

# Direct Client Disclosure Document

Version: January 2021

Barclays Bank PLC

## Indirect Clearing

### Introduction

Throughout this document references to “we”, “our”, “Barclays” and “us” are references to Barclays Bank PLC which provides indirect clearing services (the **Direct Client**). References to “you” and “your” are references to the client of the Direct Client (the **Indirect Client**). Please note that this disclosure document only covers information relating to the Direct Client role of our Barclays Bank PLC entity. The equivalent disclosure document for our affiliates, Barclays Capital Inc. and Barclays Bank Ireland PLC, which also operate as Direct Clients on certain CCPs can be found on our publicly available website.

### What is the purpose of this document?

To enable us to comply with our obligations as a Direct Client under the Indirect Clearing RTS<sup>1</sup> as it forms part of domestic law by virtue of the European Union (Withdrawal) Act 2018 (as amended) (the **EUWA**) which require that, where we are providing indirect clearing services to you that involve us clearing derivatives through a clearing broker on an EU or UK central counterparty (**CCP**)<sup>2</sup>, we must:

- Offer you a choice of a basic omnibus indirect client account and a gross omnibus indirect client account (as discussed under “The types of accounts available” in Part One B below);
- Disclose to you the details of the different levels of segregation;
- Publicly disclose the general terms and conditions under which we provide services to you (as discussed under “The terms and conditions on which we offer services to you” in Part One D below); and
- Describe the risk associated with each type of account

In respect of the treatment of margin and collateral at CCP level you should refer to the CCP disclosures that the CCPs are required to prepare.

### Organisation of this document

This document is set out as follows:

- Part One A provides some background to indirect clearing
- Part One B gives information about the differences between the basic omnibus indirect client account and the gross omnibus indirect client account, explains how this impacts on the clearing of your derivatives and sets out some of the other factors that might affect the level of protection you receive in respect of assets provided to us as margin
- Part One C sets out some of the main insolvency considerations
- Part One D sets out a general overview of the terms and conditions under which we provide services to you
- Part Two provides an overview of the different levels of segregation that the clearing brokers offer, together with an explanation of the main implications of each

In this document references to EU regulation will include the corresponding laws, regulations and guidance (as may be amended) on-shored into UK domestic law under the EUWA.

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## What are you required to do?

You must review the information provided in this document and the relevant clearing member disclosures and confirm to us in writing which account type you would like us to maintain with respect to each clearing broker through which we clear derivatives for you from time to time. We will explain how we would like you to make this confirmation and by when. If you do not confirm within the requested timeframe, we will record the positions and assets relating to you in an account that has the level of Indirect Clearing RTS-compliant segregation which is the closest to your pre-Indirect Clearing RTS account structure, provided that:

- We have used reasonable endeavours to obtain your choice of segregation and have evidence of our efforts;
- In our communication with you, we have informed you that your failure to elect a level of segregation in accordance with the Indirect Clearing RTS will result in us allocating you to an account having the level of Indirect Clearing RTS-compliant segregation which is the closest to your pre-Indirect Clearing RTS account structure (e.g. an omnibus segregation, net or gross as the case may be); and
- We have explained to you that election by us does not preclude you to elect a different (e.g. higher) level of segregation at any time by communicating it in writing to us

## Important

Whilst this document will be helpful to you when making this decision, this document does not constitute legal or any other form of advice and must not be relied on as such. This document provides a high level analysis of several complex and/or new areas of law, whose effect will vary depending on the specific facts of any particular case, some of which have not been tested in the courts. It does not provide all the information you may need to make your decision on which account type or level of segregation is suitable for you. It is your responsibility to review and conduct your own due diligence on the relevant rules, legal documentation and any other information provided to you on each of our account offerings and those of the various clearing brokers and CCPs through which we clear derivatives for you. You may wish to appoint your own professional advisors to assist you with this.

WE SHALL NOT IN ANY CIRCUMSTANCES BE LIABLE, WHETHER IN CONTRACT, TORT, BREACH OF STATUTORY DUTY OR OTHERWISE FOR ANY LOSSES OR DAMAGES THAT MAY BE SUFFERED AS A RESULT OF USING THIS DOCUMENT. SUCH LOSSES OR DAMAGES INCLUDE (A) ANY LOSS OF PROFIT OR REVENUE, DAMAGE TO REPUTATION OR LOSS OF ANY CONTRACT OR OTHER BUSINESS OPPORTUNITY OR GOODWILL AND (B) ANY INDIRECT LOSS OR CONSEQUENTIAL LOSS. NO RESPONSIBILITY OR LIABILITY IS ACCEPTED FOR ANY DIFFERENCES OF INTERPRETATION OF LEGISLATIVE PROVISIONS AND RELATED GUIDANCE ON WHICH IT IS BASED. THIS PARAGRAPH DOES NOT EXTEND TO AN EXCLUSION OF LIABILITY FOR, OR REMEDY IN RESPECT OF, FRAUDULENT MISREPRESENTATION.

Please note that this disclosure has been prepared on the basis of English law save as otherwise stated. However, issues under other laws may be relevant to your due diligence. For example, the law governing the CCP rules or related agreements; the law governing our insolvency; the law of the jurisdiction of the CCP, the law of the jurisdiction of incorporation of the clearing broker; and the law of the location of any assets

