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## Section 10

### Exchange Trades - CNS System

For the purposes of this Section 10, (i) references to “Eligible Securities” mean Eligible Securities other than China Connect Securities; (ii) references to “Participants” mean Clearing Participants and Clearing Agency Participants; and (iii) references to “Exchange Participants” include Special Participants, unless specified otherwise.

#### 10.1 ACCEPTANCE FOR SETTLEMENT UNDER THE CNS SYSTEM

##### 10.1.1 Details of Exchange Trades

Arrangements have been made by HKSCC for details of Exchange Trades to be reported to HKSCC on a daily basis. Participants will not, therefore, generally have to input into CCASS details of Exchange Trades. However, HKSCC reserves the right to require Participants to provide details of Exchange Trades executed by them or, in the case of GCPs, including those concluded and designated to them for clearing by their NCPs to it.

Subject to any Trade Amendments, any “late” Exchange Trades and trades not recognized by the Exchange as referred to in Section 10.2, Exchange Trades will be settled under the CNS System unless they are isolated from the CNS System by the counterparty Exchange Participants at the time of trade or unless they are isolated from the CNS System by HKSCC.

##### 10.1.2 Confirmation of acceptance under the CNS System

Acceptance by HKSCC of Exchange Trades for settlement under the CNS System will only be confirmed by details contained in the second batch of PCSs issued by HKSCC to Participants at or about 8:00 p.m. on each Business Day.

Subject to any Trade Amendments, any “late” Exchange Trades and trades not recognized by the Exchange as referred to in Section 10.2, an Exchange Trade accepted for settlement under the CNS System will not normally be excluded from the CNS System by HKSCC subsequent to the issue of the relevant PCS.

##### 10.1.3 "Guarantee" by HKSCC

Since acceptance for settlement under the CNS System involves the substitution of HKSCC as settlement counterparty, a form of "guarantee" is in effect provided by HKSCC to Participants in respect of Exchange Trades accepted for settlement under the CNS System.

##### 10.1.4 Availability of PCSs

Hard copies of PCSs issued by HKSCC to Participants on each Business Day can be obtained by such Participants via their CCASS Terminals or Participant Gateways. PCSs are generated twice daily on each Business Day.

##### 10.1.5 Information contained in PCSs

A PCS will provide a Participant with information in relation to all Exchange Trades and/or Clearing Agency Transactions to be cleared and settled by the Participant on that day. For a particular day, a PCS will set out the details of Exchange Trades and/or Clearing Agency Transactions to be settled under the CNS System and the details of its net stock settlement positions in each Eligible Security traded that day (and the relevant money positions). Where the Eligible Security is a Multi-counter Eligible Security, the

PCS will set out the net stock settlement positions in each of the Eligible Currency traded that day (and the relevant money positions).

For Exchange Trades relating to interest-bearing eligible Debt Securities, accrued interest amount and trade amount of the trades will be displayed separately in the PCSs. In addition, other information such as interest calculation method, interest rate used and number of days used in the calculation of accrued interest will also be provided in the PCSs.

Details of the Exchange Trades to be settled under the Isolated Trades System and details of trades in non-Eligible Securities will also be provided in the PCSs.

Details of Clearing Agency Transactions to be settled under the CNS System or the Isolated Trades System will be included in the second batch of PCSs only.

The information contained in a PCS will only be indicative of the settlement obligations of a Participant on the due settlement date (i.e. T+2). Trade Amendments may be made, "late" Exchange Trades may be accepted, trades not recognized by the Exchange may be excluded and the settlement obligations may be affected by unsettled positions under the CNS System in the intervening day (i.e. T+1) before the due settlement date.

The main purpose of a PCS, in addition to allowing a Participant to make initial preparation for settlement, is to allow a Participant to carry out daily reconciliation with its internal records of the Exchange Trades and/or Clearing Agency Transactions.

Where a Participant is in the process of opening a bank account in an Eligible Currency for money settlement of Exchange Trades and/or Clearing Agency Transactions accepted under the CNS System, a message will be posted on the PCSs of the Participant concerned to alert the Participant about the alternative payment methods available.

## **10.2 TRADE AMENDMENTS, "LATE" EXCHANGE TRADES AND TRADES NOT RECOGNIZED BY THE EXCHANGE**

### **10.2.1 Rectification of errors by Trade Amendments**

Arrangements have been made by HKSCC for details of Trade Amendments to be reported to it by the Exchange. Provided that such details are received by HKSCC on the Business Day following the relevant day of trade, before the usual time for the issue of the FCSs by HKSCC (see Section 10.2.3), HKSCC will normally accept such Trade Amendments and cause the relevant adjustments to be made to the settlement positions of the Participants concerned under the CNS System. However, HKSCC reserves the right not to accept Trade Amendments even if the Exchange has given approval and if so, will notify the Participants concerned as soon as possible. For those Trade Amendments relating to Exchange Trades in which a GCP or a Clearing Agency Participant has been substituted as a party, the GCP or Clearing Agency Participant shall notify the NCP or Special Participant concerned that the Trade Amendment has not been accepted by HKSCC.

### **10.2.2 "Late" Exchange Trades**

Exchange Trades conducted on a particular day may not be reported to the Exchange by the Exchange Participants in time for the details of such Exchange Trades to be reported by the Exchange to HKSCC on the same day. The reporting of such late Exchange Trades by the Exchange Participants concerned to the Exchange will be dealt with by the Exchange as a form of Trade Amendment. Treatment of such "late" Exchange Trades by HKSCC will be the same as Trade Amendments as described in Section 10.2.1 except that this Section 10.2.2 on "Late" Exchange Trades shall not apply to

Special Participants.

Arrangements have been made by HKSCC for details of such "late" Exchange Trades to be reported to it by the Exchange. HKSCC reserves the right not to accept such late Exchange Trades for settlement under the CNS System.

#### **10.2.2A Trades not recognized by the Exchange**

Trades in a Structured Product which are effected on or reported to the Exchange on a particular day after the time of the relevant call event as notified by the Issuer of the Structured Product to or otherwise determined by the Exchange and which are not recognized by the Exchange in accordance with the Exchange Rules may not be reported by the Exchange to HKSCC on the same day, or even if on the same day, may not be reported in time for such trades to be excluded from the relevant PCSs. Any such trades not recognized by the Exchange, if not already excluded from the PCSs issued to the Clearing Participants, will be excluded from the FCSs (see Section 10.2.3).

#### **10.2.3 Confirmation of acceptance under CNS System of Exchange Trades subject to Trade Amendments and "late" Exchange Trades and exclusion of trades not recognized by the Exchange**

Acceptance by HKSCC of the Exchange Trades subject to Trade Amendments for settlement under the CNS System and "late" Exchange Trades as referred to in Section 10.2.2, as well as exclusion of trades not recognized by the Exchange as referred to in Section 10.2.2A, will be confirmed by details contained in the FCSs issued by HKSCC daily to Clearing Participants at or about 2:00 p.m., on the Business Day following the relevant day of trade.

#### **10.2.4 Availability of FCSs**

Hard copies of FCSs, issued by HKSCC to Participants on each Business Day, can be obtained by the Participants via their CCASS Terminals or Participant Gateways.

#### **10.2.5 Information contained in FCSs**

A FCS will contain the following information in relation to (a) trades of a Participant and, in the case of a GCP, including those of its NCPs concluded on the Exchange and designated to it for clearing, or in the case of a Clearing Agency Participant, including those of its Special Participants concluded on the Exchange and/or (b) Clearing Agency Transactions of a Participant and, in the case of a GCP, including those of NCPs, effected on the previous Business Day (i.e. T-day) and which are to be settled on the following Settlement Day (i.e. T+2):

- (i) the net stock positions with HKSCC in each Eligible Security (and/or, where an Eligible Security is a Multi-counter Eligible Security, the net stock positions in each of the Eligible Currency traded) (which will each be assigned a unique settlement position number) and their related money positions under the CNS System (taking into account any Trade Amendments accepted by HKSCC, any "late" Exchange Trades accepted by HKSCC and the exclusion of any trades not recognized by the Exchange) as well as details of individual Exchange Trades and Clearing Agency Transactions of a Participant effected on the previous Business Day;
- (ii) the net money position with HKSCC for all net stock positions under the CNS System;
- (iii) details of Exchange Trades accepted for settlement under the Isolated Trades System and their related money positions (including any Trade Amendments thereto approved by the Exchange) and accrued interest amounts of Exchange

Trades in eligible interest-bearing Debt Securities;

- (iv) details of Clearing Agency Transactions accepted for settlement under the CNS System or accepted for settlement under the Isolated Trades System and their related money positions (including any amendments thereto accepted by HKSCC);
- (v) details of Trade Amendments, any "late" Exchange Trades accepted by HKSCC and the exclusion of any trades not recognized by the Exchange, if any;
- (vi) details of trades effected in securities listed on the Exchange which are not Eligible Securities (and any Trade Amendments thereto); and
- (vii) details of fees payable in relation to the settlement of Exchange Trades and Clearing Agency Transactions in CCASS (see Section 21.1).

Where a Participant is in the process of opening a bank account in an Eligible Currency for money settlement of Exchange Trades and/or Clearing Agency Transactions accepted under CNS System, a message will be posted on the FCS of the Participant concerned to alert the Participant about the alternative payment methods available.

#### **10.2.6 Accrued Interest Adjustment**

For trades in floating rate Debt Securities effected in one interest period and which are due for settlement on or after the first day of the next following interest period, it is possible that interest rate of the next following interest period may not be fixed by the trade day. Upon notification of the interest rate for the next following interest period by the issuer/issuer's agent, HKSCC may adjust the accrued interest amount of the affected positions.

Where other circumstances warrant, HKSCC may also adjust the accrued interest of both floating and fixed rate Debt Securities in line with market practice.

Details of the accrued interest adjustments are provided in the FCSs, Next Settlement Day Due/Overdue Position Reports, Settled Position Reports and Settlement Report (see CCASS Terminal User Guide for Participants for details), where applicable.

### **10.3 NETTING**

#### **10.3.1 Determination of daily stock settlement positions**

The daily stock settlement positions of a Clearing Participant or Clearing Agency Participant with HKSCC, arising out of Exchange Trades or Clearing Agency Transactions, as the case may be, accepted for settlement under the CNS System, will be determined based on the following steps:

- (i) Novation: the Novation of Exchange Trades and Clearing Agency Transactions upon their acceptance for settlement under the CNS System, pursuant to which HKSCC becomes substituted as the settlement counterparty to the relevant Clearing Participants and Clearing Agency Participants (the novated contracts being referred to as "Market Contracts");
- (ii) daily netting: the stock positions of a Clearing Participant or Clearing Agency Participant under the Market Contracts (which may include novated Clearing Agency Transactions), on the same day, in the same Eligible Security (and arising from Exchange Trades executed by the same Special Participant in the case of a Clearing Agency Participant which is a China Connect Clearing House), being

offset against each other to result in one net long or net short stock position with HKSCC, in each Eligible Security, on each Business Day (and in respect of each Special Participant in the case of a Clearing Agency Participant which is a China Connect Clearing House), provided that, in the case of an Eligible Security which is a Multi-counter Eligible Security, such offset will be for Market Contracts traded in the same Eligible Currency, so as to result in one net long or net short stock position with HKSCC in each of the Eligible Currency traded. Each such net long or net short stock position of a Clearing Participant or Clearing Agency Participant will be assigned a unique Settlement Position Number for reference purposes;

- (iii) cross-day netting: the netting process operates on a continuous basis in the sense that any outstanding unsettled stock position of a Clearing Participant or Clearing Agency Participant in an Eligible Security (and in respect of the same Special Participant in the case of a Clearing Agency Participant which is a China Connect Clearing House) on a Settlement Day is carried forward to the following Settlement Day and is offset against any opposite stock position in the same Eligible Security (and in respect of the same Special Participant in the case of a Clearing Agency Participant which is a China Connect Clearing House) due on the following Settlement Day. If the outstanding stock position so carried forward to the following Settlement Day and the stock position in the same Eligible Security (and in respect of the same Special Participant in the case of a Clearing Agency Participant which is a China Connect Clearing House) due for settlement on the following Settlement Day are both long or both short, the two stock positions will remain separate and distinct for settlement purposes in CCASS (although they will be added together for the purpose of determining the aggregate stock position of the Clearing Participant or Clearing Agency Participant in that Eligible Security, and in the case of a Clearing Agency Participant which is a China Connect Clearing House, in respect of the same Special Participant, at the time), provided that, in the case of an Eligible Security which is a Multi-counter Eligible Security, such offset under the cross-day netting process will be for Market Contracts traded in the same Eligible Currency, so as to result in one net long or net short stock position with HKSCC in each of the Eligible Currency traded; and
- (iv) same stock netting: before the first Batch-settlement-run on a Settlement Day, there will be a same stock netting process applicable to a Multi-counter Eligible Security, under which any unsettled stock positions of a Clearing Participant or Clearing Agency Participant in a Multi-counter Eligible Security traded in one Eligible Currency will be offset against the unsettled opposite direction stock positions of the same Multi-counter Eligible Security traded in other Eligible Currency (and in respect of the same Special Participant in the case of a Clearing Agency Participant which is a China Connect Clearing House) that are due or overdue on the same Settlement Day.

For a Multi-counter Eligible Security which is traded in more than two Eligible Currencies on the Exchange, HKSCC will conduct same stock netting in accordance with the following algorithm when there are more than one stock position of the same direction to be offset against another stock position of opposite direction:

- (a) age – the stock position which remains unsettled for the longest period of time; and if this is the same for all stock positions, then
- (b) position price (i.e. position amount divided by position quantity) – the long/short stock position which has the highest/lowest position price (to be calculated in HKD equivalent at the exchange rate determined by HKSCC from time to time for any non-HKD position price); and if this is the same for all stock positions, then
- (c) position size – the stock position which has the smallest size (i.e. quantity); and if this is the same for all positions, then
- (d) random.

### 10.3.2 Example (Novation)

The concept of Novation of an Exchange Trade and its replacement by two Market Contracts, with HKSCC being substituted as settlement counterparty, can be illustrated as follows.

An Exchange Trade involving Exchange Participant A buying 10,000 stock X from Exchange Participant B for HK\$100,000.

Upon Novation under the CNS System, the Exchange Trade will be replaced by the following two Market Contracts, each with HKSCC as settlement counterparty :

- (i) Market Contract between Participant A or GCP (if Participant A is a NCP) and HKSCC :

	Participant A	HKSCC
Stock position	10,000 (long)	10,000 (short)
Money position	\$100,000DR	\$100,000CR

- (ii) Market Contract between Participant B or GCP (if Participant B is a NCP) and HKSCC :

	Participant B	HKSCC
Stock position	10,000 (short)	10,000 (long)
Money position	\$100,000CR	\$100,000DR

The combined stock and money positions of HKSCC under the two Market Contracts replacing an Exchange Trade will be zero in each case.

### 10.3.3 Example (daily netting)

The concept of daily netting of Market Contracts in the same Eligible Security can be illustrated as follows :

On T-day, Participant A had the following five Exchange Trades for settlement in stock X.

Trade Counterparty	Settlement Counter-Party	Action by Participant A	Quantity (stock)	Unit Price	Money Positions
Participant B	HKSCC	Sell (Deliver)	10,000	\$10.0	\$100,000CR
Participant B	HKSCC	Sell (Deliver)	25,000	\$ 9.0	\$225,000CR
Participant C	HKSCC	Buy (Receive)	20,000	\$11.0	\$220,000DR
Participant D	HKSCC	Buy (Receive)	10,000	\$10.0	\$100,000DR
Participant E	HKSCC	Sell (Deliver)	15,000	\$11.0	\$165,000CR
			<u>Net sell (Deliver)</u>	<u>20,000</u>	<u>\$170,000 CR</u>

After netting, Participant A has a net short stock position of 20,000 in stock X, with a corresponding money position of \$170,000.00 CR. The average position price for the CNS stock position of Participant A in stock X is therefore \$8.5 (i.e. \$170,000 / 20,000).

#### 10.3.4 Example (cross-day netting - two opposite stock positions)

The concept of cross-day netting involving two opposite stock positions of a Participant in the same Eligible Security can be illustrated by using the following example:

At the beginning of a Settlement Day ("S-day"), Participant A has the following unsettled positions in stock X before the settlement on the day begins.

Due settlement date of stock positions	Unsettled stock positions	Money positions
S-1	2,000 (short)	\$2,200CR
S	3,000 (long)	\$3,600DR

At the beginning of S-day, the long stock position of 3,000 due on S-day will be offset against the outstanding short stock position of 2,000 due on S-1, as follows :

Due settlement date of stock position	Unsettled stock positions before cross-day netting on S-day	Stock positions offset under cross-day netting on S-day	Unsettled stock positions after cross-day netting
S-1	2,000 (short)	2,000 (short)	0
S	3,000 (long)	2,000 (long)	1,000 (long)

  

Due settlement date of stock positions	Money positions before cross-day netting on S-day	Money positions settled under cross-day netting on S-day	Unsettled money positions after cross-day netting
S-1	\$2,200CR	\$2,200CR	0
S	\$3,600DR	\$2,400DR*	\$1,200DR

Money position settled under cross-day netting: \$2,400 - \$2,200 = \$200 DR

\* The amount \$2,400 is derived from \$3,600 x 2,000/3,000

As a result of cross-day netting, Participant A has a net long stock position of 1,000 in stock X (with a corresponding money position of \$1,200 DR), to be settled on S-day. The amount of \$200 arising out of the process of cross-day netting will be debited by HKSCC to the Settlement Account (a sub-account of its Money Ledger) of Participant A for settlement on the same day.

Assuming the net long stock position of 1,000 with a corresponding position of \$1,200 DR in stock X has been settled during subsequent Batch-settlement-run on S-day. The total stock positions and money positions for stock X settled on S-day should be 1,000 long (3,000 - 2,000) and \$1,400 DR (\$3,600 - \$2,200)

### 10.3.5 Example (cross-day netting - stock positions both long or both short)

The concept of cross-day netting involving two stock positions of a Participant in the same Eligible Security which are both long or both short can be illustrated by using the following example.

Participant A has the following positions in stock X on S-day.

Due settlement date of stock positions	Unsettled stock positions	Money positions
S-1	2,000(short)	\$2,200CR
S	3,000(short)	\$3,600CR

On S-day, Participant A will have an aggregate short stock position of 5,000 in stock X. However, for the purpose of settlement under the CNS System, the two stock positions will remain separate and distinct. Similarly, the corresponding money positions of the two stock positions will also remain as separate and distinct.

Settlement may be effected in respect of the two stock positions in stock X on S-day.

### 10.3.6 Example (cross-day netting - three stock positions)

The concept of cross-day netting involving three stock positions of a Participant in the same Eligible Security, two of which being either both long or both short, and the remaining one being opposite to the other two, can be illustrated by using the following example. The example demonstrates that any offsetting by cross-day netting will be effected first against the oldest opposite stock position.

Participant A has the following three positions in stock X on S-day.

Due settlement date of stock positions	Unsettled stock positions	Money positions
S-2	2,000(short)	\$2,400CR
S-1	1,000(short)	\$1,300CR
S	2,600(long)	\$3,900DR

At the beginning of S-day, the long stock position of 2,600 due on S-day will be first offset against the "oldest" outstanding short position, i.e. the short stock position of 2,000 due on S-2. The remainder part of the long position will then be offset with the short position of 1,000 due on S-1. The result will be as follows:



<b>Stock Positions</b>	<b>Stock positions offset under cross-day netting</b>	<b>Money positions offset under cross-day netting</b>	<b>Unsettled stock positions after cross-day netting</b>	<b>Unsettled money positions after cross-day netting</b>
S-2	2,000(short)	\$2,400CR	Nil	Nil
S-1	600(short)	\$780CR	400(short)	\$520CR
S	2,600(long)	\$3,900DR	Nil	Nil

Following cross-day netting at the beginning of S-day, Participant A will have one outstanding CNS short position in stock X of 400, with a corresponding money position of \$520 CR.

It should be noted that a partial settlement has been made in respect of the outstanding short position of 1,000 due on S-1. The money settlement to be effected as a result of the partial delivery is worked out by multiplying \$1,300 by 600 / 1,000.

### 10.3.7 Example (daily netting for Multi-counter Eligible Securities)

Where stock X is a Multi-counter Eligible Security:

<b>Trade Counterparty</b>	<b>Settlement Counter-Party</b>	<b>Action by Participant A</b>	<b>Quantity (stock)</b>	<b>Unit Price</b>	<b>Money Positions</b>
Participant B	HKSCC	Sell (Deliver)	10,000	HKD10.0	HKD100,000CR
Participant B	HKSCC	Sell (Deliver)	25,000	HKD 12.0	HKD300,000CR
Participant C	HKSCC	Buy (Receive)	20,000	HKD11.0	HKD220,000DR
Participant D	HKSCC	Buy (Receive)	9,000	RMB10.0	RMB90,000DR
Participant E	HKSCC	Sell (Deliver)	15,000	RMB11.0	RMB165,000CR
<u>Net sell for HKD counter (Deliver)</u>			<u>15,000</u>		<u>HKD180,000 CR</u>
<u>Net sell for RMB counter (Deliver)</u>			<u>6,000</u>		<u>RMB75,000CR</u>

After daily netting, CNS positions will be generated for each of the Eligible Currency traded that day. Therefore, Participant A has a net short stock position of 15,000 (10,000 + 25,000 – 20,000) in stock X (traded in HKD counter), with a corresponding money position of HKD180,000.00 CR (HKD100,000 + HKD300,000 – HKD220,000), and a net short position of 6,000 (15,000 – 9,000) in stock X (traded in RMB counter), with a corresponding money position of RMB75,000 CR (RMB165,000 – RMB90,000). The average position price for the CNS stock position of Participant A in stock X is therefore HKD12.0 (HKD180,000 / 15,000) and RMB12.50 (RMB75,000 / 6,000) respectively.

### 10.3.8 Example (same stock netting for Multi-counter Eligible Securities - opposite stock positions)

Same stock netting only applies to opposite direction stock positions of a Multi-counter Eligible Security traded in different Eligible Currencies. The following example demonstrates that same stock netting will only apply to net long stock positions and net short stock positions of the same Multi-counter Eligible Security traded in different Eligible Currencies after the daily netting and/or cross-day netting processes.

At the beginning of S-day, Participant A has the following unsettled positions in stock W and stock X due on the same Settlement Day before the settlement on the day begins.

<b>Stock</b>	<b>Unsettled stock positions</b>	<b>Money positions</b>	<b>Money positions in HKD*</b>	<b>Unit Price in HKD</b>
Stock W	3,000 (short)	HKD15,000CR	15,000.00CR	5.00
Stock W	1,000 (long)	RMB4,500DR	4,815.00DR	4.82
Stock W	800 (long)	USD510DR	3,957.60DR	4.95
Stock X	4,000 (long)	HKD40,000DR	40,000.00DR	10.00
Stock X	2,000 (short)	RMB18,000CR	19,260.00CR	9.63
Stock X	800 (long)	USD1,025DR	7,954.00DR	9.94

*\*this example assumes the exchange rate for USD to HKD is 7.76:1 and RMB to HKD is 1.07:1.*

Pursuant to the same stock netting, the outstanding short stock position of 3,000 in stock W traded in HKD counter will be first offset against the outstanding long position of 800 in stock W traded in USD counter with the highest unit price, then 1,000 in stock W traded in RMB counter.

