X-pand into the Future

# eurex circular 008/07

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**Authorized by:** Thomas Lenz

## Eurex Product Extension into British and Irish Products: Functional Notes

**Related Eurex Circular:** 228/06

**Contact:** Markets Services Team, tel. +49-69-211-1 17 00

| **Content may be most important for:** | **Attachment:** |
|---|---|
| ➲ All departments | UK and Irish Products - Functional Notes |

In the context of the extension of CCP services provided by Eurex Clearing AG into products of the British and Irish markets, we are providing you today with further information.

**UK and Irish Products - Functional Notes**

This document provides detailed information about the functional scope of introducing British and Irish products in CCP. It addresses market participants who are admitted to clearing of trades in Eurex derivatives at Eurex Clearing AG, therefore being affected by the changes that will come into effect with the introduction.

Aforementioned document has also been posted in the Member Section of the Eurex website for download. Please follow the path

**www.eurexchange.com > Member Section > Releases > CCP 3.1 > Manuals > Functional Manuals > Eurex UK and Irish Products**

Eurex Clearing AG
Neue Börsenstraße 1
60487 Frankfurt/Main

Mailing address:
60485 Frankfurt/Main

T +49-69-211-1 17 00
F +49-69-211-1 17 01
customer.support@eurexchange.com
Internet:
www.eurexchange.com

Chairman of the Supervisory Board:
Prof. Dr. Peter Gomez

Executive Board:
Andreas Preuß (CEO),
Jürg Spillmann, Thomas Lenz,
Michael Peters, Peter Reitz

Aktiengesellschaft mit Sitz in Frankfurt/Main
HRB Nr. 44828
Amtsgericht Frankfurt/Main




# UK and Irish Products

# Functional Notes

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# 1 Management Summary

ECAG plans to further expand the product range of physically deliverable products by options on selected UK and Irish equities. These derivative products are originally traded on Eurex Deutschland and Eurex Zürich (Eurex Exchanges) or entered as bilateral transactions by participants in the Eurex system.

After Exercise / Assignment, physical deliveries in UK and Irish instruments are transferred to the Central Counterparty Platform (CCP).

Subsequently, CCP transfers these deliveries to CREST for home market settlement. All pending deliveries are subject to corporate action processing executed by CREST, if applicable.

Key benefits of introducing home market settlement for UK and Irish products are:

- The usage of the existing infrastructure and settlement processing already in place for UK and Irish securities settled in CRESTCo
- The avoidance of split settlement liquidity in UK and Irish securities due to offering settlement in the home CSD for UK and Ireland
- The avoidance of realignment effort

Product introduction in connection with this service is planned to take place in agreement with market participants in the course of the second quarter 2007.

This document focuses on CCP functionality and addresses market participants involved in deliveries out of Eurex derivative transactions, particularly ECAG Clearing Members and ECAG Settlement Institutes. The document primarily aims at functional and operational staff of the Members' middle and back offices.

Additional information can be found in the following documents which have already been published by ECAG and CRESTCo:

- Service Description 'Expansion of ECAG Product Scope into UK and Irish Products' (published at website http://www.eurexchange.com in Eurex Circular 212/06 as of October 23rd, 2006)
- White Book 'Enhancing CREST: Q1/Q2 2007 - A central counterparty for Eurex Exchanges in CREST' (published at website http://www.crestco.co.uk)

# 2 Member Structure and Set-Up

## 2.1 Participant roles

Eurex Clearing AG differentiates between the following participant roles:

- Trading Member (TM)
- Clearing Member (CM) having one or more clearing licenses (For the clearing of physically deliverable products out of options on UK and Irish equities the derivatives clearing license is used)
- Settlement Institute (SI) has limited Trade Management possibilities for UK and Irish equities within CCP and can also provide the settlement account and the Custodian Service (Settlement Participant) within CREST

For settlement purposes, CREST differentiates between:

- CM Undertaking / Sponsored CM Undertaking
- Settlement Participant having access to securities and cash functionality in CREST

Each Settlement Participant ID used by a ECAG member needs to be setup in the CCP as settlement account and needs to be assigned to a CCP Settlement Institute.

More information about participant roles and their interaction can be found in the Service Description 'Expansion of ECAG Product Scope into UK and Irish Products', chapter 4.

