



SECURITIES AND
FUTURES COMMISSION
證券及期貨事務監察委員會

Consultation on proposed changes to the Securities and Futures (Contracts Limits and Reportable Positions) Rules and the Guidance Note on Position Limits and Large Open Position Reporting Requirements

April 2022

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Foreword

The Securities and Futures Commission (**SFC**) invites market participants and interested parties to submit written comments on the proposals discussed in this consultation paper or on related matters that might have a significant impact upon the proposals by no later than 27 June 2022.

Written comments may be sent as follows:

Mail : The Securities and Futures Commission
 54/F One Island East
 18 Westlands Road
 Quarry Bay, Hong Kong

 Re: Consultation on changes to the Position Limit Regime

Fax : (852) 2521 7917

Online : <https://apps.sfc.hk/edistributionWeb/gateway/EN/consultation/doc?refNo=22CP3>

Email : position-limit@sfc.hk

Any person who wishes to submit comment on behalf of any organisation should provide the details of the organisation whose views are represented.

Please note that the names of the commentators and the contents of their submissions may be published on the SFC's website and in other documents to be published by the SFC. In this connection, please read the Personal Information Collection Statement attached to this consultation paper.

If you do not want your personal information, affiliation or the contents of your submission to be disclosed to the public, please state this clearly in your submission. In this regard, a standard confidentiality statement in an email will not be considered as a request for non-disclosure.

After the consultation ends, a consultation conclusions paper will be published in due course.

Securities and Futures Commission
Hong Kong

April 2022

Personal Information Collection Statement

This Personal Information Collection Statement (**PICS**) is made in accordance with the guidelines issued by the Privacy Commissioner for Personal Data. The PICS sets out the purposes for which your Personal Data¹ will be used following collection, what you are agreeing to with respect to the SFC's use of your Personal Data and your rights under the Personal Data (Privacy) Ordinance (Cap. 486) (**PDPO**).

Purpose of collection

The Personal Data provided in your submission to the SFC in response to this consultation paper may be used by the SFC for one or more of the following purposes:

- (i) to administer the relevant provisions² and codes and guidelines published pursuant to the powers vested in the SFC;
- (ii) in performing the SFC's statutory functions under the relevant provisions;
- (iii) for research and statistical purposes; or
- (iv) for other purposes permitted by law.

Transfer of Personal Data

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Access to data

You have the right to request access to and correction of your Personal Data in accordance with the provisions of the PDPO. Your right of access includes the right to obtain a copy of your Personal Data provided in your submission on this consultation paper. The SFC has the right to charge a reasonable fee for processing any data access request.

Retention

Personal Data provided to the SFC in response to this consultation paper will be retained for such period as may be necessary for the proper discharge of the SFC's functions.

¹ Personal Data means personal data as defined in the Personal Data (Privacy) Ordinance (Cap. 486).

² The term "relevant provisions" is defined in Section 1 of Part 1 of Schedule 1 to the Securities and Futures Ordinance (Cap. 571) and refers to the provisions of that Ordinance together with certain provisions in the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32), the Companies Ordinance (Cap. 622) and the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (Cap. 615).



Enquiries

Any enquiries regarding the Personal Data provided in your submission on this consultation paper, or requests for access to Personal Data or correction of Personal Data, should be addressed in writing to:

Data Privacy Officer
Securities and Futures Commission
54/F One Island East
18 Westlands Road
Quarry Bay, Hong Kong

A copy of the Privacy Policy Statement adopted by the SFC is available upon request.

Executive summary

1. The SFC proposes to make changes to the position limit regime for listed futures and options contracts. The SFC regularly reviews the regime to ensure that it remains appropriate and relevant for the Hong Kong financial market.
2. Under section 35(1) of the Securities and Futures Ordinance (**SFO**), the SFC may prescribe position limits and reportable positions for futures and options contracts. The statutory prescribed limits and the reportable positions are set out in the Securities and Futures (Contracts Limits and Reportable Positions) Rules (**Rules**).
3. The proposed changes address recent developments in the Hong Kong securities and futures markets and align the requirements with the SFC's regulatory policies and objectives.
4. Section A of this paper comprises three parts:
 - (a) Part I sets out the background, the proposed changes and reasons for them. In summary, the proposed changes are:
 - i. to expand the list of futures and options contracts which the SFC may authorise a person to hold or control in excess of the prescribed limit. The new contracts proposed to be added are: Weekly Hang Seng Index (**HSI**) options contracts, Weekly Hang Seng China Enterprises Index (**HSCEI**) options contracts, HSI Futures options contracts, HSCEI Futures options contracts and Hang Seng TECH Index futures contracts and options contracts;
 - ii. to prescribe reportable positions for futures and options contracts traded during holidays to complement the rollout of the Derivatives Holiday Trading program by Hong Kong Exchanges and Clearing Limited (**HKEX**);
 - iii. to clarify that a clearing participant (**CP**) of HKFE Clearing Corporation Limited (**HKCC**) or the SEHK Options Clearing House Limited (**SEOCH**) in exercising its right to dispose of its client's positions upon a default is not regarded as having the type of discretion described in section 7(3) of the Rules;
 - iv. to provide for a CP which clears excess positions of persons who have been authorised by the SFC or under the rules of the Hong Kong Futures Exchange (**HKFE**) or the Stock Exchange of Hong Kong Limited (**SEHK**) to hold or control excess positions to be eligible to apply for authorisation from the SFC or the recognised exchange company concerned to hold or control excess positions for its clients;
 - v. to provide for the application of prescribed position limits and reportable positions in relation to a person holding or controlling futures and options contracts of unit trusts;

- vi. to provide for the application of prescribed position limits and reportable positions in relation to a person holding or controlling futures and options contracts of a sub-fund of an umbrella fund; and
 - vii. to prescribe position limits and reportable positions in relation to some futures and options contracts.
- (b) Part II sets out amendments to the Rules to reflect the proposed changes stated above.
- (c) Part III sets out changes to the Guidance Note on Position Limits and Large Open Position Reporting Requirements (**Guidance Note** or **GN**).

Section A

Proposed changes to the position limit regime

1. The position limit regime, which comprises statutory prescribed limits and reportable position reporting requirements, was enhanced after the Asian Financial Crisis in 1997-98 to strengthen the transparency and orderliness of the Hong Kong securities and futures markets and prevent and discourage the build-up of positions which may affect the orderly functioning and stability of the Hong Kong financial market. Over the years, the position limit regime has helped the SFC fulfil its regulatory objectives of maintaining and promoting an orderly securities and futures industry. The regime has provided the SFC with data for market monitoring in a timely manner which in turn helps the SFC reduce systemic risks in the securities and futures industry and safeguard market stability.
2. Under section 35(1) of the SFO, the SFC may prescribe limits on the number of futures and options contracts a person may, directly or indirectly, hold or control and require a person holding or controlling a reportable position to lodge a notice of that reportable position with a recognised exchange company or the SFC. The statutory prescribed limits and reportable positions of futures and options contracts are set out in the Rules.
3. The SFC regularly reviews the regime requirements and if necessary, makes changes to ensure the regime remains appropriate and relevant to the Hong Kong financial market. In 2017, in response to market developments, the cap on the excess position limit which may be authorised by the SFC was increased from 50% to 300% of the statutory position limit and the prescribed limit for stock options contracts from 50,000 to 150,000 contracts. New excess position limits regimes for index arbitrage activities, asset managers and market makers of exchange-traded funds were also introduced.
4. The proposed changes set out in this paper would address developments in the Hong Kong securities and futures markets since the 2017 amendments and align the requirements with the SFC's regulatory policies and objectives.

Part I

Expanding the list of contracts that the SFC may authorise a person to hold or control in excess of the prescribed limit

5. Currently, the Rules provide for market participants to seek authorisation from the SFC to hold or control excess positions under certain conditions. Pursuant to sections 4C, 4D and 4E of the Rules, the SFC may grant authorisation to an exchange participant or its affiliates or an asset manager to hold or control any of the HSI futures and options contracts or HSCEI futures and options contracts in excess of the prescribed statutory limit for the purposes of facilitating the provision of services to clients, index arbitrage activity and asset management activity, respectively. These

futures and options contracts are the only “specified contract” set out in section 2 of the Rules.

6. HKEX recently launched the Weekly HSI options contracts, Weekly HSCEI options contracts, HSI Futures options contracts, HSCEI Futures options contracts and Hang Seng TECH Index futures and options contracts (**New Contracts**), and as discussed later in this paper, the SFC proposes to prescribe position limits for these contracts.
7. Under the Rules of HKFE, due to having the same underlying index (ie, HSI or HSCEI), positions in the weekly options contracts and futures options contracts and positions in other HSI and HSCEI futures and options contracts are to be aggregated and subject to aggregated position limits. Therefore, to allow market participants who have been authorised to hold excess positions in the HSI or HSCEI futures and options contracts to apply the same position limits to all contracts with HSI or HSCEI as the underlying index, they too must be authorised to hold excess positions in the Weekly HSI options, Weekly HSCEI options, HSI Futures options and HSCEI Futures options contracts. Separately, based on trading data and market feedback, the SFC noted that market participants may also need excess position limits for the Hang Seng TECH Index contracts for the purposes of facilitating the provision of services to clients, index arbitrage and asset management activities. In view of the above, the SFC proposes to add the New Contracts to the list of “specified contract”.
8. The proposal will enable exchange participants (**EPs**) or their affiliates and asset managers to seek authorisation from the SFC under sections 4C, 4D and 4E to hold or control any of the New Contracts in excess of the prescribed statutory limit.
9. The SFC is of the view that the inclusion of the New Contracts in the list of “specified contract” will not increase systemic risks to the Hong Kong financial market. In reviewing applications for excess limits, the SFC will assess whether applicants have genuine needs and sufficient internal controls and risk management measures to monitor and manage the risks associated with the excess positions. In addition, the SFC will impose conditions on each authorisation requiring the applicants to submit regular reports on their utilisation of the excess position limits. If necessary, the SFC can withdraw the excess position limits granted.

Question 1 (please provide reasons in support of your comments):

- | |
|--|
| (i) Do you have any comments on the proposed addition of the New Contracts to the list of “specified contract”? |
| (ii) Are there any other futures and options contracts traded on HKFE which should also be included on the list? |

Prescribed position limits and reportable positions in futures and options contracts traded during holidays

10. HKEX released its consultation conclusions³ on Derivatives Holiday Trading (**Holiday Trading**) in January 2022. Under this programme, HKFE will determine, from amongst its suite of non-HKD denominated futures and options contracts, which contracts (**Holiday Contracts**⁴) can be traded on HKFE or through its facilities on a Hong Kong public holiday falling on a weekday (**Holiday Trading Day**). HKEX's conclusions paper stated that HKFE will provide in its rules for an EP who holds or controls open positions in a Holiday Contract which reaches the reporting level either for its own account or on behalf of its clients to report the positions to HKFE on the next Holiday Trading Day or business day, whichever is earlier.
11. At present, the Rules only require reporting of reportable positions on business days. In other words, after the launch of Holiday Trading, if the Rules are not amended accordingly, market participants will only report their reportable positions established during Holiday Trading Days on the next business day. This will affect the SFC's capability to monitor build-ups of large positions during Holiday Trading Days which may have a negative impact on the stability of the futures market.
12. To address this issue, the SFC proposes to amend the Rules to prescribe reportable positions for the Holiday Contracts and provide for the reporting of these positions during Holiday Trading Days. The requirements will mirror those specified in the rules of HKFE as described in paragraph 10 above and the prescribed reportable positions will be set out in Schedule 1 of the Rules.

Question 2 (please provide reasons in support of your comments):

Do you have any comments on the proposed reportable position reporting requirements for Holiday Contracts?

Clearing participants have no “discretion” in relation to clearing clients’ positions

13. Section 7 of the Rules sets out how the prescribed limits and reportable positions apply to a person holding or controlling futures or options contracts for another person. Section 7(1) states that for the purpose of complying with these requirements, a person (**Person A**) shall consider his or her own contracts separate from those he or she holds or controls for another person (**Person B**). However, section 7(2) provides that Person A shall not be regarded as holding or controlling the contracts for Person B if Person A has discretion in relation to Person B's contracts. Section 7(3) further explains the concept of discretion in this context. That is, Person A will be regarded as having discretion over Person B's contracts if Person A has been

³ HKEX's Consultation Conclusions: [https://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2016-Present/November-2021-Derivatives-Holiday-Trading/Conclusions-\(Jan-2022\)/cp202201cc.pdf?la=en](https://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2016-Present/November-2021-Derivatives-Holiday-Trading/Conclusions-(Jan-2022)/cp202201cc.pdf?la=en)

⁴ Holiday Contracts refer to the contracts determined by HKFE to be tradable on public holidays in Hong Kong.

authorised by Person B to buy or sell those contracts. In other words, when Person A exercises the kind of discretion set out in Section 7(3), he or she will have to aggregate all the futures and options contracts held or controlled for Person B together with his or her own for the purpose of complying with the prescribed limits and reporting the reportable positions.

14. Section 7(3) does not apply in some situations such as those in the examples in paragraph 5.2 of the GN. One example is where a firm initiates orders to close out a position held for its client upon a default on payment by the client.
15. In practice, a situation which falls within this example would be a CP closing out its client's position when the client has defaulted on payment. It has come to the SFC's attention that despite paragraph 5.2 of the GN, there is some uncertainty about the application of section 7(3) to a CP's right to dispose of a client's position in the event of a payment default.
16. Therefore, to provide clarity and legal certainty, the SFC would like to make it clear in the Rules that a CP does not fall within the "discretion" under section 7(3) when it exercises its right to dispose of a client's position when the client has defaulted on a payment.

Question 3 (please provide reasons in support of your comments):

Do you have any comments on the proposal to set out in the Rules that a CP in exercising its right to dispose of its client's position when the client has defaulted on a payment shall not be regarded as having "discretion" as described in section 7(3)?

Excess position limit for clearing participants

17. A person who has been authorised to hold or control contracts in excess of the prescribed limit under the Rules may clear the positions by itself (if it is also a CP) or, if it is not a CP, through a CP of the recognised clearing house concerned. The CP providing clearing services to this person will hold or control the excess positions for that person. According to section 4 of the Rules, no person, unless authorised under the Rules, may hold or control contracts in excess of the prescribed limit. If the CP in question has not been authorised under the Rules, it is in breach of the Rules.
18. In the past, many of the persons who applied for excess position limits were both EPs and CPs. Thus, in cases where the SFC granted authorisation to a person to hold or control contracts in excess of the prescribed limit, that person was also a CP of the clearing house concerned and granting a separate authorisation to the CP for the same excess positions was not necessary. However, the SFC recently observed that more EPs are not holding clearing house participantships and are clearing through the services of a General Clearing Participant (**GCP**). If those EPs were granted an authorisation by the SFC to hold or control contracts in excess of the prescribed limit, the GCP providing clearing services would also need to be authorised to hold the excess positions.

19. Similarly, those persons who have been granted authorisation under the rules of HKFE or SEHK to hold or control contracts in excess of the prescribed limit for the purpose of market making or as an issuer (or its related corporation) of securities listed under Chapter 15A of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited as set out in Section 4A of the Rules, the CP or GCP which provides clearing services to these persons will also need to be authorised to hold or control the same excess positions.
20. The SFC thus proposes to introduce an authorisation mechanism for this scenario. HKFE or SEHK will authorise the CPs or GCPs which provide clearing services to the persons who are authorised by HKFE or SEHK, and the SFC will authorise those CPs or GCPs which provide services to persons who are authorised by the SFC. The process for making an application to the SFC will be set out in the GN as indicated in Appendix B.

Question 4 (please provide reasons in support of your comments):

Do you have any comments on the proposed authorisation mechanism for CPs which provide clearing services for persons authorised to hold or control contracts in excess of the prescribed limits?

Prescribed position limits and reportable positions of unit trusts

21. The restriction on the number of contracts held or controlled set out in section 4(1) of the Rules, and the lodging of a written notice of a reportable position under section 6(1), applies to a “person”. The term “person” as defined in the Interpretation and General Clauses Ordinance (**IGCO**) *“includes any public body and any body of persons, corporate or unincorporate”*. This definition does not include a trust. Thus, it may appear that a fund which is established as a unit trust, not being a “person” as defined, is not subject to the prescribed limits and reporting of reportable positions, but this is not correct. The SFC would like to amend the Rules to avoid any misconception.
22. Funds which are established as unit trusts have trustees. Typically, the trustee, if not a natural person, would be a corporate and hence would fall within the definition of a “person” as defined in the IGCO. Therefore, if the trustee holds or controls futures or options contracts on behalf of a unit trust, the trustee has the obligation to report the unit trust’s reportable positions. The trustee must also observe the prescribed limits in relation to the positions of the trust. This means that the unit trusts for which they are the trustees are subject to the prescribed limits and reporting of reportable positions. The SFC will amend the GN to remind trustees of unit trusts of their existing obligations under the Rules. In this regard, if a trustee is engaging an agent to report reportable positions on its behalf, the SFC expects the trustee to maintain proper internal records to reflect the arrangement.

23. A key regulatory objective of the position limit regime is to prevent and discourage the build-up of positions which may affect the orderly functioning and stability of the Hong Kong financial market. For this purpose, the prescribed limits apply to every fund (including sub-funds) no matter whether it is in the form of a unit trust, corporate fund or other structure. Otherwise, a person would be able to use two separate funds to create extremely large open positions in opposite market directions without breaching the prescribed limits.
24. It is the SFC's policy intention that where a person holds or controls positions of a unit trust, the prescribed limits and reportable positions should apply separately to the positions he or she owns and to the positions of the unit trust. In addition, where a person holds or controls positions of more than one unit trust, the SFC will require the person to separately apply the prescribed limits and reportable positions to the positions of each unit trust because each is distinct and has its own investment mandate. Therefore, if a trustee acts for multiple unit trusts, it would report the reportable positions for each unit trust separately and ensure that all the positions comply with the prescribed limits. Separately, a person who has discretion as described in section 7(2), such as an asset manager, would have to aggregate the positions of all the funds over which it has discretion to comply with the Rules. Amendments to the Rules are proposed to reflect this.
25. Under the existing Rules, a notice of a reportable position held or controlled for another person must be accompanied by information which provides the identity of the person and the number of contracts for the reportable position held or controlled for that person in each contract month. The SFC is proposing to apply a similar requirement for a notice of a reportable position of a unit trust, except that the unit trust's name will be specified in the notice rather than the person's identity.

