Annex N

Collateral Part

This document, which is provided for illustrative purposes only, sets out near-final and proposed changes to the Bank of England FMI Rulebook Annex N: Collateral Part, originally published as part of the consultation "Ensuring the resilience of CCPs" dated 18 July 2025 (the Consultation).

In this document, new text is underlined and deleted text is struck through.

Near-final changes to the Collateral Part made in response to the Consultation (as published alongside this document) are shown in red.

Proposed changes to the Collateral Part, subject to an open Bank of England consultation *Review of CCP Collateral Rules – letters of credit* closing 15 January 2027 are shown in green.

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COLLATERAL

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1 APPLICATION

1.1 This Part applies to a *UK CCP*.

2 COLLATERAL REQUIREMENTS

2.1 (1) A *CCP* must only accept highly liquid collateral with minimal credit and market risk to cover its initial and ongoing exposure to its *clearing members* and where relevant, *CCP*s with which it has *interoperability arrangements*.

(2) A *CCP* may accept cash, financial instruments, commercial bank letters of creditguarantees, central bank guarantees or gold as collateral subject to the requirements of this Part.

2.2 A *CCP* must apply an adequate haircut to the value of an asset that reflects the potential for its value to decline over the interval between its last revaluation and the time by which it can reasonably be assumed to be liquidated.

2.3 A *CCP* must determine the acceptable collateral and relevant haircuts taking into account:

(1) the liquidity risk following the default of a market participant; and

(2) the concentration risk that may result on certain assets from such determination.

2.4 A *CCP* may accept, where appropriate and sufficiently prudent, the underlying of the *derivative contract* or the financial instrument that originates the *CCP* exposure as collateral to cover its ~~*margine*~~exposure.

2.5 A *CCP* must establish and implement transparent and predictable policies and procedures to assess and continuously monitor the liquidity of assets accepted as collateral and take remedial action where appropriate.

2.6 A *CCP* must:

(1) review its eligible asset policies and procedures at least annually; and

(2) conduct a review whenever a material change occurs that affects the *CCP's* risk exposure.

3 CASH COLLATERAL

3.1 For the purposes of 2.1(1), highly liquid collateral in the form of cash must be denominated in one of the following:

(1) a currency the risk of which the *CCP* is able to adequately manage; or

(2) a currency in which the *CCP* clears transactions, but limited to the amount of the collateral required to cover the *CCP's* exposures in that currency.

4 FINANCIAL INSTRUMENTS CONSIDERED AS HIGHLY LIQUID COLLATERAL

4.1 For the purposes of 2.1(1), a *CCP* may only accept a financial instrument as highly liquid collateral if it meets the conditions in paragraph 1 of the Annex to Investment Policy Part or is *transferable securities* or a *money-market instrument* and meets each of the following conditions:

(1) the financial instrument has been issued by an issuer that has low credit risk based upon an adequate internal assessment by the *CCP* employing a defined and objective methodology that:

(a) does not fully rely on external opinions; and

(b) takes into consideration the risk arising from the establishment of the issuer in a particular country;

(2) the financial instrument has a low market risk based upon an adequate internal assessment by the *CCP* employing a defined and objective methodology that does not fully rely on external opinions;

(3) it is denominated in one of the following currencies:

(a) a currency the risk of which the *CCP* is able to manage; or

(b) a currency in which the *CCP* clears contracts, in the limit of the collateral required to cover the *CCP's* exposures in that currency;

(4) it is freely transferable and without any regulatory or legal constraint or third-party claims that impair liquidation;

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(5) it has an active outright sale or repurchase agreement market, with a diverse group of buyers and sellers, to which the *CCP* can demonstrate reliable access, including in stressed conditions;

(6) it has reliable price data published on a regular basis;

(7) it is not issued by:

(a) the *clearing member* providing the collateral, or an entity that is part of the same *group* as the *clearing member*, except in the case of a *covered bond* and only where the assets backing that bond are appropriately segregated within a robust legal framework and satisfy the requirements set out in this Chapter;

(b) a *CCP* or an entity that is part of the same *group* as the *CCP*; or

(c) an entity whose business involves providing services critical to the functioning of the *CCP*, unless that entity is the *Bank* or a central bank of issue of a currency in which the *CCP* has exposures; and

(8) it is not otherwise subject to significant *wrong-way risk*.

