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Hong Kong Exchanges and Clearing Limited is a recognized exchange controller under the Securities and Futures Ordinance which is the controller of The Stock Exchange of Hong Kong Limited, Hong Kong Futures Exchange Limited, Hong Kong Securities Clearing Company Limited, The SEHK Options Clearing House Limited, HKFE Clearing Corporation Limited and OTC Clearing Hong Kong Limited.

通告 CIRCULAR

Subject: Compliance Bulletin (Issue No. 7) – (1) Block Trade Execution, (2) Large Open Position (“LOP”) Reporting Procedures for Derivatives Holiday Trading, and (3) Standard Penalties under HKEX Rules

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As part of our continuous efforts to promote transparency and a compliance culture in our marketplace, the Exchange has prepared this Compliance Bulletin to offer the industry a better understanding of our enforcement work and regulatory expectations. It includes some common deficiencies and related issues identified as well as good practices observed in (1) block trade execution, and also a reminder on (2) LOP reporting requirements for Derivatives Holiday Trading and (3) standard penalties under HKEX Rules.

(1) Block Trade Execution

To ensure that Exchange Participants (“EPs”) can continuously and consistently comply with the Block Trade rules and regulations, HKEX would like to reinforce and remind EPs of the following:

1. Relevant regulations, rules and guidelines

- (i) Rules, Regulations and Procedures of the Futures Exchange (“**HKFE Rules**”)
 - o Chapter VIII (815 – 815D) – Execution of Block Trades
- (ii) Options Trading Rules of the Stock Exchange (“**SEHK OTR**”)
 - o Third Schedule – Regulations for Block Trades
- (iii) Circular
 - o Guidance on Block Trade Order Aggregation (Ref. No.: [MO/DT/116/20](#))
- (iv) Others
 - o Block Trade Facility Education Seminar Materials (18 May 2021) ([Presentation](#))
 - o Frequently Asked Questions (Updated on 19 October 2021) ([PDF](#))

2. Key requirement areas

Block Trade orders must be executed in accordance with requirements laid down in HKFE Rule 815A / Paragraph 2 of the Third Schedule to the SEHK OTR, including the following:

- (i) Execution Price: the price must be fair and reasonable, i.e. within the Permissible Price Range¹, which is determined in the following manners:
 - o When the executed price is at or within the range of highest traded price², lowest traded price, bid and ask price of contract; or
 - o When the executed price is within the price range to both sides of a reference price obtained through prevailing market prices, or if necessary, determined as the theoretical values based on the prevailing underlying values.
- (ii) Volume: the Block Trade must satisfy the Minimum Volume Threshold (“MVT”)³;
- (iii) Single Order Block Trade Requirement: When a Block Trade in HKFE with multiple legs (i.e. spread or strategy combination) involves one buyer and one seller only, EPs should follow the requirement under Note 1 of HKFE Rule 815A(2)(a) – i.e. at least one of the legs of the spread or strategy combination must meet the Minimum Volume Threshold; and
- (iv) Order Aggregation Rule: Where a Block Trade involves aggregation of separate orders, the aggregation rules under HKFE Rule 815A(2A) / Paragraph 2 of the Third Schedule to the SEHK OTR must be followed. The aggregation rules states that an EP cannot aggregate separate orders or combine separate orders to generate a spread or strategy combination Block Trade unless that order meets the applicable MVT and the EP has received instructions or has been specifically authorized to execute the order as a Block Trade.

3. Deficiencies and instances of non-compliance

Non-compliance with HKFE Rule 815A(2A)(b): For Futures Contracts only order aggregation, each separate order comprising the Block Trade has to satisfy the applicable MVT;

- (i) Some EPs aggregated orders from clients to execute the Block Trade. However, the orders failed to meet the MVT requirement for Order Aggregation (for illustration, please refer to Scenario 1 of Appendix 1);
- (ii) For a single order Block Trade involving only one buyer and one seller, some EPs inappropriately aggregated the clients’ orders with their house orders in order to fulfil the MVT requirement of the Block Trade (for illustration, please refer to Scenario 2 of Appendix 1);
- (iii) In situations where the Block Trade quantities of two clients’ bid and ask orders are different, some EPs filled the difference by using house orders, albeit failed to meet the MVT

¹ The Permissible Price Range of each product eligible for block trading is set out in the Block Trade Facility web corner of the HKEX Website.