Question 5 (please provide reasons in support of your comments):

- (i) Do you have any comments on the proposed changes to require a person, unless the person has discretion over the positions, to apply the prescribed limits and reportable positions separately to: (i) his or her own positions and the positions of a unit trust which he or she holds or controls and (ii) the positions in each unit trust where there is more than one unit trust?
- (ii) Do you have any comments on the requirement that the name of the unit trust is to be provided in a notice of a reportable position of the unit trust?

Sub-funds of an umbrella fund

26. Most funds which are set up as umbrella funds have sub-funds under the umbrella structure. Each sub-fund tends to operate as a separate unit and its portfolio is segregated from other sub-funds. The existing Rules do not provide for how the prescribed limits and reportable positions apply to these sub-funds. The SFC would like to address this in the Rules.
27. As mentioned previously, the regulatory objective of the Rules is to prevent a build-up of large positions which may pose a threat to the orderly functioning and stability of

the market. Given that each sub-fund is managed independently according to its investment mandate or strategy, the prescribed limits and reportable positions should be applied to each sub-fund individually and separately. This would be in line with how each sub-fund's positions and the associated risks are managed.

28. The SFC proposes to specify in the Rules that a person that holds or controls positions of the sub-funds of an umbrella fund apply the prescribed limits and the reportable positions separately to each sub-fund as if each one were a stand-alone fund, except in situations where the person has discretion over the positions of the sub-fund such as the fund manager which manages the positions of all the sub-funds in question.
29. The SFC noted that some market participants already report the reportable positions for each individual sub-fund separately, indicating that in practice they apply the prescribed limits and reportable positions to sub-funds individually and separately.
30. The SFC is aware of the different forms and legal structures for constituting an umbrella fund. As it is not possible to cover all the legal structures and umbrella funds are usually constituted as unit trusts or corporate funds, the SFC is therefore proposing to address these two legal structures.
31. The SFC proposes that the notice of a reportable position in respect of a sub-fund is to be accompanied by information which provides the name of the sub-fund and the number of contracts held or controlled in respect of the sub-fund for the reportable position in each contract month or option series.

Questions 6 (please provide reasons in support of your comments):

- (i) Do you have any comments on the proposal to require the prescribed limits and reportable positions to be separately applied to each of the sub-funds under an umbrella fund as if each of sub-fund were a stand-alone fund?
- (ii) Apart from umbrella funds constituted as unit trusts and corporate funds, are there any other legal forms or structures which should be addressed?
- (iii) Do you have any comments on the requirement that the name of the sub-fund be provided in a notice of a reportable position of a sub-fund?

The SFC's rationale for amending the Rules for unit trusts and sub-funds

32. The proposed amendments provide clarity and legal certainty about how the Rules are to be applied. These changes would ensure that:
 - Unit trusts and sub-funds observe prescribed limits and report reportable positions in a manner which is consistent with how those positions are managed and monitored in practice;

- Trustees and other relevant entities which hold or control positions in unit trusts or sub-funds are aware of their legal obligations under the Rules; and
- As a result of the above, the data for reportable positions available to the SFC for market monitoring purposes would be more comprehensive and more accurately reflect trading activities.

33. The proposed changes may have a greater impact on unit trusts, funds with sub-funds and other associated parties such as trustees, custodians and fund managers if they are reporting or applying limits in a manner different from that envisaged under the proposed amendments. These parties will have to adjust their arrangements for reportable position reporting and compliance with prescribed limits. However, the SFC considers that overall the proposed amendments will not create an undue burden on the fund management industry. We will provide sufficient time for the necessary adjustments and arrangements to be made.

34. Leveraged and inverse exchange traded funds using HSI and HSCEI futures contracts for hedging might see growth constrained by the prescribed limits. Although index swaps in the over-the-counter market could be used as substitutes for futures contracts, the higher cost of index swaps would affect performance of funds and reduce the return for investors. From the prospectuses of leveraged and inverse funds, we understand that the issuers are well aware of this risk. Nevertheless, we will work closely with the fund management industry to explore ways to facilitate market development without creating additional risks to the futures market.

Prescribing position limits and reportable positions in relation to the inclusion of additional futures and options contracts in Schedule 1 of the Rules

35. Since the last amendment exercise, HKEX has launched several new contracts. Proposed amendments to Schedule 1 of the Rules include the proposed prescribed limits and reporting levels for the new contracts which are same as those stipulated in the Rules of HKFE.

36. The contracts proposed to be included in Schedule 1 of the Rules are:

- (i) Weekly Hang Seng Index options contract
- (ii) Weekly Hang Seng China Enterprises Index options contract
- (iii) Hang Seng Index Futures options contract
- (iv) Hang Seng China Enterprises Index Futures options contract
- (v) Hang Seng Index (Gross Total Return Index) futures contract
- (vi) Hang Seng China Enterprises Index (Gross Total Return Index) futures contract
- (vii) Hang Seng Index (Net Total Return Index) futures contract
- (viii) Hang Seng China Enterprises Index (Net Total Return Index) futures contract
- (ix) Mini US Dollar vs Renminbi (Hong Kong) futures contract
- (x) Hang Seng TECH Index futures contract
- (xi) Hang Seng TECH Index options contract

- (xii) MSCI China A 50 Connect (USD) Index futures contract
37. In addition, HKEX proposes to revise the spot month and aggregate position limits for the USD/CNH futures and options contracts to cater for market growth. The SFC considers that the proposal is appropriate. Details of the amendments are set out in Appendix A.

Part II

Proposed amendments to the Securities and Futures (Contracts Limits and Reportable Positions) Rules (Cap 571Y)

38. Appendix A1 to this consultation paper contains the Rules with proposed amendments (which are either underlined or marked up for easy reference) to reflect the above proposals. Appendix A2 is a clean version of the amended Rules. The amendments are as follows:
- i. *Expanding the list of contracts which the SFC may authorise a person to hold or control in excess of the prescribed limit* - the definition of “specified contract” in section 2 of the Rules would be expanded to include the New Contracts;
 - ii. *Prescribed reporting requirements for futures and options contracts traded during holidays* – new sections 6(1A) and 6(1B) provide for reporting of reportable positions in a holiday contract. The terms “holiday contract” and “holiday contract trading day” are defined in section 6(5);
 - iii. *Clearing participants have no “discretion” in relation to clearing clients’ positions* – new section 7(4) expressly states that a CP of HKCC or SEOCH is not to be regarded as having the type of “discretion” as described in the Rules if the CP’s power to acquire or dispose of positions may only be exercised in the event of a default on payment;
 - iv. *Excess position limit for clearing participants* – new section 4A(e) expands the list of persons who may be authorised under the exchange rules to hold excess positions to include a CP of HKCC or SEOCH which clears positions for persons authorised by a recognised exchange company to hold or control excess positions. New section 4F provides for the SFC to authorise a CP of HKCC to hold the excess positions in a specified contract it clears for persons that have been authorised to hold or control the excess positions under sections 4C, 4D or 4E;
 - v. *Prescribed limits and reporting of reportable positions of unit trusts and sub-funds of an umbrella fund* – new sections 6(3) ad 6(4) set out the information which must be provided in a notice of reportable positions of a unit trust or a sub-fund and the new section 7A with the heading “**Compliance by persons with respect to a unit trust or a corporate fund**” provides for the application of prescribed limits and reportable positions in relation to unit trusts and sub-funds of an umbrella fund;

- vi. *Prescribing position limits and reportable positions in relation to some futures and options contracts* – the changes are self-explanatory and marked on Schedule 1.

The SFC invites the public to comment on the proposed changes to the Rules.

Part III

Proposed amendments to the Guidance Note on Position Limits and Large Open Position Reporting Requirements

39. The proposed changes would necessitate amendments to the Guidance Note which has been issued to help market participants better understand how the Rules are intended to operate. The proposed revisions to the Guidance Note are set out in Appendix B and marked up for easy reference.
40. In addition, the SFC would like to take this opportunity to propose changes to paragraphs 3.26 and 3.35 to make it clear that a fund may not hold or control excess positions notwithstanding that the fund's asset manager is authorised to hold excess positions.

Section B

Concluding remarks

41. The proposed changes are intended to address recent developments in the Hong Kong securities and futures markets and align the requirements with SFC's regulatory objectives and policies. The SFC considers that these proposals, upon implementation, would ensure that the position limit regime remains appropriate and relevant to the Hong Kong financial market and facilitate the SFC's market monitoring.



Appendix A – Proposed amendments to the Securities and Futures (Contracts Limits and Reportable Positions) Rules (Cap 571Y)

Appendix A1 – Marked-up changes of proposed amendments to the Rules

Appendix A2 – Clean version of the amended Rules

Appendix A1

Securities and Futures (Contracts Limits and Reportable Positions) Rules

(Cap. 571, section 35(1))

(*Enacting provision omitted—E.R. 1 of 2012*)

[1 April 2003] L.N. 12 of 2003

(*Format changes—E.R. 1 of 2012*)

1. (*Omitted as spent—E.R. 1 of 2012*)

2. Interpretation

(1) In these Rules, unless the context otherwise requires—

adequate financial capability (充足財政能力), in relation to an exchange participant or an affiliate of an exchange participant, means any one of the exchange participant, the affiliate or their holding company, has—

- (a) a net asset value of not less than \$5 billion as set out in its latest audited financial statements; or
- (b) a qualifying credit rating; (*L.N. 44 of 2017*)

affiliate (聯屬公司), in relation to an exchange participant, means any corporation belonging to the same group of companies as the exchange participant; (*L.N. 44 of 2017*)

constitutive documents (組成文件), in relation to a collective investment scheme, means the principal documents governing the establishment of the scheme; (*L.N. 228 of 2015*)

corporate fund (法團基金) means a collective investment scheme constituted as a corporation including an open-ended fund company;

entity (實體) means—

- (a) a natural person;
- (b) a body of persons; or
- (c) a legal arrangement, including—
 - (i) a corporation;
 - (ii) a trust; and
 - (iii) a sub-fund of an umbrella fund;

exchange traded fund (交易所買賣基金) means an open-ended collective investment scheme the shares or units of which are listed or traded on a recognized stock market; (*L.N. 228 of 2015*)

HKFECC (期貨結算公司) means the recognized clearing house known as HKFE Clearing Corporation Limited;

Listing Rules (《上市規則》) means the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited made by the Stock Exchange Company;

offering document (要約文件), in relation to a collective investment scheme, means a document—

- (a) inviting participation in the scheme by prospective shareholders or prospective unit holders of the scheme; and

(b) containing information relating to the establishment or administration of the scheme; (*L.N. 228 of 2015*)

open-ended collective investment scheme (開放式集體投資計劃) means a collective investment scheme the shares or units of which may be repurchased or redeemed at the request of any of its shareholders or unit holders—

- (a) at a price calculated wholly or mainly by reference to the net asset value of the scheme; and
- (b) in accordance with the frequency for repurchase or redemption, requirements and procedures set out in the offering document or constitutive documents of the scheme; (*L.N. 228 of 2015*)

prescribed limit (訂明上限), in relation to a futures contract or a stock options contract, means the limit on the number of contracts prescribed for it under section 5;

reportable position (須申報的持倉量) means an open position in futures contracts or stock options contracts the number of which is—

- (a) in the case of a futures contract specified in column 2 of Schedule 1, in excess of that specified opposite to it in column 4 of that Schedule; and
- (b) in the case of a stock options contract specified in column 2 of Schedule 2, in excess of that specified opposite to it in column 4 of that Schedule; (*9 of 2012 s. 55; L.N. 44 of 2017*)

scheme property (計劃財產), in relation to a unit trust or a corporate fund, means the property under the unit trust or the corporate fund (as the case may be);

SEOCH (期權結算公司) means the recognized clearing house known as The SEHK Options Clearing House Limited;

specified contract (指明合約) means any of the following futures contracts—

- (a) Hang Seng Index futures contracts and options contracts;
- (b) Hang Seng China Enterprises Index futures contracts and options contracts; (*L.N. 44 of 2017*)
- (c) Weekly Hang Seng Index options contracts;
- (d) Weekly Hang Seng China Enterprises Index options contracts;
- (e) Hang Seng Index Futures options contracts;
- (f) Hang Seng China Enterprises Index Futures options contracts;
- (g) Hang Seng TECH Index futures contracts and options contracts;

specified percentage (指明百分率) means 300%: (*L.N. 44 of 2017*)

(*9 of 2012 s. 55*)

sub-fund (子基金), in relation to an umbrella fund, means a separate part of the scheme property of the umbrella fund where assets of the part belong exclusively to the part and cannot be used to discharge the liabilities of, or the claims against, any other entity including the umbrella fund and any other part of the scheme property;

umbrella corporate fund (傘子法團基金) means an umbrella fund constituted as a corporation including an open-ended fund company;

umbrella fund (傘子基金) means a collective investment scheme whose constitutive documents provide for the division of its scheme property into separate parts and may be constituted under the laws of Hong Kong or elsewhere;

umbrella unit trust (傘子單位信託) means an umbrella fund constituted as a unit trust;

unit trust (單位信託), means a collective investment scheme that is a trust established for the purpose, or having the effect, of providing, for persons having funds available for investment, facilities for the participation or receipt by them, as beneficiaries under the trust, in any profits, income or other returns arising from the acquisition, holding, management or disposal of any property whatsoever.

(2) For the purposes of these Rules, a reference to control, in relation to futures contracts or stock options contracts, shall be construed as a reference to control of such futures contracts or stock options contracts, either directly or indirectly.

(3) For the purposes of these Rules, if a collective investment scheme is constituted in the form of an umbrella fund with one or more sub-funds, each sub-fund is to be regarded as a separate entity in relation to the umbrella fund and any of the other sub-funds of the umbrella fund.

3. Application

These Rules apply to futures contracts and stock options contracts that are traded through the facilities of a recognized exchange company in accordance with the rules of the recognized exchange company.

4. Restrictions on number of contracts held or controlled

(1) No person, other than a person referred to in subsections (2) and (3), may hold or control futures contracts or stock options contracts in excess of the prescribed limit. (*L.N. 44 of 2017*)

(2) A person specified in section 4A may be authorized under the rules of the recognized exchange company concerned to hold or control futures contracts or stock options contracts in excess of the prescribed limit. (*L.N. 44 of 2017*)

(3) A person may hold or control a futures contract or stock options contract in excess of the prescribed limit if the person is authorized by the Commission to do so under section 4B, 4C, 4D, 4E or 4E4F. (*L.N. 44 of 2017*)

(4) The Commission may, under section 4B, 4C, 4D, 4E or 4E4F, authorize a person to hold or control a futures contract or stock options contract in excess of the prescribed limit—

(a) except in circumstances where holding or controlling the excess for which authorization is sought may be authorized under the rules of the recognized exchange company concerned as referred to in subsection (2);

(b) only if the Commission is satisfied that the excess would not be prejudicial to the interest of the investing public having regard to the prescribed limit and the liquidity of the futures contract or stock options contract in question; and

(c) by giving the person a notice of authorization in writing. (*L.N. 44 of 2017*)

(5) An authorization granted under section 4B, 4C, 4D, 4E or 4E4F—

(a) subject to paragraph (b), is valid for the period (if any) that the Commission may specify in the notice of authorization given under subsection (4)(c);

(b) may be withdrawn by the Commission, at any time, by at least 5 business days' notice in writing to the person authorized and, where the person authorized is an affiliate of an exchange participant, also to the exchange participant; and

(c) is subject to any reasonable conditions that the Commission may specify in the notice of authorization given under subsection (4)(c) and the Commission may, at any time, by at least 5 business days' notice in writing to the person authorized and, where the person authorized is an affiliate of an exchange participant, also to the exchange participant, amend or revoke any condition or impose new conditions as may be reasonable in the circumstances. (*L.N. 44 of 2017*)

(6)-(10) (*Repealed L.N. 44 of 2017*)

(11) (*Added L.N. 198 of 2007 and repealed L.N. 241 of 2007*)

4A. Authorization under rules of recognized exchange company to hold or control contracts in excess of prescribed limit

A person who may be authorized for the purposes of section 4(2) is—

- (a) a person registered with the Futures Exchange Company for the purpose of performing market making or liquidity providing activities in respect of futures contracts in accordance with its rules;
- (b) a person registered with the Stock Exchange Company for the purpose of performing market making or liquidity providing activities, in accordance with its rules—
 - (i) in respect of stock options contracts; or
 - (ii) in respect of exchange traded funds, where the person holds or controls futures contracts or stock options contracts in the course of hedging the risks arising from performing market making or liquidity providing activities;
- (c) an issuer of securities listed under Chapter 15A of the Listing Rules who holds or controls futures contracts or stock options contracts in the course of hedging the risks of positions previously acquired in such listed securities for the purpose of performing liquidity providing activities in respect of such listed securities; ~~or~~
- (d) a related corporation of an issuer of securities listed under Chapter 15A of the Listing Rules, where the related corporation holds or controls futures contracts or stock options contracts in the course of hedging the risks of positions previously acquired in such listed securities for the purpose of performing liquidity providing activities in respect of such listed securities ~~; or~~ (*L.N. 44 of 2017*)
- (e) a clearing participant of HKFECC or SEOCH who clears futures contracts or stock options contracts for a person who is—
 - (i) specified in subsections (a) to (d); and
 - (ii) authorized under the rules of the recognized exchange company concerned to hold or control futures contracts or stock options contracts in excess of the prescribed limit.

