

SETTLEMENT DEFAULT FUND POLICY DUBAI CLEAR

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Establishment of the Settlement Default Fund (SDF)

Dubai Clear LLC will act as a Central Counter Party (CCP) for all trades cleared by the CCP through the novation process. In other words, Dubai Clear (the CCP) will act as a Seller to the Buyer and a Buyer to each Seller for trades to be cleared by the CCP. In order to mitigate risks in relation to the clearing process, the CCP uses compressive risk management measures including Initial Margins, Variation Margins to ensure settlement of obligations. These risk management measures provide adequate protection in majority of cases, but may not be able to guarantee settlement in case of extreme market condition. In order to support the CCP during extreme unlikely scenarios, the CCP is mandated by the Securities and Commodities Authority of the UAE (SCA) to establish and administer a Settlement Default Fund to be used in the event of a Clearing Member (CM) default. This SDF is a common feature for all CCPs globally and will be used to mitigate losses in the event a CM is unable to fulfill its obligations to the CCP or if the CCP suffers any losses as a result of a default event.

Size of the Settlement Default Fund

In line with SCA CCP regulations, the SDF must be sufficient to cover either the default of the largest CM or the total of the second and third largest CM. The size of SDF will be stress tested on a daily basis in order to ensure that the SDF is adequate in extreme but plausible market conditions. The CCP will use a combination of historical and hypothetical scenarios to test the adequacy of the SDF.

Contributions to the Settlement Default Fund (SDF)

The SDF shall be created from the contributions of the CCP and also contributions by the CMs. The Contributions made by the CCP towards the SDF (also known as “Skin-in-the-game”) shall not be less than 25% of the paid up capital of the CCP. The initial contribution from Dubai Clear shall be AED12.5 million. Contributions to the SDF by the CMs will be based upon the risk the CM posts to the CCP arising from trade positions undertaken by the CM for clearing and settlement with the CCP.

The CM contribution shall be the higher of either:

- the fixed initial contribution based on category of membership; or
- the variable contribution based on the risk portfolio of the respective CM (i.e. highest Total margin* (Initial + Variation) utilized over a pre-defined period).

The levels of Fixed Contributions shall be as follows:

Membership Category	Initial Contribution to CCP
Trade Clearing Member (TCM)	AED 200,000
General Clearing Member (GCM)	AED 500,000
Settlement Agent (SA)	Nil

The variable contribution will be 5% of highest Total Margin* (TMR) utilised by each CM for the previous month. A higher percentage may be used where required to ensure SDF meets the adequacy requirements based on stress test results.

Example:

Clearing Member (CM)	CM Type	Fixed DF Contribution	Highest TMR * Utilisation	Floating SDF Contribution (5% of highest TMR* Utilisation)	Actual SDF Contribution (Higher of Fixed/Floating)
A	GCM	500,000	4,000,000	200,000	500,000
B	GCM	500,000	15,000,000	750,000	750,000
C	TCM	200,000	300,000	15,000	200,000
TOTAL		1,200,000			1,450,000

The initial SDF contributions will be calculated on the basis of the highest Total Margin * utilised during previous month, and advised to CMs shortly thereafter.

On an ongoing basis, a CM's contribution towards the SDF shall be subject to the following:

- a) The SDF contribution shall be fixed for a calendar month.
- b) The CCP will recalculate the SDF contributions monthly (at the end of each month) for the subsequent month to ensure that the SDF contributions commensurate with the risk portfolio of the CMs.
- a) The contributions of individual CMs shall be based on the risk to the CCP i.e. the higher a CMs Total margin* utilised in a calendar month, the higher would be their floating contribution towards the SDF for the next month.
- b) The SDF contribution will be blocked from the outstanding Daily Operational Limit (DOL) with the CCP. There is no separate contribution required towards the SDF.
- c) In a Default Event and if the SDF is required to be utilized to resolve the Default Event, the "Default Waterfall" approach (ie. how the SDF will be applied to extinguish the default amount) is as follows:
 - i. Margins of the Defaulting CM will be used first, followed by;
 - ii. Outstanding collaterals of the Defaulting CM, followed by;
 - iii. Skin-in-the-game contributions of the CCP, followed by;
 - iv. The contributions of other CMs to the SDF on a pro-rated basis, followed by;
 - v. Top-up as may be approved by SCA but limited to a maximum of one time the existing contribution.

Administration of the Settlement Default Fund

1. The general administration of the SDF shall be overseen by the CCP's Risk Management Committee (RMC).
2. The CCP shall maintain books and records of the SDF in line with international best practice requirements and as per SCA's requirements.
3. The assets of the SDF shall be used solely for the management of a Default Event in line with the Default Rules.
4. The assets of the SDF shall be invested to ensure highest priority is provided to Capital Protection and Liquidation maximization.
5. Any income from the SDF shall be first used to fund all expenses related to the operation and management of the SDF investment. Any residual income may be distributed to the SDF.

* Initial Margin has been replaced with Total Margins with effect from July 2020