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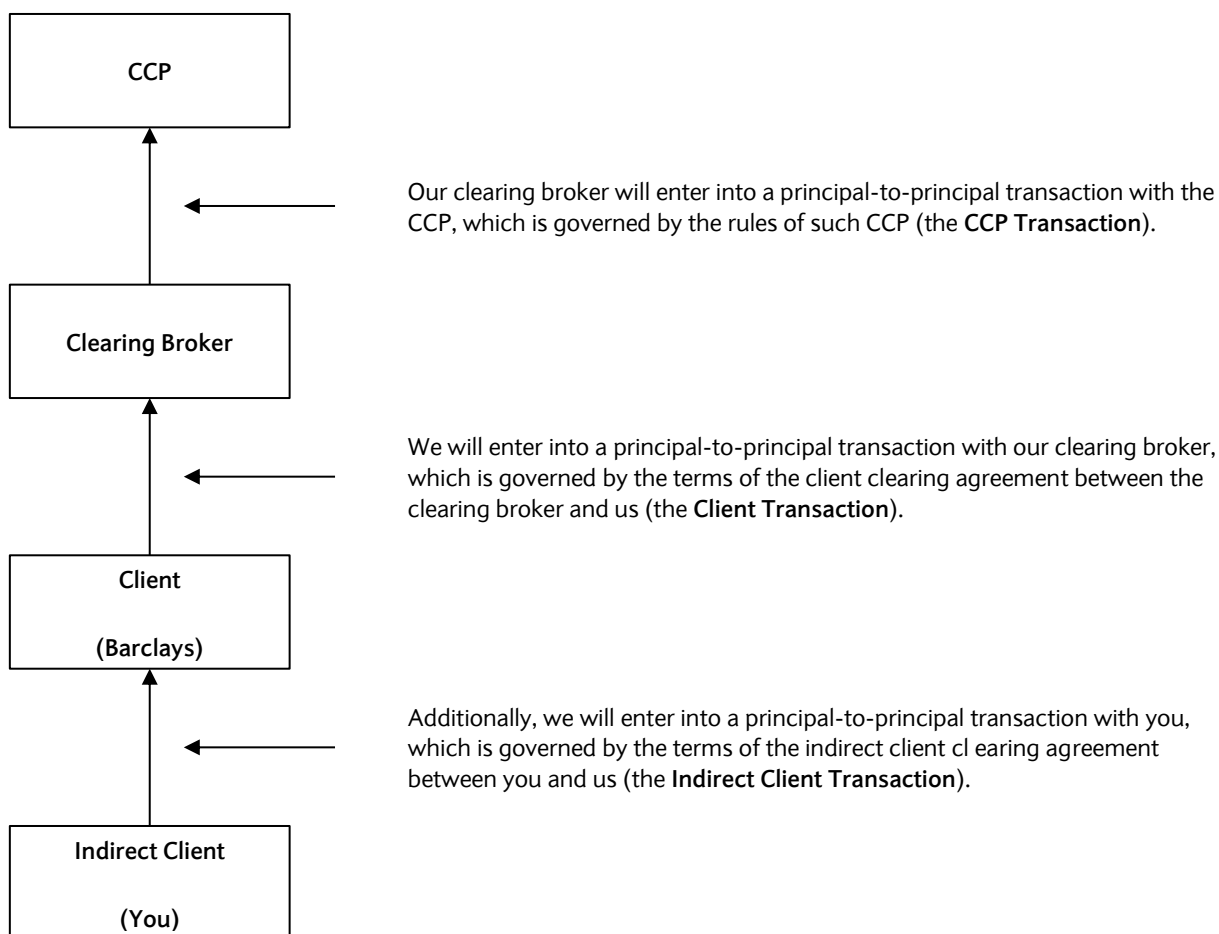
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## Part One A: A brief background to indirect clearing

The market distinguishes two main types of clearing models: the “agency” model and the “principal-to-principal” model. Most of the CCPs which our clearing brokers use adopt the “principal-to-principal” model, and this document assumes all transactions are cleared according to this model.

### The “principal-to-principal” clearing model

When clearing transactions for you through a clearing broker, we usually enter into two separate transactions. Additionally, our clearing broker will enter into a third transaction directly with the CCP.



The terms of each Client Transaction are equivalent to those of the related CCP Transaction, except that (i) each Client Transaction will be governed by a client clearing agreement between our clearing broker and us and (ii) our clearing broker will take the opposite position in the CCP Transaction to the position it has under the related Client Transaction. Similarly, the terms of each Indirect Client Transaction are equivalent to those of the related Client Transaction, except that (i) each Indirect Client Transaction will be governed by an indirect client clearing agreement between you and us, and (ii) we will take the opposite position in the Client Transaction to the position we have under the related Indirect Client Transaction.

Under the terms of the client clearing agreement between our clearing broker and us, a Client Transaction will arise without the need for any further action by either our clearing broker or us, as soon as the CCP Transaction arises between our clearing broker and the CCP. Similarly, under the terms of the indirect client clearing agreement between you and us, an Indirect Client Transaction will arise without the need for any further action by either you or us, as soon as the Client Transaction arises between our clearing broker and us. Once all three of those transactions referred to above have been entered into, your transaction is considered to be “cleared”.

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As the principal to the CCP, our clearing broker is required to provide assets to the CCP as margin for the CCP Transactions that relate to you and to ensure the CCP has as much margin as it requires at any time. We will therefore ask you for margin and, where you provide it in a form which we cannot transfer to the clearing broker, we may transform it. If you have provided us with assets as margin, you may face what we call “transit risk” – this is the risk that, if we were to default prior to providing such assets to the clearing broker, or our clearing broker were to default prior to providing such assets to the CCP, the assets that should have been recorded in your account at the CCP will not have been and will not benefit from the protections described below under “*What happens if we are declared to be in default by a clearing broker?*”. However, in many cases you may not actually face transit risk because our clearing brokers often call margin from us early in the morning to pass it on to the CCP so we will often use our own funds to satisfy the margin call and then seek to recover such amount from you. In these cases where the margin has been funded by us and has already been passed on to the CCP before we call it from you, it is rather that we are exposed to you for the interim period. The arrangements between you and us relating to how the margin calls will be funded will be set out in the indirect client clearing agreement between you and us.

If we have no direct relationship with a clearing broker who is a member of the relevant CCP ourselves and where you have opted for a Basic Omnibus Indirect Client Account, we may enter into a principal-to-principal transaction with an affiliate who is the Direct Client of a relevant clearing broker in a long chain arrangement under the Indirect Clearing RTS (a **Long Chain Arrangement**). Under a Long Chain Arrangement, both the affiliate Direct Client and we would be subject to the relevant requirements for Direct Clients in the Indirect Clearing RTS. Consequently, any references in this document to “Direct Client” should be read as including us in the capacity of a client of an affiliate Direct Client under a Long Chain Arrangement.<sup>3</sup>

Please see Part One B for an explanation of how this is relevant to the choice of account types.

### What if you want to transfer your Indirect Client Transactions to another Direct Client?

There may be circumstances where you wish to transfer some or all of your Indirect Client Transactions to another Direct Client or another clearing broker on a business as usual basis (i.e. in the absence of us having been declared in default by a clearing broker). We are not obliged to facilitate this under the Indirect Clearing RTS but we may be willing to do so subject to our ability to transfer the Client Transactions to which they relate and the margin provided to the clearing broker in connection with them (which will depend on the relevant arrangements with the clearing broker and the CCP) and any conditions set out in our indirect client clearing agreement. You will also need to find a Direct Client or clearing broker that is willing to accept such Indirect Client Transactions and/or the related Client Transactions and assets.

It may be easier to transfer Indirect Client Transactions and Client Transactions that are recorded in a Gross Omnibus Indirect Client Account than those recorded in a Basic Omnibus Indirect Client Account, (both types of account being described in more detail in Part One B) for the same reasons as set out below under “*Will the Client Transactions and assets relating to you be automatically ported to a back-up clearing broker or back-up Direct Client?*”

### What happens if we are declared to be in default by a clearing broker? <sup>4</sup>

If we are declared to be in default by a clearing broker, there are two possibilities with respect to the Client Transactions and assets related to you:

- With respect to Gross Omnibus Indirect Client Accounts, the clearing broker will, at your request, try to transfer (**port**) to another clearing broker (**a back-up clearing broker**) or another Direct Client (**a back-up Direct Client** and together with the back-up clearing broker a back-up entity), such Client Transactions and assets; or
- If porting cannot be achieved with respect to Gross Omnibus Indirect Client Accounts and in any default with respect to Basic Omnibus Indirect Client Accounts, the clearing broker will terminate the Client Transactions that relate to you (see “*What happens if porting is not achieved*” below)

The porting process will differ depending on the clearing broker but it is likely to involve a close-out (with us) and a re-establishment (with the back-up entity) of the Client Transactions, or a transfer of the open Client Transactions and related assets from us to the back-up entity. In some cases clearing brokers will support this structure legally by requiring us to grant a security interest to you over some or all of our related rights against the clearing broker but in other cases where clearing brokers can rely on the Indirect Clearing RTS and local legislation, this may not be necessary.