5 COMMERCIAL BANK LETTERS OF CREDIT~~GUARANTEES~~ CONSIDERED AS HIGHLY LIQUID COLLATERAL

5.1 For the purposes of 2.1(1), a *CCP* may only accept a commercial bank letter of credit~~guarantee~~ as highly liquid collateral if it meets the following conditions:

(1) it is issued to support the payment obligations of ~~guarantee a *clearing member* that is~~ a *non-financial counterparty* that is a *clearing member* or *client*;

(2) it specifies:

(a) the *CCP* as sole beneficiary; or

(b) the *CCP* and the *clearing member* that posts the letter of credit on behalf of the *client*, as beneficiaries, provided that the consent of the *CCP* is required before the *clearing member* may redeem the letter of credit;

(3~~2~~) it has been issued by an ~~an issuer~~ an *authorised UK credit institution* or an *authorised overseas credit institution* that has low credit risk based upon an adequate internal assessment performed by the *CCP* employing a defined and objective methodology that:

(a) does not fully rely on external opinions; ~~and~~

(b) takes into consideration the risk arising from the establishment of the issuer in a particular country; and

(c) monitors for any changes that would require a reassessment of that credit risk;

(4~~3~~) it is denominated in one of the following currencies:

(a) a currency the risk of which the *CCP* is able to adequately manage; or

(b) a currency in which the *CCP* clears contracts, in the limit of the collateral required to cover the *CCP's* exposures in that currency;

(5~~4~~) it is irrevocable, unconditional and the issuer cannot rely on any legal or contractual exemption or defence to oppose the payment of the letter of credit~~guarantee~~;

(6~~5~~) it can be honoured, on demand, within the period of liquidation of the portfolio of the defaulting *non-financial counterparty* or *clearing member* providing it without any regulatory, legal or operational constraint;

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(76) it is not issued by:

(a) an entity that is part of the same *group* as the *non-financial counterparty~~clearing member~~* covered by the letter of credit~~guarantee~~; or

(b) an entity whose business involves providing services critical to functioning of the *CCP*, unless that entity is the *Bank* or a central bank of issue of a currency in which the *CCP* has exposures;

(87) it is not otherwise subject to significant *wrong-way risk*;

~~(8) it is fully backed by collateral that meets the following conditions:~~

~~(a) it is not subject to wrong-way risk based on a correlation with the credit standing of the guarantor or the *clearing member*, unless that wrong-way risk has been adequately mitigated by haircutting of the collateral; and~~

~~(b) the *CCP* has prompt access to it and it is bankruptcy remote in case of the simultaneous default of the *clearing member* and the guarantor;~~

(9) the suitability of the issuer~~guarantor~~ has been ratified by the *board* of the *CCP* after a full assessment of the issuer and of the legal, contractual and operational framework of the letter of credit~~guarantee~~ in order to have a high level of comfort on the effectiveness of the letter of credit~~guarantee~~; ~~and~~

(10) the *CCP* has notified the *Bank* of the outcome of the ratification and assessment carried out under 5.1(9)~~.~~; and

(11) the *CCP* has undertaken appropriate due diligence, including validation checks with the issuer, to confirm the authenticity and validity of the letter of credit.

5.2 If a *CCP* accepts a letter of credit~~bank guarantee~~ from ~~*clearing member* that is~~ a *non-financial counterparty*, it must take such letter of credit~~bank guarantee~~ into account when calculating its exposure to the ~~bank~~ issuer providing the guarantee if that ~~bank~~ issuer is a *clearing member*.

