

**DISCLOSURE FRAMEWORK FOR  
SECURITIES SETTLEMENT SYSTEMS**

**Krajowy Depozyt Papierów Wartościowych SA  
(The National Depository for Securities)**

**September 2000**

## Preamble and Disclaimer Notice

The following document is the response of the KDPW SA (The National Depository for Securities), to the questionnaire entitled "Disclosure Framework for Securities Settlement Systems" developed by a joint working group of the Committee on Payment and Settlement Systems (CPSS) and the International Organizations of Securities Commissions (IOSCO).

While every effort has been made to ensure the correctness of the information in the following document, KDPW SA cannot accept any responsibility for any errors that it may contain.

Request for further information may be directed to:

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### I. Basic information

#### A. *What is the name of the SSS?*

The National Depository for Securities, Poland (*in Polish:* Krajowy Depozyt Papierow Wartosciowych) (KDPW)

#### B. *Where and in which time zone is the SSS located?*

Ul. Ksiazeca 4, Warsaw  
Central European Time (GMT +1)

#### C. *What functions does the SSS perform?*

Depository functions:

- Registration of securities admitted to public trading,
- Administration of corporate actions for securities in the system,
- Assigning ISIN codes to securities,

Settlement functions:

- Settlement of transactions on the cash market,
- Derivatives clearing house,
- Administration of settlement guarantee systems,
- Administration of securities lending and borrowing system,

Other functions:

- Distribution of information and educational role for market participants,
- Clearing of payments between open-end pension funds,
- Administration of the Pension Fund Guarantee System.

#### *1. Does the SSS serve as a securities depository and/or provide securities settlement services?*

KDPW operates as both a securities depository and a settlement institution for transactions concluded on the Warsaw Stock Exchange (WSE), on the regulated secondary off-exchange market (Central Table of Offers - CTO) and outside regulated trading.

*(a) What types of instrument are eligible for deposit at the SSS (e.g. debt, equities, warrants, etc.)?*

All types of instruments that have been admitted to public trading in Poland are eligible for deposit at KDPW. Currently, the following types of instruments are registered:

- Shares,
- Treasury bonds,
- Municipal bonds,
- Convertible bonds,
- Corporate bonds,
- Central bank bonds,
- Investment certificates,
- Share rights,
- Subscription rights,
- Warrants,
- Futures contracts.

*(b) What types of instrument are eligible for transfer within the SSS?*

All the aforementioned instruments are eligible for transfer within KDPW.

*(c) Please describe whether eligible securities are dematerialised, immobilised or transferred physically.*

All securities are dematerialised.

*(d) Does the SSS provide safekeeping for physical certificates?*

KDPW does not keep any securities in physical form.

*2. Does the SSS provide cash accounts and/or provide funds transfers in conjunction with securities transfers? If so, in what currencies?*

KDPW does not keep cash accounts. It operates on the basis of authorisation granted by direct depository participants and prepares cash transfers for transaction settlement purposes, which are carried out in the National Bank of Poland (the Polish Central Bank).

*3. Does the SSS provide a trade matching service? Do others provide such services for securities settled at the SSS?*

No. (See section V.A).

*4. Does the SSS provide a trade netting service (as distinct from undertaking the settlement of securities transfers on a net basis)? Do others provide such services for securities settled at the SSS? In either case, what types of netting (bilateral or multilateral), if any, are performed?*

KDPW generally provides multilateral netting for all transactions settled using cash through the depository. Only so-called outright transactions (the sale of Treasury bonds by the National Bank of Poland) are settled using bilateral netting. The exception to the netting rule is the settlement of Treasury bond auctions in the primary market, which are settled in gross.

*5. Does the SSS offer a securities lending or borrowing program?*

In order to ensure transaction settlement liquidity, KDPW organises and manages a securities lending and borrowing system. Securities lending is based on a system of automatic loans whose purpose is to prevent or eliminate suspensions of transaction settlement. KDPW initiates the procedure, acting as intermediary in establishing the securities loan, once it has determined that there is a lack of sufficient securities on the participant's account necessary to settle the transaction. During the lifetime of the loan, the identities of the securities lender and borrower remain anonymous to each other.

*6. Does the SSS provide custodial and/or related services such as the collection of interest, dividends, principal or withholding tax reclamations? Which types of service are provided?*

KDPW provides the following custodial services:

- Dividend and interest payments,
- Pre-emptive rights,
- Rights to new shares admitted to public trading,
- Assimilations,
- The withdrawal of securities from the Depository,
- Conversions of registered securities into bearer securities, and vice versa,
- The exchange of securities,
- Assigning ISIN numbers to securities.

*7. Does the SSS act as a central counterparty or principal to transactions with its participants?*

No

*8. Other? Please specify.*

See introduction to Section C above

*C. What type of organisation is the SSS?*

*1. Please indicate whether the SSS is a public sector or private sector entity.*

KDPW is a private sector entity.

*2. Please indicate whether the SSS is organised on a for-profit or a non-profit basis.*

KDPW is organised on a non-profit basis.

*3. What is the legal basis for the establishment of the SSS and for securities transfers made through it?*

In 1991-94, KDPW formed a part of the Warsaw Stock Exchange. In 1994, following the adoption of the Law on the Public Trading in Securities and Trust Funds, it became (and remains) an independent institution as a joint stock company. KDPW's responsibilities are defined in the Law on the Public Trading in Securities, as well as other legislation regulating particular areas of the capital market, such as the Act on the Organisation and Operation of Pension Funds.

The legal existence of the company is defined in the Polish Commercial Code and the KDPW Statute. Internal Rules governing KDPW operations include the KDPW Rules and Detailed Rules of Operation.

*E. Please describe and provide a diagram outlining the organisational and ownership structure of the SSS.*

See Figure 1.

*1. Who are the owners of the SSS?*

The KDPW shareholders are: The Warsaw Stock Exchange (33.3%), the State Treasury (33.3%) and the National Bank of Poland (33.3%).

*2. What entity or entities operate the SSS? Which functions of the SSS, if any, are outsourced to third parties?*

KDPW manages its own depository-settlement system.

*3. Does the SSS have a Board of Directors?*

KDPW has a Board of Directors - the KDPW Management Board.

*(a) What is its composition?*

President and CEO - Elzbieta Pustola  
Vice President - Ludwik Sobolewski  
Remaining members: Teresa Rogalska, Anna Szulecka

*(b) What are its responsibilities?*

The Management Board runs the Company and manages its finances, and acts as the public face of the Company. The Management Board prepares drafts of the KDPW Rules of Operation, the KDPW Supervisory Board Rules, the Rules of the KDPW Court of Arbitration and drafts and adopts detailed rules relating to the operation of the Depository.

*F. Please describe the financial resources of the SSS.*

*1. Amount of paid-in capital and retained earnings?*

Capital (according to the Balance Sheet for 31.12.1999)  
Share capital: 21 million PLN,  
Supplementary capital: 38 million PLN

Reserve capital: 91.5 million

Pre-tax profit for 1999: 36.4 million PLN

2. *Guarantees, insurance coverage or other similar arrangements?*

None

3. *Credit lines or letters of credit?*

None

4. *Powers to assess participants or equity holders?*

None

*G. Please describe whether the SSS or its operator is subject to authorisation, supervision or oversight by an external authority.*

The KDPW Rules are approved by the Polish Securities and Exchanges Commission. The Company is permanently supervised by the Supervisory Board.

## **II. Rules and procedures of the SSS**

*A. Does the SSS maintain a complete list of the rules and procedures governing the rights and obligations of participants and the duties of the SSS?*

The rules and procedures are contained within the following documents:

- The KDPW Rules
- The KDPW Detailed Rules of Operation
- The KDPW Registration Procedures

*1. How can participants obtain a copy of the rules and procedures?*

The KDPW Rules and any amendments, once they have been adopted by the KDPW Supervisory Board and immediately on being approved by the Polish SEC, are sent to all KDPW participants by fax and then a copy is sent by post.

Other regulations (such as the Detailed Rules of Operation and KDPW Registration Procedures) and amendments to them, are also sent to all KDPW participants by fax and then a copy is sent to them by post.

In addition, a copy of current rules and procedures are available from KDPW directly or from its web-site ([www.kdpw.com.pl](http://www.kdpw.com.pl)).

