

INFORMATION PAPER

RMB Equity Trading Support Facility (TSF)

October 2011



Hong Kong Exchanges and Clearing Limited
香港交易及結算所有限公司

CONTENTS

	Page No.
EXECUTIVE SUMMARY	1
PART 1 OVERVIEW OF THE TSF MODEL	3
PART 2 INPUT TSF REQUEST	6
PART 3 RMB FX RATES	7
PART 4 TSF FX SETTLEMENT	9
PART 5 EARMARKING AND DE-EARMARKING OF SHARES	20
PART 6 CORPORATE ACTIONS HANDLING FOR EARMARKED TSF STOCKS	26
PART 7 EXCEPTION MANAGEMENT	28
PART 8 SUSPENSION OF THE FX SERVICES AND RETIREMENT OF THE TSF	31
PART 9 REGISTRATION REQUIREMENTS	33
PART 10 FURTHER INFORMATION ABOUT THE TSF	36
 APPENDICES	
APPENDIX I CHECKLIST FOR TSF APPLICANTS	
APPENDIX II GLOSSARY	

EXECUTIVE SUMMARY

1. Since the announcement of a series of policy measures by Mainland regulators in 2010 which vastly expanded the opportunities for offshore renminbi (“RMB”) business, Hong Kong Exchanges and Clearing Limited (“HKEx”) has strived to engage market participants to prepare for the listing, trading and clearing of RMB products in its markets.
2. The introduction of RMB products is one of the key initiatives in HKEx’s Strategic Plan 2010-2012. As of 7 October 2011, nine RMB-traded debt securities and one RMB REIT were listed. While the Initial Public Offering (“IPO”) process, trading and clearing of RMB products have been well tested, there is increasing interest in the market in the introduction of equities to be traded in RMB.
3. RMB-traded equities are important to the further development of the offshore RMB market in Hong Kong, but the long-term growth and stability of a RMB stock market segment at HKEx is subject to the challenge of whether there is sufficient and reliable RMB liquidity in Hong Kong. HKEx plans to introduce a RMB Equity Trading Support Facility (“TSF”) to help overcome this possible hindrance.
4. The primary objective of the TSF is to serve as a back-up facility to enable investors to buy the shares of RMB-traded equities (“RMB Shares”¹) in the secondary market with Hong Kong dollars (“HKD”) if they have difficulty obtaining RMB.
5. The TSF will source RMB from one or more banks (“TSF Partner Banks”) in Hong Kong and provide the RMB through its participating brokers to investors who wish to buy RMB Shares in the secondary market. The TSF’s RMB-HKD exchange rates will be set on a commercial basis by the TSF Partner Banks. When investors sell the RMB Shares later on, they will have to return the RMB proceeds to the TSF for the equivalent amount of HKD at the TSF’s exchange rate at that time. This so-called “HKD in HKD out” mechanism will ensure that the RMB supplied by the TSF stays in the secondary market and that the offshore RMB market in Hong Kong remains intact.
6. The design of the TSF will ensure the liquidity of RMB Shares in the secondary market will not be constrained by the prevailing level of RMB in the market at any given time.
7. The TSF will be optional for investors as well as brokers and custodians. Investors may choose to use the TSF via participating brokers when they cannot source RMB from other channels. Brokers and custodians may choose to participate in the TSF after considering their business operations and customers’ needs.
8. This information paper explains the detailed operating flows of the TSF. While the TSF will operate on the trading and clearing platforms of HKEx, the paper contains a lot of technical information which are only of relevance to those market players who are interested in participating in the TSF. For those investors who want to understand

¹ For easy understanding, “RMB Shares” in this paper refers to shares being traded on the Stock Exchange of Hong Kong Limited in RMB which are supported by the TSF (please refer to paragraph 1.12 for further explanation).

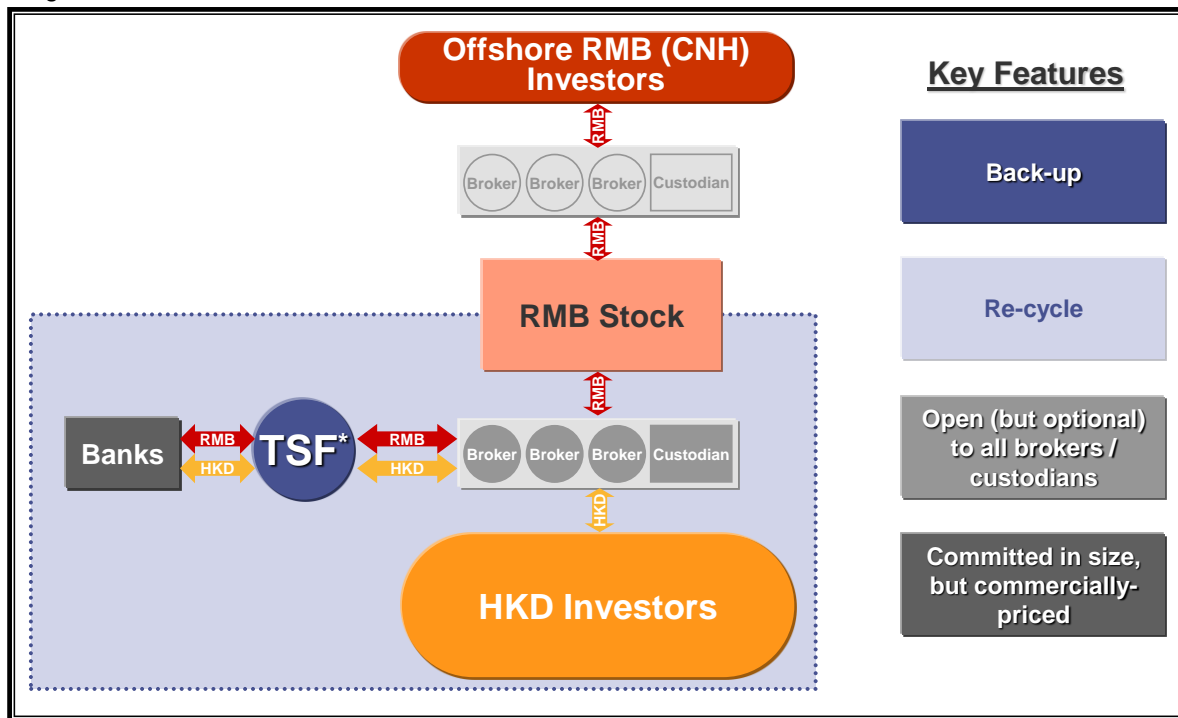
EXECUTIVE SUMMARY

more about the TSF, information provided in this Executive Summary and the following section “Overview of the TSF Model” should suffice.

9. Market players who are interested in participating in the TSF can refer to Part 9 of this paper for the registration requirements and the participant circulars at the TSF web corner for the registration procedures.

PART 1: OVERVIEW OF THE TSF MODEL

Diagram 1: Overview of the TSF model



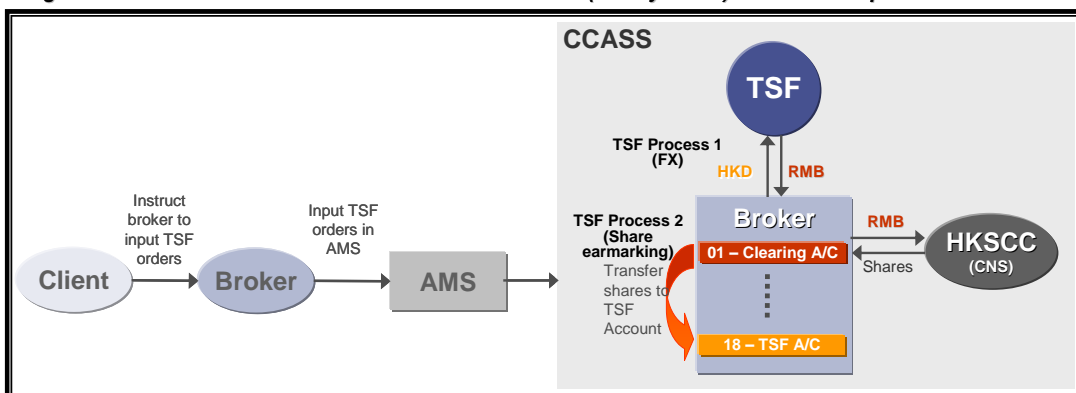
- 1.1 In addition to existing channels (such as licensed banks and brokers) where RMB can be exchanged or sourced, the TSF is designed to serve as a back-up facility to enable investors to buy RMB Shares in the secondary market with HKD.
- 1.2 The TSF will be operated by HKEx's securities clearing house, the Hong Kong Securities Clearing Company Limited ("HKSCC"). Investors can use the TSF through those brokers who have participated in the facility.
- 1.3 Brokers who are participants of the Stock Exchange of Hong Kong Limited ("SEHK") (the participants are referred as Exchange Participants or "EPs") are free to participate in the TSF, but they have to comply with certain requirements to become participating brokers. Among others, they have to be able to settle with the TSF after they have requested for its foreign exchange services ("TSF FX Services"). As the TSF FX settlement process will take place on the clearing platform operated by HKSCC (i.e. "CCASS" or Central Clearing And Settlement System), it means a TSF participating broker needs to either be a CCASS Participant, or appoint a CCASS Participant who has participated in the TSF to settle with the TSF on its behalf. The details of the settlement flow and the registration requirements are explained in Part 4 and Part 9 of this paper².
- 1.4 The TSF will source RMB from one or more banks in Hong Kong ("TSF Partner Banks") and provide the RMB through its participating brokers to investors who wish to buy RMB Shares in the secondary market. The TSF executes FX transactions with its participating

² Besides brokers, a custodian which is a CCASS Participant can also participate in the TSF, such that it can hold and act as the custodian of the RMB Shares purchased by their investor clients through the TSF FX Services.

brokers on a principal to principal basis. Upon request from a broker to use the TSF FX Services, the TSF will execute back-to-back FX transactions with its TSF Partner Banks. Each of the TSF Partner Banks will commit to execute FX transactions with the TSF up to a prescribed limit on a daily basis.

- 1.5 The FX rates used by the TSF (“RMB FX Rates”) will be set on a commercial basis by the TSF Partner Banks.
- 1.6 Through participating brokers, investors will pay HKD to buy RMB Shares. When they sell those shares later on, they will have to return the RMB proceeds to the TSF for the equivalent amount of HKD at the TSF’s RMB FX Rate at the time of sale. This so-called “HKD in HKD out” mechanism (or “recycle” concept) will ensure that the TSF is sustainable without access to an unlimited supply of RMB. It will also ensure that the RMB supplied by the TSF stays in the secondary market and that the offshore RMB market in Hong Kong, or the CNH market, remains intact.
- 1.7 For the purpose of maintaining the “HKD in HKD out” principle, RMB Shares purchased by a participating broker via the use of the TSF will be earmarked in a designated stock account (“TSF Account”) of that broker in CCASS³. When the broker sells the earmarked shares later on, it has to return the relevant RMB trade proceeds to the TSF to exchange for the equivalent amount of HKD. The TSF will de-earmark the shares for it to settle its trade.
- 1.8 Participating brokers who want to use the TSF FX Services should indicate their intention in the buy or sell order on the trading platform operated by SEHK (i.e. “AMS” or Automatic Order Matching And Execution System). Subject to the instructions of their respective clients, brokers may use the TSF FX Services for one trade, and not for another.
- 1.9 Participating brokers who have indicated their intention to use the TSF FX Services in a buy or sell order will settle with the TSF two days later (i.e. T+2). The settlement will take place on the CCASS platform. Basically, the TSF settlement process consists of two parts: execute FX transaction, and earmark (for buy trades) or de-earmark shares (for sell trades).