4B. Authorization by Commission to hold or control contracts in excess of prescribed limit in special circumstances

Subject to section 4(4)(a) and (b), the Commission may authorize a person to hold or control a futures contract or stock options contract in excess of the prescribed limit if the Commission is satisfied that there are special circumstances which warrant the person holding or controlling the excess. (*L.N. 44 of 2017*)

4C. Authorization by Commission to hold or control contracts in excess of prescribed limit for purposes of facilitating provision of services to clients

- (1) Subject to subsection (2) and section 4(4)(a) and (b), the Commission may authorize an exchange participant or an affiliate of an exchange participant to hold or control a specified contract in excess of the prescribed limit by up to the specified percentage.
- (2) The Commission must not authorize an exchange participant or an affiliate of an exchange participant to hold or control a specified contract in excess of the prescribed limit unless the exchange participant satisfies the Commission that—
- (a) the exchange participant or the affiliate (as the case may be) has a relevant business need for holding or controlling the excess for which authorization is sought;
 - (b) either the exchange participant or the affiliate has adequate financial capability to cover the potential risks arising from the excess; and
 - (c) the exchange participant has effective internal control procedures and risk management systems to manage the potential risks arising from the excess.
- (3) In this section—

relevant business need (相關業務需要), in relation to an exchange participant or an affiliate of an exchange participant, means a business need that requires the exchange participant or the affiliate to engage in hedging activities to facilitate the provision of services to its clients. (L.N. 44 of 2017)

4D. Authorization by Commission to hold or control contracts in excess of prescribed limit for purposes of index arbitrage activity

- (1) Subject to subsection (2) and section 4(4)(a) and (b), the Commission may authorize an exchange participant or an affiliate of an exchange participant to hold or control a specified contract in excess of the prescribed limit by up to the specified percentage.
- (2) The Commission must not authorize an exchange participant or an affiliate of an exchange participant to hold or control a specified contract in excess of the prescribed limit unless the exchange participant satisfies the Commission that—
- (a) the exchange participant or the affiliate (as the case may be) engages in index arbitrage activities, and will, if authorization is granted, hold or control the excess for the purposes of those activities;
 - (b) either the exchange participant or the affiliate has adequate financial capability to cover the potential risks arising from the excess; and
 - (c) the exchange participant has effective internal control procedures and risk management systems to manage the potential risks arising from the excess.
- (3) In this section—

index arbitrage (指數套戥), in relation to an exchange participant or an affiliate of an exchange participant, means a trading strategy engaged in by the exchange participant or the affiliate—

- (a) involving—
 - (i) the purchase (or sale) of a stock index futures contract; or
 - (ii) the purchase (or sale) of a stock index call options contract together with the sale (or purchase) of a stock index put options contract, where both contracts have the same underlying index, expiry date and strike price;

- (b) in conjunction with the sale (or purchase) of some or all of the stocks comprised in the underlying basket of stocks used to compile the index underlying the stock index futures contract or the stock index options contracts; and
- (c) with a view to securing a profit from any difference in price between the stocks and the stock index futures contract or the stock index options contracts.(L.N. 44 of 2017)

4E. Authorization by Commission for asset manager to hold or control contracts in excess of prescribed limit for purposes of asset management activity

- (1) Subject to subsection (2) and section 4(4)(a) and (b), the Commission may authorize a person referred to in subsection (3) to hold or control a specified contract in excess of the prescribed limit by up to the specified percentage.
- (2) The Commission must not authorize a person referred to in subsection (3) to hold or control a specified contract in excess of the prescribed limit unless the person satisfies the Commission that—
 - (a) the person has a need for holding or controlling the excess for which authorization is sought, for the purposes of the asset management activity for which the person is licensed or registered; and
 - (b) the person has effective internal control procedures and risk management systems to manage the potential risks arising from the excess.

- (3) Subsection (1) applies to a person that—

- (a) is a licensed corporation that is licensed for, or a registered institution that is registered for, Type 9 regulated activity; and
 - (b) in the course of that regulated activity, manages assets having a total value of not less than \$80 billion. (L.N. 44 of 2017)

4F. Authorization by Commission for clearing participants

- (1) Subject to section 4(4)(a) and (b), the Commission may authorize a person referred to in subsection (2) to hold or control a specified contract in excess of the prescribed limit by up to the specified percentage.

- (2) Subsection (1) applies to a person that—

- (a) is a clearing participant; and
- (b) clears the specified contract for another person that has been authorized by the Commission under 4C, 4D or 4E to hold or control the specified contract in excess of the prescribed limit.

5. Prescribed limits

For the purposes of section 4(1), the limit on the number of contracts that may be held or controlled is—

- (a) in the case of a futures contract specified in column 2 of Schedule 1, that specified opposite to it in column 3 of that Schedule; and
- (b) in the case of a stock options contract specified in column 2 of Schedule 2, that specified opposite to it in column 3 of that Schedule.

6. Notice of reportable positions

- (1) AnySubject to subsection (1A), any person who holds or controls a reportable position shallmust lodge a notice in writing of that reportable position with the

recognized exchange company concerned within one business day following— (9 of 2012 s. 56)

- (a) the day on which the person first holds or controls that reportable position; and
- (b) each succeeding day on which the person continues to hold or control that reportable position.

(1A) If the reportable position held or controlled by a person is in any holiday contract, the person must lodge a notice in writing of the reportable position with the Futures Exchange Company within one holiday contract trading day following—

- (a) the day on which the person first holds or controls the reportable position; and
- (b) each succeeding day on which the person continues to hold or control the reportable position.

(1B) For the avoidance of doubt, for the purposes of subsection (1A), section 71(1)(b) and (c) of the Interpretation and General Clauses Ordinance (Cap. 1) does not apply.

(2) ASubject to subsections (3) and (4), a notice referred to in subsections

(1) shalland (1A) must be accompanied by the following information—

- (a) the number of futures contracts or stock options contracts held or controlled by the person in respect of the reportable position in each relevant contract month or option series; and
- (b) if the reportable position is held or controlled for another person—
 - (i) the identity of that person; and
 - (ii) the number of futures contracts or stock options contracts held or controlled for such person in respect of the reportable position in each relevant contract month or option series. (L.N. 35 of 2004)

(3) If a person holds or controls a reportable position in respect of a unit trust, a notice referred to in subsections (1) and (1A) must be accompanied by the following information—

- (a) the name of the unit trust; and
- (b) the number of futures contracts or stock options contracts held or controlled in respect of the unit trust for the reportable position in each relevant contract month or option series.

(4) If a person holds or controls a reportable position in respect of a sub-fund of an umbrella fund, a notice referred to in subsections (1) and (1A) must be accompanied by the following information—

- (a) the name of the sub-fund; and
- (b) the number of futures contracts or stock options contracts held or controlled in respect of the sub-fund for the reportable position in each relevant contract month or option series.

(5) In this section—

holiday contract (假期合約) means a futures contract that is determined by the Futures Exchange Company to be a “holiday trading exchange contract” in accordance with the rules of the Futures Exchange Company;

holiday contract trading day (假期合約交易日) means in relation to a holiday contract, a day determined by the Futures Exchange Company to be a day on which the holiday contract may be traded through the facilities of the Futures Exchange Company in accordance with the rules of the Futures Exchange Company.

7. Compliance by certain persons

- (1) InSubject to section 7A, in their application to a person holding or controlling futures contracts or stock options contracts for any other person, the prescribed limits and reportable positions apply separately to any futures contracts or stock options contracts held or controlled by the first person—
 - (a) for his own account; and
 - (b) for each other person.
- (2) For the purposes of subsection (1), a person shall not to be regarded as holding or controlling futures contracts or stock options contracts for another person if he has discretion in relation to those futures contracts or stock options contracts.
- (3) ForSubject to subsection (4), for the purposes of subsection (2), a person shall to be regarded as having discretion in relation to futures contracts or stock options contracts he holds or controls for another person if—
 - (a) he may originate orders to acquire or dispose of any of the futures contracts or stock options contracts under a general authorization from the other person, whether the authorization is pursuant to a written agreement, power of attorney or otherwise; and
 - (b) such authorization enables the first person to make specific acquisitions or disposals without requiring further consent or instruction from the other person.
(L.N. 35 of 2004)
- (4) A clearing participant of HKFECC or SEOCH is not to be regarded as having discretion in relation to futures contracts or stock options contracts he holds or controls for another person if the clearing participant's power to acquire or dispose of the other person's futures contracts or stock options contracts (as the case may be) may only be exercised in the event of a default in meeting any payment obligation by the other person.

7A. Compliance by persons with respect to a unit trust or a corporate fund

- (1) Subject to subsection (2), in their application to a person holding or controlling futures contracts or stock options contracts in respect of one or more unit trusts, the prescribed limits and reportable positions apply separately to any futures contracts or stock options contracts held or controlled by the person—
 - (a) for the person's own account; and
 - (b) in respect of each unit trust.
- (2) In their application to a person holding or controlling futures contracts or stock options contracts in respect of a sub-fund of an umbrella unit trust or umbrella corporate fund, the prescribed limits and reportable positions apply separately to any futures contracts or stock options contracts held or controlled by the person—
 - (a) for the person's own account; and
 - (b) in respect of each sub-fund.
- (3) For the purposes of subsections (1) and (2), the prescribed limits and reportable positions do not apply separately to any futures contracts or stock options

contracts held or controlled by the person for the person's own account and in respect of each unit trust or each sub-fund of an umbrella unit trust or umbrella corporate fund if the person has discretion in relation to those futures contracts or stock options contracts the person holds or controls in respect of the unit trust or the sub-fund (as the case may be).

- (4) For the purposes of subsection (3), a person is to be regarded as having discretion in relation to futures contracts or stock options contracts the person holds or controls in respect of a unit trust or a sub-fund of a unit trust if—
- (a) the person may originate orders to acquire or dispose of any of the futures contracts or stock options contracts under a general authorization from the trustee of the unit trust or the sub-fund, whether the authorization is pursuant to a written agreement, power of attorney or otherwise; and
 - (b) the general authorization enables the person to make specific acquisitions or disposals without requiring further consent or instruction from the trustee of the unit trust or the sub-fund.
- (5) For the purposes of subsection (3), a person is to be regarded as having discretion in relation to futures contracts or stock options contracts the person holds or controls in respect of a sub-fund of an umbrella corporate fund if—
- (a) the person may originate orders to acquire or dispose of any of the futures contracts or stock options contracts under a general authorization from the umbrella corporate fund, whether the authorization is pursuant to a written agreement, power of attorney or otherwise; and
 - (b) the general authorization enables the person to make specific acquisitions or disposals without requiring further consent or instruction from the umbrella corporate fund.
- (6) Subject to subsection (3), for the purposes of subsections (1) and (2) in determining whether the positions in any futures contracts or stock options contracts held or controlled by a person have exceeded the prescribed limits or reached the reportable positions, the person must not aggregate or net such positions which are held or controlled by the person—
- (a) for the person's own account; and
 - (b) in respect of each unit trust or each sub-fund of an umbrella unit trust or umbrella corporate fund.
- (7) For the purposes of these Rules, a unit holder is not regarded, only by virtue of the unit holder's holding one or more units in a unit trust, as holding or controlling futures contracts or stock options contracts in respect of a unit trust.

8. Penalties

Any person who, without reasonable excuse, fails to comply with section 4(1) or 6 commits an offence and is liable—

- (a) on conviction on indictment to a fine at level 6 and to imprisonment for 2 years; or
- (b) on summary conviction to a fine at level 3 and to imprisonment for 6 months.

Schedule 1

[ss. 2(1) & 5(a)]

Prescribed Limit and Reporting Level for Futures Contracts

Item	Futures contract	Prescribed limit	Reporting level
1.	Stock futures contracts on shares listed on a stock market operated by the Stock Exchange Company	5 000 open contracts for any one contract month	1 000 open contracts for any one contract month
2.	Three-Month Hong Kong Interbank Offered Rate futures contract	Nil	1 000 open contracts for any one contract month; 4 000 open contracts for all contract months
3.	One-Month Hong Kong Interbank Offered Rate futures contract	Nil	1 000 open contracts for any one contract month; 4 000 open contracts for all contract months
4.	Hang Seng Index futures contract and options contract, <u>and</u> Mini-Hang Seng Index futures contract and options contract- <u>(L.N. 44 of 2017),</u> <u>Weekly Hang Seng Index options contract, Hang Seng Index Futures options contract,</u> <u>Hang Seng Index (Gross Total Return Index) futures contract, and Hang Seng Index (Net Total Return Index) futures contract</u>	10 000 long or short position delta limit for all contract months <u>and contract weeks</u> combined, provided that the position delta for the Mini-Hang Seng Index futures contracts or Mini-Hang Seng Index options contracts must not at any time exceed 2 000 long or short for all contract months combined	500 open Hang Seng Index futures contracts for any one contract month; 500 open Hang Seng Index options contracts for any one series; 2 500 open Mini-Hang Seng Index futures contracts for any one contract month <u>and</u> ; 2 500 open Mini-Hang Seng Index options contracts for any one series; <u>500 open Weekly Hang Seng Index options contracts for any one series, 500 open Hang Seng Index Futures options contracts for any one series, 500 open Hang Seng Index (Gross Total Return Index) futures contracts for</u>

Item	Futures contract	Prescribed limit	Reporting level
5.	<p>Hang Seng China Enterprises Index futures contract and options contract, <u>and</u> Mini-Hang Seng China Enterprises Index futures contract and options contract- <u>(L.N. 44 of 2017),</u> <u>Weekly Hang Seng China Enterprises Index options contract, Hang Seng China Enterprises Index Futures options contract, Hang Seng China Enterprises Index (Gross Total Return Index) futures contract, and Hang Seng China Enterprises Index (Net Total Return Index) futures contract</u></p>	<p>12 000 long or short position delta limit for all contract months <u>and contract weeks</u> combined, provided that the position delta for the Mini-Hang Seng China Enterprises Index futures contracts or Mini-Hang Seng China Enterprises Index options contracts must not at any time exceed 2 400 long or short for all contract months combined</p>	<p>500 open Hang Seng China Enterprises Index futures contracts for any one contract month; 500 open Hang Seng China Enterprises Index options contracts for any one series; 2 500 open Mini-Hang Seng China Enterprises Index futures contracts for any one contract month <u>and</u> 500 open Weekly Hang Seng China Enterprises Index options contracts for any one series, 500 open Hang Seng China Enterprises Index Futures options contracts for any one series, 500 open Hang Seng China Enterprises Index (Gross Total Return Index) futures contracts for any one contract month and 500 open Hang Seng China Enterprises Index (Net Total Return Index) futures contracts for any one contract month</p>

Item	Futures contract	Prescribed limit	Reporting level
6.	Hang Seng China H-Financials Index futures contract	10 000 long or short position delta limit for all contract months combined	500 open contracts for any one contract month
7.	Gold futures contract	Nil	500 open contracts for any one contract month
8.	Three Year Exchange Fund Note (EFN) futures contract	5 000 open contracts for any one contract month except that the limit for the spot month contract during the last 6 trading days is 1 000 open contracts	1 000 open contracts for any one contract month except that the reportable position for the spot month contract during the last 6 trading days is 200 open contracts
9.	FTSE/Xinhua China 25 Index futures contract and options contract <i>(L.N. 44 of 2017)</i>	6 000 long or short position delta limit for all contract months combined	500 open FTSE/Xinhua China 25 Index futures contracts for any one contract month and 500 open FTSE/Xinhua China 25 Index options contracts for any one series
10.	HSI Dividend Point Index futures contract	Nil	1 000 open contracts for any one contract month
11.	HSCEI Dividend Point Index futures contract	Nil	1 000 open contracts for any one contract month
12.	HSI Volatility Index futures contract <i>(L.N. 13 of 2013)</i>	10 000 open contracts for any one contract month	1 000 open contracts for any one contract month
13.	US Dollar vs Renminbi (Hong Kong) futures contract and options contract, <u>Mini US Dollar vs Renminbi (Hong Kong) futures contract</u> , and Renminbi (Hong Kong) vs US Dollar	<u>830</u> 000 long or short position delta limit for all contract months combined, provided that the position delta for the spot month US Dollar vs Renminbi (Hong Kong) futures contracts	500 open US Dollar vs Renminbi (Hong Kong) futures contracts for any one contract month; 500 open US Dollar vs Renminbi (Hong Kong) options contracts for any one series; <u>2 500 open Mini US Dollar</u>

Item	Futures contract	Prescribed limit	Reporting level
	futures contract- <i>(L.N. 44 of 2017)</i>	and the spot month US Dollar vs Renminbi (Hong Kong) options contracts combined during the last 5 trading days must not exceed 2 150 000 long or short	<u>vs Renminbi (Hong Kong) futures contracts for any one contract month</u> and 500 open Renminbi (Hong Kong) vs US Dollar futures contracts for any one contract month
14.	London Copper Mini futures contract <i>(L.N. 228 of 2015)</i>	50 000 net long or short contracts for all contract months combined	500 open contracts for any one contract month
15.	London Aluminium Mini futures contract <i>(L.N. 228 of 2015)</i>	25 000 net long or short contracts for all contract months combined	500 open contracts for any one contract month
16.	London Zinc Mini futures contract <i>(L.N. 228 of 2015)</i>	25 000 net long or short contracts for all contract months combined	500 open contracts for any one contract month
17.	Stock futures contracts on shares or units of exchange traded funds <i>(L.N. 228 of 2015)</i>	5 000 open contracts for any one contract month	1 000 open contracts for any one contract month
18.	London Nickel Mini futures contract <i>(L.N. 44 of 2017)</i>	50 000 net long or short contracts for all contract months combined	500 open contracts for any one contract month
19.	London Lead Mini futures contract <i>(L.N. 44 of 2017)</i>	25 000 net long or short contracts for all contract months combined	500 open contracts for any one contract month
20.	London Tin Mini futures contract <i>(L.N. 44 of 2017)</i>	15 000 net long or short contracts for all contract months combined	500 open contracts for any one contract month
21.	<u>Hang Seng TECH Index futures contract and options contract</u>	<u>21 000 long or short position delta limit for all contract months combined</u>	<u>500 open Hang Seng TECH Index futures contracts for any one contract month and 500 open Hang Seng TECH Index options</u>