*2. Does other documentation provided to participants (e.g. user guides) have the same status as the rules and procedures?*

Other documentation does not have the same status.

*3. Describe the process for changing rules and procedures, including any need for regulatory approval.*

(a) *What authority is required, and how does this differ depending on the type of change involved?*

The KDPW Rules and its amendments are adopted by the KDPW Supervisory Board at the request of the KDPW Management Board. The KDPW Rules and its amendments must then be approved by the Polish SEC, which may withhold its approval if it believes the proposed changes are in breach of legal regulations or may pose a threat to proper trading.

Other regulations such as the Detailed Rules of Operation are adopted by the KDPW Management Board, acting on the basis of the KDPW Rules.

(b) *How are participants notified of changes in rules and procedures?*

Participants are informed of all changes in rules and procedures by fax.

KDPW informs all its participants about changes in the KDPW Rules at least 2 weeks before they come into force.

As regards changes in the Detailed Rules of Operation or Registration Procedures, KDPW informs all participants at least 2 weeks before they come into force, or earlier if the changes are to be implemented sooner as a result of system demands.

(c) *Is there a procedure for participants or others to comment on proposed rule changes?*

KDPW constantly co-operates with its participants in adapting the depository-settlement system rules to the needs of a changing capital market. This is why many KDPW participants put forward proposals of changes to the KDPW Rules and Detailed Rules of Operation, which are then reviewed by the KDPW Management Board.

*B. Are the rules and procedures binding on the SSS as well as its participants? Under what conditions and on whose authority can written rules and procedures be waived or suspended by the SSS?*

The KDPW Rules, as well as other KDPW regulations, all form an integral part of the participants' agreement and are binding on both parties to that agreement: KDPW and all the KDPW participants.

### **III. Relationships with participants**

A. *A. Please describe the types of membership offered by the SSS.*

1. *How do the types differ?*

The following may become KDPW participants on the basis of a participation (membership) agreement:

- Institutions entitled by law to manage securities accounts,
- Other institutions authorised to perform brokerage activities,
- Other financial institutions, in particular banks, insurance firms, trust fund societies, pension fund societies and investment fund societies, if they invest financial assets in the securities market on their own account,
- Securities issuers,

- Foreign central depository-settlement institutions.

Participation in KDPW may take the form of:

- a) Direct participation,
- b) Indirect participation.

Direct participation involves independent relations with KDPW and other market participants. Indirect participants maintain relations with KDPW and other market participants through direct participants.

The participation agreement defines the activities the given participant will perform in the depository-settlement system, by indicating the type or types of participation status.

Types of participation status in the securities cash market:

- a) Custodian: where the participant manages clients' securities accounts not as a broker but as bank.
- b) Custodian - Own account: where the participant manages its own account with its own securities not as a broker but as bank.
- c) Depositor: where a participant authorises KDPW to manage that participant's own account with its own securities.
- d) Brokerage office: where a brokerage house or a bank carries out brokerage activities acting as an agent in securities trading.
- e) Brokerage office - Own account: where a brokerage house or bank carrying out brokerage activities manages its own account with its own securities.
- f) Lead manager - bearer securities: where a brokerage house or bank carrying out brokerage activities keeps a register of persons who are owners of bearer securities bought on the primary market or in an initial public offering.
- g) Lead manager - registered securities: where a brokerage house or bank carrying out brokerage activities keeps a register of persons who are owners of registered securities bought on the primary market or in an initial public offering.
- h) Participant's agent: where a participant, by virtue of an agreement with the participant managing securities accounts, takes responsibility for the settlement of transactions concluded on the basis of an order of the account holder.
- i) Over-the-counter market maker: where a brokerage house or bank carrying out brokerage activities buys and sells securities on their own account in order to carry out duties relating to the organisation of the regulated off-Exchange market.
- j) Stock Exchange market maker: where a brokerage house or bank carrying out brokerage activities buys and sells securities on their own account in order to carry out duties relating to the organisation of the regulated Stock Exchange market.
- k) Specialist broker: where a brokerage house or bank carrying out brokerage activities buys and sells securities on their own account in order to perform the role of specialist brokers.

Types of participation status in the securities derivatives market:

- l) Custodian - Derivatives: where the participant manages clients' securities accounts not as a broker but as bank.
- m) Custodian - Own account - Derivatives: where the participant manages its own account with its own securities not as a broker but as bank.



- n) Brokerage office - Derivatives: where a brokerage house or a bank carries out brokerage activities acting as an agent in securities trading.
- o) Brokerage office - Own account - Derivatives: where a brokerage house or bank carrying out brokerage activities manages its own account with its own securities.
- p) Participant's agent - Derivatives: where a participant, by virtue of an agreement with the participant managing securities accounts, takes responsibility for the settlement of transactions concluded on the basis of an order of the account holder.
- q) Over-the-counter market maker - Derivatives: where a brokerage house or bank carrying out brokerage activities buys and sells securities on their own account in order to carry out duties relating to the organisation of the regulated off-Exchange market.
- r) Stock Exchange market maker- Derivatives: where a brokerage house or bank carrying out brokerage activities buys and sells securities on their own account in order to carry out duties relating to the organisation of the regulated Stock Exchange market.

Direct participants may hold the status of settlement and non-settlement participants, which is related to the settlement guarantee system. The settlement participant is responsible both to KDPW and other participants for the proper and correct settlement of transactions, and is particularly involved in the establishment of the settlement guarantee system, on the basis of provisions defined in the KDPW Rules. A participant may only hold the status of settlement participant for certain types of transactions.

2. *Within each membership category, are all participants subject to the same rules and procedures? Please describe important exceptions, including both differences in rules across participants and the rationale for these differences.*

All participants holding the same status are subject to the same rules and procedures

- B. *Can participants establish accounts for their customers' assets that are segregated from their own asset accounts at the SSS?*

Yes, securities are registered with provisions for various types of participation status, which results in the requirement of separation of clients' securities from the participant's own securities.

1. *If so, is this accomplished through a single omnibus customer account or through a multiplicity of accounts and/or sub-accounts?*

For cash market instruments, KDPW accounts, which hold client securities, are omnibus accounts. For derivatives accounts in KDPW on which client derivatives are held an individual account structure exists.

2. *Is the segregation optional or compulsory?*

The segregation of clients' securities from the participant's own securities is compulsory.

3. *Does the fact that a sub-account at the SSS bears the name of a third party give any rights to that third party as a participant under the rules of the system?*

No. The fact that the system manages accounts both for participants and their clients does not entitle the clients of those participants to any rights as participants in the KDPW system.

*C. Please describe participant requirements for each type of membership.*

*1. Are participants required to be domiciled or resident in a particular jurisdiction?*

In general, only Polish financial institutions may become KDPW participants. Institutions based outside Poland that perform the functions of a central securities register or settle securities transactions may also become KDPW participants.

*2. Are participants required to be subject to a supervisory regime? If so, please describe.*

Each financial institution, according to its status, is subject to a supervisory regime (for instance, brokers and banks carrying out brokerage activities are regulated by the Polish SEC).

Irrespective of this, KDPW participants are subject to the KDPW Rules. The Supervisory Department at KDPW controls the activities of participants and whether they comply with the KDPW Rules.

*3. Are participants required to hold an equity stake in the SSS?*

No.

*4. Are there financial, economic, personal or other requirements (e.g. minimum capital requirements, "fit and proper" tests)? If so, please describe.*

The detailed terms and conditions, along with the documentation that an institution applying for KDPW participation status needs to present, are contained in the KDPW Rules.

A necessary condition for obtaining KDPW participation status is meeting the organisational, material, technical and financial conditions.

Organisational conditions require the participant to have in place a detailed system of internal rules and regulations defining in particular the flow of information, scope of duties and responsibilities, of employees performing functions relating to the management of securities accounts and carrying out transaction settlement.

Material and technical conditions require the participant to have the appropriate technical and technological equipment necessary for the correct registration of securities.

Financial conditions require the participant to maintain an adequate level of own assets and net capital.

The amount of assets belonging to settlement participants operating in the securities market may not fall below the levels defined in the KDPW Rules.

*D. Does the SSS engage in oversight of its participants to ensure that their actions are in accordance with its rules and procedures? If so, please describe.*

KDPW is responsible for supervising the correctness between the size of a securities issue and the number of securities in public trading, as well as supervising KDPW participants to see whether they have correctly followed the appropriate securities registration procedures. This supervision is carried out by analysing documentation provided by participants and carrying out inspections of the participants' offices by persons duly authorised by KDPW.

