ARTICLE 38(6) CSDR AND ARTICLE 73 FMIA PARTICIPANT DISCLOSURE

1. Introduction

The purpose of this document is to disclose the levels of protection associated with the different levels of segregation that we provide in respect of securities that we hold directly for clients with Central Securities Depositories within the EEA and Switzerland (CSDs), including a description of the main legal implications of the respective levels of segregation offered and information on the insolvency law applicable. This disclosure is required under Article 38(6) of the Central Securities Depositories Regulation (CSDR) (in relation to CSDs in the EEA) and Article 73 of the Swiss Financial Markets Infrastructure Act (FMIA) (in relation to CSDs in Switzerland).

Under CSDR, the CSDs of which we are a direct participant (see Glossary) have their own disclosure obligations and may make their own disclosures from time to time.

This document is not intended to constitute legal or other advice and should not be relied upon as such. Clients should seek their own legal advice if they require any guidance on the matters discussed in this document.

2. Background

In our own books and records, we record each client’s individual entitlement to securities that we hold for that client in a separate client account. We also open accounts with CSDs in our own (or in our nominee’s) name in which we hold clients’ securities. We currently make two types of accounts with CSDs available to clients: Individual Client Segregated Accounts (ISAs) and Omnibus Client Segregated Accounts (OSAs).

An ISA is used to hold the securities of a single client and therefore the client’s securities are held separately from the securities of other clients and our own proprietary securities.

An OSA is used to hold the securities of a number of clients on a collective basis. However, we do not hold our own proprietary securities in OSAs.

3. Main legal implications of levels of segregation

(a) Insolvency

Clients’ legal entitlement to the securities that we hold for them directly with CSDs would not be affected by our insolvency, whether those securities were held in ISAs or OSAs, except in the limited circumstances described below.

The distribution of the securities in practice upon insolvency would depend on a number of factors, the most relevant of which are discussed below.

Application of U.S. insolvency law (in relation to both head office and London branch)

We are a New York state-chartered bank and a member of the Federal Reserve System. We are subject to regulation, supervision and examination by the Federal Reserve, the U.S Federal Deposit Insurance Corporation (the FDIC) and the New York State Department of Financial Services. As a depository institution whose deposits are insured by the FDIC, our insolvency would be administered by the FDIC as conservator.
or receiver in proceedings under the Federal Deposit Insurance Act (FDIA) or pursuant to the Dodd-Frank Orderly Liquidation Authority (see Glossary). In an FDIA proceeding, the FDIC acts as the receiver for the failed bank. It succeeds to the assets of the entity and either transfers those assets to a bridge bank which it creates, sells the assets to another banking entity or liquidates and distributes the assets to creditors. As receiver, the FDIC succeeds to only the assets that the failed bank owns and not to securities which it holds as custodian. In a proceeding under the Dodd-Frank Orderly Liquidation Authority, the FDIC would liquidate our assets and distribute them to clients and creditors with limited court oversight.

Under the FDIA and applicable commercial law, securities that we hold on behalf of clients would not form part of our insolvency estate for distribution to creditors, provided that such securities have remained the property of the clients.

Rather, securities that we hold on behalf of clients would be deliverable to clients in accordance with each client’s proprietary interests in the securities.

Under the Dodd-Frank Orderly Liquidation Authority, clients that are “customers” are entitled to file customer claims for securities that we hold on their behalf. Securities that we hold in Segregated Accounts for customers (including securities held at a CSD located in Europe) are distributed to customers in satisfaction of their customer claims. Securities held for customers can also be sold by the trustee or receiver to generate cash for distribution to customers. Property held in Segregated Accounts is not available for distribution to general creditors unless all customer claims have been satisfied. (If a Segregated Account is subject to a lien that is permitted under the Customer Protection Rule, such as the lien that a CSD located in Europe is permitted to impose for custodial and administrative fees arising in connection with Segregated Accounts, then the secured creditor is permitted to satisfy such lien before turning the remaining assets over to the trustee or liquidator for distribution to customers).