In the case of stock X, the outstanding short stock position of 2,000 in stock X traded in RMB counter will be offset against the outstanding long stock position of 4,000 in stock X traded in HKD counter with the highest unit price.

The result will be as follows:

<b>Stock</b>	<b>Stock positions offset under same stock netting</b>	<b>Money positions offset under same stock netting</b>	<b>Unsettled stock positions after same stock netting</b>	<b>Unsettled money positions after same stock netting</b>
Stock W	1,800 (short)	HKD9,000CR*	1,200 (short)	HKD6,000CR
Stock W	1,000 (long)	RMB4,500DR	Nil	Nil
Stock W	800 (long)	USD510DR	Nil	Nil
Stock X	2,000 (long)	HKD20,000DR**	2,000 (long)	HKD20,000DR
Stock X	2,000 (short)	RMB18,000CR	Nil	Nil
Stock X	Nil	Nil	800 (long)	USD1,025DR

\* The amount HKD9,000 is derived from HKD15,000 x 1,800 / 3,000

\*\* The amount HKD20,000 is derived from HKD40,000 x 2,000 / 4,000

### 10.3.9 Example (same stock netting for Multi-counter Eligible Securities - stock positions both long or both short)

The concept of same stock netting process involving two stock positions of the same direction of a Multi-counter Eligible Security traded in different Eligible Currencies can be illustrated by using the following example.

Participant A has the following two positions in stock X traded in different Eligible Currencies on S-day.

<b>Due settlement date of stock positions</b>	<b>Unsettled stock positions</b>	<b>Money positions</b>
S	2,000(short)	RMB2,200CR
S	3,000(short)	HKD3,600CR

On S-day, Participant A will have an aggregate short stock position of 5,000 in stock X.

However, for the purpose of settlement under the System, the two stock positions under different Eligible Currencies will remain separate and distinct. No same stock netting will be performed if all outstanding positions are in the same direction.

Settlement may be effected in respect of the two stock positions in stock X on S-day.

#### 10.3.10 Example (cross-day netting and same stock netting for Multi-counter Eligible Securities – opposite stock positions)

The sequence of netting in respect of a Multi-counter Eligible Security will be (i) cross-day netting of the same Eligible Currency; then (ii) same stock netting for stock positions in the opposite direction in respect of different Eligible Currencies. The netting processes can be illustrated by using the following example:

At the beginning of a S-day, Participant A has the following unsettled positions in stock X before settlement on the day begins.

Due settlement date of stock positions	Unsettled stock positions	Money positions
S-1	6,500 (long)	HKD13,000DR
S-1	500 (long)	RMB870DR
S	3,000 (long)	HKD3,600DR
S	7,700 (short)	RMB14,050CR

At the beginning of S-day, two opposite stock positions under the same Eligible Currency of different settlement dates will be offset. No cross-day netting will be performed for stock X traded in HKD counter as the outstanding positions for both S-1 and S are long positions. For stock X traded in RMB counter, the cross-day netting will be as follows:

Stock positions	Stock positions offset under cross-day netting	Money positions offset under cross-day netting	Unsettled stock positions after cross-day netting	Unsettled money positions after cross-day netting
S-1	500 (long)	RMB870DR	Nil	Nil
S	500 (short)	RMB912CR*	7,200 (short)	RMB13,138

\* The amount RMB912 is derived from  $RMB14,050 \times 500 / 7,700$

As a result of cross-day netting, Participant A has a net short stock position of 7,200 in stock X traded in RMB counter (with a corresponding money position of RMB13,138 CR). The amount of RMB42 (RMB912 – RMB870) arising out of the process will be credited by HKSCC to the Settlement Account (a sub-account of its Money Ledger) of Participant A for settlement on the same day.

After cross-day netting, the outstanding unsettled stock positions of stock X will be as follows:

Due settlement date of stock positions	Unsettled stock positions	Money positions
S-1	6,500 (long)	HKD13,000DR
S	3,000 (long)	HKD3,600DR
S	7,200 (short)	RMB13,138CR

Following cross-day netting and prior to the Batch-settlement-runs, the following same stock netting for stock X will be conducted:

- (i) Settle with the oldest first

<b>Stock Positions</b>	<b>Stock positions offset under same stock netting</b>	<b>Money positions offset under same stock netting</b>	<b>Unsettled stock positions after same stock netting</b>	<b>Unsettled money positions after same stock netting</b>
S-1	6,500 (long)	HKD13,000.00DR	Nil	Nil
S	6,500 (short)	RMB11,860.69CR	700 (short)	RMB1,277.31CR

- (ii) Settle with the latest

<b>Stock Positions</b>	<b>Stock positions offset under same stock netting</b>	<b>Money positions offset under same stock netting</b>	<b>Unsettled stock positions after same stock netting</b>	<b>Unsettled money positions after same stock netting</b>
S	700 (long)	HKD840.00DR*	2,300 (long)	HKD2,760.00DR
S	700 (short)	RMB1,277.31CR	Nil	Nil

\* The amount HKD840 is derived from  $\text{HKD}3,600 \times 700 / 3,000$

As a result of same stock netting, Participant A has a net long stock position of 2,300 in stock X (with a corresponding money position of HKD2,760 DR) to be settled on S-day. Assuming such net long stock position of 2,300 in stock X has been settled during subsequent Batch-settlement-run on S-day. The total amounts arising out of the money positions offset under cross-day netting, same stock netting and Batch-settlement-run will be debited/credited by HKSCC to the Settlement Account (a sub-account of its Money Ledger) of Participant A for settlement on the same day.

The money positions of different CNS stock positions of a Participant in the same Multi-counter Eligible Securities will continue to be treated as separate and distinct. As such, HKD16,600 DR (HKD13,000 + HKD3,600) and RMB 13,180 CR (RMB14,050 – RMB870) will be posted to the Money Ledger of Participant A.

## 10.4 SECURITIES SETTLEMENT UNDER THE CNS SYSTEM

### 10.4.1 Settlement between HKSCC and Participants

Under the CNS System, Exchange Trades are replaced by Market Contracts whereby HKSCC becomes the settlement counterparty to Participants. Settlement will be effected between the Participants and HKSCC in CCASS.

### 10.4.2 Settlement of short stock positions of Participants

Short stock positions of Participants under the CNS System may be settled in CCASS in any one of the following ways:

- (i) by the input of Delivery Instructions by the delivering Participants;
- (ii) by Batch-settlement-runs automatically carried out in CCASS on each Settlement Day; or
- (iii) by cross-day netting, as referred to in Section 10.3.

In the case of settlement by Batch-settlement-runs and cross-day netting, the oldest short stock positions of a Participant will always be settled first.

Except in cases where Participants have provided Collateral Security through CCMS for a waiver of computation of Marks, the CNS short stock position in the batch settlement occurring at the beginning of each Settlement Day will be settled with the relevant Collateral Security so provided with the same settlement date and to the extent which Marks computation has been waived, if the CNS short stock position still exists. Where two or more short positions exist in the same stock and with the same settlement date, relevant Collateral Security will be used to settle the position with a higher average price first.

In the case of settlement by DIs, a delivering Participant can select any stock position for settlement without reference to age.

#### **10.4.3 Settlement of long stock positions of Participants**

As and when Eligible Securities are made available to HKSCC by Participants with short stock positions under the CNS System, these will be used by HKSCC to settle its obligations to Participants with long stock positions under the CNS System.

HKSCC will deliver the Eligible Securities made available to it to Participants with long stock positions under the CNS System in accordance with the allocation algorithm set out in Section 13.4.

Although Participants with long stock positions under the CNS System may not receive Eligible Securities in CCASS on due dates (T+2), they will be able to make use of their outstanding long stock positions to offset against short stock positions in the same Eligible Securities under the CNS System on subsequent Settlement Days.

#### **10.4.4 Partial delivery**

Partial delivery will be allowed in respect of the CNS stock positions of Participants.

### **10.5 MONEY SETTLEMENT UNDER THE CNS SYSTEM**

#### **10.5.1 DVP basis**

Settlement between Participants and HKSCC under the CNS System will normally be on a DVP basis and in the Eligible Currency in which the relevant securities are denominated. To the extent that HKSCC determines that it is not possible or reasonably practicable to make payment in such Eligible Currency, HKSCC's obligations shall be to make payment, in full or in part, in such other currency or currencies and at such conversion rate(s) as HKSCC may in its absolute discretion determine to be fair and reasonable, taking into account all relevant circumstances as it may consider appropriate. With only one exception (see Section 10.5.5), money settlement will only be effected after settlement of stock positions in CCASS.

CCASS money settlement involves HKSCC issuing instructions to the Designated Banks of Participants to cause credits and debits to be made to the Designated Bank Accounts of Participants. Where the Participant is in the process of opening a Designated Bank Account in an Eligible Currency which is the subject of the CNS Transactions, HKSCC will make payment to the Participant by telegraphic transfer or paper cheque or such other means as are considered fair and reasonable by HKSCC. Payment will be made to the delivering Participant on the Business Day following the actual date of securities settlement. The receiving Participant must make payment directly into HKSCC's stated foreign currency bank account before 5:45 p.m. on the actual date of securities settlement.

#### **10.5.2 Money position of daily net CNS stock positions**

For Exchange Trades in the same Eligible Security effected on the same day and accepted for settlement under the CNS System (and effected by the same Special Participant in the case of a Clearing Agency Participant which is a China Connect Clearing House), there will be one

daily net stock position, as described in Section 10.3.1(ii), provided that, with respect to Multi-counter Eligible Security, there will be one daily net stock position in each of the Eligible Currency traded.

This daily net CNS stock position of a Participant will have a corresponding net money position, derived from offsetting the money positions of the underlying Exchange Trades. This is illustrated in the examples set out in Sections 10.3.3 and 10.3.7.

The net money positions derived from offsetting the money positions of the underlying Exchange Trades of a Participant in each Eligible Security in the same Eligible Currency (and in respect of each of its designated Special Participants in the case of a Clearing Agency Participant which is a China Connect Clearing House) on the same day will be offset against each other to result in a total net money position with HKSCC on each Settlement Day.

### **10.5.3 Money position of CNS stock positions after cross-day netting**

If two opposite CNS stock positions of a Participant in the same Eligible Security are offset against each other as a result of cross-day netting as described in Section 10.3.1(iii), the money positions of the two CNS stock positions (or, in the case of a Clearing Agency Participant which is a China Connect Clearing House, the money positions of the two CNS stock positions in respect of each of its designated Special Participants) will also be offset against each other to result in a sum to be settled between HKSCC and the Participant concerned. Any unsettled CNS stock position will also have a corresponding money position. The position is illustrated in the examples set out in Sections 10.3.4 to 10.3.6 and 10.3.10.

The money positions of two CNS stock positions of a Participant (or, in the case of a Clearing Agency Participant which is a China Connect Clearing House, the money positions of two CNS stock positions in respect of each of its designated Special Participants) in the same Eligible Security (and, in the case of Multi-counter Eligible Securities, in respect of the same Eligible Currency traded) (such CNS stock positions being both long or both short), will continue to be treated as separate and distinct.

### **10.5.3A Money position of CNS stock positions after same stock netting for Multi-counter Eligible Securities**

If multiple opposite CNS stock positions of a Participant in the same Multi-counter Eligible Security traded in different Eligible Currencies are offset against each other as a result of same stock netting as described in Section 10.3.1(iv), the corresponding money positions of such different CNS stock positions (or, in the case of a Clearing Agency Participant which is a China Connect Clearing House, the money positions of different CNS stock positions in respect of each of its designated Special Participants) in different Eligible Currencies will not be offset against each other, and will each be posted to Money Ledger to be settled between HKSCC and the Participant concerned. Each unsettled CNS stock position will also have its corresponding money position. The position is illustrated in the examples set out in Sections 10.3.8 to 10.3.10.

The money positions of different CNS stock positions of a Participant (or, in the case of a Clearing Agency Participant which is a China Connect Clearing House, the money positions of different CNS stock positions in respect of each of its designated Special Participants) in the same Multi-counter Eligible Security (such CNS stock positions being all long or all short), will continue to be treated as separate and distinct.

### **10.5.4 Partial delivery**

In respect of any partial delivery of a CNS stock position of a Participant (in an Eligible Security due for settlement on a particular Settlement Day), the amount to be settled between HKSCC and the Participant will be determined by multiplying the number of Eligible

Securities settled, by the average position price of the CNS stock position (see Section 10.3.3). The position is illustrated in the example set out in Section 10.3.6.

#### **10.5.5 CNS positions involving both delivery and payment by HKSCC or by Participants**

In some cases, it is possible that a Participant may have a CNS stock position under which it is obliged to deliver Eligible Securities to HKSCC as well as to pay HKSCC (or the other way round, where HKSCC is obliged to deliver Eligible Securities to it as well as to make payment to it). This may, for example, arise if on a particular day, the purchases and sales in a particular Eligible Security are made by a Participant or in the case of a GCP, including those made by its NCPs designated to it for clearing, or in the case of a Clearing Agency Participant, including that made by a Special Participant in such a way that whilst having a net long stock position (i.e. net buy position), the proceeds of its sales more than offset the purchase prices payable by it.

In such cases, money settlement in respect of such CNS positions will be effected on the due dates irrespective of whether or not such CNS stock positions have been settled in CCASS.

#### **10.5.6 One daily net money position under the CNS System for each Participant**

There will be one net money position under the CNS System for each Participant on each Settlement Day. The position is illustrated in Section 10.5.7.

#### **10.5.7 Example (daily net money position under the CNS System)**

The following CNS stock positions of Participant A were settled on S-day.

Stock	Quantity	Money position
X	1,000(long)	\$10,000DR
Y	5,000(short)	\$75,000CR
X	3,000(long)	\$60,000DR
		<u>\$5,000CR</u>

The net money position of Participant A under the CNS System on S-day is \$5,000CR. The sum of \$5,000 will be payable by HKSCC to Participant A following settlement of the CNS stock positions in CCASS on S-day.

#### **10.5.8 Intra-day settlement of money obligations due to Participants under the CNS System**

Participants that wish to receive intra-day settlement of money obligations due to Participants from HKSCC under the CNS System on a Settlement Day may input Intra-day Payment Standing Instructions via the “Intra-day Payment Standing Instruction” maintenance functions. Such intra-day settlement of money obligations due from HKSCC to Participants shall be at the full discretion of HKSCC and may be subject to such conditions and limits as HKSCC may consider appropriate, including limiting the intra-day settlement amount to the amount of cash prepayments received from Participants under Section 10.12.4 and overpaid cash prepayments not refunded to Participants under Section 10.12.7 or such other amount as HKSCC may from time to time determine.

If for whatever reason, the money obligations due to Participants that have requested to receive intra-day settlement of money obligations from HKSCC under the CNS System exceed any limit determined by HKSCC, HKSCC shall have the right to allocate the intra-day settlement amounts among Participants in such manner as it shall consider fair and appropriate in the circumstances. Priority will be given to Participants that have maintained authorised Cash Prepayment Standing Instructions at the beginning of the Settlement Day. Upon determination of the actual intra-day settlement amounts of money obligations that will be

paid to Participants, HKSCC will generate Intra-day Payment Instructions to the Participants in accordance with Section 14.8.

The following is a brief description of the procedures relating to intra-day settlement of money obligations due to Participants from HKSCC under the CNS System:

- (i) Participants that wish to request HKSCC to effect intra-day settlement of money obligations due to Participants from HKSCC under the CNS System shall input Intra-day Payment Standing Instructions via the “Intra-day Payment Standing Instruction” maintenance functions to instruct HKSCC to issue Intra-day Payment Instructions covering such intra-day settlement of money obligations. Acceptance of such Intra-day Payment Standing Instructions by HKSCC will be at the discretion of HKSCC and subject to such conditions and limits as HKSCC may from time to time specify. Where the Intra-day Payment Standing Instruction of a Participant also covers intra-day payment to the Participant of cash payments arising out of nominee services on each Business Day and/or surplus cash arising from overpaid cash prepayment on each Settlement Day, the amount of Intra-day Payment in this Section 10.5.8 on a Settlement Day shall include the amount of cash payments arising out of nominee services as referred to in and determined by HKSCC under Section 8.25.2 and/or surplus cash arising from overpaid cash prepayment as referred to in and determined by HKSCC under Section 10.12.8;
- (ii) Participants shall define a pre-set threshold in their Intra-day Payment Standing Instructions. No Intra-day Payment Instruction will be issued by HKSCC to a Participant on a Settlement Day and/or a Business Day if the total amount of Intra-day Payment as determined by HKSCC to be paid to the Participant on that day via IPI is smaller than its pre-set threshold;
- (iii) in case an Intra-day Payment Standing Instruction covering intra-day settlement of money obligations due to a Participant from HKSCC under the CNS System is accepted by HKSCC on a Settlement Day at or before 1:15 p.m., an Intra-day Payment Instruction will be issued starting from that day if applicable. Otherwise, the Intra-day Payment Instruction will only be issued from the next Settlement Day/Business Day;
- (iv) following the acceptance by HKSCC of an Intra-day Payment Standing Instruction to effect intra-day settlement of money obligations due to a Participant from HKSCC under the CNS System, HKSCC will normally determine the amount of such money obligations that is due to the Participant upon completion of the third Batch-settlement-run shortly after 2:00 p.m. on each Settlement Day, or such other time as specified by HKSCC from time to time;
- (v) in determining the intra-day settlement amount of money obligations that is due to a Participant from HKSCC under the CNS System, HKSCC will consider:
  - (a) whether the Participant has maintained an authorised Cash Prepayment Standing Instruction at the beginning of the Settlement Day;
  - (b) the money obligations due to the Participant from HKSCC under the CNS System for all settled CNS short positions upon completion of the third Batch-settlement-run shortly after 2:00 p.m. and any immediate settlement by DIs;
  - (c) the money obligations due from the Participant to HKSCC under the CNS System for all settled and unsettled CNS long positions; and



- 
- (d) other types of money obligations in the Participant's Settlement Account and Miscellaneous Account of Money Ledger as HKSCC may from time to time specify;
  - (vi) if the aggregate amount of intra-day settlement of money obligations exceeds any limit set by HKSCC, HKSCC shall have the right to allocate the intra-day settlement amounts among Participants in such manner as it shall consider fair and appropriate in the circumstances. Upon determination of the actual intra-day settlement amount of money obligations that will be paid to a Participant, an Intra-day Payment Instruction will be issued by HKSCC if the total amount of Intra-day Payment of the Participant is equal to or greater than the pre-set threshold defined by the Participant;
  - (vii) HKSCC will issue Intra-day Payment Instructions to the Designated Banks of Participants on a Settlement Day or Business Day at around 2:30 p.m., or such other time as specified by HKSCC from time to time, to cause credits to be made to the Designated Bank Accounts of Participants;
  - (viii) details of Intra-day Payment Instructions issued by HKSCC including the amount of the Intra-day Payment will be available for enquiry after 2:30 p.m. on a Settlement Day via the "Enquire Intra-day Payment Summary" function in CCASS Terminal; and
  - (ix) irrespective of whether an Intra-day Payment Standing Instruction is accepted by HKSCC under Section 10.5.8(iii), whether to allow an Intra-day Payment to Participants in respect of any intra-day settlement of money obligations due to Participants from HKSCC under the CNS System will be at the full discretion of HKSCC. If (a) a Participant fails to follow the specified procedures; (b) its Intra-day Payment Standing Instruction is subsequently turned down by HKSCC for any other reason; or (c) the settlement of any money obligations due to the Participant from HKSCC under the CNS System is not effected under an Intra-day Payment Instruction for any reason, then any money obligations due to the Participant from HKSCC under the CNS System will only be paid to the Participant not later than day end via DCI.

## **10.6 LATE DELIVERY : DEFAULT FEE**

HKSCC may require Participants that fail to settle their CNS stock positions in Eligible Securities on due dates to pay to it default fees. Default fees levied by HKSCC may be retained by HKSCC for use for such CCASS purposes as HKSCC deems fit. Default fees will be prescribed by HKSCC from time to time.

## **10.7 LATE DELIVERY : COMPULSORY STOCK BORROWING BY HKSCC**

### **10.7.1 Purpose**

HKSCC reserves the right at any time to effect a Compulsory Stock Borrowing Transaction in order to:

- (i) meet the aggregate of HKSCC's CNS delivery obligations to Participants, which have not been satisfied as a result of a failure by any Participant to deliver Eligible Securities to HKSCC by the final Batch-settlement-run on the due date (i.e., T+2); or
- (ii) replace, in whole or in part, HKSCC's stock borrowing under any other Compulsory Stock Borrowing Transaction.

The rights and obligations of the Lender and HKSCC in respect of a Compulsory Stock Borrowing Transaction shall be governed by the Compulsory Stock Borrowing and Lending Regulations. HKSCC shall not be obliged to exercise its rights under this

### Section 10.7.1.

For the avoidance of doubt, any borrowing of Eligible Securities effected by HKSCC pursuant to this Section 10.7 shall not affect the obligation of the Participant to deliver Eligible Securities under the CNS System.

Notwithstanding the use of expressions such as "borrow" "lend" "redeliver" etc. which are used to reflect terminology used in the market for transactions entered into in accordance with the Compulsory Stock Borrowing and Lending Regulations, title to Eligible Securities "borrowed" or "lent" provided in accordance with those Regulations shall pass from the Lender to HKSCC as provided for in those Regulations. HKSCC as the party obtaining title being obliged to redeliver title to Equivalent Securities (as defined in the Compulsory Stock Borrowing Regulations) subject to those Regulations to the Lender.

The provisions in these Operational Procedures relating to Compulsory Stock Borrowing Transactions are subject to the detail set out in the Compulsory Stock Borrowing and Lending Regulations from time to time.

### 10.7.2 Creation of Borrowing request of HKSCC

If, in the final Batch-settlement-run, Eligible Securities made available by delivering Participants are insufficient to cover:

- (i) all long CNS stock positions pursuant to the pre-determined algorithm (see Section 13.4); and/or
- (ii) any Lender which has called for redelivery of Eligible Securities under a Compulsory Stock Borrowing Transaction;

HKSCC will, in respect of each relevant Eligible Security, initiate a compulsory stock borrowing to enable HKSCC to meet its settlement obligations to receiving Participants and/or Lenders (as applicable).

### 10.7.3 Lender Priority List

For each Eligible Security, HKSCC will, during the day end processing, compile a "Lender Priority List". The Lender Priority List will be used by HKSCC in order to select a Lender with whom HKSCC shall enter into a Compulsory Stock Borrowing Transaction on the following Settlement Day. The Lender Priority List shall be determined by reference to the ratio of total fees paid to a Lender by HKSCC in relation to Compulsory Stock Borrowing Transactions and the total amount of Eligible Securities held in a Lender's Stock Lending Account over the three month period. For the purposes of this section 10.7.3 "the three month period" means the current month and the two months which immediately precede the current month.

The calculation of the priority ratio of a Lender for an Eligible Security is as follows:-

$$\begin{array}{l}
 \text{Total fees paid to that Lender by HKSCC in relation to Compulsory} \\
 \text{Stock Borrowing Transactions over the 3 month period in proportion} \\
 \text{to that of all Lenders} \\
 \\
 = \frac{\text{Total holdings of Eligible Securities held in that Lender's Stock} \\
 \text{Lending Account over the 3 month period in proportion to that} \\
 \text{of all Lenders}}{\text{Total fees paid to that Lender by HKSCC in relation to Compulsory} \\
 \text{Stock Borrowing Transactions over the 3 month period in proportion} \\
 \text{to that of all Lenders}}
 \end{array}$$

Lenders are ranked in ascending order of their calculated priority ratio in the Lender

Priority List.

