

KELER CCP's Recovery Plan

The objective of KELER CCP's Recovery Plan is to ensure, to the greatest extent possible, the continuous and smooth operation of the central counterparty in a crisis situation that may arise, to maintain the continuity of critical services and to preserve financial stability while minimising negative impact on tax payers, and to give to the Resolution Authority all information necessary for successful resolution.

The Recovery Plan of KELER CCP:

- ✓ does not assume any extraordinary public financial support or central bank liquidity assistance,
- ✓ if implemented, the exposure of clearing members to the central counterparty cannot be unlimited,
- ✓ is non-discriminatory, and
- ✓ takes into account the interests of all stakeholders.

It treats separately the cases of default and non-default; and links recovery tools and measures to the different scenarios laid out by KELER CCP. It sets out the stress scenarios when the continuous and smooth operation of critical services of KELER CCP would be in danger, there is a significant deterioration of KELER CCP's financial situation, or risk of breaching the prudential requirements under Regulation (EU) No 648/2012.

With respect to the Recovery Plan, KELER CCP identified four critical functions¹:

1. spot market central counterparty activity,
2. derivative market central counterparty activity,
3. gas market central counterparty activity, and
4. energy market non-clearing membership service.

Recovery situations, recovery tools

The Recovery Plan covers the management of all forms of financial crisis that may arise at KELER CCP that exceeds the resources designed to handle default and other requirements pursuant to EMIR. It includes:

- a) clearing member default events (i.e. *default events*),
- b) the occurrence of other risks and losses (i.e. other, *non-default events*).

¹ The activities, services and operational processes of KELER CCP, performed or offered to parties other than the central counterparty, the termination of which would result in the interruption of services vital for the real economy or financial stability, with particular respect to the substitution possibility of activities, services or operational processes.

The recovery situations may cover the following sub-events:

a) in case of default

- the default waterfall pursuant to EMIR is exhausted, but not all default positions are closed, thus further loss may arise on such positions;
- the default waterfall pursuant to EMIR is exhausted, all default positions are closed, but there remains unallocated loss uncovered by the elements of the default waterfall pursuant to EMIR;
- the default waterfall pursuant to EMIR is exhausted, all default positions are closed, there is no unallocated loss, but it becomes difficult to find the necessary amount of financial resources to ensure operation compliant with EMIR;

b) in case of non-default:

- critical decrease of value in the own funds of KELER CCP, i.e. significant foreign exchange rate loss suffered on the investments of KELER CCP;
- occurrence of operational risk event of high amount loss;
- liquidity shortage due to the insolvency or operational issues of the account managers of KELER CCP.

c) in case of both default and non-default

- occurrence of liquidity difficulty that cannot be managed with the use of instruments normally available, and KELER CCP would become insolvent;
- KELER CCP does not comply with the capital adequacy requirements of EMIR, and the compliance in the near future cannot be ensured.

The recovery tools available in the specific default and non-default events are as follows:

A. Default events:

I. In the case of allocation of losses arising from clearing member default

- a. requiring clearing members to make a payment of predefined amount (~ cash call ~ assessment power);
- b. variation margin haircutting (VMHC));
- c. use of collaterals of non-defaulting clearing members (use of initial margin);
- d. eventual capital increase of KELER CCP.

II. To restore the neutral (zero) position (~matched book) of KELER CCP

- a. after clearing members default voluntary / forced allocation of contracts;
- b. contract termination: tear up complete/partial

B. Non-default events:

- I. use of capital, capital increase;
- II. insurance; or
- III. other instruments (e.g. clearing member payment).

KELER CCP can obtain liquidity from third parties (credit institutions) or clearing members to overcome liquidity difficulties. In order to replenish the financial resources, among recovery tools, KELER CCP can increase capital or require clearing members to make payments of predefined amount.

Stress scenarios

Individual stress scenarios posing threat to the continuous and smooth operation of KELER CCP critical functions, eroding the financial situation of KELER CCP or resulting in the increase of its risk of such an extent that would lead to non-compliance with the requirements stated in EMIR are set out in the Recovery Plan. Stress scenarios may cover the following situations:

1. significant losses or liquidity difficulties resulting from default;
2. significant losses or liquidity difficulties resulting from general business risk;
3. significant losses or liquidity difficulties resulting from operational risk events, including cyber attacks also;
4. liquidity difficulties arising due to losses realized on investments;
5. failure of third parties providing critical services to KELER CCP;
6. financial or operational difficulties arising due to parent or subsidiary company crisis;
7. financial or operational difficulties arising due to the crisis of related CCPs.