Clients’ claims to the securities that we hold on their behalf may be satisfied pro rata from the pool of available cash and securities held in Segregated Accounts regardless of whether such property is held in an OSA or an ISA. Accordingly, where we hold securities in custody for clients in Europe and those securities are considered the property of those clients rather than our own property, they should be protected following our insolvency or any subsequent resolution. This applies whether the securities are held in an OSA or an ISA.

Securities that we held on behalf of clients would also not be subject to any bail-in process (see Glossary), even though a bail-in process would apply to our parent company if we were to become insolvent.

**Application of English insolvency law (only in relation to London branch)**

Were we to become insolvent, insolvency proceedings relating to our London branch may also take place in England and be governed by English insolvency law.

Under English insolvency law, securities that we held on behalf of clients would not form part of our estate on insolvency for distribution to creditors, provided that they remained the property of the clients. Rather, they would be deliverable to clients in accordance with each client’s proprietary interests in the securities.

As a result, it would not be necessary for clients to make a claim in our insolvency as a general unsecured creditor in respect of those securities. Securities that we held on behalf of clients would also not be subject to any bail-in process (see Glossary), which may be applied to us if we were to become subject to resolution proceedings (see Glossary).

Accordingly, where we hold securities in custody for clients and those securities are considered the property of those clients rather than our own property, they should be protected on our insolvency or resolution. This applies whether the securities are held in an OSA or an ISA.

**Nature of clients’ interests**

Head office: Under the UCC (see Glossary), when we hold securities for customers with CSDs, we hold interests in those securities in accounts that we establish for the benefit of our customers. In this capacity, we are acting as a "securities intermediary" under the UCC. Those customers are referred to as "entitlement holders", and the rights they hold in the financial assets in a securities account are "security entitlements". Although the UCC describes the property interest of customers in the assets held by a securities intermediary (set out in further detail below), it does not necessarily determine how property held by a failed securities intermediary will be distributed in insolvency proceedings. If the securities intermediary fails and its

---

2 When a client has sold, transferred or otherwise disposed of its legal entitlement to securities that we hold for the client (for example, under a right to use or title transfer collateral arrangement), the securities will no longer be the property of the client.
affairs are being administered in an insolvency proceeding, the applicable insolvency law (as described above) governs how the various parties having claims against the securities intermediary (which are in turn established in accordance with applicable non-insolvency law, i.e. the UCC) are treated.

The UCC provides that a customer’s property interest with respect to a particular financial asset held through a securities intermediary is a pro rata property interest in all interests in that financial asset held by the securities intermediary. To the extent necessary for a securities intermediary to satisfy all security entitlements with respect to a particular financial asset, all interests in that financial asset held by the securities intermediary are: (a) held by the securities intermediary for its customers; (b) not the property of the securities intermediary; and (c) not subject to claims of creditors of the securities intermediary (except under limited circumstances). A securities intermediary is obligated under the UCC to promptly obtain and thereafter maintain a financial asset in a quantity corresponding to the aggregate of all security entitlements it has established in favor of its customers with respect to that financial asset. The securities intermediary is permitted to maintain those financial assets directly or through one or more other securities intermediaries (such as a CSD). In addition, except to the extent otherwise agreed by its customers, a securities intermediary may not grant any security interests in a financial asset it is obligated to maintain as described above.

London branch: Where we hold clients’ securities in our London branch, the nature of clients’ interest in those securities may be governed by English law. Under English law, although our clients’ securities are registered in our name at the relevant CSD, we hold them on behalf of our clients, who are considered to have a beneficial proprietary interest in those securities. This is in addition to any contractual right a client may have against us to have the securities delivered to them.

This applies both in the case of ISAs and OSAs. However, the nature of clients’ interests in ISAs and OSAs is different. In relation to an ISA, each client is beneficially entitled to all of the securities held in the ISA. In the case of an OSA, as the securities are held collectively in a single account, each client is normally considered to have a beneficial interest in all of the securities in the account proportionate to its holding of securities.