Item	Futures contract	Prescribed limit	Reporting level
22.	MSCI China A 50 Connect (USD) Index futures contract	28 000 net long or short contracts for all contract months combined	contracts for any one series 500 open contracts for any one contract month

(Schedule 1 replaced L.N. 117 of 2011)

Schedule 2

[ss. 2(1) & 5(b)]

Prescribed Limit and Reporting Level for Stock Options Contracts

Item	Stock options contract	Prescribed limit	Reporting level
1.	Stock options contracts on shares listed on a stock market operated by the Stock Exchange Company	150 000 open contracts per option class in any one market direction for all expiry months combined <i>(L.N. 44 of 2017)</i>	1 000 open contracts per option class per expiry month
2.	Stock options contracts on shares or units of exchange traded funds <i>(L.N. 228 of 2015)</i>	150 000 open contracts per option class in any one market direction for all expiry months combined <i>(L.N. 44 of 2017)</i>	1 000 open contracts per option class per expiry month

3-4. *(Repealed L.N. 228 of 2015)*

(Schedule 2 replaced L.N. 117 of 2011)

Appendix A2

Securities and Futures (Contracts Limits and Reportable Positions) Rules

(Cap. 571, section 35(1))

(*Enacting provision omitted—E.R. 1 of 2012*)

[1 April 2003] L.N. 12 of 2003

(*Format changes—E.R. 1 of 2012*)

1. (*Omitted as spent—E.R. 1 of 2012*)

2. Interpretation

(1) In these Rules, unless the context otherwise requires—

adequate financial capability (充足財政能力), in relation to an exchange participant or an affiliate of an exchange participant, means any one of the exchange participant, the affiliate or their holding company, has—

- (a) a net asset value of not less than \$5 billion as set out in its latest audited financial statements; or
- (b) a qualifying credit rating; (*L.N. 44 of 2017*)

affiliate (聯屬公司), in relation to an exchange participant, means any corporation belonging to the same group of companies as the exchange participant; (*L.N. 44 of 2017*)

constitutive documents (組成文件), in relation to a collective investment scheme, means the principal documents governing the establishment of the scheme; (*L.N. 228 of 2015*)

corporate fund (法團基金) means a collective investment scheme constituted as a corporation including an open-ended fund company;

entity (實體) means—

- (a) a natural person;
- (b) a body of persons; or
- (c) a legal arrangement, including—
 - (i) a corporation;
 - (ii) a trust; and
 - (iii) a sub-fund of an umbrella fund;

exchange traded fund (交易所買賣基金) means an open-ended collective investment scheme the shares or units of which are listed or traded on a recognized stock market; (*L.N. 228 of 2015*)

HKFECC (期貨結算公司) means the recognized clearing house known as HKFE Clearing Corporation Limited;

Listing Rules (《上市規則》) means the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited made by the Stock Exchange Company;

offering document (要約文件), in relation to a collective investment scheme, means a document—

- (a) inviting participation in the scheme by prospective shareholders or prospective unit holders of the scheme; and

(b) containing information relating to the establishment or administration of the scheme; (*L.N. 228 of 2015*)

open-ended collective investment scheme (開放式集體投資計劃) means a collective investment scheme the shares or units of which may be repurchased or redeemed at the request of any of its shareholders or unit holders—

- (a) at a price calculated wholly or mainly by reference to the net asset value of the scheme; and
- (b) in accordance with the frequency for repurchase or redemption, requirements and procedures set out in the offering document or constitutive documents of the scheme; (*L.N. 228 of 2015*)

prescribed limit (訂明上限), in relation to a futures contract or a stock options contract, means the limit on the number of contracts prescribed for it under section 5;

reportable position (須申報的持倉量) means an open position in futures contracts or stock options contracts the number of which is—

- (a) in the case of a futures contract specified in column 2 of Schedule 1, in excess of that specified opposite to it in column 4 of that Schedule; and
- (b) in the case of a stock options contract specified in column 2 of Schedule 2, in excess of that specified opposite to it in column 4 of that Schedule; (*9 of 2012 s. 55; L.N. 44 of 2017*)

scheme property (計劃財產), in relation to a unit trust or a corporate fund, means the property under the unit trust or the corporate fund (as the case may be);

SEOCH (期權結算公司) means the recognized clearing house known as The SEHK Options Clearing House Limited;

specified contract (指明合約) means any of the following futures contracts—

- (a) Hang Seng Index futures contracts and options contracts;
- (b) Hang Seng China Enterprises Index futures contracts and options contracts; (*L.N. 44 of 2017*)
- (c) Weekly Hang Seng Index options contracts;
- (d) Weekly Hang Seng China Enterprises Index options contracts;
- (e) Hang Seng Index Futures options contracts;
- (f) Hang Seng China Enterprises Index Futures options contracts;
- (g) Hang Seng TECH Index futures contracts and options contracts;

specified percentage (指明百分率) means 300%; (*L.N. 44 of 2017*)

(*9 of 2012 s. 55*)

sub-fund (子基金), in relation to an umbrella fund, means a separate part of the scheme property of the umbrella fund where assets of the part belong exclusively to the part and cannot be used to discharge the liabilities of, or the claims against, any other entity including the umbrella fund and any other part of the scheme property;

umbrella corporate fund (傘子法團基金) means an umbrella fund constituted as a corporation including an open-ended fund company;

umbrella fund (傘子基金) means a collective investment scheme whose constitutive documents provide for the division of its scheme property into separate parts and may be constituted under the laws of Hong Kong or elsewhere;

umbrella unit trust (傘子單位信託) means an umbrella fund constituted as a unit trust;

unit trust (單位信託), means a collective investment scheme that is a trust established for the purpose, or having the effect, of providing, for persons having funds available for investment, facilities for the participation or receipt by them, as beneficiaries under the trust, in any profits, income or other returns arising from the acquisition, holding, management or disposal of any property whatsoever.

(2) For the purposes of these Rules, a reference to control, in relation to futures contracts or stock options contracts, shall be construed as a reference to control of such futures contracts or stock options contracts, either directly or indirectly.

(3) For the purposes of these Rules, if a collective investment scheme is constituted in the form of an umbrella fund with one or more sub-funds, each sub-fund is to be regarded as a separate entity in relation to the umbrella fund and any of the other sub-funds of the umbrella fund.

3. Application

These Rules apply to futures contracts and stock options contracts that are traded through the facilities of a recognized exchange company in accordance with the rules of the recognized exchange company.

4. Restrictions on number of contracts held or controlled

(1) No person, other than a person referred to in subsections (2) and (3), may hold or control futures contracts or stock options contracts in excess of the prescribed limit. (*L.N. 44 of 2017*)

(2) A person specified in section 4A may be authorized under the rules of the recognized exchange company concerned to hold or control futures contracts or stock options contracts in excess of the prescribed limit. (*L.N. 44 of 2017*)

(3) A person may hold or control a futures contract or stock options contract in excess of the prescribed limit if the person is authorized by the Commission to do so under section 4B, 4C, 4D, 4E or 4F. (*L.N. 44 of 2017*)

(4) The Commission may, under section 4B, 4C, 4D, 4E or 4F, authorize a person to hold or control a futures contract or stock options contract in excess of the prescribed limit—

(a) except in circumstances where holding or controlling the excess for which authorization is sought may be authorized under the rules of the recognized exchange company concerned as referred to in subsection (2);

(b) only if the Commission is satisfied that the excess would not be prejudicial to the interest of the investing public having regard to the prescribed limit and the liquidity of the futures contract or stock options contract in question; and

(c) by giving the person a notice of authorization in writing. (*L.N. 44 of 2017*)

(5) An authorization granted under section 4B, 4C, 4D, 4E or 4F—

(a) subject to paragraph (b), is valid for the period (if any) that the Commission may specify in the notice of authorization given under subsection (4)(c);

(b) may be withdrawn by the Commission, at any time, by at least 5 business days' notice in writing to the person authorized and, where the person authorized is an affiliate of an exchange participant, also to the exchange participant; and

(c) is subject to any reasonable conditions that the Commission may specify in the notice of authorization given under subsection (4)(c) and the Commission may, at any time, by at least 5 business days' notice in writing to the person authorized and, where the person authorized is an affiliate of an exchange participant, also to the exchange participant, amend or revoke any condition or impose new conditions as may be reasonable in the circumstances. (*L.N. 44 of 2017*)

(6)-(10) (*Repealed L.N. 44 of 2017*)

(11) (*Added L.N. 198 of 2007 and repealed L.N. 241 of 2007*)

4A. Authorization under rules of recognized exchange company to hold or control contracts in excess of prescribed limit

A person who may be authorized for the purposes of section 4(2) is—

- (a) a person registered with the Futures Exchange Company for the purpose of performing market making or liquidity providing activities in respect of futures contracts in accordance with its rules;
- (b) a person registered with the Stock Exchange Company for the purpose of performing market making or liquidity providing activities, in accordance with its rules—
 - (i) in respect of stock options contracts; or
 - (ii) in respect of exchange traded funds, where the person holds or controls futures contracts or stock options contracts in the course of hedging the risks arising from performing market making or liquidity providing activities;
- (c) an issuer of securities listed under Chapter 15A of the Listing Rules who holds or controls futures contracts or stock options contracts in the course of hedging the risks of positions previously acquired in such listed securities for the purpose of performing liquidity providing activities in respect of such listed securities;
- (d) a related corporation of an issuer of securities listed under Chapter 15A of the Listing Rules, where the related corporation holds or controls futures contracts or stock options contracts in the course of hedging the risks of positions previously acquired in such listed securities for the purpose of performing liquidity providing activities in respect of such listed securities; or (*L.N. 44 of 2017*)
- (e) a clearing participant of HKFECC or SEOCH who clears futures contracts or stock options contracts for a person who is—
 - (i) specified in subsections (a) to (d); and
 - (ii) authorized under the rules of the recognized exchange company concerned to hold or control futures contracts or stock options contracts in excess of the prescribed limit.

4B. Authorization by Commission to hold or control contracts in excess of prescribed limit in special circumstances

Subject to section 4(4)(a) and (b), the Commission may authorize a person to hold or control a futures contract or stock options contract in excess of the prescribed limit if the Commission is satisfied that there are special circumstances which warrant the person holding or controlling the excess. (*L.N. 44 of 2017*)

4C. Authorization by Commission to hold or control contracts in excess of prescribed limit for purposes of facilitating provision of services to clients

- (1) Subject to subsection (2) and section 4(4)(a) and (b), the Commission may authorize an exchange participant or an affiliate of an exchange participant to hold or control a specified contract in excess of the prescribed limit by up to the specified percentage.
- (2) The Commission must not authorize an exchange participant or an affiliate of an exchange participant to hold or control a specified contract in excess of the prescribed limit unless the exchange participant satisfies the Commission that—
- (a) the exchange participant or the affiliate (as the case may be) has a relevant business need for holding or controlling the excess for which authorization is sought;
 - (b) either the exchange participant or the affiliate has adequate financial capability to cover the potential risks arising from the excess; and
 - (c) the exchange participant has effective internal control procedures and risk management systems to manage the potential risks arising from the excess.
- (3) In this section—

relevant business need (相關業務需要), in relation to an exchange participant or an affiliate of an exchange participant, means a business need that requires the exchange participant or the affiliate to engage in hedging activities to facilitate the provision of services to its clients. (L.N. 44 of 2017)

4D. Authorization by Commission to hold or control contracts in excess of prescribed limit for purposes of index arbitrage activity

- (1) Subject to subsection (2) and section 4(4)(a) and (b), the Commission may authorize an exchange participant or an affiliate of an exchange participant to hold or control a specified contract in excess of the prescribed limit by up to the specified percentage.
- (2) The Commission must not authorize an exchange participant or an affiliate of an exchange participant to hold or control a specified contract in excess of the prescribed limit unless the exchange participant satisfies the Commission that—
- (a) the exchange participant or the affiliate (as the case may be) engages in index arbitrage activities, and will, if authorization is granted, hold or control the excess for the purposes of those activities;
 - (b) either the exchange participant or the affiliate has adequate financial capability to cover the potential risks arising from the excess; and
 - (c) the exchange participant has effective internal control procedures and risk management systems to manage the potential risks arising from the excess.
- (3) In this section—

index arbitrage (指數套戥), in relation to an exchange participant or an affiliate of an exchange participant, means a trading strategy engaged in by the exchange participant or the affiliate—

- (a) involving—
 - (i) the purchase (or sale) of a stock index futures contract; or
 - (ii) the purchase (or sale) of a stock index call options contract together with the sale (or purchase) of a stock index put options contract, where both contracts have the same underlying index, expiry date and strike price;

- (b) in conjunction with the sale (or purchase) of some or all of the stocks comprised in the underlying basket of stocks used to compile the index underlying the stock index futures contract or the stock index options contracts; and
- (c) with a view to securing a profit from any difference in price between the stocks and the stock index futures contract or the stock index options contracts. (*L.N. 44 of 2017*)

4E. Authorization by Commission for asset manager to hold or control contracts in excess of prescribed limit for purposes of asset management activity

- (1) Subject to subsection (2) and section 4(4)(a) and (b), the Commission may authorize a person referred to in subsection (3) to hold or control a specified contract in excess of the prescribed limit by up to the specified percentage.
- (2) The Commission must not authorize a person referred to in subsection (3) to hold or control a specified contract in excess of the prescribed limit unless the person satisfies the Commission that—
 - (a) the person has a need for holding or controlling the excess for which authorization is sought, for the purposes of the asset management activity for which the person is licensed or registered; and
 - (b) the person has effective internal control procedures and risk management systems to manage the potential risks arising from the excess.

- (3) Subsection (1) applies to a person that—

- (a) is a licensed corporation that is licensed for, or a registered institution that is registered for, Type 9 regulated activity; and
 - (b) in the course of that regulated activity, manages assets having a total value of not less than \$80 billion. (*L.N. 44 of 2017*)

4F. Authorization by Commission for clearing participants

- (1) Subject to section 4(4)(a) and (b), the Commission may authorize a person referred to in subsection (2) to hold or control a specified contract in excess of the prescribed limit by up to the specified percentage.
- (2) Subsection (1) applies to a person that—
 - (a) is a clearing participant; and
 - (b) clears the specified contract for another person that has been authorized by the Commission under 4C, 4D or 4E to hold or control the specified contract in excess of the prescribed limit.

5. Prescribed limits

For the purposes of section 4(1), the limit on the number of contracts that may be held or controlled is—

- (a) in the case of a futures contract specified in column 2 of Schedule 1, that specified opposite to it in column 3 of that Schedule; and
- (b) in the case of a stock options contract specified in column 2 of Schedule 2, that specified opposite to it in column 3 of that Schedule.

6. Notice of reportable positions

- (1) Subject to subsection (1A), any person who holds or controls a reportable position must lodge a notice in writing of that reportable position with the recognized exchange company concerned within one business day following— (*9 of 2012 s. 56*)

- (a) the day on which the person first holds or controls that reportable position;
and
 - (b) each succeeding day on which the person continues to hold or control that reportable position.
- (1A) If the reportable position held or controlled by a person is in any holiday contract, the person must lodge a notice in writing of the reportable position with the Futures Exchange Company within one holiday contract trading day following—
 - (a) the day on which the person first holds or controls the reportable position;
and
 - (b) each succeeding day on which the person continues to hold or control the reportable position.
- (1B) For the avoidance of doubt, for the purposes of subsection (1A), section 71(1)(b) and (c) of the Interpretation and General Clauses Ordinance (Cap. 1) does not apply.
- (2) Subject to subsections (3) and (4), a notice referred to in subsections (1) and (1A) must be accompanied by the following information—
 - (a) the number of futures contracts or stock options contracts held or controlled by the person in respect of the reportable position in each relevant contract month or option series; and
 - (b) if the reportable position is held or controlled for another person—
 - (i) the identity of that person; and
 - (ii) the number of futures contracts or stock options contracts held or controlled for such person in respect of the reportable position in each relevant contract month or option series. (*L.N. 35 of 2004*)
- (3) If a person holds or controls a reportable position in respect of a unit trust, a notice referred to in subsections (1) and (1A) must be accompanied by the following information—
 - (a) the name of the unit trust; and
 - (b) the number of futures contracts or stock options contracts held or controlled in respect of the unit trust for the reportable position in each relevant contract month or option series.
- (4) If a person holds or controls a reportable position in respect of a sub-fund of an umbrella fund, a notice referred to in subsections (1) and (1A) must be accompanied by the following information—
 - (a) the name of the sub-fund; and
 - (b) the number of futures contracts or stock options contracts held or controlled in respect of the sub-fund for the reportable position in each relevant contract month or option series.
- (5) In this section—

holiday contract (假期合約) means a futures contract that is determined by the Futures Exchange Company to be a “holiday trading exchange contract” in accordance with the rules of the Futures Exchange Company;

holiday contract trading day (假期合約交易日) means in relation to a holiday contract, a day determined by the Futures Exchange Company to be a day on which the holiday contract may be traded through the facilities of the Futures

Exchange Company in accordance with the rules of the Futures Exchange Company.

