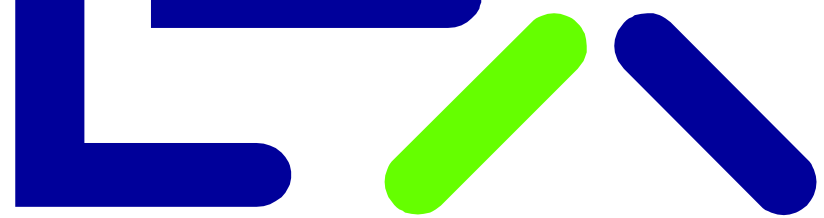


X-pand into the Future



Value of CCP in the light of Basel II

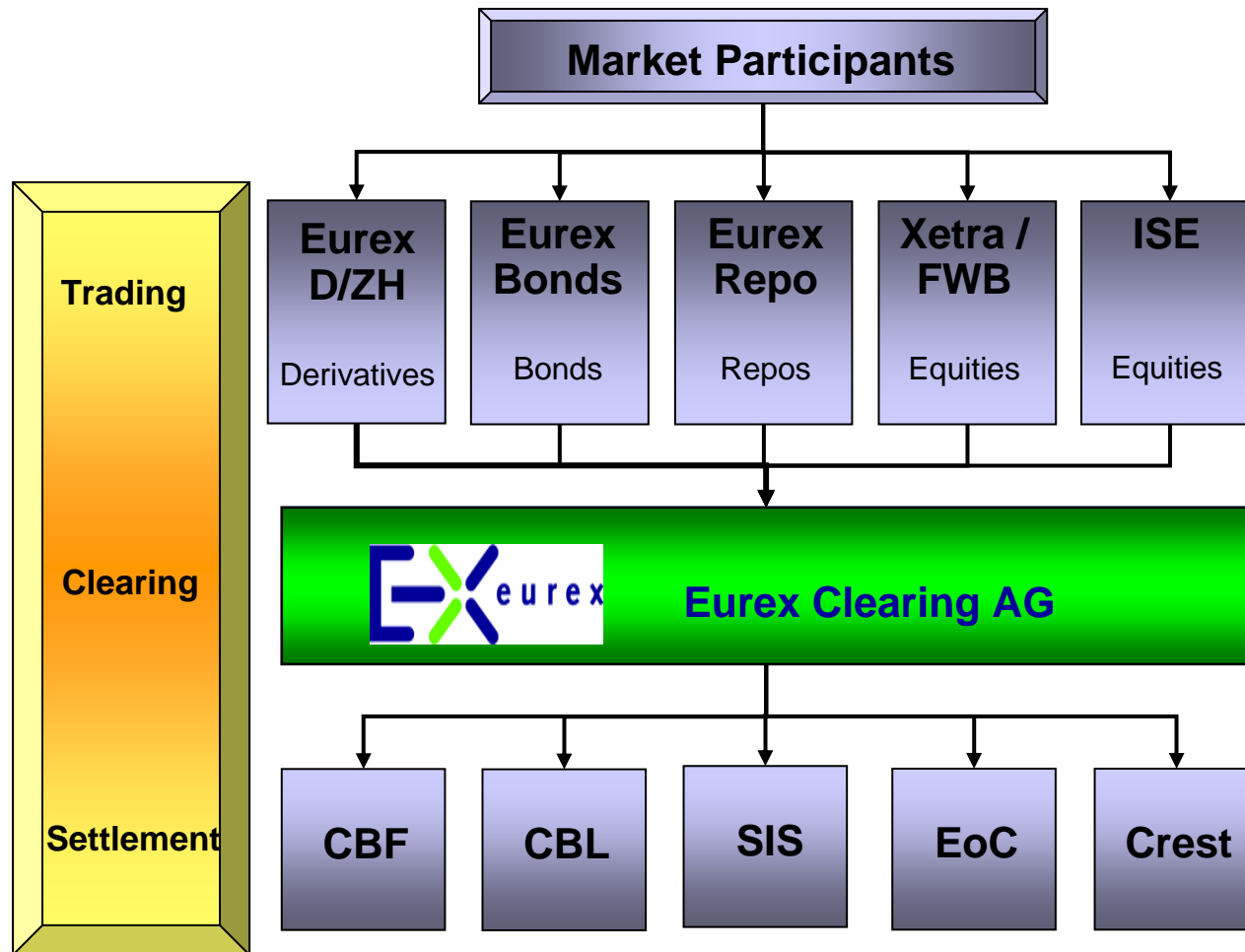
ECB/ Chicago Fed Conference “Industry Structure and Development”
4 April 2006, Frankfurt

