FMDQ EXCHANGE OPERATIONAL MODALITIES FOR MB-38 AND MB-39

PART A: REGISTRATION AND HEDGING OF FX RISKS FROM CONTINGENT CERTIFICATES OF CAPITAL IMPORTATION TRANSACTIONS AND DELIVERABLE FX FORWARDS USING OTC FX FUTURES CONTRACTS

1. Registration Requirements

(i) Registration of Certificates of Capital Importation ("**CCI**") with contingent FX risk (**"Contingent"** CCIs) and registration of deliverable Foreign Exchange ("**FX**") Forwards as required under sections 3(iii) and 2(ii) of MB-38 and MB-39 respectively, shall be conducted by filing requisite details of the Eligible Underlying Transactions ("**EUTs**") and supporting documents via the FMDQ Futures Trading & Reporting System ("**FFTRS**") or such other FMDQ Exchange-advised medium.

(ii) Timelines for registration shall be as follows:

S/N	Transaction	Registration Timeline
1.	"Contingent" CCIs*	Within two (2) business days of issuance of the "Contingent" CCI.
2.	Deliverable FX Forwards transactions executed post- publication of these Operational Modalities	Must be registered prior to the purchase of an OTC FX Futures contract.

** "Contingent" CCIs and Deliverable FX Forwards existing prior to the release of these Operational Modalities should be registered with FMDQ Exchange **on or before December 1, 2022** by the Trade Dealing Member (Bank) ("**Trade DMB**").*

(iii) The **Trade DMB**[1] shall be required to provide the following minimum documentation, at the point of registration, which shall include *inter alia*:

A. "Contingent" CCIs

- Duly completed template for reporting of "Contingent" CCIs *(see Appendix I)*
- Copy of "Contingent" CCIs
- Copy of executed agreements and supporting documents for the underlying transaction creating the contingent FX risk such as the Global Master Repurchase Agreement, ISDA[2] Master Agreement, Loan Agreement, etc. *(as applicable)*

B. Deliverable FX Forwards

- Duly completed template for reporting of deliverable FX Forwards *(see Appendix I)*
- Copy of CCI for the EUT (*i.e. Foreign Portfolio Investment ("**FPI**"), Foreign Direct Investment ("**FDI**") or Foreign Currency ("**FCY**") loan transaction*)
- Copy of relevant and duly executed FX Forward Agreement

(iv) The Trade DMB shall be responsible for the following:

- Notifying the Exchange of any change in the structure of the underlying transaction which would affect the supporting documents previously filed and providing evidence of same
- Updating the records of documentation provided e.g. the face value of the CCI where Spot FX has been purchased for the purpose of a partial or full externalisation of capital using the "Contingent" CCI
- Notifying the Exchange, in writing or such other FMDQ Exchange advised medium, of a default on the underlying transaction (i.e. *crystallisation of an FX risk*) of a "Contingent" CCI within two (2) business days of its occurrence

(v) Further to the above, relevant information and supporting documents shall be updated with the Exchange via FFTRS or the FMDQ Exchange-advised medium.

2. Hedging of FX Risks from "Contingent" CCIs and Deliverable FX Forwards

[1] Refers to the DMB that issued the "Contingent" CCI or has a short position in a deliverable FX Forward contract executed with a client on the back of a foreign capital inflow evidenced by the issuance of a CCI and corresponding conversion of the foreign capital inflow to Nigerian Naira.
[2] International Swaps and Derivatives Association

(i) **"Contingent" CCIs**

- Purchase of OTC FX Futures contracts on "Contingent" CCIs shall be permissible only upon crystallisation of FX risk in the underlying transaction (*for which the "Contingent" CCI was issued*) duly registered with FMDQ Exchange
- The Futures DMB[3] shall validate the occurrence of a default and the attendant FX risk arising from such default, as well as obtain all relevant supporting documentation from the Trade DMB (*e.g. default notice duly acknowledged by the defaulting party, contractual rights to liquidate collateral, etc.*)
- The Futures DMB shall certify in writing or such other FMDQ Exchange-advised medium that it has validated the occurrence of the default on the underlying transaction (i.e. crystallisation of the FX risk) and provide supporting documentation of same to the Exchange, following which FMDQ Exchange shall review the submission and authorise the "Contingent" CCI as an EUT for the purchase of OTC FX Futures on FFTRS
- Upon authorisation of the "Contingent" CCI as an EUT by FMDQ Exchange, the Futures DMB may proceed to purchase the OTC FX Futures contract(s)
- The Futures DMB shall be responsible for ensuring that all other required documentation as stipulated in the FMDQ OTC FX Futures Market Operational Standards, relevant Market Bulletins and such other relevant regulation as may be prescribed by the Exchange from time to time is provided and valid, at the point of purchase of the OTC FX Futures contract(s) via the FFTRS or such other FMDQ Exchange-advised medium