With respect to the Recovery Plan, KELER CCP sets out the following stress scenarios:

- A. Significant losses or liquidity difficulties due to the simultaneous default of several clearing members under extreme market conditions;
- B. VAT financing;
- C. Occurrence of operational risk loss event with large amount net damage;
- D. Foreign exchange rate loss realized on own capital due to Forint market crisis;
- E. Operational problem of KELER;
- F. ECC becomes subject to restricting payment procedures.

Recovery Plan implementation

The Plan can be implemented when there is a significant deterioration of KELER CCP's financial situation, or risk of breach of its prudential requirements under Regulation (EU) 648/2012.

The Chief Executive Officer of KELER CCP establishes the need to implement the Plan based on the indicators, or even without indicators, and informs the Supervisory Authority (Central Bank of Hungary).

However, if the viability of KELER CCP is at risk, the Resolution Authority acting under its special power and taking the opportunity of early intervention, if the insolvency of KELER CCP cannot be declared yet, instead of the recovery measures, but before the start of resolution, it attempts to remedy the arising recovery situation.

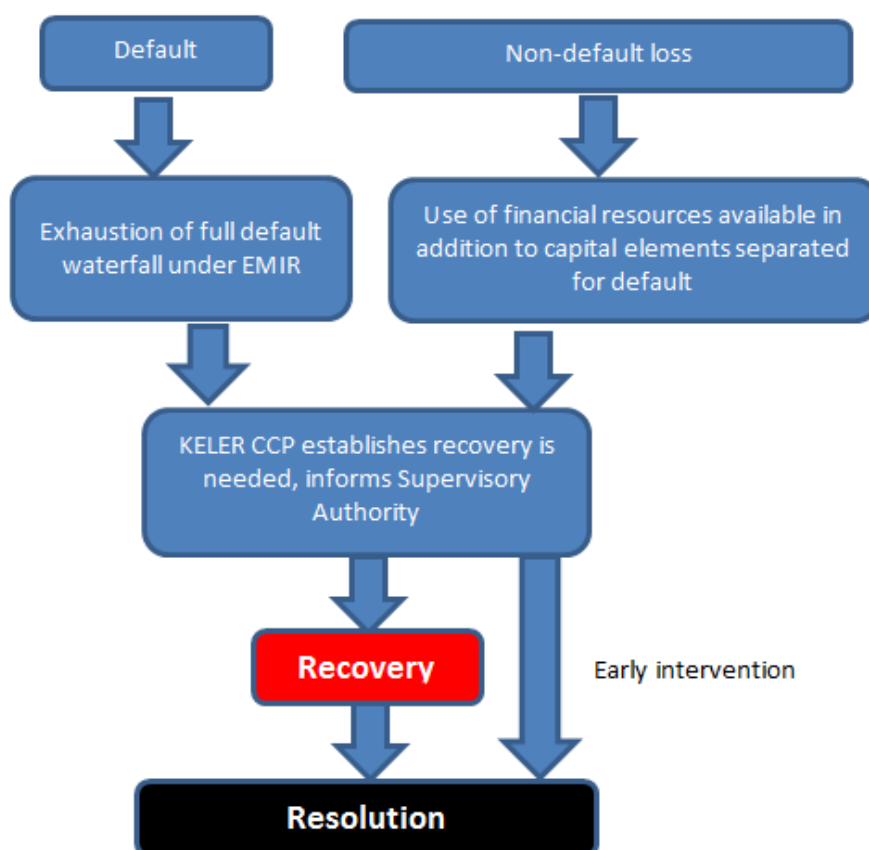
The indicators on the need to implement the recovery plan are basically derived from and linked to the recovery situations and the stress scenarios. When thresholds defined for individual indicators are reached, the Recovery Plan (can) be activated. Indicators can be of warning nature that help avoid recovery situations by giving alert or can specifically indicate the need to implement the Recovery Plan.

