

香港聯合交易所有限公司
(香港交易及結算所有限公司全資附屬公司)

THE STOCK EXCHANGE OF HONG KONG LIMITED
(A wholly-owned subsidiary of Hong Kong Exchanges and Clearing Limited)

通告 CIRCULAR

Subject: Amendments to the Options Trading Rules and the Operational Trading Procedures for Options Trading Exchange Participants (the “Procedures”) of The Stock Exchange of Hong Kong Limited (“SEHK”)

Enquiry: Mr. Hins So 2211 6297 | Mr. Calvin Ip 2211 6152

Holders of SEHK Trading Rights and Exchange Participants of SEHK are requested to note that the Securities and Futures Commission has approved amendments to the Options Trading Rules and the Procedures of SEHK for the purpose of:

- (i) allowing market makers or liquidity providers of exchange traded funds (“ETF”) to be authorized by SEHK to hold or control excess stock options contracts to hedge the risks arising from their ETF market making or liquidity providing activities;
- (ii) implementing the revised stock option position limit model; and
- (iii) introducing new risk monitoring measures on affiliates who are qualified and registered as a “Market Maker Affiliate” with the SEHK by way of satisfying the paid-up capital and shareholders’ funds requirements as prescribed by SEHK from time to time.

The amendments, as set out in the Appendices I and II, will come into effect on Thursday, 1 June 2017.

The marked-up version of the amendments can be downloaded from the following sections of the HKEX website:

- “Rule Update - Options Trading Rules of the Stock Exchange”
- “Rule Update - Operational Trading Procedures for Options Trading Exchange Participants of the Stock Exchange”

Ferheen Mahomed
Group General Counsel

Options Trading Rules

CHAPTER 4

OPTIONS EXCHANGE PARTICIPANTS AND THEIR CLIENTS

Position Limits

- 436A. Notwithstanding the above, any position limit from time to time imposed by the Exchange pursuant to Options Trading Rule 435, 436 or 438 shall not be less stringent than that prescribed by the Commission under section 35(1) of the Ordinance unless the Options Exchange Participant in question is, or is holding positions for, a person specified under section 4A of the Securities and Futures (Contracts Limits and Reportable Positions) Rules, in which case the Exchange may authorize the Options Exchange Participant to hold positions in excess of the limit prescribed by the Commission as the Exchange considers appropriate. Furthermore, an Options Exchange Participant may hold for itself or another person positions in excess of the position limit from time to time imposed by the Exchange if such Options Exchange Participant or person has been authorized by the Commission under subsection 4(3) of the Securities and Futures (Contracts Limits and Reportable Positions) Rules and the relevant Options Exchange Participant has notified the Exchange in writing of such authorization from the Commission.

CHAPTER 6

MARKET MAKERS

Risk Monitoring on an affiliate of a Market Maker holding such Market Maker's positions (a "Market Maker Affiliate")

- 614E. Rules 614F, 614G and 614H apply to an affiliate who is qualified and registered as a Market Maker Affiliate with the Exchange by way of satisfying

the paid-up capital and shareholders' funds requirements as prescribed by the Exchange from time to time.

- 614F. A Market Maker shall procure its Market Maker Affiliate to (i) submit to the Exchange, through the Market Maker, a monthly financial statement, setting out the Market Maker Affiliate's working capital as at the end of the calendar month by subtracting its current liabilities from its current assets (the "Working Capital"), within three weeks after the end of the relevant calendar month; and (ii) maintain a certain level of Working Capital on a daily basis, which shall be at least equal to (a) one-half of the Net Risk Margin ("NRM"); or (b) one-seventh of the Total Margin Requirement ("TMR"), whichever is higher, 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 the market maker account and the house account of the Options Exchange Participant.

TMR = the sum of the Total Margin Requirement for the market maker account and the house account of the Options Exchange Participant.

For the purpose of this Rule 614F, "Risk Margin" and "Total Margin Requirement" have the same meaning as set out in the Operational Clearing Procedures for Options Trading Exchange Participants of SEOCH.

- 614G. On breaching the Working Capital requirement, the Market Maker shall report to the Exchange as soon as practicable and in any event no later than 4pm on the next Business Day. If the Market Maker repeatedly fails to notify the Exchange, the Exchange may, in its sole and absolute discretion, revoke the permit granted to the Market Maker. The Market Maker shall also forthwith procure the Market Maker Affiliate to reduce its positions or increase its Working Capital within 10 Business Days.

- 614H. If the Market Maker Affiliate fails to remedy the breach of the Working Capital requirement, the Exchange may close out such open positions on the Market Maker's behalf or may request the Clearing House to effect such

closing out on the Market Maker's behalf. The Exchange may also, in its sole and absolute discretion, revoke the permit granted to the Market Maker. None of the Exchange, the Clearing House or a recognized exchange controller which is the controller of the Exchange and the Clearing House shall be liable for any loss suffered by any person or persons in respect of such closing out. The Market Maker shall indemnify and hold the Exchange, the Clearing House, and a recognized exchange controller which is the controller of the Exchange and the Clearing House harmless in respect of any costs or other expenses arising by reason of such closing out.