Diagram 2: TSF executes FX transaction and earmarks shares (for buy trades) on the CCASS platform on T+2



³ RMB Shares earmarked by the TSF are subject to certain restrictions. For example, an investor cannot directly withdraw shares certificates for earmarked shares. The restrictions applicable to earmarked shares and the relevant operating procedures are detailed in Part 5 of this paper.

-
- 1.10 TSF FX transactions will be settled through the existing CCASS money settlement channels while earmarking/de-earmarking of shares are done automatically by CCASS. Participating brokers can refer to the new CCASS daily reports to prepare for their funding position two days later, and reconcile with their back office records after completion of the TSF settlement process.
- 1.11 Trades executed on AMS are in principle settled in CCASS under the Continuous Net Settlement (“CNS”) system. It should be noted that the TSF will NOT change this CNS mechanism. A participating broker may have executed many trades in RMB Shares on a day, some using the TSF and some not. All of such trades will continue to settle under the CNS system in RMB. The FX transactions and share earmarking/de-earmarking are additional activities between the participating broker and the TSF.
- 1.12 The TSF is operated on the support of the TSF Partner Banks, and is subject to the size of funds committed by them. Without access to an unlimited supply of RMB, the TSF will be prudent at its initial launch, where it will focus on supporting the trading of RMB Shares. After times the TSF may consider expanding its service scope to other products. A list of “TSF Stocks” will be posted onto the HKEx website for investors’ and market players’ reference.
- 1.13 By the same token, the TSF will focus on supporting the trading of RMB Shares on the secondary market, and will NOT support fund raising activities initially, including IPO and post-listing fund raising activities such as rights subscription.

PART 2: INPUT TSF REQUEST

- 2.1 A participating broker who wants to use the TSF FX Services to buy and sell RMB Shares should indicate its intention when it inputs the respective buy or sell order into AMS:
- a) *Use the TSF FX Services to buy RMB Shares:* A buy order requesting for the TSF FX Services must be input in the form of an at-auction order (during pre-opening session) or a special limit order⁴, odd lot order and special lot order⁵ (during continuous trading sessions) and be identified with the indicator “TSF”⁶ in the first three characters of the reference field or BSS broker comment field at the time of order input;
 - b) *Use the TSF FX Services to sell RMB Shares:* A sell order requesting for the TSF FX Services can be input in the form of any order types but must be identified with the indicator “TSF” specified in the first three characters of the reference field or BSS broker comment field at the time of order input.
- 2.2 A broker may withdraw its request for the TSF FX Services before the respective buy or sell order is matched by removing the “TSF” specification from the reference field or BSS broker comment field.
- 2.3 Once the buy or sell order with the proper indication of requesting for the TSF FX Services is matched and becomes a trade (“TSF Exchange Trade”), the request for the TSF FX Services is irrevocable.
- 2.4 Brokers should be aware that the request to use the TSF FX Services applies to all shares of the respective order. If an investor client wants to execute an order partly by using its own RMB and partly by using the RMB provided by the TSF FX Services, the participating broker should split the order into two separate orders (i.e. an order requesting for the TSF FX Services and another order not using the TSF FX Services).
- 2.5 Shares purchased via the use of the TSF FX Services will be earmarked in the relevant broker’s TSF Account in CCASS. When such shares are subsequently sold on the market, the broker must use the TSF FX Services by specifying in the relevant sell order. Once specified in the sell order, it represents a request of the broker to de-earmark the shares from the TSF Account for trade settlement and sell the RMB proceeds to the TSF in exchange for HKD.

⁴ Any outstanding at-auction order or special limit order after matching will be cancelled automatically and will not be stored in AMS. This feature will ensure buy orders specified for using the TSF FX Services will be settled with certainty via the TSF until the fund is fully utilized and investor clients can be confirmed with the execution immediately.

⁵ Odd lot orders and special lot orders (e.g. order at a price less than \$0.01 with quantity more than one board lot) shall be input into AMS by using the operation specified for odd lot transactions.

⁶ The word “TSF” must be in capital letters when being input into the BSS broker comment field or the reference field. Otherwise, the respective order will NOT be considered for the TSF FX Services.

PART 3: RMB FX RATES

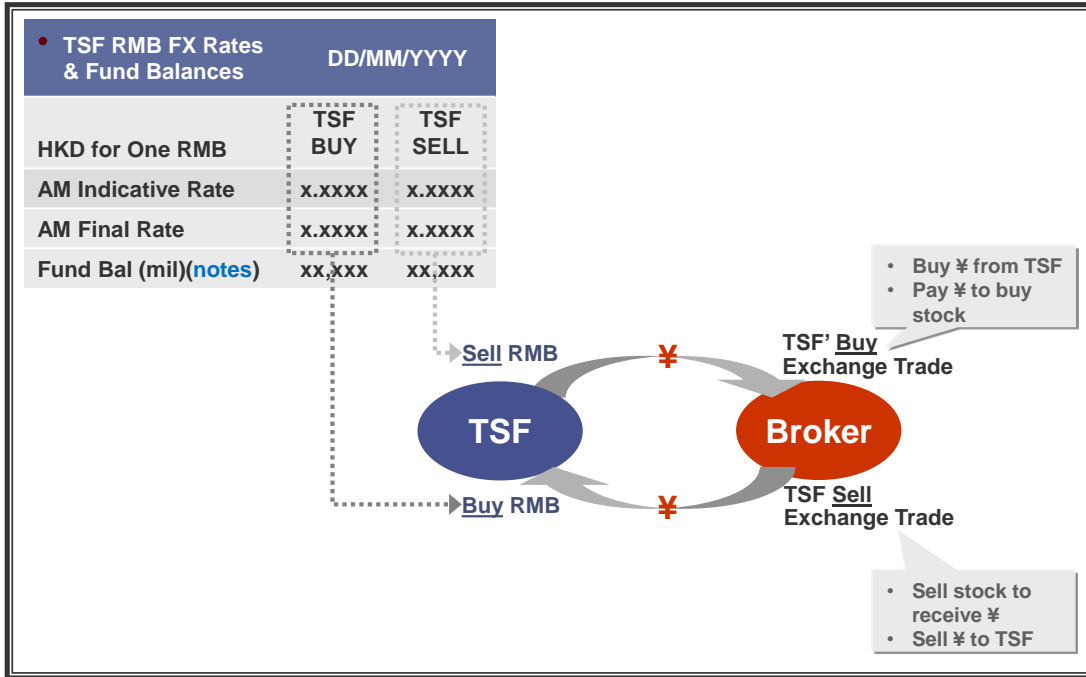
- 3.1 There will be two types of RMB FX Rates published to the market:
- a) RMB Indicative FX Rates: The RMB Indicative FX Rates, published at the beginning of the morning session and the afternoon session respectively, are indicative rates that represent the RMB Sell FX Rate (for TSF to sell RMB to participating brokers) and RMB Buy FX Rate (for TSF to buy RMB from participating brokers) for the TSF Exchange Trades concluded in the respective trading session.
 - b) RMB Final FX Rates: The RMB Final FX Rates, published shortly after each trading session, represent the actual FX rates applied to TSF Exchange Trades concluded during the trading session before the publication of the actual FX rates.
- 3.2 RMB Final FX Rates will always be equal to or better than the RMB Indicative FX Rates of the respective trading session (i.e. RMB Sell Final FX Rate will not be higher than the RMB Sell Indicative FX Rate and RMB Buy Final FX Rate will not be lower than the RMB Buy Indicative FX Rate).
- 3.3 For the morning session⁷, the RMB Indicative and Final FX Rates will normally be available at around 9:30 a.m. and 12:45 p.m. respectively. For the afternoon session, the RMB Indicative and Final FX Rates will normally be available before 1:00 p.m. and at around 4:45 p.m. respectively.
- 3.4 The TSF will publish the RMB FX Rates (for buying and selling RMB) on the HKEx website. Following the existing practice of the FX market, the RMB FX Rates will be quoted from the perspective of the TSF. For a TSF Buy Exchange Trade, the TSF will sell RMB to the participating broker for it to buy RMB Shares and therefore will apply the relevant RMB Sell Final FX Rate for calculating the FX obligations. Similarly, for TSF Sell Exchange Trades, the RMB Buy Final FX Rate will be applied.
- 3.5 All TSF Exchange Trades executed in the same trading session (i.e. morning session including pre-opening session; and afternoon session) are subject to the same RMB FX Rates. However, different RMB FX Rates may apply to different trading sessions depending on market conditions.

Example 1: TSF FX Rates on the HKEx website

• TSF RMB FX Rates & Fund Balances	DD/MM/YYYY	
	TSF BUY	TSF SELL
HKD for One RMB		
AM Indicative Rate	x.xxxx	x.xxxx
AM Final Rate	x.xxxx	x.xxxx
Fund Bal (mil)(notes)	xx,xxx	xx,xxx

⁷ The RMB FX Rates of the morning session are also applicable to trades concluded during the pre-opening session.

Diagram 3: TSF's RMB FX Rates vs. TSF Exchange Trades



PART 4: TSF FX SETTLEMENT

FX settled on a net basis on T+2 through the CCASS money settlement mechanism

- 4.1 Participating brokers who have executed TSF Exchange Trades on T-day will settle the relevant FX transaction with the TSF on T+2⁸.
- 4.2 A broker may have executed different buy and sell TSF Exchange Trades on a day. The TSF will calculate the broker's FX obligation for each TSF Exchange Trade on a gross basis, but only require the broker to settle the FX obligations with it on a net basis.
- 4.3 To settle the FX transaction, the TSF will only make payment to the broker after the transaction amount of the opposite currency is received in full. These collection and payment activities will be done by using the existing CCASS money settlement mechanism.

FX settled through RTGS, bank transfer and CCASS day end money settlement

- 4.4 As further elaborated in the following paragraphs, the collection and payment activities of the FX transactions may be done at different times on T+2, subject to the broker's CNS settlement obligations and status.
- 4.5 In any case, if a broker needs to make payment to the TSF during the day (and in normal cases before 3 p.m.), the TSF will collect the money through a mechanism similar to the existing CCASS cash prepayment arrangement. The broker can maintain standing instruction with CCASS for it to issue CHATS Payment Instructions ("CPI") to the broker's designated bank for payment through the Real Time Gross Settlement ("RTGS") system of the Hong Kong Interbank Clearing Limited ("HKICL").
- 4.6 Alternatively, the broker can pay the TSF through other means such as bank transfer. Where the broker is not required to make payment to the TSF during the day before 3 p.m., the TSF will collect the money from the broker through CCASS's day end money settlement mechanism by debiting the broker's CCASS Money Ledger.
- 4.7 The TSF will make payment to the broker to settle the FX transaction by crediting the broker's CCASS Money Ledger. The broker will receive the money from the TSF through CCASS's day end money settlement mechanism.

Participating brokers make payment to HKSCC's agent bank accounts

- 4.8 Brokers who need to make payment to the TSF through RTGS or bank transfer during the day should pay to the bank accounts of the TSF opened with HKSCC's agent banks. Any payment in HKD should be paid to HKSCC's designated bank account opened with HSBC. Any payment in RMB should be paid to HKSCC's designated bank account opened with Bank of China (Hong Kong).

⁸ The TSF will settle the FX transaction with the broker on the day when the broker settles the relevant trade with HKSCC, which is normally on T+2. In cases where trade settlement is deferred due to the hoisting of Typhoon Signal No.8 or above or issue of Black Rainstorm Warning, the TSF will also defer the settlement of the FX transaction accordingly.

How to calculate a participating broker's payment obligations?

