



# Euroclear Finland Default Board Policy

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# 1.Scope

- This document sets out the principles, considerations and procedures that Euroclear Finland -can apply in handling the default of participants (“Default Policy” or “Policy”). A default is defined to be any of the following measures:<sup>1</sup> Opening of bankruptcy proceedings (*konkurssimenettely*)
- Company restructuring (*yrittöksen saneerausmenettely*)
- Decision on the interruption of operations (*toiminnan keskeyttäminen*)
- Liquidation (*selvitystila*)
- Closing or withdrawal of an authorization (*sulkeminen tai toimiluvan peruuttaminen*)
- Another decision of an authority on the commencement of executory proceedings (*muu verrattava viranomaisen päätös pakkotäytäntöönpanoon ryhtymisestä*)

In order to test the effectiveness and practicality of the default procedure, Euroclear Finland will undertake with its participants and other relevant stakeholders testing and review at least annually.

The Default Policy is based on Euroclear Finland’s Rules and CEO’s decisions governing Euroclear Finland’s rights and obligations on processing participant’s default. Euroclear Finland’s Rules and CEO’s decisions are sent to the market and authorities for consultation prior to approval.

The purpose of the policy is to cover not only legal but also relevant business aspects in order to manage business processes and risks related to the default of a participant.

It should be noted that the policy has been prepared mainly for bankruptcy of a participant, but it may be applied to the appropriate extent also on other default of a participant, such as withdrawal of an authorization.

The relevant stakeholders in the default of a participant:

- Euroclear Finland
- External stakeholders:
  - Insolvency estate/administrator
  - Authorities:
    - Finnish Financial Services Authority (“FIN-FSA”, incl. agent potentially nominated by FIN-FSA to control insolvency estate’s business)
    - Bank of Finland
    - Ministry of Finance
    - Financial Stability Authority (“RVV”)
    - ESMA
    - District Court
  - Other participants (settlement participants, account operators, issuer agents etc.)
  - Trading venues
  - CCPs (CCPs clearing trades with Finnish securities)
  - Linked CSDs

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<sup>1</sup> Act on Certain Securities and Currency Trading and Clearing System 2 §.

## 1.1. Objectives

Euroclear Finland's default management process has the following main objectives:

- To share information effectively with key stakeholders (participants, venues, regulators, CCPs etc.)
- To minimise the impact on other participants
- To settle as many of the insolvent participant's transactions as possible
- To prevent systemic risk (e.g. mitigating bankruptcy estate disputes on settled transactions)

## 1.2. Implementation

The policy includes a description for the management of a participant's default. On a high level, the process consists of following steps:

1. Initiation of default management process,
2. Initial actions (Priority 1 Actions),
3. Other actions of 0-day (Priority 2 Actions),
4. Continuation of settlement

A more detailed description is given in section 2.

# 2. Management process of a participant's default

## 2.1. Initiation of the Default Management Process

Initiation of the default management process takes place after Euroclear Finland has received information about participant's default.

The information should be received from the relevant authority which depends on the default situation in question (e.g. district court, FIN-FSA, Ministry of Finance, RVV or respective foreign authority).

It is also possible for Euroclear Finland to receive the information on default of a participant from a wide range of sources, such as from relevant trading venues, CCPs, or other Euroclear group entities. Moreover, Euroclear Finland Rules require that participants shall notify of their default to Euroclear Finland as soon as possible. This information will need to be verified from an official source, such as formal ruling by district court.

The information should be provided to Euroclear Finland's email address [settlement.finland@euroclear.eu](mailto:settlement.finland@euroclear.eu)

Other possible contact methods to inform Euroclear Finland of a default is by phone at +358 20 770 6559 or by Fax at +358 20 770 6655

Euroclear Finland will evaluate the information received and to decide upon whether initiation of the default management process shall take place or whether additional information is required.

After information about the default of a participant is verified (FIN-FSA, or other trusted source), Euroclear Finland will initiate the default management process.

Euroclear Finland will contact FIN-FSA (and if considered necessary, other authorities) in order to

- share the information available at the moment (if not already shared)
- receive any further information about the situation and
- agree upon the information sharing during the course of the process.