Direct participants holding the participation status of brokerage house are required to maintain the value of net capital and levels of reserve assets at a level defined in the appropriate legal

regulations that set out the minimal level of own assets required, the maximum limit of credits, loans and debt securities issued in relation to the brokerage house's own assets, as well as defining the minimal amount of own assets set aside for carrying out brokerage activities by the bank. In the event that a particular safety level defined in the regulations is crossed, the participant is obliged to inform KDPW of this within two days, indicating the reasons for the infringement and steps that will be taken to remedy it.

Direct participants are also responsible for calculating each day the engagement level, protection rate and credit indicators as defined in the appropriate regulations.

Direct participants holding the participation status of brokerage house are required to provide KDPW with:

- 1) An annual financial report,
- 2) A financial report every six months,
- 3) Financial information containing detailed calculations for net capital on the last day of the month, as well as the engagement level, protection rate and credit indicators,
- 4) Other information necessary for the correct assessment of the financial standing of the participant. Banks, which are direct KDPW participants, are in addition required to provide KDPW with quarterly financial information, as demanded by banking regulations.

If there is substantial evidence that the activities of a particular KDPW participant threaten the safety of trading, or that the probability of such a threat is high, the KDPW Management Board may order the direct participant, acting as a settlement participant, to provide information about the amount of its total debts, its net capital and its current engagement level.

*E. Under what conditions can participants terminate their membership in the SSS? Does this mark the end of all liabilities of the participant? If not, please describe what liabilities could remain.*

A participant may decide to close its depository accounts at KDPW, and at the same time give notice of its intent to terminate its participation in the Depository only when securities have ceased to be registered on its depository accounts. Once participation terminates, all duties and responsibilities arising from that participation in the Depository cease; however, all liabilities existing up to the day participation in KDPW ends, such as:

- liabilities arising as a result of transactions concluded on the day before participation ends, and not settled until that day,
- payments owed to KDPW from unpaid fees, continue to apply.

*F. Under what conditions can the SSS terminate a participant's membership in the SSS?*

KDPW may terminate a participation agreement with immediate effect (loss of participation status) or refrain from carrying it out (suspension of participation status) in instances where a participant creates a threat to the safety of trading or to the proper operation of the depository-settlement system.

Loss and suspension of participation status does not affect the duties of the participant arising from any operations carried out up to the day of the loss or suspension of that status.

Upon the loss or suspension of participation status, only those operations, which took place up to the day of the loss or suspension of that status, are executed in the KDPW accounts managed for that participant.

A participant whose participation status has ceased at KDPW is obliged to transfer securities registered on its accounts to another participant. KDPW reserves the right to sell securities

owned by that participant, operating on that participant's account, in the event that they were not transferred to another participant within one month of the day participation status ceased. In the event that participation status has been lost or suspended, KDPW immediately informs the Stock Exchange and the Over-the-Counter Market; these are then obliged to limit or suspend that participant's activities on the regulated market.

*G. Please describe the scope of the SSS's liability to participants, including the standard of liability (negligence, gross negligence, willful misconduct, strict liability or other), the force majeure standard, and any limitation to the scope of liability of the SSS (e.g. indirect or consequential damages). Where are these liabilities and their limitations set out (e.g. in statute or contract)?*

KDPW's liability to its participants is based on the principle of fault. Fault includes within its scope both intentional harm (direct and consequential), and unintentional harm (all degrees of negligence).

Included in the aforementioned instances and within the limits of KDPW's normal (usual) liability as a result of its failure to perform or improper performance of its duties are losses borne by the participant and potential benefits that may have been acquired were it not for the harm caused. KDPW bears no liability in instances of force majeure as an external, extraordinary and unstoppable event.

The aforementioned principles of liability arise from general legal regulations contained in the Polish Civil Code and are not affected by agreements with participants.

#### **IV. Relationships with other SSSs and commercial intermediaries**

*A. Does the SSS maintain linkages (including sub-custodian or cash correspondent relationships) or other relationships with other SSSs?*

No.

*1. Please identify each of the other SSSs used and the type of securities transferred via the linkages.*

*(a) What is the name of the other SSS? Where is it located?*

*(b) What securities are eligible for transfer via the linkage to the other SSS?*

*(c) Are transfers of securities made via the linkage to the other SSS limited to only those that are free of payment or are transfers against payment also made via the linkage to the other SSS? If against payment, please describe the timing of the transfers and the corresponding payments.*

*(d) Does the other SSS provide custody services to the SSS and, if so, who bears any credit or custody risks?*

Not applicable.

*B. Does the SSS use securities custodians (other than the other SSSs addressed in the previous question) and/or commercial cash correspondents? Please identify the custodians or cash correspondents used and the duties that each performs.*

No.

*C. Please describe the standards used in approving or reviewing relationships with other SSSs, custodians or cash correspondents, including any financial or operational requirements or the presence of insurance or public supervision.*

Not applicable.

*D. Does the SSS advance funds or securities to or on behalf of other intermediaries such as issuing or paying agents? If so, please identify the circumstances in which such exposure could arise.*

No

*E. Please describe measures in place to protect the SSS and its members against the failure of other SSSs or commercial intermediaries to meet obligations to the SSS, including risk controls, collateral or alternative sources of funds and securities.*

Not applicable.

## **V. Securities transfers, funds transfers and linkages between transfers**

*A. Please discuss whether and how settlement instructions are matched between participants prior to processing by the SSS.*

*1. Is matching required for all transactions without exception?*

All transactions concluded on the WSE and CTO are confirmed on the given market by the parties to the transaction. At the end of Day 'T' (transaction day), KDPW receives from the WSE and CTO lists of confirmed transactions, which it treats as a list of matched settlement instructions.

For transactions concluded outside the regulated markets, KDPW prepares a formal registration document on the basis of a document confirmed by both parties to the transaction, forming the basis for settlement.

KDPW will shortly implement matching that will be mandatory for all transactions from the unregulated market and settlements between a brokerage house and a custodian, for transactions concluded by that broker on behalf of that custodian or its client. The matching function will also be available for several free of payment securities transfers, in particular when they will relate to the accounts of various participants.

*2. What procedure is used when instructions do not match?*

Not applicable yet.

*3. Are matched settlement instructions binding on participants?*

Yes, matched settlement instructions are binding on participants.

*(a) If so, please describe the consequences of failure by participants to meet obligations (e.g. forced settlement, penalties, short positions).*

The failure of a participant to meet its obligations leads to the suspension of the settlement of a transaction, until the shortage of assets has been compensated. The participant who was responsible for the suspension of transaction settlement is required to pay a penalty fine, as determined by the KDPW Rules. In instances where a participant is responsible for the suspension of a guaranteed transaction (that is, stock exchange transactions, transactions on the secondary regulated off-exchange market (CTO) ) as a result of a shortage of funds on its cash account, the Settlement Guarantee Fund may be used to provide funds. Where a participant is responsible for the suspension of a transaction as a result of a shortage of securities on its depository account, an automatic securities loan may be used to meet its obligations.

*(b) Please describe whether this is a feature of the SSS's rules and procedures or of national law or regulations.*

These principles are governed by the KDPW Rules and the Detailed Rules of Operation.

*(c) Please provide a time line indicating the points at which matched instructions become binding, as well as any pre-matching process that takes place.*

We do not foresee the provision of pre-matching processes.

For stock exchange transactions, the moment the transaction data has been received from the stock exchange, i.e. around 17.00 on transaction day, KDPW treats these transactions as matched settlement instructions.

*B. Are securities transferred within the SSS registered?*

All securities admitted to public trading in Poland are registered at KDPW. Trading in these securities is fully dematerialised. Securities admitted to public trading do not exist in paper form - they exist only as an electronic record on a securities account.

Only bearer securities are traded on the regulated market. For registered securities, title may only pass by means of an agreement between the parties governed by civil law.

*1. Who is the registrar?*

According to the Polish Commercial Code, a securities issuer is required to keep a register of owners of registered securities. This duty may also be carried out using an agent.

Poland does not have a central securities register. Persons entitled to rights from securities are identified by name by a record on a securities account. Securities accounts are kept by authorised institutions such as brokerage houses, banks authorised to keep securities accounts by the Polish Securities and Exchanges Commission (custodians), and KDPW itself.