(ii) **Deliverable FX Forwards**

- Upon the successful registration of the deliverable FX Forward (evidenced by a written notification from the Exchange), purchase of OTC FX Futures contracts on the registered deliverable FX Forwards shall be immediately permissible by the Futures DMB

The Exchange reserves the right to, request for such additional information and/or supporting documentation as may be deemed relevant to validate and authorise the purchase of OTC FX Futures contracts to hedge Contingent CCIs and deliverable FX Forwards exposures.

PART B: PRE-LIQUIDATION OF OTC FX FUTURES CONTRACTS

1. Parties to a Pre-Liquidation Transaction

(i) Pre-liquidating Transaction Counterparty: This is the Futures DMB initiating a pre-liquidation request on behalf of a foreign portfolio investor.

(ii) Non-pre-liquidating Transaction Counterparty: This is the transaction counterparty (i.e. the Central Bank of Nigeria ("**CBN**")) from whom the Pre-Liquidating Transaction Counterparty had initially purchased the contract(s) to be pre-liquidated.

2. Pre-Liquidation of OTC FX Futures Contracts

(i) In line with MB-38, foreign portfolio investors may fully or partially pre-liquidate their positions in OTC FX Futures contracts through their Futures DMB (i.e. the Pre-liquidating Transaction Counterparty).

(ii) Subject to the fulfillment of the conditions outlined in MB-38, the Pre-liquidating Transaction Counterparty shall initiate a request for pre-liquidation of OTC FX Futures contract(s), providing relevant details of the OTC FX Futures contract to be pre-liquidated *(see Appendix II)* via an email to the **Clearing & Settlement Operations Group** (clg@fmdqgroup.com) or such other FMDQ Exchange-advised medium.

(iii) Such requests by the Pre-liquidating Transaction Counterparty shall be reviewed by the Clearing & Settlement Operations Group and the status of the request shall be communicated as either **Approved or Rejected** via email or such other FMDQ Exchange-advised medium, within five (5) business days of receipt of the pre-liquidation request.

[3] *Refers to a DMB that executes an OTC FX Futures contract with a Client.*

(iv) Upon approval of the pre-liquidation request, standard settlement processes for the pre-liquidated amount will be triggered within two (2) business days with the following nuances:
- Any Settlement Amount gain due to the Pre-liquidating Transaction Counterparty shall not be transferred to the Pre-liquidating Transaction Counterparty
- In the event that the OTC FX Futures contract is at a loss, the Pre-liquidating Transaction Counterparty's CBN operating account shall be debited for the Settlement Amount
- All pre-liquidation costs shall be debited from the Pre-liquidating Transaction Counterparty's CBN operating account
- Upon completion of a pre-liquidation exercise, the outstanding contract value on the relevant OTC FX Futures contract (i.e. in the case of a partial liquidation) held by the Pre-liquidating Transaction Counterparty shall be subject to daily mark to market in line with extant market structure
- Where the OTC FX Futures contract is wholly or partially pre-liquidated, the Futures DMB shall immediately return the attendant initial margin to the Client and update the FFTRS accordingly

PART C: HEDGING OF RETURNS EARNED ON NAIRA INVESTMENTS

1. Determination of US Dollar Notional Amounts for Hedging of Returns Earned on Fixed Income Investments

The US Dollar Notional Amount (i.e. value of OTC FX Futures contract) of returns earned on fixed income investments (i.e. pre-determined fixed income returns [i.e. interest and discount amounts]) eligible to be hedged by FPIs using OTC FX Futures shall be calculated as follows:

$$\textit{USD Notional Amount of OTC FX Futures contract} = \textit{Total Eligible Naira Amount} \div \textit{Applicable OTC FX Futures Rate (as at deal date)}$$

