Corpay

Schedule 1

FX Derivatives Risk Disclosure Statement

General Advice Only

The purpose of this statement is to provide an overview of the risks associated with foreign exchange derivatives. It is not intended to disclose all relevant information for you to determine whether a foreign exchange forward contract, vanilla option or structured option is an appropriate risk management tool for your particular business requirements and financial circumstances. Please refer to the more in-depth PDS document that more fully explains the features, risks, and costs of the derivatives offered by Corpay. The PDS should be read carefully before entering into a derivative agreement and a copy should be retained for future reference.

Suitability

A foreign exchange derivative may be suitable for you if you have a strong understanding of advanced foreign exchange hedging strategies and markets. If you are not confident about your understanding of the material contained in the PDS, we strongly encourage you to seek independent advice before entering into a forward contract, vanilla option or structured option. Please contact your Corpay representative for further information.

What is a Foreign Exchange Forward?

A foreign exchange forward is the simplest and most commonly used currency hedging product. A forward is used to set an exchange rate today for settlement at a future date, typically within 12 months. The exchange rate is fixed and not subject to fluctuations in the spot market.

Foreign Exchange Forward Risks

The primary risk of foreign exchange forwards is that you are obliged to transact at the contractual rate which may be worse than the prevailing spot rate. You will not be able to participate in favourable market moves. In the event your business circumstances change and the forward contract is no longer required you may incur a loss on close out.

In addition, you may be required to pay margin/deposit to cover the mark-to-market risk of the contract.

What is a Foreign Exchange Option?

A Foreign Exchange Option is a financial contract entered into by two parties: a buyer and a seller. The buyer of an Option contract pays a Premium to the seller and receives the right, but not the obligation, to exchange a specified amount of currency for another currency at a prescribed foreign exchange rate, referred to as the strike rate, on a specified date. The seller of an option receives a premium for offering these rights to the buyer and is assigned the obligation to fulfill the terms of the contract if the buyer exercises their rights.

There are two general types of option contracts: a put option and a call option. A put option provides the right, but not the obligation, to sell the underlying currency. A call option provides the right, but not the obligation, to buy the underlying currency. A put option is used to protect against the depreciation of the underlying currency, while a call option is used to protect against the appreciation of the underlying currency.

What is a Vanilla Option?

vanilla option provides you with the right, but not the obligation, to exchange the underlying currency at a specified exchange rate and time. A vanilla option provides protection in the event of adverse spot market movement as well as the opportunity to participate in favourable spot market movement.

Vanilla Option Risks

The risk of a vanilla option is limited to the amount of the non-refundable premium paid to acquire the option.

What is a Structured Option?

A structured option is a foreign exchange risk management product that allows the user to achieve a wider variety of hedging outcomes than a foreign exchange forward or vanilla option. A structured option involves the simultaneous purchase and sale of two or more options. For example, a collar option is a structured option that involves buying a call option and selling a put option with different strike rates for the same expiry date. Structured options may involve vanilla and/or exotic options, may involve multiple legs (i.e. two or more legs in one structure), may incorporate the use of leverage, and may be structured at zero-premium.

Risks of Structured Options

Whenever a structured option is entered into, the seller is providing the buyer the right to transact at a particular foreign exchange rate (the strike rate) at their discretion. The strike rate may not be a favourable rate relative to the spot rate at the time the option is exercised. The seller must ensure that the strike rate and notional amount they may be obligated to trade are consistent with their hedging objectives and needs. Because of the nature of knock-out and knock-in options, you may be obligated to trade at a foreign exchange rate that is significantly worse than the spot rate at the time of the expiry date.

Should the sold leg of a structured option be exercised, the seller is obligated to transact. From the date of booking until the expiry date, there is the risk that the seller's business circumstances may change and there is no longer a need for the structured hedge. Should Corpay's client wish to unwind or cover the hedge they may have to pay a premium to do so if the sold option is out-the-money to the seller and the bought option is not in-the-money.

Structured options are only suitable for persons who:

a) understand and accept the risks involved in transacting in financial derivatives involving foreign exchange;
b) Have available funds to meet any potential margin requirements;
c) are end users of foreign exchange for hedging purposes; and
d) meet the requirements in their location of incorporation for entering into a derivatives contract as determined by the appropriate regulatory policies.

Corpay recommends that you obtain independent financial and legal advice before entering into any options, including vanilla and structured options. Because vanilla and structured options are highly customizable, the structures can become quite complex to the point where they might not actually meet the objective of providing a prudent hedge. It is paramount that hedging goals are reasonable and clearly identified and structures are implemented to achieve specific goals.