The applicability of the actions described in section 2.2, 2.3, and 2.4, provide a framework to apply when processing participant's default. The main criteria affecting the judgement of the decisions and actions taken are;

- whether confirmation is received from an official source
  - Without official confirmation no action is taken by Euroclear Finland
- type of default
  - Whether the default type requires immediate action by Euroclear Finland
- whether the insolvency estate is known and in control of the estate
  - Insolvency estate may allow for defaulting participant's operations to continue with minimal disruptions
- the status of the settlement day/settlement process
  - If the information of the default is received outside of settlement hours, certain actions may not be necessary

## 2.2. Initial Actions (Priority 1 Actions)

Objectives of initial actions are:

- To freeze settlement process preventing further settlement of transactions until information on settlement day's status and which transactions can be settled is available.
- Suspension of the participant's status in order to prevent insolvent participant on entering new settlement instructions.
- To prevent repatriation of funds from the system in order to secure that such funds can be used for settlement of the clearing party's transactions (in the manner provided by Section 11, Subsection 2 of the Act on Certain Securities and Currency Trading and Clearing System ("the Netting Act")).
  - With Euroclear Finland's permission, the insolvent participant can deposit additional funds into the system.
- Inserting the appropriate restriction for the insolvent participant own accounts in the system. This has the following consequences:
  - The insolvent participant's matched settlement instructions are put on hold.
  - The insolvent participant's unmatched settlement instructions are cancelled.
  - Pending rights and restrictions will be cancelled for designated book-entries.

By taking these actions, Euroclear Finland aims to limit the impact of participant's default to the market. This includes ensuring that the transactions that are settled are legally irrevocable despite participant's default and won't cause further systemic risk to the market.

Initial (priority 1) actions can be divided into system specific actions and general actions. Key principles are also further elaborated below.

It should be noted that priority 1 actions and priority 2 actions can be taken in parallel.

### Priority 1 actions in Infinity system

- Registering default restriction to participant's own data (book-entry account data on the account's right holder): this action will effectively (due to time priority rule of registrations) mean that securities kept in book-entry accounts opened in the insolvent participant's own name can no longer be used for settlement (or dispose otherwise) unless the insolvency estate/administrator take actions to use such securities for settlement (or dispose otherwise). This registration will not affect participant's clients' transactions from settling provided that those transactions are protected under the Netting Act.
- Disabling the insolvent participant's connections to Infinity system: this action will effectively disable participants operations in the system (incl. transfer of funds from payment transfer account / deposit) unless it is later agreed with the insolvency estate/administrator that it will continue business operations of the insolvent participant.
- Settlement process will be put on hold: this action means that operation of Infinity meaning both settlement and execution of corporate action payments of the securities issued in the Infinity System is on hold for all participants until Euroclear Finland's further decision.
- Settlement instructions that are not protected under the Netting Act are put on party hold.
- Prevention of whole account transfers to the insolvent participant.
- Suspension of participant's status in the system.

### Communication with external stakeholders (General actions)

Euroclear Finland will stay in regular contact with the authorities and will transmit the following information to FIN-FSA and the Ministry of Finance as soon as possible after the initiation of the default management process:

- The type of the insolvent participant
  - Legal status, license, activity, whether it is a key participant
- Pending settlement instructions of the insolvent participant
  - The total volume and value
  - If possible, estimate of the volume and value of instructions that may fail
  - The type of transactions and financial instruments that those instructions relate to
- When applicable, in which common settlement infrastructure (e.g. T2S) the defaulting participant's settlement instructions are processed
- When available, any indicators of cross-border activities of the insolvent participant
- When known, the number of clients of the insolvent participant
- Information on any risks that the default might entail (market impact)

Actions to be taken are notified as soon as possible to FIN-FSA, the Ministry of Finance and the insolvent participant. Euroclear Finland will also inform as soon as possible all participants, FIN-FSA, the Ministry of Finance, Bank of Finland, ESMA, trading venues and CCPs served by Euroclear Finland and the linked CSDs of the actions taken by Euroclear Finland.

Euroclear Finland has prepared in advance templates to be used at least for the following notifications during 0-day:

- 1<sup>st</sup> Notification:
  - a participant has been declared insolvent and that settlement process has been put on hold. This notification will be sent as soon as possible after initiation of the default management process with information that Euroclear Finland will send a further notification on the matter as soon as possible after priority 1 actions have been taken.
- 2<sup>nd</sup> Notification:

- information on the immediate actions taken due to participant's default (i.e. that participant's operations towards Euroclear Finland's system have been restricted and that its participant status has been suspended). This notification will be sent as soon as possible after priority 1 actions have been taken. Participants are also informed on the actions Euroclear Finland is taking to restrict settlement of transactions that are added into the systems after the said moment.