## 2.2 Member Settings

The following accounts are required to process deliveries in UK and Irish instruments in EUR and GBP on the CCP platform:

- Securities settlement account at CREST, with related cash account in GBP and EUR
- Cash settlement account at a Payment Bank[1] or Deutsche Bundesbank[2] for EUR payments
- Cash settlement account at a Payment Bank[1] for GBP payments

For UK and Irish instruments, only a default settlement account on the level of TM and currency / account type can be set up for Eurex deliveries. No specific settings on ISIN level are possible. The CM has to decide on the default settlement account to be used and communicate it to Eurex Clearing AG.

[1] A cash account per currency is mandatory at CREST for settlement.
[2] Deutsche Bundesbank can only be used for payments from CCP (e.g. Eurex cash compensation), but not for payments out of settlement at CREST

## 3 Process Overview

Equity options (American style) with underlying UK / Irish equities are traded on the Eurex Exchanges or are entered in the Eurex system as bilaterally agreed transactions.

Resulting from Exercise/Assignment of Eurex positions, deliveries in UK and Irish instruments with settlement currency EUR or GBP are created. These deliveries are transmitted from Eurex to the CCP platform after Exercise/Assignment is executed on day T and are subsequently processed by the CCP platform.

On T+1, deliveries in UK and Irish instruments are sent to CREST for home market settlement. Deliveries in UK / Irish equities have a standard settlement period of T+4.

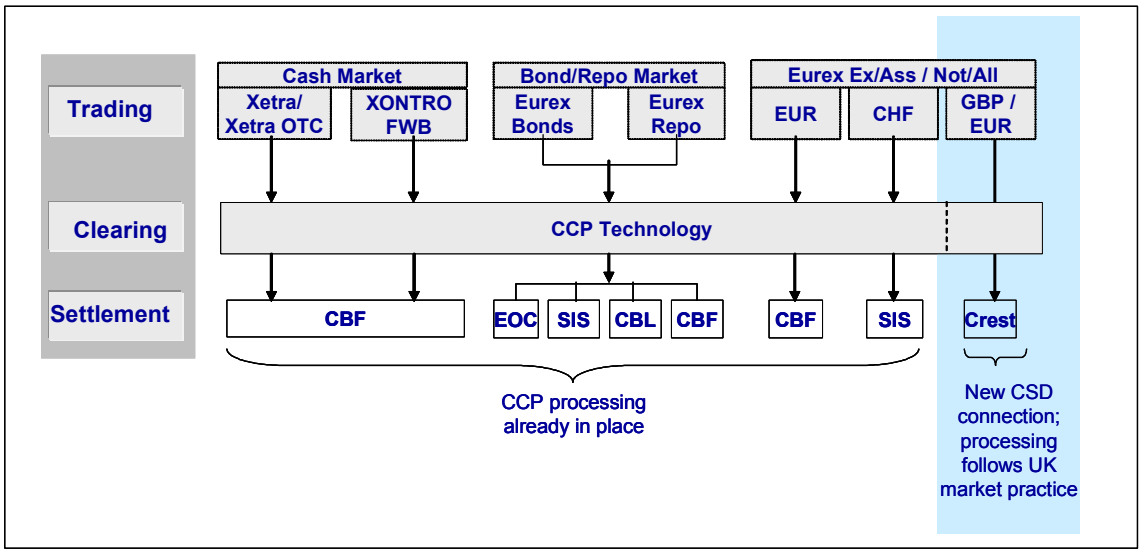



**Figure: Inclusion of Eurex Deliveries in CCP**

Due to the home market settlement at CREST, the processing of deliveries in UK and Irish instruments in settlement currency EUR and GBP follows UK market practice. Resulting from this fact, the following specific features of Eurex deliveries in UK and Irish instruments within CCP have to be considered:

- Eurex deliveries in UK and Irish instruments are always registered as gross and released within the CCP
- The only available gross delivery management function for UK and Irish instruments is inquiry of trades; no other gross delivery management functions are available
- Transactions will be settled in CREST as gross transactions
- Cash payments resulting from settlement processes and Corporate Action processing are initiated by CREST
- Corporate Actions processing will be provided by CREST
- CREST settlement information and CREST Corporate Actions information is reflected in CCP risk and trade reporting as far as possible
- No specific Corporate Action reporting is provided by CCP

- Payments Banks (EUR / GBP) or Bundesbank (EUR) are used for cash payments initiated by the CCP (due to buy-in or compensation payments).