*2a. Is it normal practice to register the securities in the name of the SSS (or its nominee) or in the name of the beneficial owner?*

Securities are only registered in the name of their owner on securities accounts kept by authorised institutions (see Point 1 above).

However, in instances where the beneficial owner is a foreign client, it is possible to register that client's securities on the account of a foreign intermediary, kept at a local custodian.

*2b. Are there instances in which securities housed within the SSS are registered to neither the SSS (or its nominee) nor the beneficial owner?*

None.

*3. If the SSS offers custodial services, will it hold securities registered in the name of the beneficial owner?*

KDPW manages depository accounts kept for direct depository participants. The participant's securities and the participant's clients' securities are registered on separate accounts. Securities belonging to participants' clients' are registered on an omnibus account, which means it impossible to identify individual securities owners at the KDPW level.

KDPW manages securities accounts on which securities belonging to participants with the status of depositors are registered.

*4. Under what circumstances does the SSS initiate registration of securities in the buyer's name?*

KDPW never initiates registration of securities in the buyer's name.

*5. How long does the registration process typically take? Are participants notified when registration is complete?*

Not applicable to KDPW.

*6. Can securities be transferred within the SSS before registration in the buyer's name is complete? If so, do the rules and procedures of the SSS provide for an unwind or reversal of such transfers in case of bankruptcy or other events which result in the buyer's name not being entered on the register?*

Not applicable to KDPW.

*C. Please describe how securities transfers are processed within the SSS.*

*1. Please indicate whether the transfers are processed as debits and credits to members' accounts or via some other method.*

All securities transfers are processed as debits and credits on the appropriate participants' accounts. The depository system managed by KDPW constantly ensures that for each security, the number of securities issued (registered on the global issue account) is equal to the number of securities registered on the depository accounts kept by KDPW for its participants. Moreover, KDPW participants are required to ensure that the number of securities registered on the clients' accounts in their registration system is equal to the number of securities on the depository account in KDPW.

*2. On a continuous (real-time) basis, or in one or more batches?*

Securities transfers are currently processed in one daily batch.

*3. If continuous, during what hours does the processing occur? If in batches, at what time or times is the processing initiated and completed?*

See figure 2.

*4. Do securities settlements occur daily? Please identify securities for which settlement occurs only on specific days of the week or month.*

Securities settlements take place daily on settlement days (all business days with the exception of those days defined in KDPW Management Board resolutions).

*D. Please describe whether final funds transfers in conjunction with the SSS are made as debits and credits to balances held at the SSS, at one or more commercial banks, at the central bank, or via some other method.*

The system used to clear cash funds is owned and managed by the National Bank of Poland (the Polish Central Bank). Cash clearing takes place in the NBP's Payment System Department (PSD). KDPW defines the depository participants' clearing positions and informs participants of their amounts. Next, KDPW on the basis of an agreement with the NBP, as well as authorisation provided by participants, sends payment orders to the PSD, based on the calculated amounts.

*1. Does the SSS maintain cash accounts for its participants? Are these accounts equivalent to deposit accounts at a commercial or central bank or do they serve only as "cash memorandum" accounts?*

KDPW does not maintain cash accounts for its participants. Direct participants of the cash clearing system are banks holding accounts in the PSD and at the same time holding direct participant status in KDPW. A KDPW participant not holding its own cash account at the PSD (for instance, a brokerage house), needs to indicate (after having concluded the appropriate agreement with a bank) an account in a bank within the PSD through which cash clearing arising from its participation in the depository-settlement system will be carried out. In such cases, the bank performs the role of payment bank.

*2. On what entity (SSS or other) does the participant bear cash deposit risk?*

The payment bank.

*3. Under what circumstances does the SSS provide credit extensions or advances of funds to its participants and thereby expose itself to credit risk?*

There are no circumstances in which KDPW provides credit extensions or advances to its participants.

*4. How long can such credit extensions last? How long do they typically last?*

Not applicable.

*E. Is the SSS a DVP system? If so, please describe the DVP model used according to the models outlined in the DVP Report (see the Introduction). Please also provide a diagram*



*indicating the timing of events in the processing of securities and funds transfers in the SSS. Where the SSS provides more than one alternative for settlement processing, please provide a response for each alternative and indicate the relative importance of each alternative.*

The settlement process is described in Figure 3.

The KDPW settlement system works on the principle of DVP according to Model 2 (BIS Report, 1992) - Securities are settled in gross, while the cash funds are netted.

The exception is the settlement of Treasury bond auctions in the primary market, where settlement is carried out according to Model 1: securities and cash are settled in gross.

*1. Are funds transfers and securities transfers processed within the same system or in different systems? If different, how are they linked?*

Funds transfers and securities transfers are processed in different systems (in KDPW and the NBP).

*(a) Please describe whether each securities transfer is linked to a specific funds transfer on a trade-by-trade basis or on a net basis or via some other method.*

Each securities transfer involving transactions concluded on the secondary market is linked to a specific cash funds transfer on a net basis; only securities transfers involving Treasury bond auctions on the primary market are linked with specific cash transfers on a gross basis.

*(b) Does the SSS "split" large transactions into multiple transactions or require participants to do so?*

KDPW does not split large transactions into multiple transactions and does not require participants to do so.

*2. When do securities transfers and funds transfers become final?*

*(a) At what time do securities transfers become final? After what event or events?*

Securities transfers that are the result of transaction settlement become final the moment they are registered on the accounts kept in the KDPW system, which takes place once confirmation has been received from the NBP about the execution of the cash payment orders.

*(b) At what time do funds transfers become final? After what event or events? Does this timing allow for same-day retransfer of funds received in exchange for securities?*

Cash fund transfers become final the moment they are executed in the NBP (about 1 p.m.). The timing allows for same-day retransfer of funds received in exchange for securities.

*(c) If final delivery of securities precedes the final transfer of funds, can participants dispose freely of such securities prior to funds finality? If so, what actions will be taken if funds are not received?*

Settlement is carried out on the basis of DVP.

*(d) If final delivery of funds precedes the final transfer of securities, can participants dispose freely of such funds prior to securities finality? If so, what actions will be taken if securities are not received?*

Settlement is carried out on the basis of DVP.

*(e) Does the timing of finality differ depending on the type of security transferred or the currency in which payment is to be made? Please describe.*

The timing of finality of settlement does not depend on the type of security transferred. All payments are carried out in Polish Zlotys only.

*3. Please discuss whether participants are notified of securities or funds transfers while they are still provisional, only when they are final, or both.*

Participants are informed of securities transfers when they are registered (which means they are final). The KDPW system does not carry out provisional transfers.

*F. Does the SSS itself "guarantee" funds or securities transfers?*

KDPW itself does not guarantee securities or cash transfers. KDPW manages a Settlement Guarantee Fund, whose assets may be used in instances defined in the Settlement Guarantee Fund Rules, when there is a shortage of funds on the participant's account for transactions covered by the settlement guarantee system. Moreover, KDPW manages a securities lending and borrowing system for settlement purposes.

*1. Under what circumstances and at what point are transfers guaranteed by the SSS?*

See point 7 or see above.

*2. What actions does the guarantee obligate the SSS to take?*

See point 7 or see above.

*3. Please indicate whether the guarantee is a feature of the SSS's rules and procedures or of national law or regulations.*

See point 7 or see above.

## **VI. Default procedures**

*A. Please discuss the events or circumstances that would constitute default of a participant under the rules and procedures of the SSS or that would lead the SSS to make use of exceptional settlement arrangements or unwind procedures.*

*1. Failure by a participant to meet a test of its solvency under the applicable laws of its jurisdiction?*

KDPW does not verify the solvency of participants. The financial standing of participants is examined by authorised supervisory bodies (the Polish SEC, Banking Supervisors). On the

basis of decisions of these bodies, special procedures may then be initiated as regards the participant.

*2. Failure to make payments or deliveries of securities within the time specified?*

The failure to deliver securities within the time specified leads to the suspension of transaction settlement. The participant is obliged to provide securities necessary for settlement without delay. For settlements covered by the settlement guarantee system, if the KDPW participant is unable to deliver the necessary assets (is unable to manage its responsibilities resulting from its participation in the settlement system) the KDPW Management Board may decide to suspend its KDPW participation status, while itself initiating special procedures for the buy-in of the missing securities.