Operational Trading Procedures for Options Trading Exchange Participants

Chapter 5: Client Services Support

5.9 Position Limit and Reporting Level

Subject to *Options Trading Rule 436A*, limits are imposed on the open positions any single party (Options Exchange Participant or client) can carry at any one time. Reporting levels, in excess of which a party (Options Exchange Participant or client) is required to report to the Exchange, are also prescribed. Without prejudice to the powers of the Exchange under *Options Trading Rules 435 and 439*, the position limits^(Note 1) currently applicable are classified into 3 levels, namely 150,000, 100,000 and 50,000 open contracts per option class in any one market direction for all expiry months combined. The applicable level of position limit is determined by reference to the methodology set out in 5.9A below. Reporting level^(Note 2) for all option classes is 1,000 open contracts per option class per expiry month.

Notes:

1. *Position Limit* – this represents the maximum number of open contracts a single party can hold for any option class in any one market direction for all expiry months combined (N.B. long calls/short puts combined are in one direction and short calls/long puts combined are in another direction).

Example A, if the limit is 50,000 and an Options Exchange Participant is long a total of 47,000 calls and short 3,000 puts in the same option class, it has reached the limit, but if it is long 47,000 calls and long 3,000 puts, it has not.

Example B, if the limit is 150,000 and an Options Exchange Participant is long a total of 135,000 calls and 15,000 puts and short a total of 10,000 puts and 132,000 calls in the same option class, it has not reached the limit, since the positions in one market direction will be 145,000 contracts (long 135,000 calls and short 10,000 puts) and 147,000 contracts (short 132,000 calls and long 15,000 puts)

A Market Maker or an Options Exchange Participant which is, or is holding positions for, a person specified under section 4A of the Securities and Futures (Contracts Limits and Reportable Positions) Rules may hold positions in excess of the limit prescribed by the Commission under the Securities and Futures (Contracts Limits and Reportable Positions) Rules provided that it is authorized to do so by the Exchange under 5.12 below.

2. *Reporting level* – this is the number of open contracts in any one single expiry month of an option class, including all types, strike prices, long and short positions in excess of which a position shall be reported to the Exchange. Where positions

exceeding this level are held for a client, the Options Exchange Participant must notify the Exchange of the client's identity. Positions arising from market making activities that are held by Market Makers in their Market Maker Accounts are treated as having been reported to the Exchange.

5.9A Methodology for Setting the Position Limit

The position limit is set based on the contract-equivalent number and shall be calculated by reference to the market capitalization and liquidity of the underlying stock relating to that particular stock options contract.

Contract-equivalent number (X)	Position limit
150,000 contracts $\leq$ X	150,000 contracts
100,000 $\leq$ X < 150,000 contracts	100,000 contracts
X < 100,000 contracts	50,000 contracts

X = 5 per cent of the outstanding shares divided by the contract size subject to the provisions set out below:

- (i) if 5% of the outstanding shares is less than 25 per cent of the stock's turnover for the previous six months (the "25% Threshold"), X shall be deemed to be equal to the 25% Threshold divided by the contract size subject to (iii) below;
- (ii) if 5% of the outstanding shares is greater than 33 per cent of the stock's turnover for the previous six months (the "33% Threshold"), X shall be deemed to be equal to the 33% Threshold divided by the contract size subject to (iii) below; and
- (iii) if X as calculated above is more than the Liquidity Threshold divided by the contract size, it shall be deemed to be equal to the Liquidity Threshold divided by the contract size. "Liquidity Threshold" means 6.7% of the stock's turnover in the previous six months.

The Liquidity Threshold could be revised from time to time as deemed appropriate by the Exchange.

The position limits will be reviewed regularly on an annual basis to adjust for any substantial changes due to market development. The formula above will be applied to all option classes at the end of November each year, and if revisions are required, the updated position limits will be announced in December in the same year, and they will take effect on the first business day of April in the next calendar year.

Following a corporate action which results in a material change in the value of an underlying stock, the Exchange may consider adjusting the contract size of the affected stock option to substantively maintain its notional value. The decision as to whether or not an adjustment will be made to the terms of an options contract and the nature of that adjustment will be announced no later than the tenth trading day after the company

announcement of the relevant corporate actions is made.

5.12 Increasing a Position Limit

Subject to *Options Trading Rule 436A*, an Options Exchange Participant or a client may request the Exchange to increase the position limit imposed by the Exchange or, in the case of a Market Maker or Options Exchange Participant which is, or is holding positions for a person specified under section 4A of the Securities and Futures (Contracts Limits and Reportable Positions) Rules, to authorize it to hold positions in excess of the limit prescribed by the Commission thereunder (the “Commission’s prescribed limit”). Such a request should be made in writing to the Exchange. The Options Exchange Participant or its client or the Market Maker that made the request may be required to justify the increase of the limit imposed by the Exchange or the holding of positions in excess of the Commission’s prescribed limit. The Exchange may at its absolute discretion grant or refuse the request. Approval from the Exchange must be received prior to entering into positions which exceed the position limit imposed by the Exchange or the Commission’s prescribed limit.