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### **Will the Client Transactions and assets relating to you be automatically ported to a back-up entity?**

No, there will be a number of conditions which must be satisfied before the Client Transactions and assets that relate to you can be ported to a back-up entity. These conditions will be set by the clearing broker and will include obtaining your consent. In all cases you will need to have a back-up entity that has agreed to accept the Client Transactions. You may wish to appoint a back-up entity upfront as part of your clearing arrangements but the backup entity is unlikely to be able to confirm that it is willing to accept the Client Transactions until the default occurs.

The back-up entity may also have conditions that they require you to meet. You may also be able to agree with the clearing broker that it may choose a back-up entity on your behalf. If you have not appointed a back-up entity prior to our default, or agreed with the clearing broker that it may appoint one on your behalf, then this may mean that porting is less likely to occur.

If porting is achieved, your Indirect Client Transactions with us will terminate in accordance with our indirect client clearing agreement. We would expect your back-up entity to put in place new indirect client transactions/client transactions between itself and you.

The type of account and level of segregation you choose will have an impact on the ability to port Client Transactions and assets to a back-up entity upon our default.

If you choose a Basic Omnibus Indirect Client Account (described in more detail in Part One B), no contractual arrangements are required to be put in place for porting and, therefore, porting will ordinarily not be available.<sup>5</sup>

If you choose a Gross Omnibus Indirect Client Account (described in more detail in Part One B), you can appoint a back-up entity with respect to just your Client Transactions (i.e. independently of our other clients in the same Gross Omnibus Indirect Client Account).

### **What happens if porting is not achieved?**

Each clearing broker is permitted to specify a period of time after which, if it has not been able to achieve porting, it will be permitted to actively manage its risks in relation to the Client Transactions. This period of time will vary across clearing brokers. If you want to port your Client Transactions (where possible), you will need to notify the clearing broker and show that you can satisfy the other conditions within this period.

Otherwise, the clearing broker will terminate the Client Transactions and perform a close-out calculation in respect of them in accordance with the client clearing agreement. If there is an amount owed by the clearing broker in respect of the Client Transactions, the clearing broker will attempt to pay such amount directly to you if you have chosen a Gross Omnibus Indirect Client Account. If the clearing broker does not succeed in this attempt or if you have chosen a Basic Omnibus Indirect Client Account, the clearing broker will pay it to us (or our insolvency practitioner) for the account of our clients.

If the clearing broker terminates the Client Transactions, then the Indirect Client Transactions between you and us are also likely to terminate. The termination calculations in respect of those Indirect Client Transactions will be performed in accordance with the indirect client clearing agreement between you and us and such calculations will likely mirror those performed by the clearing broker in respect of the Client Transactions. If you are due a payment from us as a result of the close-out calculations in respect of our Indirect Client Transactions, the amount due from us to you will be reduced by any amount that you receive (or are deemed to receive) directly from the clearing broker.

Please see Part One C for a consideration of the main insolvency considerations.

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## Part One B: Your choice of account type and the factors to consider

### The types of accounts available

Reference to accounts means the accounts in the books and records of each clearing broker. The clearing broker uses these accounts to record the Client Transactions that we enter into in connection with the clearing of your related Indirect Client Transactions and the assets that we provide to the clearing broker in respect of such Client Transactions.

There are two basic types of indirect client accounts available – Basic Omnibus Indirect Client Accounts and Gross Omnibus Indirect Client Accounts. Some of the CCPs then offer different levels of segregation within some of those account types as described in Part Two of this document.

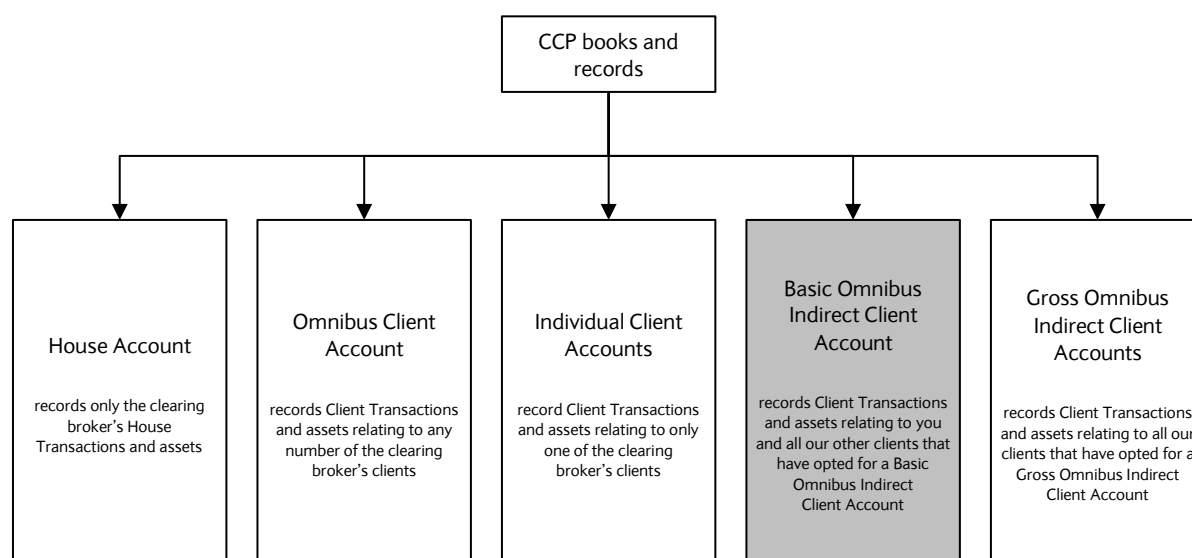
As noted, we refer you to the CCP disclosures which the CCPs are required to prepare and which set out the treatment of margin and collateral at CCP level. We have also included below a general overview of the most common segregation approaches taken by CCPs, but note that for any particular CCP, there is no substitute for that CCP's own disclosure.