Daniel Gisler, Eurex, Member of the Executive Committee

1. Eurex Clearing AG: Description of CCP

- 2. Basel II supports risk free CCP functions
- 3. Demand for market efficiency
- 4. Special case: non clearing member

Many Markets – One Clearinghouse

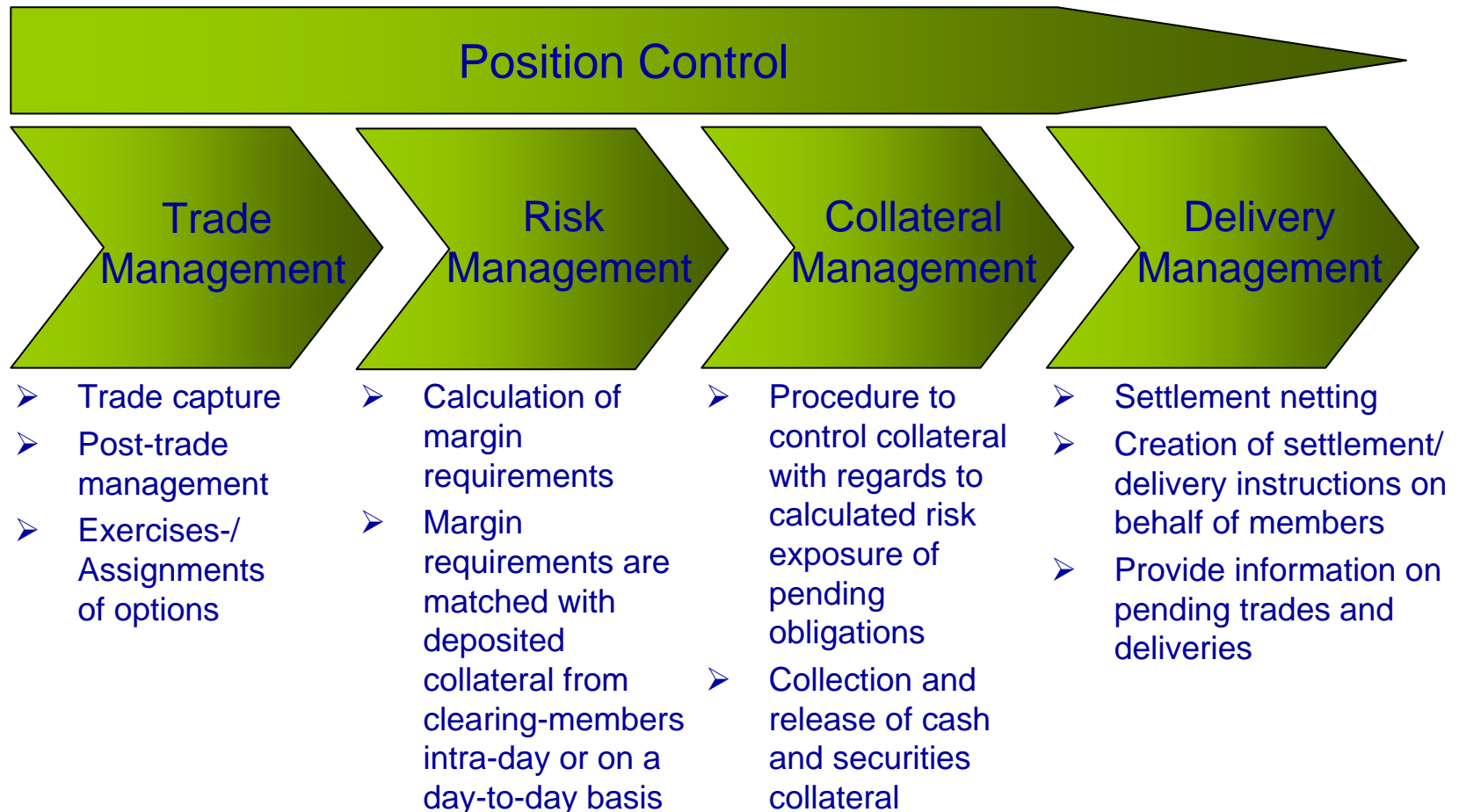


- Eurex Clearing AG is the central counterparty for different trading locations
- Effective risk & collateral management
- Reduction of cross border settlements

Function of Eurex Clearing AG

- Eurex Clearing AG's function in the value chain:
> Execution > **Clearing** > Settlement > Custody
- **Definition of clearing:**
Clearing is the management (risk management, transaction monitoring, netting) of a transaction after matching of a buy and sell trade being processed in preparation for the change of ownership of the product until legal fulfillment of the respective obligation.
- **Simplified processes through central counterparty:**
Being connected with various CSDs, Eurex Clearing AG not only assumes the counterparty risk for all clearing members, but also simplifies settlement processes for the clearing members.

Business of Eurex Clearing AG – A Trade Life Cycles' View



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Regulators have accepted market driven solution

- Market driven solution have led to a maximum risk reduction in CCP business.
- Regulators have accepted market driven solution:
 - **CPSS-IOSCO Recommendations** have defined a common industry standard for risk management of a CCP.
 - **ESCB-CESR Standards** promote and sustain the integration and competitiveness of European markets by encouraging efficient structures and market-led responses to developments.
 - **Basel II** as well as the EU **Capital Requirements Directive** support risk free functions of CCP.
 - **National requirements**, e.g. BMF/BaFin intend to agree to risk free functions of CCP.

Basel II and CRD support risk free CCP functions

- **In the past:** In a first final version of Basel II, there was no explicit regulation with regard to the handling of outstanding credit risks with a central counterparty.
- **Current status:** Basel II and CRD support a 0% credit risk weighting, for banks exposures to central counterparty clearing houses.
- In the version of **Basel II**, International Convergence of Capital Measurement and Capital Standards, A Revised Framework, updated in November 2005, the following text was added (page 212):