4.9 **Two ways to reduce brokers' liquidity pressure:** A broker may have executed TSF Buy and Sell Exchange Trades on a day, each of which represents a commitment of the broker to execute FX transaction with the TSF. The TSF normally requires a broker to make the required payment by 3 p.m. on T+2 via RTGS or bank transfer, such that the TSF can pay the corresponding money to the broker on the same day. In order to reduce brokers' liquidity pressure, the TSF will nevertheless consider two things in determining a broker's payment obligations:

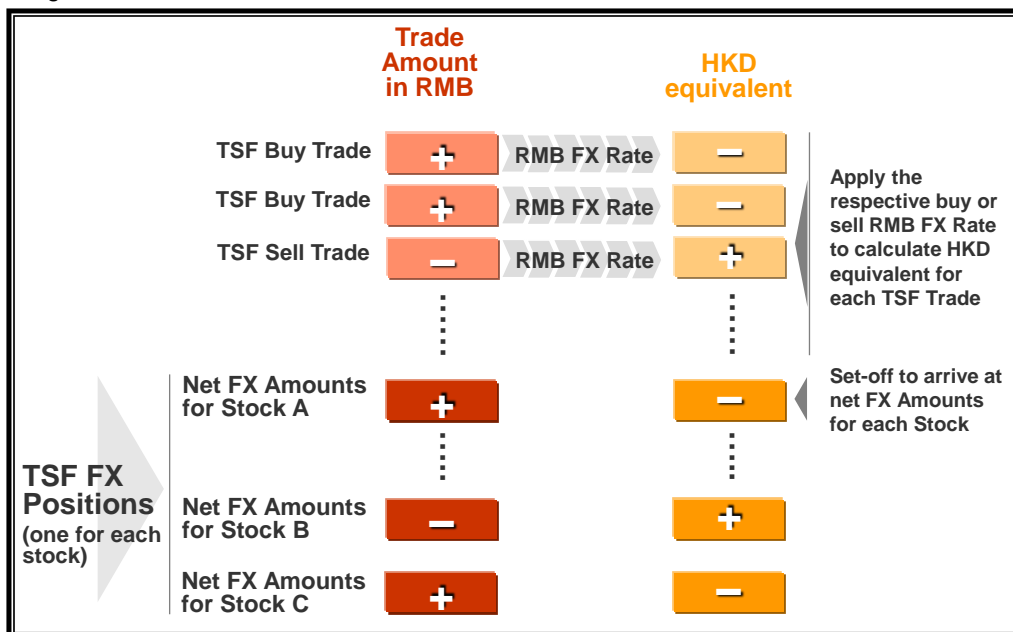
- a) if the broker needs to pay RMB to the TSF, the TSF will use the broker's CNS receivable monies of the respective stock to cover its RMB payment obligation as far as possible; and
- b) apply netting across FX amounts as far as possible.

The following paragraphs explain the details of how the TSF will calculate a broker's payment obligations, at what time and in what amount.

4.10 **Calculate HKD equivalent for each trade:** Depending on in which trading session a TSF Exchange Trade is executed, the TSF will apply the respective buy / sell RMB Final FX Rate to the TSF Exchange Trade to calculate the HKD equivalent of the trade amount.

4.11 **Calculate the TSF FX Position for each stock:** The TSF will then aggregate the RMB trade amounts and their HKD equivalent amounts of all TSF Exchange Trades of each stock respectively. After aggregation, a broker will have a TSF FX Position for each of the stock that it has executed TSF Exchange Trades. Each TSF FX Position will normally have a net RMB amount and a net HKD amount, where the broker will need to pay HKD to the TSF in exchange for RMB, or vice versa.

Diagram 4: TSF FX Position for each stock



Example 2: Calculate TSF FX Position for a stock

A participating broker executed 3 TSF Trades in Stock A on a day:

	Trade Amount in RMB	RMB Final FX Rate	HKD Equivalent
TSF Buy Trade	¥ 100 +	1.17	\$ 117 –
TSF Buy Trade	¥ 400 +	1.19	\$ 476 –
TSF Sell Trade	¥ 200 –	1.16	\$ 232 +
TSF FX Position for Stock A	¥ 300 +		\$ 361 –

For Stock A, the participating broker is expecting to pay HK\$361 to the TSF in exchange for RMB300

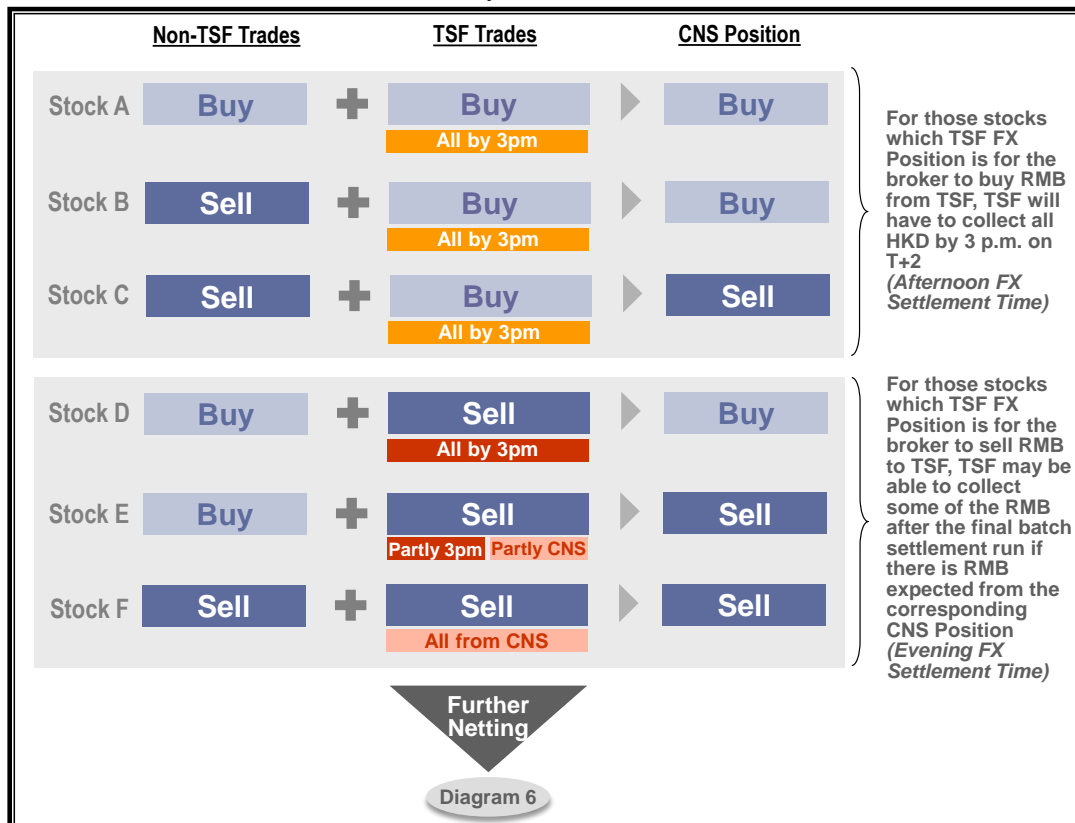
- 4.12 **Compare TSF FX Position with CNS Position to determine the FX amount to be paid by the broker in cash by 3 p.m. and the amount to draw on CNS receivables:** The TSF may require a broker to settle its payment obligation with respect to a TSF FX Position at different times on T+2:
- a) For those TSF FX Positions which are for the broker to pay HKD to the TSF, the HKD will be designated for collection by 3 p.m.
 - b) For those TSF FX Positions which are for the broker to pay RMB to the TSF, a portion or the whole sum of the RMB amount may be collected after CNS settlement:
 - The TSF will compare the FX RMB amount with the corresponding CNS position amount.
 - If the corresponding CNS position is a net buy position (which means the broker will not receive any RMB from HKSCC for the CNS position), the FX RMB amount will be designated for collection by 3 p.m.
 - If the corresponding CNS position is a net sell position, where the RMB receivable amount of the CNS position can cover, the TSF will collect the FX RMB amount from the broker after the CCASS final batch settlement run⁹ on T+2 when the CNS position should have settled, the remaining amount which cannot be covered by the CNS receivable monies will be designated for collection by 3 p.m.

⁹ CCASS executes four batch settlement runs a day, respectively at 10:30 a.m., 12:00 noon, 2:00 p.m. and 3:45 p.m.

c) By going through this process, the TSF will segregate the TSF FX Positions of different stocks into two batches:

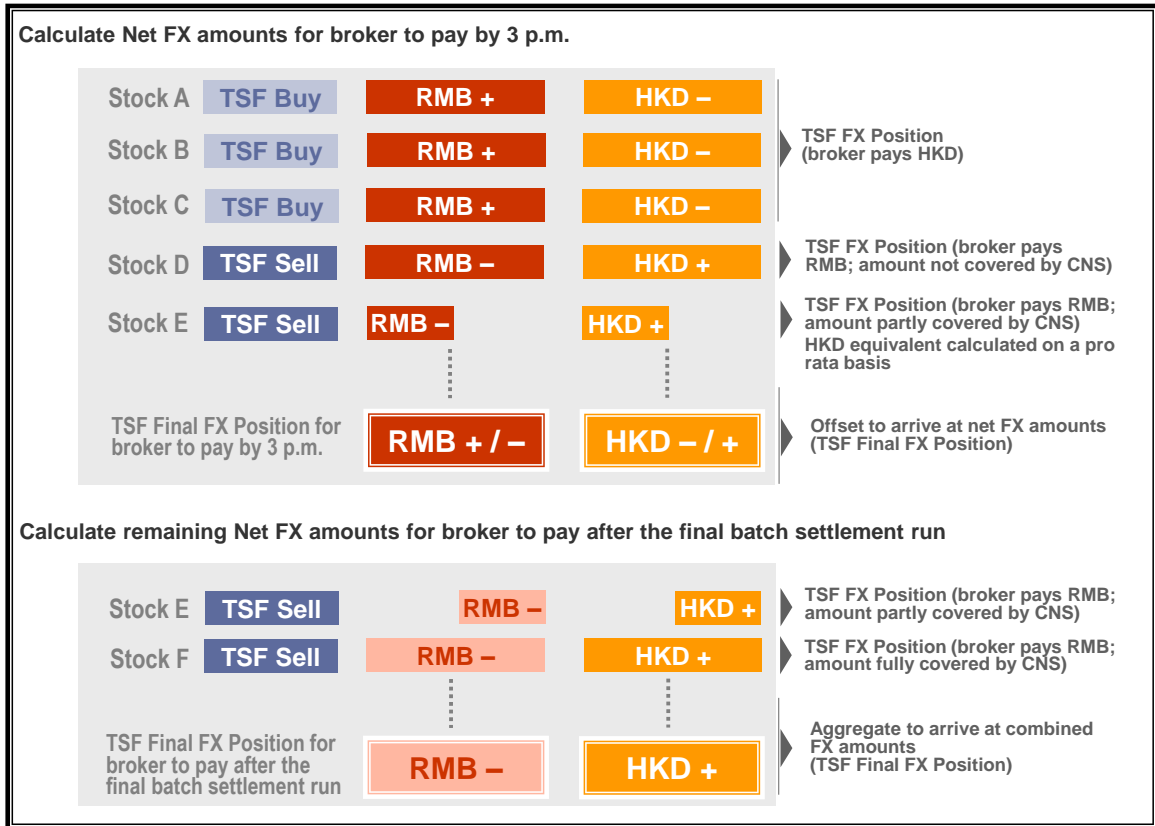
- One batch to collect payment from the broker by 3 p.m. (i.e. the “Afternoon FX Settlement Time”): Within this batch, there are TSF FX Positions of those stocks that the broker has to pay HKD to the TSF in exchange for RMB, and also the TSF FX Positions of those stocks that the broker has to pay RMB (the whole or a portion of the FX amount which is not covered by any CNS receivable monies) to the TSF in exchange for HKD; and
- Another batch to collect payment from the broker after the CCASS final batch settlement run (i.e. the “Evening FX Settlement Time”): TSF FX Positions within this batch are only for the broker to pay RMB to the TSF in exchange for HKD, and the FX RMB amount can be covered by the broker’s CNS receivable monies.