As soon as possible after information on the participant's default is verified, relevant trading venues are informed of the matter by Euroclear Finland, if the participant was acting as a settlement member for trades made on such trading venue. Also the CCP in the market is informed on the matter (as the CCP is a participant of Euroclear Finland it will receive the information simultaneously with other participants).

FIN-FSA is contacted as soon as possible by Euroclear Finland in order to share information and to receive information whether FIN-FSA has appointed an agent to control insolvency estate's business and how the regulators' cooperation is/will be arranged in a cross-border case. Cooperation with FIN-FSA will be agreed at this early stage.

Though gathering of status information in general is considered to take place as priority 2 action, it is started as soon as possible. The actions are done in parallel with priority 1 actions to the extent possible without delaying priority 1 actions.

Euroclear Finland contacts the Insolvency estate/administrator as soon as possible in order to discuss the situation in more detail.

### 2.3. Other Actions of 0-Day (Priority 2 Actions)

Objective of priority 2 actions is to minimise the impact of participant's default to the market. Thus, Euroclear Finland will take actions to allow as many transactions as possible (by taking into account the Netting Act) to be settled despite the default.

Euroclear Finland's rules gives Euroclear Finland the right to change, extend or cut short the settlement schedule due to participant default.

#### Gathering of relevant status information

At least following information will be gathered:

- moment of when Euroclear Finland is considered to have become aware of the beginning of the default proceedings and moment when default proceedings were initiated (note that Euroclear Finland has reasonable time to react to the information)
- status of settlement day/settlement process
- payment liability of participant (during the day and coming days)
- the amount of participant's transactions in the systems (0-day, coming days)
- has the insolvent participant added transactions into the systems after the moment when Euroclear Finland was/should have become aware of the default proceedings
- amount of participant's settlement instructions that are not yet irrevocable
- participant's roles: does it settle only own transactions or others' as well?
- is the participant an issuer or an issuer agent in the market with payments due on 0-day or coming days

**Definition of a moment when default proceeding were initiated / Euroclear Finland became aware of it**

According to Netting Act and Euroclear Finland's Rules, settlement is protected in the event of default of a participant if transaction was added into the system prior to the moment of opening of the default proceedings.

Additionally, settlement is protected in the event that the transaction became irrevocable (added into the system by both participants and matched) after default proceedings began but before Euroclear Finland knew or should have known of the opening of default proceedings. These transactions can be settled only on the day the default proceedings began.

In practice Euroclear Finland needs reasonable time to react to the information it receives on a participant's default and this has also been recognised by Netting Act's preamble. When information is received through electronic communication means, the moment when Euroclear Finland should have known of the opening of bankruptcy proceedings is the receipt timestamp of the message plus reasonable time to react. When information is received otherwise than electronically, there is more room for interpretation.

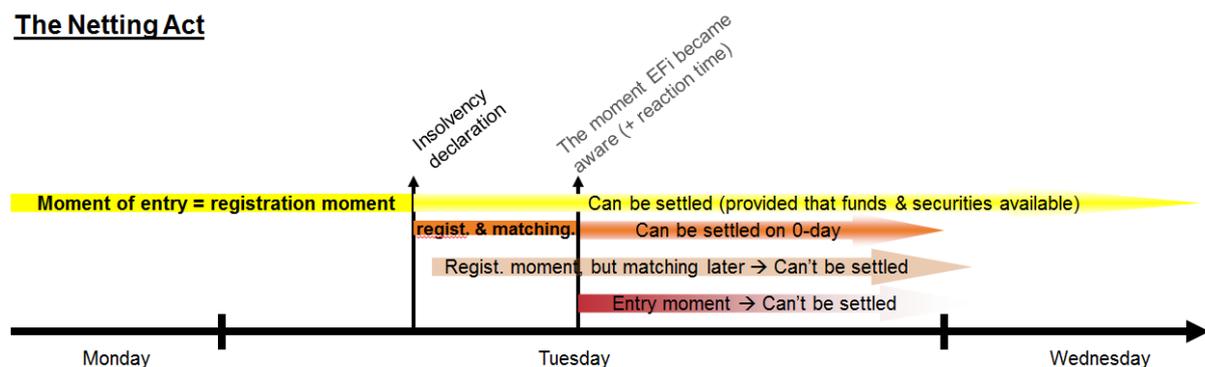
### Status of settlement day/settlement process