„6. **An exposure value of zero for counterparty credit risk can be attributed to derivative contracts or SFTs that are outstanding with a central counterparty (e.g. a clearing house).** This does not apply to counterparty credit risk exposures from derivative transactions and SFTs that have been rejected by the central counterparty. Furthermore, an exposure value of zero can be attributed to banks' credit risk exposures to central counterparties that result from the derivative transactions, SFTs or spot transactions that the bank has outstanding with the central counterparty. This exemption extends in particular to credit exposures from clearing deposits and from collateral posted with the central counterparty. A central counterparty is an entity that interposes itself between counterparties to contracts traded within one or more financial markets, becoming the legal counterparty such that it is the buyer to every seller and the seller to every buyer. In order to qualify for the above exemptions, the central counterparty CCR exposures with all participants in its arrangements must be fully collateralized on a daily basis, thereby providing protection for the central counterparty's CCR exposures. Assets held by a central counterparty as a custodian on the bank's behalf would not be subject to a capital requirement for counterparty credit risk exposure.“

Basel II and CRD support risk free CCP functions

- Extract from **Capital Requirement Directive**, Annex III, 12890/05 ADD 2, page 9:

“6. An exposure value of zero for CCR can be attributed to derivative contracts, or repurchase transactions, securities or commodities lending or borrowing transactions, long settlement transactions and margin lending transactions outstanding with a central counterparty and that have not been rejected by the central counterparty. Furthermore, an exposure value of zero can be attributed to credit risk exposures to central counterparties that result from the derivative contracts, repurchase transactions, securities or commodities lending or borrowing transactions, long settlement transactions and margin lending transactions or other exposures, as determined by the competent authorities, that the credit institution has outstanding with the central counterparty. The central counterparty CCR exposures with all participants in its arrangements shall be fully collateralised on a daily basis.”

