

## **CHAPTER XVI**

### **DESIGNATED INDEX ARBITRAGE TRANSACTIONS AND STOCK FUTURES HEDGING TRANSACTIONS**

#### **General**

1601. The Rules in this Chapter are applicable to (i) any Exchange Participant which intends to apply to SEHK, through an SEHK Participant designated by the Exchange Participant, for exemption from compliance with the Tick Rule in respect of Designated Index Arbitrage Short Selling conducted for its account or for the account of a registered arbitrageur (as defined in Rule 1603) by the Exchange Participant's designated SEHK Participant and (ii) any Market Maker in the Stock Futures Market which intends to apply to SEHK, through an SEHK Participant designated by the Market Maker, for exemption from compliance with the Tick Rule in respect of Stock Futures Hedging Short Selling conducted for its account by the designated SEHK Participant.
1602. For the purposes of this Chapter, "Tick Rule" means the requirement under the Rules of SEHK that short selling of a security on SEHK must not be made below certain price as specified under the Rules of SEHK, and "Tick Rule Exemption" shall be construed accordingly.

#### **Tick Rule Exemption in relation to Designated Index Arbitrage Transactions**

1603. In order for an SEHK Participant which has been designated by an Exchange Participant under Rule 1604(c) to be exempt from compliance with the Tick Rule in respect of Designated Index Arbitrage Short Selling conducted (i) for the Exchange Participant's account; (ii) for the account of an affiliate of the Exchange Participant; (iii) for the account of the SEHK Participant; or (iv) for the account of any person which is an affiliate of the SEHK Participant, the Exchange Participant must be registered with the Exchange as a Designated Index Arbitrage Participant. In order to be so registered, an Exchange Participant shall apply to the Exchange by completing such form and complying with such instructions as may from time to time be prescribed by the Exchange. The Exchange Participant shall also apply to the Exchange to register those persons for whose account the Exchange Participant will be conducting Designated Index Arbitrage Transactions ("registered arbitrageur"). The decision as to whether or not to approve the application is entirely at the discretion of the Exchange. The Exchange may impose such conditions as it thinks fit on the approval of such application. For the purposes of Designated Index Arbitrage Transactions, the term "affiliate", in relation to a company, means a subsidiary of the company, the holding company of the company or a subsidiary of the holding company of the company.

1604. An Exchange Participant shall ensure that so long as it is registered as a Designated Index Arbitrage Participant, the following conditions are at all times satisfied when conducting Designated Index Arbitrage Transactions and in order for the Tick Rule Exemption to apply to any Designated Index Arbitrage Short Selling conducted as part of a Designated Index Arbitrage Transaction:

- (a) the Designated Index Arbitrage Transaction is only conducted in such Stock Index Futures Contracts as may from time to time be designated by the Exchange (“Designated Stock Index Futures Contracts”);
- (b) the Designated Index Arbitrage Transaction is only conducted for its own account or for the account of a registered arbitrageur;
- (c) it has designated and its registered arbitrageur has designated an SEHK Participant which is registered with SEHK as a Designated Index Arbitrage Short Selling Participant under the Rules of SEHK to conduct on SEHK such parts of the Designated Index Arbitrage Transaction that need to be conducted on SEHK;
- (d) each of its registered arbitrageurs which trades Designated Stock Index Futures Contracts as part of its Designated Index Arbitrage Transactions trades for its own account only;
- (e) it shall ensure, and procure that its registered arbitrageur shall ensure, that any Designated Index Arbitrage Short Selling conducted by its or its registered arbitrageur’s designated SEHK Participant on its or its registered arbitrageur’s behalf comply with the conditions and criteria set forth in the Rules of SEHK relating to Designated Index Arbitrage Short Selling; and
- (f) such other conditions as may from time to time be prescribed by the Exchange.