² The highest traded price means the day-high at the time when the block trade is reported.

³ The MVT each product eligible for block trading is set out in the Block Trade Facility web corner of the HKEX Website.

requirement. This is in breach of the aggregation requirement (for illustration, please refer to Scenario 3 of Appendix 1); and

- (iv) Some EPs misunderstood that each post-trade allocation (i.e. give-up and take-up) needs to fulfil the MVT requirements for Order Aggregation. As long as the original order meets the MVT requirement, the related post trade allocation would not have caused the Block Trade to have breached the MVT requirement (for illustration, please refer to Scenario 4 of Appendix 1).

4. Common misunderstandings on Block Trade execution requirements

Below are two common misunderstandings:

- (i) Interpreting single order Block Trade as Block Trade with order aggregation incorrectly

For a Block Trade that involves multiple legs arising from one buyer and one seller only, some EPs misunderstood that such Block Trade constitutes an aggregation of order and apply the Block Trade Aggregation Rule. In fact, they should regard the Block Trade as a single order Block Trade and follow the requirement in Note 1 of HKFE Rule 815A(2)(a) (Frequently Asked Questions Q5).

- (ii) Misunderstanding of requirement of Order Aggregation Rule

- For a Block Trade comprising orders with futures and options legs, some EPs misunderstood that only one of the separate orders comprising a future leg satisfying the applicable MVT is sufficient in complying with HKFE Rule 815A(2A)(c) – For Futures Contracts and / or Option Contracts with Order Aggregation, at least one of the separate orders comprising an option leg has to satisfy the applicable MVT. This is an incorrect understanding as the requirement is one of the separate orders comprising an option leg has to satisfy the applicable MVT;
- For a Block Trade strategy involves Futures Contracts only, some EPs misunderstood that each leg comprising the Block Trade strategy needs to satisfy the applicable MVT, which in fact is each separate order needs to satisfy the applicable MVT (HKFE Rule 815A(2A)(b)).

5. Good practices observed

- (i) Regular training: provide staff responsible for Block Trade execution to ensure that they are familiar with the relevant rules and requirements in relation to Block Trades executed via the Block Trade Facility, in particular when there are personnel changes;
- (ii) Proper internal controls and procedures: in relation to Block Trade execution via the Block Trade Facility, such as independent checking by compliance officer / operation teams;
- (iii) Regular review of the policies, procedures and internal controls in relation to Block Trade execution via the Block Trade Facility;

- (iv) Proactively clarify with the Exchange on questions in Block Trade executions prior to execution to avoid rule breach;
- (v) Avoid using the same value (e.g. company names) in the Info Field in Block Trade throughout the day, which may unintentionally group separate Block Trades into the same strategy; and
- (vi) Input different values to the Info Field to differentiate separate Block Trade strategies within the same firm. E.g. Different traders should use different Info Field from each other to avoid unintentional grouping of their Block Trades.

6. Consequence of non-compliance

Hong Kong Futures Exchanges Limited (“**HKFE**”)/The Stock Exchange of Hong Kong Limited (“**SEHK**”) will consider the nature and specific circumstance of the case that resulted in non-compliance. In cases where non-compliance was resulted from genuine mistakes or errors, HKFE/SEHK may take enforcement actions against the EP, including issuance of compliance reminder to the EP at the first time of non-compliance and reserve the right to take further disciplinary actions such as prohibition of Block Trade execution or imposition of restrictions/additional criteria should there be any repeated non-compliance on the part of the EP.

Pursuant to HKFE Rule 815C and Regulation 5 of the Third Schedule of the SEHK OTR, if the Chief Executive of HKFE/SEHK is of the opinion that any of the prescribed criteria are not properly followed by an EP, the Chief Executive may prohibit the EP from using the Block Trade Facility or impose such restrictions or additional criteria as he may consider appropriate on its use. Any Block Trade which is executed in breach of such notice will not be considered as a valid trade by the Exchange and will not be registered or cleared by the relevant clearing house.