Our books and records constitute evidence of our clients’ beneficial interests in the securities. The ability to rely on such evidence would be particularly important on insolvency. In the case of either an ISA or an OSA, an insolvency practitioner may require a full reconciliation of the books and records in respect of all securities accounts prior to the release of any securities from those accounts.

Applicable regulatory rules

Head office: Clients are protected against the risk that a securities intermediary might fail and not have the securities that it was supposed to be holding on behalf of its clients, either because the securities were never acquired by the securities intermediary or because the securities intermediary wrongfully sold or pledged securities that should have been kept to satisfy its clients’ claims, by the regulatory regimes under which securities intermediaries operate. As a regulated financial institution, we are subject to supervision and examination by various Federal and state banking regulators to monitor our compliance with the legal duties under the UCC set out above.

London branch: We are subject to the client asset rules of the UK Financial Conduct Authority (CASS Rules), which contain strict and detailed requirements as to the maintenance of accurate books and records and the reconciliation of our records against those of the CSDs with which accounts are held. We are also subject to regular audits in respect of our compliance with those rules. As long as books and records are maintained in accordance with the CASS Rules, clients should receive the same level of protection from both ISAs and OSAs.

(b) Shortfalls

If there were a shortfall between the number of securities that we are obliged to deliver to clients and the number of securities that we hold on their behalf in either an ISA or an OSA, this could result in fewer securities than clients are entitled to being returned to them upon our insolvency. If a shortfall arose, clients may have a claim against us for any loss suffered. If we were to become insolvent prior to covering a shortfall, clients would rank as general unsecured creditors for any amounts owing to them in connection with such a claim. Clients would therefore be exposed to the risks of our insolvency, including the risk that they may not be able to recover all or part of any amounts claimed.

How a shortfall may arise

A shortfall could arise for a number of reasons including as a result of administrative error, intraday movements or counterparty default following the exercise of rights of reuse.
We do not generally permit clients to make use of or borrow securities belonging to other clients for intra-day settlement purposes, even where the securities are held in an OSA, in order to reduce the chances of a shortfall arising as a result of the relevant client failing to meet its obligation to reimburse the OSA for the securities used or borrowed. It is nevertheless possible that such use or borrowing could occasionally occur as a result of operational processes where securities are held in an OSA.

Treatment of a shortfall

Head office: In the US, because the UCC provides that a customer's property interest with respect to a particular financial asset held through a securities intermediary is a pro rata property interest in all interests in that financial asset held by the securities intermediary, the allocation of a shortfall as between an ISA and an OSA would be proportional to the interests in that financial asset held in the two accounts. Clients would share pro rata in the shortfall, irrespective of whether their securities were held in an ISA or an OSA.

London branch: In the UK, in the case of an ISA, the whole of any shortfall on that ISA would be attributable to the client for whom the account is held and would not be shared with other clients for whom we hold securities. Similarly, the client would not be exposed to a shortfall on an account held for another client or clients.

In the case of an OSA, the shortfall would be shared among the clients with an interest in the securities held in the OSA (see further below). Therefore, a client may be exposed to a shortfall even where securities have been lost in circumstances which are completely unrelated to that client.

The risk of a shortfall arising is, however, mitigated as a result of our obligation under the CASS Rules in certain situations to set aside our own cash or securities to cover shortfalls identified during the process of reconciling our records with those of the CSDs with which securities are held.

If securities were held in an ISA, the entire loss would be borne by the client for whom the relevant account was held. If securities were held in an OSA, the loss would be allocated between the clients with an interest in that account.