Example (Lender Priority List)

Lenders (Participants A, B,C and D) have: (i) earned the following stock lending fees; and (ii) holdings of stock X in their respective Stock Lending Accounts as at end of day Y:

Lender	Current Month (M)		Month M-1		Month M-2	
	Lending Income (\$)	Stock X Holdings (Shs)	Lending Income (\$)	Stock X Holdings (Shs)	Lending Income (\$)	Stock X Holdings (Shs)
A	1,500	1,000,000	2,000	2,000,000	2,500	1,500,000
B	3,000	2,500,000	1,000	1,500,000	1,500	2,000,000
C	1,000	1,000,000	500	1,000,000	1,000	500,000
D	6,000	10,000,000	2,000	2,000,000	1,000	1,000,000
Total	11,500	14,500,000	5,500	6,500,000	6,000	5,000,000

Based on the priority ratio calculation method described above, the priority ratio of the Lenders of Stock X will be:

Lender	Priority Ratio of Stock X
A	$\frac{(1500+2000+2500) / (11500+5500+6000)}{(1m+2m+1.5m) / (14.5m + 6.5m + 5m)} = 1.507246$
B	$\frac{(3000+1000+1500) / (11500+5500+6000)}{(2.5m+1.5m+2m) / (14.5m + 6.5m + 5m)} = 1.036232$
C	$\frac{(1000+500+1000) / (11500+5500+6000)}{(1m+1m+0.5m) / (14.5m + 6.5m + 5m)} = 1.130435$
D	$\frac{(6000+2000+1000) / (11500+5500+6000)}{(10m+2m+1m) / (14.5m + 6.5m + 5m)} = 0.782609$

Based on the calculated priority ratio of the lenders the ranking of Lenders A, B, C and D under the Lender Priority List will be D,B,C and then A, i.e., Lender D will be the first Lender to be selected to enter into a Compulsory Stock Borrowing Transaction in respect of stock X on the next day.

#### 10.7.4 Batch Matching

In the final Batch-settlement-run, HKSCC will match the borrowing requests of HKSCC to Lenders based on the following algorithm:

- (i) priority ratio (lowest) - a Lender which has lowest priority ratio for a particular stock, then
- (ii) random if Lenders have same priority ratio.

Upon matching, a new unique "Lending Position Number" will be assigned.

Each Compulsory Stock Borrowing Transaction shall remain outstanding until there is a redelivery or a payment of cash compensation in accordance with the Compulsory Stock Borrowing and Lending Regulations. For each day on which a Compulsory Stock Borrowing Transaction is outstanding, HKSCC will pay a Lender as the counterparty of the Compulsory Stock Borrowing Transaction a stock lending fee calculated at the annual percentage most recently announced by HKSCC via CCASS Terminals, Participant Gateways or circular divided by 365 and multiplied by the day-end nominal value (based on the stock price transmitted by the Exchange to HKSCC) of the borrowed securities under that Compulsory Stock Borrowing Transaction. For any day which is not a trading day, the last day-end nominal value (based on the stock price transmitted by the Exchange to HKSCC) of the borrowed securities under the Compulsory Stock Borrowing Transaction will be used. A one day stock lending fee will be paid if Eligible Securities are redelivered to the Lender on the same day on which the borrowed Eligible Securities are delivered to HKSCC. The fee is calculated and payable on a daily basis by DCI.

#### **10.7.5 Recall Request**

In relation to a Compulsory Stock Borrowing Transaction, the Lender may call for redelivery of all but not part only of the equivalent Eligible Securities at any time by serving a notice of recall on HKSCC. Any notice of recall which is input by the Lender before 12:00 noon on any Business Day shall be treated as having been served on that day. Any notice of recall which is input at any other time shall be treated as having been served on the next succeeding Business Day following the date of input. Except as expressly provided in the Compulsory Stock Borrowing and Lending Regulations (see Appendix 6), HKSCC shall redeliver Eligible Securities within five Business Days after the date notice of recall is treated as having been served. Lenders shall not, in relation to any Compulsory Stock Borrowing Transaction, submit a notice of recall on the same day as Eligible Securities are delivered to HKSCC under that transaction; however, nothing herein shall restrict HKSCC from terminating a particular Compulsory Stock Borrowing Transaction in whole or in part and redelivering the relevant Eligible Securities under that transaction at any time (including under that transaction) on the same day as the Eligible Securities are delivered to HKSCC.

The Lender shall, in relation to any borrowing of Eligible Securities, specify, in the relevant notice of recall, the Stock Account to be credited with the redelivered Eligible Securities.

In relation to any Compulsory Stock Borrowing Transaction, the Lender may elect for cash compensation to be paid by HKSCC in accordance with the Compulsory Stock Borrowing and Lending Regulations. Any such payment made by HKSCC shall constitute complete satisfaction of HKSCC's redelivery obligations under that transaction.

#### **10.7.6 Redelivery**

Eligible Securities may, at the election of HKSCC, be redelivered by batch processing during the final Batch-settlement-run (see Section 6.2(iv)) or through on-line delivery between 9:30 a.m. and 3:45 p.m. on a Business Day.

In relation to Compulsory Stock Borrowing Transactions which are settled by redelivery through batch processing, HKSCC will redeliver in accordance with the following allocation algorithm:

- (i) status - outstanding Compulsory Stock Borrowing Transactions in respect of which a notice of recall has been validly served (referred to in this section 10.7.6 as transactions with 'Recalled' status) will be settled with priority over all other

Compulsory Stock Borrowing Transactions (referred to in this section 10.7.6 as transactions with 'Active' status); and if more than one Compulsory Stock Borrowing Transaction shares the same status, then

- (ii) age (oldest) - for transactions with 'Active' status, the transaction which has remained outstanding for the longest time will be settled with priority and for transactions with 'Recalled' status, the transaction which has remained unsettled for the longest time since the date the notice of recall is treated as having been served will be settled with priority; and if Eligible Securities were delivered to HKSCC on the same date in respect of more than one Compulsory Stock Borrowing Transaction, then, in relation to those transactions,
- (iii) random.

At any time, Lenders may receive partial redeliveries of Eligible Securities in respect of outstanding Compulsory Stock Borrowing Transactions in accordance with the Compulsory Stock Borrowing and Lending Regulations.

#### **10.7.7 Entitlements arising from borrowed securities**

The procedures relating to entitlements arising in respect of borrowed Eligible Securities shall be specified in the Compulsory Stock Borrowing and Lending Regulations.

#### **10.7.8 Cash Compensation to discharge HKSCC's obligations**

If, in relation to a Compulsory Stock Borrowing Transaction:

- (a) Eligible Securities are not redelivered by the fifth Business Day of the date on which a notice of recall is treated as having been served and the Lender elects to receive cash compensation;
- (b) the date on which Eligible Securities are to be redelivered falls on a day when the relevant Eligible Security is suspended from trading on the Exchange and HKSCC elects to pay cash compensation; or
- (c) the Eligible Securities borrowed are suspended from trading on the Exchange for 31 consecutive days and HKSCC elects to pay cash compensation;

Then such cash compensation shall be paid in an amount which HKSCC fairly and reasonably believes to be the value of the Eligible Securities which are to be redelivered calculated, where appropriate, by reference to the closing price transmitted to HKSCC by the Exchange of such securities on the date that cash compensation is paid.

Cash compensation paid by HKSCC in respect of a Compulsory Stock Borrowing Transaction shall constitute complete satisfaction of HKSCC's obligations in respect of that transaction.

For further details reference should be made to the Compulsory Stock Borrowing and Lending Regulations (see Appendix 6).

#### **10.7.9 Functions available for use**

The functions available for use by a Participant via a CCASS Terminal in relation to a Compulsory Stock Borrowing Transaction are as follows:

- (i) "Add Recall Request" function: which allows a Participant to input a notice of recall;

- (ii) "Change Cash Compensation Indicator" function: which allows a Participant to elect to receive cash compensation;
- (iii) "Enquire Lending Position" function: which provides the details of outstanding Compulsory Stock Borrowing Transactions of a Participant; and
- (iv) "Enquire Stock Borrowing Information" function: which provides the summary of new and outstanding stock loans made in CCASS and total holdings of Eligible Securities available for borrowing in CCASS.

#### **10.7.10 Reports available**

The reports available to a Participant via a CCASS Terminal or a Participant Gateway in relation to Compulsory Stock Borrowing Transactions are as follows:

- (i) Stock Borrowing/Lending Activity Report: this report lists notices of recall, elections to receive cash compensation and redeliveries by HKSCC each in relation to a Participant;
- (ii) Stock Borrowing/Lending Position Status Report: this report lists a Participant's Compulsory Stock Borrowing Transactions by 'Active' status, 'Recalled' status, 'Returned' status, 'Frozen' status (due to the Participant being declared a defaulter in accordance with the Rules), 'Cancelled' status (due to delisting, compulsory takeover or exchange of shares in relation to the Participant's borrowed securities, etc.), 'Compensated' status (due to cash compensation paid by HKSCC in relation to the Participant's borrowed securities) and 'Converted' status (due to consolidation, splitting etc. in relation to the Participant's borrowed securities).

### **10.8 LATE DELIVERY : BUY-IN**

#### **10.8.1 Purpose**

The purpose of a Buy-in is to ensure that outstanding stock positions of Participants under the CNS System are settled without delay.

#### **10.8.2 Timing of Buy-in**

Unless (i) HKSCC grants an exemption under Section 10.8.3, (ii) there is a risk management reason affecting HKSCC, which is considered valid by the Risk Management Committee or (iii) a Buy-in has been executed by HKSCC pursuant to Rule 3501(iv) in respect of the short CNS stock positions of a Participant, HKSCC shall have the right, but shall not be obliged, to effect a Buy-in on behalf of the short Participant on T+3 (or if it is not practicable to do so on T+3, at any time thereafter) as HKSCC in its absolute discretion considers appropriate in respect of short stock positions of a Participant under the CNS System which are outstanding for settlement on the due date (i.e., unsettled after settlement processing on T+2).

A Buy-in trade executed by HKSCC on behalf of the short Participant on or off the Exchange will normally be settled under the CNS System, subject to the usual T+2 settlement period and will go through the substitution process (where applicable) and normal novation, daily netting, cross-day netting and same stock netting processing.

Notwithstanding the preceding paragraph, HKSCC may require a Buy-in trade (which will be an Exchange Trade, if effected on the Exchange) to be settled under the Isolated Trades System. Although a Buy-in will normally be subject to the usual T+2 settlement period, HKSCC may also require a Buy-in to be settled on the same day of execution or such other period as HKSCC in its absolute discretion considers appropriate.

In the event that a short Participant wishes to make an irrevocable request to HKSCC to

execute a Buy-in pursuant to Rule 3501(iv), such Participant shall complete and submit to HKSCC the prescribed form of request (See CCASS Terminal User Guide for Participants for the form). HKSCC reserves the right to accept or reject the short Participant's Buy-in request in its absolute discretion as it may think fit. If the request form is received and accepted by HKSCC between 8:01 p.m. and 12:00 noon, orders will be placed on or off the Exchange during the afternoon trading session at the Exchange. If the request form is received and accepted by HKSCC between 12:01 p.m. and 8:00 p.m., orders will be placed on or off the Exchange on the following trading day. HKSCC shall effect the Buy-in at what it determines to be the best prevailing market price and terms available (but taking into account HKSCC may need to act promptly and provided that HKSCC shall have no liability if it acts in good faith). The short Participant shall be liable to and shall indemnify HKSCC, the Exchange, and a recognized exchange controller which is the controller of HKSCC against all costs and expenses incurred by HKSCC in connection with the Buy-in.

### **10.8.3 Exemption from Buy-in**

HKSCC may grant an exemption from a Buy-in on behalf of a short Participant on T+3 if such Participant is able to provide HKSCC with satisfactory evidence in accordance with Section 10.8.4 that a ground for exemption as set out below applies:

- (i) the Participant applying for exemption or the delivering Participant has made a deposit of sufficient Eligible Securities into the CCASS Depository prior to 4:15 p.m. on a Settlement Day but the CCASS Depository is unable to process the stock deposit before the final Batch-settlement-run;
- (ii) defects in the relevant instruments of transfer (such as use of outdated instruments of transfer, the transferor's signature not being in the correct place or defacement of the instrument of transfer) provided that there is prima facie evidence that the transferor has signed the instrument of transfer;
- (iii) [Repealed]
- (iv) the relevant Eligible Securities are not credited to the Stock Clearing Account of the Participant applying for exemption due to severe weather conditions, acts of God or due to the occurrence of other events beyond the relevant Participant's reasonable control such as labour disputes, strike, mechanical breakdowns, computer or electronic system or network failures, unavailability of or restrictions on any communication media or any other event (including sanctions or the issuance of a court order or a restriction notice or order by a competent authority) as determined by HKSCC at its sole discretion to be an acceptable ground for exemption on a case-by-case basis;
- (v) in respect of oversold trades due to clerical or calculation error of the short Participant applying for exemption (or in the case of a GCP, including such oversold trades of its NCP designated to it for clearing), the delivery obligations of the Participant applying for exemption will be settled fully on T+3 pursuant to purchase transactions executed on T+1, or, if trading of the underlying Eligible Security is suspended on T+1, within two Settlement Days after resumption of trading;
- (vi) in respect of assigned Clearing Agency Transactions, the delivery obligations of the Participant applying for exemption will be settled fully on T+3 pursuant to purchase transactions executed on T+1, or, if trading of the underlying Eligible Security is suspended on T+1, within two Settlement Days after resumption of trading;
- (vii) for trades where a client buys and sells the same Eligible Securities on the same day through different Exchange Participants), sufficient Eligible Securities which are due

to be credited to the Stock Clearing Account of the delivering Participant by HKSCC for onward delivery to the Participant applying for exemption have not been so credited as a result of relevant Eligible Securities not having been made available to HKSCC by Participants with short stock positions under the CNS System for allocation on the relevant due Settlement Day;

(viii) [Repealed]

- (ix) in respect of Units or Eligible Securities to be received from a creation or redemption of Units, the Participant applying for exemption has an unconditional entitlement to receive sufficient Units or Eligible Securities to cover the relevant short position on T+2;
- (x) the Participant applying for exemption can provide evidence satisfactory to HKSCC that it or the delivering Participant has sufficient Eligible Securities in its Stock Account on T+2 to cover the relevant short position and the Participant applying for exemption or the delivering Participant has received valid instruction from the selling client to make delivery of the relevant Eligible Securities for settlement on T+2 but is unable to do so due to clerical error;
- (xi) in respect of transactions in Eligible Securities which are subject to parallel trading on the Exchange, the Participant applying for exemption or the delivering Participant has: (a) long positions in Eligible Securities of the relevant issuer; or (b) sufficient Eligible Securities of the relevant issuer in its Stock Account, which following conversions of such long positions or holdings of Eligible Securities (as applicable) in CCASS, are sufficient to settle the relevant short positions on T+2;
- (xii) in respect of market making transactions in any Market Making Security as specified by HKSCC from time to time, the Participant applying for exemption has duly executed Cross-Border Transfer Instructions transferring sufficient Eligible Securities to HKSCC's account with the Appointed Depositary to cover the relevant short position resulting from the market making activities as aforesaid on T+2 but is unable to cover such short position on T+2 due to clerical error of the Participant or the Appointed Depositary;
- (xiii) in respect of market making transactions in any Market Making Security as specified by HKSCC from time to time, the Participant applying for exemption has sufficient Eligible Securities to cover the relevant short position resulting from the market making activities as aforesaid on T+2 but the transfer of the Eligible Securities by Cross-Border Transfer Instructions to HKSCC's account with the Appointed Depositary cannot be effected to cover the relevant short position as a result of a holiday in the market of the Appointed Depositary;
- (xiv) the person who is under an obligation to deliver, whether directly or indirectly, to the Participant applying for exemption the relevant quantity of Eligible Securities for settlement had lent such Eligible Securities and has duly executed a notice of recall pursuant to which such Eligible Securities will be delivered to the Participant on T+3 for settlement of its delivery obligation in full, and that person is an approved lending agent as defined in the Securities and Futures (Disclosure of Interests – Securities Borrowing and Lending) Rules; or
- (xv) in respect of market making transactions in any Market Making Security as specified by HKSCC from time to time, the Participant applying for exemption can provide evidence satisfactory to HKSCC that a creation, borrowing and/or purchase of sufficient Eligible Securities has been effected but the relevant Eligible Securities will



only be delivered on T+3 to cover the short positions resulting from the market making activities. HKSCC will review this exemption from time to time and may suspend the availability of this exemption for any Participant and any Market Making Security at any time and for such period in its absolute discretion.

For the avoidance of doubt, the market making transactions in a Market Making Security in respect of which an exemption is claimed under Section 10.8.3(xii), (xiii) or (xv) may be conducted by a Securities Market Maker for its own account, or for the account of any of its affiliates or for the account of any of its Designated Specialists as part of its or their market making activities in accordance with the Exchange Rules.

The short Participant to whom an exemption from a Buy-in is granted shall be obliged to settle all overdue short positions of which exemption is granted by day-end of T+3. In the event that such Participant fails to do so for whatever reason, HKSCC may consider executing on behalf of such Participant a Buy-in on T+4 (or, if it is not practicable to do so on T+4, at any time thereafter) in its absolute discretion as it may think fit.

#### **10.8.4 Application for exemption from Buy-in on T+3**

A short Participant wishing to claim exemption under Section 10.8.3 must apply to HKSCC not later than 8.00 p.m. on the due date for settlement (i.e., T+2) by completing and submitting an Application Form for Exemption of Buy-in (see CCASS Terminal User Guide for Participants for the form). The Application Form shall be sent by facsimile or such other means as HKSCC may consider appropriate and shall be deemed received when received by HKSCC. In addition, the short Participant applying for exemption must provide HKSCC with satisfactory supporting documents as set out below on or before T+6, unless otherwise notified by HKSCC. Unless (i) HKSCC grants an exemption under Section 10.8.3, (ii) there is a risk management reason affecting HKSCC, which is considered valid by the Risk Management Committee, (iii) a Buy-in has been executed by HKSCC pursuant to Rule 3501, or (iv) in respect of the short CNS stock positions of a short Participant, HKSCC shall have the right, but shall not be obliged, to effect a Buy-in on behalf of the short Participant on T+3 (or if it is not practicable to do so on T+3, at any time thereafter) through HKSCC's authorized brokers as HKSCC in its absolute discretion considers appropriate.

In respect of an exemption claimed under Section 10.8.3(i), the Participant applying for exemption is required to provide HKSCC with a certified copy of the temporary receipt issued by the CCASS Depository for the shares deposited.

In respect of an exemption claimed under Section 10.8.3(ii), the Participant applying for exemption is required to provide HKSCC with a certified copy of the relevant Stock Deposit Form endorsed by the CCASS Depository.

In respect of an exemption claimed under Section 10.8.3(iv), the Participant applying for exemption will, if so requested by HKSCC, provide HKSCC with evidence supporting its application at such time as specified by HKSCC.

In respect of an exemption claimed under Section 10.8.3(v), the Participant applying for exemption will have to provide HKSCC with a copy of (i) the relevant report to the Exchange and (ii) the relevant CCASS report evidencing a purchase has been executed on T+1 to cover the shortfall of Eligible Securities. If the trading of the underlying Eligible Security is suspended on T+1, a copy of the relevant CCASS report evidencing a purchase has been executed upon resumption of trading shall be provided as soon as practicable subsequent to the submission of the application for exemption under Section 10.8.3(v).

In respect of an exemption claimed under Section 10.8.3(vi), the Participant applying for exemption will have to provide HKSCC with a copy of (i) the assignment report generated

by The SEHK Options Clearing House Limited and (ii) the relevant CCASS report evidencing a purchase has been executed on T+1 to cover the shortfall of Eligible Securities. If the trading of the underlying Eligible Security is suspended on T+1, a copy of the relevant CCASS report evidencing a purchase has been executed upon resumption of trading shall be provided as soon as practicable subsequent to the submission of the application for exemption under Section 10.8.3(vi).

In respect of an exemption claimed under Section 10.8.3(vii), the Participant applying for exemption is required to provide HKSCC with a copy of (i) the relevant bought and sold contract notes and (ii) the relevant CCASS report evidencing a matched SI.

In respect of an exemption claimed under Section 10.8.3(ix), (x), (xi), (xii) and (xiii), the Participant applying for exemption is required to provide HKSCC with a copy of the relevant CCASS reports or other supporting documents satisfactory to HKSCC evidencing that the relevant Units, Eligible Securities or long positions (as applicable) are available to cover the relevant short positions on T+2.

In respect of an exemption claimed under Section 10.8.3(xiv), the Participant applying for exemption is required, at the time when it submits the application for exemption, to provide HKSCC with the required reference numbers assigned to the supporting documents to be submitted to HKSCC on T+6. The supporting documents include: (i) a document which records the sales transaction executed by such Participant; (ii) a notice of recall which has been duly executed by an approved lending agent in respect of the Eligible Securities lent; and (iii) such other supporting documents as HKSCC may require.

In respect of an exemption claimed under Section 10.8.3(xv), the Participant applying for exemption is required to provide HKSCC with a copy of the relevant CCASS reports or other supporting documents satisfactory to HKSCC evidencing that the relevant Eligible Securities are available to cover the relevant short positions on T+3.

#### **10.8.5 Buy-in process by HKSCC on behalf of a short Participant**

The following explains the process of Buy-in by HKSCC on behalf of a short Participant in greater detail:

- (i) in respect of the short stock positions of a short Participant under the CNS System still outstanding at the end of the due date (i.e., T+2), a Buy-in Notification Report containing such outstanding short stock positions will be generated by HKSCC. Unless (a) HKSCC grants an exemption under Section 10.8.3, (b) there is a risk management reason affecting HKSCC which is considered valid by the Risk Management Committee or (c) a Buy-in has been executed by HKSCC pursuant to Rule 3501(iv) in respect of the short CNS stock positions of a short Participant, HKSCC shall have the right, but shall not be obliged, to effect Buy-in on T+3 (or if it is not practicable to do so on T+3, at any time thereafter) as HKSCC in its absolute discretion considers appropriate of all outstanding short stock positions stated in the Buy-in Notification Report;
- (ii) the Buy-in Notification Report will be available to the short Participant through its CCASS Terminals and Participant Gateways after the final Batch-settlement-run;
- (iii) the short Participant may apply for exemption from Buy-in to HKSCC in accordance with the provisions of section 10.8.4;
- (iv) HKSCC may instruct its authorized brokers to assist in effecting a Buy-in on or off the Exchange;
- (v) HKSCC shall effect a Buy-in at what it determines to be the best prevailing market

price and terms available (but taking into account HKSCC may need to act promptly and provided that HKSCC, the Exchange, and a recognized exchange controller which is the controller of HKSCC shall have no liability if HKSCC acts in good faith). The short Participant shall be liable to and shall indemnify HKSCC, the Exchange, and a recognized exchange controller which is the controller of HKSCC against all costs and expenses incurred by HKSCC in connection with the Buy-in;

- (vi) after effecting such a Buy-in, the relevant Buy-in details will be available to the short Participant via the CCASS enquiry function of "Enquire Buy-in Confirmation". The relevant Buy-in details will also be posted under the section "Buy-in Confirmation" in the Buy-in Notification Report; and
- (vii) upon receipt of confirmation of good funds in relation to the cost of the Buy-in, Eligible Securities received under the Buy-in will be delivered to the short Participant.