(2) Large Open Positions (“LOP”) – Reminder for LOP reporting requirements during Holiday Trading days

HKFE has launched the Derivatives Holiday Trading in May 2022. To ensure the Holiday Trading EPs can consistently comply with the LOP reporting procedures and requirements for Holiday Trading Exchange Contracts (“**H-Contracts**”) during the Hong Kong public holidays with trading and clearing services (“**H-Days**”), HKEX would like to remind Holiday Trading EPs of the following:

1. LOP report submission during consecutive H-Days

Holiday Trading EPs are reminded that LOP report for H-Contracts shall be filed with HKFE by no later than 12:00 noon of the next Trading Day, regardless of whether it is a Hong Kong public holiday or not, after the positions are opened or accumulated and shall continue to make reports for as long as the Holiday Trading EPs or their Clients hold a LOP on H-Contracts.

For example, in the upcoming consecutive Hong Kong public holidays on Good Friday (7th April) and Easter Monday (10th April), Holiday Trading EPs are reminded to continue to file the LOP report on each of the Trading Day as long as their own accounts or their Clients hold a LOP in any of the H-Contracts.

2. Possible enforcement actions against non-compliance of LOP reporting requirements

Reference is made to the Circular published in April 2022 (Ref. No.: [MSM/003/2022](#)), any failure to comply of LOP reporting requirements for H-Contracts during the H-Days may result in the below possible regulatory actions from the HKFE:

(i) Holiday Trading EP

The HKFE may impose, depending on the seriousness, a summary fine and/or take further disciplinary actions against a Holiday Trading EP for any non-compliance of the LOP reporting requirements in accordance with the HKFE Rules.

(ii) A person other than a Holiday Trading EP

Pursuant to HKFE Rule 630(a), where the Exchange has grounds to believe that any person has failed to comply with the LOP reporting requirements, the Exchange may prescribe the maximum number or value of long or short H-Contracts in respect of any Market which any Holiday Trading EP or Holiday Trading EPs is/are permitted to buy or sell on behalf of such person.

In this regard, Holiday Trading EPs shall put in place adequate controls and procedures to ensure compliance with the LOP reporting requirements at all times. Furthermore, Holiday Trading EPs should take all reasonable steps to inform their clients of the LOP reporting procedures and requirements related to H-Contracts during the H-Days.

(3) Standard Penalties under HKEX Rules

EPs and Clearing Participants (“**CPs**”) (collectively “**Participants**”) are expected to keep abreast of all the relevant HKEX rules and regulations applicable to them at all times. HKEX takes any rule breaches seriously and may consider taking disciplinary actions against any non-compliant Participants, including issuance of warning letter, imposition of fine and initiation of disciplinary proceedings.

Accordingly, HKEX would like to remind Participants of a few key areas under the exchange and clearing rules where standard penalties would apply to certain offences (“**Summary Fine Offences**”) as explained further below. These offences include the failure to comply with (i) investor eligibility requirements, (ii) certain submission requirements under the Hong Kong Investor Identification Regime (“**HKIDR**”), (iii) settlement obligations towards the clearing houses, and (iv) capital-based position limit (“**CBPL**”).

(i) Investor Eligibility Requirements and (ii) HKIDR submission requirements under the Rules of the Exchange (“SEHK Rules”)

Reference is made to circulars published in December 2021 (Ref. No.: [LSD/091/2021](#)) and March 2023 (Ref. No.: [LSD/016/2023](#)) which respectively requested EPs to note, amongst other things, the following Summary Fine Offences:

Rules Reference	Summary Fine Offences	Schedule of Penalties
<ul style="list-style-type: none"> ▪ SEHK Rules Chapter 7 ▪ SEHK Disciplinary Procedures Part II and the Schedule of Penalties 	<p>(1) Investor Eligibility Requirements</p> <p>Failure of an EP, a China Connect EP or a SPAC EP to comply with the requirements under SEHK Rules 525A(2), Rule 14A06(15), Rule 14B06(18) or Rule 593(6), as the case may be, within a 12 month rolling period.</p> <p>(2) HKIDR</p> <p>Failure of a Relevant Regulated Intermediary, which is an EP, to comply with the requirements under Rule 538A(3), 538A(4), 538A(5), 538A(6)(d) and 538A(8), as the case may be, within a 12-month rolling period.</p>	<p><u>First offence</u> Issuance of a warning letter</p> <p><u>Second offence</u> An imposition of a fine of HK\$25,000</p> <p><u>Third offence</u> An imposition of a fine of HK\$50,000</p> <p><u>Any subsequent offence</u> To be treated as an offence to be dealt with by hearings in accordance with the Procedures For Offences To Be Dealt With By Hearings</p>

(iii) Settlement Obligations towards clearing houses and (iv) CBPL respectively under the Rules and Procedures of HKCC (“HKCC Rules”), General Rules of CCASS (“CCASS Rules”) and Options Clearing Rules of SEOCH (“SEOCH Rules”)

In addition, CPs should note the circular published in March 2019 (Ref No.: MSM/003/2019 – [HKCC/HKSCC/SEOCH](#)), which stated, amongst other things, that without prejudice to any other actions that the relevant clearing house may take against the non-compliant CP, standard penalties summarized as follows shall apply:

Clearing House	Rules Reference	Summary Fine Offences	Standard Penalties
HKCC	<ul style="list-style-type: none"> ▪ HKCC Rule 527 	<ol style="list-style-type: none"> 1. A late payment of any settlement amount, variation adjustment or margin due to operations oversight or other minor mistakes. 2. A breach of CBPL⁴ 	<p><u>First offence</u> Issuance of a compliance advice letter</p>
HKSCC	<ul style="list-style-type: none"> ▪ CCASS Rule 2008 ▪ Section 20.5.2 of the CCASS Operational Procedures 	Late payment of any settlement amount or failure to comply with any collateral requirement due to operations oversight or other minor mistakes.	<p><u>Second offence</u> Issuance of a warning letter and imposition of a fine of HK\$10,000</p> <p><u>Third offence</u> Issuance of a warning letter and imposition of a fine of HK\$25,000</p>
SEOCH	<ul style="list-style-type: none"> ▪ SEOCH Rule 807 	<ol style="list-style-type: none"> 1. A late payment of Premium, Settlement Amount or margin due to operations oversight or other minor mistakes 2. A breach of CBPL⁵ 	<p><u>Fourth offence</u> Refer the case to Disciplinary Committee</p>

The Exchange would like to point out that the requirements and examples set out in this compliance bulletin are by no means exhaustive and Participants should always take into consideration their own circumstances and adopt appropriate internal controls and measures to ensure compliance with the relevant rules and requirements.

Participants are strongly advised to review their current set up and implement appropriate measures to strengthen their controls. Any identified non-compliance incidents should be reported to the Exchange as soon as practicable.

Participants are also encouraged to contact the Market Surveillance and Monitoring Department (email: surveillance@hkex.com.hk) should they have any questions on the above.

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This circular has been issued in English together with Chinese translation of the same. If there is any discrepancy between the Chinese translation and the English version, the English version shall prevail.

⁴ Unless, in the case of a breach of position limit during the T Session, the breach is remedied by the HKCC Participant within 10 Business Days as provided under section 5.2 of the HKCC Clearing Procedures.

⁵ Unless the breach is remedied by the SEOCH Participant within 10 Business Days as provided under Section 12.5 of the Operational Clearing Procedures.

Appendix 1

Scenario 1

Clients' Order Instructions (Price of \$8,600):

Client A: Long x100 contracts of HHIU1.

Client B: Short x50 contracts of HHIU1.

Client C: Short x50 contracts of HHIU1.

MVT = 100. The clients' orders do NOT fulfil MVT

Client B & Client C's orders were below the MVT requirement of HHI Futures for Order Aggregation, which is in breach of Order Aggregation Rule.