7. Compliance by certain persons

- (1) Subject to section 7A, in their application to a person holding or controlling futures contracts or stock options contracts for any other person, the prescribed limits and reportable positions apply separately to any futures contracts or stock options contracts held or controlled by the first person—
 - (a) for his own account; and
 - (b) for each other person.
- (2) For the purposes of subsection (1), a person is not to be regarded as holding or controlling futures contracts or stock options contracts for another person if he has discretion in relation to those futures contracts or stock options contracts.
- (3) Subject to subsection (4), for the purposes of subsection (2), a person is to be regarded as having discretion in relation to futures contracts or stock options contracts he holds or controls for another person if—
 - (a) he may originate orders to acquire or dispose of any of the futures contracts or stock options contracts under a general authorization from the other person, whether the authorization is pursuant to a written agreement, power of attorney or otherwise; and
 - (b) such authorization enables the first person to make specific acquisitions or disposals without requiring further consent or instruction from the other person.
(L.N. 35 of 2004)
- (4) A clearing participant of HKFECC or SEOCH is not to be regarded as having discretion in relation to futures contracts or stock options contracts he holds or controls for another person if the clearing participant's power to acquire or dispose of the other person's futures contracts or stock options contracts (as the case may be) may only be exercised in the event of a default in meeting any payment obligation by the other person.

7A. Compliance by persons with respect to a unit trust or a corporate fund

- (1) Subject to subsection (2), in their application to a person holding or controlling futures contracts or stock options contracts in respect of one or more unit trusts, the prescribed limits and reportable positions apply separately to any futures contracts or stock options contracts held or controlled by the person—
 - (a) for the person's own account; and
 - (b) in respect of each unit trust.
- (2) In their application to a person holding or controlling futures contracts or stock options contracts in respect of a sub-fund of an umbrella unit trust or umbrella corporate fund, the prescribed limits and reportable positions apply separately to any futures contracts or stock options contracts held or controlled by the person—
 - (a) for the person's own account; and
 - (b) in respect of each sub-fund.
- (3) For the purposes of subsections (1) and (2), the prescribed limits and reportable positions do not apply separately to any futures contracts or stock options contracts held or controlled by the person for the person's own account and in respect of each unit trust or each sub-fund of an umbrella unit trust or umbrella corporate fund if the person has discretion in relation to those futures contracts or

stock options contracts the person holds or controls in respect of the unit trust or the sub-fund (as the case may be).

- (4) For the purposes of subsection (3), a person is to be regarded as having discretion in relation to futures contracts or stock options contracts the person holds or controls in respect of a unit trust or a sub-fund of a unit trust if—
 - (a) the person may originate orders to acquire or dispose of any of the futures contracts or stock options contracts under a general authorization from the trustee of the unit trust or the sub-fund, whether the authorization is pursuant to a written agreement, power of attorney or otherwise; and
 - (b) the general authorization enables the person to make specific acquisitions or disposals without requiring further consent or instruction from the trustee of the unit trust or the sub-fund.
- (5) For the purposes of subsection (3), a person is to be regarded as having discretion in relation to futures contracts or stock options contracts the person holds or controls in respect of a sub-fund of an umbrella corporate fund if—
 - (a) the person may originate orders to acquire or dispose of any of the futures contracts or stock options contracts under a general authorization from the umbrella corporate fund, whether the authorization is pursuant to a written agreement, power of attorney or otherwise; and
 - (b) the general authorization enables the person to make specific acquisitions or disposals without requiring further consent or instruction from the umbrella corporate fund.
- (6) Subject to subsection (3), for the purposes of subsections (1) and (2) in determining whether the positions in any futures contracts or stock options contracts held or controlled by a person have exceeded the prescribed limits or reached the reportable positions, the person must not aggregate or net such positions which are held or controlled by the person—
 - (a) for the person's own account; and
 - (b) in respect of each unit trust or each sub-fund of an umbrella unit trust or umbrella corporate fund.
- (7) For the purposes of these Rules, a unit holder is not regarded, only by virtue of the unit holder's holding one or more units in a unit trust, as holding or controlling futures contracts or stock options contracts in respect of a unit trust.

8. Penalties

Any person who, without reasonable excuse, fails to comply with section 4(1) or 6 commits an offence and is liable—

- (a) on conviction on indictment to a fine at level 6 and to imprisonment for 2 years; or
- (b) on summary conviction to a fine at level 3 and to imprisonment for 6 months.

Schedule 1

[ss. 2(1) & 5(a)]

Prescribed Limit and Reporting Level for Futures Contracts

Item	Futures contract	Prescribed limit	Reporting level
1.	Stock futures contracts on shares listed on a stock market operated by the Stock Exchange Company	5 000 open contracts for any one contract month	1 000 open contracts for any one contract month
2.	Three-Month Hong Kong Interbank Offered Rate futures contract	Nil	1 000 open contracts for any one contract month; 4 000 open contracts for all contract months
3.	One-Month Hong Kong Interbank Offered Rate futures contract	Nil	1 000 open contracts for any one contract month; 4 000 open contracts for all contract months
4.	Hang Seng Index futures contract and options contract, Mini-Hang Seng Index futures contract and options contract, Weekly Hang Seng Index options contract, Hang Seng Index Futures options contract, Hang Seng Index (Gross Total Return Index) futures contract, and Hang Seng Index (Net Total Return Index) futures contract	10 000 long or short position delta limit for all contract months and contract weeks combined, provided that the position delta for the Mini-Hang Seng Index futures contracts or Mini-Hang Seng Index options contracts must not at any time exceed 2 000 long or short for all contract months combined	500 open Hang Seng Index futures contracts for any one contract month; 500 open Hang Seng Index options contracts for any one series; 2 500 open Mini-Hang Seng Index futures contracts for any one contract month; 2 500 open Mini-Hang Seng Index options contracts for any one series; 500 open Weekly Hang Seng Index options contracts for any one series, 500 open Hang Seng Index Futures options contracts for any one series, 500 open Hang Seng Index (Gross Total Return Index) futures contracts for

Item	Futures contract	Prescribed limit	Reporting level
			any one contract month and 500 open Hang Seng Index (Net Total Return Index) futures contracts for any one contract month
5.	Hang Seng China Enterprises Index futures contract and options contract, Mini-Hang Seng China Enterprises Index futures contract and options contract, Weekly Hang Seng China Enterprises Index options contract, Hang Seng China Enterprises Index Futures options contract, Hang Seng China Enterprises Index (Gross Total Return Index) futures contract, and Hang Seng China Enterprises Index (Net Total Return Index) futures contract	12 000 long or short position delta limit for all contract months and contract weeks combined, provided that the position delta for the Mini-Hang Seng China Enterprises Index futures contracts or Mini-Hang Seng China Enterprises Index options contracts must not at any time exceed 2 400 long or short for all contract months combined	500 open Hang Seng China Enterprises Index futures contracts for any one contract month; 500 open Hang Seng China Enterprises Index options contracts for any one series; 2 500 open Mini-Hang Seng China Enterprises Index futures contracts for any one contract month; 2 500 open Mini-Hang Seng China Enterprises Index options contracts for any one series; 500 open Weekly Hang Seng China Enterprises Index options contracts for any one series, 500 open Hang Seng China Enterprises Index (Gross Total Return Index) futures contracts for any one contract month and 500 open Hang Seng China Enterprises Index (Net Total Return Index) futures contracts for any one contract month

Item	Futures contract	Prescribed limit	Reporting level
6.	Hang Seng China H-Financials Index futures contract	10 000 long or short position delta limit for all contract months combined	500 open contracts for any one contract month
7.	Gold futures contract	Nil	500 open contracts for any one contract month
8.	Three Year Exchange Fund Note (EFN) futures contract	5 000 open contracts for any one contract month except that the limit for the spot month contract during the last 6 trading days is 1 000 open contracts	1 000 open contracts for any one contract month except that the reportable position for the spot month contract during the last 6 trading days is 200 open contracts
9.	FTSE/Xinhua China 25 Index futures contract and options contract <i>(L.N. 44 of 2017)</i>	6 000 long or short position delta limit for all contract months combined	500 open FTSE/Xinhua China 25 Index futures contracts for any one contract month and 500 open FTSE/Xinhua China 25 Index options contracts for any one series
10.	HSI Dividend Point Index futures contract	Nil	1 000 open contracts for any one contract month
11.	HSCEI Dividend Point Index futures contract	Nil	1 000 open contracts for any one contract month
12.	HSI Volatility Index futures contract <i>(L.N. 13 of 2013)</i>	10 000 open contracts for any one contract month	1 000 open contracts for any one contract month
13.	US Dollar vs Renminbi (Hong Kong) futures contract and options contract, Mini US Dollar vs Renminbi (Hong Kong) futures contract, and Renminbi (Hong Kong) vs US Dollar	30 000 long or short position delta limit for all contract months combined, provided that the position delta for the spot month US Dollar vs Renminbi (Hong Kong) futures	500 open US Dollar vs Renminbi (Hong Kong) futures contracts for any one contract month; 500 open US Dollar vs Renminbi (Hong Kong) options contracts for any one series; 2 500 open Mini US Dollar

Item	Futures contract	Prescribed limit	Reporting level
	futures contract	contracts and the spot month US Dollar vs Renminbi (Hong Kong) options contracts combined during the last 5 trading days must not exceed 15 000 long or short	vs Renminbi (Hong Kong) futures contracts for any one contract month and 500 open Renminbi (Hong Kong) vs US Dollar futures contracts for any one contract month
14.	London Copper Mini futures contract <i>(L.N. 228 of 2015)</i>	50 000 net long or short contracts for all contract months combined	500 open contracts for any one contract month
15.	London Aluminium Mini futures contract <i>(L.N. 228 of 2015)</i>	25 000 net long or short contracts for all contract months combined	500 open contracts for any one contract month
16.	London Zinc Mini futures contract <i>(L.N. 228 of 2015)</i>	25 000 net long or short contracts for all contract months combined	500 open contracts for any one contract month
17.	Stock futures contracts on shares or units of exchange traded funds <i>(L.N. 228 of 2015)</i>	5 000 open contracts for any one contract month	1 000 open contracts for any one contract month
18.	London Nickel Mini futures contract <i>(L.N. 44 of 2017)</i>	50 000 net long or short contracts for all contract months combined	500 open contracts for any one contract month
19.	London Lead Mini futures contract <i>(L.N. 44 of 2017)</i>	25 000 net long or short contracts for all contract months combined	500 open contracts for any one contract month
20.	London Tin Mini futures contract <i>(L.N. 44 of 2017)</i>	15 000 net long or short contracts for all contract months combined	500 open contracts for any one contract month
21.	Hang Seng TECH Index futures contract and options contract	21 000 long or short position delta limit for all contract months combined	500 open Hang Seng TECH Index futures contracts for any one contract month and 500 open Hang Seng TECH

Item	Futures contract	Prescribed limit	Reporting level
			Index options contracts for any one series
22.	MSCI China A 50 Connect (USD) Index futures contract	28 000 net long or short contracts for all contract months combined	500 open contracts for any one contract month

(Schedule 1 replaced L.N. 117 of 2011)

Schedule 2

[ss. 2(1) & 5(b)]

Prescribed Limit and Reporting Level for Stock Options Contracts

Item	Stock options contract	Prescribed limit	Reporting level
1.	Stock options contracts on shares listed on a stock market operated by the Stock Exchange Company	150 000 open contracts per option class in any one market direction for all expiry months combined	1 000 open contracts per option class per expiry month
2.	Stock options contracts on shares or units of exchange traded funds	150 000 open contracts per option class in any one market direction for all expiry months combined	1 000 open contracts per option class per expiry month

(L.N. 44 of 2017)

(L.N. 228 of 2015)

(L.N. 44 of 2017)

3-4. (Repealed L.N. 228 of 2015)

(Schedule 2 replaced L.N. 117 of 2011)



Appendix B – Proposed amendments to the Guidance Note on Position Limits and Large Open Position Reporting Requirements



SECURITIES AND
FUTURES COMMISSION
證券及期貨事務監察委員會

Appendix B

Guidance Note on Position Limits and Large Open Position Reporting Requirements

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1. Introduction

- 1.1. Section 35(1) of the Securities and Futures Ordinance (Cap. 571) (“**SFO**”) empowers the SFC to make rules to (i) prescribe limits on the number of futures contracts¹ or options contracts² that may be held or controlled by a person; and (ii) require a person holding or controlling a reportable position to notify the recognized exchange company or the SFC³.
- 1.2. The Securities and Futures (Contracts Limits and Reportable Positions) Rules (“**the Rules**”) were made by the SFC under Section 35(1) of the SFO to prescribe limits and reportable positions applicable to futures contracts and stock options contracts traded on the recognized exchange company.
- 1.3. This Guidance Note is issued to help market participants better understand how the Rules are intended to operate in practice and explain compliance requirements of the Rules.
- 1.4. The Guidance Note is intended to clarify the SFC’s policy intent and position on issues raised by the industry and does not have the force of law. The SFC will revise the Guidance Note to clarify its position in response to market developments and to reflect legislative changes in the future.

2. Prescribed Limits on Futures and Stock Options Contracts

Prescribed limits

- 2.1. Section 4(1) of the Rules imposes restrictions on the maximum number of futures contracts or stock options contracts that may be held or controlled by a person. The prescribed limits on futures contracts⁴ and stock options contracts are specified respectively in Schedule 1 and Schedule 2 of the Rules.
- 2.2. Schedule 1 of the Rules specifies the maximum number of futures contracts for any one contract month or series that may be held or controlled by a person. In other words, the prescribed limits in this Schedule apply to individual contract months or options series. *For example, the prescribed limit on any stock futures contract is 5,000 contracts for any one contract month. If a person longs 3,000 contracts of the September futures contract and longs 2,000 contracts of the October futures contract, he will not reach the prescribed limit on this contract.*
- 2.3. The prescribed limits on certain futures contracts such as stock index futures and stock index options contracts, currency futures contracts and commodity futures contracts are calculated on a net basis for all contract months combined. Moreover,

¹ Section 35(1)(a)

² Section 35(1)(b)

³ Section 35(1)(c)

⁴ In accordance with Schedule 1 to the SFO, the definition of “futures contract” includes not only a futures contract but also an option on a contract made under the rules or conventions of a futures market. In other words, futures and options contracts traded on the Hong Kong Futures Exchange are referred to as “futures contracts” in the Rules.

for stock index futures and stock index options contracts with the same underlying index, as well as currency futures and currency options contracts with the same underlying currency pair, the futures-equivalent positions in options contracts are added to the positions in futures contracts for purposes of determining compliance with the prescribed limits. The futures-equivalent position in an options contract is the delta value⁵ of the options contract determined by the Hong Kong Futures Exchange (“HKFE”) at the close of market on each trading day multiplied by the number of contracts held or controlled.

Example :

A person holds the following positions:

- Long 8,000 September HSI futures contracts
- Short 1,000 October HSI futures contracts
- Long 2,500 November Mini-HSI futures contracts
- Long 5,000 September HSI calls with a delta value of 0.5

Since the contract value of the Mini-HSI futures contract is one-fifth of that of the HSI futures contract, 2,500 Mini-HSI futures contracts are equivalent to 500 HSI futures contracts. The futures-equivalent positions in September HSI calls are 2,500 contracts which are obtained by multiplying the delta value (0.5) by the number of contracts held (5,000 contracts). In deciding whether the person has reached the prescribed limit of 10,000 contracts, positions in all contracts are netted, i.e. 8,000 contracts (long September HSI futures contract) minus 1,000 contracts (short October HSI futures contract) plus 500 contracts (long November Mini-HSI futures contract) plus 2,500 contracts (long September HSI calls). That means the person holds a net position of 10,000 contracts and has reached the prescribed limit.

- 2.4. Schedule 2 of the Rules specifies the maximum number of stock options contracts in any one market direction⁶ for all expiry months combined that may be held or controlled by a person. For example, the prescribed limit on any stock options contract is 150,000 contracts in any one market direction. If a person holds 30,000 long calls in month A, 100,000 short calls in month B and 50,000 long puts in month C, he will reach the prescribed limit on this contract for the short market direction, but will still be able to hold 120,000 more contracts for the long market direction. (The position in the long market direction is 30,000 contracts (i.e. 30,000 long calls) and the position in the short market direction is 150,000 contracts (i.e. 100,000 short calls plus 50,000 long puts).)
- 2.5. ~~In general, Market participants should note that in addition to the prescribed limits in Schedule 1 and Schedule 2 are also reflected in rules of the HKFE and the Stock Exchange of Hong Kong (“SEHK”). Market participants should note that in addition to the prescribed limits, the HKFE and SEHK may impose other position limits on a particular contract, Exchange Participant or client where situations warrant such action.~~

⁵ Delta is the amount by which the price of an option will change for a corresponding change in price of the underlying market. Delta can be used to equate the directional risk of an option position with a position of similar size in the underlying market. For example, if a person holds 1,000 HSI options contracts (delta value of the contract is +0.6), he is long 600 deltas or in equivalent terms, 600 HSI futures contracts.

⁶ Long calls and short puts are in the same market direction; and short calls and long puts are in the same market direction.

Aggregation requirements

(This section should be read in conjunction with paragraph 5 [below](#) on Compliance by Agents.)

- 2.6. The prescribed limits apply to all positions held or controlled by any person including positions held by the person for his own account and positions belonging to other persons but under the control of such person. While the word “control” is not defined in the SFO or the Rules, there are circumstances where the SFC takes the view that a person is regarded as having control of positions as for example where a person is allowed to exercise discretion⁷ to trade or dispose of the positions independently without the day-to-day direction of the owner of the positions.
- 2.7. Notwithstanding the foregoing, the SFC accepts that the prescribed limits do not apply to a person who controls positions merely by virtue of its corporate relationship (e.g. a parent company in relation to positions held by its affiliates/subsidiaries) provided that such person does not give its affiliates/subsidiaries any day-to-day direction with respect to trading.