### Basic Omnibus Indirect Client Account<sup>6</sup>

Under this account type, at the level of the clearing broker, the Client Transactions (including the corresponding assets in the clearing broker's accounts) relating to you are segregated from:

- Any transactions the clearing broker has cleared for its own account (the clearing broker's **House Transactions**) and any of their assets;
- Any Client Transactions (including corresponding assets in the clearing broker's accounts) relating to us or the account of one of the clearing broker's other Direct Clients (regardless of whether they/we have opted for an individual client account or omnibus client account);
- Any Client Transactions (including corresponding assets in the clearing broker's accounts) relating to any clients of the clearing broker's other clients that have also opted for a Basic Omnibus Indirect Client Account and which are recorded in a different Basic Omnibus Indirect Client Account; and
- Any Client Transactions (including corresponding assets in the clearing broker's accounts) relating to any of our clients or any clients of the clearing broker's other clients that have opted for a Gross Omnibus Indirect Client Account

However, the Client Transactions (including corresponding assets in the clearing broker's accounts) that relate to you will be commingled with the Client Transactions (including corresponding assets in the clearing broker's accounts) relating to any of our other clients that have also opted for a Basic Omnibus Indirect Client Account and which are recorded in the same Basic Omnibus Indirect Client Account.



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Can Client Transactions and related collateral be netted with the clearing broker's House Transactions and assets?	No
Can Client Transactions and related assets be netted with those relating to us or the clearing broker's other Direct Clients?	No
Can Client Transactions and related collateral be netted with those relating to our clients?	Yes (provided our other clients' Client Transactions and assets are recorded in the same Basic Omnibus Indirect Client Account)
Can Client Transactions and related collateral be netted with those relating to the clearing broker's other Indirect Clients?	No

The clearing broker will agree not to net the Client Transactions relating to you with its House Transactions or any Client Transactions not recorded in the same Basic Omnibus Indirect Client Account, nor use the assets relating to such Client Transactions with respect to any House Transaction or Client Transaction recorded in any other account.

However, both we and the clearing broker may net the Client Transactions that are recorded in the same Basic Omnibus Indirect Client Account. The assets provided in relation to the Client Transaction credited to that Basic Omnibus Indirect Client Account can be used in relation to any Client Transaction credited to that Basic Omnibus Indirect Client Account.

Please see Part Two for an overview of the risks in relation to a Basic Omnibus Indirect Client Account and for details of the different levels of segregation that may be available at different CCPs.

### **Gross Omnibus Indirect Client Account<sup>7</sup>**

Under this account type, at the level of the clearing broker, the Client Transactions (including the corresponding assets in the clearing broker's accounts) relating to you are segregated from:

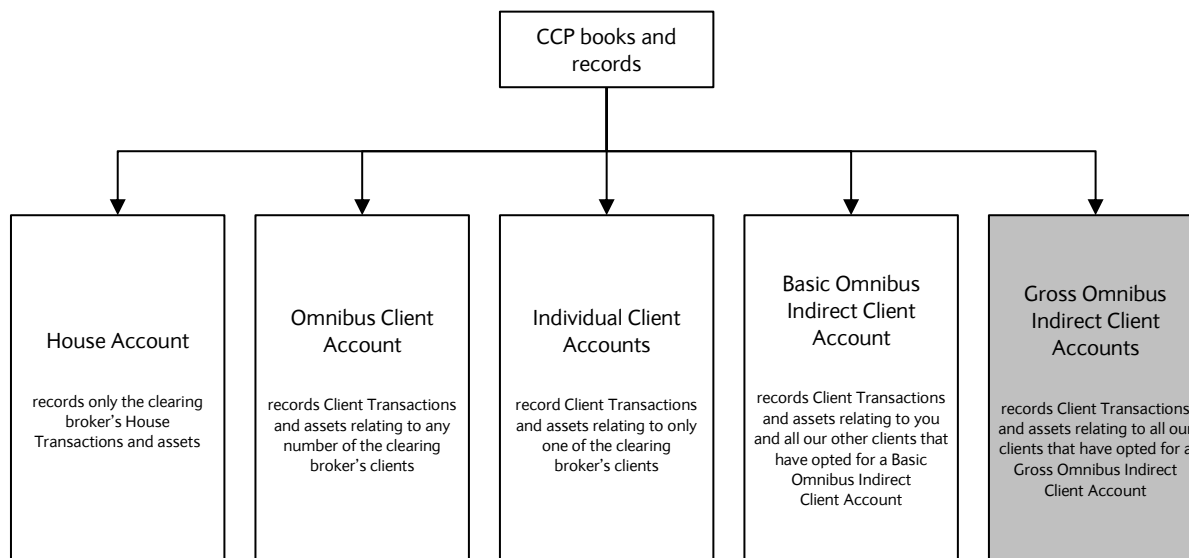
- Any House Transactions and any of their assets;
- Any Client Transactions (including corresponding assets in the clearing broker's accounts) relating to us or the account of one of the clearing broker's other Direct Clients (regardless of whether they/we have opted for an individual client account or omnibus client account);
- Any Client Transactions (including corresponding assets in the clearing broker's accounts) relating to any of our clients or clients of the clearing broker's other clients that have opted for a Basic Omnibus Indirect Client Account; and
- Any Client Transactions (including corresponding assets in the clearing broker's accounts) relating to any clients of the clearing broker's other clients that have also opted for a Gross Omnibus Indirect Client Account and which are recorded in a different Gross Omnibus Indirect Client Account

However, the Client Transactions (including corresponding assets in the clearing broker's accounts) that relate to you will be commingled with the Client Transactions (including corresponding assets in the clearing broker's accounts) relating to any of our other clients that have also opted for a Gross Omnibus Indirect Client Account and which are recorded in the same Gross Omnibus Indirect Client Account.

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Can Client Transactions and related collateral be netted with the clearing broker's House Transactions and assets?	No
Can Client Transactions and related assets be netted with those relating to us or the clearing broker's other Direct Clients?	No
Can Client Transactions and related collateral be netted with those relating to our clients?	The Client Transactions relating to you will not be netted with the Client Transactions relating to any of our other clients.  However, the collateral relating to you may be used to cover Client Transactions of our other clients to the extent it is recorded in the same Gross Omnibus Indirect Client Account.
Can Client Transactions and related collateral be netted with those relating to the clearing broker's other Indirect Clients?	No

The clearing broker will agree not to net Client Transactions relating to you with its House Transactions, the Client Transactions relating to us or the clearing broker's other Direct Clients, the Client Transactions of the clearing broker's other Direct Clients' clients or any Client Transactions relating to our other clients (regardless of whether they are recorded in the same Gross Omnibus Indirect Client Account).

The clearing broker will also agree not to use the assets relating to Client Transactions relating to you with respect to any House Transaction or Client Transaction recorded in any other account. However, both we and the clearing broker may use the assets provided in relation to the Client Transactions relating to you in relation to any Client Transaction relating to our other clients that have also opted for a Gross Omnibus Indirect Client Account which are credited to the same Gross Omnibus Indirect Client Account.

Please see Part Two for an overview of the risks in relation to a Gross Omnibus Indirect Client Account and for details of the different levels of segregation that may be available at different clearing brokers.

### Affiliates

Except for Long Chain Arrangements, we treat our affiliates in the same way as clients when complying with the Indirect Clearing RTS. This means that affiliates also have a choice between types of account. An affiliate may be part of the same account as other clients.