Leverage

Structured options may utilize leverage to achieve a more favourable exchange rate. Leveraging structured options is a process where the client sells a notional amount for one or more of the underlying options, which is larger than the notional amount of the underlying options that are purchased. This means you may be obligated to trade a larger notional amount (the sold options) than the protected amount (the bought options).

The increased obligation within the structured option is offset by more favourable rates for the underlying structure. These enhanced rates give you the potential to achieve better outcomes than what is normally available with the non-leveraged version of the product. Whilst the benefits of enhanced rates are clear, there are increased risks when using leverage with structured options.

Risks of Structured Options

The use of leverage creates additional risks compared to non-leveraged structured options. When leverage is used, these new risks can add to the already existing risks of non-leveraged structured options. The risks associated with leverage are set out below:

a) You may be obligated to purchase a larger notional amount than you are protected for in the structured option. If at the expiry date the structured option outcome results in you buying the obligated amount on the sold leg of the option, then this will be a multiplier (up to two times) of the bought leg on the option.
b) A leveraged structured option may not provide you with a fully hedged position (protection against adverse currency movement), when being used to hedge a fixed amount of currency exposure. This is because the obligated amount would match the fixed currency exposure, and this amount will be a multiplier (up to two times) the protected amount.
c) The use of leverage can result in difficulties in managing currency exposure, as the amount you will be obligated to exchange may not be known until the expiry date of the structured option.

Barriers (Knock-In and Knock-Out)

Structured Options may incorporate a knock-in or knock-out barrier to enhance the participation and protection rates achievable. A barrier is a feature of the sold leg of a structured option that if triggered will either activate (knock-in barrier) or terminate (knock-out barrier) the underlying option. A barrier is triggered if the spot rate reaches the barrier rate during the barrier period.

Risks of Option Barriers

Barriers add complexity and uncertainty as to the actual participation and protection rates afforded by an option. A favourable market move could be completely nullified if a knock-in barrier is triggered; or a contract (and its protection) could be completely terminated if a knock-out barrier is triggered. Knock-out barriers are generally not suitable for hedging purposes.

Close-Out/Cancellation

You may request to close out or cancel your forward or option at any time where you no longer require the currency that you have agreed to purchase on the expiry date. Any close out or cancellation is subject to approval by Corpay and may be declined by Corpay at its sole discretion. Any costs that are incurred in terminating and unwinding your derivative will be payable by you. You will also be liable for any OTM position in relation to your forward or option. Corpay may require supporting documentation confirming a change in your currency obligations to support your request for the close-out or cancellation.

Termination of an Option

Corpay may terminate a forward or option contract in limited circumstances. You will be liable for any losses or costs incurred as a result of any termination event. The circumstances in which a termination event may be carried out are set out in full in the Master Terms and Conditions.

Margin Deposits

Forwards and structured options may require margin deposits at initiation or at a pre-determined mark-to-market valuation. Client margin deposits are segregated, however, as per the Terms and Conditions margin deposits may be used by Corpay to meet its counterparty margin requirements.

System Risks

Corpay relies on technology to provide our trading facilities to you. A disruption to the facility may mean you are unable to trade when you want to. Alternatively, an existing transaction may be aborted as a result of a technology failure.

Operational Risks

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or external events. It is possible that process problems at Corpay may lead to delays in the execution and settlement of a transaction.

Transactions Are Not Transferrable

As each transaction you enter into with Corpay is a transaction between you and us and is not traded on an exchange or market, you will not be able to sell, transfer or assign the transaction to any other person without our prior consent.

Abnormal Market Conditions or Force Majeure

We reserve the right to close out some or all of your open transactions between you and us if an event occurs that is beyond your or our control, where such event either wholly or partially prevents, hinders, obstructs, delays or interferes with your ability to meet your obligations.

Taxation

Foreign exchange derivatives require special consideration for income tax purposes. You should consult your tax advisor prior to entering into derivatives transactions.

Legal

Foreign exchange derivatives require special consideration with regard to legal and contractual matters. You should consult your legal advisor prior to entering into derivatives transactions.

Corpay's Regulatory Approval

Corpay is not registered under the securities, commodity futures or derivatives laws of any jurisdiction of Canada. Client assets are not protected under the Canadian Investor Protection Fund (CIPF), the U.S. Securities Investor Protection Corporation, or equivalent protections.

Corpay offers services connected to foreign exchange derivative hedging solutions to our customers under the framework outlined in the Exemptive Relief Application in Multiple Jurisdictions granted by the Ontario Securities Commission. The full detail of the decision to grant the exemption relief can be found here.

Corpay.com

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