

KEY ASPECTS OF THE PROCEDURE IN THE EVENT OF DEFAULT OF A KDPW_CCP CLEARING MEMBER**I TRIGGERS FOR MEASURES**

KDPW_CCP in cooperation with the Central Securities Depository of Poland (KDPW), basing on reliable information and having first requested the member to immediately perform its obligations (unless that member has been declared bankrupt) decides to take certain measures in response to events resulting in default or threat of default of a KDPW_CCP clearing member, which events qualify as breach under the Rules of Transaction Clearing (Organised Trading) and the Rules of Transaction Clearing (Non-organised Trading), respectively, including but not limited to any of the following circumstances:

- 1) Shortage or lack of funds found in the clearing bank account held for the KDPW_CCP clearing member or in the bank account of that member's payment agent necessary to meet that member's obligations in settlement of the transactions executed;
- 2) Failure of the KDPW_CCP clearing member to make the required supplementary contributions to the clearing fund and to the relevant (ATS or OTC) guarantee fund or towards collateral deposits (organised and non-organised trading);
- 3) Lack of funds found for the KDPW_CCP clearing member necessary to execute transaction clearing as a consequence of failure of another entity to deliver securities to be sold to provide a source of such funding;
- 4) Discontinuance of all or part of its operations by the KDPW_CCP clearing member upon withdrawal of either the PFSA license for broker activities or the PFSA license for managing securities accounts or revocation of an authorisation to set up a bank or commencement of a winding-up procedure in respect of the KDPW_CCP clearing member or any other similar event if such events affect the liquidity of the guaranteed transactions settlement;
- 5) Reliable information is received to the effect that PFSA has decided to suspend the operations of the KDPW_CCP clearing member being a bank or filing a petition for bankruptcy against the KDPW_CCP clearing member with the court by a member or members of the management board or other authorised representatives of that member or being notified by the National Bank of Poland or by another reliable source that the KDPW_CCP clearing member has been declared bankrupt;
- 6) Reliable information is received to the effect that the competent resolution authority has issued a decision which affects the participation of the clearing member in the clearing system and/or affects cleared transactions for which such member is a clearing counterparty.

II SCOPE OF MEASURES**1. Default Committee**

If any events resulting in default or threat of default of a KDPW_CCP clearing member occur:

- a) KDPW_CCP Chief Risk Officer notifies the KDPW_CCP Management Board that a risk exceeding the tolerance threshold has been identified;

- b) the Default Committee (“Committee”) is held and chaired by the President of the KDPW_CCP Management Board. A Management Board Member appointed by the President of the Management Board or, if the President of the Management Board appoints no substitute, a Management Board Member appointed by the Management Board is the Deputy Chair of the Committee who directs the work of the Committee in the event of the Chair’s absence. The Committee is responsible for co-ordinating measures taken by internal organisational units of KDPW_CCP and KDPW as necessary to ensure the payment of debits resulting from the clearing of transactions which requires the use of resources of the clearing guarantee system controlled by KDPW_CCP and to prevent further default resulting from failure of the defaulting KDPW_CCP clearing member to pay debits.

If members of the Committee receive information about events resulting in default of a KDPW_CCP clearing member or circumstances which in their opinion may result in default of a KDPW_CCP clearing member, they notify the Chair of the Committee or the Deputy Chair, which results in a meeting of the Committee being convened by the Chair of the Committee or the Deputy Chair, of which the Polish Financial Supervision Authority is immediately notified. Furthermore, members of the Committee notify the Chair of the Committee or the Deputy Chair of measures taken within individual organisational limits upon the occurrence of events and co-operate within the Committee in order to develop solutions enabling the transfer or closing out of open positions of a defaulting KDPW_CCP clearing member.

Following an in-depth analysis of the events within the Committee:

- a) in the event of reasonable doubt as to the solvency of a KDPW_CCP clearing member, even if it does not represent default at this time, the Chair of the Committee or the Deputy Chair issues the following orders:
- to request relevant organisational units of KDPW and KDPW_CCP to take specific measures in order to monitor the KDPW_CCP clearing member in detail;
 - to draft a resolution suspending the member’s participation in a given clearing system and specifies whether the suspension of participation should concern all operations of the KDPW_CCP clearing member under the participation agreement or a certain scope thereof, as well as the period of suspension of such member;
 - to take other measures under the applicable Rules of Transaction Clearing.
- b) in the event that default of a KDPW_CCP clearing member is identified, the Chair of the Committee or the Deputy Chair orders to draft a resolution:
- cancelling the participation of the defaulting entity;
 - suspending its participation in a given clearing system and specifies whether the suspension of participation should concern all operations of the KDPW_CCP clearing member under the participation agreement or a certain scope thereof, as well as the period of suspension of such member.

The concerned KDPW_CCP clearing member, the Polish Financial Supervision Authority and the operators of the guaranteed markets on which the clearing member or entities represented by it in clearing of transactions operate are informed about the adoption of a resolution cancelling the participation of a clearing member or suspending its operation in a given clearing system. Furthermore, KDPW_CCP sends a message blocking the defaulting KDPW_CCP clearing member or entities which conclude transactions for such member on all guaranteed markets.

