



To the Members of SIX x-clear Ltd

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Kontaktperson:

Zürich, 12 January 2016

SIX x-clear Ltd:
Consultation process for the new Financial Collateral Agreement

Dear Sir/Madam,

In accordance with the regulations governing the amendment of agreements pursuant to the Contract for Clearing Services (section 3), please find enclosed our draft of the new **Financial Collateral Agreement** for consultation purposes.

This is a wide-ranging agreement, which governs all key points with regard to the collateralisation of risks arising in the Clearing business with SIX x-clear. The two currently established agreements – the “Pledge Agreement for Margins” and the “Pledge Agreement for Default Funds” – as well as the “Agreement on the Amendment of the two Pledge Agreements” have been combined and integrated into a single document. Furthermore, individual detailed regulations can continue to be found in the General Terms and Conditions and the Lending Norms (so-called “Contractual Relationship”).

At a material level, we intend to expand the scope and purpose of Collateral provided. Specifically, the following material changes and additions shall be made:

1. Change from a regular to irregular pledge in the Default Fund

While an irregular pledge is not enshrined in Swiss law from a legal perspective, it is accepted and widely documented by case law and scholars as a legal form, in particular with regard to financial contracts. With a view to European countries outside Switzerland, Article 6 of the applicable EU Directive 2002/47/EC concerning financial collateral arrangements expressly demands that member states must ensure that a financial collateral arrangement “can take effect in accordance with its terms” in the form of a “title transfer arrangement” or irregular pledge. The rights and obligations of the parties are thus determined in line with the agreement and not according to rules of substantive law (no “conditional proprietary right in rem”).

Due to its full contractual involvement in the trades of its Members, SIX x-clear Ltd considers a full transfer of ownership of the collateral to be adequate, even with regard to Default Fund Contributions.



Furthermore, an irregular pledge enables SIX x-clear to use the collateral in a legally sound and administratively efficient manner to ensure its own liquidity and for short-term investments.

By switching from a regular pledge to a full title transfer for the Default Fund Contributions, it is ultimately possible to combine the two agreements and optimise the consistency and clarity of the regulations.

2. Strengthening of system for Collateral

SIX x-clear intends to introduce an additional layer in the system of collateral ("waterfall of resources") – the so-called "**Top-up Contribution**". This element would come into effect as a resource in the event of a very large loss (Default) or of several major defaults – but only if all preceding layers of collateral (in particular the entire Default Fund) have been exhausted. The Top-up Contribution could therefore be claimed for each exceeding (uncovered) loss in the following two possible basic scenarios:

- An individual Default exceeds all preceding resources (pursuant to chapter 18 GTC), i.e. the Defaulting Member's own Margins, the Defaulting Member's own Default Fund Contribution, the Dedicated Capital Contribution of SIX x-clear Ltd as well as the entire amount of the aggregated Default Fund Contributions of the non-defaulting Members to the relevant Default Fund Segment;

Numerical example:

Dedicated Capital Contribution of SIX x-clear AG ("skin in the game") = 22; Default Fund Segment = 300; total loss from a Default exceeds the Default Fund Segment by 28. A Top-up Contribution of 28 is requested from the remaining Members.

- One or more additional Defaults that impact the Default Fund Segment occur within the ongoing Cooling-off Period (i.e. the 20 Business Days period in which a Default Fund Segment that has been used in full or in part does not have to be replenished). The loss from the ongoing Default Procedure and the newly incurred loss(es) resulting from this/these further Default(s) lead to a combined loss that exceeds the remainder of the Default Fund Segment not yet used. **(See also graphical scheme as depicted in the annex)**

Numerical example:

Dedicated Capital Contribution of SIX x-clear Ltd ("skin in the game") = 22; Default Fund Segment = 300; the initial Default results in 178 being used from the Default Fund Segment. After 5 Business Days, a second Default occurs, resulting in a loss of 150; 122 can be taken from the remainder of the Default Fund Segment, while 28 has to be covered using Top-up Contributions from Members.

After another 7 Business Days, a third large Default occurs, resulting in a loss of 320, which can no longer be covered using resources from the Default Fund Segment. The non-defaulting Members must pay a Top-up Contribution of 272 (300 minus 28).

