

## PART V      DEFAULT MANAGEMENT PROCESS

### Chapter 16   Default Management Process

#### Default Management Process

1601. The “**Default Management Process**” means the provisions set out in this PART V of these Clearing Rules and Chapter 8 of the Clearing Procedures, or the process described therein, as applicable, which shall be carried out by OTC Clear, in consultation with, and with the assistance of, the Default Management Group. The Default Management Process shall commence:

- (1) immediately following the occurrence of an Automatic Early Termination Event or the delivery of a Notice of Default with respect to one or more Clearing Members;
- (2) at a time determined by OTC Clear in the event of the occurrence of a Force Majeure Event or Illegality with respect to one or more Clearing Members pursuant to Clearing Rule 210(4); and
- (3) at a time determined by OTC Clear in the event of the occurrence of an event described in Clearing Rule 610 with respect to one or more Clearing Members,

each of the above, a “**DMP Event**”.

1602. Upon the occurrence of a DMP Event, OTC Clear will arrange for the following to occur in the order set out below:

- (1) to convene the Default Management Group;
- (2) if applicable and to the extent reasonably practicable, to arrange for the Affected Contracts to be ported as further described in Chapter 17 of these Clearing Rules;
- (3) to create on the Special Default Account a notional portfolio the economic profile of which is equivalent to the Contracts registered in the name of the Defaulting Clearing Member (but excluding any Affected Contracts registered in the name of such Defaulting Clearing Member which have been successfully ported pursuant to Chapter 17 of these Clearing Rules);
- (4) to execute measures in order to mitigate the risks associated with the DMP Event by putting on Hedging transactions for OTC Clear’s own account in accordance with the Hedging strategy proposed by the Default Management Group and approved by OTC Clear, as further described in Chapter 18 of these Clearing Rules; and
- (5) to complete the Auction process as further described in Chapter 19 of these Clearing Rules.

The provisions set out in Chapter 17, Chapter 18 and Chapter 19 of these Clearing Rules are implemented pursuant to Clearing Rule 1601 upon the occurrence of a DMP Event.

1603. Each Clearing Member must participate in the Default Management Process to the extent specified in the Clearing Rules, and take all steps and execute all documents necessary or desirable in relation thereto, including but not limited to executing relevant agreement(s) each in a form prescribed by OTC Clear for the purpose of execution of a Hedging transaction between a Non-Defaulting Clearing Member and OTC Clear.

1604. Whenever the Default Management Process is implemented by OTC Clear in respect of a Defaulting Clearing Member, OTC Clear will, with the assistance of the Default Management Group, provide such ongoing information to the Non-Defaulting Clearing Members as OTC Clear deems reasonably appropriate in respect of the progress of the Default Management Process, provided that OTC Clear is not under any obligation to disclose information in respect of the Default Management Process which, in the reasonable opinion of OTC Clear, may be subject to obligations of confidentiality, may constitute market sensitive data or is, in OTC Clear's reasonable opinion, inappropriate for disclosure to Clearing Members.

### **Default Management Group**

1605. The Default Management Group shall convene:

- (1) immediately following the occurrence of a DMP Event, and at sufficiently frequent intervals thereafter for a period so long as may be necessary to assist OTC Clear in the implementation of the Default Management Process relating to such DMP Event; or
- (2) at such other time as OTC Clear may deem appropriate and/or necessary from time to time.

1606. The Default Management Group shall be made up of representatives from both OTC Clear and Clearing Members.

1607. Upon request by OTC Clear, a Defaulting Clearing Member shall provide a representative to participate in the Default Management Group.

1608. The terms of reference of the Default Management Group will be published on HKEX website. Any amendment to the terms of reference of the Default Management Group will be subject to the approval of the OTC Clear Board. OTC Clear Board will, if it deems necessary, consult with the Risk Management Committee prior to approving any such proposed amendment.

### **Undertaking by Clearing Members**

1609. Each Clearing Member agrees, and shall procure, that:

- (1) it shall, at all times, provide representatives (each a "**DMG Delegate**") to participate in the processes described in Clearing Rules 1611 and 1612. The exact number of DMG Delegates that a Clearing Member shall provide, and the skill and expertise required from each such DMG Delegate will be notified by OTC Clear to each Clearing Member from time to time;
- (2) if OTC Clear requests a substitute where it believes a Clearing Member's nominated representative in the Default Management Group, as appropriate, is conflicted for its role as a DMG Member, or does not have the requisite skills or expertise, it shall provide such substitute;
- (3) its DMG Member will be fully available, at any time and for such periods of time as OTC Clear may require during the Default Management Process, to perform his function as a member of the Default Management Group including attending meetings in person or by telephone, considering and advising OTC Clear on the Default Management Process. The Clearing Member shall ensure that its DMG Member's other work commitments will not affect his availability for this purpose;

- (4) to take all steps to respect the confidential capacity in which its DMG Member receives information through the Default Management Group and to establish adequate procedures to prevent the disclosure or use for any purpose outside the scope of the Default Management Process of any such confidential information by it or its DMG Member. Such procedures shall normally include, without limitation, the establishment of Information Barriers within the Clearing Member; and
- (5) to be bound by and to ensure that it and any of its executives, directors or employees serving on the Default Management Group complies with the provisions set out in Chapter 20 and Chapter 21 of these Clearing Rules.

Each DMG Member, in performing its role in the Default Management Process, shall act in the best interests of OTC Clear only and each Clearing Member agrees that it shall not require its DMG Member to undertake any obligations to it which would result in that DMG Member being in breach of this duty.

### **Amendments to Default Management Process**

1610. Notwithstanding any contrary provisions contained in these Clearing Rules, in the event that OTC Clear, after consultation with the Risk Management Committee, deems appropriate to amend the Default Management Process, OTC Clear or the Risk Management Committee may present the relevant proposed amendments to the OTC Clear Board, which shall have the power to amend the Default Management Process in accordance with Clearing Rule 201.
1611. The DMG Delegates shall:
- (1) at least once a year, gather for the purpose of reviewing the provisions of the Default Management Process, and to the extent considered appropriate, recommend any amendment or revision to such provisions for consideration by the Risk Management Committee and the OTC Clear Board. The OTC Clear Board may, after consultation with the Risk Management Committee, approve any such proposed amendment or revision to the Default Management Process in accordance with Clearing Rule 201; and
  - (2) participate in each fire drill conducted by OTC Clear in relation to the Default Management Process. Fire drills in relation to the Default Management Process will be held at least once a year.
1612. If, during the implementation of the Default Management Process following the occurrence of a DMP Event with respect to a Clearing Member, OTC Clear, in consultation with the Default Management Group determines that it would be necessary or desirable for the efficient management of such default to deviate from, or supplement, the Default Management Process, it may, without prior notice to the Clearing Members, implement the Default Management Process in such modified manner or timetable as it sees fit, provided that OTC Clear, with the assistance of the Default Management Group shall promptly notify the Risk Management Committee of such decision. OTC Clear and the Default Management Group shall take into account interest of the investing public, the Non-Defaulting Clearing Members and OTC Clear in determining whether it is necessary or desirable to deviate from, or supplement, the Default Management Process.