6 CENTRAL BANK GUARANTEES CONSIDERED AS HIGHLY LIQUID COLLATERAL

6.1 For the purposes of 2.1(1), a *CCP* may accept a bank guarantee issued by a central bank as highly liquid collateral if it meets the following conditions:

(1) it is issued by the *Bank* or a central bank of issue of a currency in which the *CCP* has exposures;

(2) it is denominated in one of the following currencies:

(a) a currency the risk of which the *CCP* is able to adequately manage;

(b) a currency in which the *CCP* clears transactions, in the limit of the collateral required to cover the *CCP's* exposures in that currency;

(3) it is irrevocable, unconditional and the issuing central bank cannot rely on any legal or contractual exemption or defence to oppose the payment of the guarantee; and

(4) it can be honoured within the period of liquidation of the portfolio of the defaulting *clearing member* providing it without any regulatory, legal or operational constraint or any third-party claim on it.

7 GOLD CONSIDERED AS HIGHLY LIQUID COLLATERAL

7.1 For the purposes of 2.1(1), a *CCP* may accept gold as highly liquid collateral if it is allocated pure gold bullion of recognised good delivery and meets one of the following conditions:

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(1) the gold is directly held by the *CCP;*

(2) the gold is deposited with the *Bank* or a central bank of issue of a currency in which the *CCP* has exposures that has adequate arrangements so as to safeguard *clearing member* or *client*s' ownership rights to the gold and enable the *CCP* prompt access to the gold when required;

(3) the gold is deposited with an *authorised UK credit institution* (not including any establishment of that *credit institution* outside the *UK*) or an *overseas credit institution UK branch* that:

(a) has adequate arrangements so as to safeguard *clearing member* or *clients'* ownership rights to the gold and enable the *CCP* prompt access to the gold when required; and

(b) has a low credit risk based upon an adequate internal assessment by the *CCP* employing a defined and objective methodology that does not fully rely on external opinions; or

(4) the gold is deposited with an *authorised overseas credit institution* or a *UK credit institution overseas branch* that:

(a) is subject to and complies with prudential rules at least as stringent as those applicable to an *authorised UK credit institution;*

(b) has robust accounting practices, safekeeping procedures and internal controls;

(c) has adequate arrangements so as to safeguard *clearing member* or *client*s' ownership rights to the gold and enable the *CCP* prompt access to the gold when required; and

(d) has a low credit risk based upon an internal assessment by the *CCP* employing a defined and objective methodology that:

(i) does not fully rely on external opinions; and

(ii) takes into consideration the risk arising from the establishment of the *authorised overseas credit institution* or the *UK credit institution overseas branch* in a particular country.

8 VALUING COLLATERAL

8.1 For the purposes of valuing highly liquid collateral, a *CCP* must establish and implement policies and procedures to monitor on a near to real time basis the credit quality, market liquidity and price volatility of each asset accepted as collateral.

8.2 A *CCP* must:

(1) monitor on a regular basis, and at least annually, the adequacy of its valuation policies and procedures, and

(2) carry out such a review whenever a material change occurs that affects the *CCP's* risk exposure.

8.3 A *CCP* must mark-to-market its collateral on a near to real time basis and, where not possible, a *CCP* must be able to manage the related risks.

9 HAIRCUTS

9.1 A *CCP* must establish and implement policies and procedures to determine prudent haircuts to apply to collateral values.

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9.2 A *CCP* must ensure haircuts recognise that collateral may need to be liquidated in stressed market conditions and take into account the time required to liquidate it.

9.3 A *CCP* must be able to demonstrate to the *Bank* that haircuts are calculated in a conservative manner to limit as far as possible procyclical effects.

9.4 For each collateral asset, the *CCP* must determine the haircut by taking into consideration relevant criteria, including:

(1) the type of asset and level of credit risk associated with the financial instrument based upon internal assessment by the *CCP*.

(2) the maturity of the asset;

(3) the historical and hypothetical future price volatility of the asset in stressed market conditions;

(4) the liquidity of the underlying market, including bid/ask spreads;

(5) the foreign exchange risk, if any; and

(6) *wrong-way risk*.

