

KEY ASPECTS OF THE DEFAULT MANAGEMENT PROCEDURES

of Nasdaq Clearing AB

Circumstances which constitute a “default”

The circumstances when a clearing member or customer (with a direct contractual relationship with the clearing house) of Nasdaq Clearing AB is considered to be in default are stated in section 1.8 in the Clearing Rules of Nasdaq Derivatives Markets and in section 8 in the General terms of the Clearing Rules – Commodity Derivatives, respectively. These include an actual or an anticipated breach of the rules and regulations governing the clearing house’s operations and circumstances where a clearing member is no longer deemed suitable, e.g. as a consequence of its insolvency, the withdrawal of its license or its suspension from another exchange or clearing house.

The default process and decision-making

The Default Committee is the single decision-making authority within Nasdaq Clearing for evaluating default situations and events and deciding which actions to be taken as permitted under the Rules of Nasdaq Clearing as well as any applicable legal agreements. The Default Committee is made up of the following representatives in order to help ensure that all decision(s) made are well informed.

Members of the Clearing Default Committee:

- Chief Executive Officer (CEO), President of Nasdaq Clearing (veto)
- Chief Risk Officer (CRO) of Nasdaq Clearing (chair)
- Chief Technology Officer (CTO) of Nasdaq Clearing
- Chief Compliance Officer (CCO) of Nasdaq Clearing
- Representative from Legal
- Representatives from Treasury
- Representative from Group Risk Management (observer – no quorum)
- Representative from Communications (observer – no quorum)
- Any other person(s) deemed appropriate by the Default Committee during a default situation.

The Chairman and President have veto in the decision making of the Default Committee.

Non-compliant participants and default procedures

Nasdaq Clearing is continuously reviewing clearing participants to ensure that they fulfill the participant requirements as stipulated in the rules and regulations of Nasdaq Clearing. In case of a breach of the requirements, the participant is considered to be in “technical default” and Clearing Risk Management will present the breach to the Default Committee, which will decide on appropriate actions to be taken. In cases where the participant does not immediately address the breach, the Default Committee can decide on temporary exceptions to the participant requirements before declaring a default, if the risk of doing so can be mitigated. The exception shall be limited in time and can be set with a condition of an extraordinary margin requirement for the non-compliant participant. Any temporary exception may not, including extra margin, result in material increased risk for Nasdaq Clearing. Possible temporary and/or permanent actions could, among other things, include;

- Require the participant to post a parent company guarantee (if possible)
- Require the participant to conduct a capital injection
- Add a temporary extraordinary margin requirement to mitigate the risk of not fulfilling the requirements
- Only accept risk reducing transactions
- Suspend the participant from trading and/or clearing

Nasdaq Clearing may charge the non-compliant member for any costs associated with the additional review or other measures that are taken (such as obtaining a legal opinion etc). If temporary measures are not sufficient or if the participant does not address the breach, the clearing house may proceed to declare a default.

Default management measures

If clearing members, clearing clients, direct pledging customers or indirect pledging customers are declared in default, Nasdaq Clearing has the right to elect, at the expense of the defaulting party, to take one or more of the measures summarized below, provided that client/customer accounts must be treated in accordance with the rules and procedures for segregation and porting. Unless otherwise specified, Nasdaq Clearing has the right to take such measures without consulting the defaulting party in advance. Please note that the below is only a summary of the relevant sections of the Rules.

- Withhold settlement or delivery due to the defaulting counterparty.
- To declare any obligations of the counterparty to be due and payable and set-off any obligations due to the counterparty against any obligations due to Nasdaq Clearing.
- To refuse registration of any transactions.
- To effect a close-out in respect of the counterparty’s positions.
- To enter into hedging transactions.
- To buy or sell positions on behalf of the counterparty.
- To settle the counterparty’s contracts in advance, in whole or in part.
- To liquidate or appropriate collateral posted by the counterparty.
- To convert collateral to required currency.
- To purchase or sell deliverable instruments or the contract base, cancel the counterparty’s settlement obligation and claim compensation.

- To terminate any Customer/Clearing Client Agreements to which a defaulting clearing member is a party.
- To terminate the clearing membership or Customer Agreement of the defaulting counterparty.

Client or customer accounts

Client or customer collateral and positions may be transferred to a back-up clearing member when so required by the client(s) in the relevant account and where accepted by such back-up clearing member within the so-called porting window (which is currently 24 hours). The defaulting clearing member's approval is not required to initiate porting.

In the absence of porting (i.e. where porting is not requested or is not successful) the clearing house will close out the positions in the account and apply collateral provided against such positions as necessary, and pay out the remaining balance in the account to the relevant client(s) directly or, if the identity of the client(s) is not known to the clearing house, to the defaulting clearing member for the account of the client(s).

Close out of portfolios

The following is applicable if the Default Committee decides that the defaulting portfolio(s) shall be liquidated.

The Default Committee has the mandate to act in every possible way, acting within the Rules, to reduce the risk in the portfolio. This means that Default Committee is authorized by the Board to choose whatever solution adequate to reduce or eliminate the risk exposure. In this respect, there are different ways to reduce and eliminate the risk exposure:

- Open new trades/positions to create synthetic hedges (which do not need to be perfect hedges as long as they have a substantial risk reducing effect)
- Close out trades
- Prioritize close out based on a risk assessment

The Default Committee decides on the process of closing out trades/reducing risk, but the process will be depending of internal and external factors.

The Default Committee shall consider all possible ways to close down positions. All possible channels shall be considered:

- Close out trades on the OTC market through brokers
- Close out trades directly towards clearing members: open or closed "auction sale", collect binding bid/ask prices from clearing members
- Supervised close out, i.e letting the defaulting party do the close out trades by itself
- Close out trades on the exchange, depending on liquidity and impact on market prices

Default Strategy

Head of Risk Management Financial Market and Head of Risk Management Commodities are responsible to maintain updated pre-defined strategies on how to act and close out a defaulting position for their respective asset class(es).

The default strategies shall be recorded in documents (each a Default Strategy) which should include instructions on:

- Risk assessment of the portfolio, including risk measures

- Hedging methods, including available instruments
- Means of execution (auction, orderbook, OTC, close out providers etc)
- Execution contact list

The Default Strategies shall be approved and reviewed by the Default Committee. Further information regarding default strategies can be found on Nasdaq Clearing Risk Management webpage, <http://www.nasdaqomx.com/transactions/posttrade/clearing/europeanclearing/risk-management>

This document is made available on Nasdaq Clearing's website to address the requirement laid down in Commission Delegated Regulation (EU) No 153/2013 art. 61.2 to make key aspects of the clearing house's default procedures publicly available. This version was reviewed and adopted by the Default Committee (Default Committee) of Nasdaq Clearing on December 22, 2015.