With respect to a Buy-in of a Multi-counter Eligible Security, under normal circumstances, such Buy-in will be effected in the trading counter in HKD. HKSCC reserves the right to execute the Buy-in in any other trading counter of such Multi-counter Eligible Security in its absolute discretion as it may think fit.

#### 10.8.6 Buy-in to be effected under the Isolated Trades System

Where a Buy-in is required by HKSCC to be effected under the Isolated Trades System, the selling counterparty Exchange Participant to a Buy-in executed on behalf of the short Participant will have to be so informed by HKSCC or its authorized broker.

The selling counterparty Exchange Participant to a Buy-in will then identify the Buy-in trade as one to be settled under the Isolated Trades System by keying in "B" in the "reference field" on the trading terminal of the Exchange.

Where relevant, the selling counterparty Exchange Participant to a Buy-in will also be informed that the Buy-in is to have a different settlement period than the normal settlement period of T+2.

If the selling counterparty Exchange Participant (or where applicable, its GCP) to a Buy-in fails to settle on time, it will be subject to a further Buy-in to be effected under the Isolated Trades System.

#### 10.8.7 Example (Buy-in Exemption)

In respect of oversold trades due to calculation or clerical errors, exemption from Buy-in on T+3 will be granted on the condition that the exempted quantity is purchased on T+1.

Example: Broker A has executed the following Exchange Trade in stock Y.

	<b>T day</b> (Sept 1)	<b>T+1</b> (Sept 2)	<b>T+2</b> (Sept 3)	<b>T+3</b> (Sept 4)
Trade quantity	-15,000	+5,000 -14,000	0	0
Day end CNS position	-15,000	-9,000		
Due position			-15,000	-15,000 -9,000
Outstanding position				-12,000**

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at day end	-15,000	-9,000
Outstanding quantity subject to Buy-in on the following trading day	10,000*	9,000*** 2,000***

\* Broker A applies for Buy-in exemption on Sept 3 for 5,000 shares which he claims to be oversold and bought back on Sept 2. As a result of the exemption, only 10,000 shares (15,000 shares - 5,000 shares) are subject to Buy-in.

\*\* The broker has deposited 3,000 shares to his account on Sept 4 and thus reducing the outstanding balance to 21,000 shares (12,000 shares + 9,000 shares) at day end.

\*\*\* The 9,000 shares due on Sept 4 which remain unsettled at day end of Sept 4 will be subject to Buy-in. In respect of the 2,000 shares due on Sept 3 which remain unsettled at day end of Sept 4, HKSCC may consider executing a Buy-in in its absolute discretion as it may think fit.

#### 10.8.8 Participants may effect cash prepayment

Participants that have outstanding payment obligations to HKSCC under any Buy-in but wish to utilize any or all of the Eligible Securities to be received under the Buy-in for any purpose, including to settle ISI/SI Transactions and Isolated Trades during a Settlement Day, may pay same day available funds in the relevant Eligible Currency to HKSCC to reduce their monetary obligations.

A Participant may pay same day available funds to HKSCC by inputting Cash Prepayment Instructions on each Settlement Day or by inputting a Cash Prepayment Standing Instruction via the “Cash Prepayment Standing Instruction” maintenance functions to authorize HKSCC to generate recurring Cash Prepayment Instructions on behalf of the Participant concerned on each Settlement Day. The cash prepayment amount that will be generated under a Cash Prepayment Standing Instruction will equal to the total outstanding Buy-in cost on the Settlement Day. Any Cash Prepayment Standing Instruction remaining in the “pending status” ten calendar days after its last updated date will be automatically purged from CCASS.

#### 10.8.9 Procedures

The following is a brief description of the procedures relating to cash prepayment on each Settlement Day:

- (a) Cash Prepayment Instructions with “CHATS” set as the payment method
  - (i) Participants that wish to make prepayments by means of CPIs shall select “CHATS” as the payment method when creating a Cash Prepayment Instruction via a CCASS Terminal from 8:00 a.m. to 2:00 p.m. or such other time specified by HKSCC from time to time or when creating a Cash Prepayment Standing Instruction via a CCASS Terminal from 8:00 a.m. to 7:00 p.m. or such other time specified by HKSCC from time to time;
  - (ii) To avoid undue concentration of HKSCC's exposure to a bank appointed by HKSCC as receiving bank for cash payment, cash prepayment is subject to the concentration limit predetermined by HKSCC in respect of an appointed receiving bank. HKSCC will only accept or generate Cash Prepayment Instructions within the predetermined concentration limit of the receiving bank. In case a Cash Prepayment Standing Instruction is created and authorized by a

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Clearing Participant, Cash Prepayment Instructions will be generated by HKSCC, if applicable, at approximately 8:00 a.m. starting from the following Settlement Day;

- (iii) Upon the creation and authorization of Cash Prepayment Instructions by Participants or the generation of Cash Prepayment Instructions by HKSCC pursuant to Cash Prepayment Standing Instructions, CPIs will be generated to collect the cash prepayments from their Designated Bank Accounts. The CPIs information will be included in the Electronic CHATS Payment Instruction Report (CSEPI03). Based on the report, Designated Banks will issue CPIs to the Clearing House of HKAB to make payment on their behalf. Clearing Participants must ensure that there are sufficient funds in their Designated Bank Accounts and that the CHATS payments are completed by their Designated Banks no later than 3:30 p.m. or such other time as may be prescribed by HKSCC from time to time;
  - (iv) Upon being notified by the Clearing House of HKAB of the finality of such payment, HKSCC will update the Miscellaneous Accounts of Participants' Money Ledgers to reduce their corresponding monetary obligations due to HKSCC and as a result, release the Eligible Securities received under the Buy-ins to the Participants. Participants' Statements of Money Ledger will show the relevant entries. Participants can check the status of a Cash Prepayment Instruction via the CCASS enquiry function of "Enquire Cash Prepayment Instruction"; and
  - (v) In case the relevant cash payment under a Cash Prepayment Instruction input or generated on a Business Day is not received by HKSCC, the Cash Prepayment Instruction will be purged from CCASS at the end of the Business Day.
- (b) Cash Prepayment Instructions with "OTHERS" set as the payment method
- (i) Participants that wish to make prepayments by other means must indicate "OTHERS" as the payment method when creating a Cash Prepayment Instruction via a CCASS Terminal from 8:00 a.m. to 2:30 p.m. or such other time specified by HKSCC from time to time or when creating a Cash Prepayment Standing Instruction via a CCASS Terminal from 8:00 a.m. to 7:00 p.m. or such other time specified by HKSCC from time to time;
  - (ii) To avoid undue concentration of HKSCC's exposure to a bank appointed by HKSCC as receiving bank for cash payment, cash prepayment is subject to the concentration limit predetermined by HKSCC in respect of each appointed receiving bank. HKSCC will only accept or generate Cash Prepayment Instructions within the predetermined concentration limit of the receiving bank. In case a Cash Prepayment Standing Instruction is created and authorized by a Participant, Cash Prepayment Instructions will be generated by HKSCC, if applicable, at approximately 8:00 a.m. starting from the following Settlement Day;
  - (iii) Participants must ensure that same day available funds are transferred to HKSCC's specified bank account no later than 2:45 p.m. or such other time prescribed by HKSCC from time to time. For Participants using the same bank as the appointed receiving bank of HKSCC, they can make use of the internal account transfer function of the bank (see CCASS Terminal User Guide for Participants for details) or its electronic banking system to transmit available funds. For others, they can instruct their banks to make payment to HKSCC via

inter-bank transfer with CHATS payment (see CCASS Terminal User Guide for Participants for details);

- (iv) Based on the details of Cash Prepayment Instructions, HKSCC will follow up the funds with its appointed receiving bank and the relevant Participants. Only when available funds in the relevant Eligible Currency are confirmed will HKSCC update Participants' Miscellaneous Accounts of Money Ledger to reduce their corresponding monetary obligations due to HKSCC and as a result, release the Eligible Securities received under the Buy-ins to the Participants. Participants' Statements of Money Ledger will show the relevant entries. Participants can check the status of a Cash Prepayment Instruction via the CCASS enquiry function of "Enquire Cash Prepayment Instruction";
- (v) Acceptance of the prepayment requests will be at HKSCC's full discretion. If Participants fail to follow the procedures, and/or for any other reason the requests are subsequently turned down by HKSCC, then the funds received will only be refunded the following Business Day without interest;
- (vi) In the event of default of payment (e.g., for any transfers subsequently reversed by the Clearing House of HKAB), HKSCC shall have recourse against the relevant Participant;
- (vii) In case cash remittance is made by a Participant to HKSCC as cash prepayment not pursuant to any Cash Prepayment Instruction, HKSCC reserves the right not to effect the updating of the Participant's Money Ledger on the same day. Such cash payment will be refunded without interest to the Participant by crediting the cash payment amount to its Money Ledger on the next Business Day; and
- (viii) In case the relevant cash payment under a Cash Prepayment Instruction input or generated on a Business Day is not received by HKSCC, the Cash Prepayment Instruction will be purged from CCASS at the end of the Business Day.

## **10.9 LATE DELIVERY : ADJUSTMENTS FOR ENTITLEMENTS**

### **10.9.1 General**

A Participant's entitlement to participate through CCASS in corporate actions etc. affecting Eligible Securities will be determined by HKSCC by reference to the holding of that Participant in the relevant Eligible Securities as at the date on which the entitlement of HKSCC or the Nominee is determined (usually the last registration day before the relevant book close or record date).

If, as at that date, a Participant has any outstanding unsettled stock positions under the CNS System, certain adjustments to its entitlements may have to be made between HKSCC and such Participant.

This Section explains the facilities and procedures in CCASS to deal with adjustments or claims in respect of entitlements accruing to Eligible Securities which may be necessary as a result of late deliveries by Participants under the CNS System.

For convenience, Participants with long CNS stock positions giving rise to adjustments are referred to in this Section as "Long Participants". Participants with short CNS stock positions giving rise to adjustments are referred to in this Section as "Short Participants".

Where a benefit entitlement election or election to participate in corporate actions in

respect of any Eligible Securities has to be made by a Long Participant by a specific time on any day which is the last election day by delivering the Eligible Securities to the registrar by the specified time (usually 4:00 p.m.) to take up the entitlement and/or participate in the corporate action, and the Long Participant is unable to do so by reason of not having received the relevant Eligible Securities in settlement under CNS following the second Batch-settlement-run (currently 12:00 noon), in such case, HKSCC shall hold the Short Participant who still maintains an unsettled CNS short position in such Eligible Securities after the second batch-settlement-run on such Settlement Day, being the last day of election and delivery of the Eligible Securities to the registrar, responsible and accountable for the benefit entitlement that a Long Participant has indicated for election in the application form submitted to HKSCC in accordance with Sections 10.9.8 et seq.

### **10.9.2 General principles**

The facilities and procedures in CCASS in relation to adjustments or claims to entitlements as a result of late deliveries under the CNS System reflect HKSCC's role as the settlement counterparty to the Long Clearing Participants and to the Short Clearing Participants.

Under these facilities and procedures in CCASS, HKSCC will pass on entitlements it receives from the Short Clearing Participants to the Long Clearing Participants. HKSCC may also require the Short Clearing Participants to pay such additional amount to ensure that, Long Clearing Participants will, in so far as practicable, be put in the same position as if there had been no late delivery under the CNS System. Accordingly, even if Short Clearing Participants fail to deliver securities or other cash entitlements accruing to Eligible Securities, HKSCC will still be responsible to Long Clearing Participants in the manner as indicated below. Except as expressly provided, HKSCC, the Exchange, and a recognized exchange controller which is the controller of HKSCC shall have no liability to Long Clearing Participants.

To ensure that Short Clearing Participants comply with the relevant CCASS procedures and to minimize its risk exposure to such Short Clearing Participants, HKSCC may, under the Rules, require Short Clearing Participants to provide cash Collateral or to purchase relevant securities, or HKSCC may itself purchase the relevant securities. HKSCC will normally redeliver the cash Collateral upon receipt from the Short Clearing Participant of the relevant securities required, or if that is not possible or reasonably practicable, at such other time as HKSCC considers appropriate.

Section 10.9.3 explains how the principles set out in this Section will apply to the different categories of corporate actions affecting Eligible Securities.

Section 10.9.4 to Section 10.9.16 deal with specific types of corporate actions affecting Eligible Securities and explain how adjustments for entitlements will be processed in CCASS in such cases.

Section 10.9.17 deals with fractional securities entitlements as a result of the relevant adjustment procedures in CCASS.

HKSCC will from time to time notify Participants of the procedures or additional procedures to be followed in relation to adjustments for entitlements under the CNS System in respect of corporate actions, either generally or on a case by case basis.

The procedures for adjustments for entitlements under the CNS System, as set out in this Section, or as may be notified by HKSCC from time to time, will be binding on Participants. Save as provided in this Section, Long Participants shall have no claim

against HKSCC in respect of benefit entitlements accruing to their outstanding long CNS stock positions.

### **10.9.3 Different categories of corporate actions**

Corporate actions affecting Eligible Securities can be broadly divided into four categories. The extent of procedures and facilities available in CCASS in relation to adjustments for entitlements in respect of the four categories of corporate actions can be summarized as follows :

- (i) Announcements/communications : in relation to announcements or issues of circulars by issuers of Eligible Securities, no facilities will be offered in CCASS for "adjustments" to entitlements. All Participants in CCASS should have access to these announcements or circulars (see Section 8.4 and Section 8.5);
- (ii) Voting : in relation to corporate actions to be voted on, only limited facilities will be offered in CCASS to allow Long Clearing Participants to give instructions relating to voting through CCASS (see Section 10.9.4);
- (iii) Entitlements/actions (not requiring the exercise of discretion): in relation to corporate actions such as dividend payments or bonus issues of securities, where no decision is required to be made by Participants, HKSCC will normally establish procedures in CCASS whereby relevant entitlements (money or securities) will be collected by it from the Short Clearing Participants and then distributed to Long Clearing Participants (see Section 10.9.5, Section 10.9.6, Section 10.9.11A and Section 10.9.12); and
- (iv) Entitlements/actions (requiring the exercise of discretion) : in relation to corporate actions affecting Eligible Securities, such as rights issues, take-over offers etc., where a decision as to whether or not to participate in such corporate actions is required to be made by Participants. In most cases, the relevant CCASS procedures will involve HKSCC obtaining relevant instructions from Long Clearing Participants and requiring Short Clearing Participants to comply accordingly (see Section 10.9.7, Section 10.9.8, Section 10.9.9, Section 10.9.10 and Section 10.9.11).

### **10.9.4 Voting**

Long Clearing Participants that wish to give instructions relating to voting for a meeting held in Hong Kong may apply to HKSCC by completing and submitting to HKSCC a "Voting Request Form - CNS Positions" (see CCASS Terminal User Guide for Participants for the form) by 2:00 p.m. one Business Day before the relevant meeting date or by such other means specified by HKSCC which may be subject to other time limits. Otherwise, the deadline prescribed by HKSCC on Long Clearing Participants for the giving of instructions will be on a day which in the opinion of HKSCC would enable it to have sufficient time to submit the proxy form or the relevant document for appointment of corporate representative, as the case may be, to the designated place by the stipulated time. This will be dealt with by HKSCC in the normal way (see Section 8.6.2).

To the extent that there are available relevant Eligible Securities in CCASS for which voting instructions with or without demand poll request have not been received from relevant Participants, HKSCC may in its absolute discretion entertain requests to vote by Long Clearing Participants. Long Clearing Participants that are unable to vote in respect of the relevant Eligible Securities or whose requests are not entertained by HKSCC shall have no claim against HKSCC.

### **10.9.5 Cash dividend entitlements**



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In the case of cash dividends in an Eligible Currency, the following procedures will usually apply :

- (i) on the Business Day following the last Settlement Day preceding the relevant book-close or record date, HKSCC will debit the Entitlements Account (a sub-account of the Money Ledger) of the Short Clearing Participants to collect from them amounts in respect of dividends accruing to their outstanding short CNS stock positions; and
- (ii) on the dividend payment date, HKSCC will credit the Entitlements Accounts of the Long Clearing Participants with amounts in respect of dividends accruing to their outstanding long CNS stock positions.

In the case of cash dividends in a foreign currency which is not an Eligible Currency, the following procedures will usually apply :

- (i) Short Clearing Participants will be required to arrange for funds of the exact amount and currency in respect of dividends accruing to their outstanding short CNS stock positions to be directly paid into the stated bank account of HKSCC by telegraphic transfers (see below);
- (ii) such transfers by the Short Clearing Participants, as referred to in paragraph (i) above, are to be provided to HKSCC at the latest by the close of business on the Business Day following the book-close or record date or other time specified by HKSCC. At the time of arranging such transfers, Short Clearing Participants are also required to submit evidence of such transfers, such as application forms to their banks, to HKSCC; and
- (iii) on the dividend payment date, HKSCC will make available for collection by the Long Clearing Participants relevant foreign currency bank drafts for the amounts in respect of dividends accruing to their outstanding long CNS stock positions. The costs and expenses of arranging these bank drafts will be charged to the Long Clearing Participants.

Any funds derived from payment of cash dividends in a currency which is not an Eligible Currency from Short Clearing Participants must be transferred to one or more bank accounts of HKSCC as from time to time specified by it.

Without prejudice to the above, if HKSCC is reasonably satisfied that the Long Clearing Participants in respect of any or all of their long outstanding CNS stock positions are exempt from or are eligible for a lower rate of withholding tax but the dividends accruing to the Short Clearing Participants' outstanding short CNS stock positions are net of a higher rate of withholding tax (whether withheld by HKSCC or any other parties), HKSCC may require Short Clearing Participants to pay such additional amount, in any Eligible Currency as may be determined by HKSCC from time to time, so that the Long Clearing Participants will receive such amount of cash dividend entitlements as if there had been no late delivery under the CNS System.

HKSCC will be responsible, following the distribution date, to pay Long Clearing Participants the cash dividend entitlements accruing to their outstanding CNS long stock positions irrespective of whether or not HKSCC receives such entitlements from Short Clearing Participants.

### 10.9.6 Bonus issues of securities

In relation to bonus issues of securities, the following procedures will usually apply :

- (i) Short Clearing Participants will normally be required by HKSCC to provide Collateral in the form of cash on the Business Day following the last Settlement Day preceding the relevant book-close or record date;
- (ii) where the bonus securities concerned are already available in the market, Short Clearing Participants are required to have in their Entitlement Account (their Stock Segregated Account 02) the number of bonus securities accruing to their outstanding short CNS stock positions on or before the distribution date of such bonus securities;
- (iii) in the event that a Short Clearing Participant fails to have the relevant number of bonus securities in its Entitlement Account at the close of business on the distribution date referred to in paragraph (ii) above, HKSCC will normally require such Short Clearing Participant to purchase such bonus securities for delivery to HKSCC and the purchase will have to be effected on the Business Day following the distribution date;
- (iv) where the bonus securities concerned are not yet available in the market, Short Clearing Participants will have until the day before the first dealing date of such bonus securities to have the relevant number of bonus securities in their Entitlement Accounts and failure to do so will normally result in HKSCC requiring such Short Clearing Participant to purchase the relevant number of bonus securities on the first dealing date of such bonus securities;
- (v) in the event a Short Clearing Participant fails to purchase the relevant bonus securities as required by HKSCC, HKSCC may itself purchase such bonus securities for the account of that Short Clearing Participant; and
- (vi) upon receipt of all the relevant bonus securities from the Short Clearing Participants, HKSCC will credit such bonus securities into the Entitlement Accounts of the Long Clearing Participants on or after the relevant distribution dates. If such bonus securities are not Eligible Securities, HKSCC will require the Long Clearing Participants to withdraw such bonus securities from the CCASS Depository.

HKSCC will be responsible, following the distribution date, to deliver to Long Clearing Participants the bonus securities accruing to their outstanding CNS long stock positions (or if that is not possible or reasonably practicable, as determined by HKSCC, HKSCC shall provide money compensation to the Long Clearing Participants by reference to the value of such bonus securities as determined by HKSCC), irrespective of whether or not HKSCC receives such entitlements from Short Clearing Participants.

### 10.9.7 Dividend entitlements with options

In relation to dividend entitlements with options, the following procedures will usually apply:

- (i) Short Clearing Participants will normally be required by HKSCC to provide Collateral in the form of cash on the Business Day following the last Settlement Day preceding the relevant book-close or record date;
- (ii) Long Clearing Participants will be required to elect the option they prefer via CCASS Terminals or by such other means specified by HKSCC;
- (iii) Based on the options chosen by the Long Clearing Participants (or their default options), HKSCC will require the Short Clearing Participants to provide it with the relevant

entitlements (in the form as required by HKSCC). The way in which such dividend entitlements are to be provided by the Short Clearing Participants will be as specified in Section 10.9.5 (for cash dividends in an Eligible Currency or in a currency which is not an Eligible Currency) and Section 10.9.6 (for stock dividends), as the case may be; and

- (iv) upon receipt of all the dividend entitlements from Short Clearing Participants, HKSCC will credit such dividend entitlements into the Long Clearing Participants' Entitlement Accounts (for stock dividends), their Entitlements Accounts (for cash dividends), or notify them to collect foreign currency bank drafts, in the manner as specified in Section 10.9.5 and Section 10.9.6, as the case may be.

HKSCC will be responsible, following the distribution date, to pay Long Clearing Participants the relevant cash dividends or to deliver the stock dividends accruing to their outstanding CNS long stock positions (or if that is not possible or reasonably practicable in the case of stock dividend entitlements, as determined by HKSCC, HKSCC shall provide money compensation to the Long Clearing Participants by reference to the value of such stock dividends as determined by HKSCC), irrespective of whether or not HKSCC receives such entitlements from Short Clearing Participants.

#### **10.9.8 Rights issues**

In relation to rights issues (other than rights issues relating to China Connect Securities), the following procedures will usually apply:

- (i) Short Clearing Participants will normally be required by HKSCC to provide Collateral in the form of cash on the Business Day following the last Settlement Day preceding the relevant book-close or record date;
- (ii) Short Participants will be required to have the relevant number of nil paid rights in their Entitlement Account on or before the day before the first dealing date of such nil paid rights;
- (iii) if a Short Clearing Participant fails to have the relevant number of nil paid rights in its Entitlement Account in time, HKSCC will normally require such Short Clearing Participant to purchase such nil paid rights for delivery to HKSCC and the purchase will have to be effected on the first dealing date of such nil paid rights;
- (iv) in the event a Short Clearing Participant fails to purchase relevant nil paid rights as required by HKSCC, HKSCC may itself purchase such nil paid rights for the account of such Short Clearing Participant; and
- (v) upon receipt of all nil paid rights from Short Clearing Participants, HKSCC will credit such nil paid rights into the Entitlement Accounts of the Long Clearing Participants.

If Short Clearing Participants fail to deliver nil paid rights required to enable Long Clearing Participants to apply for rights shares, they will be required to deliver to HKSCC the rights shares which would have been subscribed for by the Long Clearing Participants (based on the instructions of Long Clearing Participants to HKSCC) by depositing the rights shares into their Entitlement Accounts on or before the day of distribution of the rights shares. If a Short Clearing Participant fails to have the relevant number of rights shares in its Entitlement Account in time, HKSCC will normally require such Short Clearing Participant to purchase such rights shares for delivery to HKSCC and the purchase will have to be effected on the Business Day following the date of distribution of rights shares. In the event that such Short Clearing Participant fails to purchase the relevant rights shares as required by HKSCC, HKSCC may itself purchase such rights shares for the account of that Short Clearing

Participant. Following delivery, the relevant subscription monies from the Long Clearing Participants will be paid to the Short Clearing Participants.