9.5 In performing the assessment for 9.4(1), a *CCP* must employ a defined and objective methodology that:

(1) does not fully rely on external opinions; and

(2) takes into consideration the risk arising from the establishment of the issuer in a particular country.

9.6 A *CCP* must monitor on a regular basis the adequacy of the haircuts.

9.7 A *CCP* must review the haircuts policies and procedures:

(1) at least annually, and

(2) whenever a material change occurs that affects the *CCP* risk exposure.

9.8 A *CCP* must avoid as far as possible disruptive or big step changes in haircuts that could introduce procyclicality.

9.9 A *CCP* must ensure its haircut policies and procedures are independently validated at least annually.

10 CONCENTRATION LIMITS

10.1 (1) A *CCP* must establish and implement policies and procedures to ensure that the collateral remains sufficiently diversified to allow its liquidation within a defined holding period without a significant market impact.

(2) A *CCP's* policies and the procedures must determine the risk mitigation measures to be applied when the concentration limits specified in 10.2 are exceeded.

10.2 A *CCP* must determine concentration limits at the level of:

(1) individual issuers;

(2) type of issuer;

(3) type of asset;

(4) each *clearing member*; and

(5) all *clearing members*.

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10.3 A *CCP* must determine concentration limits in a conservative manner taking into account all relevant criteria, including:

(1) financial instruments issued by issuers of the same type in terms of economic sector, activity, geographic region;

(2) the level of credit risk of the financial instrument or of the issuer based upon an internal assessment performed by the *CCP* employing a defined and objective methodology that:

(a) does not fully rely on external opinions; and

(b) takes into consideration the risk arising from the establishment of the issuer in a particular country; and

(3) the liquidity and the price volatility of the financial instruments.

10.4 ~~(1)~~ A *CCP* must ensure that no more than 5~~10~~% of its collateral ~~that is in the form of commercial bank guarantees~~ is in the form of letters of credit issued~~guaranteed~~ by:

(1~~a~~) a single *credit institution*; or

~~(2b) a single *financial institution* that is based in a country or territory other than the *UK*; or~~

(2~~c~~) an entity that is part of the same *group* as the *credit institution* ~~or *financial institution*~~.

~~(2) Where the collateral received by the *CCP* in the form of commercial bank guarantees is higher than 50% of the total collateral, the *CCP* may set this limit up to 25%.~~

10.5 (1) In calculating the limits in 10.2, a *CCP* must include the total exposure of a *CCP* to an issuer, including the cumulative amount of credit lines, certificates of deposit, time deposits, savings accounts, deposit accounts, current accounts, *money-market instruments* and reverse repurchase facilities used by the *CCP*.

(2) A *CCP* must not apply the concentration limits ~~in~~determined under 10.2 to collateral held by the *CCP* in excess of the minimum requirements for ~~*initial*~~*margins* (including, where appropriate, *variation margin*), *default fund* or other financial resources.

10.6 When determining the concentration limit for a *CCP's* exposure to an individual issuer, a *CCP* must aggregate and treat as a single risk its exposures to all financial instruments issued by the issuer or by a *group* entity (or explicitly guaranteed by the issuer or by a *group* entity), and to financial instruments issued by undertakings whose exclusive purpose is to own means of production that are essential for the issuer's business.

10.7 A *CCP* must monitor on a regular basis the adequacy of its concentration limit policies and procedures.

10.8 A *CCP* must:

(1) review its concentration limit policy and procedure at least annually, and

(2) review this policy whenever a material change occurs that affects the risk exposure of the *CCP*.

10.9 A *CCP* must inform the *Bank* and the *clearing members* of the applicable concentration limits and of any amendment to these limits.

10.10 If the *CCP* materially breaches a concentration limit set out in its policies and procedures, it must inform the *Bank* immediately and rectify the breach as soon as possible.

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