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## Other factors that may impact on the level of protection you receive in respect of assets that you provide to us as margin for Indirect Client Transactions

There are a number of factors that, together, determine the level of protection you will receive in respect of assets that you provide to us as margin for Indirect Client Transactions:

- Whether you choose a Basic Omnibus Indirect Client Account or a Gross Omnibus Indirect Client Account (as discussed under “*The types of accounts available*” above);
- In each case, whether such assets are transferred by way of title transfer or security interest;
- Whether or not cash that you transfer to us is treated as client money in accordance with the FCA client money rules;
- Whether we call any excess margin from you or you pay excess margin to us;
- Whether you will get back the same type of asset as you provided as margin; and
- The bankruptcy and other laws that govern the clearing broker, us and the CCP

The rest of Part One B sets out further details for each of these variables and their implications under English Law.

## Will you provide cash or non-cash assets as margin for the Client Transactions?

As noted under “*The “principal-to-principal” clearing model*” in Part One A, as a Direct Client of the clearing broker, we are required to transfer assets to the clearing broker in respect of the Client Transactions related to your Indirect Client Transactions. Clearing brokers only accept certain types of liquid cash and non-cash assets as margin.

As is market practice, we will decide what types of assets to accept from you as margin for your Indirect Client Transactions. What we will accept from you as margin for the Indirect Client Transactions will not necessarily be the same type of assets that the clearing brokers will accept from us for the Client Transactions, in which case we may provide you with a collateral transformation service, under which we transform the assets you provide to those which we can pass onto the clearing broker.

## Do you provide assets to us on a title transfer or a security interest basis?

### Title Transfer

Typically, Barclays indirect client clearing agreements provide for the transfer of assets by way of title transfer. Consequently, when you transfer assets (**Transferred Assets**) to us, we become the *full owner* of such assets and you lose all rights in such assets. We will record in our books and records that we have received such Transferred Assets from you with respect to the applicable Indirect Client Transaction. We will be obliged to deliver to you equivalent assets to such Transferred Assets (**Equivalent Assets**) in the circumstances set out in the indirect client clearing agreement.

We may either transfer such Transferred Assets on to the clearing broker with respect to the Client Transaction related to the Indirect Client Transaction, or we may transfer other assets to the clearing broker with respect to such Client Transaction.

You bear our credit risk with respect to our obligation to deliver Equivalent Assets to you. This means that if we were to fail, unless we are declared to be in default by the clearing broker, who would then be obliged to follow the requirements under the Indirect Clearing RTS with respect to a direct client default, you will have no right of recourse to the clearing broker or to any assets that we transfer to the clearing broker and you will instead have a claim against our estate for a return of the assets along with all our other general creditors. Even if we are declared to be in default by the clearing broker, the extent of your rights in relation to the clearing broker, if any, will depend on the particular clearing broker.

### Security Interest

Where the indirect client clearing agreement provides for the transfer of assets by way of security interest, when you transfer assets to us, you *retain* full beneficial ownership of such assets. Such assets are transferred to us on the basis that the assets still belong to you, but you have granted us a security interest with respect to such assets.

We may enforce that security interest if you default in your obligations to us. Only at the point of such enforcement would title in such assets or their liquidation value transfer to us. We will record in our books and records that we have received such assets from you with respect to the applicable Indirect Client Transaction.

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### **What is the impact if we treat cash you transfer to us as client money in accordance with the FCA client money rules?**

This question is separate to the question of what level of segregation you want and results from the FCA's client money regime rather than the Indirect Clearing RTS. As set out in the question, "Do you provide assets to us on a title transfer or a security interest basis?", where specified in the relevant indirect client clearing agreement, we may accept cash margin from you on a title transfer basis. Otherwise, because Barclays is as CRD credit institution (as such term is defined in the FCA client money rules), it will hold your money as banker and not as trustee which means that cash will not be held in accordance with the client money rules and not subject to the statutory trust provided for under the FCA client money rules. This means that Barclays will not segregate such cash from its own in accordance with the client money rules and will not be liable to account to you for any profits made by its use as banker of such cash.

As set out above, you bear our credit risk with respect to our obligation to repay cash deposited with us as collateral. This means that if we were to fail, unless we are declared to be in default by the clearing broker, who would then be obliged to follow the requirements under the Indirect Clearing RTS with respect to a direct client default, you will have no right of recourse to the clearing broker or to any assets that we transfer to the clearing broker and you will instead have a claim against our estate for a return of the assets along with all our other general creditors. Even if we are declared to be in default by the clearing broker, the extent of your rights in relation to the clearing broker, if any, will depend on the particular clearing broker.

### **How will any excess margin we call from you be treated?<sup>8</sup>**

Excess margin is any amount of assets we require from you or you provide to us in respect of an Indirect Client Transaction that is over and above the amount of assets the clearing broker requires from us in respect of the related Client Transaction.

Under the Indirect Clearing RTS, excess margin should be treated in accordance with the terms of the indirect client clearing agreement between you and us. Depending on those terms, you may take credit risk on us in respect of it.

### **Will you get back the same type of asset as you originally provided to us as margin for an Indirect Client Transaction?**

In a business as usual situation, whether we will deliver the same type of asset to you that you originally provided to us will be governed by the indirect client clearing agreement between you and us.

In the event of our default, if you are due a payment, you may not receive back the same type of asset that you originally provided to us. This is because the clearing broker is likely to have wide discretion to liquidate and value assets and make payments in various forms, and also because the clearing broker may not know what form of asset you originally provided to us as margin for the Indirect Client Transaction and as a result of any asset transformation services we may provide. This risk is present regardless of what type of client account you select.

Please see Part One C for a consideration of the main insolvency considerations.

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## Part One C: What are the main insolvency considerations?

### General insolvency risks

If we enter into insolvency proceedings, you may not receive all of your assets back or retain the benefit of your positions and there are likely to be time delays and costs (e.g. funding costs and legal fees) connected with recovering those assets. These risks arise in relation to both Basic Omnibus Indirect Client Accounts and Gross Omnibus Indirect Client Accounts because:

- You will not have any rights directly against the CCP; except for clearing broker-specific porting solutions described earlier and the comments below under “*Margin rights*”, you will not have any rights directly against the clearing broker; and you will only have contractual claims against us (i.e. rather than being able to recover particular assets as owner);
- Our insolvency proceedings are most likely to be insolvency proceedings opened and controlled by the Prudential Regulation Authority, the Bank of England and the UK Treasury, under the UK Special Resolution Regime (“**SRR**”) introduced as a result of the Banking Act 2009. This regime provides the PRA, the Bank of England and the UK Treasury with special tools to resolve failing UK banks and protect depositors. Under the SRR, subject to a few exceptions, you will not be able to take any action against us without court or insolvency administrator consent (which can be a time consuming process with an uncertain outcome); and
- Any stage of a cleared transaction (e.g. Indirect Client Transactions, Client Transactions and porting) may be challenged by our insolvency official if, broadly speaking, it was not on arm’s length terms. If successful, the court has broad powers to unwind or vary all of those stages

Please also note that:

- Insolvency law may override the terms of contractual agreements, so you should consider the legal framework as well as the terms of disclosures and legal agreements; and
- A large part of your protection comes from CCP arrangements and the legal regimes surrounding them. Therefore, you should understand these in order to evaluate the level of protection that you have on our default. It is important that you review the relevant disclosures by the relevant clearing broker and the CCP in this respect

### Insolvency of clearing brokers, CCPs and others

Except as set out in this section “*Insolvency of clearing brokers, CCPs and others*”, this disclosure deals only with our insolvency. You may also not receive all of your assets back or retain the benefit of your positions if other parties in the clearing structure default – e.g. the clearing broker, the CCP, a custodian or a settlement agent.