Application for rights shares and excess shares by Long Participants will be effected by completing and submitting to HKSCC a "Rights Issues Subscription Election Form - CNS Positions" (see CCASS Terminal User Guide for Participants for the form) together with a cashier order for the subscription money or by any other means as specified by HKSCC by 2:00 p.m. on the Business Day before the last day for subscription for rights shares or any other time as specified by HKSCC, and may not result in HKSCC requiring Short Participants to take action.

If Long Clearing Participants fail to receive rights shares applied for in respect of their outstanding CNS long stock position as a result of late delivery under the CNS System, HKSCC will be responsible, following distribution date, to deliver such rights shares to Long Clearing Participants (against receipt of the relevant subscription monies) or if that is not possible or reasonably practicable as determined by HKSCC, HKSCC shall provide money compensation to the Long Clearing Participants by reference to the value of such rights shares as determined by HKSCC (but taking into account the subscription monies paid or payable by Long Clearing Participants), irrespective of whether or not HKSCC receives such rights shares from Short Clearing Participants.

#### **10.9.9 Open Offers**

In relation to open offers (other than open offers relating to China Connect Securities), the following procedures will usually apply:

- (i) Long Participants wishing to apply for new shares or excess shares under an open offer will be required to complete and submit to HKSCC a "Subscription of Open Offer Form - CNS Positions" (see CCASS Terminal User Guide for Participants for the form) and provide HKSCC with a cashier's order for the relevant amount or by such other means as specified by HKSCC by 2:00 p.m. on the Business Day before the last day for acceptances under an open offer or any other time as specified by HKSCC;
- (ii) in the event that the Long Clearing Participants fail to obtain what would have been their pro-rata entitlements under the terms of an open offer (as a result of full subscription or over subscription under the open offer), HKSCC will require Short Clearing Participants to have in their Entitlement Account on or before the date of distribution of new shares under an open offer, the relevant number of new shares representing the pro-rata entitlement in respect of their outstanding short CNS stock positions under the terms of such open offer;
- (iii) HKSCC will normally require Collateral in the form of cash from Short Clearing Participants;
- (iv) based on the number of new shares required to satisfy the pro-rata entitlement of Long Clearing Participants, HKSCC will debit the relevant number of new shares from the Entitlement Accounts of the Short Clearing Participants and a Short Clearing Participant having an insufficient number of new shares in its Entitlement Account will normally be required by HKSCC to purchase such new shares for delivery to HKSCC and such purchase will have to be effected on the Business Day following the date of distribution of new shares under the open offer. In the event that such Short Clearing Participant fails to purchase the relevant new shares as required by HKSCC, HKSCC may itself purchase such new shares for the account of that Short Clearing Participant;
- (v) HKSCC will cause the relevant amounts, based on the subscription price of new shares under the terms of the open offer, to be credited to the Entitlements Accounts of the

Short Clearing Participants upon receipt of new shares from them (HKSCC will have received the relevant subscription money from the Long Clearing Participants in advance); and

- (vi) Upon receipt from the Short Clearing Participants of all the new shares required to satisfy the pro-rata entitlements of the Long Clearing Participants, HKSCC will credit such new shares into the Entitlement Accounts of the Long Clearing Participants.

Applications for excess shares by Long Participants will be dealt with in the normal manner (see Section 8.11.4) and will not usually result in HKSCC requiring Short Participants to take action.

If Long Clearing Participants fail to receive new shares pursuant to their pro-rata entitlements under open offers in respect of their outstanding CNS long stock positions (as a result of late delivery under the CNS System), HKSCC shall be responsible, following the distribution date, to deliver such new shares to Long Clearing Participants (against receipt of the relevant subscription monies) or if that is not possible or reasonably practicable as determined by HKSCC, HKSCC shall provide money compensation to the Long Clearing Participants by reference to the value of such new shares as determined by HKSCC (but taking into account the subscription monies paid or payable by Long Clearing Participants), irrespective of whether or not HKSCC receives such new shares from Short Clearing Participants.

#### **10.9.10 Take-over offers**

In relation to takeover offers, the following procedures will usually apply :

- (i) Short Clearing Participants will normally be required by HKSCC to provide Collateral in the form of cash on the last acceptance day of the take-over offer;
- (ii) Long Clearing Participants who wish to accept a take-over offer will have to complete and submit election forms called "Take-over Offer Acceptance/Election Form - CNS Positions" (see CCASS Terminal User Guide for Participants for the form) to HKSCC or to apply to HKSCC by any other means as specified by HKSCC by 2:00 p.m. on the last Business Day before the last day of acceptance of a take-over offer or any other time as specified by HKSCC; and
- (iii) since take-over offers may involve a number of variations on a case by case basis, HKSCC will require Short Clearing Participants to provide relevant monies or securities (or appropriate compensation) in such manner as HKSCC may in its absolute discretion consider fair and appropriate to provide compensation to Long Clearing Participants.

#### **10.9.11 Conversion of warrants**

In relation to conversion of warrants close to expiry or otherwise subject to corporate actions, the following procedures will normally apply :

- (i) on the due date of settlement of the last trading day of warrants about to expire, or the Business Day before the last day to participate in corporate actions affecting the warrants, as the case may be, Long Participants will be asked by HKSCC to elect whether or not to subscribe for securities under the warrants. A Long Participant wishing to subscribe for securities under warrants will be required to complete a "Warrant Conversion Election Form - CNS Positions" (see CCASS Terminal User Guide for Participants for the form) and provide HKSCC with a cashier's order for the relevant amount or to apply to HKSCC by any other means as specified by HKSCC by 2:00 p.m. on the Business Day before the last day of subscription of the warrants

(or the Business Day before the last day to participate in corporate actions affecting the warrants, as the case may be) or any other time as specified by HKSCC;

- (ii) based on the instructions of the Long Clearing Participants, HKSCC will require Short Clearing Participants to have in their Entitlement Accounts on or before the date of distribution of securities under the warrants, the relevant number of such securities capable of being subscribed for in respect of their outstanding short CNS stock positions;
- (iii) HKSCC will normally require Collateral in the form of cash from Short Clearing Participants;
- (iv) based on the number of securities required by Long Clearing Participants, HKSCC will debit the relevant number of such securities from the Entitlement Accounts of the Short Clearing Participants and a Short Clearing Participant not having sufficient securities will normally be required by HKSCC to purchase such securities for delivery to HKSCC and such purchase will have to be effected on the Business Day following the date of distribution of such securities under the warrants. In the event that such Short Clearing Participant fails to purchase such securities as required by HKSCC, HKSCC may itself purchase such securities for the account of that Short Clearing Participant;
- (v) HKSCC will cause the relevant amounts, based on the subscription price of the securities under the warrants, to be credited to the Entitlements Accounts of the Short Clearing Participants upon receipt of securities from them (HKSCC will have received the relevant subscription money from the Long Clearing Participants in advance); and
- (vi) upon receipt from the Short Clearing Participants of all such securities required to satisfy the requirements of the Long Clearing Participants, HKSCC will credit such new securities into the Entitlement Accounts of the Long Clearing Participants.

If Long Clearing Participants fail to receive new shares they would have subscribed for under warrants in respect of their outstanding CNS long stock positions (as a result of late delivery under the CNS System), HKSCC shall be responsible, following the distribution date, to deliver such new shares to Long Clearing Participants (against receipt of the relevant subscription monies) or if that is not possible or reasonably practicable as determined by HKSCC, HKSCC shall provide money compensation to the Long Clearing Participants by reference to the value of such new shares as determined by HKSCC (but taking into account the subscription monies paid or payable by Long Clearing Participants), irrespective of whether or not HKSCC receives such new shares from Short Clearing Participants.

#### **10.9.11A Automatic exercise / Redemption of listed Structured Products at expiry**

Structured Products listed on the Exchange which are in-the-money will be exercised automatically at expiry upon the lapse of the date of expiry specified in the relevant listing document (“normal expiry”) or upon the Structured Products being early terminated as a result of the occurrence of the relevant call event (“early expiry”). In relation to the cash payments to which Participants are entitled upon the automatic exercise of such Structured Products at expiry, the following procedures will usually apply:

- (i) on the Business Day following the second Settlement Day in the case of early expiry or the second Business Day following the expiry day in the case of normal expiry, HKSCC will debit the Entitlements Account (a sub-account of the Money Ledger) of each Short Clearing Participant to collect from it an amount representing the cash payment accruing to its outstanding short CNS stock positions in the Structured

Products. For administrative convenience or if the expiry day does not fall on a Settlement Day or if considered appropriate by HKSCC, HKSCC may in its absolute discretion collect the cash payment from each Short Clearing Participant on some other date; and

- (ii) on the payment day or such other date as HKSCC shall consider fair and appropriate, HKSCC will credit the Entitlements Account of each Long Clearing Participant with an amount representing the cash payment accruing to its outstanding long CNS stock positions in the Structured Products.

HKSCC will be responsible, following the payment day, to pay the Long Clearing Participants the cash payments accruing to their outstanding CNS long stock positions in the Structured Products irrespective of whether or not HKSCC is able to collect such amounts from the Short Clearing Participants.

In relation to the redemption of Structured Products listed on the Exchange at expiry, the following procedures will usually apply:

- (i) in respect of redemption proceeds in the form of cash payment in an Eligible Currency:
  - (a) on the first Business Day immediately after the expiry day, HKSCC will debit the Entitlements Account (a sub-account of the Money Ledger) of each Short Clearing Participant to collect from it the cash payment accruing to its outstanding short CNS stock positions in the Structured Products; and
  - (b) on the payment day or such other date as HKSCC shall consider fair and appropriate, HKSCC will credit the Entitlements Account of each Long Clearing Participant with the cash payment accruing to its outstanding long CNS stock positions in the Structured Products.

HKSCC will be responsible, following the payment day, to pay the Long Clearing Participants the cash payments accruing to their outstanding CNS long stock positions in the Structured Products irrespective of whether or not HKSCC is able to collect such cash payments from the Short Clearing Participants.

- (ii) in respect of redemption proceeds in the form of underlying securities (being Eligible Securities):
  - (a) on the second Business Day immediately after the expiry day, Short Clearing Participants will normally be required by HKSCC to provide Collateral in the form of cash;
  - (b) on or before the distribution day, Short Clearing Participants are required to have in their Entitlement Accounts (their Stock Segregated Account 02) the relevant quantities of underlying securities accruing to their outstanding short CNS stock positions in the Structured Products;
  - (c) in the event that a Short Clearing Participant fails to have the relevant quantities of underlying securities in its Entitlement Account at the close of business on the distribution day, HKSCC will normally require such Short Clearing Participant to purchase such quantities of underlying securities for delivery to HKSCC and the purchase will have to be effected on the Business Day following the distribution day;

- (d) in the event that a Short Clearing Participant fails to purchase the relevant quantities of underlying securities as required by HKSCC, HKSCC may itself purchase such quantities of underlying securities for the account of that Short Clearing Participant; and
- (e) upon receipt or purchase of the relevant quantities of underlying securities from or for the account of the Short Clearing Participants, HKSCC will credit such quantities of underlying securities to the Entitlement Accounts of the Long Clearing Participants on the distribution day or such other date as HKSCC shall consider fair and appropriate.

HKSCC will be responsible, following the distribution day, to deliver to the Long Clearing Participants the relevant quantities of underlying securities accruing to their outstanding CNS long stock positions (or if that is not possible or reasonably practicable as determined by HKSCC, HKSCC shall provide money compensation to the Long Clearing Participants by reference to the value of such quantities of underlying securities as determined by HKSCC), irrespective of whether or not HKSCC receives such quantities of underlying securities from the Short Clearing Participants.

#### **10.9.11B Repealed**

#### **10.9.11C Repealed**

#### **10.9.12 Interest Payments**

In the case of interest payments, the following procedures will usually apply:

- (i) on the Business Day following the last Settlement Day preceding the relevant book-close day or the relevant CCASS Record Date (the date by reference to which the entitlements to interest payments are determined), HKSCC will debit the Entitlements Account of the Short Clearing Participants to collect from them amounts in respect of interest payments accruing to their outstanding short CNS positions; and
- (ii) on the interest payment date or on the dates the relevant outstanding long CNS stock positions are settled or on such other dates as HKSCC shall consider fair and appropriate, HKSCC will credit the Entitlements Accounts of the Long Clearing Participants with amounts in respect of interest payments accruing to their outstanding long CNS stock positions.

HKSCC will be responsible, following the distribution date, to pay Long Clearing Participants the interest payment entitlements accruing to their outstanding long CNS stock positions irrespective of whether or not HKSCC receives such entitlements from Short Clearing Participants.

#### **10.9.13 Redemption of Debt Securities**

In relation to redemption of eligible Debt Securities called by the issuer effected at or before its maturity, and either in part or full, the following procedures will usually apply:

- (i) Short Clearing Participants will normally be required by HKSCC to provide Collateral in the form of cash on the Business Day following the last Settlement Day preceding the relevant book-close day or the relevant CCASS Record Date (the date by reference to which the entitlements to take part in such redemption are determined); and



- (ii) on the distribution date or the dates their outstanding CNS long stock positions are settled or such other dates as HKSCC shall consider fair and appropriate, HKSCC will cause the relevant principal amounts and accrued interest where applicable to be credited to the Entitlements Accounts to the Long Clearing Participants.

In the case of redemption applying to specific certificate numbers, the Participants with outstanding CNS stock positions will be excluded from the random computerised balloting for determining from which Participants' Stock Accounts, and in what quantities, the relevant Debt Securities are to be redeemed.

#### **10.9.14 Conversion of Debt Securities**

In relation to conversion of eligible Debt Securities close to expiry, the following procedures will usually apply :

- (i) on the due date of settlement of the Business Day before the last day of the conversion period, Long Clearing Participants who wish to subscribe/convert for securities accruing to their due Debt Securities positions through CCASS will be required to complete a "Debt Securities Conversion Request Form – CNS Positions" (see CCASS Terminal User Guide for Participants for the form) and provide HKSCC with a cashier order for the relevant amount or to apply to HKSCC by any other means as specified by HKSCC by 2:00 p.m. on the Business Day before the last day of subscription/conversion of the Debt Securities or such other means or time as may be specified by HKSCC;
- (ii) based on the instructions of the Long Clearing Participants, HKSCC will require Short Clearing Participants to have in their Entitlement Accounts on or before the date of distribution of securities under the Debt Securities conversion, the relevant number of such securities capable of being subscribed for in respect of their outstanding short CNS stock positions;
- (iii) HKSCC will normally require Collateral in the form of cash from Short Clearing Participants;
- (iv) based on the number of securities required by Long Clearing Participants, HKSCC will debit the relevant number of such securities from the Entitlement Accounts of the Short Clearing Participants and a Short Clearing Participant not having sufficient securities will normally be required by HKSCC to purchase such securities for delivery to HKSCC and such purchase will have to be effected on the Business Day following the date of distribution of such securities under the Debt Securities conversion. In the event that such Short Clearing Participant fails to purchase such securities as required by HKSCC, HKSCC may itself purchase such securities for the account of that Short Clearing Participant;
- (v) HKSCC will cause the relevant amounts, based on the subscription price of the securities under the Debt Securities conversion, to be credited to the Entitlements Accounts of the Short Clearing Participants upon receipt of securities from them (HKSCC will have received the relevant subscription money from the Long Clearing Participants in advance); and
- (vi) upon receipt from the Short Clearing Participants of all such securities required to satisfy the requirements of the Long Clearing Participants, HKSCC will credit such securities received into the Entitlement Accounts of the Long Clearing Participants.

If Long Clearing Participants fail to receive the securities they would have subscribed for under Debt Securities conversion in respect of their outstanding long CNS stock positions

(as a result of late delivery under the CNS System), HKSCC shall be responsible, following the distribution date, to deliver such securities to the Long Clearing Participants (against receipt of the relevant subscription monies) or if that is not possible or reasonably practicable as determined by HKSCC, HKSCC shall provide money compensation to the Long Clearing Participants by reference to the value of such securities as determined by HKSCC (but taking into account the subscription monies paid or payable by Long Clearing Participants), irrespective of whether or not HKSCC receives such securities from Short Clearing Participants.

#### **10.9.15 Daily accrued interest of interest bearing Debt Securities**

In cases where the Short Participant cannot deliver the eligible Debt Securities on the due settlement day of the Exchange Trade in such eligible Debt Securities, daily accrued interest amount of that Exchange Trade concerned will remain unchanged even if the eligible Debt Securities involved are settled in a later day.

#### **10.9.16 Sub-divisions, consolidations etc.**

The procedures for handling outstanding stock positions in the event of sub-divisions, consolidations and stock conversions affecting Eligible Securities are set out in Section 8.14.

#### **10.9.17 Fractional securities**

Fractional securities entitlements as a result of adjustments for late deliveries under the CNS System will be dealt with in the same manner as set out in Section 8.21.

### **10.10 RISK MANAGEMENT : MARKS**

#### **10.10.1 General**

As settlement counterparty to Participants under the CNS System, HKSCC is exposed to market risks as a result of unfavourable fluctuations of prices in respect of the unsettled stock positions of Participants under the CNS System. In this Section 10.10, any unsettled stock positions in Eligible Securities under the CNS System are referred to as “CNS stock positions”, provided that, in respect of a Multi-counter Eligible Security, all its CNS stock positions will be considered on a cross-currency offset basis for risk management calculation purpose using the methodology set out in the RMS Guide.

To monitor and control such risk exposure, HKSCC will Mark-to-market the CNS stock positions of Participants and collect Marks from Participants. In respect of the CNS stock positions in any Eligible Security, HKSCC will compute Marks in accordance with the provisions of this Section 10.10 in the Eligible Currency in which that Eligible Security is traded (or, in the case of a Multi-counter Eligible Security, in such Eligible Currency as designated by HKSCC from time to time).

HKSCC will collect Marks from the Participant in Hong Kong dollar unless the Participant has maintained a Preferred Single Settlement Currency in another currency or unless the Marks are to be collected from a Clearing Agency Participant.

Where the Eligible Currency in which an Eligible Security is traded is not Hong Kong dollar, HKSCC will convert Marks in the Eligible Currency to Hong Kong dollar at such exchange rate and subject to such haircut as determined by HKSCC from time to time. Where the Participant has maintained a Preferred Single Settlement Currency which is not Hong Kong dollar, HKSCC will further convert Marks from Hong Kong dollar to the Preferred Single Settlement Currency at such exchange rate and subject to such haircut rate as determined by HKSCC from time to time, and collect Marks from the Participant in the Preferred Single Settlement Currency. Notwithstanding the foregoing, HKSCC reserves the right to collect the required amount of Marks in any Eligible Currency.

Where the Participant is a Clearing Agency Participant which is a China Connect Clearing House, Marks will be computed and collected from or redelivered to such Participant separately in respect of each of its designated Special Participants with reference to the CNS stock positions arising from Exchange Trades executed by such Special Participant, and references to the CNS stock positions of a Participant in this Section 10.10 shall be construed accordingly for such Clearing Agency Participant. HKSCC will convert the Marks to Renminbi at such exchange rate and subject to such haircut rate as determined by HKSCC from time to time and collect the Marks from the Clearing Agency Participant in Renminbi. Unless HKSCC otherwise agrees, the Clearing Agency Participant shall pay Marks to HKSCC in Renminbi. Notwithstanding the foregoing, HKSCC reserves the right to collect the required amount of Marks in any Eligible Currency.

Mark-to-market of a CNS stock position involves the evaluation of the risk exposure of a Participant to HKSCC relating to the CNS stock position by reference to the extent to which the Mark-to-market value of the CNS stock position has moved against the value originally agreed in respect of such CNS stock position.

Under the Rules, HKSCC has the right to collect Marks from Participants in respect of all CNS stock positions, whether or not due for settlement and whether or not such CNS stock positions may be subsequently amended or excluded or not accepted for settlement under the CNS System in accordance with the Rules.

Marks will normally be collected in the form of cash. HKSCC may in exceptional cases collect Marks in the form of Collateral Securities acceptable to it.

This Section 10.10 describes the extent to and the manner in which Marks from Participants will be collected and redelivered by HKSCC.

The provisions of this Section 10.10 shall also be applicable, in so far as they are relevant to risk management measures detailed in Section 12.2.9(i), in respect of Clearing Agency Transactions.

#### **10.10.2 Various terms explained**

For the purpose of this Section, the term "Favourable Marks" refers to Marks computed by the Mark-to-market of a CNS stock position which are favourable to a Participant and the term "Unfavourable Marks" has the opposite meaning.

A "day-end Marks position", in relation to the calculation and collection of day-end Marks, comprises the following stock positions of a Participant:

- (i) "pending CNS stock positions", which are the unsettled CNS stock positions of the Participant which are not yet due for settlement.

Under a T+2 settlement system, pending CNS stock positions of a Participant on a Business Day will be derived from Exchange Trades which were effected by the Participant and, in the case of a GCP or a Clearing Agency Participant, will include Exchange Trades effected and, where applicable, designated to it for clearing by each NCP or Special Participant with which such GCP or Clearing Agency Participant has entered into a Clearing Agreement, on that Business Day ("Current Day") and the immediately preceding Business Day ("Previous Day") and which had been accepted by HKSCC for settlement under the CNS System. Such pending CNS stock positions on the Current Day and Previous Day shall be referred to in this Section 10.10.2 as "Current Day positions" and "Previous Day positions" respectively. Unless otherwise stated, "pending CNS stock positions" in this Section

10.10.2 cover both Current Day positions and Previous Day positions;

- (ii) “overdue CNS stock positions”, which are the CNS stock positions of the Participant which are due for settlement but not yet settled; and
- (iii) “corporate action entitlement positions”, which are the stock positions to which the Participant is entitled under CCASS, as determined by HKSCC based on the holding of that Participant in the relevant Eligible Securities as at the date by reference to which the entitlement is determined.

An "intra-day Marks position", in relation to the calculation and collection of intra-day Marks, may comprise any of the following stock positions of a Participant which are not covered by cash prepayment or credit from settlement activities:

- (i) pending CNS stock positions, as referred to in this Section 10.10.2;
- (ii) overdue CNS stock positions, as referred to in this Section 10.10.2;
- (iii) corporate action entitlement positions, as referred to in this Section 10.10.2; and
- (iv) Allocated Positions.

### **10.10.3 Computation of Marks**

The value of the Mark on a CNS stock position of a Participant is the difference between:

- (i) the money position of that CNS stock position (see Section 10.5.2); and
- (ii) the prevailing market value of such CNS stock position (as determined by HKSCC).

The Marks on CNS stock positions of any Eligible Security, other than any Multi-counter Eligible Security, will first be calculated and denominated in the Eligible Currency in which the Eligible Security is traded. In respect of a Multi-counter Eligible Security, all its CNS stock positions under different Eligible Currencies will be offset against each other first and then Marks will be calculated in Hong Kong dollars by converting the value of any non-Hong Kong dollar positions into Hong Kong dollars subject to such haircut as determined by HKSCC from time to time. Favourable Marks and Unfavourable Marks in the same Eligible Currency will offset against one another to arrive at the Favourable Marks or Unfavourable Marks in that Eligible Currency.