Leg	Trade	Contract	Volume	Price	Bid/Ask	Client / House Order
1	Trade Entered	HHIU1	100	\$8,600		
	Take Up	HHIU1	100		Bid	Client A
	Take Up	HHIU1	50		Ask	Client B
	Take Up	HHIU1	50		Ask	Client C

Scenario 2

Clients' Order Instructions (Price of \$9,400):

Client A: Long x20 contracts of HHIU1.

Client B: Short x20 contracts of HHIU1.

MVT = 100. The clients' order does NOT fulfil MVT

The EP aggregates its house order with its clients' orders for the purpose of fulfilling the MVT requirement of 100 contracts, which is in breach of Order Aggregation Rule

Leg	Trade	Contract	Volume	Price	Bid/Ask	Clients/ House Order
1	Trade Entered	HHIU1	100	\$9,400		
	No Take Up	HHIU1	80		Bid	House Order
	No Take Up	HHIU1	80		Ask	House Order
	Take Up	HHIU1	20		Bid	Client A
	Take Up	HHIU1	20		Ask	Client B

Scenario 3

Clients' Order Instructions (Price of \$8,775)

Client A: Long x100 contracts of HHIX1

Client B: Short x103 contracts of HHIX1

MVT = 100. The clients' order fulfil MVT

Client A and Client B's orders have already fulfilled the MVT requirements but the quantities of Client A's bid order and Client B's ask order of the Block Trade did not match.

The EP aggregates its house orders with clients' orders of which the house orders fail to meet the MVT requirement for Order Aggregation, which is in breach of Order Aggregation Rule

Leg	Trade	Contract	Volume	Price	Bid/Ask	Client / House Order
1	Trade Entered	HHIX1	103	\$8,775		
	No Take Up	HHIX1	3		Bid	House Order
	Take Up	HHIX1	100		Bid	Client A
	Take Up	HHIX1	103		Ask	Client B

Scenario 4

Clients' Order Instructions (Price of \$600.55):

Client A: Long x218 contracts of MTWX1

Client B: Short x109 contracts of MTWX1

Client C: Short x109 contracts of MTWX1

MVT = 50. The clients' orders fulfil MVT

The EP executed orders from Client A, Client B and Client C into an Aggregated Block Trade and split them each into two trades (Leg 1 and Leg 2) in order to match with order price (i.e. \$600.55).

However, the EP misunderstood that the two legs of Ask order of x49 contracts of Client B and Client C were below the MVT requirements for Order Aggregation.

The EP entered 220 contracts and adjusted the 2 legs of Ask Order x49 contracts of Client B and Client C to x50 contracts by aggregating house orders of x2 contracts with clients' orders in order to meet the MVT requirements. The house order of x2 contracts failed to meet the MVT requirement of 50, hence a breach of the Order Aggregation Rule (see table below for details):

Leg	Trade	Contract	Volume	Price	Bid/Ask	Client / House Order
1	Trade Entered	MTWX1	120	\$600.5		
	Take Up	MTWX1	120		Bid	Client A
	No Take Up	MTWX1	2		Ask	House Order
	Take Up	MTWX1	59		Ask	Client B
	Take Up	MTWX1	59		Ask	Client C
2	Trade Entered	MTWX1	100	\$600.6		
	Take Up	MTWX1	98		Bid	Client A
	No Take Up	MTWX1	2		Bid	House Order
	Take Up	MTWX1	50		Ask	Client B
	Take Up	MTWX1	50		Ask	Client C

The aggregated Block Trade would have met the Block Trade Order Aggregation Rule if treated as below:

Leg	Trade	Contract	Volume	Price	Bid/Ask	Client / House Order
1	Trade Entered	MTWX1	120	\$600.5		
	Take Up	MTWX1	120		Bid	Client A
	Take Up	MTWX1	60		Ask	Client B
	Take Up	MTWX1	60		Ask	Client C
2	Trade Entered	MTWX1	98	\$600.6		
	Take Up	MTWX1	98		Bid	Client A
	Take Up	MTWX1	49		Ask	Client B
	Take Up	MTWX1	49		Ask	Client C