The failure to make payment within the time specified for transfers covered by the settlement guarantee system leads to special procedures being implemented to release the assets of the Settlement Guarantee Fund.

*3. To the extent that the rules and procedures grant discretion in the determination of the use of default or other exceptional procedures, please discuss where the authority to exercise such discretion resides and the circumstances in which this authority would be used.*

The KDPW Rules define in detail the procedures in such circumstances. Depending on the risk that may be caused by exceptional circumstances, the KDPW Management Board reserves the right to suspend KDPW participation status. In such circumstances, KDPW informs without delay the WSE and the CTO market, and these are in turn obliged to limit or suspend that participant's operations on the regulated market. If the participant's situation does not improve, further decisions are taken with the Securities and Exchanges Commission.

*B. What procedures are followed by the SSS once it has determined that a default event has occurred or that exceptional settlement arrangements are to be employed?*

*1. How and at what point are participants notified that this has occurred?*

Participants who are parties to a transaction are informed about the default immediately it has happened (either by means of a report or a telephone call).

*2. Would the SSS be expected to continue to meet all its obligations to participants under these circumstances? Please discuss the resources in place to ensure that this would occur (e.g. collateral, participants' fund, insurance, loss-sharing arrangements, etc.).*

KDPW manages the Settlement Guarantee Fund, which guarantees obligations arising from transactions concluded on the WSE and CTO market (with the exception of transactions concluded outside the sessions, transactions introducing securities to trading in the form of a public sale on the WSE, and transactions concluded outside the regular trading session at the CTO). The Settlement Guarantee Fund operates in such a way as to meet the obligations of a given participant for four consecutive settlement days.

Moreover, transactions concluded on the derivatives market are guaranteed by initial and maintenance margins. For warrants, whose exercise requires collateralisation, issuers are required to maintain the appropriate level of margin deposits to guarantee the exercise of the warrants. Margins on the derivatives market and the exercise of warrants may be deposited in cash, securities accepted by KDPW or bank guarantees.

*3. Please describe and provide a time line indicating the order in which these resources would be used as well as the timing of participant notifications and important deadlines (e.g. when the SSS's obligations to participants would be met, when participants would need to cover their loss-sharing obligations).*

On transaction settlement day, until 12.00, the participant should have available on its cash account in payment bank the amount necessary to settle the transaction, and the necessary securities on its depository account.

In the event of a shortage of securities on the participant's account, or difficulties arising as a result of a lack of cash funds to settle the transaction, procedures defined in the KDPW Rules and the Detailed Rules of Operation are then initiated.

If the shortage of cash funds to settle the transaction is not the fault of the participant, the shortage is covered by funds from the Settlement Guarantee Fund and takes the form of a loan. If the participant is to blame, the shortage is covered (in order) first from the current credits due to the participant, next from the participant's contribution to the Settlement Guarantee Fund; if these funds are insufficient, the contributions of the remaining participants of the Fund are then used.

In the event of a shortage of securities on a participant's account, a securities loan is initiated, if this is possible; if not, the settlement of the transaction is suspended. If the participant does not act in any way to allow the settlement of the transaction, KDPW may carry out a securities purchase order on the participant's account, using the cash funds from the Settlement Guarantee Fund.

If a participant operating on the derivatives market is unable to meet its obligations, KDPW closes all open positions, using the maintenance margin, followed by the initial margin. If these funds are insufficient, the appropriate part of the Settlement Guarantee Fund is then used. Margin deposits collateralising the exercise of warrants are used when the issuer of the warrants does not hold the appropriate amount on the account indicated by KDPW by 11.30 to meet obligations on the day of the redemption.

When the participant's liabilities exceed the amount of its contributions to the Settlement Guarantee Fund, the remaining participants are obliged to make up the remaining balance in that part of the Fund.

*4. Please describe all conditions under which provisional transfers of securities or funds could be unwound by the SSS.*

Transfers of securities and cash cannot be unwound in the KDPW system once they have been realised.

Transactions covered by the guarantee system may not be revoked.

Outside the regulated market a transaction may be revoked (cancelled) if the parties to that transaction mutually agreed this possibility. KDPW does not guarantee the settlement of such transactions. Any possible liabilities arising from the cancellation of these transactions are agreed between the parties.

*(a) How and on what authority would a decision to unwind securities or funds transfers be made by the SSS?*

Not applicable to KDPW.

*(b) When and how would participants be notified of a decision to unwind provisional securities or funds transfers?*

Not applicable to KDPW.

*(c) How long would participants have to cover any debit positions in their own securities or funds accounts resulting from an unwind?*

Not applicable to KDPW.

*(d) In the event of an unwind, would all transfers be unwound or would only a subset of transfers (e.g. only securities purchases or only those of a subset of participants) be unwound?*

Not applicable to KDPW.

*(e) If only a subset of transfers, what procedure would be followed to determine which transfers and in what order?*

Not applicable to KDPW.

*5. Can bankruptcy or insolvency be declared retrospectively in the SSS's jurisdiction (e.g. under a "zero-hour" rule), and could this cause provisional securities or funds transfers to be unwound?*

According to Article 138 of the Polish Law on the Public Trading in Securities, liabilities determined according to net calculations are binding from the moment the transaction has been concluded, that is, even before the amount has been defined by the clearing institution. The purpose of this provision is to guarantee the protection of the net amounts in instances where bankruptcy proceedings were initiated between the conclusion of the transaction and the determination of the debit and credit amounts, or the settlement of the transaction.

Article 139 of the aforementioned Law states that where bankruptcy or liquidation proceedings have been initiated, these cannot affect the payment which the participant is obliged to make as a consequence of the settlement of a transaction.

It should however be noted that there exists a body of legal opinion which states that the "zero hour rule" applies in Polish law, although the existence of a scenario in the public market where a participant, on the day of its declared bankruptcy, is still able to conclude transactions covered by the settlement guarantee system is wholly theoretical.

*6. Please describe any circumstances in which transfers of securities or funds that were defined as final in response to question V.E.2 above would ever be unwound.*

Not applicable.

*C. Has a participant in the SSS ever been declared in default or become insolvent?*

There have been no incidents of a participant becoming insolvent. Before changes in the rules in January 1999, there were instances of credit being given for the purpose of settlement of a transaction by a commercial bank, which was at the same time acting as the clearing bank for KDPW. These credits were repaid by participants within the set time-limit with interest. Once

new rules were introduced, there have been no cases yet of having to use the assets of the Settlement Guarantee Fund.

*1. Have loss-sharing procedures been invoked?*

The need has never arisen.

*2. Please describe whether any of these defaults or insolvencies resulted in losses for the SSS or its participants and how they were absorbed.*

This has never occurred.

## **VII. Securities overdrafts, securities lending and back-to-back transactions**

*A. Is it possible for debit positions (overdrafts) in securities accounts at the SSS to arise?*

*1. Under what conditions could such debit positions occur?*

*(a) Do these conditions always result in debit positions in securities accounts rather than failed transactions? If not, please explain the basis for differential treatment by the SSS.*

Debit positions, or overdrafts, are not permitted on security accounts.

Shortages of securities necessary for the settlement of transactions are possible, however - these result in the settlement of the transaction being suspended. The most common reason for a shortage of securities necessary for the settlement of a transaction are as follows:

- A participant's error in the settlement instruction,
- The conclusion of a transaction without a client order,
- "A chain of suspensions", where the suspension of settlement of a sale transaction is caused by the suspension of settlement of a purchase transaction.

The settlement of a suspended transaction takes place when the appropriate assets are deposited on the account of the participant responsible for the suspension. The participant is obliged to provide the securities necessary for settlement without delay. If the participant does not carry out this obligation, KDPW takes over the responsibilities from the participant and attempts on its behalf and its account to eliminate the suspension.

The exception to this are transactions concluded outside the regulated market, which may be cancelled at the request of both parties.

*(b) Are these situations covered explicitly by the rules and procedures of the SSS?*

The settlement and suspension of settlement of transactions are clearly defined in the KDPW regulations: The KDPW Rules, the Detailed Rules of Operation and the KDPW Registration Procedures.

*2. How long can such debit positions last? How long do they typically last?*

Not applicable to KDPW.

*3. How are debit positions in securities accounts prevented, rectified or managed?*

Not applicable to KDPW.