In addition standard CCP services are provided:

- Settlement information and Corporate Action information received from CREST will be reflected in the continuous CCP Member Settlement Reporting as far as possible
- Risk based margining is available for all pending Eurex deliveries

Please refer to sections 4 - 6 for more information on the processing of these deliveries.

A full list of UK and Irish instruments available as Eurex Underlyings will be published in a separate circular at a later point in time.

# 4 Gross Delivery Management

For Eurex Deliveries in UK and Irish instruments, only limited Gross Delivery Management (GDM) functionality for Clearing Members and/or Settlement Institutions is available:

Eurex Deliveries in UK and Irish instruments are always registered as gross and released in CCP.

These deliveries can be inquired on the business day following Exercise/Assignment.

Besides inquiry of trades no other GDM functionality is available, i.e. **none** of the following actions can be performed on deliveries in UK and Irish instruments: Block, Release, Partial Release of Trade, Linking of Trades, Marking of Trades for gross / net processing.

Inquiry of trades can be performed via the VALUES API interface or the @X-PERT CCP Member GUI.

## 4.1 Values API

Inquiry of trades and inquiry of external settlement results can be performed by using the existing Values Requests.

For further information, please refer to the VALUES API Member Front End Development Guide Release CCP 3.1.

## 4.2 MSIF (Member Settlement Instruction File) / SWIFT Access

Block/release functionality for deliveries in UK and Irish instruments to be settled at CREST is not supported.

## 4.3 CCP Member GUI

No new version of Member GUI will be provided, GUI version released with CCP 3.1 is still valid. For further information, please refer to the CCP 3.1 User Guide.

For deliveries in UK and Irish instruments the gross delivery management is limited to inquiring the trade overview and the settlement results view.

For filtering deliveries in UK and Irish instruments, the already existing settlement location CCO (i.e. CrestCo) can be used.

# 5 Delivery Management

For the settlement of Eurex Deliveries in UK and Irish instruments, each CREST Settlement Participant ID used by an ECAG member needs to be setup in the CCP as settlement account and needs to be assigned to a CCP Settlement Institute.

Settlement account and settlement location of a Eurex delivery are determined according to the Trading Member's default setting maintained for UK and Irish instruments.

## 5.1 Settlement Locations

CCP supports the settlement location CrestCo (CCO) for Eurex deliveries in UK and Irish instruments to be settled in EUR or GBP. These deliveries are always assigned for settlement against Eurex Clearing AG at CrestCo (settlement participant CCPEC in CREST).

Eurex Deliveries in UK and Irish instruments are received by CCP on T, the exercise date of the option. Deliveries in UK / Irish equities have a standard settlement period of T+4.

On T+1, these deliveries are sent to CREST for external settlement. Within CREST these deliveries are considered as gross transactions and are subject to CREST settlement processes. Settlement netting service is not provided.

After settlement has taken place in CREST, this information is reflected in the CCP.

## 5.2 Cash Settlement

### 5.2.1 Cash-only Instructions

In addition to the cash payments resulting from the corporate action and the settlement process in CREST, the CCP system initiates cash payments for the following reasons:

- Compensation payments due to exercise / assignment of capital adjusted option series in the Eurex system (i.e. fractional units per lot):
  In case of settlement currency GBP, these payments are settled via a Payment Bank. In case of settlement currency EUR, these payments can be settled via a Payment Bank or via the Deutsche Bundesbank, depending on member's individual settings.
- Cash payments to Clearing Members related to a buy-in, fees and margin:
  In case of GBP payments, these payments are settled via a Payment Bank, in case of EUR payments, these payments are settled via the Deutsche Bundesbank.

### 5.2.2 Cash Settlement Locations

For the settlement of cash only payments related to deliveries in UK and Irish instruments, the CCP provides interfaces to the Deutsche Bundesbank (for EUR payments) and to the following supported Payment Banks (for EUR and GBP payments):

- Barclay Bank plc (BAR)

- Citibank N.A. (CIT)
- Deutsche Bank AG (DEU)
- HSBC Bank plc (HSB)
- The Royal Bank of Scotland (RBS)

Cash accounts serve to settle cash-only instructions at the supported payment locations. Each Clearing Member has to specify cash-only accounts (including the respective payment location) for EUR and GBP per settlement account for settling cash-only instructions as outlined above.

