INITIAL MARGIN

EXTERNAL FAQ

This FAQ covers both EU and US regulations. In case of discrepancies between the two, the stricter set of rules will apply.

DISCLAIMER

Societe Generale Corporate & Investment Banking (SG CIB) is a marketing name for corporate and investment banking businesses of Societe Generale (SG) and its subsidiaries worldwide. This document is for informational purposes only and does not constitute an offer, or the solicitation of an offer, or a recommendation, to buy or sell any securities, futures, derivatives or other financial instruments, services or products. Nothing in this document should be construed as an official position of Societe Generale on the legal or regulatory matters discussed herein or its interpretation of any of the legal or regulatory requirements. Although the information herein has been obtained from sources believed to be reliable, SG and its affiliates make no representation or warranty regarding the accuracy or completeness of any information and are not responsible for errors of any kind. This material is for institutional and corporate clients only. The information contained herein does not have regard to specific investment, financial situations or the specific needs of any specific entity or person. Clients should make their own appraisal of the risks and appropriateness of investing in, or trading the types of products described herein given their own investment objectives, experience, financial and operational resources and other relevant circumstances. This document is not intended to have an advisory character or intended to represent an investment recommendation or a recommendation regarding any transaction, strategy, product or service. The information contained herein may not be relied upon as investment, accounting, legal, regulatory or tax advice or an investment recommendation. The addressees of this document are encouraged to seek their own legal or regulatory advice.

Notice to French clients: This material is issued in France by or through Societe Generale which is authorized and supervised by the Autorite de Controle Prudentiel et de Résolution and regulated by the Autorite des Marches Financiers.

Notice to UK clients: This document is issued in the U.K. by the London Branch of Societe Generale. Societe Generale is a French credit institution (bank) authorised by the Autorité de Contrôle Prudentiel et de Résolution (the French Prudential Control and Resolution Authority) and the Prudential Regulation Authority and subject to limited regulation by the Financial Conduct Authority and Prudential Regulation Authority. Details about the extent of our authorisation and regulation by the Prudential Regulation Authority, and regulation by the Financial Conduct Authority are available from us on request.

Notice to US clients: If you are a "U.S. Person" (as defined by the U.S. Commodity Futures Trading Commission or the U.S. Securities and Exchange Commission), please visit https://wholesale.banking.societegenerale.com/en/compliance-regulatory-information/market-regulation/dodd-frank-act/ for important information with respect to derivative products. By transacting with Société Générale, you are deemed to acknowledge that you have read and accepted the information contained in the disclosure documents on this website.

Notice to Canadian clients: This document is for information purposes only and is intended for use by Permitted Clients, as defined under National Instrument 31-103, Accredited Investors, as defined under National Instrument 45-106, Accredited Counterparties as defined under the Derivatives Act (Quebec) and "Qualifies Parties" as defined under the ASC and BCSC Orders.

Additional information is available upon request. This document may not be reproduced, distributed, or published by any other person without the prior consent of SG.

© 2021 Societe Generale Group ("SG") and its affiliates. All rights reserved.

What is Initial Margin?

Financial regulators globally have imposed an obligation on certain types of entities (see below) to exchange collateral in the form of Variation Margin ("VM") and, where applicable, Initial Margin ("IM") for OTC derivatives which are not cleared through Central Clearing Counterparties ("CCPs") to protect against the risk of a default by a counterparty.

VM is collateral collected on a regular basis to reflect changes to the market value of outstanding OTC derivative contracts. IM is collected to cover a counterparty's current and potential future exposures in the interval between the last exchange of VM and the liquidation of positions following default of its counterparty as well as the hedging of that exposure.

While VM requirements were introduced in a single "Big Bang" in March 2017, IM requirements are being phased in over a 7 year period, with the largest number of counterparties concentrated in Phase 5 and Phase 6 which come into force in September 2021 and 2022 respectively.

What are the main differences between VM and IM?