Replenishment: 15 Business Days after the first Default the size of the Default Fund Segment was reduced by SIX x-clear from 300 to 250. At $t_1 + 20$ a replenishment of the Default Fund Segment in the amount of 148 ($250 / 300 * 178$) is to be effected by the non-defaulting Members. 15 Business Days after the second Default the Default Fund Segment was again reduced, i.e. from 250 to 200. Therefore, at $t_2 + 20$ Business Days another replenishment of the Default Fund Segment is to be effected by the remaining Members in an amount of 52 (200 minus 148).

The Top-up Contribution must be provided by the Members within 2 Business Days. This means that during the Cooling-off Period of 20 Business Days, the Contributions (Top-ups) from the Members could cover a loss that exceeds the size of the Default Fund Segment, even after the latter's full exhaustion.



The amount of the Top-up Contribution is limited to the amount of the individual contribution by the Member to the entire Default Fund Segment at the time of the Default occurring with a loss exceeding the Default Fund ("Exceeding Drawdown"). The maximum contribution of a non-defaulting Member to the replenishment of the Default Fund Segment (in form of a Default Fund Replenishment Contribution) and to the coverage of a loss exceeding the Default Fund Segment (in form of a Top-up Contribution) could thus, in an extreme case of an Extraordinary Default, amount to twice the size of that Member's regular Default Fund Contribution. This applies for the respective Cooling-off Period.

The remaining equity capital of SIX x-clear Ltd (75 per cent) would only be used as the last level of cover after the Default Fund Segment in question has been exhausted and the Top-up Contributions due from the non-defaulting Members have been used.

Our regulators (SNB and FINMA) support the strengthening of our collateralisation, the more so, since our renowned international competitors (EuroCCP and LCH) have similarly expanded their collateral systems in recent years.

3. Use of Collateral to ensure SIX x-clear's liquidity

In the period between receiving the Collateral and the time at which it is contractually obliged to return it to the Member (usually T + 2), SIX x-clear Ltd may also use the funds received as cash or convert the intermediated securities by means of an agreement (Repurchase Agreement) into liquid funds and make use of these on a short-term basis. While SIX x-clear Ltd is legally authorised to do so based on the transfer of title, the character of the Collateral provided must be taken into account and this form of use shall be expressly agreed with the Member.

4. Use of Collateral for short-term investments

The comments under section 3 (above) shall apply analogously for this form of use. For reasons of clarity, SIX x-clear Ltd intends to contractually set out its ability to invest the Collateral over the short term. The regulations governing this use are defined in the "Investment Regulations" and – after being approved by the supervisory authorities – made available to the Members for information.

5. General Terms and Conditions: Amendment regarding x-clear's Dedicated Capital Contribution

In the case of a Member Default which exceeds the collateral (Margin and Default Fund Contribution) contributed by the defaulting Member, SIX x-clear shall – according to the "waterfall of resources" – have to contribute a Dedicated Capital Contribution ("skin in the game") to cover losses before the collaterals of the non-defaulting Members are used. Several Default events that would take place in succession within a short time could weaken the equity capital base of SIX x-clear Ltd substantially or even exhaust it completely. SIX x-clear Ltd, therefore, intends to introduce a grace period ("**Cooling-off Period**"), which allows it not to pay such Dedicated Capital Contribution during a **6-month period** after its full-scale use. If within a Cooling-off Period a portion of the Dedicated Capital Contribution has been used to cover one or more precedent Member Defaults, x-clear shall have an obligation to provide the unexpired portion of its equity contribution ("skin in the game") only.

Clause 18.2 of the future GTC shall read as follows:

Before using Default Fund Contributions of non-defaulting Members x-clear shall use 25 per cent of its own capital (as defined by Swiss law, in particular the Financial Market Infrastructure Act



and the Ordinance on Capital Adequacy) to cover losses caused by a Member Default ("Dedicated Capital Contribution").

x-clear shall make a Dedicated Capital Contribution only once for a period of 6 months following a Member Default or several Member Defaults which necessitated the full use of such contribution ("Cooling-off Period of x-clear"). In case a portion of the Dedicated Capital Contribution (being a fraction of the 25 per cent of x-clear's capital) has been used by one or several precedent Member Default(s) within such Cooling-off Period, x-clear shall pay the remainder of the Dedicated Capital Contribution only.