Penalties

- 2.8. Except as otherwise authorized by the SFC, HKFE or SEHK (please refer to paragraph 3 below), a person who contravenes Section 4(1) of the Rules without reasonable excuse is liable (i) on conviction on indictment to a fine of HK\$100,000 and to imprisonment for 2 years; or (ii) on summary conviction to a fine of HK\$10,000 and to imprisonment for 6 months.
- 2.9. In addition to any other powers and sanctions contained in the SFO or the Rules, the HKFE and SEHK may require an Exchange Participant carrying an account in which a position is in excess of the prescribed limit to take immediate steps to reduce the position below the prescribed limit pursuant to their rules. Where the HKFE or SEHK becomes aware that any person holds or controls positions in accounts with more than one Exchange Participant such that the aggregate position in all accounts exceeds the prescribed limit, the HKFE or SEHK may require any of the Exchange Participants carrying such accounts to reduce positions in the relevant accounts so that the aggregate position in all accounts will comply with the prescribed limit.

3. Authorization to Exceed Prescribed Limits

- 3.1. No person may hold or control futures contracts or stock options contracts in excess of the prescribed limits except as otherwise authorized by the HKFE or SEHK (as the case may be) in accordance with Section 4(2) of the Rules, or by the SFC in accordance with Section 4(4) of the Rules.

⁷ Sections [7\(3\)](#), [7A\(4\)](#) and [7A\(5\)](#) of the Rules explain the situations in which a person is considered to have discretion to trade or dispose of positions independently.

Authorization for excess positions by the HKFE/SEHK

- 3.2. Section 4(2) of the Rules provides that the HKFE or SEHK may authorize a person to hold or control futures contracts or stock options contracts in excess of the prescribed limits if the person is one of those described in Section 4A of the Rules.
- 3.3. In accordance with Section 4A, the following persons may be authorized by the HKFE or SEHK to hold or control excess positions:
 - (1) a person registered with the SEHK for the purpose of performing market making or liquidity providing activities in accordance with its rules (i) in respect of stock options contracts (e.g. *an Options Trading Exchange Participant holds excess positions in stock options contracts for which it is registered with the SEHK to make a market*) or (ii) in respect of exchange traded funds where the person holds or controls futures contracts or stock options contracts in the course of hedging the risks arising from performing market making or liquidity providing activities;
 - (2) a person registered with the HKFE for the purpose of performing market making or liquidity providing activities in respect of futures contracts in accordance with its rules (e.g. *an HKFE Participant holds excess positions in futures contracts for which it is registered with the HKFE to make a market*);
 - (3) an issuer of securities listed under Chapter 15A of the Listing Rules who holds or controls futures contracts or stock options contracts in the course of hedging the risks of positions previously acquired in such listed securities for the purpose of performing liquidity providing activities in respect of such listed securities (e.g. *an issuer of structured products like derivative warrants and equity-linked instruments holds excess positions in futures contracts or stock options contracts to hedge the risks of positions in the structured products issued by it*); **or**
 - (4) a related corporation⁸ of an issuer of securities listed under Chapter 15A of the Listing Rules, where the related corporation holds or controls futures contracts or stock options contracts in the course of hedging the risks of positions previously acquired in such listed securities for the purpose of performing liquidity providing activities in respect of such listed securities (e.g. *an associate of an issuer of structured products like derivative warrants and equity-linked instruments holds excess positions in futures contracts or stock options contracts to hedge the risks of its positions in the structured products issued by the issuer*); **or**
 - (5) **a Clearing Participant of HKFE Clearing Corporation Limited (“HKCC”) or The SEHK Options Clearing Limited (“SEOCH”) who provides clearing services to a person specified in paragraphs 3.3(1)-(4).**
- 3.4. A person who has the need to exceed the prescribed limits pursuant to Section 4(2) should make an application to the HKFE or SEHK (as the case may be) in accordance with its rules. The approval from the HKFE or SEHK must be received prior to entering into positions which exceed the limits.

⁸ The term “related corporation” is defined in Section 3 of Schedule 1 to the SFO.

Authorization for excess positions by the SFC

- 3.5. Section 4(4) of the Rules provides that the SFC may authorize a person to hold or control futures contracts or stock options contracts in excess of the prescribed limits if (i) special circumstances exist (Section 4B); or if the person (ii) has a relevant business need (Section 4C); (iii) carries out index arbitrage activity (Section 4D); ~~or~~ (iv) is an asset manager that meets the specified criteria (Section 4E); ~~or (v) is a Clearing Participant that clears the excess positions of a person that has been authorized by the SFC to hold or control the excess positions concerned (Section 4F)~~. Section 4(4) is however only applicable to situations falling outside Section 4(2). That is, the SFC will not accept applications which may be dealt with by the HKFE or SEHK in accordance with Section 4(2).
- 3.6. Pursuant to Section 4(4), the SFC may authorize a person to hold or control futures contracts or stock options contracts in excess of the prescribed limits under Section 4B, 4C, 4D, ~~4E~~ or ~~4E~~^{4F} by giving the person a notice of authorization if:
- (1) the person is not one of those described in Section 4A; and
 - (2) the SFC is satisfied that the excess positions would not be prejudicial to the interest of the investing public having regard to the prescribed limits and the liquidity of the futures contracts or the stock options contracts in question.

Authorization under Section 4B – in “special circumstances”

- 3.7. An authorization under Section 4B may only be granted where such person can show that there are special circumstances which warrant his holding or controlling the excess positions in question.
- 3.8. The phrase “special circumstances” is not defined in the SFO. However, the SFC considers that the reference to “special” implies that the circumstances should normally be unique or unusual (i.e. out of the ordinary) in some way. So, for example, requiring excess positions to serve a regular business need would not be regarded as constituting special circumstances.

Authorization under Section 4C – for purposes of facilitating provision of services to clients

- 3.9. An authorization under Section 4C may only be granted:
- (1) to an Exchange Participant or an affiliate of an Exchange Participant; and
 - (2) where such person has a relevant business need for the excess positions in question.
- 3.10. The phrase “relevant business need” is defined in Section 4C(3) and essentially means a need to engage in hedging activities as a result of providing client facilitation services (i.e. services to facilitate client transactions – whether conducted on exchange or off exchange, and in futures or options contracts or other products). The

definition is designed to ensure that excess positions are sought and authorized only for the purposes of helping Exchange Participants and their affiliates to better serve their clients, and not for purely proprietary trading. For instance, a client wants to buy a large number of futures contracts, but is concerned that the purchase will push up market prices materially and thus increase his execution prices. The Exchange Participant may facilitate this client's purchase of the futures contracts by selling the contracts to the client as principal over-the-counter ("OTC") and then buying the futures contracts in the exchange market throughout the day to minimize the impact on market prices and to cover the OTC position established for the client. In this case, the futures contracts traded on the exchange are the proprietary positions of the Exchange Participant resulting from client facilitation activities.

Authorization under Section 4D – for purposes of index arbitrage activity

3.11. An authorization under Section 4D may only be granted:

- (1) to an Exchange Participant or an affiliate of an Exchange Participant; and
- (2) where such person engages in index arbitrage activities and will hold or control the excess for the purposes of those activities.

3.12. The phrase "index arbitrage" is defined in Section 4D(3) to mean a trading strategy engaged in by the person-

- (a) involving (i) the purchase or sale of a stock index futures contract (***the futures contract***); or (ii) the purchase (or sale) of a stock index call options contract together with the sale (or purchase) of a stock index put options contract, where both contracts have the same underlying index, expiry date and strike price (***the options contracts***);
- (b) in conjunction with the sale or purchase of some or all of the stocks comprised in the underlying basket of stocks (***the stocks***) used to compile the index underlying the futures contract or the options contracts; and
- (c) with a view to securing a profit from any difference in price between the stocks and the futures contract or the options contracts.

The SFC accepts that "the stocks" do not necessarily include all the components stocks of the underlying index of the futures or options contracts, the SFC however expects the applicant to demonstrate that the tracking error of the stocks is immaterial.

3.13. The SFC may grant authorizations under Sections 4C and 4D to an Exchange Participant or persons who belong to a group of companies that includes an Exchange Participant. This is because Exchange Participants and their affiliates generally have a greater need for holding excess positions to provide client facilitation services. In addition, Exchange Participants are licensed corporations under the SFO and therefore the SFC can better assess whether they would have the capabilities to hold excess positions and manage the resultant risks.

- 3.14 The SFC will determine the size of excess positions to be authorized for an applicant on a case by case basis after taking into consideration various factors including the prevailing market situation. It should be noted that although the upper limit set by the specified percentage is a per applicant upper limit, the SFC will take into account any excess positions already authorized to other members within the same group as the applicant. Under Section 4(4)(b), the SFC may authorise the excess sought only if it is satisfied that the excess would not be prejudicial to the interest of the investing public having regard to the prescribed limit and the liquidity of the futures contract or stock options contract in question.
- 3.15 Additionally, the SFC may only authorize excess positions under Sections 4C and 4D if –
- (1) the Exchange Participant or affiliate in question has adequate financial capability to cover the potential risks arising from any authorized excess position; and
 - (2) the Exchange Participant in question has effective internal control procedures and risk management systems to manage such risks.

This is irrespective of whether the person authorized is the Exchange Participant or one of its affiliates.

- 3.16 The SFC will normally look to the Exchange Participant to ensure that excess positions are properly used and any resultant risks properly managed, as that is the regulated entity within the group. Consequently, the SFC will expect a single entity within the group (normally the Exchange Participant, as that is the regulated entity) to carry the relevant positions. In other words, if any member within a group (including the Exchange Participant) is authorized to hold excess positions in a particular specified contract⁹, the SFC will normally expect all of such person's holdings in that contract (i.e. not just the excess positions) to be held through an account carried by the Exchange Participant. Additionally, if the group Exchange Participant is not a clearing participant Clearing Participant (of a recognized clearing house), positions must be carried through both the group Exchange Participant and a general clearing participant Clearing Participant (of a recognized clearing house) appointed by the group Exchange Participant. The following further points should be noted also –
- (1) Positions can be carried through any affiliate, but must be carried through the group Exchange Participant at the Exchange level. Hence, if an affiliate is not an Exchange Participant but the group wants the positions to be carried through that affiliate, then the positions must be carried through both the group Exchange Participant (at the Exchange level) and that affiliate.
 - (2) It is not necessary for execution (i.e. acquisitions and disposals) to be conducted through the group Exchange Participant. Accordingly, any execution broker may be used (including the group Exchange Participant).

⁹ The term “specified contract” is defined in the Rules.

- (3) If the excess positions are to be carried through a Clearing Participant appointed by the group Exchange Participant, the Clearing Participant will need to seek authorization for excess positions by the SFC under Section 4F.

The above requirements will facilitate the SFC in monitoring compliance with the prescribed limits and any authorized excesses.

Authorization under Section 4E – for purposes of asset management activity

3.17. An authorization under Section 4E may only be granted:

- (1) to an intermediary that is (i) licensed or registered for Type 9 regulated activity under the SFO (asset manager); and (ii) manages assets having a total value (“AUM”) of not less than HK\$80 billion;
- (2) where such asset manager needs excess positions to facilitate its asset management activity; and
- (3) the asset manager has effective internal control procedures and risk management systems to manage the potential risks arising from the excess.

3.18. For the purposes of Section 4E, the AUM of an asset manager is determined as follows:

- (1) in the case that the applicant is a Licensed Corporation (“LC”) under the SFO, it is the “Total aggregate net value of assets under management” figure reported in its latest filing to the SFC under the Securities and Futures (Financial Resources) Rules; and
- (2) in the case that the applicant is a Registered Institution under the SFO, the applicant is to use the figure reported under its asset management activity in its latest filing to the Hong Kong Monetary Authority under Section 63 of the Banking Ordinance on securities related activities. This figure is to be used as the basis for further adjustment by the applicant to arrive at an adjusted figure equivalent to the “Total aggregate net value of assets under management” figure mentioned in sub-paragraph (1) above.

3.19. The SFC is mindful that any excess positions granted should be commensurate with the asset manager’s business need. Under Section 4(4)(b), the SFC may authorise the excess sought only if it is satisfied that the excess would not be prejudicial to the interest of the investing public having regard to the prescribed limit and the liquidity of the futures contract or stock options contract in question. In this regard, the SFC in determining the size of the excess position to be granted to an asset manager under Section 4E will take into account the following:

- (1) investment mandates and size of all the funds managed by the asset manager; and
- (2) the investment strategies of the asset manager.

Authorization under Section 4F – for purposes of client clearing activity

3.20. An authorization under Section 4F may only be granted:

- (1)** to a person that is a Clearing Participant of HKCC; and
- (2)** clears the excess positions for another person that has been authorised by the SFC under sections 4C, 4D or 4E to hold or control the excess positions in question.

Application process for authorizations by the SFC

3.20.3.21. An application for authorization from the SFC to hold excess positions may be submitted by the following persons:

- (1)** where authorization is sought under Section 4B, either:
 - (a)** the person acting as principal for the account(s) for which the authorization is sought; or
 - (b)** a person who acts as an agent for the principal;
- (2)** where authorization is sought under Sections 4C and 4D, the Exchange Participant concerned; and
- (3)** where authorization is sought under Section 4E, the asset manager concerned; and
- (3)(4)** where authorization is sought under Section 4F, either the Clearing Participant concerned or its clearing client.

3.21.3.22. In the case of an authorization sought under Sections 4C and 4D, although the application must be submitted by the Exchange Participant concerned, the SFC will not dictate which members of its group should take the excess positions and hence need authorization. However, where any member of a group is authorized to hold or control excess positions in respect of a particular contract, the SFC will normally expect all of its holdings in that contract (i.e. not just the excess positions) to be carried through the Exchange Participant. It follows therefore that the Exchange Participant will in any event need to be authorized under Sections 4C and 4D of the Rules.

3.22.3.23. All applications to the SFC should be made in writing to the Supervision of Markets Division of the SFC. Applications may be made on the basis of an immediate need, or in advance in anticipation of prospective needs based on past experience.

3.23.3.24. There is no prescribed format for the application. It can be a letter or any written document supported by reasons and/or supporting documents for the

application. The application must be approved by the SFC before positions in the relevant futures contracts or stock options contracts may be increased above the prescribed limit.

3.24.3.25. In the case of an application for authorization under Section 4C, the SFC will require the applicant to provide the following information:

- (a) a description of the nature of positions held or controlled (including transactions in other related markets which are an integral part of the entire portfolio);
- (b) a full and complete explanation of the needs for holding or controlling excess positions and how the excess positions will be used to support the business of the relevant Exchange Participant and (if applicable) the affiliate and such explanation to include:
 - the nature and size of the positions established, or to be established, in connection with the excess positions for which authorization is sought, and on which market (e.g. OTC market, overseas exchange markets) such positions have been, or will be executed;
 - an estimate of the maximum level of the excess positions intended to be established; and
 - the estimated duration of holding or controlling the excess positions.
- (c) details of the relevant Exchange Participant's and (if applicable) the affiliate's or their holding company's financial position, such information to be sufficient to demonstrate that the Exchange Participant or affiliate or their holding company meets the adequate financial capability requirement and should normally include at least its latest annual audited financial statements or information on its credit rating (if any);
- (d) details of the relevant Exchange Participant's internal control procedures and risk management systems, such information to be sufficient to demonstrate that the Exchange Participant has effective internal control procedures and risk management systems to manage the potential risks arising from the excess positions, and should normally include at least the following:
 - (i) a brief summary of the risk management policies and procedures that will be adopted to monitor and address the key risks connected with the excess positions (such as market risk, concentration risk, etc.), including:
 - *the counterparty due diligence process* that the Exchange Participant or its affiliate (as the case may be) will use when assessing the counterparty risk of clients who are, or will be, provided with client facilitation services by the Exchange Participant or its affiliate in relation to the excess positions held or controlled by it

- *the contingency measures that will be applied to minimize the impact of a default by the counterparties, including the procedures for dealing with the excess positions in the event of such default*
 - *the techniques that will be used to measure, monitor, control and reduce various types of risks arising as a result of the excess positions and the related position*
- (ii) a brief summary of the internal control procedures that will be put in place to ensure implementation of the risk management policies and procedures mentioned in the preceding sub-paragraph (i).

3.25-3.26. In the case of an application for authorization under Section 4D, the SFC will require the applicant to provide the following information:

- (a) the index arbitrage trading strategy and the relevant positions, which include:
- a description of how index arbitrage activities are conducted, or will be conducted, in connection with the excess positions for which authorization is sought;
 - a description of the current nature and size of the positions related to the index arbitrage trading strategy in question (including positions in other related markets which are an integral part of the index arbitrage portfolio);
 - the methodology adopted to determine the underlying stocks involved in the index arbitrage portfolio and their relative weighting of the entire portfolio;
 - the timing of execution in the stock market and the relevant stock index derivatives market;
 - an estimate of the maximum level of the excess positions intended to be established;
 - an estimate of the duration of holding or controlling the excess positions; and
 - the circumstances under which the index arbitrage portfolio will be unwound and the detailed unwinding strategy and process.
- (b) the monitoring process to ensure that the excess positions sought are executed according to the strategy described above;
- (c) information to demonstrate that the trading desk/book for index arbitrage activities is standalone;
- (d) details of the internal control measures and compliance monitoring process to prevent and detect potential misuse or abuse of the excess positions which

should include a Chinese Wall (or equivalent internal control measures) in place between the index arbitrage trading desk and other trading desks;

- (e) details of the relevant Exchange Participant's and (if applicable) the affiliate's or their holding company's financial position, such information to be sufficient to demonstrate that the Exchange Participant or affiliate or their holding company meets the adequate financial capability requirement and should normally include at least its latest annual audited financial statements or information on this credit rating (if any);
- (f) details of the relevant Exchange Participant's internal control procedures and risk management systems to demonstrate that the Exchange Participant has effective internal control procedures and risk management systems to manage the potential risks arising from the excess position, and should normally include at least the following:
 - (i) a brief summary of the risk management policies and procedures that will be adopted to monitor and address the key risks connected with the excess position (such as market risk, concentration risk, tracking error etc.). The summary should cover *the techniques that will be used to measure, monitor, control and reduce various types of risks* arising as a result of the excess positions and the related position; and
 - (ii) a brief summary of the internal control procedures that will be put in place to ensure the implementation of the risk management policies and procedures mentioned in the preceding sub-paragraph (i).