In relation to a clearing broker or CCP insolvency, broadly speaking, our (and therefore your) rights will depend on the law of the country in which the clearing broker or the CCP is incorporated (i.e. not necessarily English law) and the specific protections that the clearing broker or the CCP has put in place. You should review the relevant disclosures carefully in this respect and take legal advice to fully understand the risks in these scenarios. In addition, please note the following:

- We expect that an insolvency official will be appointed to manage the clearing broker or the CCP. Our rights against the clearing broker or the CCP will depend on the relevant insolvency law and/or that official;
- It may be difficult or impossible to port Client Transactions and/or CCP Transactions and related margin, so it would be reasonable to expect that they will be terminated at the level of the clearing broker and/or the CCP. The steps, timing, level of control and risks relating to that process will depend on the clearing broker and/or the CCP, the applicable rules or agreements and the relevant insolvency law. However, it is likely that there will be material delay and uncertainty around when and how much assets or cash we will receive back from the clearing broker or the CCP. Subject to the bullet points below, it is likely that we will receive back only a percentage of assets available depending on the overall assets and liabilities of the clearing broker or the CCP;
- It is unlikely that you will have a direct claim against the clearing broker or the CCP because of the principal-toprincipal model described in Part One A;

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- Under the indirect client clearing agreement, Indirect Client Transactions will terminate at the same time as the matching Client Transactions unless our clearing agreement with the clearing broker provides otherwise. This will result in a net sum owing between you and us. However, your claims against us are limited recourse so that you will only receive amounts from us in relation to Indirect Client Transactions if we receive equivalent amounts from the clearing broker or the CCP in relation to relevant Client Transactions;
- If recovery of margin in these scenarios is important, then you should explore whether any clearing brokers offer “bankruptcy remote” or “physical segregation” structures. It is beyond the scope of this disclosure to analyse such options but your due diligence on them should include analysis of matters such as whether other creditors of the type described in “Porting – preferential creditors” below will have priority claims to margin; whether margin or positions on one account could be applied against margin or positions on another account (notwithstanding the client clearing agreement); the likely time needed to recover margin; whether the margin will be recovered as assets or cash equivalent; and any likely challenges to the legal effectiveness of the structure (especially as a result of the clearing broker’s insolvency)

## Margin rights

If you provide assets to us by way of security interest, then you should have a legal right to recover the balance of those assets (after settling your obligations to us) ahead of other creditors. However, please note that, depending on the exact set up of our security arrangements, it may be that some preferential creditors will still have a prior claim to your assets (please see “Porting – preferential creditors” below which deals with a similar point).

If you have retained the assets (e.g. in a custody account over which you have given us a security interest) then you will have the best chance of recovering them. If you have transferred the assets to our name by way of security (e.g. by giving us a mortgage over the assets) then you bear more risk if there is a shortfall in any of the assets that we are holding. Generally speaking, your risk of loss will be highest in relation to non-client money cash margin; lower in relation to securities held by us in an omnibus account; and lower still if securities are segregated in our books and records and at custody level identifying you as the client.

The actual result will be highly fact specific and will depend on, amongst other things, the exact terms of our legal arrangements; how we have operated accounts; and claims that other intermediaries (e.g. custodians and settlement systems) have to those assets.

We do not expect the above position to change materially if you have a Basic Omnibus Indirect Client Account or Gross Omnibus Indirect Client Account.

## Companies Act 1989, Part VII

Part VII may apply because we are an English company (generally speaking, it does not apply to non-English companies) and may give specific protection against some of the legal risks that arise on our insolvency.

Specifically, if we are declared in default by a clearing broker which clears on a CCP that has the benefit of Part VII protection, then Part VII will generally apply to the relevant Indirect Clearing Transactions if the CCP Transactions corresponding to the Indirect Clearing Transactions are transferred<sup>9</sup> within:

- The period specified for this purpose in the default rules of the relevant CCP; or
- If no such period is specified in the default rules of the relevant CCP, a period of 14 days beginning with the day of our insolvency<sup>10</sup>

This Part VII protection generally applies where actions have been taken as set out above pursuant to the default rules of:

- An English CCP that has been (re)authorised by the Bank of England; or
- A non-English CCP that has been authorised or recognised by other competent authorities or ESMA (as applicable), provided that the non-English CCP’s default provisions either meet certain requirements set out in the UK Recognition Requirements<sup>11</sup> or the non-English CCP has applied for, and the Bank of England has granted, an order stating that Part VII will apply to transfers of assets and positions under that non-English CCP’s default provisions

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In either case, Part VII focuses on protecting counterparties from our default. It is not clear that it would provide any wider protection – e.g. if the CCP itself became insolvent.

Additionally, certain protections under Part VII may apply more generally to the transfer by the clearing broker to a back-up entity of the termination or close-out value of ported Client Transactions under certain circumstances.

Where Part VII applies, our insolvency official cannot challenge actions taken against us:

- To settle the Client Transactions corresponding to the Indirect Client Transaction; or
- To transfer those Client Transactions together with the corresponding Indirect Client Transactions and related assets to a back-up entity<sup>12</sup>

Please note that Part VII is a complex and unclear piece of legislation and this summary is not a substitute for detailed legal analysis – particularly of Part VII in the context of actions taken by a clearing broker in the context of the default of one of its clients – with your professional advisors.

Please see below an outline of some specific insolvency risks and related Part VII commentary.

The protection is from insolvency law so will not necessarily help, for example, with the issue described under “*Porting – preferential creditors*” below because that relates, at least in part, to security law.

### Close-out netting

If we default and the clearing broker cannot port the Client Transactions and collateral (e.g. because a back-up entity cannot be found), then we would expect it to terminate and net our Client Transactions and apply related assets.

You and we would want this to work differently from normal bilateral close-out netting that would apply to all positions and assets between us and the clearing broker – e.g. assets on an Gross Omnibus Indirect Client Account relating to you could be netted with our house or another indirect client account at the clearing broker. There is a risk that this netting across accounts could happen automatically as a result of ordinary English insolvency law. However, to the extent that Part VII applies, this should not occur.<sup>13</sup>

A similar risk occurs between us and you in relation to the Indirect Client Transactions. It is most likely to materialise in a pre-porting period during which English law may automatically set off Indirect Client Transactions and collateral relating to one clearing broker with Indirect Client Transactions and collateral relating to another. This risk arises regardless of what you and we may provide for in our clearing documentation. Whilst the resulting termination amount should represent our net exposure to each other, it will make porting difficult or impossible. Part VII does not provide you any direct protection in this case but, depending on the relevant clearing structure, a security interest may provide some protection in this regard (as mentioned under “*What happens if we are declared to be in default by a clearing broker?*”).