In order to calculate clients’ shares of any shortfall in respect of an OSA, each client's entitlement to securities held within that account would need to be established as a matter of law and fact based on our books and records. Any shortfall in a particular security held in an OSA would then be allocated among all clients with an interest in that security in the account. It is likely that this allocation would be made rateably between clients with an interest in that security in the OSA, although arguments could be made that in certain circumstances a shortfall in a particular security in an OSA should be attributed to a particular client or clients. It may therefore be a time consuming process to confirm each client's entitlement. This could give rise to delays in returning securities and initial uncertainty for a client as to its actual entitlement on an insolvency. Ascertaining clients' entitlements could also give rise to the expense of litigation, which could be paid out of clients' securities.

(c) Security interests

Security interest granted by clients to third parties outside the custody chain

Security interests granted over clients’ securities could have a different impact in the case of ISAs and OSAs.

Where a client purported to grant a security interest over its interest in securities held in an OSA and the security interest was asserted against the CSD with which the account was held, there could be a delay in the return of securities to all clients holding securities in the relevant account, including those clients who had not granted a security interest, and a possible shortfall in the account. However, in practice, we would expect that the beneficiary of a security interest over a client’s securities would perfect its security by notifying us rather than the relevant CSD and would seek to enforce the security against us rather than against such CSD, with which it had no relationship.

In order to perfect a security interest granted by a client, under the UCC the creditor would have to reach the client's interest in the securities either by filing a financing statement or by obtaining control with respect to the client's security entitlement against us. Under the UCC, the creditor could not reach our interest against a CSD through which the security was held.

We would also expect CSDs to refuse to recognise a claim asserted by anyone other than ourselves as account holder.

Security interest granted by us to a CSD

Where the CSD benefits from a security interest over securities held for a client, there could be a delay in the return of securities to a client (and a possible permanent loss) in the event that we failed to satisfy our
obligations to the CSD and the security interest was enforced. This applies whether the securities are held in an ISA or an OSA. However, in practice, we would expect that a CSD would first seek recourse to any securities held in our own proprietary accounts to satisfy our obligations and only then make use of securities in client accounts. We would also expect a CSD to enforce its security rateably across client accounts held with it.

Furthermore, the CASS Rules restrict the security interests that we may grant over securities held in a client account to those securing debts relating to clients or the provision of services to clients, except where security interests are required by applicable law.

**GLOSSARY**

*bail-in* refers, as applicable, to the process under the U.K. Banking Act 2009 applicable to failing UK branches of third country banks and investment firms, or the process under the FDIA applicable to our bank holding company, under which our (in the case of the Banking Act 2009) liabilities to clients may be modified, for example by being written down or converted into equity. Under the FDIA, this process is applicable to our bank holding company, but not to us.

**Central Securities Depository or CSD** is an entity which records legal entitlements to dematerialised securities and operates a system for the settlement of transactions in those securities.

**Central Securities Depositories Regulation or CSDR** refers to EU Regulation 909/2014 which sets out rules applicable to CSDs and their participants.

**direct participant** means an entity that holds securities in an account with a CSD and is responsible for settling transactions in securities that take place within a CSD. A direct participant should be distinguished from an indirect participant, which is an entity, such as a global custodian, which appoints a direct participant to hold securities for it with a CSD.

**Dodd-Frank Orderly Liquidation Authority** refers to Title II of the U.S. Dodd-Frank Wall Street Reform and Consumer Protection Act.

**EEA** means the European Economic Area.

**FDIC** means the U.S. Federal Deposit Insurance Corporation.

**FDIA** means the U.S. Federal Deposit Insurance Act.

**Financial Markets Infrastructure Act or FMIA** refers to FinfraG (Finanzmarktinfrastrukturgesetz), a Swiss law which sets out rules applicable to CSDs and their participants.

**resolution proceedings** are, as applicable, proceedings for the resolution of failing insured depositary institutions under the FDIA or for the resolution of failing UK banks and investment firms under the U.K. Banking Act 2009.

**Segregated Accounts** are accounts opened and maintained with European CSDs and other custodians and depositaries to custody cash and securities for clients.

**UCC** means the Uniform Commercial Code in effect in the State of New York.