

# Payment purpose exemption and forward exchange contracts

## What is a forward exchange contract (FEC)?

A forward exchange contract is a binding agreement between two parties to exchange specified currencies at a fixed rate on a future date (beyond two days).

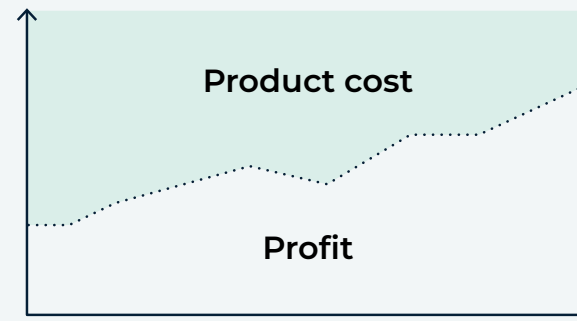
### KEY BENEFITS OF AN FEC

- Locks in the exchange rate for future cash flows.
- Helps protect against adverse currency movements.
- Provides certainty for importers and exporters by minimizing FX risk.



### CONSIDERATION

- No ability to benefit from favorable exchange rate movements after the contract is agreed.



## Two types of FECs

### Closed forward (fixed date)

The spot rate is adjusted by forward points for a specific date.

- If the discount or premium is in your favour, then the outright forward rate is better than the spot rate.
- If the discount or premium is not in your favour, then the outright forward rate is worse than the spot rate.

### Open forward (window)

The spot rate is potentially adjusted for a range of dates.

- If the discount or premium is in your favour, then the outright forward rate is only improved to the earliest date the contract can be used (window date).
- If the discount or premium is not in your favour, then the outright forward rate is calculated to the longest possible date (i.e. the same as a closed forward).

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## How do forward points work?

Forward points reflect interest rate differentials between currencies and are added or subtracted from the spot rate to calculate the forward rate.

- Forward points are not an indication of currency direction.
- Forward points are not a fee charged by Convera.

## What is a payment purpose exemption (PPE)?

Under MiFID II and related regulations (such as EMIR), FECs are regulated financial instruments. However, if an FEC is entered into solely to facilitate payment for identifiable goods or services, it may qualify for PPE.

### Benefits of PPE

- Exemption from MiFID II and EMIR reporting requirements.
- No need for a Legal Entity Identifier (LEI).
- Avoids ongoing transaction reporting costs to a central repository.



### PPE checklist

To qualify, FECs must:

- ✓ Have at least one counterparty be a corporate entity (non-financial).
- ✓ Be for payment of identifiable goods or services (e.g., invoices, purchases).
- ✓ Be entered into bilaterally and not on a regulated trading venue or exchange (Convera does not offer FECs of this nature).
- ✓ Be settled physically (i.e. currencies exchanged as specified in the FEC).



#### EXAMPLES OF PPE TRADES\*

- ✔ SME hedging USD to pay for imports from China (purchase of goods).
- ✔ UK business paying overseas employees in local currency (purchase of services).

In these examples, the FEC would qualify for PPE because it is being used to facilitate payment for identifiable goods or services.

#### EXAMPLES OF NON-PPE TRADES

- ❗ Hedging value of overseas factory or currency loan.
- ❗ A non-deliverable or cash-settled forward.

In these examples, the FEC would not qualify for PPE because it isn't being used to facilitate payment for identifiable goods or services.

*\* More examples are set out in Chapter 13 of the UK FCA's Perimeter Guidance Manual.*

*This guide to PPE Forward Contracts is provided for information only and does not constitute legal advice. It provides a simplified overview of the PPE requirements. Convera does not accept any liability to any person for the information which is provided in this document. We strongly recommend that you seek legal advice in order to fully understand the requirements of PPE.*



**Speak to a Convera specialist for guidance and support on our currency risk management product and services.**

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