*4. What procedures would be followed by the SSS in case the debit cannot be rectified? (e.g. failure by a participant with a debit balance in a securities account or unavailability of the securities in the market)*

*(a) Application of loss-sharing provisions allocating the loss to participants?*

*(b) Absorption of the loss by the SSS?*

*(c) Other? Please specify.*

Not applicable to KDPW.

*B. Under what circumstances does the SSS provide for the lending of securities to ensure settlements?*

*1. Is the process for lending securities automatic? If not, please describe the procedures used by the SSS to determine whether a securities loan will be made.*

In order to ensure the liquidity of transaction settlement, KDPW organises and manages a securities lending and borrowing system for securities that form part of transactions concluded on the regulated market.

The KDPW system provides for two types of securities loans:

- Automatic securities loans, executed on or after the settlement day, whose purpose is the prevention or the elimination of the suspension of transaction settlement,
- On request securities loans whose purpose is to ensure the liquidity of transaction settlement, executed before the settlement day.

Currently, only automatic securities loans are executed at KDPW.

*2. At what point are participants notified that securities are being lent to them in order to complete their settlements?*

For automatic securities loans, participants are notified that securities are being lent to them in order to complete their settlement, on settlement day at around 13.00-14.00.

*3. Which securities on deposit at the SSS are eligible for lending? Do participants have the option to make securities available for lending or is it mandatory?*

KDPW indicates those securities, which may form the basis of a securities lending agreement. Securities loans are not made on the record day of those securities, or made involving securities, which would need to be returned after the record day.

Participation in the automatic securities lending and borrowing program is mandatory only for participants acting as borrowers. Participants who wish to act as securities lenders may only do so after granting KDPW their authorisation.

*4. Are lent securities identified by the SSS with specific participants as lenders or only with a common pool of securities available for lending? Does the participant whose securities are lent become a principal to the transaction?*

Securities intended to be loaned are registered on special participants' accounts (set aside for automatic securities loans). In the event of a shortage of necessary securities on these

accounts, KDPW informs all participants of the securities lending system of demand for particular securities. A participant ready to provide a securities loan in answer to the request from KDPW informs of the ID and amount of securities, which are being, set aside to be loaned, and the account on which they are registered.

The securities lender does not become a principal to the transaction. The parties to a securities loan remain anonymous.

*C. How does the SSS settle back-to-back transactions?*

KDPW does not settle back-to-back transactions.

*1. Under what conditions are delivery instructions by participants receiving and redelivering securities on the same day under back-to-back transactions settled for same-day value?*

Not applicable to KDPW.

*(a) Only if the participant has securities on deposit with the SSS that have been received pursuant to a final securities transfer?*

*(b) If the participant has securities on deposit with the SSS that have been received pursuant to a provisional securities transfer?*

*(c) Before securities have been received either provisionally or finally, but when a matched receipt instruction exists for the same or greater value? Is such a practice limited to markets where matching is binding?*

*(d) Before securities have been received either provisionally or finally, but when a third party has promised to deliver to the SSS securities of the same or greater value? Must the provider of the guarantee have itself received the securities through a final transfer? Please describe how the SSS evaluates such promises, and whether they are addressed by the written rules and procedures of the SSS.*

*(e) Other? Please specify.*

Not applicable to KDPW.

*2. Please describe limits or controls in place with respect to any of the above arrangements for the settlement of back-to-back transactions, including limits on amounts involved or related to the liquidity of the underlying securities.*

Not applicable to KDPW.

*3. Under what conditions are payment instructions by participants in the SSS under back-to-back transactions settled for same-day value? Can participants use the proceeds of an on-delivery of securities without the need for an extension of credit?*

Not applicable to KDPW.

## **VIII. Risk control measures**

*A. Please describe the roles and responsibilities of those areas of the SSS responsible for risk management and control.*



*1. Please describe the process for the internal review of risk management policies and procedures.*

The internal review of existing risk management policies and procedures is a constant process. This means that projects are currently being carried out to improve the effectiveness of existing risk management systems, and constant monitoring of solutions implemented in other countries, along with an assessment of whether such solutions could be implemented at KDPW.

*2. Is there a risk management policy that addresses the review and approval of new products and services offered by the SSS? At what level of the organisation is risk management approval given for a new product or service?*

There exists a policy of approval of risk management principles related to new products by the KDPW Management Board. The sections responsible for risk management recommends to the Management Board models and solutions for the risk inherent in new products.

*3. Does the SSS have a risk management function with clear independence from and authority over operational or marketing functions?*

Yes, it has. Departments responsible for risk management on the cash and derivatives market have their risk management functions clearly separated from operational or marketing functions.

*4. Does the Board of Directors review risk management policies and procedures? Does the Board have a risk management or audit committee?*

Acceptance of risk management policy, as well as all modification procedures and the introduction of new products and services takes place at the level of the Management Board. KDPW does not have a formal risk management or audit committee.

*B. Please describe any internal or external audits or supervisory/regulatory examinations that are performed with respect to the SSS. For each such audit or examination, please address the following questions.*

*1. Who performs the audit or examination?*

Internal examinations are carried out by the Internal Audit Department on the basis of half-yearly examination plans approved by the KDPW President and CEO. Examination plans are drawn up on the basis of recommendations of the KDPW Management Board and propositions from heads of departments.

*2. What is the scope of the audit or examination?*

*(a) Please indicate whether and how it addresses the sufficiency of and compliance with internal controls.*

*(b) Please indicate whether and how it addresses the SSS's compliance with its own rules and procedures.*

Examinations are carried out by the external auditors to verify KDPW financial statements (in order to assess whether correct accounting procedures are used, whether registration is

properly carried out and the assets and finances of the company are correctly presented). Internal examinations are carried out on the basis of a half-yearly examination plan. The results and recommendations of the internal audit are discussed with the heads of the particular department subject to the examination. A report is signed by the head of the department subject to the examination, as well as the person carrying out the examination and the Head of the Internal Audit Department, and is then presented and discussed with the President and CEO of KDPW. Subsequent examinations verify whether earlier recommendations have been implemented.

The internal audit assesses:

- The effectiveness of KDPW operations,
- The level of efficiency of procedures taking place in KDPW,
- Whether KDPW is operating according to internal and external rules and regulations.

In instances where, in the opinion of the Internal Audit Department, there are procedures, which are not fully efficient, the Department presents the KDPW President and CEO with proposals for raising efficiency.

The Internal Audit Department examines whether internal procedures are correct and up to date and presents potential changes to the KDPW Management Board. All procedures carried out within KDPW are subject to examination. New procedures are examined in the early stages of their realisation.

### *3. What is the frequency of the audit or examination?*

According to regulations, external audits are carried out annually. Exceptions include situations where correctness needs to be defined in a narrower scope, where audits may take place several times a year.

The frequency of internal examinations of operating procedures is dependent on the assessment of the risk of the failure to carry out, or the improper carrying out of a given procedure or action. Examinations are carried out on the basis of half-yearly plans, although on-the-spot examinations are possible where procedures or actions have been found to be incorrect or are suspected of being so. Half-yearly examination plans are prepared based on:

- Recommendations from the Management Board and directors of individual departments,
- Proposals put forward by heads of department,
- Results of examinations carried out previously,
- Risk analysis.

### *4. Are audit or examination reports available for review by participants?*

External audit reports are available to KDPW participants (a report is included in the Annual KDPW report).

Internal audit reports are given to the KDPW President and CEO. Annual reports on Internal Audit Department operations are presented to the KDPW Management Board.

*C. Please discuss whether the SSS has the capacity to value (i.e. mark to market) the securities that it holds.*

#### *1. Please describe how these valuations are used by risk control systems at the SSS.*

KDPW has an integrated valuation system for securities used as collateral

*2. How frequently are securities revalued?*

Securities are revalued once a day.

*3. What are the sources for security valuations?*

*(a) What outside price or data sources are used?*

The principle source for valuation are securities prices, received from the regulated markets and documents from the money and foreign exchange markets.

*(b) If pricing models are used, please describe how the models are chosen and how the model inputs are obtained.*

Currently, pricing is only used for Treasury bonds, which may be used as collateral. A 'haircut' of 10% of the market value is calculated.

*D. Please discuss whether the SSS has a lien on the securities held in or transferred through it.*

No, it doesn't.

*1. Does the lien apply only to the securities owned by the participants themselves or does it extend to the securities beneficially owned by customers of participants?*

Not applicable.