The key differences between VM and IM are summarised in the table below:

	Variation Margin	Initial Margin
What is being collateralised?	Mark-to-Market (i.e. replacement cost)	Margin period of risk (MPOR) - the interval between the last exchange of VM and close-out.
Collateral taker right to use collateral?	Yes	No
How is the value of exposure determined?	SG's estimate of transaction replacement costs (MTM) per ISDA Agreement	Standard calculation using either: 1) "SIMM" model; or 2) standard regulatory "GRID"
Segregation	No; full right of use	Yes; collateral segregation is required
Transfer of Collateral	Net	Gross
Primary Collateral Type	Cash	Non-cash (securities)
Legal Security Mechanism	Title Transfer English law/ New York law security interest	Security interest over accounts at custodian
Level of Complexity	Low	High

Who is subject to IM requirements under EMIR?

Under EMIR, **FC** and **NFC+**[1] entities become subject to IM based on their **Aggregate Average Notional Amount ("AANA")** of OTC Derivatives. The threshold for Phase 5 is EUR 50 billion with a compliance date of 1st September 2021 which drops to EUR 8 billion* in Phase 6 with a compliance date of 1st September 2022.

	Compliance Date	AANA Thresholds (EUR/USD)	In Scope Client Examples
Phase 1	September 1st 2016	>3.0 trillion	Large banks, insurers and hedge funds
Phase 2	September 1st 2017	>2.25 trillion	
Phase 3	September 1st 2018	>1.5 trillion	
Phase 4	September 1st 2019	>0.75 trillion	Mid-size banks and hedge funds
Phase 5**	September 1st 2021	>50.0 billion	Smaller financial institutions and funds managed by asset managers
Phase 6**	September 1st 2022	>8.0 billion	

Under DFA Title VII, the US rules apply to swap dealers, security-based swap dealers, major swap participants, major security-based swap participants and financial end-users. In addition, the calculation is based on average daily aggregate notional amount (as opposed to AANA) and the thresholds above are reflected in USD.

On July 23rd 2019, BCBS-IOSCO agreed to extend the final implementation of the margin requirements by introducing an additional implementation phase whereby, as of 1 September 2020, covered entities with an AANA of non-centrally cleared derivatives greater than EUR 50 billion would be subject to IM requirements. With this extension, the final implementation phase would take place on 1 September 2021, at which point covered entities with an AANA of non-centrally cleared derivatives greater than EUR 8 billion will be subject to the requirements.

On April 3, 2020, BCBS/IOSCO agreed to further extend the deadline for completing the final two implementation phases of the margin requirements for non-centrally cleared derivatives by one year. As of September 1, 2021, covered entities with an AANA of non-centrally cleared derivatives greater than EUR 50 billion will be subject to the requirements and the final implementation phase will take place on September 1, 2022 at which point covered entities with an AANA of greater than EUR 8 billion will be subject to the requirements.

[1] Financial Counterparties ("FCs") are those Union-regulated entities (or entities managed by Union-regulated managers) in the financial services, funds and insurance sectors including banks, investment firms, insurance companies, UCITS, AIFs, Pension Funds.

Non-Financial Counterparties ("NFCs") are all other Union counterparties to OTC derivative transactions (other than central counterparties). NFCs are further divided into groups of those, (1) conducting large volumes of derivative trading activity for reasons besides hedging, and those (2) use derivatives to a lesser degree or chiefly for the purpose of hedging their normal commercial activities. The divide is based on whether the NFC is part of a group in which the aggregate notional amount of outstanding derivatives, excluding hedging transactions, entered by all NFCs within the group, exceeds the applicable "clearing threshold". An NFC above the clearing threshold is often referred to as an "NFC+", and an NFC below the clearing threshold is referred to as an "NFC-".

If the group's rolling average position exceeds the clearing threshold over any 30-day period, the NFC is an NFC+ and will be required to clear OTC derivative contracts within four months of becoming subject to the Clearing Obligation. Equally, if the NFC can demonstrate that its rolling average position over a 30-day period falls below the clearing threshold, it will no longer be required to clear its OTC derivative contracts.