Favourable Marks or Unfavourable Marks in an Eligible Currency will then be offset against the Unfavourable Marks or Favourable Marks, as the case may be, in other Eligible Currencies in the sequence as HKSCC considers appropriate to arrive at the Net Favourable Marks or Net Unfavourable Marks on the CNS stock positions. For the purpose of performing such cross-currency offset, Favourable Marks and Unfavourable Marks in Eligible Currencies other than Hong Kong dollar will be converted to Hong Kong dollar equivalent at such exchange rate and subject to such haircut rate as determined by HKSCC from time to time for computation.

Where a Participant has provided the relevant quantity of Collateral Security to cover a part or the whole of a short CNS stock position not due for settlement to HKSCC pursuant to Rule 3601, the short CNS stock position covered by the Collateral Security will be waived from computation of Marks. HKSCC has absolute right to use such Collateral Security to settle the covered portion of the short CNS stock position on or before its Settlement Day.

Where a Participant has provided the relevant amount of Specific Cash Collateral to cover

the corresponding money position of a part or the whole of a long CNS stock position not due for settlement to HKSCC pursuant to Rule 3601, the long CNS stock position covered by the Specific Cash Collateral will be waived from computation of Marks. HKSCC has absolute right to use such Specific Cash Collateral to settle the money position of the covered portion of the long CNS stock position on or before its Settlement Day.

#### **10.10.3A Marks on day-end Marks position**

In relation to the calculation and collection of day-end Marks on day-end Marks positions, Favourable Marks and Unfavourable Marks on such positions in the same Eligible Currency will be offset against each other to arrive at the Net Favourable Marks or Net Unfavourable Marks in that Eligible Currency.

Net Favourable Marks or Net Unfavourable Marks in an Eligible Currency will then be offset against the Net Unfavourable Marks or Net Favourable Marks, as the case may be, on day-end Marks positions in other Eligible Currencies in the sequence as HKSCC considers appropriate to arrive at the Net Favourable Marks or Net Unfavourable Marks on such day-end Marks positions. For the purpose of performing such cross-currency offset, Favourable Marks and Unfavourable Marks in Eligible Currencies other than Hong Kong dollar will be converted to Hong Kong dollar equivalent at such exchange rate and subject to such haircut rate as determined by HKSCC from time to time for computation. After cross-currency offset, any resulting Net Unfavourable Marks will be collected by HKSCC as day-end Marks from the Participant at day end. The Net Favourable Marks on day-end Marks positions will be used to offset the day-end Margin, if any, of the Participant.

Net Favourable Marks on day-end Marks positions resulting from the computation of day-end Marks, if any, will not be paid to the Participant by HKSCC.

#### **10.10.3B Marks on intra-day Marks positions**

In relation to the calculation and collection of intra-day Marks on intra-day Marks positions, Favourable Marks and Unfavourable Marks on such positions in the same Eligible Currency will be offset against each other to arrive at the Net Favourable Marks or Net Unfavourable Marks in that Eligible Currency.

Net Favourable Marks or Net Unfavourable Marks in an Eligible Currency will then be offset against the Net Unfavourable Marks or Net Favourable Marks, as the case may be, on intra-day Marks positions in other Eligible Currencies in the sequence as HKSCC considers appropriate to arrive at the Net Favourable Marks or Net Unfavourable Marks on such intra-day Marks positions. For the purpose of performing such cross-currency offset, Favourable Marks and Unfavourable Marks in Eligible Currencies other than Hong Kong dollar will be converted to Hong Kong dollar equivalent at such exchange rate and subject to such haircut rate as determined by HKSCC from time to time for computation. After cross-currency offset, any resulting Net Unfavourable Marks will be collected by HKSCC as intra-day Marks from the Participant by the time prescribed by HKSCC.

Net Favourable Marks on intra-day Marks positions resulting from the computation of intra-day Marks, if any, will not be paid to the Participant by HKSCC.

#### **10.10.4 [Repealed]**

#### **10.10.5 [Repealed]**

#### **10.10.6 [Repealed]**

#### **10.10.7 [Repealed]**

**10.10.8A [Repealed]****10.10.8B [Repealed]****10.10.9 [Repealed]****10.10.10 Interest on Marks collected**

HKSCC may allow or charge, at its absolute discretion, to Participants interest on the Marks collected in cash calculated at a rate determined by HKSCC from time to time for each CCMS House Collateral Account allocated to the Participants. HKSCC reserves the right to deduct any administrative costs from any interests to be allowed or to charge such administrative cost to the Marks collected in cash.

Unless otherwise specified by HKSCC, interest to be allowed or charged on Marks provided in cash, if any, will be accrued daily and paid (after deduction of the administrative costs, if applicable) or charged (together with the administrative costs, if applicable) monthly by HKSCC to Participants in the same currency as the cash on which the interest accrued, by crediting or debiting, as the case may be, the CCMS House Collateral Accounts allocated to the Participants, or in the case of a Clearing Agency Participant which is a China Connect Clearing House, to such Clearing Agency Participant in respect of the relevant Special Participant on the first Business Day of the following month.

**10.10.11 Collection of Marks****(i) Clearing Participants**

Marks to be requested from a Clearing Participant on each Business Day will be collateralized against the value (or the Discounted Market Value, if applicable) of the General Collateral Inventory in the CCMS House Collateral Account of the Clearing Participant. For details of the collateralization process, reference should be made to Section 10.15.3.

**(ii) Clearing Agency Participants**

In respect of CNS stock positions arising from Exchange Trades executed by each designated Special Participant of a Clearing Agency Participant, HKSCC will convert the Marks to Renminbi at such exchange rate and subject to such haircut rate as determined by HKSCC from time to time. Unless HKSCC otherwise agrees, the Clearing Agency Participant shall pay Marks to HKSCC in Renminbi. Notwithstanding the foregoing, HKSCC reserves the right to collect the required amount of Marks in any Eligible Currency.

Unless otherwise agreed by HKSCC, any shortfall in day-end Marks required from a Clearing Agency Participant in respect of a designated Special Participant, as determined by HKSCC, will be debited to the Miscellaneous Account allocated to the Clearing Agency Participant in respect of the designated Special Participant and will be collected from such Clearing Agency Participant on the Business Day following T-day by issuing DDIs for same day settlement to the Designated Bank of the Clearing Agency Participant as part of the CCASS money settlement process, or in any other manner determined by HKSCC from time to time. In general, any surplus cash collateral over Marks in the CCMS House Collateral Account allocated to a Clearing Agency Participant in respect of a designated Special Participant will be automatically redelivered to the Clearing Agency Participant in respect of such designated Special Participant on the Business Day following T-day by HKSCC issuing DCIs for same day settlement to the Designated Bank of the Clearing Agency Participant as part of the CCASS money settlement process, or in any other manner determined by HKSCC

from time to time. Notwithstanding the foregoing, HKSCC reserves the right not to redeliver surplus cash collateral at any time it considers appropriate.

If there is any shortfall in Marks after the collateralization, HKSCC will collect the shortfall in Hong Kong dollar unless the Clearing Participant has maintained a Preferred Single Settlement Currency which is not Hong Kong dollar. Where the Clearing Participant has maintained a Preferred Single Settlement Currency which is not Hong Kong dollar, HKSCC will convert the shortfall to the Preferred Single Settlement Currency at such exchange rate and subject to such haircut rate as determined by HKSCC from time to time, and HKSCC will collect the shortfall in Marks in the Preferred Single Settlement Currency. Notwithstanding the foregoing, HKSCC reserves the right to collect the required amount of Marks in any Eligible Currency.

Unless otherwise agreed by HKSCC, any shortfall in Marks required, as determined by HKSCC, will be debited to the Marks and Margin Account of a Clearing Participant and will be collected from the Clearing Participant on a daily basis by HKSCC via CPIs or by issuing DDIs to the Designated Bank of the Clearing Participant as part of the CCASS money settlement process, or in any other manner determined by HKSCC from time to time. Subject to the determination of HKSCC, any surplus cash collateral over Marks and Margin in the CCMS House Collateral Account will not be automatically redelivered at the end of the day and HKSCC reserves the right to redeliver surplus cash collateral at any time it considers appropriate. HKSCC may redeliver such surplus to the Clearing Participant upon redelivery instruction from the Clearing Participant given to HKSCC in such form prescribed by HKSCC, and the redelivery will be made in such manner and at such time as prescribed by HKSCC from time to time.

## **10.10A RISK MANAGEMENT: MARGIN**

### **10.10A.1 General**

As settlement counterparty to Participants under the CNS System, HKSCC is exposed to market risks as a result of potential unfavourable fluctuations of prices in respect of the unsettled stock positions of Participants under the CNS System. In this Section 10.10A, any unsettled stock positions in Eligible Securities under the CNS System are referred to as “CNS stock positions”, provided that, in respect of a Multi-counter Eligible Security, all its CNS stock positions will be considered on a cross-currency offset basis for risk management calculation purpose using the methodology set out in the RMS Guide.

To monitor and control such risk exposure, HKSCC will compute Margin on the CNS stock positions of Participants and collect Margin from Participants. In respect of the CNS stock positions in any Eligible Security, HKSCC will compute Margin in accordance with the provisions of this Section 10.10A in the Eligible Currency in which that Eligible Security is traded (or, in the case of a Multi-counter Eligible Security, in such Eligible Currency as designated by HKSCC from time to time).

#### **(i) Clearing Participants**

HKSCC will collect Margin from the Clearing Participant in Hong Kong dollar unless the Clearing Participant has maintained a Preferred Single Settlement Currency which is not Hong Kong dollar.

#### **(ii) Clearing Agency Participants**

Where the Participant is a Clearing Agency Participant which is a China Connect Clearing House, Margin will be computed and collected from or redelivered to such Participant separately in respect of each of its designated Special Participants with

reference to the CNS stock positions arising from Exchange Trades executed by such Special Participant, and references to the CNS stock positions of a Participant in this Section 10.10A shall be construed accordingly for such Clearing Agency Participant. HKSCC will convert the Margin to Renminbi at such exchange rate and subject to such haircut rate as determined by HKSCC from time to time and collect the Margin from the Clearing Agency Participant in Renminbi. Unless HKSCC otherwise agrees, the Clearing Agency Participant shall pay Margin to HKSCC in Renminbi. Notwithstanding the foregoing, HKSCC reserves the right to collect the required amount of Margin in any Eligible Currency.

Where the Clearing Participant has maintained a Preferred Single Settlement Currency which is not Hong Kong dollar, HKSCC will convert Margin calculated in Hong Kong dollar to the Preferred Single Settlement Currency at such exchange rate and subject to such haircut rate as determined by HKSCC from time to time, and collect Margin from the Clearing Participant in the Preferred Single Settlement Currency. Notwithstanding the foregoing, HKSCC reserves the right to collect the required amount of Margin in any Eligible Currency.

The computation of Margin on a CNS stock position involves the estimation of the risk exposure of a Participant to HKSCC relating to the CNS stock position by reference to the estimated future market movement against the Mark-to-market value of such CNS stock position.

Under the Rules, HKSCC has the right to collect Margin from Participants in respect of all CNS stock positions, whether or not due for settlement and whether or not such CNS stock positions may be subsequently amended or excluded or not accepted for settlement under the CNS System in accordance with the Rules.

Margin will normally be collected in the form of cash. HKSCC may in exceptional cases collect Margin in the form of Collateral Securities acceptable to it.

This Section 10.10A describes the extent to and the manner in which Margin from Participants will be collected and redelivered by HKSCC.

The provisions of this Section 10.10A shall also be applicable, in so far as they are relevant to risk management measures detailed in Section 12.2.9(i), in respect of Clearing Agency Transactions.

#### **10.10A.2 Computation of Margin**

##### **(i) Margin requirement**

The Margin requirement on CNS stock positions of a Participant will be computed in accordance with the methodology referred to in the Initial Margin Calculation Guide.

The amount of Margin requirement on CNS stock positions in an Eligible Security is computed in Hong Kong dollar. Where the Clearing Participant has maintained a Preferred Single Settlement Currency which is not Hong Kong dollar, HKSCC will convert Margin calculated in Hong Kong dollar to the Preferred Single Settlement Currency at such exchange rate and subject to such haircut rate as determined by HKSCC from time to time, and collect Margin from the Clearing Participant in the Preferred Single Settlement Currency. Notwithstanding the foregoing, HKSCC reserves the right to collect the required amount of Margin in any Eligible Currency.

For the avoidance of doubt, HKSCC has the right to compute Margin requirement using other methods and assumptions as HKSCC may from time to time consider appropriate.



## (ii) Marginable Position

Marginable Position refers to the CNS stock positions included in the computation of Margin using a hybrid approach or such other methodology as may from time to time be determined by HKSCC and referred to in the Initial Margin Calculation Guide. Marginable Positions can be broadly divided into three categories, which are summarised as follows:

- (i) primary tier (Tier P) positions: subject to portfolio margining and minimum margin levels prescribed by HKSCC from time to time;
- (ii) non-constituent Tier (Tier N) positions: subject to a flat Margin Rate and margin multipliers prescribed by HKSCC from time to time; and
- (iii) corporate action entitlement positions: subject to a flat Margin Rate prescribed by HKSCC from time to time.

In respect of the methodology of categorisation, please refer to the Initial Margin Calculation Guide.

Multi-counter Eligible Securities of the same class of an Issuer will be netted against each other for the determination of the Mark-to-market value of the CNS stock positions as mentioned above.

Where a Participant has provided the relevant quantity of Collateral Security to cover a part or the whole of a short CNS stock position not due for settlement to HKSCC pursuant to Rule 3601A, the Mark-to-market value of the net short day-end Marks positions or intra-day Marks positions, and hence the Marginable Position for computation of Margin, will be reduced by the Mark-to-market value of the short CNS stock position covered by the Collateral Security, as HKSCC considers appropriate. HKSCC has absolute right to use such Collateral Security to settle the covered portion of the short CNS stock position on or before its Settlement Day.

Where a Participant has provided the relevant amount of Specific Cash Collateral to cover the corresponding money position of a part or the whole of a long CNS stock position not due for settlement to HKSCC pursuant to Rule 3601A, the Mark-to-market value of the net long day-end Marks positions or intra-day Marks positions, and hence the Marginable Position for computation of Margin, will be reduced by the Mark-to-market value of the long CNS stock position covered by the Specific Cash Collateral, as HKSCC considers appropriate. HKSCC has absolute right to use such Specific Cash Collateral to settle the money position of the covered portion of the long CNS stock position on or before its Settlement Day.

## (iii) Margin Rate

The flat Margin Rates for Tier N positions and corporate action entitlement positions will be determined by HKSCC in its absolute discretion from time to time.

## (iv) Margin Multiplier

The Margin Multiplier will be defined and applied to Tier N positions at individual Participant level as HKSCC may consider appropriate. It will be determined by HKSCC in its absolute discretion from time to time by reference to the level of risk exposure of the individual Participant to HKSCC and such other matters as HKSCC may consider relevant.

## (v) Favourable Marks Offset

The Margin amount calculated on Marginable Position in Hong Kong dollar will be offset by the Net Favourable Marks on day-end Marks positions.

## (vi) Margin Credit

The Margin Credit is the credit limit allowed to each Clearing Participant and the credit limit will be determined by HKSCC in its absolute discretion from time to time. HKSCC has the right to determine the credit limit on an individual Clearing Participant basis. In general, Margin Credit will be valued in Hong Kong dollar.

In the case where a Clearing Participant has Marginable Position in more than one Eligible Currency, Margin will be converted to and calculated in Hong Kong dollar and Margin Credit in Hong Kong dollar will be applied to such Margin.

For the avoidance of doubt, the Margin Credit shall only be utilized for the purpose of reducing the Margin requirement of the Clearing Participant as described in paragraph (i) above. HKSCC will not be required to make any actual payment in respect of the Margin Credit or any part thereof, irrespective of whether it has been utilized or not, to the Clearing Participant at any time, as referred to in Rule 2507A.

Margin Credit is not applicable to Clearing Agency Participants for the purpose of computing their Margin requirement.

(vii) HKSCC's rights

HKSCC reserves the right to use any other formula or adopt any other methodology in computing Margin, and the right to determine the Marginable Position, flat Margin Rates, Margin Multiplier and Margin Credit of a Clearing Participant or a Clearing Agency Participant in any manner. HKSCC will inform Participants of any changes to the Margin formula or methodology, the Margin Multiplier, flat Margin Rates and the Margin Credit.

Notwithstanding the above, HKSCC may prescribe Margin requirement on a Participant in any amount and manner, and at any time. For the avoidance of doubt, HKSCC may at any time at its absolute discretion require or demand higher Margin from Participants or any individual Participant. The Participants or individual Participant shall pay such higher Margin to HKSCC forthwith on demand.

### **10.10A.3[Repealed]**

### **10.10A.4 Example (Computation of Day-end Margin Requirement)**

For examples of computation of day-end Margin, please refer to the Initial Margin Calculation Guide.

### **10.10A.5 Intra-day Margin**

In addition to day-end Margin which is collected from Participants on a daily basis, HKSCC has full discretion to call for intra-day Margin on CNS stock positions from all or any Participants. HKSCC may call for and collect intra-day Margin on CNS stock positions under any of the following circumstances:

- (i) if, in the opinion of HKSCC, sudden fluctuations of the securities market operated by the Exchange are apparent;
- (ii) where some of the markets, which in the opinion of HKSCC are major markets, remain open when the securities market operated by the Exchange is closed for more than one calendar day, excluding Saturday and Sunday, due to public holidays; or
- (iii) where HKSCC considers it appropriate under any other circumstances.

For examples of computation of intra-day Margin, please refer to the Initial Margin Calculation Guide. If a Participant is unable to meet its intra-day Margin payment by the

prescribed deadline for any reason, the Participant will be subject to such action which HKSCC may take under the Rules.

#### **10.10A.5A Margin Add-Ons**

HKSCC may apply Margin add-ons to Clearing Participants to monitor and control the risk exposure of HKSCC. The application of such Margin add-ons by HKSCC will be at the discretion of HKSCC and subject to such conditions and limits as HKSCC may from time to time specify.

For Margin add-ons application and computation, please refer to the Initial Margin Calculation Guide.

#### **10.10A.6 [Repealed]**

#### **10.10A.7 Interest on Margin collected**

HKSCC may allow or charge, at its absolute discretion, to Participants interest on the Margin collected in cash, calculated at a rate determined by HKSCC from time to time for each CCMS House Collateral Account allocated to Participants. HKSCC reserves the right to deduct any administrative costs from any interests to be allowed or to charge such administrative costs to the Margin collected in cash.

Unless otherwise specified by HKSCC, interest to be allowed or charged on Margin provided in cash, if any, will be accrued daily and paid (after deduction of the administrative costs, if applicable) or charged (together with the administrative costs, if applicable) monthly by HKSCC to each Participant in the same currency as the cash on which the interest accrued, by crediting or debiting, as the case may be, the CCMS House Collateral Account allocated to the Participant, or in the case of a Clearing Agency Participant which is a China Connect Clearing House, to such Clearing Agency Participant in respect of the relevant Special Participant on the first Business Day of the following month.

#### **10.10A.8 Collection of Margin**

Margin to be requested from a Participant on each Business Day will be collateralized against the value (or Discounted Market Value, if applicable) of the General Collateral Inventory in the CCMS House Collateral Account of the Participant. For details of the collateralization process, reference should be made to Section 10.15.3.

##### **(i) Clearing Participants**

If there is any shortfall in Margin after the collateralization process, HKSCC will collect the shortfall in Hong Kong dollar unless the Clearing Participant has maintained a Preferred Single Settlement Currency which is not Hong Kong dollar. Where the Clearing Participant has maintained a Preferred Single Settlement Currency which is not Hong Kong dollar, HKSCC will convert the shortfall in Hong Kong dollar to the Preferred Single Settlement Currency at such exchange rate and subject to such haircut rate as determined by HKSCC from time to time, and HKSCC will collect the shortfall in Margin in the Preferred Single Settlement Currency. Notwithstanding the foregoing, HKSCC reserves the right to collect the shortfall in Margin required in any Eligible Currency.

##### **(ii) Clearing Agency Participants**

In respect of CNS stock positions arising from Exchange Trades executed by each designated Special Participant of a Clearing Agency Participant, HKSCC will convert the Margin to Renminbi at such exchange rate and subject to such haircut rate as determined by HKSCC from time to time. Unless HKSCC otherwise agrees, the Clearing Agency Participant shall

pay Margin to HKSCC in Renminbi. Notwithstanding the foregoing, HKSCC reserves the right to collect the required amount of Margin in any Eligible Currency. Unless otherwise agreed by HKSCC, any shortfall in day-end Margin required, as determined by HKSCC, from a Clearing Agency Participant in respect of a designated Special Participant will be debited to the Miscellaneous Account allocated to the Clearing Agency Participant in respect of the designated Special Participant and will be collected from the Clearing Agency Participant on the Business Day following T-day by issuing DDIs for same day settlement to the Designated Bank of the Clearing Agency Participant as part of the CCASS money settlement process, or in any other manner determined by HKSCC from time to time. In general, any surplus cash collateral over Margin in the CCMS House Collateral Account allocated to a Clearing Agency Participant in respect of a designated Special Participant will be automatically redelivered to the Clearing Agency Participant in respect of such designated Special Participant on the Business Day following T-day by HKSCC issuing DCIs for same day settlement to the Designated Bank of the Clearing Agency Participant as part of the CCASS money settlement process, or in any other manner determined by HKSCC from time to time. Notwithstanding the foregoing, HKSCC reserves the right not to redeliver surplus cash collateral at any time it considers appropriate.

Unless otherwise agreed by HKSCC, any shortfall in Margin required, as determined by HKSCC, will be debited to the Marks and Margin Account of a Clearing Participant and will be collected from the Clearing Participant. Day-end Margin will be collected from the Clearing Participant on a daily basis by HKSCC by issuing DDIs to the Designated Bank of the Clearing Participant as part of the CCASS money settlement process, or in any other manner determined by HKSCC from time to time. Intra-day Margin demanded by HKSCC pursuant to Section 10.10A.5 will be collected by HKSCC via CPIs or by issuing DDIs to the Designated Bank of the Clearing Participant as part of the CCASS money settlement process, or in any other manner determined by HKSCC from time to time. Subject to the determination of HKSCC, any surplus cash collateral over Margin in the CCMS House Collateral Account will not be automatically redelivered at the end of the day and HKSCC reserves the right to redeliver surplus cash collateral at any time it considers appropriate. HKSCC may redeliver such surplus to the Clearing Participant upon redelivery instruction from the Clearing Participant given to HKSCC in such form prescribed by HKSCC, and the redelivery will be made in such manner and at such time as prescribed by HKSCC from time to time.

## **10.11 RISK MANAGEMENT: COLLATERAL**

### **10.11.1 Purpose of Collateral**

HKSCC monitors its risk exposure to Participants on a continuous basis. From time to time, circumstances peculiar to a particular Participant may warrant HKSCC taking additional risk management measures against it.

For example, a Participant's financial well-being may be in question. Similarly, the trading pattern of a Participant may in HKSCC's view create excessive risks.

In appropriate cases, HKSCC will require a Participant to provide it with Collateral. HKSCC may collect Collateral based on HKSCC's assessment of its exposure on the risks arising out of Market Contracts and defects affecting the Eligible Securities of a Participant.

The provisions of this Section 10.11 shall also be applicable, in so far as they are relevant to the risk management measures detailed in Section 12.2.9(ii) in respect of Clearing Agency Transactions.