Diagram 5: Separate TSF FX Positions into two batches (pay by 3 p.m. and pay after final batch settlement run) – check if RMB amount can be covered by CNS receivable monies



4.13 **Netting across different stocks to arrive at a TSF Final FX Position:** While the 3 p.m. batch may contain TSF FX Positions in opposite directions, the TSF will apply netting within the batch to further reduce the broker’s intra-day liquidity pressure. The TSF will respectively aggregate the RMB amounts and the HKD equivalent amounts of all TSF FX Positions within the batch, arriving at a TSF Final FX Position. Based on this TSF Final FX Position, the broker will usually either need to pay one lump sum of HKD to the TSF by 3 p.m. in exchange for RMB, or vice versa.

Diagram 6: Determine the FX amounts for broker to pay at different times on T+2 – netting among stocks



Example 3: Calculate the net FX amounts to be paid by broker respectively by 3 p.m. and after the final batch settlement run

	CNS Positions (RMB)			TSF FX Positions (3pm batch)			TSF FX Positions (day end batch)		
	Non-TSF Trade	+ TSF Trade	= CNS	Broker Buy / Sell ¥ from / to TSF	RMB	HKD	Broker Sell ¥ to TSF	RMB	HKD
Stock A	¥ 100 -	¥ 100 -	¥ 200 -	Buy	¥ 100 +	\$ 117 -			
Stock B	¥ 100 +	¥ 200 -	¥ 100 -	Buy	¥ 200 +	\$ 234 -			
Stock C	¥ 400 +	¥ 300 -	¥ 100 +	Buy	¥ 300 +	\$ 351 -			
Stock D	¥ 500 -	¥ 400 +	¥ 100 -	Sell	¥ 400 -	\$ 464 +			
Stock E	¥ 300 -	¥ 500 +	¥ 200 +	Sell	¥ 300 -	\$ 348 +	Sell	¥ 200 -	\$ 232 +
Stock F	¥ 100 +	¥ 600 +	¥ 700 +				Sell	¥ 600 -	\$ 696 +
					¥ 100 -	\$ 110 +		¥ 800 -	\$ 928 +

Compare broker's RMB FX payment amount against CNS Positions to segregate TSF FX Positions into two batches

Offset FX amounts in each batch to calculate TSF Final FX Position

Partially covered by CNS

All covered by CNS

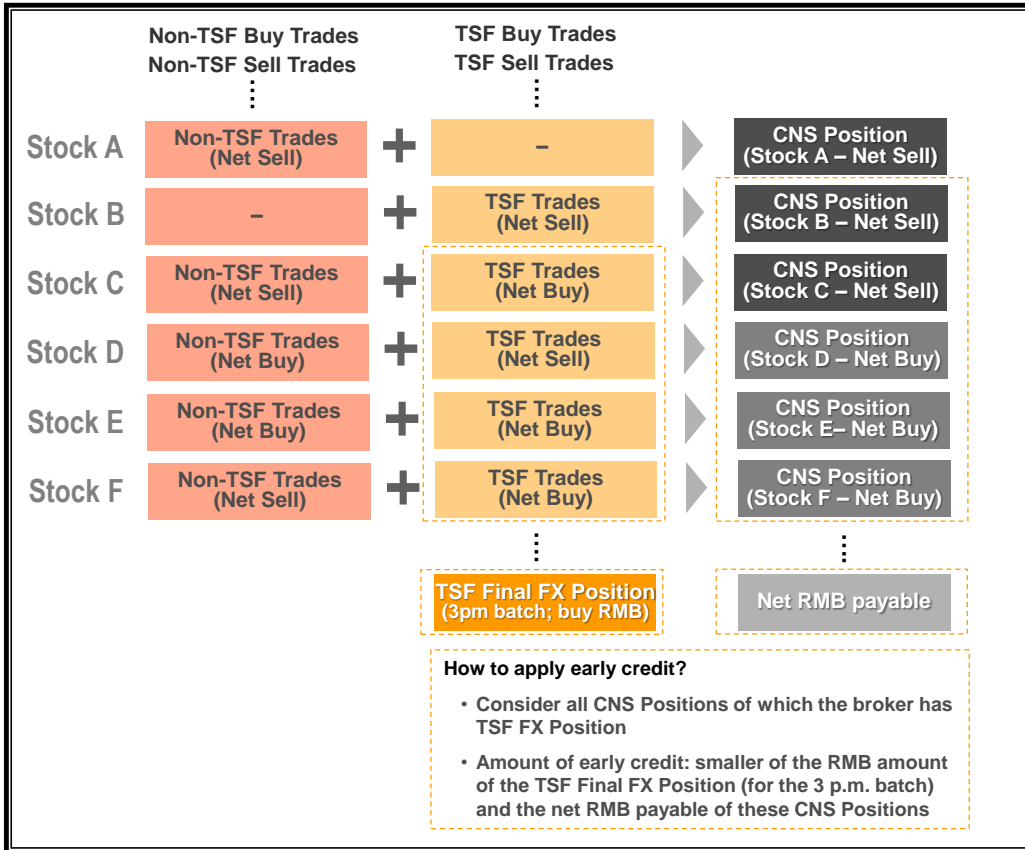
Note: RMB Sell Final FX Rate at 1.17 (for TSF Buy Exchange Trades)
RMB Buy Final FX Rate at 1.16 (for TSF Sell Exchange Trades)

How to settle a TSF Final FX Position where the participating broker is required to pay HKD to the TSF by 3 p.m. on T+2?

- 4.14 The TSF Final FX Position of the 3 p.m. payment batch can be of either direction, i.e., it may be for the broker to pay HKD or RMB to the TSF. If the TSF Final FX Position of the batch is for the broker to pay HKD to the TSF, the collection of HKD and payment of RMB will be processed by the TSF in the following manner:
- a) The broker will need to pay the HKD to the TSF by 3 p.m.
 - b) The HKD payment should be made via CPI or bank transfer.
 - c) Upon receiving the HKD from the broker, the TSF will pay RMB to the broker via crediting its CCASS money ledger. The broker will receive the RMB in its designated bank account at the end of T+2 via the CCASS day end money settlement process.
 - d) The TSF will normally credit the broker's CCASS money ledger for the RMB amount before the end of the final batch settlement run in CCASS. The broker can then use the RMB received from the TSF to settle its CNS money obligations. This will be done automatically when the RMB credit entry for the TSF Final FX Position offsets the RMB debit entry of the broker's respective CNS position.
 - e) Currently, some brokers may make cash prepayment to HKSCC to use its CNS allocated shares¹⁰ on T+2. To facilitate a participating broker to do the same, the TSF may credit the broker's CCASS money ledger for the whole or a portion of the RMB amount of the TSF Final FX Position as soon as it has received the respective HKD, which may be well before the final batch settlement run. The amount of this early credit will be determined by the broker's CNS positions in relation to its TSF Exchange Trades.
 - f) In short, the TSF will calculate the net money position of the broker's CNS positions in relation to the stocks that the broker has TSF FX Positions. If the net CNS money position is for the broker to pay RMB to HKSCC, the TSF will base on this net CNS RMB payable amount to apply the early credit, up to the RMB amount of the TSF Final FX Position for 3 p.m.

¹⁰ Under the CNS system, HKSCC will allocate shares to a buying broker's stock account on T+2 and collect the respective settlement money from the broker through the day end money settlement process. As money is not received at the time of share allocation, the CNS allocated shares will be put on hold in the broker's stock account until the money is paid in full. For those brokers who want to use the CNS allocated shares, they will pay HKSCC via RTGS or bank transfer ("cash prepayment") during the day on T+2, instead of settling the money obligations through the day end money settlement process.

Diagram 7: TSF pays RMB to broker (for TSF Final FX Position for 3 p.m. batch) – consider participating broker's CNS Positions to credit RMB to its CCASS money ledger earlier



Example 4: TSF pays RMB to broker (for TSF Final FX Position for 3 p.m. batch) – calculate the amount of early credit

	CNS Money Positions			TSF FX Positions (3pm batch)		
	Non-TSF Trade	+ TSF Trade	= CNS	Broker Buy RMB from / Sell RMB to TSF	RMB	HKD
Stock A	¥ 500 +	-	¥ 500 +			
Stock B	-	¥ 100 +	¥ 100 +			
Stock C	¥ 600 +	¥ 300 -	¥ 300 +	Buy	¥ 300 +	\$ 351 -
Stock D	¥ 300 -	¥ 200 +	¥ 100 -	Sell	¥ 200 -	\$ 232 +
Stock E	¥ 200 -	¥ 100 -	¥ 300 -	Buy	¥ 100 +	\$ 117 -
Stock F	¥ 100 +	¥ 400 -	¥ 300 -	Buy	¥ 400 +	\$ 468 -
			¥ 300 -		¥ 600 +	\$ 704 -

Amount of RMB early credit: ¥300 (i.e. smaller of the two)

Note: RMB Sell Final FX Rate at 1.17 (for TSF Buy Exchange Trades)
RMB Buy Final FX Rate at 1.16 (for TSF Sell Exchange Trades)

How to settle a TSF Final FX Position where the participating broker is required to pay RMB to the TSF by 3 p.m. on T+2?

- 4.15 Depending on the netting result of the 3 p.m. payment batch, a broker may need to pay RMB to the TSF by 3 p.m. in exchange for HKD. In that case the collection of RMB and payment of HKD will be processed by the TSF in the following manner:
- a) The broker will need to pay the RMB to the TSF by 3 p.m.
 - b) The RMB payment should be made via CPI or bank transfer.
 - c) After receiving the full amount of RMB from the broker, the TSF will pay HKD to the broker via crediting its CCASS money ledger before the end of the final batch settlement run. The broker will receive the HKD in its designated bank account at the end of T+2 via the CCASS day end money settlement process.

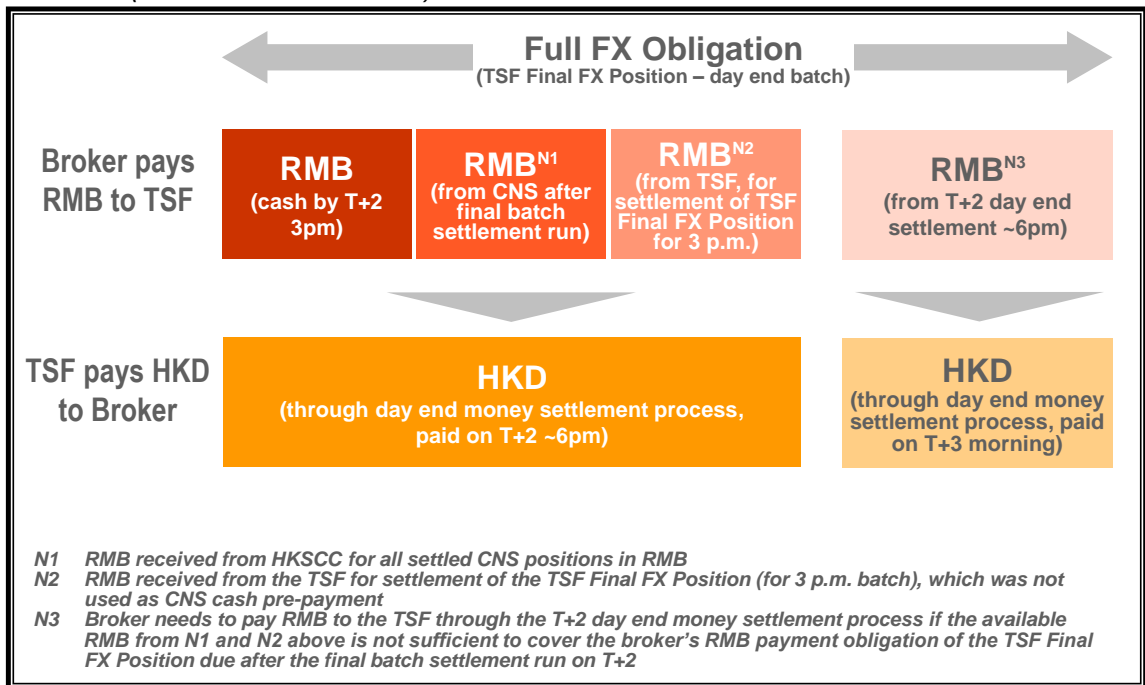
How to settle a TSF Final FX Position where the participating broker is required to pay RMB to the TSF after the CCASS final batch settlement run on T+2?