Counterparties are expected to confirm their exemption annually.

Are there any exemptions from the obligations to collect IM?

Exemptions from IM requirements are applicable to the following products/scenarios:

- where the traded derivative products are cleared through a recognised CCP;
- FX spot trades;
- physically-settled FX (forwards and swaps) and exchanges of principal payment on cross currency swaps are not subject to IM;
- single-stock equity and index options are either permanently exempt under US rules (except certain high delta options) or temporarily exempt until January 2024 under EMIR; and
- under EMIR, in-scope entities do not need to exchange IM when the trade is an **intra-group transaction**, provided certain conditions are met and approved by the regulator;
- under DFA USPR, IM is not required for inter-affiliate trades if approved by the regulator; and
- for certain types of counterparties, such as those benefiting from an end-user exemption (DFA) or characterized as NFC- (EMIR).

What does SG post and collect as IM collateral?

While cash is allowed under the regulations, fungibility and perfection of security issues around cash mean that custodians, SG and other banks prefer to avoid accepting it. SG, together with the rest of the industry, is looking into available options to accept cash with a view to immediately re-investing it into Money Market Funds which would be compliant with EMIR and/or US rules, as applicable.

In the meantime, and subject to regulatory requirements, SG's preference from a funding cost perspective (but subject to our credit risk department approval) is to post/collect a wide range of securities. Please be advised, however, that non-cash collateral must be eligible under EMIR and USPR requirements and is subject to standardized haircuts and minimum regulatory ratings.

IM Thresholds

There is a regulatory maximum allowed IM threshold of **EUR/USD 50 million** in aggregate across all IM CSA between 2 counterparty Groups under which counterparties may decide not to exchange IM.[2]

Parties are free to propose the allocation of this threshold amongst their group entities when facing those in another counterparty group. The SG Group has allocated all of its 50 million threshold to Societe Generale SA. If a counterparty has multiple trading relationships with Societe Generale SA, the threshold can be split amongst the different counterparty entities.

High-level example:

2 entities in SG group facing 3 entities in Client group, with the projected IM exposure in relation to various entities in their group reflected in how SG has allocated its threshold.

SG Entity	Client Entity	SG Threshold	Client Threshold
Societe Generale SA	Client Entity 1	30 million	Client to decide
Societe Generale SA	Client Entity 2	20 million	Client to decide
Societe Generale SA	Client Entity 3	0	Client to decide

[2] For example, the aggregate IM thresholds across all IM CSAs between all SG Group Entities, facing all of a counterparty's entities, cannot exceed EUR/USD 50 million.