*2. Under what circumstances and in what manner would such a lien allow the SSS to use the securities?*

Not applicable.

*E. Please discuss the circumstances in which the SSS requires collateral to limit or mitigate risks.*

*1. Does the SSS manage its own collateral system?*

KDPW manages its own collateral system, which is used for securing securities loans and for the safeguard system for the derivatives market.

*2. Does the SSS share a collateral system with another SSS or payment system?*

At present, a KDPW project is being discussed with the National Bank of Poland, whose purpose is to offer KDPW participants the ability to offer Treasury bills as collateral, which are kept on deposit by the NBP Central Treasury Bill Register.

*3. Can collateral at the SSS be posted and returned on the same day?*

If collateral is posted in the form of securities, the collateral is recognised on the day of posting.

If collateral is returned, the transaction limit (or purchase power) of the participant is verified. If the value of the transaction limit is positive, i.e. the participant's remaining assets are greater than the participant's real and potential liabilities, securities may be released on the same day. If the opposite is the case, the participant must post substitute collateral, after which the collateral may be released.

*4. What types of transaction at the SSS involve the use of collateral?*

On the cash market, automatic securities loans used for settlement purposes require collateral. On the derivatives market, transaction limits (the so-called 'purchase power') of clearing members form an integral part of the safeguard system. Assets which may form part of the vadium, which defines the size of the limit, include, apart from cash, Treasury securities and bank guarantees. Apart from a vadium, KDPW accepts margins for derivatives in the form of Treasury bonds (the non-cash part may form up to 60% of the value of margin).

*5. What are the policies with regard to the type of collateral used or haircuts required?*

Currently, the only securities that may be accepted as collateral are Treasury bonds. The amount of the haircut for Treasury bonds is defined in the KDPW Rules and is equal to 10%. The value of the collateral is marked to market daily on the basis of the market price of the bonds.

*6. How are collateral valuation methodologies developed and reviewed?*

The valuation methodology of securities forming collateral is developed using documents published by the Bank for International Settlement, Risk Metrics Group and other sources dealing with market risk and liquidity risk.

*7. To what extent are collateral policies described in the written rules and procedures of the SSS?*

The KDPW Rules, sent to KDPW participants, contain a list of those securities, which may be used as collateral, and the level of haircuts.

*F. Please describe the SSS's use of limits on exposures to monitor or control risks.*

*1. Please explain the types of limit used and the exposures to which they apply.*

KDPW has introduced transaction and engagement (or concentration) limits. The transaction limit allows participants to open new derivatives positions. Its chief purpose is to prevent overnight risk in KDPW for new positions, which will be collateralised by clearing members with a margin before the next session.

The engagement limit calculates the level of concentration on the derivatives market, according to individual accounts administered by individual clearing members. Its purpose is to prevent excessive concentration of derivatives in investors' individual portfolios.

*2. Do the limits apply to all participants and/or to other SSSs with which the SSS is linked? What are the exceptions to the limits?*

Transaction limits apply uniformly to all clearing members on the derivatives market. The engagement limit is not currently implemented owing to the infancy of the derivatives market in Poland.

*3. Do limits apply to participants individually or in the aggregate or both?*

Transaction limits are applied individually for each clearing member. The engagement limit was created to be used as a flexible method of assessing concentration at the following levels:

- Individual investor level,
- The level for a group of pre-defined investors,
- Clearing member level.

*4. Do limits apply to implicit as well as explicit extensions of credit or securities (e.g. when on-deliveries of securities are permitted pursuant to provisional but not final delivery of securities)?*

Securities used as collateral in transaction limits are dedicated by the clearing member. Bank guarantees are subject to initial approval by the KDPW Management Board if they are to be used as collateral.

*5. Does the SSS automatically reject transactions that exceed limits or is compliance determined ex post?*

The application that monitors the transaction limit sends a message to the administrator, once a clearing member has exceeded 90% of the level of the individual transaction limit. On receipt of this message, the clearing member is informed of the need to raise assets posted as collateral for the transaction limit. In instances where the participant does not transfer the assets for the vadium (which determines the amount of the transaction limit) onto the appropriate account in KDPW, once the transaction limit has been fully exceeded (100%) level, the clearing member may be suspended from making any further orders.

*6. How are limit policies developed and reviewed?*

Limit policies are under constant review as a result of the emergence of new instruments and services, as well as recommendations of international institutions on credit risk management.

*7. To what extent are limit policies described in the written rules and procedures of the SSS? Where does additional authority to set or amend limit policies reside?*

Limit policy is defined in the KDPW Rules and in the terms and conditions of the issue and trading of derivatives. Additional authority to set internal limits is held by intermediary institutions, such as brokerage houses.

*G. Please describe other controls to mitigate or reduce risks at the SSS.*

*1. Does the SSS or its participants have the capacity to monitor participants' accounts continuously during processing?*

No. Participants receive information on the balances in their accounts once a day. This is as a result of a one batch processing cycle.

*2. Is there a special risk control regime that the SSS would apply to a participant known to be experiencing financial difficulties?*

KDPW is finalising a project analysing the credit risk of clearing members in the derivatives market, whose purpose is the diversification of participants' risk by means of internal rating.

*3. Does the SSS maintain or administer loss-sharing arrangements other than those applicable to events of default and addressed in Section VI above? Are these loss-sharing pools pre-funded by participants?*

No.

## **IX. Operational risks**

*A. Please provide assessments of the operational reliability of the computer and other systems used by the SSS, including any criteria that the SSS uses internally for this purpose.*

*1. What is the percentage uptime of the systems used by the SSS?*

*(a) Whole system overall?*

100% for the last 3 years.

*(b) Broken down by major components? (e.g. communications network, central processing facility)*

KDPW's Wide Area Network availability remains at 99.9% (the figures may be different for individual participants).

Other components: 100%.

*(c) During critical processing periods?*

See above.

*2. Has the SSS experienced major operational problems during the past two years?*

No

*(a) Have settlements been delayed, been disrupted or otherwise failed because of operational problems during this period?*

No

*(b) Please describe the nature of any such problems.*

Not applicable to KDPW.

*B. Please describe contingency or disaster recovery planning at the SSS.*

The KDPW contingency strategy is based on the use of a disaster recovery site where all elements of the KDPW system are duplicated. In an emergency, depending on conditions, the back-up systems can be activated and/or KDPW employees transfer to the disaster recovery site.

The main databases are transferred to the back-up system after each phase of processing and additionally all data is replicated on the back-up system on a daily basis.

*1. Does the SSS have a formal plan for business continuity in place?*

Yes, it does. It is called the KDPW Operation Continuity Maintenance System.

*2. Is this plan available for review by participants?*

No, it is not. The principle behind the activation of the disaster recovery system is that from the point of view of the participant, the only visible change is the change of KDPW telephone number and address; participants do not therefore need to review the plan.

*3. How often is this plan tested? Does this involve participants in the SSS?*

Normally, tests take place at least three times a year. They consist of the activation of the disaster recovery site and verification of data and launch of all applications. The participants take part in the test.

*4. What are the major elements of the business continuity plan?*

All information that can be made available is given above.

*5. How long would it take the SSS to resume operations if primary systems become unusable?*

Depending on the type of emergency and the time it occurred, the disaster recovery site is expected to be activated within 3 to 6 hours.

*C. What are the key features of the internal controls covering operations and security at the SSS (e.g. change controls or those covering remote access)?*

*1. Please describe controls or security procedures in place to ensure that the SSS acts only on authentic settlement instructions from valid participants.*

Data exchange between KDPW and participants takes place using the Electronic System for the Distribution of Information, which uses cryptography and electronic signatures. The cipher keys are provided by KDPW. Each participant's workstation and the employee are authenticated in the server by means of user ID and a password. Communications are protected both by KDPW (using file filtering and firewalls) and telecom service providers. For direct interfacing with KDPW computers, the standard security procedures are used: user profiles and passwords and, where required, encoded links.

*2. Are internal operational and security controls included in the internal and/or external audits of the SSS?*

Yes, they are.

*3. Are internal operational and security controls covered by regulatory requirements applicable to the SSS?*

All internal security controls included in regulatory requirements applicable to the SSS has been employed in KDPW.

*D. Does the SSS impose minimum operational or performance standards on third parties (e.g. communications providers)?*

All co-operation with third parties is based on agreements for each product provided.