1605. A Designated Index Arbitrage Participant, or a Designated Index Arbitrage Participant on behalf of a registered arbitrageur, may purchase or sell a Designated Stock Index Futures Contract for the purpose of rebalancing a Designated Index Arbitrage Transaction. The Exchange may at any time limit the number of contracts or the total value of contracts purchased or sold as part of the rebalancing of a Designated Index Arbitrage Transaction. A Designated Index Arbitrage Participant shall notify the Exchange, in such manner as prescribed by the Exchange from time to time, if the total value of contracts purchased or sold for the purpose of rebalancing a Designated Index Arbitrage Transaction in one Trading Day exceeds 4% of the total value of the Designated Index Arbitrage Transaction (valued as at the previous Trading Day).

1606. A Designated Index Arbitrage Participant shall, and shall procure that its registered arbitrageur shall, ensure that any closing-out or unwinding of a Designated Index Arbitrage Transaction conducted by its or its registered arbitrageur's designated SEHK Participant on its or its registered arbitrageur's behalf complies with the conditions and criteria set forth in the Rules of SEHK relating to the closing-out or unwinding of a Designated Index Arbitrage Transaction.
1607. Unless otherwise permitted by the Exchange, no external allocation or transfer of positions in a Designated Stock Index Futures Contract conducted as part of a Designated Index Arbitrage Transaction for which the Tick Rule Exemption is claimed from one Designated Index Arbitrage Participant to another will be permitted.
1608. Each Designated Index Arbitrage Participant shall keep as part of its records and make available to the Exchange or the Commission for inspection when requested to do so and within such period of time as specified in the request, all information regarding Designated Index Arbitrage Transactions conducted for its own account or for the account of its registered arbitrageur.
1609. Each Designated Index Arbitrage Participant shall procure its registered arbitrageur to make available to the Exchange or the Commission for inspection all books and records regarding the registered arbitrageur's relevant Designated Index Arbitrage Transactions within 3 Business Days of the Exchange or the Commission's request or within such other period as may be specified by the Exchange or the Commission in its request.
1610. The Exchange may disclose any information relating to a Designated Index Arbitrage Participant or its registered arbitrageur to SEHK or any recognized exchange controller which is the controller of the Exchange in connection with any inquiry, investigation, action or disciplinary proceedings that may be brought against the Designated Index Arbitrage Short Selling Participant (as defined in the Rules of SEHK) which the Designated Index Arbitrage Participant or its registered arbitrageur has designated to conduct Designated Index Arbitrage Transactions on SEHK on its behalf. The Exchange shall also be permitted to use and rely on any information regarding a Designated Index Arbitrage Participant or its registered arbitrageur that has been provided by SEHK or any recognized exchange controller which is the controller of SEHK in connection with any inquiry, investigation, action or disciplinary proceedings that may be brought against the Designated Index Arbitrage Participant.
1611. Each order of a Designated Stock Index Futures Contract relating to a Designated Index Arbitrage Transaction for which the Tick Rule Exemption is claimed shall be entered into HKATS by a Designated Index Arbitrage Participant with a specific transaction indicator assigned by the Exchange followed by a transaction nature indicator and a transaction reference number

in the customer information field of the Order Entry Window (in sequential order). The Designated Index Arbitrage Participant shall ensure that the same assigned transaction indicator, transaction nature indicator and transaction reference number is used by the relevant Designated Index Arbitrage Short Selling Participant of SEHK when executing the Designated Index Arbitrage Transactions that correspond to such order on SEHK on its or its registered arbitrageur's behalf.

1612. Each Designated Index Arbitrage Participant shall report all errors relating to a Designated Index Arbitrage Transaction in such manner as may be prescribed by the Exchange from time to time.
1613. Each Designated Index Arbitrage Participant shall procure its registered arbitrageur to comply with the relevant obligations set forth in the Rules of this Chapter and shall be fully responsible and liable and may be subject to disciplinary proceedings for any non-compliance by its registered arbitrageur.