Please also note more generally that your freedom to close out Indirect Client Transactions is more limited under the indirect client clearing agreement than in other arrangements that you may be used to. In particular, the main termination event under our indirect client clearing agreement is that the relevant clearing broker has declared us to be in default under the client clearing agreement between it and us. The intention is to match the treatment of Client Transactions and Indirect Client Transactions as much as possible. However, this may mean that – unless the clearing broker declares a default under the client clearing agreement – you cannot terminate Indirect Client Transactions for common reasons such as a payment or insolvency default on our part.

### Porting – prohibition

As mentioned above, except in specific (e.g. physically segregated) structures, a clearing broker only owes us (not you) obligations in relation to Client Transactions and related assets.

As a result, when these contracts and assets are transferred to a back-up entity, there is a risk of insolvency challenge because our rights have effectively been taken from us on or around the time of our insolvency. Applicable laws may not permit this and there is a risk that the courts may therefore not permit, or may unwind, any porting and related Indirect Client Transactions with this back-up entity.

That said, to the extent Part VII applies (please see above under “*Companies Act 1989, Part VII*”), we expect the risk of challenge to be low in relation to the porting of Client Transactions and matching Indirect Client Transactions.

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## Porting – preferential creditors

As mentioned under “*What happens if we are declared to be in default by a clearing broker?*” in Part One A, a clearing broker’s porting structure may be based on or supported by a security interest. This can take different forms but generally involves us creating security over our rights against the clearing broker in relation to a Basic Omnibus Indirect Client Account or a Gross Omnibus Indirect Client Account in your favour or in favour of another person (e.g. an independent trustee) to hold the security on your behalf. Broadly speaking, the security interest should support the argument that these assets are not part of our insolvency estate (i.e. are not to be shared with our general creditors).

However, depending on the exact structure, insolvency law gives certain statutory creditors priority over secured creditors. This means that some creditors may have a claim on client account assets ahead of you. Statutory creditors are likely to include, amongst others, our insolvency official (e.g. in respect of its costs and expenses), a relatively small amount of unsecured creditors, some employee salaries and pension contributions.

## Mismatch of CCP/Client Transactions and assets

It could be that our net assets in relation to Client Transactions do not match our net obligations to each other in relation to the matching Indirect Client Transactions. This can slow down or make porting impossible either operationally or legally.

For example, it may occur at clearing broker level as a result of Fellow Client Risk (see the explanation of this term in Part Two of this document) in a Gross Omnibus Indirect Client Account, with the result that there are insufficient assets available for porting to satisfy our obligations to you in relation to the Indirect Client Transactions.

Alternatively, it could be that all of your Indirect Client Transactions with us are netted automatically as a result of English insolvency law (please see above under “*Close-out netting*”).

## Banking Act 2009

The Banking Act applies because we are an English company that falls within its scope. As a result, in serious circumstances, we may be nationalised or we (or any of our assets and liabilities) may be transferred to a third party by a combination of the Treasury, Bank of England or FCA. In that case, your counterparty and/or your counterparty risk may change. It is unlikely that you will be able to stop such transfer or to enforce any early termination rights against us as a result of such transfer.

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## Part One D: The terms and conditions on which we offer services to you

A general description of the principal terms and conditions governing our relationship with our clients in respect of indirect clearing is set out below. The actual provisions of the clearing agreement that we enter into with any client are more detailed. The specific terms and conditions of the clearing agreement that we enter into with any client may also differ depending on our analysis of the risks that such client's trading and clearing activities may present.

### What general terms and conditions apply when we offer indirect clearing?

Before providing indirect client services to you, we will generally require that you:

- satisfy our usual client onboarding and KYC criteria, including by providing us with such information that we may request.
- provide us with such information as we may reasonably require from time to time to enable us or any affiliate of ours to comply with any applicable regulation including the Indirect Clearing RTS.
- at all times satisfy the credit criteria applicable to our clients.
- enter into a legally binding clearing agreement with us or have in place an existing clearing agreement with us, in each case governed by English law with general provisions including but not limited to:
  - your capacity and authority
  - your agreement to comply with applicable law, regulation, exchange and CCP rules
  - your agreement to meet all margin calls with respect to client transactions and comply with trading limits
  - our rights to adjust trading limits and fees
  - our rights upon an event of default in respect of you, including rights to liquidate any client transactions and margin
  - limitation of our liability
- You must enter into additional legally binding provisions to the clearing agreement between you and us as are necessary/desirable to enable us and you to comply with our respective obligations under the Indirect Clearing RTS, the rules of the relevant CCPs and our agreement with the applicable clearing member.
- If you do not make an account election within a reasonable period of time as determined by us, you will be treated as if you have elected a Basic Omnibus Indirect Client Account.

Please note that any account election, including any deemed election of a Basic Omnibus Indirect Client Account, will take effect only upon notice by us to you that all relevant steps have been completed by you and us to implement such account.

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## Part Two: Clearing broker indirect client account structures<sup>14</sup>

As noted in Part One B, each clearing broker is required under the Indirect Clearing RTS to offer at least the choice of a Basic Omnibus Indirect Client Account or a Gross Omnibus Indirect Client Account. This Part Two contains an overview of the levels of segregation of each account type, together with an overview of the main protections afforded by and the main legal implications of each.

The descriptions given in this Part Two are very high level and consider the minimum requirements for indirect client account types under the Indirect Clearing RTS and the respective levels of segregation. However, the particular characteristics of the accounts will affect the exact levels of protection they offer and the legal implications so you must review the information provided by the clearing brokers to fully understand the risks of the specific account we maintain in relation to you at each clearing broker. You may also need to seek professional advice to understand the differences in detail. However, we hope that the questions raised and factors described in both parts of this document will help you to know which questions to ask and to understand the impact of the answers you receive.

The descriptions have been prepared on the basis of the minimum requirements in the Indirect Clearing RTS.

The Annex seeks to compare the main account types and levels of segregation against the following risks:

Risks used to compare each account type and level of segregation	Explanation of risk
Transit Risk	Whether you are exposed to us at any point in the process of providing or receiving margin in respect of Indirect Client Transactions.
Fellow Client Risk	Whether assets provided to the clearing broker or CCP in respect of Client Transactions related to you could be used to cover losses in Client Transactions relating to another client.
Liquidation Risk	Whether, if the Client Transactions and assets relating to them were to be ported, there is a risk that any noncash assets would be liquidated into cash. If this were to happen, the value given to such assets by the clearing broker may differ from what you perceive to be the full value of the assets.
Haircut Risk	Whether the value of the assets that relate to Client Transactions might be reduced or not increase by as much as you expect because the clearing broker applied a haircut that did not properly reflect the value of the asset.
Valuation Mutualisation Risk	Whether the value of the assets that relate to Client Transactions could be reduced or not increase by as much as you expect because the assets posted in relation to other clients' Client Transactions have decreased in value.
Clearing Broker Insolvency Risk	Whether you are exposed to the insolvency or other failure of the clearing broker.