*1. How does the SSS ensure that such standards are met on a continuing basis and what sanctions are available to the SSS if they are not?*

KDPW constantly monitors all components dependent on third parties (e.g. the efficiency of telecommunication links). Moreover, wherever possible, all equipment is periodically verified.

*2. How would the SSS allocate losses incurred due to operational problems caused by third parties?*

From financial penalties based on agreements with the third parties and from KDPW's own funds.



Figure 1. The organizational structure of the KDPW

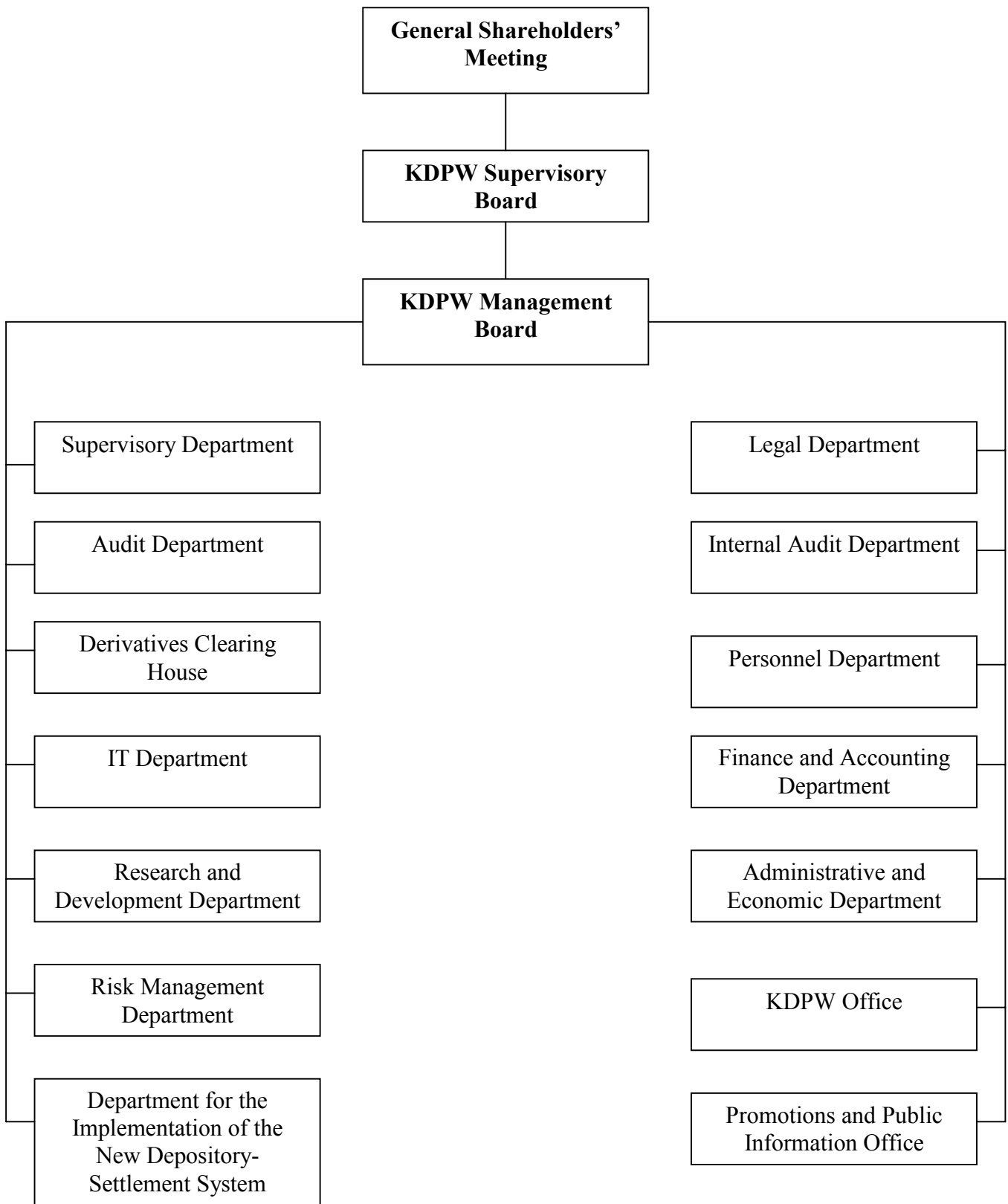


Figure 2. The KDPW accounting day

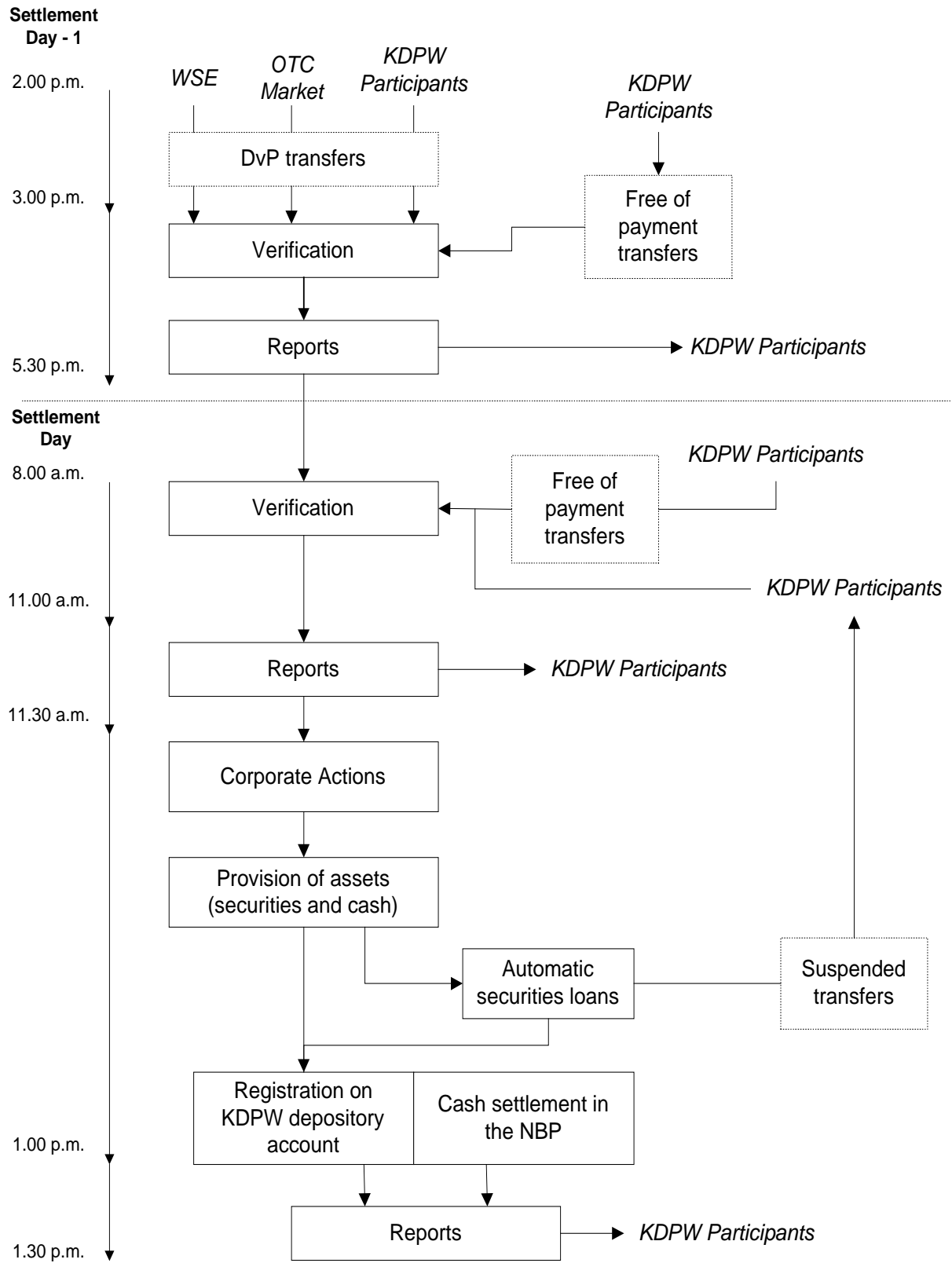


Figure 3. The KDPW settlement cycle