#### Tick Rule Exemption in relation to Stock Futures Hedging Transactions

1614. A Market Maker in the Stock Futures Market wishing to be exempt from the Tick Rule in relation to Stock Futures Hedging Short Selling must be registered with the Exchange as a Stock Futures Hedging Participant. In order to be so registered, the Market Maker shall apply to the Exchange by completing such form and complying with such instructions as may from time to time be prescribed by the Exchange. The Market Maker shall also apply to the Exchange to register an SEHK Participant which will conduct on SEHK on its behalf such parts of the Stock Futures Hedging Transaction that need to be conducted on SEHK. The decision as to whether or not to approve the application is entirely at the discretion of the Exchange. The Exchange may impose such conditions as it thinks fit on the approval of such application.
1615. A Market Maker shall ensure that so long as it is registered as a Stock Futures Hedging Participant, the following conditions are at all times satisfied:
  - (i) Stock Futures Hedging Transactions are only conducted for an account of the Market Maker;
  - (ii) it has designated only one SEHK Participant, which is registered with SEHK as a Designated Stock Futures Hedging Short Selling Participant under the Rules of SEHK to conduct on SEHK on behalf of the Market Maker such parts of the Stock Futures Hedging Transactions that need to be conducted on SEHK; and
  - (iii) such other conditions as may from time to time be prescribed by the Exchange.

1616. Each Exchange Participant shall, and shall procure that the Designated Stock Futures Hedging Short Selling Participant which it has designated to conduct Stock Futures Hedging Transactions on SEHK on its behalf shall, ensure that, at all times, the extent to which the Tick Rule Exemption may be claimed by a Designated Stock Futures Hedging Short Selling Participant in respect of Stock Futures Hedging Short Selling of shares underlying a particular Stock Futures Contract conducted for the account of each Stock Futures Hedging Participant shall be subject to a maximum hedging limit. For the purpose of Stock Futures Hedging Transactions, the maximum hedging limit for each Stock Futures Contract equals 1.1 multiplied by the number of contracts held by the Stock Futures Hedging Participant in the Stock Futures Contract which are not hedged by an offsetting transaction multiplied by the Contract Multiplier of the Stock Futures Contract. Positions in such Stock Futures Contract which are not hedged by offsetting transactions cannot be carried forward to the next Trading Day for the calculation of the maximum hedging limit, unless they have been reported to the Exchange in such manner as prescribed by the Exchange from time to time. Under no circumstances shall a position in Stock Futures Contract which is not hedged be carried forward for more than one Trading Day for the calculation of the maximum hedging limit.
1617. Each Exchange Participant shall keep as part of its records and make available to the Exchange or the Commission for inspection when requested to do so and within such period of time as specified in the request, all information regarding Stock Futures Hedging Transactions of the Stock Futures Hedging Participants registered through it, including but not limited to the following:
- (i) details of each component comprising a hedging portfolio, whether such component relates to a Stock Futures Contract, securities or any other type of instrument;
  - (ii) the positions, whether long or short, of each component comprising the hedging portfolio at the beginning and at the close of each Trading Day; and
  - (iii) any other particulars as may be prescribed by the Exchange from time to time.
1618. The Exchange may disclose any information relating to a Stock Futures Hedging Participant or a Designated Stock Futures Hedging Short Selling Participant to SEHK or any recognized exchange controller of the Exchange in connection with any inquiry, investigation, action or disciplinary proceedings that may be brought against the Designated Stock Futures Hedging Short Selling Participant. The Exchange shall also be permitted to use and rely on any information regarding a Stock Futures Hedging Participant or a Designated Stock Futures Hedging Short Selling Participant that has been provided by SEHK or any recognized exchange controller which is the controller of SEHK in connection with any inquiry, investigation, action or

disciplinary proceedings that may be brought against an Exchange Participant in respect of any Stock Futures Hedging Participant registered through it.

1619. Each Exchange Participant shall report all errors relating to transactions in Stock Futures Contracts conducted by its Stock Futures Hedging Participants as part of their Stock Futures Hedging Transactions in such manner as prescribed by the Exchange from time to time.