Next steps

Should you have any questions, please do not hesitate to contact your Relationship Manager or:

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We kindly ask you to examine this draft. You can issue your response to us electronically by no later than **Monday, 22 February 2016**, to your Relationship Manager. We will then consolidate the results as soon as possible and notify you of the further process. It is our goal to implement the new contract and the revised GTC before end of March 2016.

Kind regards

SIX x-clear AG

Christian Sjöberg
Head Clearing

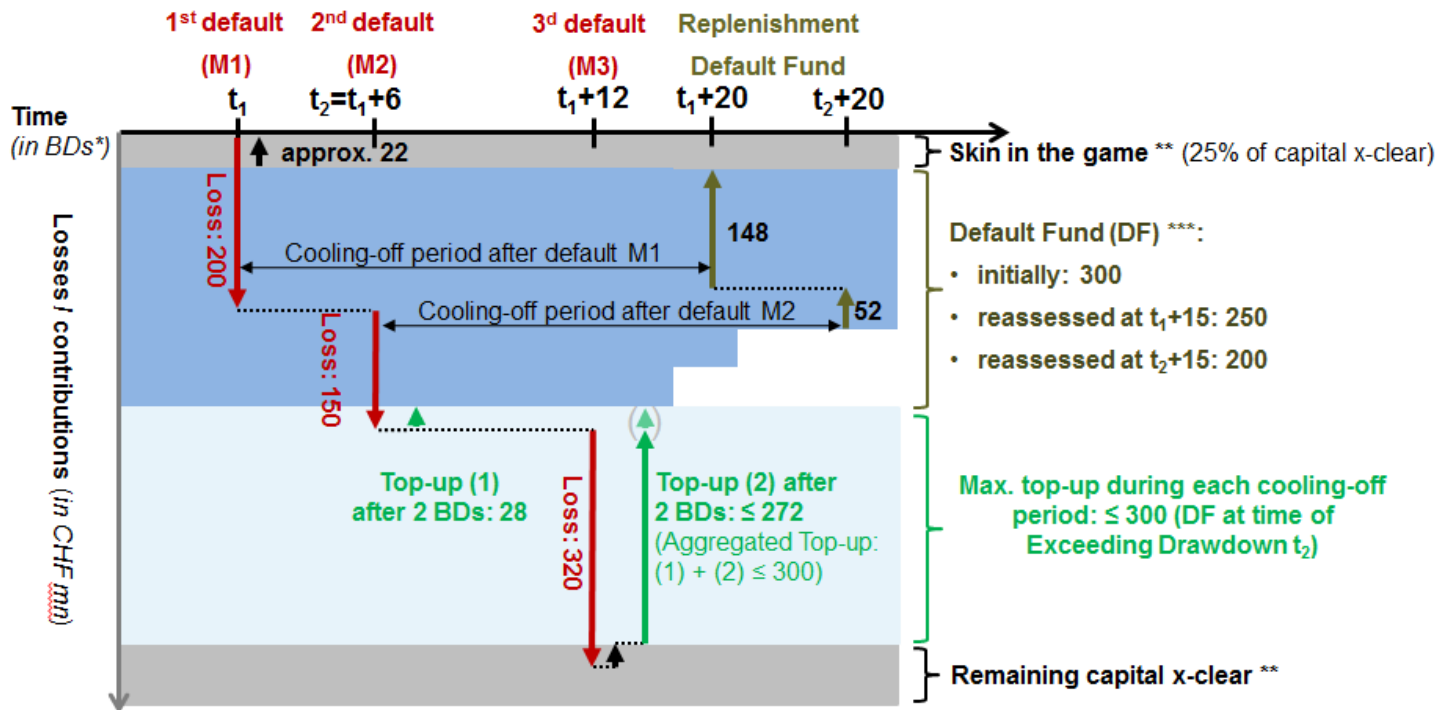
Markus Heiniger
Head Risk Management Operations

Enclosure: "Financial Collateral Agreement" – proposal January 2016



Example of Several Defaults over Short Period of Time

Exemplary Presentation: Extreme Total Loss of CHF 670mn due to three Events within 20 Days



* BD stands for Business Days

** available only once for a period of 6 months following defaults of Members (M1, M2 etc.)

*** The size of the Default Fund differs from its initial size due to reassessment after default of one or several Members. 1