

**IMPORTANT NOTE:** This FCM Rates Service Default Management Disclosure Notice (this “Notice”) is provided for information purposes only and does not constitute a full description of the default management arrangements applicable to the Clearing House’s FCM Rates Service. In providing the information in this Notice, the Clearing House is not making any recommendations or providing any advice (commercial, legal or otherwise) to any clearing member, client (in both such cases, whether potential or already existing) or to any other party in relation to the use, selection of, economic consequences of, or the selection of particular levels of protection and particular segregation arrangements in relation to the FCM Rates Service (or of any service offered by the Clearing House). Accordingly, no FCM Client may rely upon the contents of this Notice and should make its own decisions regarding the FCM Rates Service (and all other services offered by the Clearing House) based on independent advice from its professional advisors.

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## FCM Rates Service Default Management Disclosure Notice

### 1. Introduction

LCH Limited (the “Clearing House” or “LCH”) provides a clearing service in respect of over-the-counter (“OTC”) interest rate swaps (the “SwapClear Service”) to its members (“FCM Clearing Members” or “FCMs”) and to their FCM Clients. LCH also provides a separate clearing service in respect of certain exchange-traded interest rate futures contracts traded on, or pursuant to the rules of, certain trading venues (the “Listed Rates Service”) to its members (the “FCM Listed Rates Clearing Members”) and their FCM Clients. LCH combined the SwapClear Service and the Listed Rates Service into a single service (the “Rates Service”), which shares a common default fund as well as specific default management arrangements. The information contained in this Notice is intended to provide FCM Clients with important information regarding the liquidation provisions of these default management arrangements.

Capitalised terms used, but not otherwise defined, in this Notice shall have the meanings set forth in the Clearing House’s FCM Regulations, FCM Procedures, Default Rules, and Settlement Finality Regulations, each as amended from time to time (collectively, the “Rulebook”).

### 2. FCM Portfolio Margining Service

The Clearing House permits FCM Joint Rates Service Clearing Members (*i.e.*, FCMs that are also FCM Listed Rates Clearing Members) the right to participate in a portfolio margining service (the “Portfolio Margining Service”, and such Clearing Members, “Portfolio Margining Clearing Members”), whereby positions in cleared listed interest rate futures (“Listed Interest Rates Contracts”) are commingled with cleared positions in OTC interest rate swaps (“SwapClear Contracts”). All positions commingled in this manner are generally treated as SwapClear Contracts for margining purposes. Portfolio Margining

Clearing Members may also offer the Portfolio Margining Service to FCM Clients that meet the eligibility criteria set out in the FCM Procedures.

### **3. Default Management**

The Clearing House has adapted its Rates Service default management plan (“**Rates Service DMP**”) to account for the comingling of Listed Interest Rates Contracts with SwapClear Contracts as a consequence of the Portfolio Margining Service.

#### *3.1 Porting*

Where a Defaulter is a Portfolio Margining Clearing Member, the Rates Service DMP provides for the porting of such Defaulter’s FCM Client positions, provided, however, that any transferee Clearing Member must also be a Portfolio Margining Clearing Member.

#### *3.2 Liquidation*

Where the Clearing House determines that one or more FCM Clients will not be ported (each, a “**Non-Porting Client**”), the Clearing House shall establish a notional account in a given currency referencing the SwapClear Contracts and Listed Interest Rates Contracts in that currency attributable to such Non-Porting Client(s) for purposes of allocating losses (each such account, the “**Hedged Account**”). As each Hedged Account is a notional account only, the establishment and operation of the Hedged Account(s) will not implicate any actual comingling of the positions or collateral of any FCM Clients following the bankruptcy filing of the Defaulter. Instead, the use of Hedged Accounts is intended to facilitate the efficient hedging and liquidation of the overall portfolio of positions in the account.

The Clearing House will reference in each Hedged Account the SwapClear Contracts and Listed Interest Rates Contracts in the applicable currency that are to be liquidated, regardless of the FCM Clients for which such Contracts are held. Therefore, for example, a Non-Porting Client that participates only in the Listed Interest Rates Service may find that its positions in Listed Interest Rates Contracts are notionally referenced in a Hedged Account that also contains SwapClear Contracts in the same currency of other Non-Porting Clients. Similarly, a Non-Porting Client that participates only in the SwapClear Service may find that its positions in SwapClear Contracts are notionally referenced in a Hedged Account containing Listed Interest Rates Contracts in the same currency of other Non-Porting Clients.

Each Non-Porting Client is assigned a risk factor (“**Account Class Risk Factor**”) in respect of its set of SwapClear Contracts (if any) and its set of Listed Interest Rates Contracts (if any) referenced in one or more Hedged Accounts. The value of each Account Class Risk Factor is equal to the proportion of the hypothetical (where applicable) margin requirement associated with the SwapClear Contracts and Listed Interest Rates Contracts, respectively, referenced in the relevant Hedged Account for a particular currency, determined as of the time that the Contracts are first referenced in the relevant Hedged Account. Listed Interest Rates Contracts that have been portfolio margined will be treated as SwapClear Contracts for these purposes.

Gains and losses in each relevant Hedged Account will be allocated to each Non-Porting Client pro rata based on such Non-Porting Client’s Account Class Risk Factor(s). LCH has established procedures to ensure the appropriateness of the Account Class Risk Factor calculations where contracts of additional Non-Porting Clients are subsequently referenced in the Hedged Account(s). Following liquidation of a Hedged Account, actual gains and losses

will be allocated to each Non-Porting Client's relevant Client Account based on such Non-Porting Client's pro rata allocation of such gains or losses referenced in such Hedged Account.

Whilst the Clearing House believes that this approach to liquidating Non-Porting Client positions provides a good faith reflection of the gains and losses allocable to each Non-Porting Client, there can be no assurance that a particular Non-Porting Client's gains (or losses) will be equivalent to the gains (or losses) that such Non-Porting Client would have incurred had its positions been liquidated separately and not allocated to one or more Hedged Accounts.

#### **4. More Information**

More information regarding the Portfolio Margining Service, including eligibility requirements, can be found in the FCM Procedures. Further details regarding the Clearing House's arrangements for liquidation of FCM Client positions and the use of Hedged Accounts can be found in the FCM Procedures.