3.26.3.27. In the case of an application for authorization under Section 4E, the SFC will require the applicant to provide the following information:

- (a) a summary of the investment objectives and characteristics of each of the funds under its management and a description of the nature of positions held or controlled by each of the funds (including investments in other related markets which are an integral part of the entire portfolio);
- (b) a full and complete explanation of the needs for holding or controlling excess positions and how the excess positions will be used for asset management purposes;
- (c) an estimate of the maximum level of the excess positions intended to be established for each of the funds and an estimate of the excess positions hence required by the asset manager;
- (d) the relevant asset manager's internal control procedures and risk management systems to demonstrate that the asset manager has effective internal control procedures and risk management systems to manage the potential risks arising from the excess position, and should normally include at least the following:

- (i) a brief summary of the risk management policies and procedures that will be adopted to monitor and address the key risks connected with the excess position (such as market risk, concentration risk, etc.). The summary should cover the techniques that will be used to measure, monitor, control and reduce various types of risks arising as a result of the excess positions and the related position; and
 - (ii) a brief summary of the internal control procedures that will be put in place to ensure implementation of the risk management policies and procedures mentioned in the preceding sub-paragraph (i).
- (e) information showing that the applicant's total assets under management is not less than HK\$80 billion:
- (i) For licensed corporations, the latest filing made by the applicant to the SFC under the Securities and Futures (Financial Resources) Rules which contains a "Total aggregate net value of assets under management" figure.
 - (ii) For registered institutions, the latest filing made by the applicant to the Hong Kong Monetary Authority under Section 63 of the Banking Ordinance on securities related activities should be used as the basis for further adjustment by the applicant to arrive at a figure equivalent to the "Total aggregate net value of assets under management" figure mentioned in (i).

3.27-3.28. In the case of an application for authorization under Section 4F, the SFC will require the applicant to submit an application with information of the identity of the clearing client, the name of the specified contract that it will be clearing for the client and the excess positions that it is applying for (which will be the same as that of its clearing client). For a more efficient and streamlined application process, the clearing client may submit the application on behalf of its Clearing Participant together with its application to the SFC for excess positions made pursuant to Sections 4C – 4E.

Other considerations for authorization

3.28-3.29. Depending on the facts and circumstances of each individual case, the SFC may also request other information as it considers necessary. The SFC may also have regard to any information or material in its possession which it considers relevant.

3.29-3.30. The SFC will determine an application to hold or control excess positions on the basis of the information supplied, the relevant prescribed limits, the liquidity of the futures contracts or stock options contracts for which the authorization is sought and such other factors as the SFC deems appropriate.

3.30-3.31. As a guiding principle, the SFC will not grant an authorization for any excess if the relevant preconditions set out in the Rules are not satisfied, or if the authorization

is inconsistent with the SFC's regulatory objectives in Section 4 of the SFO, in particular:

- (1) to maintain and promote the fairness, efficiency, competitiveness, transparency and orderliness of the securities and futures industry;
- (2) to reduce systemic risks in the securities and futures industry; or
- (3) to assist the Financial Secretary in maintaining the financial stability of Hong Kong by taking appropriate steps in relation to the securities and futures industry.

3.31.3.32. The SFC may decide to approve or deny the application or impose conditions on the authorization. Conditions imposed on an authorization may be varied or revoked subsequently on at least five business days' notice. New conditions may also be imposed (Section 4(5)(c)). A notice of authorization will be provided to the applicant in writing (Section 4(4)(c)).

3.32.3.33. The SFC will endeavour to notify the applicant of its decision within four weeks after all information as requested by the SFC to support the application is provided to its full satisfaction. However, since authorizations that may be granted by the SFC under Section 4B are special cases, it may take more time for the SFC to consider and review some particular cases. A person who has the need to exceed the prescribed limits is advised to submit an application accompanied by the supporting information to the SFC as soon as practicable.

Use and evidencing use of excess positions

3.33.3.34. Excess positions authorized under Section 4C must be used to hold positions that facilitate client transactions. However, the SFC will not require that they be used in relation to a particular client transaction, or a particular client. Similarly, the SFC will not impose any limitation on the order in which excess positions are used. Example 1 in Appendix 1 further illustrates how excess positions may be used.

3.34.3.35. The SFC will expect Exchange Participants/their affiliates to evidence the use of their excess positions. To this end, the SFC will expect authorized Exchange Participants/affiliates to submit regular reports confirming/providing the following information:

- (1) the amount of excess used;
- (2) the type of clients involved;
- (3) a general description of the nature of the client transactions including their notional and market values; and
- (4) an overall description of the positions they have taken, but not details in relation to each client on an individual basis.

3.35.3.36. Excess positions authorized under Section 4D must be used solely for index arbitrage activities. Please refer to Example 2 in Appendix 1 which illustrates how excess positions may be used for index arbitrage activities. The SFC will expect

Exchange Participants/their affiliates to evidence the use of their excess positions. To this end, the SFC will expect authorized Exchange Participants/affiliates to submit regular reports confirming providing the following information:

- (1) the amount of excess used;
- (2) a general description of the size of the stock index derivatives positions used for index arbitrage activities;
- (3) details of the stock portfolio established; and
- (4) the daily risk position of the entire index arbitrage portfolio containing the stock index derivatives positions and the stock positions.

3.36.3.37. Excess positions authorized under Section 4E must be used for asset management purposes. The SFC will expect asset managers to evidence the use of excess positions. To this end, the SFC will expect the asset manager authorized to submit regular reports providing details of the following:

- (1) The amount of the excess positions used for each of the funds under its management;
- (2) The total number of futures positions held by each of the funds under its management; and
- (3) The notional value of futures positions as a percentage relative to the fund size for each of the funds under its management.

3.38. For excess positions authorized under Section 4F, the authorized Clearing Participant will be holding the excess positions for its clearing client that has been authorized by the SFC under Sections 4C or 4D or 4E. The clearing client will be required to submit quarterly reports to evidence the use of excess positions as stipulated in the above paragraphs. Since the authorization granted to the Clearing Participant would be related to the same excess positions, there is no need for the authorized Clearing Participant to submit any quarterly reports.

3.37.3.39. The SFC will normally require reports mentioned above to be submitted quarterly within two weeks of the end of the relevant quarter. However, more frequent or additional reporting requirements may be required in individual cases as necessary.

Validity and renewal of authorizations by the SFC

3.38.3.40. A person who has been authorized by the SFC under Section 4B, 4C, 4D, 4E or 4E4F should submit a new application to the SFC if he wishes to continue to hold or control the excess positions after the expiration date of the initial authorization. The new application should be submitted to the SFC no later than two months prior to the expiration date of the initial authorization. If the SFC does not grant any further authorization for the excess positions, the person will be required to close out the position in excess of the prescribed limit upon the expiration date of the initial authorization.

Withdrawal of authorizations by the SFC

3.39-3.41. The SFC may at any time withdraw an authorization granted under Section 4B, 4C, 4D, 4E or 4E4F by giving at least five business days' notice to the person (Section 4(5)(b)). Upon a withdrawal coming into effect, the authorization will cease to apply.

3.40-3.42. In determining the effective date of a withdrawal, the SFC will consider:

- (1) whether any excess positions are already held or controlled and if so, whether they are within the limits of the authorization previously granted;
- (2) when the relevant contracts are due to expire; and
- (3) whether the withdrawal may be delayed until the time of such expiry taking into account the reasons for the withdrawal.

3.41-3.43. As a guiding principle, the SFC will not normally consider withdrawing an authorization unless it believes:

- (1) one or more of the relevant preconditions set out in the Rules in respect of the authorization in question cease to exist;
- (2) the authorization ceases to be consistent with the SFC's regulatory objectives in Section 4 of the SFO; or
- (3) one or more of the conditions attached to the authorization have failed to be met and adequate steps have not been taken, or cannot be taken, to rectify the failure and avoid similar failures in future.

Appeals

3.42-3.44. A person may appeal against a decision of the SFC to refuse to authorize excess positions under Section 4B, 4C, 4D, 4E or 4E4F of the Rules to the Securities and Futures Appeals Tribunal ("Tribunal") pursuant to Section 216 of the SFO (Section 4(4)(c) and item 78 under Division 1 of Part 2 of Schedule 8 of the SFO). An application for review of the decision must be made to the Tribunal by the person against whom the decision is made within 21 days of notice of the decision. Upon review of the decision under appeal, the Tribunal may confirm, vary or set aside the decision or substitute any other decision which the Tribunal considers more appropriate or it may remit the matter to the SFC with directions to revisit the decision. For the avoidance of doubt, before the Tribunal determines otherwise, the decision of the SFC shall remain valid and the person is required to act in accordance with the decision of the SFC.

Positions held or controlled indirectly by virtue of corporate relationship

3.43-3.45. As discussed in paragraph 2.7 above, the SFC considers that the prescribed limits do not apply to a person who controls positions merely by virtue of its corporate

relationship. In view of this, if a person is permitted by the SFC to hold or control excess positions, its affiliates (including any holding company), which indirectly controls the same positions by virtue only of the corporate relationship, will not be required to seek approval from the SFC separately to control the positions.

4. Notice of Reportable Positions

Reportable positions

- 4.1. In order to facilitate the HKFE and SEHK in monitoring market activities, Section Sections 6(1) and 6(1A) of the Rules ~~requires~~ require a person holding or controlling a reportable position to notify the recognized exchange company of that reportable position in writing.
- 4.2. Reportable positions for futures contracts and stock options contracts are specified in Schedule 1 and Schedule 2 of the Rules respectively. Similar to the prescribed limits, the reportable positions for futures contracts are calculated based on the number of contracts held or controlled for a contract month or series while the reportable positions for stock options contracts are calculated based on the number of contracts held or controlled in an expiry month.
- 4.3. The aggregation requirements as mentioned in paragraphs 2.6 and 2.7 above equally apply to the reportable positions for futures contracts and stock options contracts.

Responsibilities of reporting

- 4.4. The notice of a reportable position specified in Section Sections 6(1) and 6(1A) may be submitted by:
 - (1) a person (e.g. the Exchange Participant) acting as an agent for the principal to carry the account of the reportable position; or
 - (2) the person acting as principal for the reportable position.

If one of the above parties has submitted the notice of the reportable position to the Exchange, the SFC accepts that the other parties party will not be required to notify the Exchange of the same reportable position under Section Sections 6(1) and 6(1A).

- 4.5. In other words, a person holding or controlling a reportable position can choose to submit the notice of the reportable position to the Exchange directly or through an Exchange Participant or its agent where the latter agrees to make the report on the person's behalf. However, no matter which party is chosen by the person to submit the notice to the Exchange, it is the responsibility of each person holding or controlling the reportable position to fulfill its obligations under Section Sections 6(1) and 6(1A).
- 4.6. In the event that a person holds or controls a reportable position in accounts at more than one agent, the person should have the sole responsibility to notify the Exchange of the reportable position. If the person decides to submit the notice of the reportable position to the Exchange through the agents, it should provide to one agent with its total positions held at other agents so that the agent can submit the notice of the

reportable position to the Exchange on its behalf. Alternatively, the person can ask all agents to separately report positions in each of the accounts to the Exchange even though positions in the individual accounts may not exceed the reportable level.

- 4.7. Similar to the prescribed limits, the SFC agrees that a person controlling a reportable position merely by virtue of its corporate relationship is not required to submit the notice of the reportable position to the Exchange.

Reporting requirements

- 4.8. In accordance with Sections 6(1)~~(a)~~, 6(1A) and 6(1B), the notice of reportable positions should be made within one reportingbusiness day (or in the case of holiday contacts, the next holiday contract trading day) following:

- (1) the day on which the person first holds or controls the reportable positions; and
- (2) each succeeding day on which the person continues to hold or control the reportable positions.

For the avoidance of doubt, once a person has held or controlled a reportable position, it will be required to file the notice of the reportable position to the HKFE or SEHK (as the case may be) on each reporting day even though his position remains unchanged.

- 4.9. SectionSections 6(2) – (4) of the Rules further requiresrequire that the notice of a reportable position shall be accompanied by the following information:

- (1) the number of futures contracts or stock options contracts held or controlled by the person in respect of the reportable position in each relevant contract month or option series; and
- (2) where the reportable position is held or controlled for another person (e.g. a client), the identity of that person, where it is for a unit trust or a sub-fund, the name of the unit trust or sub-fund and the number of futures contracts or stock options contracts held or controlled for such person, unit trust or sub-fund in respect of the reportable position in each relevant contract month or option series.

In respect of the information about the identity of a client, the requirements are set out in the Code of Conduct for Persons Licensed by or Registered with the Securities and Futures Commission and the Client Identity Rule Policy.

- 4.10. In the stock options market, positions held by a market maker are recorded by the SEHK Options Clearing House in a segregated clearing account. Under SEHK rules, positions held by market makers in segregated clearing accounts are treated as having been reported to the SEHK. The SFC accepts that if the segregated clearing account is used exclusively to keep positions of a single market maker, the market maker will be deemed to have fulfilled the reporting requirements as stated in Sections 6(1), 6(1A) and 6(2) of the Rules.

- 4.11. Appendix 2 provides examples to illustrate the application of the prescribed limits and reportable positions.

Other reporting requirements specified by the HKFE/SEHK

- 4.12. The HKFE and SEHK have developed more detailed reporting requirements to facilitate their monitoring of reportable positions as required under Section 6 of the Rules. These requirements include the use of a prescribed form for reporting and the specific deadline for submission of the notice of reportable positions¹⁰.
- 4.13. The HKFE and SEHK also request Exchange Participants and the person reporting to provide additional information other than those specified in Section Sections 6(2) – (4) such as (i) the account number, account name and identity of the transaction originator of a reportable position; (ii) the nature of a reportable position (i.e. for hedging, arbitrage or trading purposes); and (iii) the account type (i.e. house account, client account or market maker account). Exchange Participants should refer to the relevant position reporting procedures prescribed by the HKFE or SEHK for details.
- 4.14. In order to assess the systemic impact of large reportable positions on the market and monitor concentration risk more effectively, the HKFE and SEHK may make enquiries into transactions/positions in other markets (e.g. OTC market) underlying the reportable positions held by Exchange Participants. For this reason, Exchange Participants may be requested by the HKFE or SEHK to obtain details of such transactions/positions from the clients or their counterparties. Failure to provide such information to the HKFE or SEHK could lead to the imposition of position limits other than the prescribed limits according to the HKFE or SEHK rules.

Penalties

- 4.15. A person who contravenes Section 6 of the Rules without reasonable excuse is liable (i) on conviction on indictment to a fine of HK\$100,000 and to imprisonment for 2 years; or (ii) on summary conviction to a fine of HK\$10,000 and to imprisonment for 6 months.

5. Compliance by Agents

- 5.1. Section Sections 7 and 7A of the Rules enables stipulate that a person who holds or controls futures contracts or stock options contracts for other persons to another person or a unit trust or a sub-fund should apply the prescribed limits and reportable positions separately to his own position and to each of the positions he holds or controls for the other persons person or unit trust or sub-fund except where the person has discretion over the positions held or controlled by him for the other persons person or unit trust or sub-fund. In other words, a person can should disaggregate his own position and the positions he holds or controls for each of the other persons person or unit trust or sub-fund in the application of prescribed limits

¹⁰ HKFE requires Exchange Participants to submit the notice of reportable positions by 12:00 noon on the reporting day (T+1).

and reportable positions provided that he does not have discretion over the positions held or controlled for the other persons. A typical example in question. Examples of such person is persons are an Exchange Participant or a person providing intermediary services to its clients., a trustee of a unit trust or trustee of a sub-fund of an umbrella unit trust.

- 5.2. In accordance with Sections 7(2)-(3) and 7A(3)-(5) of the Rules, a person will be considered to have discretion in relation to a position he holds or controls for another person if: or a unit trust or a sub-fund if:

- (1) he may originate orders to acquire or dispose of any position in futures contracts or stock options contracts under a general authorization from the other person, whether the authorization is pursuant to a written agreement, power of attorney or otherwise or in the case of a unit trust or a sub-fund of an umbrella unit trust, a general authorisation from the trustee of the unit trust, and in the case of a sub-fund of a corporate fund, a general authorisation from the company; and
- (2) such authorization enables him to make specific acquisitions or disposals without requiring further consent or instruction from the other person or trustee or company,

and in such case, he will not be regarded as holding or controlling the position for the other person, unit trust or sub-fund for the purpose of applying the disaggregation provision to this position.

Examples of such person include a fund manager controlling positions for his funds and a trader managing discretionary accounts. However, it does not include a trader with a short-term discretion from his client to manage an order (e.g. if a client leaves an order to buy or sell futures contracts at any price within a specified range, the agent will not be regarded as having discretion) or a firm initiating orders to close out a position held for its client for risk control purposes (e.g. the client has defaulted on his payment to the firm). In this regard, Section 7(4) provides that a Clearing Participant in exercising its right to initiate orders to close out a client's positions in the event of the client defaulting on a payment is not to be regarded as having discretion over the positions of its clearing client.