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Market efficiency – achieving the value of CCP

Current status:

- To achieve this goal we need a consistent implementation of Basel II/CRD to avoid legal uncertainty and distortion of competition.
- Example: At present time,
 - BaFin intends to develop an explicit regulation regarding the status of CCPs
 - it is not clear if FSA and other European supervisory authorities will also develop such a regulation
 - there are no passporting requirements or a harmonized acceptance procedure for CCPs within the EU
- Most of Eurex Clearing members have their domicile in Germany as well as in Switzerland and UK. Therefore, they are subject to different regulations. In this context, there is a need for further harmonization.

Market efficiency – achieving the value of CCP Proposal:

- To achieve this goal
 - we welcome a consistent implementation of the Basel II regulatory framework within the EU
 - we need harmonized acceptance procedure or passporting for CCPs
 - we demand for a level-playing field in this area
 - we need a non-discriminatory acceptance procedure for foreign CCPs in all Member States

- In this context, CPSS/IOSCO Recommendations give a well-balanced basis for a harmonized acceptance procedure for CCPs within the EU.

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Handling of collateralization requirements to Non-Clearing-Members

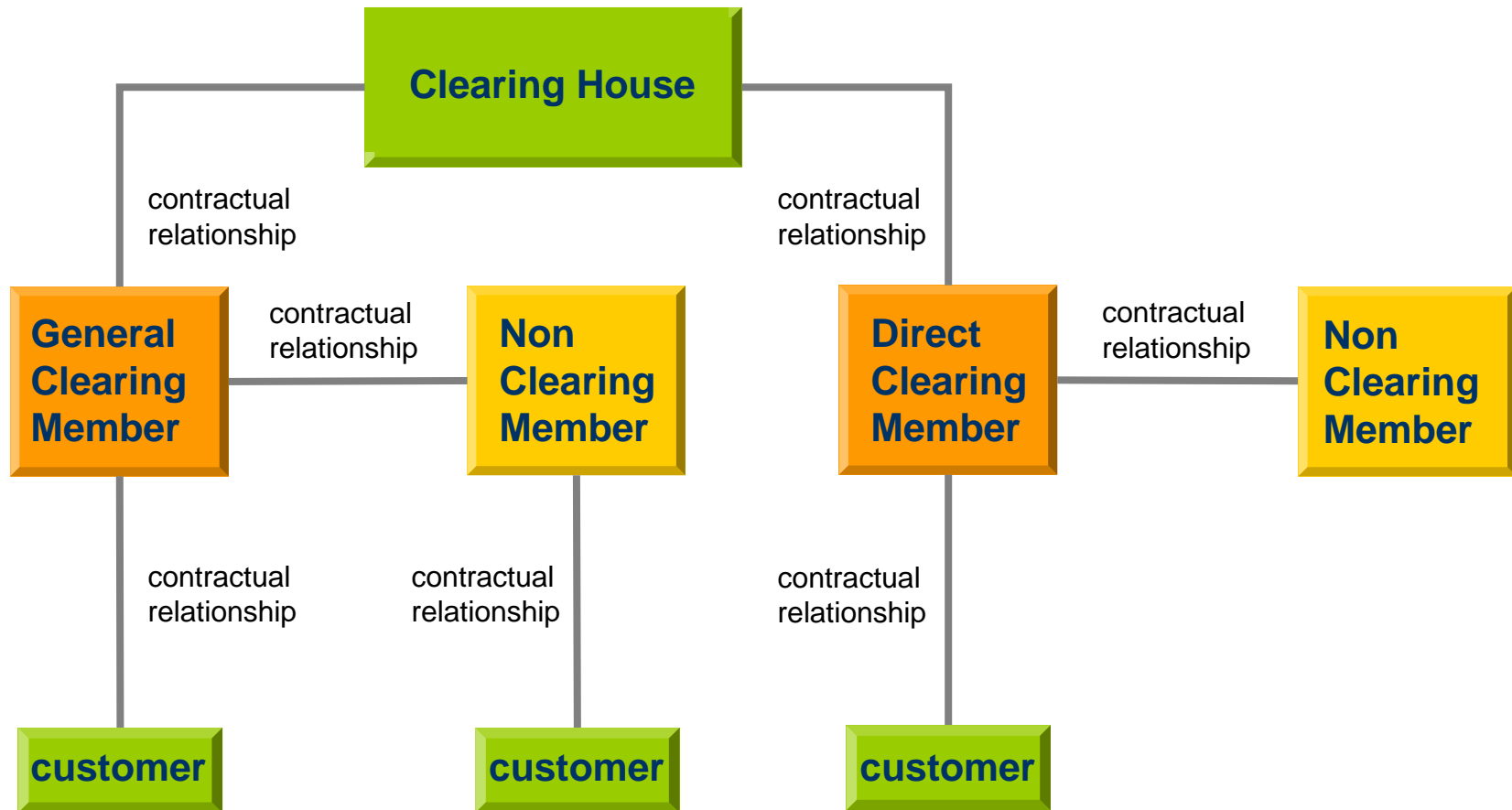
- Example:
 1. Level: CCP – Clearing Member A
 2. Level: Clearing Member A – Exchange Member B
 3. Level: Exchange Member B – Bank C
 4. Level: Bank C – recipient customer