2. Positions and assets of a defaulting KDPW CCP clearing member and its clients

Following the adoption of a resolution of the KDPW_CCP Management Board to liquidate the positions of a defaulting clearing member, default is handled in the following steps:

- a) The KDPW_CCP clearing member and entities cleared by such member are blocked on all guaranteed markets.
- b) The positions and collateral of NCM clients of the defaulting member are transferred to another clearing member.
- c) The defaulting member's positions are closed out.
- d) The gains and losses on the closing of the defaulting member's positions are paid. Losses, if any, are paid from the clearing guarantee system.

3. Operating actions necessary to close out positions:

a) **In organised trading:**

On the cash market:

- i. KDPW rejects settlement instructions of the defaulting clearing member or KDPW_CCP withdraws from the settlement system all settlement instructions concerning the defaulting clearing member.
- ii. On the basis of written instructions of a KDPW_CCP non-clearing member who is a client of the defaulting KDPW_CCP clearing member, KDPW_CCP transfers the unsettled transactions and collateral to a specific KDPW_CCP clearing member which has signed a relevant agreement with the KDPW_CCP non-clearing member.
- iii. For positions in cash transactions, securities buy-in or sell-out procedures are initiated as follows:
 - BISO transactions;
 - Open market buy-in – GPW regulated market or ATS, BondSpot ATS;
 - Transactions of the Buy-in Agent;
 - Auctions.
- iv. For positions in repo transactions, an auction is opened. For positions resulting from a settlement fail of the closing leg of a repo, the same methods may be used as for cash transactions.
- v. Actions taken during an auction:
 - the auction is opened, participant quotes are presented;
 - the offers are analysed, the best offers are accepted taking into account potential losses and the value of resources of the clearing guarantee system;
 - clearing members are informed of the auction results.

On the derivatives market:

- i. All derivatives positions of a defaulting KDPW_CCP clearing member which have not been transferred will be closed out.
- ii. Transactions are executed in the first place on the exchange market of block trades and, subsequently, in regular exchange trade.
- iii. Block trades are a result of bilateral arrangements between KDPW_CCP and KDPW_CCP clearing members accepting the positions.

b) In non-organised trading:

- i. KDPW_CCP clearing accounts are opened, to which the defaulting member's positions are to be transferred.
- ii. The positions of the defaulting member and its clients which have not been transferred to other members are transferred to KDPW_CCP accounts.
- iii. For positions of all clients of the defaulting KDPW_CCP clearing member which have not been transferred to another KDPW_CCP clearing member and for proprietary positions of the defaulting KDPW_CCP clearing member, auctions are carried out (separately for derivatives and repo transactions) in order to close out all open positions.

Following the payment of all debits and the transfer or close-out of all positions of clients of the defaulting KDPW_CCP clearing member, if any assets posted as initial margins have remained in collateral accounts held for clients, KDPW_CCP transfers such assets:

- a) directly to the KDPW_CCP non-clearing members whose transactions were secured with assets so posted;
- b) to the defaulting KDPW_CCP clearing member to the extent of assets posted as collateral of transactions executed for the account of clients of the KDPW_CCP clearing member who are not KDPW_CCP non-clearing members and where the return of assets directly to a KDPW_CCP non-clearing member is not feasible or is excessively cumbersome.

Where the measures of KDPW_CCP fail to ensure that entitlements involving securities are satisfied under transactions, KDPW_CCP S.A. makes substitute payments in the circumstances and on the terms and conditions set forth in the Rules of Transaction Clearing (Organised Trading) and the Rules of Transaction Clearing (Non-organised Trading), respectively.

III CLEARING GUARANTEE SYSTEM WATERFALL

KDPW_CCP uses assets in the event of default of a KDPW_CCP clearing member according to the following waterfall:

- a) credits of the defaulting KDPW_CCP clearing member;
- b) initial clearing deposit of the defaulting KDPW_CCP clearing member;
- c) initial margin of the defaulting KDPW_CCP clearing member;
- d) contribution of the defaulting KDPW_CCP clearing member to the clearing fund or the guarantee funds;
- e) dedicated resources of KDPW_CCP in an amount equal to at least 25% of the capital requirement taking into account the allocation of such resources to the given fund;
- f) contributions of the other KDPW_CCP clearing members to the relevant fund;
- g) other own capital of KDPW_CCP up to 110% of the capital requirement;
- h) additional contributions of the other KDPW_CCP clearing members to the relevant fund (max. 50% of the most recent basic contribution);
- i) other own funds of KDPW_CCP.

IV DEFAULT PROCEDURE REVIEW AND TESTING

KDPW_CCP reviews the Procedure in the Event of Default of a KDPW_CCP Clearing Member once per quarter and, where its amendment is required, asks the opinion of the Risk Committee. Internal testing of the procedure is performed once per quarter. Testing of the procedure with the participation of KDPW_CCP clearing members and other relevant infrastructure entities is conducted once per year or upon a significant amendment of the procedure.