- 4.16 As explained above, the TSF will consider collecting the RMB for the FX transaction by drawing on the broker's CNS receivable monies. In that case a TSF Final FX Position will be generated for the broker for settlement after the final batch settlement run, when the relevant CNS Short Positions (of which the broker has corresponding TSF Sell Exchange Trades) should have settled.
- 4.17 However, based on the FX calculation mechanism, a participating broker may need to pay HKD to the TSF by 3 p.m. on a day in exchange for RMB (i.e. a TSF Final FX Position designated for settlement by the broker by 3 p.m.), and at the same time have an obligation to pay RMB to the TSF after the final batch settlement run on the same day in exchange for HKD (i.e. another TSF Final FX Position designated for settlement by the broker after the final batch settlement run). Under such scenario, when the broker is due to pay RMB to the TSF after the final batch settlement run, it may be able to, in addition to its CNS receivable monies, use the RMB received from the TSF earlier on the day to fulfill its RMB payment obligations with respect to the TSF Final FX Position.
- 4.18 In short, if a participating broker is required to pay RMB to the TSF after the final batch settlement run on a day in exchange for HKD, the TSF will collect the RMB by accepting and/or taking up any "available RMB" in the broker's money ledger:
- a) firstly, accepting or taking up any RMB paid to the participating broker for its settled net CNS money positions; and
 - b) secondly, accepting and taking up any RMB paid to the participating broker before the end of the final batch settlement run for settling the Final FX Position of the 3 p.m. payment batch, provided that such RMB has not been used by the broker to release its CNS allocated shares (as detailed in paragraph 4.14).

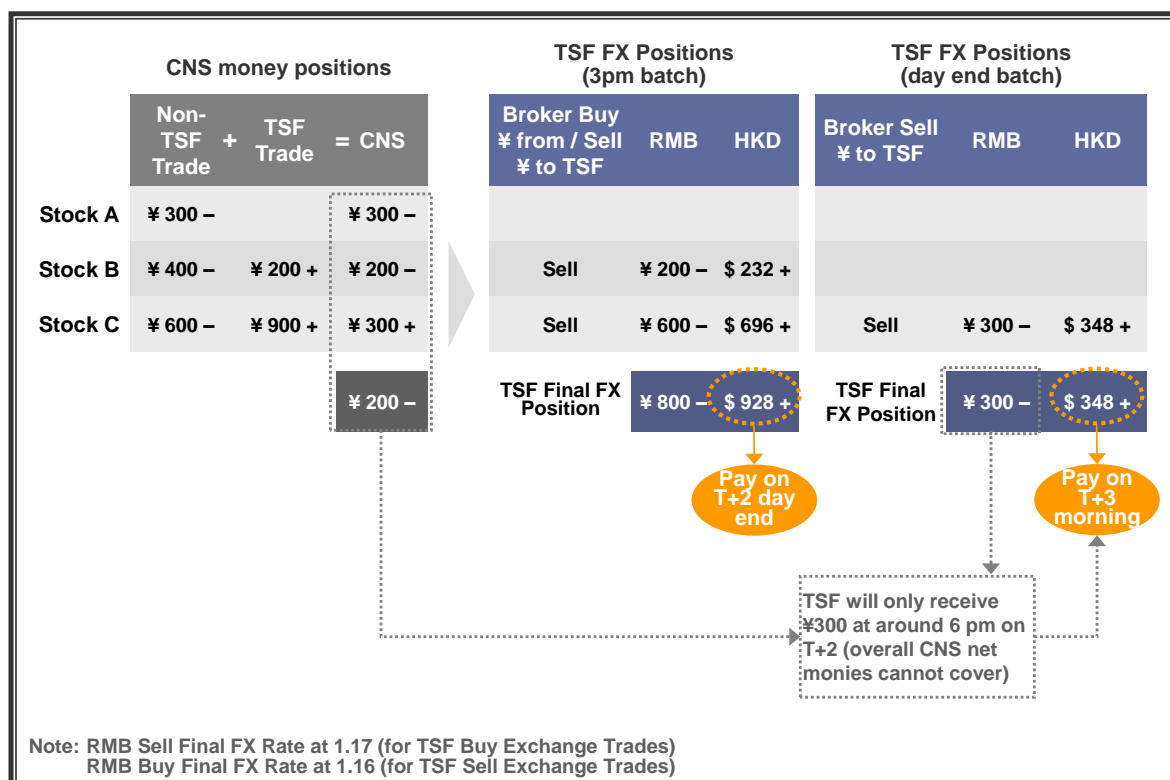
-
- 4.19 The TSF will collect the RMB amount of the TSF Final FX Position by posting a debit entry to the broker's CCASS money ledger after the final batch settlement run on T+2. Under normal circumstances where the broker's "available RMB" as explained in paragraph 4.18 above is sufficient to cover its RMB payment obligation, the TSF will consider the broker has fully settled its RMB payment obligation, and pay the corresponding HKD to the broker by immediately posting a credit entry to the broker's CCASS money ledger, in which case the broker will receive the HKD at the end of T+2. However, subject to the broker's CNS settlement status, there may be a chance that the broker's "available RMB" is not sufficient to cover its FX RMB payment obligation:
- a) The FX RMB amount was supposed to be covered by the receivable monies of some of the broker's CNS Short Positions (of which the broker has corresponding TSF Sell Exchange Trades). If the broker has settled such CNS Short Positions on T+2, the TSF should be able to collect the RMB from the broker by offsetting against the CNS receivable monies.
 - b) However, a broker's CNS monies arising from different CNS Positions are viewed as a whole for risk management purposes. The CNS receivable monies relating to the TSF transactions may be used to offset against the broker's other CNS payable items, before they are considered for paying the TSF. When that happened, the broker may not have sufficient CNS receivable monies to fulfill its RMB payment obligation with respect to the TSF Final FX Position.
 - c) In other words, when the TSF accepts or takes up the broker's CNS monies after the final batch settlement run on T+2 to settle its TSF Final FX Position, the TSF is only able to accept or take up the broker's RMB in relation to its settled net CNS money position for all stocks.
- 4.20 The TSF will only pay HKD to a participating broker when it has received the corresponding RMB. Under the situation where the broker's "available RMB" is not sufficient to cover its RMB FX payment obligation, the TSF will have to collect the outstanding amount from the broker through the CCASS day end money settlement process. The relevant RMB amount will normally be paid into the TSF's bank account at around 6:00 p.m. on T+2, after then the TSF can pay the corresponding HKD to the broker.
- 4.21 The broker may therefore receive the corresponding HKD at the end of T+2 and/or in the morning of T+3:
- a) *T+3 morning*: If the broker does not have any "available RMB" as described in paragraph 4.18 above to settle the TSF Final FX Position, the TSF will need to wait until it has received the outstanding RMB amount at around 6:00 p.m. on T+2, after then the TSF will credit the broker's CCASS money ledger for the corresponding HKD, which will be paid into the broker's bank account in the morning of T+3 (valued on T+2).
 - b) *T+2 day end*: If the broker's "available RMB" as described in paragraph 4.18 above is sufficient to fully settle the TSF Final FX Position, the TSF will consider the broker has fully met its FX obligation and credit its CCASS money ledger for the corresponding HKD after the final batch settlement run on T+2. The broker will then receive the HKD at the end of T+2.

c) *T+2 day end AND T+3 morning*: If the broker’s “available RMB” as described in paragraph 4.18 above can only partially settle the TSF Final FX Position, the TSF will consider the broker has only partially met its FX obligation, while the outstanding RMB amount will only be paid into the TSF’s bank account at around 6:00 p.m. on T+2. Under this situation, the broker will receive part of the HKD at the end of T+2 (for amount corresponding to the “available RMB” as described in paragraph 4.18), and part of the HKD in the morning of T+3 (but valued at T+2; for amount corresponding to the RMB to be paid to the TSF’s bank account at 6:00 p.m. on T+2).

Diagram 8: TSF may pay some of the HKD to participating broker in the morning of T+3 (when broker sells RMB to TSF)



Example 5: TSF pays HKD to broker – some on T+2 day end and some on T+3 morning



Confirmation report for reconciliation

4.22 The conversion details of each TSF Exchange Trade, details of the FX transactions, the TSF FX Position in respect of each relevant RMB Shares, the TSF Final FX Positions, representing the amounts to be paid to the TSF by respective times on T+2, and the projected CCASS money settlement details (which might be used to cover the broker's FX obligation) will be provided in the TSF Confirmation Report available through CCASS at 6 p.m. on T-day and T+1. Participating brokers can refer to the report for funding preparation and reconciliation.

PART 5: EARMARKING AND DE-EARMARKING OF SHARES

TSF Accounts

- 5.1 To ensure investors who have purchased RMB Shares by using the TSF will only receive HKD when they sell the shares (the “HKD in HKD out” principle), shares bought through the TSF will be earmarked in CCASS (“earmarked TSF Stocks”).
- 5.2 Two CCASS Stock Accounts will be opened for each TSF participating broker for share earmarking purposes (i.e. TSF Segregated Account 17 and TSF Principal Account 18).
- 5.3 The primary function of TSF Account 18 is to host brokers’ shares purchased through the use of the TSF. The TSF will automatically transfer shares from a broker’s Clearing Account 01 to TSF Account 18 on T+2 for the broker’s TSF Buy Exchange Trades (i.e. earmarking), and from the broker’s TSF Account 18 to Clearing Account 01 for the broker’s TSF Sell Exchange Trades (i.e. de-earmarking).
- 5.4 Participating brokers can also use their TSF Account 17 to maintain the earmarked TSF Stocks if they need to segregate their client shares from proprietary shares.
- 5.5 Investors may choose to maintain their shares with custodians. Therefore, custodians which are CCASS Participants can also choose to participate in the TSF, in which cases the custodians will have TSF Accounts 17 and 18 to maintain the RMB Shares purchased through the TSF FX Services.
- 5.6 Shares maintained in the TSF Accounts are subject to certain restrictions. Generally speaking, a broker or custodian can only transfer earmarked TSF Stocks out of its TSF Accounts to a non-TSF Account by paying the TSF the market value of the shares in RMB in exchange for HKD, otherwise, the shares can only be transferred to another TSF Account, either of the same broker/custodian or another broker/custodian¹¹.
- 5.7 A broker or custodian will only receive shares into its TSF Accounts under the following situations:
 - a) Through Settlement Instruction (“SI”) from another broker’s or custodian’s TSF Accounts;
 - b) Through Account Transfer Instruction (“ATI”) initiated by the broker to transfer shares from other stock accounts to TSF Account 17 or 18, up to the number of shares overdue or due for earmarking;
 - c) Through settlement of TSF transaction initiated by TSF Buy Exchange Trades where the TSF will automatically transfer shares from the broker’s Clearing Account 01 to TSF Account 18 for earmarking purposes; and

¹¹ Transfer of shares from the TSF Accounts to the accounts in the Common Collateral Management System (CCMS) as specific stock collateral is also NOT allowed.