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## Typical account characteristics at the clearing broker level

	Basic Omnibus Indirect Client Account	Gross Omnibus Indirect Client Account
<b>Who will the Client Transactions recorded in the account relate to?</b>	Basic Omnibus Indirect Client Accounts record both assets and Client Transactions that relate to you (where you have opted for a Basic Omnibus Indirect Client Account) and the assets and Client Transactions that relate to our other clients that have also opted for a Basic Omnibus Indirect Client Account.	Gross Omnibus Indirect Client Accounts record both assets and Client Transactions that relate to you (where you have opted for a Gross Omnibus Indirect Client Account) and the assets and Client Transactions that relate to our other clients that have also opted for a Gross Omnibus Indirect Client Account.
<b>Which losses can assets recorded in the account be used for?</b>	Assets that are provided to the clearing broker as margin for a Client Transaction recorded in a Basic Omnibus Indirect Client Account may be used to cover any losses in that account, whether such losses relate your Client Transactions or Client Transactions relating to one of our other clients within that Basic Omnibus Indirect Client Account.	Assets that are provided to the clearing broker as margin for a Client Transaction recorded in a Gross Omnibus Indirect Client Account may be used to cover any losses in that account, whether such losses relate your Client Transactions or Client Transactions relating to one of our other clients within that Gross Omnibus Indirect Client Account.
<b>Will the clearing broker know which Client Transactions and types of assets relate to you?</b>	The clearing broker may not know which Client Transactions and assets recorded in a Basic Omnibus Indirect Client Account relate to you.	Yes, but prior to our default it may not know your identity.
<b>Will the clearing broker record the assets provided by value only or will it identify the type of asset provided?</b>	The clearing broker may identify in its records the type of asset provided as margin for the Basic Omnibus Indirect Client Account but will not be able to identify which type of assets relate to any client's Client Transactions within that Basic Omnibus Indirect Client Account.	The clearing broker may identify in its records the type of asset provided as margin for the Gross Omnibus Indirect Client Account but is unlikely to be able to identify anything other than the value of assets provided in respect of any of our client's Client Transactions within that Gross Omnibus Indirect Client Account.
<b>Will the Client Transactions recorded in the account be netted?</b>	It is likely that the Client Transactions recorded in the account will be netted. This means that Client Transactions that relate to you may be netted with Client Transactions that relate to our other clients whose Client Transactions are recorded in the same Basic Omnibus Indirect Client Account.	Client Transactions relating to you are likely to be netted with other Client Transactions relating you. However, Client Transactions relating to you should not be netted with Client Transactions relating to any of our other clients recorded in the same Gross Omnibus Indirect Client Account.
<b>Will the margin be calculated on a gross or net basis?</b>	The margin will be calculated on a net basis.	The margin will be calculated on a gross basis.

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	Basic Omnibus Indirect Client Account	Gross Omnibus Indirect Client Account
<b>Will you have to enter into any documentation or operational arrangements directly with the clearing broker?</b>	You may have to enter into legal documentation to which the clearing broker is party. It is unlikely that you will have to set up any operational arrangements with the clearing broker directly.	You may have to enter into legal documentation to which the clearing broker is party. It is possible but unlikely that you will have to set up some operational arrangements with the clearing broker directly.
<b>Transit Risk</b>	Yes	Yes
<b>Fellow Client Risk</b>	Yes	Yes
<b>Liquidation Risk</b>	Yes	Yes (unless the clearing broker is able to port the assets recorded in the account or is able to transfer the assets to you without needing to liquidate some or all of them first).
<b>Haircut Risk</b>	Yes	Yes
<b>Valuation Mutualisation Risk</b>	Yes	Yes
<b>Clearing Broker Insolvency Risk</b>	Yes	Yes
<b>How likely it is that porting will be achieved if we default?</b>	Unlikely <sup>15</sup>	If you have satisfied all of the clearing broker's and back-up entity's conditions, porting is more readily facilitated in the event of our default.

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- <sup>1</sup> Commission Delegated Regulation (EU) No. 2017/2154 supplementing Regulation (EU) No 600/2014 with regard to regulatory technical standards on indirect clearing arrangements, and Commission Delegated Regulation (EU) No. 2017/2155 amending Commission Delegated Regulation (EU) No 149/2013 with regard to regulatory technical standards on indirect clearing arrangements.
- <sup>2</sup> ESMA confirms in paragraphs 9, 10 and 92 of the May 2016 Final Report on the Indirect Clearing RTS that (indirect) clearing on recognised non-EU CCPs is out of scope of the Indirect Clearing RTS requirements. At the time the UK was part of the EU and this disclosure is designed for clearing on EU CCPs and UK CCPs only.
- <sup>3</sup> This description is based on Articles 6(2)(b) and 6(4) of the Indirect Clearing RTS.
- <sup>4</sup> This description is based on Articles 4 (5) to (7) of the Indirect Clearing RTS.
- <sup>5</sup> This paragraphs refers to porting not being available “ordinarily”. This is because porting may be envisaged under local insolvency law for all relevant accounts, including Basic Omnibus Indirect Client Accounts.
- <sup>6</sup> This description is based on Article 4(2)(a) of the Indirect Clearing RTS.
- <sup>7</sup> This description is based on Article 4(2)(a) of the Indirect Clearing RTS.
- <sup>8</sup> This section refers to excess margin as described in Recital 5 of the Indirect Clearing RTS.
- <sup>9</sup> Please note that “transfer” under Part VII has been defined in Section 189A(3) of the Companies Act 1989 to include a transfer of the CCP Transaction to a different account at the same CCP. Therefore, if there is a back-up client (and the clearing broker remains the same) or if the clearing broker acts as back-up clearing member itself, the “transfer” would simply consist of a re-designation of the existing account at the CCP.
- <sup>10</sup> This description is based on Section 155(2B) and (2D) of the Companies Act 1989.
- <sup>11</sup> Financial Services and Markets Act 2000 (Recognition Requirements for Investment Exchanges and Clearing Houses) Regulations 2001 SI 2001/995.
- <sup>12</sup> This description is based on Section 159(2)(c), (d) and (e) of the Companies Act 1989.
- <sup>13</sup> This description is based on Section 188(1A)(b) of the Companies Act 1989 on the assumption that HMT will update this provision to reflect the Indirect Clearing RTS.
- <sup>14</sup> In preparing the overview of typical indirect client account characteristics, we have based our analysis on the minimum requirements as set out in the Indirect Clearing RTS.
- <sup>15</sup> See Endnote 5 above.

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