If Euroclear Finland receives information on participant's default during any optimization batch, such batch will be run through and settlement system will be put on hold immediately after the processing has ended. Based in status information, there will be a new settlement schedule planned for the rest of the day. The plan has to also cover links and take into account the amount of unsettled transactions. Also an evaluation of the need to amend settlement schedule on 1-day will be made. Changes to settlement schedule shall be approved by the CEO of Euroclear Finland (or his/her deputy).

Infinity system operates continuously during 06:00 - 19:00 on all TARGET-opening days.

### Segregation of transactions depending on their status

#### The Netting Act



Processing of insolvent participant's instructions (instructing party):

1. Inserted into the system before the moment of 'Default Declaration' => Can be settled regardless of status

2. Inserted and matched between the moment of 'Default Declaration' and the moment when 'Euroclear Finland became aware of default (+ reaction time)' => Can be settled only during the day when the default was declared, not after that.
3. Inserted between the 'Default Declaration' and the moment when 'Euroclear Finland became aware of default (+ reaction time)' but matched after the moment when 'Euroclear Finland became aware (+reaction time) of default' => Can't be settled. => Put on party hold.
4. Inserted after the moment when 'Euroclear Finland became aware of default (+reaction time)' => Can't be settled. => Put on party hold.

The party hold -functionality is used in Infinity.

Payment liabilities (for 0-day and for coming days) and amount of transactions of the insolvent participant are key information while evaluating effects of the participant's default to the market.

In the event the insolvent participant has acted as a clearing party for other brokers, such other brokers' transactions will be listed. This is a preliminary measure, in the event such transactions are transferred later on to some other clearing party for settlement. Brokers that have used the insolvent participant for settlement will be subject to suspension of their trading rights as they have no longer clearing and settlement of the transactions arranged. Such brokers shall arrange clearing and settlement of their transactions with other clearing party in order to restore their broker's rights.

### **Segregation of new transactions**

As it may be possible that the insolvency estate/administrator will continue business of the insolvent participant, at least in order to run down its business, it is important to keep separated transactions that can be settled without limitation and the transactions that are not protected under the Netting Act. It should be noted that the insolvency estate/administrator may decide to continue the participant's operations and commit to the settlement of transactions. However, these transactions are then the obligations of the estate and not the participant.

### **Contacting insolvency estate/administrator**

The insolvency estate/administrator will be contacted as soon as possible. At least the following matters will be discussed with the administrator:

- information is given to the administrator on the insolvent participant's roles within Euroclear Finland
- status of obligations as well as on operations of the participant is given in order to assure that transactions that could be settled under the Netting Act are settled in order to mitigate systemic risk
- prerequisites of the insolvency estate to act as Euroclear Finland's participant
- in the event there exists prerequisites for insolvency estate to continue business, necessary user rights will be defined and created after necessary decisions
- necessary guarantees need to be arranged before insolvency estate may continue business.

### **Actions to be taken after priority 2 actions**

After necessary priority 2 actions have been taken, Euroclear Finland will make a decision on releasing settlement processing from hold. The following notifications are sent to participants and authorities:

- 3<sup>rd</sup> Notification
  - processing will start at defined moment in time. Participants are informed on the moment when default proceedings took place and Euroclear Finland was informed about the matter (or should have become aware of this matter). Participants are also informed about transactions that can be settled normally and about transactions that would not be protected under Netting Act and are thus inactivated or put on party hold by Euroclear Finland. This notification is to be sent after priority 2 actions have been taken.
- 4<sup>rd</sup> Notification
  - Notification on releasing the settlement process from hold.

#### **Actions at the end of 0-day**

According to Netting Act, transactions that became irrevocable after the default declaration but before settlement system operator become aware of this matter, can be settled only during the day when default proceedings began. The moment of transaction's irrevocability is the moment when a transaction is matched.