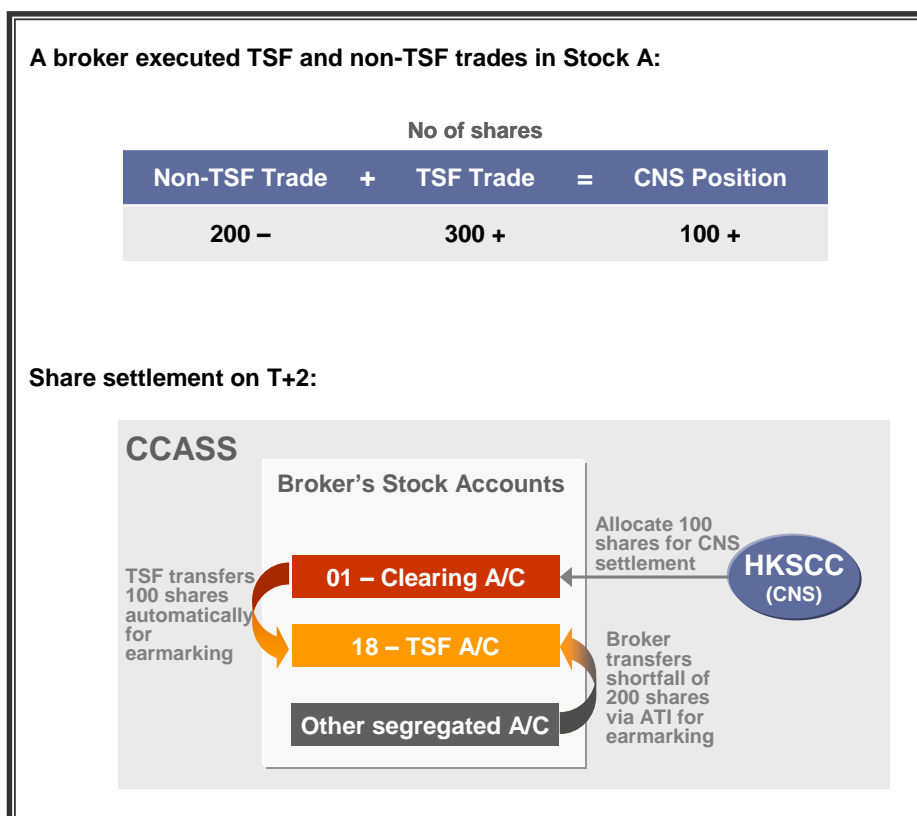
-
- d) Through share transfer made by the TSF at the broker's or custodian's request to transfer bonus shares and other share entitlements from its Entitlement Account 02 to TSF Account 17 or 18 (please refer to Part 6 for the operating details).
- 5.8 Share will only be transferred out of a broker's or custodian's TSF Accounts under the following situations:
- a) Through SI to another broker's or custodian's TSF Accounts;
 - b) Through settlement of TSF transaction initiated by TSF Sell Exchange Trades where the TSF will automatically transfer shares from the broker's TSF Account 18 to Clearing Account 01 for de-earmarking purposes;
 - c) Through a new CCASS Stock Release Request function input by the broker or custodian where the broker or custodian will pay the TSF prescribed amount of RMB in exchange for HKD (please refer to paragraphs 5.14 to 5.15 for the operating details); or
 - d) Through being released (i.e. de-earmarking) by the TSF, either with or without payment of the equivalent value of RMB, upon the TSF ceasing to operate or upon a suspension of the TSF FX Services (please refer to Part 8 for the operating details).
- 5.9 Brokers and custodians who wish to withdraw shares certificates for shares maintained in their TSF Accounts should first transfer the shares to other stock accounts by way of Stock Release Request.

The share earmarking and de-earmarking process

- 5.10 Earmarking and de-earmarking of shares are done on a net basis for each stock. All TSF Buy Exchange Trades and TSF Sell Exchange Trades of the same stock will be aggregated to a net long / short TSF stock position. The TSF will effect share transfer between participating broker's Clearing Account 01 and TSF Account 18 based on the net TSF Stock Position.
- 5.11 For net long TSF stock position, the broker can transfer the net number of shares from its Clearing Account 01 or other segregated accounts to TSF Account 17 or 18 before the final batch settlement run on T+2, otherwise the TSF will transfer the shares from the broker's Clearing Account 01 to TSF Account 18 automatically :
- a) The TSF will transfer the shares after the final batch settlement run at around 4:15 p.m.
 - b) The TSF may not be able to debit the full number of shares from the broker's Clearing Account 01 immediately after the final batch settlement run as some of the CNS shares allocated to the broker's Clearing Account 01 may be put on hold pending money settlement. In that case the TSF will debit the remaining number of shares from the broker's Clearing Account 01 and credit to TSF Account 18 after finalization of the money settlement process, at around 8:30 p.m.
 - c) A broker may execute different trades in a stock on the same day, some using the TSF FX Services and some do not. Therefore, the broker's CNS Position may differ from its TSF Position. In case the number of shares allocated for the CNS Position (if any) is not able to cover the total earmarking obligation of the net long TSF stock position, the

broker will need to transfer the shortfall into TSF Account 17 or 18 to fulfill its earmarking obligation. Alternatively, the broker can transfer the shortfall into its Clearing Account 01 so that the TSF can transfer those shares to the TSF Account 18 automatically. The amount of earmarking obligations and the relevant CNS stock positions will be available in the TSF Confirmation Report. Participating brokers can calculate the shortfall based on the information in the report. (please refer to paragraph 5.16 for details)

Example 6: Broker transfers shares to TSF Account to fulfill earmarking obligation



- 5.12 As instructed by the client, a broker may input an SI into CCASS to onward deliver the earmarked TSF Stocks from its TSF Account to another broker's or custodian's TSF Account on T+2. To ensure the SI can be settled on T+2, the broker should transfer the CNS settled shares from its Clearing Account 01 to TSF Account 17 or 18, otherwise the SI will only be settled on T+3 as the TSF will only earmark shares after the final batch settlement run.
- 5.13 For net short TSF stock position, the TSF will transfer the net number of shares from the broker's TSF Account 18 to Clearing Account 01 on T+2:
- The TSF will transfer the shares 15 minutes before each batch settlement run, until the full amount of shares for de-earmarking is transferred.
 - To ensure the broker's CNS positions can be settled as soon as possible, where available, the TSF will transfer the shares up to the quantity required for settling the corresponding

CNS position (in which case a CNS short position). The TSF can then draw on the CNS settlement monies to settle the broker's FX obligation.

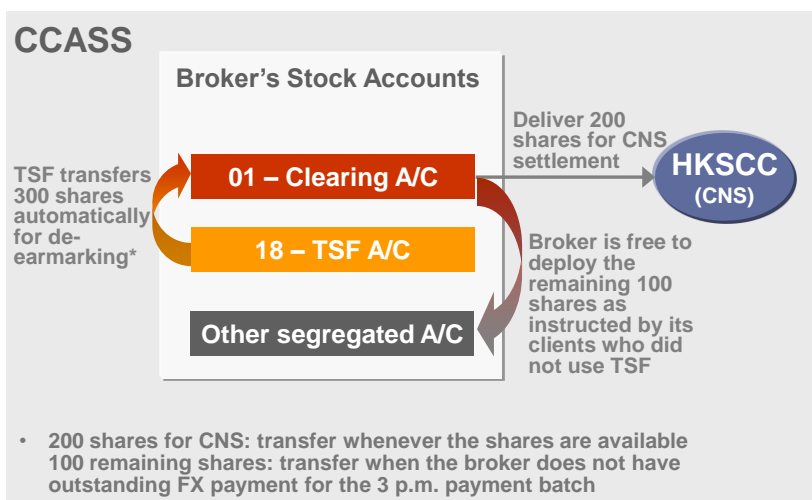
- c) The number of shares to be de-earmarked under a net short TSF stock position may be in excess of the number of shares required to deliver for the corresponding CNS short position, as the broker may have executed some buy trades in the same stock not using the TSF FX Services. The relevant FX RMB to be paid by the broker for these de-earmarking shares in excess would have been designated for collection by 3 p.m. on T+2. The TSF will transfer these remaining shares from the broker's TSF Account 18 to Clearing Account 01 when the broker has settled the relevant RMB payment. For the avoidance of doubt, the TSF will transfer these remaining shares if the broker has settled its FX payment obligation designated for the 3 p.m. batch.
- d) After the remaining shares are transferred to the broker's Clearing Account 01, the broker is free to deploy the shares as instructed by its clients who did not use the TSF.

Example 7: Broker is free to deploy de-earmarked shares in excess of its CNS delivering obligation

A broker executed TSF and non-TSF trades in Stock A:

No of shares			
Non-TSF Trade	+	TSF Trade	= CNS Position
100 +		300 -	200 -

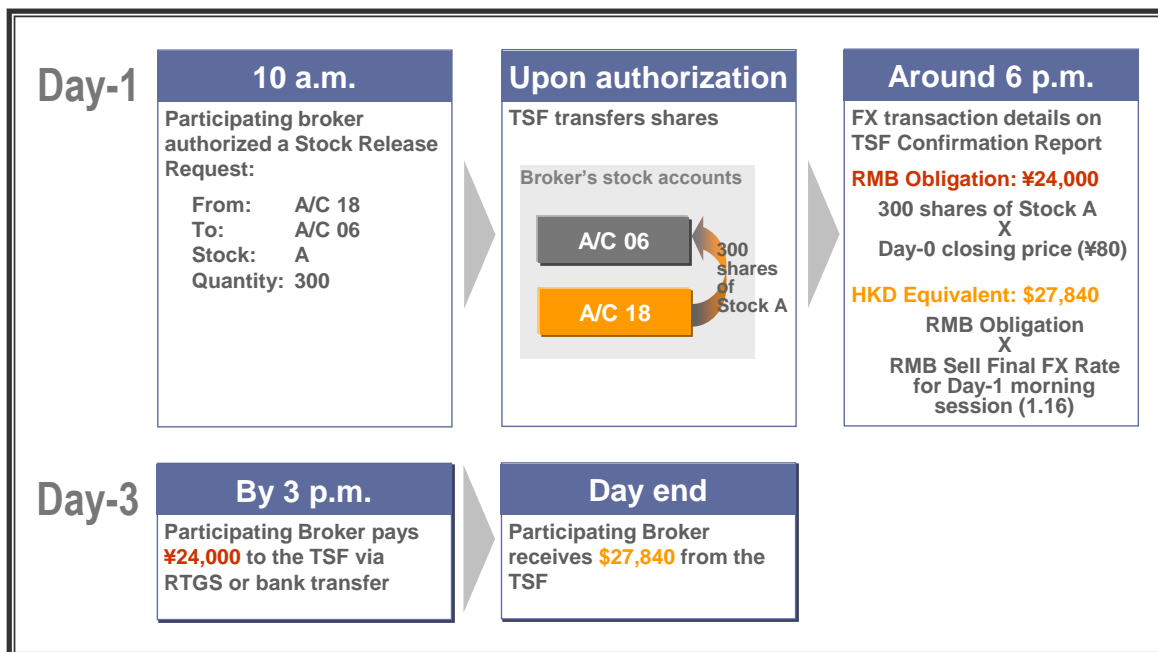
Share settlement on T+2:



Stock Release Request – to de-earmark shares without selling on SEHK

- 5.14 Shares maintained in the TSF Accounts will normally be transferred out only upon selling on the SEHK, or transferring to another TSF Account. The TSF will nevertheless provide flexibility to investors if they want to free up the shares without going through the above processes (e.g. for withdrawing paper certificates of the earmarked TSF Stocks from CCASS).
- 5.15 A participating broker (or a CCASS Custodian Participant who participates in the TSF) can use a new CCASS function to input a “Stock Release Request” into CCASS at any time to request the TSF to de-earmark shares without selling the shares on SEHK:
- a) Upon accepting the on-line request, the TSF will immediately transfer the specified number of shares from TSF Account 17 or 18 to the specified stock account.
 - b) The broker or custodian will need to pay RMB to the TSF on T+2 in exchange for HKD. The RMB obligation is the value of the releasing shares, determined by the closing price of the stock as of the previous day. The TSF will refer to the RMB Buy FX Rate for the trading session where the Stock Release Request is authorized to determine the amount of HKD to be paid to the broker or custodian. For the avoidance of doubt, Stock Release Request authorized after the morning session (i.e. after 12:00 noon) will be subject to the RMB Buy FX Rate for the afternoon session.
 - c) The broker or custodian will need to pay RMB to the TSF through RTGS or bank transfer before 3 p.m. on T+2. For those brokers who have maintained standing instruction with CCASS to settle TSF payments through RTGS, a single TSF payment instruction (i.e. CPI) will be issued to their designated banks for RMB payments of all Stock Release Requests due on the day. Separate CPIs will be issued if the broker has to settle FX payments for its Stock Release Request as well as TSF Exchange Trades on the same day.
 - d) Upon receiving the RMB in full, the TSF will pay HKD to the broker or custodian by crediting its money ledger. The HKD will be paid into the broker or custodian’s designated bank account at the day end of T+2.