We use (where possible) an alerting system similar to the “traffic light approach” to qualify the utilisation of thresholds, which assists to recognize the negative processes perceived in normal operation and take the necessary measures to avoid the violation of threshold values.

As a general principle, recovery is not started automatically based on indicators only. It must be preceded by a possibly very rapid quality analysis and consultation with the Supervisory Authority. In justified cases, it is possible not to activate the Recovery Plan despite red indicators; however, this is subject to prior consultation with and agreement by the Supervisory Authority.

Indicator monitoring is performed in close cooperation with the relevant authorities; monitoring results are forwarded to the competent authority and ESMA.

Separate recovery actions are assigned to the events, stress scenarios and related indicators triggering the specific recovery, during such actions the earlier defined recovery tools are used.



The following circumstances and procedures ensure the timely implementation of recovery actions:

- system of indicators, its monitoring and reporting within the organization and to the Supervisory Authority;
- flat organization of KELER CCP facilitating extremely fast exchange of information (in both directions);
- physical proximity of the Chief Executive Officer and all KELER CCP employees, making informal flow of information efficient;
- continuous availability of the Chief Executive Officer, the Clearing Operation Officer and the Chief Risk Officer, and technical capabilities such as corporate mail system installed on phones and remote access ensure rapid reaction;
- owing to these factors and based on the corporate culture of KELER CCP also, management control is tight and managers and subordinates have close work relationships.

Final loss allocation:

Final loss allocation in case of default can be performed if KELER CCP has exhausted all the guarantee elements stated in its General Business Rules for the default concerned, but additional financial resources are needed to remedy the situation. Final loss allocation is detailed by markets in the Recovery Plan of KELER CCP.

Difficulties, risks

Difficulties, risks identified in the case of individual recovery situations that may limit the effectiveness of recovery are as follows:

1. The Clearing Member is unwilling to meet its cash-call, or making such payment would deteriorate its financial position to such an extent that would pose an even bigger threat to financial stability by triggering a spiral effect;
2. The owner refuses to grant capital increase or equity loan;
3. KELER CCP cannot get external liquidity as third parties are unwilling to provide liquidity; owner refuses to grant capital increase or equity loan;
4. The success of recovery is not necessarily ensured in the case of liquidity shortage arising due to the insolvency or operational problems of the account manager of KELER CCP;
5. KELER CCP as general clearing member is subjected to requirements that make it significantly difficult or even impossible to exit as general clearing member, or until exit unaffordable financial burden would arise at KELER CCP.

Crisis communication

Consistency between external and internal communication related to individual crisis situations is of high importance. This basic principle helps prevent inappropriate, incorrect information spread both within and outside the organization.

The KELER CCP Recovery Plan can be implemented exclusively after communication with the relevant authority, as part of which KELER CCP informs the relevant authority on the problem arising and the instruments and measures to be used in the course of recovery. Additionally, KELER CCP defines precisely the period it deems necessary to recover its financial position.

Communication during the first 24 hours after the start of the crisis situation is a critical point, and is the most decisive in an uncertain situation. This communication includes the communication of measures and instruments that KELER CCP intends to use.

The KELER CCP regulation on giving media statements and crisis communication defines responsibility for internal and external communication in specific situations. The Chief Executive Officer is responsible for the communication of KELER CCP, therefore any media statement is to be made subject to prior consent, or control if needed, by the Chief Executive Officer. As a general rule, the KELER CCP Chief Executive Officer is entitled to give statements in any crisis situation. Deviation from this rule is allowed; in this case the KELER CCP Chief Executive Officer delegates the task or appoints another person for this task in its absence.

Simultaneously with the establishment of the crisis communication situation, it is possible to order a news blackout for all staff members of the KELER Group, as a result of which no employee of the KELER Group can give written, verbal, official or unofficial statement related to the crisis situation.

KELER Group can provide information, external communication material or the extract of it directly to the clients involved in the crisis subject to consultation and approval by the KELER CCP Chief Executive Officer or the KELER Chief Executive Officer, or the Management of KELER, if needed the communication specialist. External communication to clients is primarily based on information published on the KID system, and/or in electronic mail and/or on the web sites www.kelerkszf.hu and www.keler.hu. If these channels are not available, information is provided by fax or on the phone.