### **10.11.2 Form of Collateral**

Normally, HKSCC will require Participants to provide Collateral in the form of cash or

Collateral Securities, subject to the Rules.

### 10.11.3 Amount of Collateral

The amount of Collateral required to be provided by a Participant will be decided by HKSCC, taking into account HKSCC's exposure posed by the Participant.

Unless otherwise agreed by HKSCC, a Clearing Agency Participant which is a China Connect Clearing House is required to provide such amount of Eligible Securities as shall represent the short CNS stock positions in Exchange Trades executed by each of its designated Special Participants in such Eligible Securities to HKSCC as Collateral Security in such manner as may be considered appropriate by HKSCC pursuant to Rule 3602.

HKSCC shall be entitled from time to time to require a Clearing Agency Participant which is a China Connect Clearing House to provide on demand Collateral in such form, to such extent and in such manner as is determined by HKSCC to cover any shortfall in respect of the CNS positions arising from Exchange Trades executed by each of its designated Special Participants in the event that its Marks, Margin and Collateral Securities held in HKSCC are insufficient to cover its stressed default loss determined by HKSCC from time to time in light of market conditions and such other factors as HKSCC may consider appropriate. Unless otherwise agreed by HKSCC, the required Collateral will be collected from the Clearing Agency Participant which is a China Connect Clearing House on the Business Day following T-day by issuing DDIs for same day settlement to the Designated Bank of the Clearing Agency Participant which is China Connect Clearing House as part of the CCASS money settlement process, or in any other manner determined by HKSCC from time to time.

#### 10.11.3A [Repealed]

#### 10.11.3B [Repealed]

### 10.11.3C Guarantee Fund Risk Collateral

HKSCC may require a Clearing Participant to provide from time to time on demand Guarantee Fund Risk Collateral if, when assessed by reference to the historical data from each of the realized stressed market conditions and/or hypothetical data for each of the unrealized stressed market conditions as HKSCC may determine:

- (i) the stressed default loss, determined by HKSCC from time to time in light of market conditions and such other factors as HKSCC may consider appropriate (less Margin and Collateral, each as may be specified by HKSCC from time to time in the Stress Test Value Calculation Guide and collected by HKSCC), arising from all the CNS stock positions of the Clearing Participant ("Guarantee Fund Expected Uncollateralised Loss") exceeds the Guarantee Fund Risk Predefined Limit; and
- (ii) the prevailing Guarantee Fund size is equal to the Guarantee Fund Threshold.

Clearing Participants may refer to the Stress Test Value Calculation Guide for examples of the calculation of stressed default loss.

The amount of Guarantee Fund Risk Collateral required from the Clearing Participant is:

$$\text{Guarantee Fund Expected Uncollateralised Loss} - \text{Guarantee Fund Risk Predefined Limit}$$

For the avoidance of doubt, if Guarantee Fund Risk Collateral is required under two or more stressed market conditions, the higher or highest (as the case may be) Guarantee Fund Risk Collateral amount shall be imposed.

Notwithstanding the above requirements of this Section, should HKSCC accept the Clearing Participant's request to waive the whole or part of the Guarantee Fund Risk Collateral requirement, the Clearing Participant must close out such positions as may reduce the Guarantee Fund Expected Uncollateralised Loss to an amount which is less than the sum of the Guarantee Fund Risk Predefined Limit and Guarantee Fund Risk Collateral maintained by HKSCC (if any) by the end of the same Business Day as the Guarantee Fund Risk Collateral requirement collection due date, failing which HKSCC may subsequently close out such positions on behalf of the Clearing Participant. For the avoidance of doubt, any Guarantee Fund Risk Collateral provided by a Clearing Participant shall form part of such Clearing Participant's Collateral pursuant to Rule 3602 and shall not be regarded as resources of the Guarantee Fund.

#### **10.11.3D Example (Computation of Guarantee Fund Risk Collateral)**

Suppose: Guarantee Fund Threshold = HK\$320M  
 Guarantee Fund Risk Predefined Limit = HK\$160M

		HK\$ million
Guarantee Fund size	=	320
Guarantee Fund Expected Uncollateralised Loss	=	180

The Guarantee Fund size is equal to the Guarantee Fund Threshold and the Guarantee Fund Expected Uncollateralised Loss exceeds the Guarantee Fund Risk Predefined Limit.

The amount of Guarantee Fund Risk Collateral required from the Clearing Participant  
 = HK\$180 million – HK\$160 million  
 = HK\$20 million.

#### **10.11.4 Notification by HKSCC**

Except for Collateral demanded from a Clearing Agency Participant which is a China Connect Clearing House the collection of which is described in Section 10.11.3, and except for Collateral calculated by reference to a Participant's apportioned liquid capital the collection of which will be by issuing DDIs to the Designated Bank of the Participant as part of the CCASS Hong Kong dollar money settlement process or in any other manner or Eligible Currency determined by HKSCC from time to time, HKSCC will notify a Participant in writing of the amount of any other Collateral required and the Participant will have to provide the Collateral within the time period specified.

#### **10.11.5 Return or Redelivery of Collateral**

Collateral provided by Participants will be returned or redelivered to them by HKSCC in such manner and at such time as is considered appropriate by HKSCC.

#### **10.11.6 Interest on Collateral**

HKSCC may allow or charge, at its absolute discretion, to Participants interest on Collateral provided by Participants in cash calculated at a rate determined by HKSCC from time to time for each CCMS House Collateral Account allocated to Participants. HKSCC reserves the right to deduct any administrative costs from any interest to be allowed or to charge such administrative cost to the Collateral provided in cash.

Unless otherwise specified by HKSCC, interest to be allowed or charged on Collateral provided in cash, if any, will be accrued daily and paid (after deduction of the administrative costs, if applicable, and net of any Withholding Tax (whether withheld by HKSCC or any other parties) or charged (together with the administrative costs, if applicable) monthly, by HKSCC to each Participant in the same currency as the cash on which the interest accrued, by crediting or debiting, as the case may be, the CCMS House

Collateral Account allocated to the Participant, or in the case of a Clearing Agency Participant which is a China Connect Clearing House, to such Clearing Agency Participant in respect of the relevant Special Participant on the first Business Day of the following month.

Without prejudice to the above, to the extent required by the Tax Information Exchange Framework, HKSCC shall be entitled to deduct or withhold Withholding Tax (whether withheld by HKSCC or any other parties) from any payment of interest allowed on Collateral to a Participant (or from any other payment made by HKSCC to a Participant) and shall have no obligation to gross-up any such payment or to pay any additional amount as a result of such Withholding Tax.

## **10.12 RISK MANAGEMENT: SECURITIES-ON-HOLD**

### **10.12.1 Purpose of Securities-on-hold**

On each Settlement Day, HKSCC will, in respect of Eligible Securities made available to it by Participants with short stock positions under the CNS System, allocate such Eligible Securities to the Stock Clearing Accounts of those Participants with long stock positions under the CNS System.

Since under the current design of the CCASS money settlement process, payment by Participants to HKSCC via their Designated Banks (as part of CCASS money settlement process) will only be confirmed good and irrevocable at day end after the Eligible Securities have been delivered to Participants under the CNS System in CCASS, HKSCC faces significant risk exposure from the time of delivery of Eligible Securities in CCASS to the time when confirmation of good and irrevocable payment is issued by the Designated Banks of Participants and the receiving bank of HKSCC.

To guard against this risk exposure, the Rules provide that until such time as HKSCC is satisfied that (i) it has received payment in full in respect of Eligible Securities delivered by HKSCC to a Participant under the CNS System on a Settlement Day; and (ii) such payment is good and irrevocable, or unless otherwise agreed by HKSCC, title and property in such Eligible Securities shall not pass to the Participant. Until then, Participants will not be allowed to use or withdraw some or all of such Eligible Securities, except as permitted by HKSCC.

The provisions of this Section 10.12 shall, in the case of a Clearing Agency Participant which is a China Connect Clearing House, apply separately to the Stock Clearing Account and Money Ledger allocated to such Participant in respect of each designated Special Participant, and references to the Stock Clearing Account or Money Ledger of a Participant in this Section 10.12 shall be construed accordingly for such Clearing Agency Participant.

The provisions of this Section 10.12 shall also be applicable, in so far as they are relevant, to the risk management measures detailed in Section 12.2.9(iii) in respect of Clearing Agency Transactions.

### **10.12.2 Quantity of Eligible Securities allocated which can be used**

The quantity of Eligible Securities allocated to the Stock Clearing Account of a Participant under the CNS System on a Settlement Day which will not be allowed to be used or withdrawn by the Participant, will depend on the amount to be paid by the Participant to HKSCC under the CNS System on that day.

If a Participant wishes to make use of any of such Eligible Securities in its Stock Clearing Account before payment of the amount owed to HKSCC is confirmed good and irrevocable, as long as the value of such Eligible Securities (in Hong Kong dollars or its Hong Kong

dollar equivalent converted at the exchange rate determined by HKSCC) which are to remain in the Stock Clearing Account of the Participant (determined by using the Mark-to-market values of the relevant Eligible Securities at the time), discounted by a percentage to be decided by HKSCC (normally ten per cent), is not less than the total amount owed to HKSCC (in Hong Kong dollars or its Hong Kong dollar equivalent converted at the exchange rate determined by HKSCC), the Participant will be allowed by HKSCC to make use of the Eligible Securities. For the purpose of calculating the total amount owed by a Participant to HKSCC, sums so owed and denominated in one Eligible Currency shall not be reduced by sums owed to that Participant by HKSCC which are denominated in any other Eligible Currency.

When payment of the total amount owed to HKSCC is confirmed good and irrevocable, all Eligible Securities allocated under the CNS System to the Stock Clearing Account of a Participant will become available for use by it.

### **10.12.3 [Repealed]**

### **10.12.4 Participants may effect cash prepayment**

Participants that have outstanding payment obligations to HKSCC but wish to utilize any or all of the Securities-on-hold covering such outstanding payment obligations for any purpose, including to settle ISI/SI Transactions and Isolated Trades, if applicable, during a Settlement Day, may pay same day available funds in the relevant Eligible Currency to HKSCC to reduce their monetary obligations and to have the equivalent discounted market value of Securities-on-hold released.

A Participant may pay same day available funds to HKSCC by inputting Cash Prepayment Instructions on each Settlement Day or by inputting a Cash Prepayment Standing Instruction via the “Cash Prepayment / TSF Payment Standing Instruction” maintenance functions to authorize HKSCC to generate recurring Cash Prepayment Instructions on behalf of the Participant on each Settlement Day. The cash prepayment amount that will be generated under a Cash Prepayment Standing Instruction will depend on the payment basis of the standing instruction given by the Participant, and will be either (a) the gross amount of the unsettled money obligations on its long CNS stock positions; or (b) the net amount of the unsettled money obligations on its long and short CNS stock positions, plus a certain percentage of the net amount input by the Participant. Where the Participant has selected “CHATS” as the payment method when creating the Cash Prepayment Standing Instruction, the cash prepayment amount will be generated as aforesaid on a Settlement Day will be reduced by the relevant amount of Specific Cash Collateral, as described in Section 10.12.4A.

Any Cash Prepayment Standing Instruction remaining in the “pending status” ten calendar days after its last updated date will be automatically purged from CCASS.

#### **10.12.4A Use of Specific Cash Collateral to reduce cash prepayment amount**

This Section 10.12.4A is applicable where a Cash Prepayment Standing Instruction to release Securities-on-hold has been created and authorized by a Participant, with “CHATS” set as the payment method.

In respect of the generation of Cash Prepayment Instruction by HKSCC under the Cash Prepayment Standing Instruction on a Settlement Day, HKSCC will reduce the cash prepayment amount by the relevant amount of Specific Cash Collateral that the Participant has provided to HKSCC to cover long CNS stock positions due for settlement on that Settlement Day.



When Eligible Security is allocated to the Stock Clearing Account of the Participant in respect of the long CNS stock position covered by the Specific Cash Collateral, and in any event upon completion of the third Batch-settlement-run on that Settlement Day, HKSCC will update the Settlement Account of the Participant's Money Ledger with the amount of the Specific Cash Collateral to reduce the corresponding monetary obligations due to HKSCC. As a result, HKSCC will release equivalent discounted market value of the Securities-on-hold.

#### 10.12.5 Procedures

The following is a brief description of the procedures relating to cash prepayment on each Settlement Day:

- (a) Cash Prepayment Instructions with "CHATS" set as the payment method
  - (i) Participants that wish to make prepayments by means of CPIs shall select "CHATS" as the payment method when creating a Cash Prepayment Instruction via a CCASS Terminal from 8:00 a.m. to 2:00 p.m. or such other time specified by HKSCC from time to time or when creating a Cash Prepayment Standing Instruction via a CCASS Terminal from 8:00 a.m. to 7:00 p.m. or such other time specified by HKSCC from time to time;
  - (ii) To avoid undue concentration of HKSCC's exposure to a bank appointed by HKSCC as receiving bank for cash payment, cash prepayment is subject to the concentration limit predetermined by HKSCC in respect of an appointed receiving bank. HKSCC will only accept or generate Cash Prepayment Instructions within the predetermined concentration limit of the receiving bank. In case a Cash Prepayment Standing Instruction is created and authorized by a Participant, Cash Prepayment Instructions will be generated by HKSCC, if applicable, at approximately 8:00 a.m. starting from the following Settlement Day. The cash prepayment amount under the Cash Prepayment Instruction generated by HKSCC may be reduced in the manner as described in Section 10.12.4A;
  - (iii) Upon the creation and authorization of Cash Prepayment Instructions by Participants or the generation of Cash Prepayment Instructions by HKSCC pursuant to Cash Prepayment Standing Instructions, CPIs will be generated to collect the cash prepayments from their Designated Bank Accounts. The CPIs information will be included in the Electronic CHATS Payment Instruction Report (CSEPI03). Based on the report, Designated Banks will issue CPIs to the Clearing House of HKAB to make payment on their behalf. Participants must ensure that there are sufficient funds in their Designated Bank Accounts and that the CHATS payments are completed by their Designated Banks no later than 3:30 p.m. or such other time as may be prescribed by HKSCC from time to time;
  - (iv) Upon being notified by the Clearing House of HKAB of the finality of such payment, HKSCC will update the Settlement Accounts of Participants' Money Ledgers to reduce their corresponding monetary obligations due to HKSCC and as a result, release equivalent discounted market value of Securities-on-hold (see Section 10.12.6). Participants' Statements of Money Ledger will show the relevant entries. Participants can check the status of a CPI via the "Enquire Payment Instruction" function of CCASS. For the status of a Cash Prepayment Instruction, Participants can make use of the "Enquire Cash Prepayment Instruction" function;

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- (v) Participants can operate ATIs to check whether the Securities-on-hold have been released and rely on DIs or batch-settlement-runs to settle SI Transactions, ISI Transactions and Isolated Trades;
  - (vi) Since HKSCC allocates shares according to a pre-set algorithm, Participants making prepayments may still not get all the allocated shares. Any surplus funds thus arising will be returned to the Participants not later than day end. Please refer further to Section 14.4.2;
  - (vii) In case the relevant cash payment under a Cash Prepayment Instruction input or generated on a Business Day is not received by HKSCC, the Cash Prepayment Instruction will be purged from CCASS at the end of the Business Day.
- (b) Cash Prepayment Instructions with “OTHERS” set as the payment method
- (i) Participants that wish to make prepayments by other means must indicate “OTHERS” as the payment method when creating a Cash Prepayment Instruction via a CCASS Terminal from 8:00 a.m. to 2:30 p.m. or such other time specified by HKSCC from time to time or when creating a Cash Prepayment Standing Instruction via a CCASS Terminal from 8:00 a.m. to 7:00 p.m. or such other time specified by HKSCC from time to time;
  - (ii) To avoid undue concentration of HKSCC's exposure to a bank appointed by HKSCC as receiving bank for cash payment, cash prepayment is subject to the concentration limit predetermined by HKSCC in respect of each appointed receiving bank. HKSCC will only accept or generate Cash Prepayment Instructions within the predetermined concentration limit of the receiving bank. In case a Cash Prepayment Standing Instruction is created and authorized by a Participant, Cash Prepayment Instructions will be generated by HKSCC, if applicable, at approximately 8:00 a.m. starting from the following Settlement Day;
  - (iii) Participants must ensure that same day available funds are transferred to HKSCC's specified bank account no later than 2:45 p.m. or such other time prescribed by HKSCC from time to time. For Participants using the same bank as the appointed receiving bank of HKSCC, they can make use of the internal account transfer function of the bank (see CCASS Terminal User Guide for Participants for details) or its electronic banking system to transmit available funds. For others, they can instruct their banks to make payment to HKSCC via inter-bank transfer with CHATS payment (see CCASS Terminal User Guide for Participants for details);
  - (iv) Based on the details of Cash Prepayment Instructions, HKSCC will follow up the funds with its appointed receiving bank and the relevant Participants. Only when available funds in the relevant Eligible Currency are confirmed will HKSCC update Participants' Settlement Accounts of Money Ledger to reduce their corresponding monetary obligations due to HKSCC and as a result, release equivalent discounted market value of Securities-on-hold (see Section 10.12.6). Participants' Statements of Money Ledger will show the relevant entries. Participants can check the status of a Cash Prepayment Instruction via the CCASS enquiry function of "Enquire Cash Prepayment Instruction";
  - (v) Participants can operate ATIs to check whether the Securities-on-hold have been released and rely on DIs or batch-settlement-runs to settle SI Transactions, ISI Transactions and Isolated Trades;

- (vi) Since HKSCC allocates shares according to a pre-set algorithm, Participants making prepayments may still not get all allocated shares. Any surplus funds thus arising will be returned to the Participants not later than day end. Please refer further to Section 14.4.2;
- (vii) Acceptance of the prepayment requests will be at HKSCC's full discretion. If Participants fail to follow the procedures, and/or for any other reason the requests are subsequently turned down by HKSCC, then the funds received will only be refunded the following Business Day without interest;
- (viii) In the event of default of payment (e.g., for any transfers subsequently reversed by the Clearing House of HKAB), HKSCC shall have recourse against the relevant Participant;
- (ix) In case cash remittance is made by a Participant to HKSCC as cash prepayment not pursuant to any Cash Prepayment Instruction, HKSCC reserves the right not to effect the updating of the Participant's Money Ledger on the same day. Such cash payment will be refunded without interest to the Participant by crediting the cash payment amount to its Money Ledger on the next Business Day; and
- (x) In case the relevant cash payment under a Cash Prepayment Instruction input or generated on a Business Day is not received by HKSCC, the Cash Prepayment Instruction will be purged from CCASS at the end of the Business Day.

#### 10.12.6 Example (Quantity of Eligible Securities which can be used)

On a Settlement Day, Participant A was allocated 4,000 of Stock X (denominated in HKD) and 3,000 of Stock Y (denominated in HKD) and has HK\$80,000 due to HKSCC. Participant A has provided to HKSCC cash prepayment of HK\$30,000. The prevailing Mark-to-market price for Stock X is HK\$10 and for Stock Y is HK\$20.

Then :

- (i) Mark-to-market value of Eligible Securities allocated to Participant A
  - = HK\$10 X 4,000 (stock X) + HK\$20 X 3,000 (stock Y)
  - = HK\$100,000
- (ii) Discounted market value of such allocated Eligible Securities
  - = HK\$100,000 X (1 - 0.1)
  - = HK\$90,000
- (iii) Discounted market value of allocated Eligible Securities which could be withdrawn
  - = Discounted market value of allocated Eligible Securities - Amount due to HKSCC not covered by cash prepayment
  - = HK\$90,000 - (HK\$80,000 - HK\$30,000)
  - = HK\$40,000

Participant A will be allowed by HKSCC to use allocated Eligible Securities with a total discounted market value of not more than HK\$40,000.

Participant A can therefore use no more than either : -

- (i) 4,444 of Stock X (derived from  $\text{HK\$40,000} \div \text{HK\$10} \div (1-0.1)$ ); or

- (ii) 2,222 of Stock Y (derived from  $\text{HK\$}40,000 \div \text{HK\$}20 \div (1-0.1)$ ); or
- (iii) a combination of Stock X and Stock Y so long as their total discounted market value does not exceed HK\$40,000.

The amount of Stock X and Stock Y which must be retained in the Stock Clearing Account of Participant A will be treated by HKSCC as Securities-on-hold.

#### **10.12.7 Participants may request intra-day refund of overpaid cash prepayment**

Participants that have overpaid cash prepayment to HKSCC to cover outstanding payment obligations may request HKSCC to effect intra-day refund to the Participants of any surplus cash arising from such overpaid cash prepayment on each Settlement Day by inputting Intra-day Payment Standing Instruction via the “Intra-day Payment Standing Instruction” maintenance functions. HKSCC will determine the amount of surplus cash arising from the overpaid cash prepayment and generate Intra-day Payment Instructions to refund any surplus cash (if any) to the Participants intra-day in accordance with Section 10.12.8.

#### **10.12.8 Procedures**

The following is a brief description of the procedures relating to intra-day refund of surplus cash arising from overpaid cash prepayment on a Settlement Day:

- (a) Participants that wish to request HKSCC to effect intra-day refund to the Participants of surplus cash arising from overpaid cash prepayment on each Settlement Day shall input Intra-day Payment Standing Instructions via the “Intra-day Payment Standing Instruction” maintenance functions to instruct HKSCC to issue Intra-day Payment Instructions covering such surplus cash on each Settlement Day. Acceptance of such Intra-day Payment Standing Instructions by HKSCC will be at the discretion of HKSCC and subject to the requirements as HKSCC may from time to time specify. Where the Intra-day Payment Standing Instruction of a Participant also covers intra-day payment to the Participant of cash payments arising out of nominee services on each Business Day and/or intra-day settlement of money obligations due to the Participant from HKSCC under the CNS System on each Settlement Day, the amount of Intra-day Payment in this Section 10.12.8 on a Settlement Day shall include the amount of cash payments arising out of nominee services, as referred to in and determined by HKSCC under Section 8.25.2 and/or the intra-day settlement amount of money obligations due to the Participant from HKSCC under the CNS System, as referred to in and determined by HKSCC under Section 10.5.8;
- (b) Participants shall define a pre-set threshold in their Intra-day Payment Standing Instructions. No Intra-day Payment Instruction will be issued by HKSCC to a Participant on a Settlement Day and/or a Business Day if the total amount of Intra-day Payment as determined by HKSCC to be paid to the Participant on that day via IPI is smaller than its pre-set threshold;
- (c) in case an Intra-day Payment Standing Instruction covering surplus cash arising from overpaid cash prepayment is accepted by HKSCC on a Business Day at or before 1:15 p.m., an Intra-day Payment Instruction will be issued starting from that day if applicable. Otherwise, the Intra-day Payment Instruction will only be issued from the next Settlement Day/Business Day;
- (d) following the acceptance by HKSCC of an Intra-day Payment Standing Instruction to effect intra-day refund of surplus cash arising from overpaid cash prepayment to the Participant, HKSCC will normally determine the amount of surplus cash arising from overpaid cash prepayment to be included in the Intra-day Payment upon completion

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- of the third Batch-settlement-run shortly after 2:00 p.m. on each Settlement Day, or such other time as specified by HKSCC from time to time;
- (e) in determining the amount of surplus cash arising from cash prepayment to be refunded intra-day, HKSCC will consider:
    - (i) the total cash prepayments received, confirmed and updated to the Participant's Settlement Account of Money Ledger at or before 1:15 p.m. on the Settlement Day or such other time as specified by HKSCC from time to time;
    - (ii) the Margin amount updated to the Settlement Account of Participant's Money Ledger around 10:00 a.m. on the Settlement Day;
    - (iii) the amount of Specific Cash Collateral updated to the Settlement Account of Participant's Money Ledger on the Settlement Day upon the completion of the third Batch-settlement-run;
    - (iv) the CNS money obligations upon the completion of the third Batch-settlement-run and any immediate settlement before 2:00 p.m. by DIs; and
    - (v) other types of money obligations in the Participant's Settlement Account and Miscellaneous Account of Money Ledger as HKSCC may from time to time specify;
  - (f) if the total amount of Intra-day Payment of the Participant including the amount of surplus cash arising from overpaid cash prepayment determined by HKSCC under Section 10.12.8(e) is equal to or greater than the pre-set threshold defined by the Participant, an Intra-day Payment Instruction will be issued by HKSCC;
  - (g) HKSCC will issue Intra-day Payment Instructions to the Designated Banks of Participants on a Settlement Day or Business Day at around 2:30 p.m., or such other time as specified by HKSCC from time to time, to cause credits to be made to the Designated Bank Accounts of Participants;
  - (h) Participants that have input Intra-day Payment Standing Instructions may enquire the estimated amount of surplus cash arising from overpaid cash prepayment to be refunded before 2:30 p.m. on a Settlement Day via the "Enquire Intra-day Payment Summary" function in CCASS Terminal. Details of Intra-day Payment Instructions issued by HKSCC including the amount of the Intra-day Payment will be available for enquiry after 2:30 p.m. on a Settlement Day via the "Enquire Intra-day Payment Summary" function in CCASS Terminal;
  - (i) irrespective of whether an Intra-day Payment Standing Instruction is accepted by HKSCC under Section 10.12.8(c), whether to allow an intra-day refund to Participants of any surplus cash arising from overpaid cash prepayment will be at the full discretion of HKSCC. If (a) a Participant fails to follow the specified procedures; (b) its Intra-day Payment Standing Instruction is subsequently turned down by HKSCC for any other reason; or (c) any surplus cash arising from overpaid cash prepayment is not refunded intra-day to the Participant for any reason, HKSCC shall have full discretion to make use of such surplus cash for any purpose it deems appropriate, including but not limited to applying it for the intra-day settlement of money obligations due to other Participants from HKSCC under the CNS System. Where HKSCC does not allow intra-day refund, any surplus cash arising from overpaid cash prepayment on a Settlement Day will only be returned to the Participant not later than day end via DCI.

