

12. POSITION CONTROL

While daily and intra-day margining cover day-to-day risk, SEOCH also needs to ensure that each SEOCH Participant will continue to be able to meet margin calls. This, in practice, means ensuring SEOCH Participants' positions do not become larger than their resources are able to support.

In this regard, SEOCH will apply two measures in order to put an upper boundary on the positions held by SEOCH Participants, namely, position limit (for each option class) and capital based position limit (for each SEOCH Participant).

12.1 Position Limit

The position limit for each option class, measured in terms of number of contracts, and the necessary reporting and uplift application procedures are identical to those as defined in the Operational Trading Procedures. There are no separate reporting or uplift application procedures required by SEOCH, unless advised otherwise.

These position limits may be subject to revision as determined by the Chairman of the SEOCH Board in consultation with the Exchange and the Securities and Futures Commission provided that any limit so revised shall be, at all times, at least as stringent as that imposed by the Exchange under the *Options Trading Rules* or *Operational Trading Procedures*.

12.2 Capital Based Position Limit

The capital based position limit is a measure which seeks to ensure that the risk exposures of SEOCH Participants are commensurate with their financial strength in terms of liquid capital or, in the case of GCPs which are Registered Institutions, Adjusted Capital. For the purpose of this Chapter, the term "liquid capital" or "Adjusted Capital" shall, where applicable, be construed as the "apportioned liquid capital" or "apportioned Adjusted Capital" respectively under 12.3A.

Unless otherwise determined by SEOCH on a case by case basis, under this measure, net, gross and total limits are assigned to each SEOCH Participant on the basis of its latest reported liquid capital or Adjusted Capital, as appropriate, as follows:

Net Limit = 3 x LC or AC (i.e. 3 x LC or AC \geq NRM)

Gross Limit = 6 x LC or AC (i.e. 6 x LC or AC \geq GRM)

TMR Limit = 10 x LC or AC (i.e. 10 x LC or AC \geq TMR)

where

NRM = the sum of the Risk Margin (determined on a net basis and after offsetting any Mark-to-Market margin credit, where applicable) for all accounts of the SEOCH Participant in DCASS

GRM = the sum of the Risk Margin (determined on a net or gross basis as the case may be and after offsetting any Mark-to-Market margin credit, where applicable) for all accounts of the SEOCH Participant in DCASS

TMR = the Total Margin Requirement of the SEOCH Participant

- LC = in respect of a SEOCH Participant other than a GCP which is a Registered Institution, the apportioned amount or percentage of its liquid capital (calculated as per the Financial Resources Rules) notified to SEOCH under 12.3A, as adjusted upwards by any contribution to the Reserve Fund paid in cash by the SEOCH Participant as of the date of its latest monthly return filed with the Commission under the Financial Resources Rules and received by SEOCH from the Commission
- AC = in respect of a GCP which is a Registered Institution, the apportioned amount or percentage of its Adjusted Capital notified to SEOCH under 12.3A.

The Mark-to-Market Margin, Risk Margin and Total Margin Requirement of the SEOCH Participant will be measured in Hong Kong dollars or its non-Hong Kong dollar currency equivalent based on the exchange rate determined by SEOCH for each type of Settlement Currency.

For the purpose of calculating the net limit of a SEOCH Participant, all positions in each of its Client Offset Claim Accounts will be aggregated with the short positions in its Omnibus Client Account and margined together on a net basis to determine the Risk Margin and Mark-to-Market Margin of these two types of accounts; the short positions in its Sink Account will be margined together on a net basis to determine the Risk Margin and Mark-to-Market Margin of its Sink Account; and the long positions in its Omnibus Client Account and Sink Account will be treated as nil and disregarded in the calculation.

For the purpose of calculating the gross limit of a SEOCH Participant, since positions in the House, Market Maker, Individual Client and Client Offset Claim Accounts are margined on a net basis, the respective resultant Risk Margin and Mark-to-Market Margin of these accounts will be used in calculating the gross limit of the SEOCH Participant.