To facilitate the settlement process for customers and to improve settlement efficiency Eurex Clearing AG acts via 'Power of Attorney' (PoA) procedures. For each payment location, Members have to provide a Direct Debit Mandate to Eurex Clearing AG ('PoA' on cash accounts); this allows Eurex Clearing AG to directly instruct the Member's cash accounts.

## 6 Corporate Action Processing

Corporate Actions Processing will be performed in CREST according to UK market practice. CREST distinguishes between "transformations" and "claims". In CCP terms this can result in Income and Non-Income events.

Information about adapted / new trades as well as cash payments is therefore accessible for CREST participants via CREST.

The following information will be made available in CCP:

In case of non-income events, adapted / new trades will be reflected in the CCP. These trades will be considered in Risk Management. Moreover, they can be inquired via CCP Member GUI / Values API interface and are also included in the CCP Pending Delivery reports / Settled Delivery reports. No Corporate Actions reporting via CA180 is offered.

In case of income events, cash payments are considered in Risk Management. Cash payments will not be included in CCP member reporting. In particular no Corporate Actions reporting via CA160 is offered.

## 7 Risk Management

Eurex Clearing AG provides central risk management by applying Eurex's Risk Based Margining method and reports risk positions to Clearing Members.

Risk management for Eurex Deliveries in UK and Irish instruments is in accordance to the principles valid for Eurex deliveries (for an overview please refers to the CCP 3.1 Final Release Notes).

For Eurex deliveries to be settled in GBP, the margin class currency will be GBP.

# 8 Member Reporting

Deliveries in UK and Irish instruments will be reported in the delivery reports resulting from continuous reporting (reporting stream CORPT).

As Corporate Actions are processed in CREST, the following has to be noted:

- In case of non-income events, adapted / new trades will be reported by CCP in the reports CE260 / CE265 / CE270, but not in the report CA180
- In case of income events, no CCP member reporting takes place, i.e. cash payments related to UK and Irish instruments will not be reported in the report CA160

The following table highlights how deliveries in UK and Irish instruments are reported in the existing CCP member reports:

| Report ID | Report Title | Contains deliveries in UK and Irish instruments | Comments | Report Generation |
|---|---|---|---|---|
| Common | Common | | Additional possible values for currency: GBP<br>CCO is set up as full settlement location<br>Additional payment location BAR, CIT, DEU, HSB, RBS<br>CREST settlement participant ID of ECAG is "CCPEC". On the delivery reports this is shown as "CSD account" (print report) and "Safekeeping account" of ECAG (raw reports). | Continuous reporting (CORPT)<br>End-of day processing (EOD)<br>Instrument type specific report (EXS and BONDS) |
| RPTCA130 (CM)<br>RAWCA130 (CM)<br>RPTCA131 (SI)<br>RAWCA131 (SI) | Compensation Partner | No | | EOD |
| RPTCA160 (CM)<br>RAWCA160 (CM)<br>RPTCA161 (SI)<br>RAWCA161 (SI) | Custody Payment Statement | No | | EOD |
| RPTCA180 (CM)<br>RAWCA180 (CM)<br>RPTXA181 (SI)<br>RAWCA181 (SI) | Capital Adjustments on Trades | No | | EOD |
| RPTCB225 (CM)<br>RAWCB225 (CM) | Daily EUREX Fines | No | | EOD |
| RPTCB230 (CM)<br>RAWCB230 (CM)<br>RPTCN231 (SI)<br>RAWCB231 (SI) | Daily Gross Delivery Mgmt | Yes | | EOD |
| RPTCB300 (CM)<br>RAWCB300 (CM) | Daily Clearing Fees | Yes (EXS)<br>No (Bonds) | Contains UK and Irish equities | EXS<br>BONDS |

