the value of collateral for the purposes of Article 21

1. The value of the collateral shall be adjusted as follows:

$C_{value} = C \cdot (1 - H_C - H_{FX})$

where:

C = the market value of the collateral;

H_C = the haircut appropriate to the collateral, as calculated under paragraph 2;

H_{FX} = the haircut appropriate to currency mismatch, as calculated under paragraph 6.

2. Counterparties shall apply at least the haircuts provided in the following Tables 1 and 2 to the market value of the collateral:

Table 1

Haircuts for long term credit quality assessments

Credit quality step with which the credit assessment of the debt security is associated	Residual maturity	Haircuts for debt securities issued by entities described in Article 4 (1) (c) to (e) and (h) to (k), in (%)	Haircuts for debt securities issued by entities described in Article 4 (1) (f), (g), (l) to (n) in (%)	Haircuts for securitisation positions meeting the criteria in Article 4 (1) (o) in (%)
1	≤ 1 year	0,5	1	2
	> 1 ≤ 5 years	2	4	8
	> 5 years	4	8	16
2-3	≤ 1 year	1	2	4
	> 1 ≤ 5 years	3	6	12
	> 5 years	6	12	24
4 or below	≤ 1 year	15	N/A	N/A
	> 1 ≤ 5 years	15	N/A	N/A
	> 5 years	15	N/A	N/A

Table 2

Haircuts for short term credit quality assessments

Credit quality step with which the credit assessment of a short term debt security is associated	Haircuts for debt securities issued by entities described in Article 4(1) (c) and (j) in (%)	Haircuts for debt securities issued by entities described in Article 4(1) (m) in (%)	Haircuts for securitisation positions and meeting the criteria in Article 4(1) (o) in (%)
1	0,5	1	2
2-3 or below	1	2	4

1. Equities in main indices, bonds convertible to equities in main indices and gold shall have a haircut of 15 %.

2. For eligible units in UCITS the haircut is the weighted average of the haircuts that would apply to the assets in which the fund is invested.

3. Cash variation margin shall be subject to a haircut of 0 %.

4. For the purpose of exchanging VM, a haircut of 8 % shall apply to all non-cash collateral posted in a currency other than those agreed in an individual derivative contract, the relevant governing master netting agreement or the relevant credit support annex.

5. For the purpose of exchanging initial margin, a haircut of 8 % shall apply to all cash and non-cash collateral posted in a currency other than the currency in which the payments in case of early termination or default have to be made in accordance with the single derivative contract, the relevant exchange of collateral agreement or the relevant credit support annex ('termination currency'). Each of the counterparties may choose a different termination currency. Where the agreement does not identify a termination currency, the haircut shall apply to the market value of all the assets posted as collateral.

The rating category per credit quality step for the purposes of Article 15 of the Commission Implementing Regulation (EU) 2016/1799 is set out in Annex II to that Regulation. The correspondence of the rating categories of each ratings agency with the credit quality step is set out in Annex III to that Regulation.