For the purpose of calculating the net, gross or total limit of a SEOCH Participant, the following steps will be performed:

- i. The Mark-to-Market Margin, Risk Margin and Total Margin Requirement of all accounts (individually or aggregated if accounts are margined together) of the SEOCH Participant in DCASS will be calculated.
- ii. If the Risk Margin of any account (or accounts if margined together) after offsetting any Mark-to-Market Margin credit or the Total Margin Requirement is a credit, it shall be set to zero.
- iii. The respective Risk Margin and Total Margin Requirements of all accounts will be summed up for the determination of its NRM, GRM and TMR.

Below is an example illustrating the position treatment for calculating the net, gross or total limit of a SEOCH Participant.

Example

Assume a SEOCH Participant has the following positions:

<u>Account</u>	<u>Contract</u>	<u>Long</u>	<u>Short</u>
Omnibus Client	HKZ DEC 95 C	<u>1</u>	<u>2</u>
	HKZ JAN 100 P	<u>0</u>	<u>3</u>
Client Offset Claim	HKZ DEC 95 C	<u>0</u>	<u>1</u>
	HKZ JAN 100 P	<u>0</u>	<u>2</u>
Individual Client 001	HKZ DEC 95 C	<u>1</u>	<u>0</u>
	HKZ JAN 100 P	<u>0</u>	<u>3</u>
House	HKZ DEC 95 C	<u>2</u>	<u>0</u>
	HKZ JAN 100 P	<u>0</u>	<u>5</u>
Sink	HKZ DEC 95 C	<u>2</u>	<u>0</u>
	HKZ JAN 100 P	<u>0</u>	<u>2</u>

(i) net limit:

<u>Account</u>	<u>Contract</u>	<u>Margining Basis</u>	<u>Long</u>	<u>Short</u>
Omnibus Client and Client Offset Claim	HKZ DEC 95 C	<u>Net</u>	<u>treat as 0</u>	3
	HKZ JAN 100 P		<u>0</u>	5
Individual Client 001	HKZ DEC 95 C	<u>Net</u>	<u>1</u>	<u>0</u>
	HKZ JAN 100 P		<u>0</u>	<u>3</u>
House	HKZ DEC 95 C	<u>Net</u>	<u>2</u>	<u>0</u>
	HKZ JAN 100 P		<u>0</u>	<u>5</u>
Sink	HKZ DEC 95 C	<u>Net</u>	<u>treat as 0</u>	<u>0</u>
	HKZ JAN 100 P		<u>0</u>	<u>2</u>

For the purpose of calculating the net limit, the short positions in the SEOCH Participant's Omnibus Client Account and the positions in its Client Offset Claim Account will be aggregated and the 1 and 2 long HKZ DEC 95 C in the Omnibus Client and Sink Accounts respectively will be treated as nil and disregarded in the calculation.

(ii) gross or total limit:

<u>Account</u>	<u>Contract</u>	<u>Margining Basis</u>	<u>Long</u>	<u>Short</u>
Omnibus Client	HKZ DEC 95 C	<u>Gross</u>	<u>1</u>	<u>2</u>
	HKZ JAN 100 P		<u>0</u>	<u>3</u>
Client Offset Claim	HKZ DEC 95 C	<u>Net</u>	<u>0</u>	<u>1</u>
	HKZ JAN 100 P		<u>0</u>	<u>2</u>
Individual Client 001	HKZ DEC 95 C	<u>Net</u>	<u>1</u>	<u>0</u>
	HKZ JAN 100 P		<u>0</u>	<u>3</u>
House	HKZ DEC 95 C	<u>Net</u>	<u>2</u>	<u>0</u>
	HKZ JAN 100 P		<u>0</u>	<u>5</u>
Sink	HKZ DEC 95 C	<u>Gross</u>	<u>2</u>	<u>0</u>
	HKZ JAN 100 P		<u>0</u>	<u>2</u>

For the purpose of calculating the gross or total limit, the positions in the Client Offset Claim, Individual Client 001 and House Accounts of the SEOCH Participant will be margined on a net basis.

