Recent regulatory developments that affect our trading relationships

As you may be aware, there are four recent regulatory developments that affect trading relationships between counterparties which, in turn, require amendments to the trading agreements Russell Investments ("RI", "we" or "us") has executed on your behalf. We are writing to provide you with a high-level summary of these developments (as further detailed in Annex A) and to explain the actions we are taking on your behalf as a result of these new regulations. The four regulatory developments are:

Margin Requirements for Uncleared Swaps

Several G20 regulators have promulgated, or are in the process of promulgating, uncleared margin rules ("UMR") requiring the posting of initial margin and/or variation margin by certain counterparties entering into uncleared swaps. Note that some UMR may apply to certain foreign exchange transactions.

You will be required to post and collect variation margin as of March 1, 2017. If and when you are required to post and collect regulatory initial margin will depend on your aggregate average notional amount ("AANA") across all relevant transactions (as specified in the applicable UMR), entered into by you or on your behalf, during a specific period of time. AANA thresholds, calculations and the types of derivative transactions subject to UMR vary depending on the jurisdiction that is relevant to the trade. We recommend that you consult with your counsel to determine your AANA and whether you may be required to post and collect initial margin prior to September 1, 2020.

Our expectation is that you will not be required to post and collect initial margin until September 1, 2020, if at all.

Please let us know immediately if you believe that you will be required to post and collect initial margin from September 1, 2020 or any sooner.

Special Resolution Regimes ("SRR")

To facilitate the orderly resolution of financial institutions, several G20 regulators have promulgated, or are in the process of promulgating, rules which, among other things, temporarily impose stays on certain contractual termination rights of a counterparty to a financial institution in the event of the resolution of such financial institution.

European Union's Bank Recovery and Resolution Directive ("BRRD")

The BRRD establishes a resolution regime for European Union ("EU") financial institutions which gives resolution authorities in EU member states certain "bail-in" powers, including the power to write-down and/or convert into equity certain liabilities of a financial institution in resolution.

With respect to both the SRR and the BRRD, to ensure the enforceability of stays and bail-in powers in cross-border transactions, the resolution authorities' rules include a prohibition on financial institutions from entering into financial contracts where the governing law of the contract is not the law of the jurisdiction of the financial institution (or the law of an EU member state with respect to an EU entity), unless the counterparty to such financial contract recognizes the enforceability of the resolution authority's power to suspend contractual termination rights, and/or exercise its bail-in powers. EU financial institutions trading under New York law governed contracts are required to ensure their counterparties contractually recognize such suspension and bail-in powers.

Internal Revenue Service Regulations regarding Dividend Equivalent Transactions ("Section 871(m)")

Regulations under Section 871(m) of the U.S. Internal Revenue Code subject dividend equivalent payments made to foreign persons under certain equity derivatives with U.S. underliers to a withholding requirement.

In connection with each regulatory development, parties subject to the new rules are required to amend trading documentation with their counterparties to ensure regulatory compliance (UMR, SRR and BRRD) or to appropriately allocate tax payment responsibility (Section 871(m)). The International Swaps and Derivatives Association ("ISDA") has produced amendment protocols for purposes of facilitating the required amendments. These protocols allow counterparties to meet their regulatory requirements or allocate risk, by amending their trading agreements with their trading counterparties through adherence to the protocols. Some protocols will also require filling out questionnaires and matching through ISDA Amend, a joint service provided by HIS Markit Ltd. and ISDA.

We have been informed that, to the extent an amendment is required, dealers will only trade with those clients who have made the relevant amendment prior to the implementation date applicable to the relevant regulation. Thus, RI plans to adhere to the ISDA protocols (or negotiate bilateral amendments to your trading agreements) on your behalf prior to the relevant implementation deadline. Please note that we intend to take these steps if we trade on your behalf under RI trading agreements. However, if we trade under your trading agreements, you will need to determine how to amend your documents to address the regulatory requirements.

While we will proceed as described above to ensure that you can continue to trade with your counterparties after the applicable implementation dates, we continue to monitor, manage and mitigate counterparty credit risk on your behalf. Should you have any concerns after reviewing this communication, please contact your relationship team.

Annex A

Margin Requirements for Uncleared Swaps

As a result of the Global Financial Crisis, the 2009 G20 Summit in Pittsburgh developed a framework aimed at improving the bilateral over-the-counter derivatives ("OTC") markets. The recommendations with regard to OTC trades were to:

- Move standardized trades to electronic trading platforms or exchanges
- Clear trades on exchanges
- Report trades to a trade repository
- Require margin for uncleared derivatives

Both the US and the EU were early adopters in terms of proposing rules pertaining to trading, clearing and reporting. Indeed, Russell Investments ("RI") has worked with many derivatives clients since 2012 to complete the necessary steps to achieve these G20 principles. The US, EU and several other jurisdictions have now promulgated rules with respect to the posting and collection of margin for uncleared swaps.