2. Determination of Total Eligible Naira Amount for Hedging of Returns Earned on Naira Investments

(i) The Total Eligible Naira Amount for pre-determined returns earned on fixed income investments (i.e. interest and discount amounts) shall be as follows:
- ***Interest-bearing investments*** – Naira value of periodic coupon/interest payable on the value of the underlying investment *[e.g. the Total Eligible Naira Amount on a ₦ 100,000,000 investment in an FGN Bond or Fixed Placement with an annual coupon/return rate of 10% will be **₦ 10,000,000** i.e. 10% × ₦ 100,000,000]*
- ***Discounted securities*** – Difference between the face value and the discounted value of the securities *[e.g. the Total Eligible Naira Amount on a ₦ 90,000,000 investment in a Nigerian Treasury Bill with a Face Value of ₦ 100,000,000 will be **₦ 10,000,000** i.e. ₦ 100,000,000 – ₦ 90,000,000]*

(ii) Where the discounted or face value of the underlying investments is greater than the Naira value of the underlying CCI, and the variance is not backed by evidence of returns earned on prior investments (i.e. evidence that the Naira value of the underlying CCI has been previously invested and earned positive returns re-invested in other investments), the Total Eligible Naira Amount shall be:
- ***Interest-bearing investments –*** Naira value of periodic coupon/interest payable on the Naira value of the underlying CCI
- ***Discounted securities –*** Difference between the face value and the discounted value of the underlying investment calculated on a pro-rata basis (i.e. the ratio of the Naira value of the underlying CCI to the discounted value of the underlying investment)

3. Documentation Requirements

The Total Naira Amounts eligible for hedging with OTC FX Futures shall be supported with the documents listed below and such other documentation as may be prescribed by FMDQ Exchange from time to time:

(i) Valid Certificate of Capital Importation.

(ii) Evidence of investment in the underlying security.

(iii) Dividend payments as evidenced by a Board Resolution and duly reported in the latest audited accounts of the company in whose security the investment was made

APPENDICES

Appendix I: Template for Registration of Eligible Underlying Transactions*

Data Field	Details
Reporting DMB Name	
Reporting Staff Name	
CCI Details	
CCI Type	"*Contingent*" for contingent CCIs; "*Regular*" for CCIs issued on the back of deliverable FX Forwards
CCI Number	*Issuing Bank Code + six-digit code on the top righthand corner of the certificate*
CCI Issuance Date	
CCI Face Value ($'mm)	
Transferor	
Beneficiary	
Details of Underlying Transaction	
Customer Name	
EUT[4] Type	*e.g. FDI/FPI/FCY loan*
Transaction Type	*"Foreign Currency Repos with NGN collateral, Cross Currency Swaps, Total Return Swaps, Foreign Currency Borrowings collaterised with NGN collateral"* for contingent CCIs or; *"Deliverable Forwards"* for CCIs issued on the back of deliverable FX Forwards
Transaction Counterparty	
Underlying Transaction Initiation Date	
Underlying Transaction Maturity Date	
Underlying Transaction Value ($'mm)	

**This registration template is subject to change and may be updated from time to time as may be determined by FMDQ Securities Exchange Limited.*

[4] Eligible Underlying Transactions

Appendix II: Supporting Information for Pre-Liquidation Request**

Data Field	Details
Futures DMB Name	*The Name of the Futures DMB which purchased the OTC FX Futures contract to hedge the FPI (i.e. the Pre-Liquidating Transaction Counterparty)*
Client Name	*Name of the Client i.e. the Foreign Portfolio Investor (Buyer (from the Futures DMB) of the OTC FX Futures contract on FFTRS)*
Contract Code	*e.g. NGUS DEC 30 2020*
Client Contract Ref.	
CBN Contract Ref.	
Reason for Pre-Liquidation	
Pre-Liquidation Amount ($)	*Notional amount of the OTC FX Futures contract sold to the Client to be pre-liquidated (It may be full [i.e. the entire notional amount of the contract sold to the Client] or partial [a portion of the entire notional amount of the contract sold to the Client])*

***The information presented in the table above is not exhaustive and represents the minimum amount of information that must be provided upon filing of a pre-liquidation request. FMDQ Securities Exchange Limited reserves the right to request additional information or relevant supporting documentation to process pre-liquidation requests.*