### **10.13 RISK MANAGEMENT: EVIDENCE OF SECURITIES AVAILABLE FOR SETTLEMENT**

In relation to Exchange Trades in Eligible Securities which are subject to expiry (e.g. warrants) or which HKSCC considers as high risk securities and which are to be settled under the CNS System, the delivering Participants must ensure that when they or in the case of GCPs, including their NCPs, place a selling order they have readily available evidence showing that, on or before the due date for settlement of the Market Contracts, they or in the case of GCPs, including their NCPs, have or will have the required quantity of Eligible Securities in their stock accounts in CCASS for settlement of the Market Contracts. The delivering Participants shall provide the evidence to HKSCC upon request.

If at any time HKSCC is not satisfied that a delivering Participant has or will have the Eligible Securities on the due date for settlement of the Market Contract, HKSCC may direct that Participant to arrange or may on behalf of that Participant execute immediately a Buy-in on or off the Exchange to purchase the Eligible Securities required by that Participant to settle its obligations in respect of that Market Contract. If a Buy-in is unable to be effected, HKSCC may require additional cash Collateral to be provided by a Participant in such amount as HKSCC considers appropriate.

The provisions of this Section 10.13 shall also be applicable, in so far as they are relevant to the risk management measures detailed in Section 12.2.9(iv) in respect of Clearing Agency Transactions.

### **10.14 RISK MANAGEMENT: CLOSING-OUT**

#### **10.14.1 Purpose of Closing-out**

Under Rule 3607, in the occurrence of an Event of Default of a Participant, HKSCC may Close-out any or all unsettled obligations of that Participant under the CNS System (whether or not due for settlement).

The two main purposes of Closing-out are (i) to enable HKSCC to crystalize its exposure to a Participant in default and (ii) to enable HKSCC to meet its obligations under the CNS System to other Participants. The end result of Closing-out of all unsettled positions of a Participant under the CNS System is that all obligations to deliver or receive Eligible Securities will be replaced by sums payable and a net sum will become payable by or to the defaulting Participant. This Section is only concerned with the mechanics of Closing-out.

The provisions of this Section 10.14 shall also be applicable, in so far as they are relevant to the risk management measures detailed in Section 12.2.9(v) in respect of Clearing Agency Transactions.

#### **10.14.2 Procedures**

In brief, Closing-out of an unsettled stock position of a Participant under the CNS System involves HKSCC entering into, on behalf of the defaulting Participant, an opposite transaction to offset the unsettled stock position, resulting in a sum payable by or to the Participant (the money position of the unsettled stock position will be offset against the money position of the opposite transaction as a result of Closing-out).

In relation to unsettled stock positions of a defaulting Participant under the CNS System, HKSCC will instruct one or more of its authorized brokers to Close-out such positions by entering into relevant transactions on or off the Exchange. The costs and expenses of the Closing-out transactions will be borne by the defaulting Participant.

#### **10.14.3 Example (Closing-out)**

Participant A has defaulted in making payment to HKSCC and is declared a defaulter by HKSCC. At the time, Participant A has the following unsettled stock positions under the CNS System.

Stock	Quantity	Money position
Stock X	1,000 (long)	HK\$5,000DR
Stock Y	2,000 (short)	HK\$8,000CR
Stock Z	3,000 (long)	HK\$9,000DR

On behalf of Participant A, HKSCC instructs its authorized broker to enter into the following Closing-out transactions at the best prevailing market price.

Stock	Quantity	Money position	Money position after offsetting
Stock X	Sell 1,000	HK\$5,500 CR	HK\$500 CR
Stock Y	Buy 2,000	HK\$9,000 DR	HK\$1,000 DR
Stock Z	Sell 3,000	HK\$9,200 CR	HK\$200 CR
			-----
			<u>HK\$300 DR</u>

Assuming HK\$500 was spent as the costs and expenses of effecting the Closing-out transactions, Participant A would be obliged to pay HK\$500+HK\$300 = HK\$800 to HKSCC.

#### 10.14.4 Default by Participants

On the occurrence of an Event of Default against a Participant, HKSCC may declare the Participant a defaulter and if so, will effect Closing-out in respect of all of the unsettled obligations of the Participant under the CNS System.

If, as a result of Closing-out, the Participant owes money to HKSCC, HKSCC will apply the Marks, Margin, Collateral, Mainland Settlement Deposit, Mainland Security Deposit and Charged Property provided by the Participant (as well as all other assets and property which may be applied by HKSCC for such purpose) towards such indebtedness.

If a Participant which is an Exchange Participant is declared a defaulter, HKSCC will notify the Exchange forthwith and request the Exchange to suspend the Participant from trading. HKSCC will also request the Exchange to suspend from trading any NCP of the GCP or any Special Participant of the Clearing Agency Participant which does not have in place immediately upon suspension of the GCP or Clearing Agency Participant a valid, binding and effective Clearing Agreement with another GCP or Clearing Agency Participant, as the case may be. If a Participant which is not an Exchange Participant or Special Participant is declared a defaulter, HKSCC will request the Exchange to suspend from trading any NCP of the GCP or any Special Participant of the Clearing Agency Participant which does not have in place immediately upon suspension of the GCP or Clearing Agency Participant a valid, binding and effective Clearing Agreement with another GCP or Clearing Agency Participant, as the case may be.

A Participant declared a defaulter will also be suspended from further activities in CCASS.

### 10.15 RISK MANAGEMENT: CASH AND COLLATERAL SECURITIES

#### 10.15.1 Cash

Cash in Hong Kong dollar and other currencies recorded as credit entries in any CCMS Collateral Account of the Participant are amounts paid by the Participant to HKSCC. The only obligation of HKSCC to the Participant in respect of such amounts shall be to pay the Participant an amount equal to the balance remaining after satisfaction of all obligations and liabilities (actual or contingent) of such Participant to HKSCC.

### **Security**

HKSCC shall have a first fixed charge over:-

- (a) the Collateral Securities from time to time credited to any CCMS Collateral Account of the Participant; and
- (b) the Derived Assets

by way of a continuing security (i) for the discharge and satisfaction of any Marks, Margin and Collateral obligations of such Participant, (ii) for the discharge and satisfaction of all other obligations and liabilities (actual or contingent) of such Participant to HKSCC arising directly in connection with HKSCC ensuring the settlement of Market Contracts to which such Participant is a party, (iii) for the discharge and satisfaction of all liabilities (actual or contingent) of such Participant to HKSCC arising from a loss or defects affecting Eligible Securities pursuant to Rule 812, Rule 813, Rule 814 and Rule 815, and (iv) for the discharge and satisfaction of all other obligations (actual or contingent) of such Participant to HKSCC. Each of the charges created over the assets specified in (a) and (b) and in respect of the Participant's obligations in (i), (ii), (iii) and (iv) above shall form a separate security.

Such Collateral Securities and the Derived Assets shall also be a continuing security for HKSCC's waiver of computation of Marks and reduction of Marginable Position for computation of Margin required from such Participant.

The provisions of this Section 10.15 shall also be applicable, in so far as they are relevant, to the risk management measures in respect of Clearing Agency Transactions.

### **10.15.2 Valuation of Collateral Securities, etc.**

For the purpose of the collateralization process under Section 10.15.3, the "Discounted Market Value" of a collateral, if applicable, in the CCMS House Collateral Account of a Participant, is determined as below:

Collateral Securities-

Quantity of a security x valuation price x (1 - haircut rate of the security) x exchange rate x (1 - haircut rate of the relevant currency)

Cash in an Eligible Currency other than Hong Kong dollar-

Cash amount in original currency x exchange rate x (1 - haircut rate of the relevant currency)

The valuation price, exchange rates and haircut rates shall be determined by HKSCC in its absolute discretion from time to time. All Eligible Securities shall have haircut ratio and valuation price which shall be determined by HKSCC in its absolute discretion from time to time. If applicable, the "Discounted Market Value" of a collateral in Eligible Currency other than Hong Kong dollar will be converted into its Hong Kong dollar equivalent at the exchange rate and haircut rate determined by HKSCC. Participants may enquire the applicable valuation price, exchange rates and haircut rates via the CCMS.



### 10.15.3 Collateralization process

The purpose of the collateralization process is to determine the aggregate amount or value of cash recorded in, and of Collateral Securities credited to, the CCMS House Collateral Account of a Clearing Participant acceptable to HKSCC from time to time for the purpose of discharging the Clearing Participant's Marks, Margin and/or Collateral obligations, and other obligations (actual or contingent).

Unless HKSCC otherwise determines, HKSCC may accept Non-cash Collaterals to secure Marks, Margin, Collateral and other obligations of a Clearing Participant up to the amount calculated by the Non-cash Collateral Cap.

The Marks, Margin, Collateral and other obligations of a Clearing Participant on a Business Day will be collateralized against the General Collateral Inventory in the CCMS House Collateral Account of the Clearing Participant in the following order, or in such order as HKSCC considers appropriate:

- (i) Non-cash Collateral up to the amount calculated by the Non-cash Collateral Cap;
- (ii) cash in the currency in which the Marks, Margin, Collateral and other obligations (actual or contingent) is calculated and denominated; and
- (iii) cash in other currencies.

The following is a brief description of the collateralization process:

- (a) The Marks, Margin, Collateral and other obligations of the Clearing Participant will first be collateralized against the value (or Discounted Market Value, if applicable) of the Non-cash Collateral, namely the Discounted Market Value of Collateral Securities, up to the amount calculated by the Non-cash Collateral Cap. Such collateralized value of the Non-cash Collateral, up to but not exceeding the amount calculated by the Non-cash Collateral Cap, will be shown as the non-cash Ear-marked Value in the CCMS House Collateral Account of the Clearing Participant;
- (b) Any amount of the Marks, Margin, Collateral and other obligations of the Clearing Participant in excess of such non-cash Ear-marked Value will be collateralized against cash in the same currency in which the Marks, Margin, Collateral and other obligations is calculated and denominated. Unless otherwise specified by HKSCC and subject to Sections 10.10, 10.10A and 10.11, such collateralized amount of cash shall be paid out of the General Collateral Inventory in the CCMS House Collateral Account, and will be re-categorised and treated as Contract Currency Collateral;
- (c) Any remaining amount of Marks, Margin, Collateral and other obligations will then be collateralized against the Discounted Market Value of cash in other currencies. For this purpose, if the remaining amount of Marks, Margin, Collateral and other obligation is denominated in currencies other than Hong Kong dollar, it will be converted to Hong Kong dollar equivalent at such exchange rate and subject to such haircut rate as determined by HKSCC from time to time. The collateralized amount will be shown as cash Ear-marked Value in the CCMS House Collateral Account; and

Subject to the above and Sections 10.10, 10.10A and 10.11, any amount of Marks, Margin, Collateral and other obligations of the Clearing Participant remaining after the above collateralization process shall be paid by the Clearing Participant in cash in the currency in which the Marks, Margin, Collateral and other obligations are calculated save where otherwise specified by HKSCC.

### 10.15.4 Example (Marks and Margin covered by Non-cash Collateral)

On a given trade day, the Marks and Margin obligations of Participant A are HK\$10,000,000 and HK\$6,000,000 respectively. Prevailing Non-cash Collateral Cap is 40%.

Suppose at the time of collateralization, the total Discounted Market Value of the Collateral Securities in the General Collateral Inventory of the CCMS House Collateral Account of Participant A is HK\$8,000,000.

Maximum Marks and Margin amount that can be covered by Collateral Securities

$$\begin{aligned}
 &= \text{Marks and Margin obligation} \times \text{Non-cash Collateral Cap} \\
 &= (\text{HK\$10,000,000} + \text{HK\$6,000,000}) \times 40\% \\
 &= \text{HK\$6,400,000}
 \end{aligned}$$

Note: The actual Marks and Margin amount that will be covered by Collateral Securities is also HK\$6,400,000 because the total Discounted Market Value of the Collateral Securities available at the time of collateralization is more than this figure. The Ear-marked Value of Participant A is HK\$6,400,000.

$$\begin{aligned}
 &\text{Marks and Margin requirement amount that must be paid in cash} \\
 &= (\text{HK\$10,000,000} + \text{HK\$6,000,000}) - \text{HK\$6,400,000} \\
 &= \text{HK\$9,600,000}
 \end{aligned}$$

#### 10.15.5 Quantity of Collateral Securities which cannot be used

Collateral Securities credited to the CCMS House Collateral Account of a Participant may not be transferred from such account without the express consent of HKSCC, given in a manner as determined by HKSCC in its absolute discretion. Participants will not be allowed to use or withdraw Collateral Securities from the CCMS House Collateral Account except with the express consent of HKSCC, given in a manner as determined by HKSCC in its absolute discretion.

If the Participant wishes to make use of and/or withdraw from the CCMS House Collateral Account any Collateral Securities, as long as the total value (or Discounted Market Value, if applicable) of the General Collateral Inventory is greater than the Ear-marked Value of the Participant, the Participant may be allowed by HKSCC in its sole discretion to make use of and/or withdraw the Collateral Securities with value greater than the Ear-marked Value.

In the event that Eligible Securities are transferred from a Participant's Stock Accounts in CCASS to a collateral account in CCMS maintained by another Recognized Clearing House for the Participant in its capacity as a participant of such Recognized Clearing House, such Eligible Securities will have to be re-transferred to the Participant's Stock Accounts in CCASS, other than the Stock Collateral Control Account, prior to any withdrawal being made. The Recognized Clearing House may withdraw such Eligible Securities from CCASS or otherwise deal with such Eligible Securities in relation to the enforcement of its rights under any charge or security interest granted in its favour by the Participant in respect of such Eligible Securities.

#### 10.15.6 Application of moneys

Without prejudice to HKSCC's rights in Rule 3702, upon any failure by a Participant to perform its obligations to HKSCC under the CNS System or when HKSCC otherwise deems it necessary for its own protection;

- (i) HKSCC may sell or apply the Charged Property of the Participant without further reference to the Participant and the provisions of Rule 3702 shall apply equally to such sale. Following such sale or application, the only obligation of HKSCC to such

Participant in respect of its Charged Property shall be to pay such Participant an amount equal to the balance and/or to return to such Participant the balance of the Charged Property remaining after satisfaction of all obligations and liabilities (actual or contingent) of such Participant to HKSCC;

- (ii) Derived Assets credited to the Entitlement Account may not be transferred from such Account without the express consent of HKSCC and may be transferred to the Participant's CCMS Collateral Account by HKSCC; and
- (iii) all dividends, interests and other distributions in respect of the Charged Property not forming part of the Derived Assets may be retained and used by HKSCC.

All moneys arising from the exercise of the powers of sale in Rule 3608 and Rule 3702 shall be held and applied in or towards the payment or discharge of the Participant's obligations and liabilities (actual or contingent) under the Rules (but without prejudice to the right of HKSCC to recover any shortfall from the Participant).

## **10.16 RISK MANAGEMENT: CONTRACT TERMINATION**

### **10.16.1 General**

Following the occurrence of an Event of Default, if HKSCC reasonably believes that: (i) it will not be able to effect Closing-out Contracts with respect to all or any Market Contracts of the defaulting Clearing Participant or Clearing Agency Participant within a reasonable time as determined by HKSCC; or (ii) there will not be sufficient resources to satisfy its obligations and liabilities arising out of prevailing Market Contracts with non-defaulting Clearing Participants and Clearing Agency Participants as a result of such Event of Default, HKSCC may, without prejudice to any other rights under the Rules, invoke the contract termination process as provided for in Rule 3709 in consultation with the Commission.

For the purposes of this Section, (i) references to "Eligible Securities" mean Eligible Securities other than China Connect Securities; and (ii) references to "Market Contract" mean a Market Contract other than a contract between HKSCC and a China Connect Clearing Participant arising as a result of the Novation of a China Connect Securities Trade to be settled under the CNS System.

If HKSCC invokes contract termination in accordance with Rule 3709, it shall determine the Identified Market Contracts under Rule 3709 and notify the relevant Clearing Participants and Clearing Agency Participants of its determination, including details of the Identified Market Contracts and the effective date of termination of such Identified Market Contracts. Notwithstanding the above, at any time during the contract termination process but prior to the effective date of termination of the relevant Identified Market Contracts, HKSCC may instead of proceeding with the termination of such Market Contracts, declare the occurrence of a Clearing Service Termination Event, and in such case the Identified Market Contracts shall not be terminated in accordance with the contract termination process but shall be terminated in accordance with Rule 4301.

### **10.16.2 Calculation of termination value**

The termination value for each Identified Market Contract shall be determined based on the prevailing market price at the time of contract termination, or if such market price is not available, the price shall be such price as HKSCC may reasonably determine.

On the basis of the termination value established for each Identified Market Contract, HKSCC shall, with respect to the CNS positions of each relevant Clearing Participant or Clearing Agency Participant arising from its Identified Market Contracts, determine the resulting net sum payable by such Clearing Participant or Clearing Agency Participant to HKSCC (the "Termination Value Payable") or the resulting net sum receivable by such Clearing Participant or Clearing Agency Participant from HKSCC (the "Unadjusted

Termination Value Receivable"). The Unadjusted Termination Value Receivable of a Clearing Participant is subject to adjustment in accordance with Section 10.16.3 below.

### 10.16.3 Payment of Termination Value Payable and Termination Value Receivable

#### (i) Termination Value Payable

HKSCC will notify each relevant Clearing Participant or Clearing Agency Participant of its Termination Value Payable and each such Clearing Participant or Clearing Agency Participant shall pay the specified Termination Value Payable to HKSCC in full within one Business Day or within such other time specified by HKSCC in the notice. If the relevant Clearing Participant or Clearing Agency Participant fails to pay the Termination Value Payable within the time specified in the notice, HKSCC may declare such Clearing Participant or Clearing Agency Participant as a defaulter.

In the event that HKSCC does not receive any part of the Termination Value Payable from a Clearing Participant or Clearing Agency Participant, HKSCC shall take reasonable steps to recover such amount. Such Clearing Participant or Clearing Agency Participant shall be responsible for any costs HKSCC reasonably incurs in attempting to recover such amounts and accordingly the Termination Value Payable actually received from such Clearing Participant or Clearing Agency Participant shall be deemed to be decreased by an amount equal to such costs, unless such costs are paid by such Clearing Participant or Clearing Agency Participant.

#### (ii) Termination Value Receivable

The amount payable by HKSCC to each relevant Clearing Participant or Clearing Agency Participant with respect to its CNS positions arising from Identified Market Contracts shall be known as the "Termination Value Receivable". The Termination Value Receivable of a Clearing Agency Participant shall be equal to its Unadjusted Termination Value Receivable determined in accordance with Section 10.16.2 above. In the case of a Clearing Participant, its Termination Value Receivable shall be calculated by multiplying its Unadjusted Termination Value Receivable by a percentage ("Termination Value Applicable Percentage") which is equal to the lesser of (a) and (b) below provided that if such percentage is a negative number, it should be set to zero:

(a) 100%; and

$$(b) \frac{\sum (\text{Termination Value Payable received by HKSCC}) + \sum (\text{available default resources}) - \sum (\text{Termination Value Receivable of Clearing Agency Participants})}{\sum (\text{Unadjusted Termination Value Receivable of Clearing Participants})}$$

where:

"Termination Value Payable received by HKSCC" means the amount of Termination Value Payable actually received from relevant Clearing Participants and Clearing Agency Participants by the time prescribed by HKSCC; and

"available default resources" means the aggregate of the resources (if any) that may be available to HKSCC including those available to be applied under Rules 2507, 2507A and 3702(ii).

HKSCC will notify each relevant Clearing Participant or Clearing Agency Participant of its Termination Value Receivable upon determination.

#### (iii) Payment

Payment of any Termination Value Payable and Termination Value Receivable shall be settled by HKSCC issuing DDIs or DCIs, where applicable, to the Designated Bank of the relevant Clearing Participant or Clearing Agency Participant as part of the CCASS money settlement process, or in any other manner determined by HKSCC from time to time. The

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Termination Value Payable and Termination Value Receivable shall be settled in the Eligible Currency in which the relevant Eligible Securities are denominated. To the extent that HKSCC determines that it is not possible or reasonably practicable to make payment in such Eligible Currency, HKSCC's obligations shall be to make payment, in full or in part, in such other currency or currencies and at such conversion rate(s) as HKSCC may in its absolute discretion determine to be fair and reasonable, taking into account all relevant circumstances as it may consider appropriate.

(iv) HKSCC's liability

Upon termination of one or more Identified Market Contracts under Rule 3709, all prevailing obligations of HKSCC and the relevant Clearing Participant or Clearing Agency Participant in respect of each such Identified Market Contracts between them (including the obligation to deliver any Eligible Securities under the Identified Market Contracts) shall cease and be replaced with the obligation of HKSCC or the relevant Clearing Participant or Clearing Agency Participant, as the case may be, to pay the other party a net sum equal to the aggregate termination value of each Identified Market Contract between them, as determined by HKSCC and where applicable adjusted in accordance with Rule 3709 and this Section of the Operational Procedures.