- Based on this example, it has to be clarified if the „Bank C“ is allowed to make use of the specific national requirements regarding the collateralization privilege of CCP.

- This may be clarified based on the structure of the segregation of assets throughout all involved levels.

BACK UP

Contractual Relationship at Eurex and Eurex Clearing AG



Eurex Clearing Licenses – Cleared and Settled Products

Clearing License	Cleared and settled products
Derivatives Clearing	Futures and options products Futures leg of basis trades*
Bonds Clearing	Fixed-rate bonds of the Federal Republic of Germany or the Treuhandanstalt Jumbo Pfandbriefe of German issuers Issues of the Kreditanstalt für Wiederaufbau**, the European Investment Bank and the German States Securities leg of basis trades*
Repo Clearing	General Collateral and Special Repo with: Fixed-rate bonds of the Federal Republic of Germany or the Treuhandanstalt Jumbo Pfandbriefe from German issuers Bonds issued by Kreditanstalt für Wiederaufbau and German States
Equity Clearing	Shares held in collective safe custody that are traded on the FWB floor or via Xetra

Eurex / Eurex Clearing Membership Requirements to become a Clearing Member

The applicant

- Is domiciled in the EU or Switzerland and is licensed by the local authority to operate the conduct of safe custody business, lending operations and the receipt of collateral
- Is under surveillance of responsible local authority
- Has a minimum liable equity capital of
 - EUR 125 Mio. for a GCM or EUR 12.5 Mio. for a DCM Derivatives Clearing License
 - EUR 25 Mio. for a GCM or EUR 2.5 Mio. for a DCM Equity Clearing Licence
 - EUR 50 Mio. for a GCM or EUR 5 Mio. for a DCM Bond Clearing License
 - EUR 175 Mio. for a GCM or EUR 17.5 Mio. For a DCM Repo Clearing License
- Provides a contribution to clearing fund
- Provides evidence of a securities and a pledged securities account at either CBF or SIS
- Maintains an account at the Deutsche Bundesbank (DBB) or the Schweizer National Bank (SNB)
- Provides at least one qualified trader and one qualified back office staff
- Guarantees the orderly processing of all transactions in the clearing process
- Fulfills the Eurex technical requirements

Eurex Membership Requirements NCM

The applicant must

- be registered in its country of origin. Eurex does not allow individual personal memberships.
- be regulated by the banking/securities supervisory authority in the country of origin.
- maintain capital of at least EUR 50,000 unless the applicant is a bank.
- guarantee the orderly processing of all transactions in the clearing process.
- fulfill the Eurex technical requirements.