| Report ID | Report Title | Contains deliveries in UK and Irish instruments | Comments | Report Generation |
|---|---|---|---|---|
| RPTCB305 (CM)<br>RAWCB305 (CM) | Daily Settlement Fees | No | | EXS |
| RPTCB310 (CM)<br>RAWCB310 (CM) | Daily Service Fees | Yes | | EOD |
| RPTCD150 (CM)<br>RAWCD150 (CM)<br>RPTCD151 (SI)<br>RAWCD151 (SI) | Cash Obligations | No | | EOD |
| RPTCD250 (CM)<br>RAWCD250 (CM)<br>RPTCD251 (SI)<br>RAWCD251 (SI) | Settled Cash Transactions | Yes | | EOD |
| RPTCE260 (CM)<br>RAWCE260 (CM)<br>RPTCE261 (SI)<br>RAWCE261 (SI)<br>RPTCE262 (TM)<br>RAWCE262 (TM) | Pending Delivery | No (BRP)<br>Yes (COPRT) | Field Delivery Id: For deliveries to be settled at CrestCo filled with CREST transaction id.<br><br>Printable report: As long as a trade is not due, it is shown in section 'Open Trades'.<br>In section 'Open Trade', for trades with settlement location CCO the label 'Delivery id' is always shown. As soon as the CREST transaction id is available in CCP, it will be indicated here.<br>When the trade is due, it will be shown in section 'Deliveries marked for gross processing'.<br><br>Raw report: For trades with settlement location CCO, the field 70E, subfield "/D" indicates the CREST transaction id if available, else the value "TRADE" is shown. | BRP<br><br>CORPT |
| RPTCE265 (CM)<br>RAWCE265 (CM)<br>RPTCE266 (SI)<br>RAWCE266 (SI)<br>RPTCE267 (TM)<br>RAWCE267 (TM) | Pending Delivery before NTP | Yes | Field Delivery Id: For deliveries to be settled at CrestCo filled with CREST transaction id.<br><br>Printable report: As long as a trade is not due, it is shown in section 'Open Trades'.<br>In section 'Open Trade', for trades with settlement location CCO the label 'Delivery id' is always shown. As soon as the CREST transaction id is available in CCP, it will be indicated here.<br>When the trade is due, it will be shown in section 'Deliveries marked for gross processing'.<br><br>Raw report: For trades with settlement location CCO, the field 70E, subfield "/D" indicates the CREST transaction id if available, else the value "TRADE" is shown. | CORPT |

| Report ID | Report Title | Contains deliveries in UK and Irish instruments | Comments | Report Generation |
|---|---|---|---|---|
| RPTCE270 (CM)<br>RAWCE270 (CM)<br>RPTCE271 (SI)<br>RAWCE271 (SI)<br>RPTCE272 (TM)<br>RAWCE272 (TM) | Settled Delivery | No (BRP)<br>Yes (CORPT) | Field Delivery Id: For deliveries settled at CrestCo filled with CREST transaction id. | BRP<br>CORPT |
| RAWCE290 | Eurex deliveries | Yes | 82D counterparty filled with 7525 | EOD |

Please refer to the following documents for additional information: 'Member File Based & SWIFT Interface', 'Description Report Layouts', and 'Description of Report Raw Data' published with CCP 3.1.

## 9 Late Delivery Handling

Settlement discipline for equities is ensured by modified buy-in fees for equity derivatives and cash market. The buy-in fees are calculated as percentage rate of the outstanding buy-in amount. A floor and a cap are applied. The buy-in fees will be published at a later point in time.

# 10 List of Abbreviations

| Abbreviation | Stands for |
|---|---|
| BAR | Barclay Bank plc |
| BRP | Batch oriented reporting |
| BuBa | Deutsche Bundesbank |
| CA | Corporate Action |
| CB | Central Bank |
| CCO | CrestCo |
| CCP | Central Counter Party |
| CIT | Citibank N.A |
| CM | Clearing Member |
| CORPT | Continuous Reporting |
| CREST | Central Securities Depository for UK and Ireland |
| CSD | Central Securities Depository |
| DEU | Deutsche Bank AG |
| DTP | Day Time Processing |
| DvP | Delivery versus Payment |
| ECAG | Eurex Clearing AG |
| EOD | End of Day |
| EUR | Euro |
| GBP | Great Britain Pound |
| GDM | Gross Delivery Management |
| HSB | HSBC Bank plc |
| NTP | Night Time Processing |
| PB | Payment Bank |
| PoA | Power of Attorney |
| RE | Risk Engine |
| RSB | The Royal Bank of Scotland |
| RvP | Receive versus Payment |
| SI | Settlement Institution |
| SLU | Settlement Locations Unit |
| SNA | System Network Architecture |
| TM | Trading Member |