At the end of 0-day such unsettled transactions will be put on party hold in Infinity. Thus, such transactions will not be settled automatically.

## **2.4. Continuation of Settlement**

After the decision to release settlement processing from hold (this decision should take place as soon as necessary actions have been taken during 0-day) has been made, the settlement will be continued as normally as possible.

However, as the restriction on bankruptcy or other applicable restriction is registered to the book-entry accounts of the insolvent participant, settlement from/to insolvent participant's own accounts will require actions from the insolvency estate/administrator.

Securities held in the accounts of the insolvent participant's clients can be used normally for settlement provided that the transactions are protected under the Netting Act. Of course, they also have to have the general prerequisites to settle, i.e. sufficient securities in the book-entry account and/or sufficient assets in relevant payment transfer account/deposit.

The insolvency estate may transfer additional assets to the payment transfer account / deposit once Euroclear Finland has re-enabled the funds transfer.

There may be a situation that the insolvency estate/administrator can't be reached during 0-day. This may cause a situation where there could be a material lack of securities, liquidity or instructions for transactions, and thus, severe disturbances to settlement of other participants' transactions.

In the event insolvency estate/administrator is reached, Euroclear Finland will stay in regular contact with the administrator.

## **3. Development, Review and Testing of Default**

Euroclear Finland involves the relevant internal staff and stakeholders in developing and reviewing the default process.

Effectiveness and practicality of Euroclear Finland's default management process is tested with relevant internal staff and stakeholders at least annually and additionally if substantive changes are made to the default process or if requested by the authorities. Such test is arranged with a relevant sample of participants, internal staff, relevant market infrastructures and any other entities as appropriate.

The annual test includes a simulation exercise and a test of the communication procedures. Euroclear Finland defines the parameters according to which the test is run before every test. Euroclear Finland takes into account at least the following factors:

- different types of participants (in terms of volume, activity, etc.),
- participants located in different countries and time zones,
- participants holding different types of accounts (omnibus and segregated) and
- relevant market infrastructures, as appropriate.

If any weaknesses are identified in the test, Euroclear Finland will make necessary improvements to the default process. Where the simulation exercise reveals the lack of knowledge or readiness to apply the default process by the participants or other market infrastructures, Euroclear Finland uses normal supervision process to inform these entities and to make sure that they take actions to remove such weaknesses. If internal lack of knowledge or readiness is found, Euroclear Finland will address these issues and provide additional internal training.

The test results and the possible contemplated changes to the default process are reported to the Euroclear Finland Risk Committee and the Board of Directors of Euroclear Finland. The test results and possible changes to the default process are shared with FIN-FSA, the Ministry of Finance and Bank of Finland. The summary of the test results and possible changes to the default process are also disclosed to Euroclear Finland's participants.

## 4. Oversight of this Board policy

The content of this document is approved by the Board of Euroclear Finland.

Euroclear Finland Operations is accountable for overseeing its implementation.

Euroclear Finland Operations will review this document every year and report any review findings internally, and recommend amendments or additions, when appropriate.

## 5. Creating awareness on Euroclear Finland's Default policy

Euroclear Finland Operations is responsible for creating awareness around this Default policy both internally and with the relevant stakeholders.

Practical awareness tools include:

- Internally ensuring that Euroclear Finland's default policy is available to all relevant staff members and relevant staff members are appropriately trained annually.

- Externally organising annual exercises involving relevant staff members and stakeholders to ensure the preparedness of both Euroclear Finland and its stakeholders in the event of a market participant default.

## 6. Definitions

Definitions of significant terms used in this document are set out below:

|                   |   |
|-------------------|---|
| Board             | The board of directors of Euroclear Finland.  |
| Staff             | Any person employed full-time or part-time by a Euroclear Company under a contract of employment, whether based at a Euroclear Company's premises or otherwise. |
| Euroclear Finland | A direct wholly-owned subsidiary of Euroclear plc.  |
| CCP               | Central Counterparty  |
| Policy Documents  | Euroclear's board policies and policy handbooks   |
| 0-Day             | 0-Day stands for the day when the default procedure began.  |
| Netting Act       | Act on Certain Conditions of Securities and Currency Trading as well as Settlement Systems (1084/1999)  |
| FIN-FSA           | Finnish Financial Supervisory Authority (Finanssivalvonta)  |



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