- 5.3. If a person has discretion over positions held with him for other persons, all these positions should be aggregated with his own position in the application of the prescribed limits and reportable positions.
- 5.4. *For example, an agent holds 400, 3,000, and 8,000 futures contracts for Clients A, B and C respectively. Client A is a discretionary account operated by the agent. The agent also holds 200 futures contracts for his own account. Since the agent has discretion over the position held for Client A, the agent's own position and Client A's position should be aggregated in the application of the prescribed limits and reportable positions. Assume that the reportable level is 500 contracts and the prescribed limit is 10,000 contracts. The agent should notify the Exchange of each of the reportable positions held with him (i.e. 600 contracts held by its own account and Client A, 3,000 contracts held by Client B and 8,000 contracts held by Client C) and identities of the persons. Since these reportable positions are within the prescribed limit, the agent fully complies with the Rules.*

- 5.5. If a person is aware that a number of its client accounts are held for the same person, all positions in these accounts should not be treated separately. They should be aggregated for purposes of determining compliance with the Rules.
- 5.6. There are situations where a person holds or controls positions for the other person who is acting as agent. In accordance with the Client Identity Rule Policy, a person holding or controlling positions for an agent should find out who are the ultimate clients and obtain the client identity information from the agent. As an agent is allowed to disaggregate positions held for his clients, his total positions may exceed the prescribed limits even though each of the client positions is within the limits. The SFC accepts that a person is in compliance with the prescribed limits in respect of the positions held for an agent provided that he has obtained the client identity information to determine that the agent is allowed to hold excess positions in accordance with the Rules. If the person is not able to obtain the client identity information to decide whether the agent complies with the prescribed limits (e.g. the agent does not want to disclose the information for commercial reasons), the person should not apply the disaggregation provision to this agent account (i.e. all positions held by the agent should be aggregated in applying the prescribed limits).

6. Application of the Rules to Different Entities

Persons holding or controlling positions at multiple firms

- 6.1. If a person holds or controls positions in accounts at more than one firm, the person should have the obligation to aggregate positions for purposes of applying the prescribed limits and reportable position requirements.
- 6.2. If a person holding or controlling positions at multiple firms chooses to submit the notice of reportable positions to the Exchange through one of the firms (e.g. an Exchange Participant) where the firm agrees to submit the notice on the person's behalf, it should provide to the firm with its total positions held at other firms.
- 6.3. For the avoidance of doubt, if a person holds a reportable position but only part of the position (which has not exceeded the reportable level) is held by a firm, the firm will not need to report that position to the Exchange unless it knows that the total position held by the person in other firms has exceeded the reportable level.

Transaction originators

- 6.4. A transaction originator is a person who is ultimately responsible for originating instructions for transactions on behalf of the other person. The most common type of transaction originator is a fund manager who manages assets of a fund at his own discretion according to the investment policy of the fund. As explained in paragraph 5.2 above, since the transaction originator has discretion in relation to positions he holds or controls for his principals, he is not allowed to disaggregate the positions held or controlled for each of the principals for the purpose of applying the Rules.
- 6.5. If the total positions controlled by a transaction originator (including positions belonging to different principals, e.g. different funds, but under his control) have exceeded the reportable level, the transaction originator will be required to notify the

HKFE or SEHK (as the case may be) of such positions. As required in Section 6(2) of the Rules, the transaction originator should also provide the information about identities of each of his principals whose positions have exceeded the reportable level. *For example, assume a fund manager is in charge of the investment of three funds, namely, Fund A, Fund B and Fund C. Currently, there are 1,000, 800 and 200 futures contracts held by Fund A, Fund B and Fund C respectively. If the reportable level for the futures contract is 500 contracts, the fund manager should notify the Exchange of the total positions under his control (i.e. 2,000 contracts), names of the funds in which position has exceeded the reportable level (i.e. Fund A and Fund B) and the positions held in these funds.*

- 6.6. A transaction originator can choose to notify the HKFE or SEHK (as the case may be) of the reportable positions by himself or through its agent (e.g. an Exchange Participant) which agrees to make the report on his behalf.
- 6.7. The prescribed limits apply to the total positions controlled by a transaction originator even if the positions are held for different principals.

Unit trusts and corporate funds

Unit trusts

- 6.8. A unit trust is a collective investment scheme (“CIS”) constituted under a trust deed which pools investors’ money into a single fund managed by a fund manager. In most cases, the trustee is the legal holder of positions of the unit trust. As the holder of positions of a unit trust, the trustee is required to comply with the prescribed limits and report reportable positions in relation to the positions of the unit trust of which it is acting as the trustee.
- 6.9. As the trustee does not typically have discretion over the positions of the unit trust or the positions of the sub-funds under an umbrella unit trust, if a trustee is acting for multiple unit trusts, it must apply the prescribed limits and the reportable positions separately to each of the unit trusts (i.e. no netting of positions between different unit trusts), and in the case of sub-funds under an umbrella unit trust, apply the prescribed limits and the reportable positions separately to each of the sub-funds (i.e. no netting of positions between different sub-funds under an umbrella unit trust).
- 6.10. For example, assume a trustee holds positions for two unit trusts (UT A and UT B) and one umbrella trust where there are three sub-funds (SF X, SF Y and SF Z) under the umbrella trust. UT A has 6,000 long futures contracts, UT B has 6,000 short futures contracts, SF X has 200 long futures contracts, SF Y has 500 short futures contracts and SF Z has 800 long futures contracts. Assume that the reportable level is 500 contracts and the prescribed limit is 10,000 contracts. The trustee should notify the Exchange of each of the reportable positions held by him at the unit trust level or at the sub-fund level of an umbrella trust (i.e. 6,000 contracts each held by UT A and UT B respectively, 500 contracts held by SF Y and 800 contracts held by SF Z). Since these reportable positions are within the prescribed limit, the trustee fully complies with the Rules.

- 6.11. If the above unit trusts and umbrella unit trust are managed by the same fund manager, the fund manager would have to aggregate all the positions of the unit trusts and the umbrella trust in the application of the prescribed limits and reportable positions, i.e. the fund manager should notify the Exchange of 500 long futures contracts under his control and the aggregated positions should not exceed the prescribed limits of 10,000 contracts.
- 6.12. A trustee may report the reportable position to the HKFE or SEHK (as the case may be) itself or through its agent (e.g. an Exchange Participant) which agrees to make the report on its behalf.
- 6.13. Fund manager(s) of unit trusts or of sub-funds of an umbrella unit trust will have to comply with the prescribed limits and report positions in respect of the positions held by the unit trust or sub-funds of an umbrella unit trust as explained in the previous section on “Transaction originators”.

Corporate funds

- 6.14. In the case of a standalone corporate fund, the company should comply with the prescribed limits and report reportable positions in respect of the standalone corporate fund. In the case of an umbrella corporate fund that have sub-funds, the company should apply the prescribed limits and the reportable positions separately to each of the sub-funds under the umbrella corporate fund, i.e. no netting of positions between different sub-funds under an umbrella corporate fund.
- 6.15. For example, assume there are three sub-funds under an umbrella corporate fund (SF X, SF Y and SF Z), SF X has 200 long futures contracts, SF Y has 500 short futures contracts and SF Z has 800 long futures contracts. Assume that the reportable level is 500 contracts and the prescribed limit is 10,000 contracts. The company should notify the Exchange of each of the reportable positions of each of the sub-funds (i.e. 500 contracts held by SF Y and 800 contracts held by SF Z). Since these reportable positions are within the prescribed limit, the company fully complies with the Rules.
- 6.16. The company may report the reportable positions to the HKFE or SEHK (as the case may be) itself or through its agent (e.g. an Exchange Participant) which agrees to make the report on his behalf.
- 6.17. Fund manager(s) of sub-funds of an umbrella corporate fund will have to comply with the prescribed limits and report positions in respect of the positions held by the sub-funds as explained in the previous section on “Transaction originators”.

Omnibus accounts

6.8.6.18. In the case of an omnibus account, the Rules apply separately to the positions held by each of the underlying clients of the omnibus account except where the omnibus account operator has discretion over the positions. For this reason, positions held by different underlying clients should not be netted off for purposes of calculating and reporting reportable positions or determining compliance with the prescribed limits.

6.9.6.19. If an underlying client of the omnibus account holds or controls a reportable position, the omnibus account operator should inform the HKFE or SEHK (as the case may be) of such reportable position. An omnibus account operator can notify the Exchange of the reportable positions by itself or ask its agent (e.g. an Exchange Participant) carrying the account to submit the notice of reportable positions. The notice of reportable positions should be accompanied by the information about identities of the underlying clients whose positions have exceeded the reportable level.

6.10.6.20. There are situations where an underlying client of the omnibus account is also an omnibus account, i.e. there are more than one layer of omnibus account. If the omnibus account operator in one layer has notified the Exchange of the reportable positions held by the ultimate clients including identities of each of them (either by itself or through its agent), the SFC accepts that the other omnibus account operators below this layer will not be required to notify the Exchange of any reportable positions held in their accounts.

Example:

Suppose that Exchange Participant A has an omnibus account B holding 1,000 long futures contracts. One of the underlying clients of omnibus account B is also an omnibus account (account C) which holds 900 long futures contracts. Positions in omnibus account C are owned by Company D (800 long futures contracts) and other small investors (a total of 100 long futures contracts).

Assume that the reportable level is 500 contracts. Exchange Participant A should inform the Exchange of the position held by the omnibus account B (i.e. 1,000 contracts). If the operator of omnibus account B has obtained the information about the ultimate client from the operator of omnibus account C and notified the Exchange of the reportable position held by Company D including its identity (the reportable position can be reported to the Exchange by the operator B itself or through the Exchange Participant A), the operator of omnibus account C will not be required to submit any notice of reportable positions to the Exchange.

6.11.6.21. Where the omnibus account operator has discretion over positions held with it, it should aggregate such positions with its own position in the application of the prescribed limits.

Appendix 1

Examples illustrating the use of excess positions

Example 1:

Assume a firm's proprietary trading desk has a position of HSI futures contracts equivalent to 9,000 position delta, and that its sales desk wants to facilitate clients' trades resulting in the use of about 30,000 HSI futures contracts for hedging purpose. Assume also that the specified percentage is 300%. Can the firm apply for excess?

- Yes, it can apply for excess of up to 30,000 contracts. However, the size of excess positions authorized for an applicant will be determined on a case by case basis after taking into consideration various factors such as the prevailing market situation.

If an excess of 30,000 contracts is authorized, the firm's limit will increase to 40,000 contracts –

- The firm can use up to 10,000 contracts for proprietary trading purposes and any remaining balance for client facilitation purposes. The firm may therefore also use the entire 40,000 limit for client facilitation purposes if it holds no proprietary trading position.
- The SFC is not concerned as to the order in which the limit is consumed (ie whether the limit is first used to acquire contracts for client facilitation purposes and then for proprietary trading purposes or vice versa). It is however concerned to ensure that any holdings over 10,000 contracts are held only for client facilitation purposes – i.e. that holdings for proprietary trading purposes do not exceed the statutorily prescribed limit.

Example 2:

Assume a firm already holds a short position in HSI futures contract equivalent to 8,000 position delta for its proprietary trading business, and that it wishes to hold another 30,000 position delta for its index arbitrage activities in the same short direction. Assume that the specified percentage is 300%. Can the firm apply for excess?

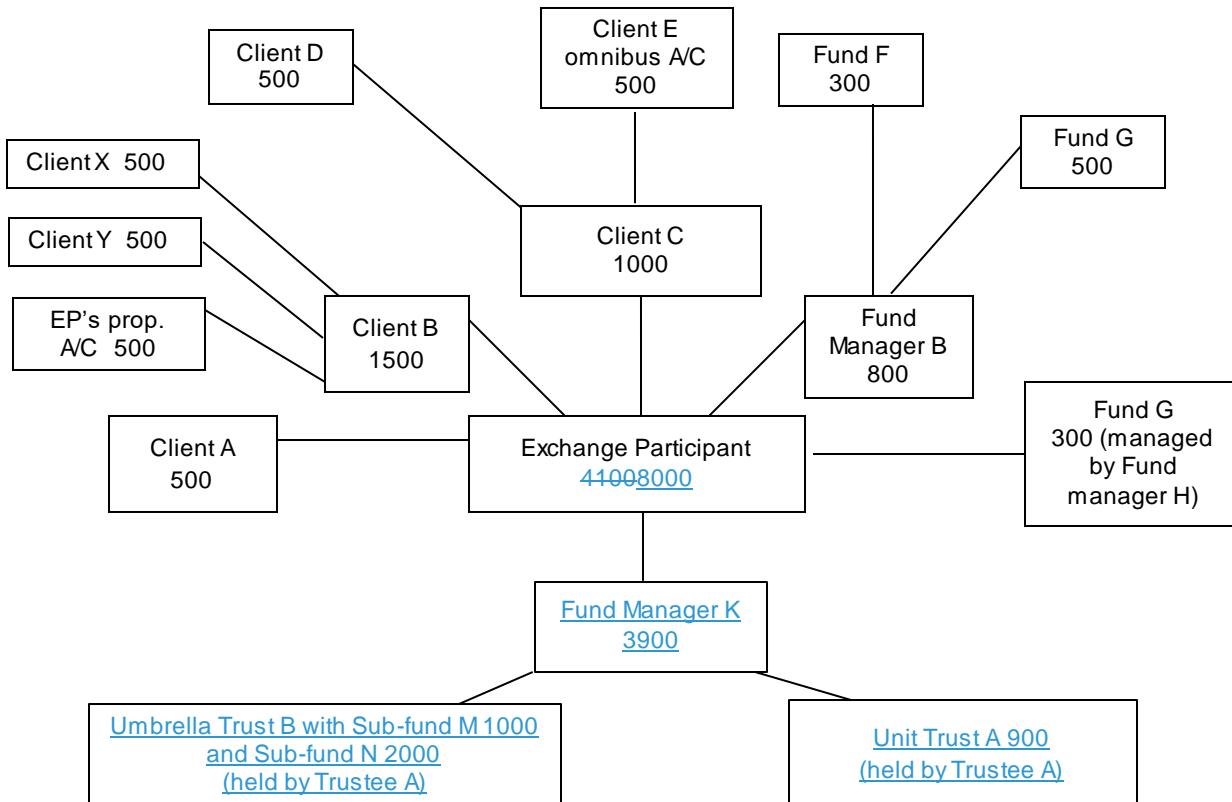
- Yes, it can apply for excess of up to 30,000 contracts. However, the size of excess positions authorized for an applicant will be determined on a case by case basis after taking into consideration various factors such as the prevailing market situation.

If an excess of 30,000 contracts is authorized, the firm's limit will increase to 40,000 contracts –

- The firm can use up to 10,000 contracts for its proprietary trading business (not including index arbitrage activities) and any remaining balance for its index arbitrage activities. The firm may therefore also use the entire 40,000 limit for its index arbitrage activities if it holds no other proprietary trading position.

Appendix 2

For example: Reportable Position is 450 contracts



Client A has an account with the Exchange Participant which contains 500 contracts.

The Exchange Participant has a client account under the name of **Client B** which it uses for booking transactions for his **proprietary trading** and for the trading of **Clients X and Y**. Client X and Client Y each hold 500 contracts. The Exchange Participant's proprietary position booked into the Client B account is also 500 contracts. The Client B account therefore has a total of 1500. Provided that the Exchange Participant does not have discretion over Client X's and Client Y's positions, Client X, Client Y and the Exchange Participant's proprietary position can each be treated separately (i.e. disaggregated) by virtue of Section 7 of the Rules.

Client C is a non-exchange participant agent. He holds positions for Clients D and E who have 500 contracts each. Client E is an omnibus account. Provided that Client C does not have discretion over Client D's and Client E's positions, positions held for Clients D and E can be treated separately. In respect of the omnibus account itself, if the operator of Client E does not have discretion over positions in the account, it can apply disaggregation to the positions held for each of the underlying clients.

Fund Manager B has an account with the Exchange Participant. He manages **Funds F and G** which hold 300 and 500 contracts respectively. Separately, Fund G has an account with the Exchange Participant. This account is managed by Fund Manager H. Fund G, through this account, holds 300 contracts. Funds F and G's trades held by Fund Manager B are executed by him. The positions held

for Funds F and G cannot be treated separately as Fund Manager B has discretion over these positions.

Trustee A acts for Unit Trust A which holds 900 contracts and Umbrella Trust B which has Sub-fund M with 1,000 contracts and Sub-fund N with 2,000 contracts. Both Unit Trust A and Umbrella Trust B are managed by Fund Manager K. Trustee A should disaggregate the positions of Unit Trust A, Sub-fund M and Sub-fund N as it does not have discretion over these positions. However, Fund manager K should aggregate the positions of Unit Trust A, Sub-fund M and Sub-fund N.

Notices of Reportable Positions to be filed –

- (a) the Exchange Participant should notify the Exchange of –
 - 500 contracts each for its proprietary position and Client A, 1500 contracts held by Client B, 1000 contracts held by Client C, ~~and~~ 800 contracts held by Fund Manager B and 3,900 contracts held by Fund Manager K.
- (b) Client B should notify the Exchange of 500 contracts each held by the ~~EP's~~ Exchange Participant's proprietary account, Client X and Y.
- (c) Client A, Client X, Client Y, Client D, Client E, should each notify the Exchange of their own positions of 500 contracts.
- (d) Client C should notify the Exchange of 500 contracts each held by Client D and Client E.
- (e) Fund Manager B should notify the Exchange of the 800 contracts he controls and that 500 contracts are for Fund G.
- (f) Fund G should notify the Exchange of its 800 contracts, 500 of which are held by Fund Manager B and 300 held by Fund Manager H.
- (g) Trustee A should notify the Exchange separately of the 900 contracts held for Unit Trust A, the 1,000 contracts held for Sub-fund M under Umbrella Trust B, and the 2,000 contracts for Sub-fund N.
- (h) Fund manager K should notify the Exchange of 3,900 contracts he controls that comprises of 900 contracts of Unit Trust A, 1,000 contracts of Sub-fund M under Umbrella Trust B and 2,000 contracts of Sub-fund N.

Notwithstanding the above filing requirements, the notice of a reportable position may be submitted by the agent or the person acting as principal (see paragraph 4.4). As long as there is an arrangement in place for reporting such positions, the SFC accepts that if ~~one of the parties appointed agent~~ has submitted the notice of reportable position, the ~~other parties principal~~ will not be required to notify the Exchange of the same reportable positions.