How is IM calculated?	IM exposures must be calculated by both parties using: ▪ SIMM – based on risk factors and sensitivities; or ▪ GRID – based on a fixed percentage of the notional. Like most major dealers, **SG primarily uses SIMM** for most OTC products which encompasses the key IM valuation criteria set out in the regulations. The primary benefit of SIMM is it considers the actual risk exposure of the portfolio. Please be advised that SG's SIMM model is US rule compliant and therefore, even where the US rules do not apply, SIMM exceptions will always be applied to the following products: ▪ Weather swaps, ▪ Longevity or mortality swaps, ▪ Natural disaster or catastrophe swaps, ▪ Tax revenue swaps, ▪ Dividend swaps, ▪ Recovery locks and swaps, and ▪ Home price swaps. When counterparties do not support SIMM, SG can fall back to the GRID method subject to SG internal approval.
Choice of Custodian	Counterparties are free to elect their own non-affiliated third-party custodian and preferred segregation structure (triparty or third party). SG is able to use the triparty custodial services of **JP Morgan**, **BNYM** and **Clearstream**.
Use of Industry Negotiation Platforms	There is one main online negotiation platform on offer, **ISDA Create** (collaboration between ISDA and Linklaters). Its former competitor, Margin X (collaboration between Markit and A&O), withdrew from the competition in the second half of 2019. ISDA Create is a paid service for sell-side firms but free to use for buy-side. **SG has decided not to sign up for the platform** for Phase 5/6.
Must IM documentation be put in place below the 50m IM threshold?	In March 2019, BCBS-IOSCO issued guidance highlighting that the framework for implementing margin requirements does not specify a need for documentation, custodial or operational arrangements where the bilateral IM amount does not exceed the EUR/USD 50 million IM threshold. In other words, as noted above, even if an entity is in scope for IM requirements, it may continue to trade with its counterparties without IM documentation, if the aggregate IM across all eligible products traded between both parties (at group level) is less than EUR/USD 50 million. European and US regulators have confirmed this interpretation. The ESAs consider that there is no need to amend the Delegated Regulation on bilateral margin requirements for counterparties below the 50 million IM exchange threshold to defer the relevant operational and legal set-up in place until they are closer to it. Therefore, no amendment related to this was included in the draft RTS published on 5 December 2019. From a US perspective, the USPRs amended their rules to align with the BCBS-IOSCO IM documentation relief and to clarify that IM trading documentation is not required to be in place prior to the time that IM is required to be collected/posted under the USPR margin rules. In addition, the CFTC Staff issued an Advisory confirming the BCBS-IOSCO interpretation. Subject to internal approval, dealers can agree to deferring negotiations with counterparties who are below the EUR/USD 50 million IM threshold provided that both parties act diligently to monitor their IM exposures and ensure that IM documentation and custodial arrangements are in place before the applicable threshold is reached.
What happens if trades are subject to multiple regulatory regimes?	When rules of multiple regimes apply to a trading relationship, **parties will comply with the regime with the strictest set of rules**.

<table>
<tr><td>Do the rules apply to legacy trades?</td><td>No, the rules only apply to trades concluded from the date of entry into application of the rules (subject to lifecycle events).</td></tr>
<tr><td>Do new collateral agreements need to be entered with our counterparties?</td><td>Yes, a new IM document suite, including custodial arrangements, must be put in place if both counterparties are above the EUR/USD 50 million threshold. Below this threshold, counterparties may choose to defer negotiations of IM documentation based on the BCBS-IOSCO statement.</td></tr>
<tr><td>What happens if regulatory compliance is not achieved by the deadline?</td><td>Current SG policy is that in the absence of regulatory compliant IM documentation, or a counterparty's ability to rely on the BCBS-IOSCO statement below the EUR/USD 50 million IM threshold, trading of in-scope products is prohibited.</td></tr>
<tr><td>Collateral Management and Dispute Resolution Tools</td><td>SG is using Acadiasoft, as with most of the industry's participants, to calculate its IM requirements, manage its margin calls and manage dispute resolution. Additionally SG uses TriOptima for trade reconciliation as well as dispute resolution (unmatched trades).</td></tr>
<tr><td>Do the SEC's new security-based swap dealer rules impact these requirements?</td><td>No, SG SA, the Group's only SEC-registered security-based swap dealer ("SBSD"), is exempt from the SEC/SBSD uncleared margin requirements and applies the USPR margin rules instead (the USPR rules encompass both swaps and security-based swaps booked to SG SA).</td></tr>
<tr><td>Phase 6 General Timetable</td><td>Please see the table below for SG's key project milestones and interim deadlines to assist with planning:
<table>
<tr><th>Activity</th><th>Deadline</th></tr>
<tr><td>Custodian Documentation Complete/Submitted to Custodian for Setup</td><td>March 31st 2022</td></tr>
<tr><td>IM Negotiations Complete/Submitted for Internal Setup</td><td>July 31st 2022</td></tr>
</table></td></tr>
<tr><td>SG contact details for IM related queries</td><td>Please direct all IM related queries to: WORLD-SGCIB-UMR-Team@sgcib.com</td></tr>
</table>