For some clients, these new rules imposing the posting and collection of margin on OTC derivative trades may not result in significant changes in the short term. The margin rules have two components, initial margin and variation margin. Few, if any, RI clients currently post initial margin. Initial margin under the new rules is subject to a phase-in schedule which extends to 2020 and is triggered by the average notional amount of derivatives calculated over a specific period of time, depending on the applicable jurisdiction. After reviewing our current client base, we assume that few, if any, clients will need to post or collect regulatory initial margin. If you believe that you will be required to post and collect initial margin, please let us know as soon as possible. The second component is variation margin. It is market standard to move variation margin on all bilateral OTC instruments except for foreign exchange transactions ("FX"). If you trade FX transactions and would like more information on how the margin rules may impact your trades, please see the article by Joe Hoffman, Director, Global Head of Currency, *"Uncleared margin rules, Currency investors brace for change".*

The new rules impose requirements as to the frequency of exchange of variation margin, the type of collateral that can be posted to satisfy these requirements and the types of transactions that are subject to the rules. Unfortunately, the new global uncleared margin rules are not consistent, and different requirements will apply based on the regulation applicable to the trade.

To comply with the relevant margin rules, counterparties will be required to enter into or amend Credit Support Annexes to reflect the strictest set of rules applicable to their trades. The International Swaps and Derivatives Association ("ISDA") has a produced the ISDA 2016 Variation Margin Protocol (the "VM Protocol") to facilitate the implementation of these amendments. RI will either amend your existing trading agreements bilaterally or adhere to the VM Protocol on your behalf, to ensure compliance with the uncleared margin rules.

We may contact you at a later date to update our information and obtain further details from you for margin purposes.

Special Resolution Regimes and the European Union's Bank Recovery and Resolution Directive

The new regulatory requirements apply directly to banking organizations. They require the banking organization to include certain contractual terms in certain types of trading agreements that the banking organizations may enter into. As a consequence, various banking organizations have been, or soon will be, requiring their counterparties to amend trading agreements to include these new terms.

Overview. Various regulatory initiatives in recent years have targeted "too-big-to-fail" banking organizations. Two of those initiatives, both of which are international in scope, concern what happens when a banking organization becomes subject to resolution proceedings. The first of the initiatives relates to limitations applicable during resolution proceedings that restrict, or "stay", the exercise of termination rights by the bank's counterparties under certain trading agreements, including swap and other derivative agreements, as well as repo and securities lending agreements. The second initiative relates to the ability of resolution authorities in the European Union to modify, or "bail in", certain liabilities, including certain trading liabilities, of banks that are in resolution.

In connection with each regulatory initiative, banking organizations subject to the new rules are required to amend trading documentation with their counterparties. ISDA has produced amendment protocols for purposes of facilitating the mandated amendments. Each regulatory initiative and its related documentation requirements are summarized below.

Special Resolution Regimes

Limitations on Certain Termination Rights. Special resolution regimes in the United States, the European Union, Japan and other countries empower regulators that take over a failed banking organization to impose temporary stays on the exercise of certain transaction termination rights. Typically, the stays prevent counterparties from terminating trades for a period of one or two business days, while resolution authorities try to resolve and reorganize the troubled bank in a manner that permits some operations – including trading relationships – to continue. Transactions that are subject to such stays include swap and other derivative transactions governed by ISDA master agreements, and repo and securities lending transactions governed by other industry-standard master agreements. Such agreements are generally referred to below as "trading agreements."

Regulatory authorities in several jurisdictions – principally, the United States, the United Kingdom, Germany, France, Switzerland and Japan – have become concerned that the cross-border enforceability of stays under their national resolution regimes is not entirely certain. For example, UK regulatory authorities are not certain that a New York court would respect a UK stay of termination rights under a trading agreement that is governed by New York law. Accordingly, a number of regulatory authorities are requiring banking organizations to amend their trading agreements to include provisions under which counterparties contractually acknowledge the enforceability of such stays; this removes concern about cross-border enforcement. The largest international banking organizations have already amended trading agreements among themselves. Now, in connection with the adoption of new regulatory requirements in various jurisdictions, banking organizations must amend trading agreements with non-bank counterparties as well.

The new regulations require a banking organization to amend its trading agreements that are not governed by the laws of its jurisdiction (or the law of an EU member state with respect to an EU entity) before further transactions may be executed under the agreement; in the absence of such amendment, the banking organization would likely not be permitted to trade further under the agreement. ISDA has published an amendment protocol that, for parties that adhere to it, achieves the necessary amendments of existing trading agreements. The protocol covers ISDA master agreements, and also non-ISDA master agreements (such as master repo agreements). The protocol is called the ISDA Resolution Stay Jurisdictional Modular Protocol, or "JMP" for short.