Example 8: Settlement of Stock Release Request



Confirmation report for reconciliation

5.16 A TSF Confirmation Report will be provided to participating brokers and custodians at around 6 p.m. on each business day. Among others, the report will detail:

- a) The number of shares of each stock to be earmarked or de-earmarked on the next day (i.e. the net long / short TSF stock position) and the days after for TSF Exchange Trades executed on previous day and on the day respectively;
- b) The number of shares that have been de-earmarked on the day for Stock Release Requests authorized on the day.

Brokers and custodians can refer to the report for reconciliation and/or action.

PART 6: CORPORATE ACTIONS HANDLING FOR EARMARKED TSF STOCKS

- 6.1 Shares earmarked in TSF Accounts 17 and 18 (“earmarked TSF Stocks”) may undergo corporate actions. These shares will subject to the same corporate actions processes as those shares maintained in other CCASS stock accounts.
- 6.2 Today, a broker or custodian may maintain shares of the same stock in its different CCASS stock accounts. If the stock undergoes consolidation or splitting, CCASS will consolidate or split the shares for each of the broker’s stock account. The resulting shares will be put in respective stock accounts. This process will also apply to the shares earmarked in TSF Accounts 17 and 18.

Example 9: Shares in TSF Accounts undergo consolidation

A broker has 1,500 shares of Stock A in different stock accounts
Stock A undergoes a 3:1 consolidation

Stock Account	No. of shares before consolidation	No. of shares after consolidation
01	100	33
03	200	66
04	300	100
17	400	133
18	500	166
Total	1,500	498

Shares in TSF Account 17 and 18 go through the same consolidation process as those shares in other accounts

- 6.3 An issuer may pay cash dividend in any currency. CCASS will distribute the cash dividend in its original currency as paid by the issuer to its participants for their shares maintained in their CCASS stock accounts without converting the currency. This will also apply to the shares earmarked in TSF Accounts 17 and 18. For the avoidance of doubt, if issuers of RMB Shares pay cash dividend in RMB, CCASS will distribute the RMB to its participants for their shares earmarked in TSF Accounts 17 and 18.
- 6.4 Today, if an issuer distributes share entitlements such as bonus shares and scrip dividend, CCASS will calculate the share entitlement quantity of individual participants based on their aggregate shareholdings in different stock accounts, and credit the entitled shares to their Entitlement Account 02. This process will also apply to the shares earmarked in TSF Accounts 17 and 18.
- 6.5 Subject to the operating practice of individual brokers and custodians, some of them may want to maintain entitled shares arising from earmarked TSF Stocks in the TSF Accounts. Flexibility will be provided to these market players. After receiving the entitled shares into their Entitlement Account 02, brokers and custodians can submit manual instruction to CCASS to transfer the entitled shares from their Entitlement Account 02 to their TSF Account 17 or 18. Brokers and custodians can transfer the whole quantity of entitled shares

arising from their earmarked TSF Stocks, or only a portion of it. It should be noted that the entitled shares will be subject to the earmark rules once being transferred to TSF Account 17 or 18.

- 6.6 The primary objective of the TSF is to support the trading of RMB Shares on the secondary market. The TSF therefore will not support rights subscription, which is a fund raising activity. If a broker or custodian wants to subscribe to the underlying shares of rights received for its earmarked TSF Stocks, it has to do it by using RMB (assuming RMB is the subscription currency).

PART 7: EXCEPTION MANAGEMENT

7.1 The TSF will build in different processes to facilitate brokers using the facility. However, similar to the existing trading and clearing arrangements, brokers will have to establish and follow corresponding operation procedures to ensure the smooth running of the process. In the event that the established procedures were not properly followed where the TSF process deviates from its normal track, brokers will need to execute additional procedures to fix the problem, and may be subject to additional costs.

Participating brokers forgot to indicate in orders or indicated wrongly

7.2 If an investor client requested a broker to buy shares by using the TSF but the broker forgot to indicate the request in the buy order, the TSF will not provide TSF FX Services to the broker. While the broker will receive HKD from its client, the broker will need to arrange FX for its client in the market to meet its CNS obligations (in RMB).

7.3 If an investor client did not request a broker to buy shares by using the TSF but the broker wrongly indicated in the buy order to use the TSF FX Services, the broker will need to settle with the TSF on T+2. The broker will need to pay HKD to the TSF in exchange for RMB, and the relevant shares will be earmarked in its TSF Account 18. After the TSF settlement process, the broker can use the Stock Release Request function to de-earmark the shares, and return the RMB to the TSF two days later in exchange for HKD. It should however be noted that the FX amount of the Stock Release Request may be different from that of the relevant buy order. The broker may need to bear the cost.

7.4 If an investor client requested a broker to sell earmarked TSF Stocks but the broker forgot to indicate in the sell order to use the TSF FX Services, the TSF will not know that it has to de-earmark shares for the broker to settle its CNS position. The broker will need to use the Stock Release Request function on or before T+2 to de-earmark the shares for CNS settlement, and return the RMB to the TSF two days later in exchange for HKD.

7.5 If an investor client did not request a broker to sell earmarked TSF Stocks but the broker wrongly indicated in the sell order to use the TSF FX Services, the broker may not have sufficient shares in its TSF Account 18 for the TSF to de-earmark. Notwithstanding the fact that the broker may not be able to meet its share de-earmarking obligation, the TSF will continue to collect RMB from the broker in exchange for HKD on T+2 to complete the FX transaction. Upon receiving HKD from the TSF, the broker will need to arrange FX in the market to pay RMB to its client.

7.6 The following table summarizes the actions that a participating broker should take when the broker forgot to indicate the use of TSF in a buy or sell order or indicated wrongly in an order:

Case	Buy / Sell	Client instructed to use the TSF FX Services?	Broker indicated in the order to use the TSF FX Services?	What should the broker do?
a)	Buy	Yes	No	Get RMB from the market to meet CNS obligations and/or settle with other clients who did not use the TSF FX Services
b)	Buy	No	Yes	Input Stock Release Request* in CCASS to: <ul style="list-style-type: none"> • Release wrongly earmarked shares immediately • Return RMB to the TSF two days after releasing the earmarked shares
c)	Sell	Yes	No	Input Stock Release Request* in CCASS to: <ul style="list-style-type: none"> • Release earmarked shares immediately for CNS settlement • Return RMB to the TSF two days after releasing the earmarked shares
d)	Sell	No	Yes	<ul style="list-style-type: none"> • Ensure sufficient shares in Account 01 for CNS settlement • Use HKD received from the TSF to buy RMB in the market* to settle with client

* Participating broker will subject to additional FX costs in executing these transactions

Participating brokers failed to settle with the TSF on T+2

7.7 Once an order specified to use the TSF FX Services is matched in AMS and becomes a TSF Exchange Trade, the broker is committed to execute FX transaction with the TSF on T+2. The TSF will execute back-to-back FX transaction with the TSF Partner Banks to support its FX transaction with the broker. If a broker failed its FX payment, it is an event of default and the TSF will need to square its position by reversing the FX transaction, and collect the relevant costs and charges from the defaulting broker.

7.8 If a broker should pay HKD to the TSF on a day in exchange for RMB but failed to make the HKD payment, the TSF will:

- a) not execute the FX transaction with the broker, and the broker may need to arrange FX in the market to source RMB to settle its CNS position (if required);
- b) execute a reversed FX transaction with the TSF Partner Bank, and recover any FX loss and overdraft cost (if any) from the broker, plus penalty charges; and

-
- c) continue to complete the share earmarking process with the broker.
- 7.9 If a broker should pay RMB to the TSF on a day in exchange for HKD but failed to make the RMB payment, the TSF will execute reversed FX transaction with the TSF Partner Bank, and recover any FX loss and overdraft cost (if any) from the broker, plus penalty charges.
- 7.10 In addition to FX, the TSF will earmark or de-earmark shares for a broker's net TSF stock positions. In cases where the required earmarking quantity is not fully provided on T+2, the following procedures will apply:
- a) If the shortfall is due to overdue CNS position, where CCASS did not allocate sufficient shares to the broker for the CNS position, the TSF will earmark the remaining shares on T+3 after the CNS position is completely settled.¹²
 - b) If the shortfall is due to the broker not able to prepare sufficient shares in its Clearing Account 01 or TSF Account 18, the broker will have to fill up the shortfall by T+3, otherwise the TSF will execute reversed FX transaction with the broker and collect penalty charges from it.
- 7.11 In cases the required de-earmarking quantity is not fully provided in the broker's TSF Account 18 on T+2, the following procedures will apply:
- a) If the broker has a corresponding CNS Long Position, or the broker has a corresponding CNS Short Position and the CNS Short Position is fully settled, no further action will be taken. The broker will have effectively executed an FX transaction to sell RMB to the TSF without de-earmarking any shares.
 - b) If the broker has a corresponding CNS Short Position but the CNS Short Position is not fully settled, the broker would have failed the whole or part of its FX obligation (as the TSF would be expecting to draw on the broker's CNS receivable monies to cover its TSF Final FX Positions at Evening FX Settlement Time). The TSF will execute reversed FX transaction for the broker for the unsettled FX portion, and recover any FX loss and overdraft costs (if any) from the broker, plus penalty charges.

¹² The TSF will have completed the FX transaction with the broker on T+2 but not able to earmark the shares on the same day. The broker should retain the RMB received from the TSF in the bank account for CNS settlement on T+3.

PART 8: SUSPENSION OF THE FX SERVICES AND RETIREMENT OF THE TSF

TSF might need to suspend FX services under extreme situation

- 8.1 The FX services provided by the TSF are backed up by the TSF Partner Banks. Each of the TSF Partner Banks commits to a FX line for the TSF to draw on anytime as requested by the participating brokers. The size of the TSF will be correlated with the size of the RMB offerings that the TSF will support, and sufficient buffer will be built into this correlation to ensure the smooth running of the TSF. Having said that, the TSF FX Services are nevertheless constrained by its size, and under extreme situation, there might be possibility that the TSF would need to temporarily suspend the TSF FX Services.
- 8.2 Although it is believed that the triggering of the TSF suspension would be extremely remote, the TSF has nevertheless established proper procedures to minimize any possible impact to participating brokers.
- 8.3 The TSF will normally post the available fund balance of the TSF on the designated area of the HKEx website before the commencement of the trading day and of the afternoon session, and after the market close for the reference of the general investing public.
- 8.4 Alert message and suspension announcement will be made to the market through the AMS, CCASS Terminal and the HKEx website:
- a) Alert message will be provided to the market when the TSF fund balance is dropped to a prescribed level. The market will be alerted that the TSF FX Services may be suspended shortly subject to the availability of fund. Participating brokers should assess its risk exposure and consider amend or cancel their outstanding odd lot/special lot orders which have been specified to use the TSF FX Services as appropriate and stop requesting for the TSF FX Services in new buy orders.
 - b) Announcement will be made to the market when the TSF fund balance drops to zero. The TSF will not provide FX services for trades matched beyond the zero point.¹³
- 8.5 As board lot buy orders intended for use of the TSF FX Services are in the form of special limit order or at-auction order, any unmatched portion of the order at the time of input will be cancelled by the system immediately. It thus eliminates the case where an outstanding board lot buy order specified to use the TSF FX Services is matched after the TSF has suspended the TSF FX Services, and the broker is short of RMB to settle its CNS Position.
- 8.6 Under normal situation, a broker who wants to sell its earmarked TSF Stocks must return the relevant amount of RMB to the TSF in exchange for HKD. If the TSF has to suspend its FX services to the effect that it does not buy any RMB from brokers, the TSF will ensure that the earmarked TSF Stocks in relation to TSF Sell Exchange Trades will be de-

¹³ To avoid error input, the AMS will be enhanced to on-line reject any further input of buy order which is specified to use the TSF FX Services when the TSF fund balance drops to zero. However, it should be noted that the automatic order rejection feature will only be implemented tentatively in the first quarter of 2012. Before then, participating brokers should prepare necessary procedures to avoid inputting buy orders for using the TSF FX Services after the TSF fund size drops to zero, as the TSF will not provide any TSF FX Services for trades matched beyond that point.

earmarked for brokers' normal trade settlement, although it will not execute any FX transaction with the brokers. In this case the brokers will be receiving RMB after selling the de-earmarked shares.