12.3A Apportionment of Liquid Capital or Adjusted Capital

Where a SEOCH Participant is also a CCASS Clearing Participant or HKCC Participant or conducts various types of regulated activities under the Securities and Futures Ordinance, that SEOCH Participant must apportion either a designated amount or a percentage of the liquid capital (unless otherwise determined by SEOCH, as per its latest monthly return filed with the Commission under the Financial Resources Rules and received by SEOCH from the Commission) or in the case of a GCP which is a Registered Institution a designated amount or percentage of its Adjusted Capital as notified to SEOCH for the purpose of its Exchange Traded Options Business or satisfying its payment or other obligations as a SEOCH Participant to SEOCH, and such SEOCH Participant's capital based position limit will be calculated on the basis of its apportioned liquid capital or Adjusted Capital, as appropriate, as notified to SEOCH. Notification of a SEOCH Participant's initial liquid capital or Adjusted Capital apportionment or any change thereof shall be made by such SEOCH Participant in such manner, using such form and according to such schedule as may be prescribed by SEOCH from time to time. Any notification of changes to the apportionment received by SEOCH before a time specified by SEOCH from time to time shall become effective on the same Business Day the notification is received by SEOCH. Otherwise, changes to the apportionment shall become effective on the commencement of the next Business Day following receipt of the notification by SEOCH. Notwithstanding the foregoing, SEOCH reserves the right to accept or reject any initial apportionment or change of apportionment notified to it at its sole discretion. If no apportionment is notified to SEOCH, SEOCH reserves the right to apportion the liquid capital or Adjusted Capital, as appropriate, on behalf of the SEOCH Participant.

12.4 Monitoring of the Capital Based Position Limit

It is the responsibility of each SEOCH Participant to monitor its capital based position limits as conditions and positions change from time to time. It is in the interests of SEOCH Participants to ensure that they monitor their capital based position limits so as to give themselves the opportunity to make changes to their financing structure and/or trading positions well in advance of the limits being breached, since it may take time for SEOCH Participants to close out their positions or otherwise increase their liquid capitals or, in the case of GCPs which are Registered Institutions, their Adjusted Capital to bring the limits into line.

12.5 Remedies in Case of Breach

Unless an extension is granted subject to such conditions as may be imposed by SEOCH on a case by case basis, a SEOCH Participant whose positions have breached the net, gross and/or total limit assigned to it by SEOCH on a daily basis under 12.2 will be given 10 Business Days (as may be extended and subject to such conditions as aforesaid) to comply with the limit(s) provided that during such time, the SEOCH Participant pays SEOCH an additional margin equivalent to 25% of:

- i. its NRM in excess of its net limit;
- ii. its GRM in excess of its gross limit; or
- iii. its TMR in excess of its total limit;

whichever is the highest.

If the SEOCH Participant fails to pay or deliver any such additional margin, the breach must be remedied immediately.

A SEOCH Participant whose positions have breached any limit set out under 12.2 may remedy the breach by increasing its liquid capital or, in the case of a GCP which is a Registered Institution, its Adjusted Capital, whether by revising the amount or percentage of liquid capital or Adjusted Capital apportioned or otherwise. If the SEOCH Participant's declared remedy of the breach is to increase its

liquid capital or Adjusted Capital, SEOCH may demand proof to the satisfaction of SEOCH that the increase in the SEOCH Participant's liquid capital or Adjusted Capital actually has been achieved.

Notwithstanding the above, if the SEOCH Participant cannot comply with SEOCH's requirement by the specified time (as may be extended as aforesaid), the SEOCH Participant must, or failing which SEOCH may, close out or transfer to any other SEOCH Participant or SEOCH Participants all positions in excess of the capital based position limit.