Each relevant national jurisdiction will impose requirements on its own banking organizations. Thus, industry participants may adhere to the JMP on a jurisdiction-by-jurisdiction basis, may amend agreements to incorporate terms of the JMP by reference, or may otherwise amend agreements to comply with the requirements in each separate jurisdiction. For example, adherence or other amendments for purposes of UK regulations and UK banking organizations will be separate from adherence or other amendments for purposes of German regulations and German banking organizations. For those countries, as well as others, adherence or other amendments will result in contractual changes to confirm the cross-border enforceability of the respective country's resolution regime stay provisions for certain existing agreements and for future agreements.

In the case of large U.S. banking organizations, amendments to trading agreements are expected to have a second consequence. Like authorities in other countries, U.S. authorities have proposed rules that would require trading agreement amendments to ensure the cross-border enforceability of U.S. resolution stay provisions (under the special resolution regimes in the United States for systemically important financial institutions and for FDIC-insured banks). In addition, however, the proposed U.S. rules would require amendments that prevent or delay the exercise of certain cross-default rights that would be triggered by a wide variety of other insolvency proceedings, such as under Chapter 11 of the U.S. Bankruptcy Code. Thus, for example, trading agreements with the dealer subsidiary of a large U.S. bank holding company would need to be amended to limit the dealer's counterparties ability to exercise cross-default termination rights that are triggered because the parent bank holding company enters Chapter 11 reorganization proceedings. The rights affected concern both domestic agreements (e.g., an agreement between two U.S. entities governed by New York law) and cross-border agreements. The precise restrictions on cross-default rights will not be known until the rules are finalized by U.S. authorities sometime in the future.

European Union's Bank Recovery and Resolution Directive

Bail-in Powers. Under the EU bank resolution regime (the Bank Recovery and Resolution Directive, or "BRRD"), regulatory authorities have the power to bail in a broad range of liabilities of a troubled EU banking or financial institution that becomes subject to resolution proceedings. EU bail-in powers may be used to reduce and write down the liabilities of the relevant EU institution, or to convert those liabilities into equity. Liabilities subject to bail-in may include those generated under virtually any contract, including under various kinds of trading agreements; a few kinds of liabilities, including fully secured liabilities, are not subject to bail-in.

The BRRD requires EU institutions to include specific contractual provisions in various agreements that are governed by non-EU law. Under those provisions, counterparties must recognize, and agree to be bound by, an EU resolution authority's powers to write down or convert liabilities under such agreements. These contractual provisions reduce the risk, perceived by EU resolution authorities, that a non-EU court would not respect the exercise of such bail-in powers by an EU resolution authority.

Industry participants may effect necessary amendments to trading agreements by means of an ISDA amendment protocol published for that purpose, by amendments that incorporates terms of the protocol, or by other amendments to comply with the requirements. This protocol is called the ISDA 2016 Article 55 BRRD Protocol, or “Article 55 Protocol” for short. Unlike the JMP, the Article 55 Protocol calls for one-time adherence (rather than jurisdiction-by-jurisdiction adherence) to cover trading agreements with banking organizations in the relevant EU jurisdictions (France, Germany, Ireland, Italy, Luxembourg, the Netherlands, Spain and the United Kingdom). Upon adherence, trading agreements of clients which are governed by the laws of a non-EU jurisdiction, will be amended to include the mandated provision recognizing, and agreeing to be bound by, an EU resolution authority’s bail-in powers.

Internal Revenue Service Regulations regarding Dividend Equivalent Transactions (“Section 871(m)”)

Section 871(m). Enacted in 2010, Section 871(m) of the US Internal Revenue Code imposes withholding tax on certain dividend equivalent payments made to non-US persons. Affected transactions include certain swaps and other equity-linked instruments on US equities if the long party to the transaction is a non-US person. Prior to the enactment of Section 871(m), dividend equivalent payments made to a non-US person under swaps on US equities were generally not subject to U.S. withholding tax. . For transactions entered into on or after January 1, 2017, withholding will apply only to US equity-linked swaps and other derivatives that are deemed economically equivalent to an investment in the underlying US equities (so-called “delta-one” transactions). A broader range of US equity linked swaps and other derivatives (that have a “delta” of .8 or higher), including certain equity index option strategies, are folded in the rules starting January 1, 2018. Swaps and other instruments (including swaps on ETFs) that reference certain passive equity indices (“qualified indices”) are exempt from Section 871(m) withholding. Non-US long counterparties are expected to act through an entity that is not subject to 871(m) withholding, because the entity is acting as a Qualified Derivatives Dealer or is a US entity; in either case, our clients should not be required to withhold for Section 871(m) purposes.

To comply with these changes, counterparties will be required to amend their trading agreements. The 2015 Section 871(m) Protocol enables market participants to amend their ISDA Master Agreements to allocate the withholding tax to the party that takes the long position. RI will adhere to the ISDA 2015 Section 871(m) Protocol on your behalf before the end of 2016 to ensure compliance with these changes to the US tax laws.

Important information

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