TSF will retire when there is sufficient RMB liquidity in the market

- 8.7 The TSF is there to ensure the liquidity of the RMB Shares in the secondary market will not be constrained by the prevailing level of RMB in the market at any given time. When the RMB offshore market grows to a reasonable size, the TSF would have served its terms and not be needed anymore.
- 8.8 When the time comes and the TSF should close its operation, the TSF will de-earmark all shares from brokers' TSF Accounts.
- 8.9 Sufficient time will be given to participating brokers to make any necessary back office preparation before the TSF formally retires.

PART 9: REGISTRATION REQUIREMENTS

List of “TSF Participants” on HKEx website

9.1 Use of the TSF FX Services is not mandatory. However, EPs, CCASS Clearing Participants and CCASS Custodian Participants who wish to utilize the TSF are required to comply with certain registration criteria. Upon successful registration with the TSF, the EPs, CCASS Clearing Participants or CCASS Custodian Participants will become a “TSF Participant”. The list of TSF Participants will be published on the HKEx website for reference by the investing public

Types of EPs and CCASS Participants who can apply to become a TSF Participant

9.2 The following types of EPs can apply to become a TSF Participant for the purposes of using the FX services of the TSF:

- a) EPs who are themselves Direct Clearing Participant¹⁴ or General Clearing Participants¹⁵ under the CCASS Rules; and
- b) EPs who are not CCASS Participants but who have entered into a Clearing Agreement with a General Clearing Participant under the CCASS Rules and where the General Clearing Participant is a TSF Participant.

9.3 The following types of CCASS Participants can apply to become a TSF Participant for the purposes of clearing and settling TSF Exchange Trades:

- a) Direct Clearing Participants under the CCASS Rules; and
- b) General Clearing Participants under the CCASS Rules.

9.4 CCASS Custodian Participants can also apply to become a TSF Participant to hold and act as the custodian of RMB Shares purchased through the TSF FX Services.

9.5 For the avoidance of doubt, Clearing Agency Participants, Investor Participants, Stock Lender Participants and Stock Pledgee Participants under the CCASS Rules will not be permitted to use the TSF at the initial stage.

Registration Criteria

9.6 An EP or a CCASS Participant who applies to become a TSF Participant should also comply with the following registration criteria:

- a) The applicant should demonstrate to the satisfaction of the SEHK and/or HKSCC that it has adequate internal controls to differentiate earmarked securities under the TSF;

¹⁴ Direct Clearing Participants are CCASS Participants who can clear and settle their own trades executed on SEHK.

¹⁵ General Clearing Participants are CCASS Participants who can clear their own trades executed on SEHK as well as trades executed by other EPs who have entered into Clearing Agreements with them.

-
- b) The applicant should successfully complete any system test(s) prescribed by SEHK and/or HKSCC from time to time or prove to the satisfaction of SEHK and/or HKSCC of its system readiness for conducting and/or clearing TSF Exchange Trades; and
 - c) The applicant should declare its readiness to SEHK and/or HKSCC to use the TSF and to deal in and/or clear RMB securities.

Important points to consider

- 9.7 EPs and CCASS Participants who want to participate in the TSF should ensure that they have the back office capabilities to provide the service to their clients and deal with the TSF. In assessing their capabilities EPs and CCASS Participants should pay special attention to the TSF operation processes which are different from their existing practice, and the special actions they need to take under contingent situations, which may expose them to risks. Among others, EPs and CCASS Participants should note the following:

FX Rates

- a) The RMB FX Rates are provided by TSF Partner Banks on a commercial basis, and may not necessarily be more attractive than the FX rates offered on the market.
- b) Participating brokers which purchase shares through the use of the TSF FX Services shall, subject to certain exceptions, be obliged to sell such shares through the use of the TSF FX Services. Brokers have to accept the sale proceeds of such shares in HKD, and that they would be subject to the RMB Buy FX Rate which is unknown at the time of share purchase.

FX settlement

- c) Participating brokers may need to make FX payment to the TSF by 3 p.m. on T+2, as opposed to the existing CNS payment process which is normally settled at the end of T+2. (Please refer to paragraphs 4.9 to 4.15 for details)
- d) Subject to the broker's overall CNS settlement status, the broker may only receive FX HKD payment from the TSF in the morning of T+3 (valued T+2), which will be later than the usual CNS money settlement. (Please refer to paragraphs 4.16 to 4.21 for details)

Share earmarking and onward delivery

- e) Shares earmarked in the TSF Accounts are subject to certain restrictions. (Please refer to paragraphs 5.6 to 5.9 for details)
- f) Additional share transfer process is required if a broker wants to onward deliver the earmarked TSF Stocks to another broker's or custodian's TSF Account on the same day when it receives the shares from CNS settlement. The broker will need to effect Account Transfer Instruction to transfer the shares from its Clearing Account 01 to TSF Account 18 on T+2, otherwise the broker can only

onward deliver the shares to another CCASS Participant on T+3. (Please refer to paragraph 5.12 for details)

Exceptions

- g) A broker making mistakes in processing clients' requests on using the TSF FX Services may be subject to additional FX costs and charges. (Please refer to Part 7 for details)
- h) For the purpose of providing the TSF FX Services and facilitating the settlement of shares purchased through the TSF, the TSF will acquire RMB from, and sell RMB to, one or several TSF Partner Banks on a principal-to-principal basis. Subject to obtaining such RMB funding from TSF Partner Banks, the TSF will provide the TSF FX Services to participating brokers also on a principal-to-principal basis. The TSF's obligations to provide the TSF FX Services for a TSF FX transaction is conditional and dependent on the relevant TSF Partner Bank delivering to HKSCC the relevant funds in RMB or HKD, as the case may be.
- i) The TSF FX Services will be provided upon the terms and subject to the conditions as set out in the Rules of the Exchange and CCASS Rules, which may be amended from time to time. Specifically, the TSF may be suspended or may cease to provide the FX services temporarily or permanently. Participating brokers will need to establish corresponding procedures to cater for this situation. (Please refer to Part 8 for details)

- 9.8 EPs and CCASS Participants who are interested in becoming TSF Participants should contact their internal IT department and/or back office system vendors to make necessary system enhancements to support the TSF operations (e.g. capability to handle orders requesting for the TSF FX Services, segregation of earmarked and non-earmarked shares, etc). They should also review and make any necessary changes to their internal policies, risk management measures, and procedures including documents such as client agreement, contract notes, client statement, etc.
- 9.9 A checklist for TSF applicants is available in Appendix I for EPs' and CCASS Participants' reference to assess their readiness in participating in the TSF.

PART 10: FURTHER INFORMATION ABOUT THE TSF

- 10.1 A dedicated web corner had been set up at the HKEx website to host all information about the TSF. Interested parties can refer to the web corner for more information: (http://www.hkex.com.hk/eng/market/sec_tradinfra/TSF/TSF.htm).
- 10.2 HKEx has issued circulars to EPs and CCASS Participants explaining the procedures to apply for TSF participantship. The circulars are available at the TSF web corner.
- 10.3 EPs and CCASS Participants who are interested in becoming TSF Participants at its initial launch may be required to participate in a Simulation Test. Participants can refer to the circular available at the TSF web corner for the detailed arrangements.

APPENDIX I: CHECKLIST FOR TSF APPLICANTS

This checklist is aimed to help EPs and CCASS Participants who are interested in becoming TSF Participants to assess their operation readiness. As individual EPs and CCASS Participants may have different operating models, this checklist may not be comprehensive. EPs and CCASS Participants should consider their own needs and operational structure to assess their readiness in participating in the TSF.

Trading System and Operations

1. Is your firm's order management and routing systems capable of handling orders requesting for the TSF FX Services?
2. Is your firm's trading system (including online trading system) capable of handling orders requesting for the TSF FX Services?
3. Is your firm's operation ready to support orders requesting for the TSF FX Services? (e.g. reserve first three spaces of the reference field or BSS broker comment field of order to indicate the use of TSF)
4. Are your firm's client communications channels capable of handling orders requesting for the TSF FX Services? (e.g. websites, IVRS, SMS and mobile phone applications, etc)
5. Have you reviewed and made necessary amendments to client documents to handle TSF Exchange Trades and earmarked TSF Stocks? (e.g. trade confirmation and monthly statements)
6. If you are not a CCASS Participant, have you checked with your appointed CCASS General Clearing Participant whether it is eligible to participate in the TSF? Have you made necessary amendment to your Clearing Agreement?

Clearing and Settlement

7. Are your firm's back-office systems capable of handling TSF and non-TSF Exchange Trades at the same time? (e.g. clearing and settlement, accounting and billing systems)
8. Have you notified your clients on the internal policies, procedures and risk management measures of trading and settling RMB Shares using TSF?
9. Have you reviewed and made necessary amendments to the client agreements regarding your internal procedures and policies on using TSF?
10. Have you checked and agreed with your custodians (if relevant) the procedures to handle transfer of earmarked TSF Stocks?

RMB Designated Bank Account for CCASS Money Settlement

11. For your clients who have indicated interest in using the TSF, have you checked with them whether they have RMB bank accounts to receive RMB such as cash dividend? If they do not have RMB bank accounts, do you have procedures in place to convert the RMB for them?

Risk Management

12. Will you apply different risk management measures on using TSF to trade RMB Shares? If you have different risk management measures, do such measures require amendments to your internal system?
13. Have you read and do you understand the features of the TSF operations as described in this Information Paper, especially those which may be different from your existing practice, as highlighted in paragraph 9.7 of this Information Paper?

General

14. Is your firm ready to deal in and clear transactions in RMB-traded securities?

APPENDIX II: GLOSSARY

AMS	Automatic Order Matching And Execution System
ATI	Account Transfer Instruction
CCASS	Central Clearing And Settlement System
CHATS	Clearing House Automated Transfer System
CNH	Offshore RMB market in Hong Kong
CNS	Continuous Net Settlement
CPI	CHATS Payment Instruction
EP	Exchange Participant, or participant of the Stock Exchange of Hong Kong
FX	Foreign Exchange
GCP	General Clearing Participant as defined under the General Rules of CCASS
HKD	Hong Kong Dollar
HKEx	Hong Kong Exchanges and Clearing Limited
HKICL	Hong Kong Interbank Clearing Limited
HKSCC	Hong Kong Securities Clearing Company Limited
HSBC	The Hongkong and Shanghai Banking Corporation Limited
IPO	Initial Public Offering
RMB	Renminbi
RMB Shares	Shares being traded on the SEHK in RMB
SI	Settlement Instruction
RTGS	Real Time Gross Settlement
SEHK	The Stock Exchange of Hong Kong
TSF	RMB Equity Trading Support Facility

