

TOPIC 4 - OVERVIEW

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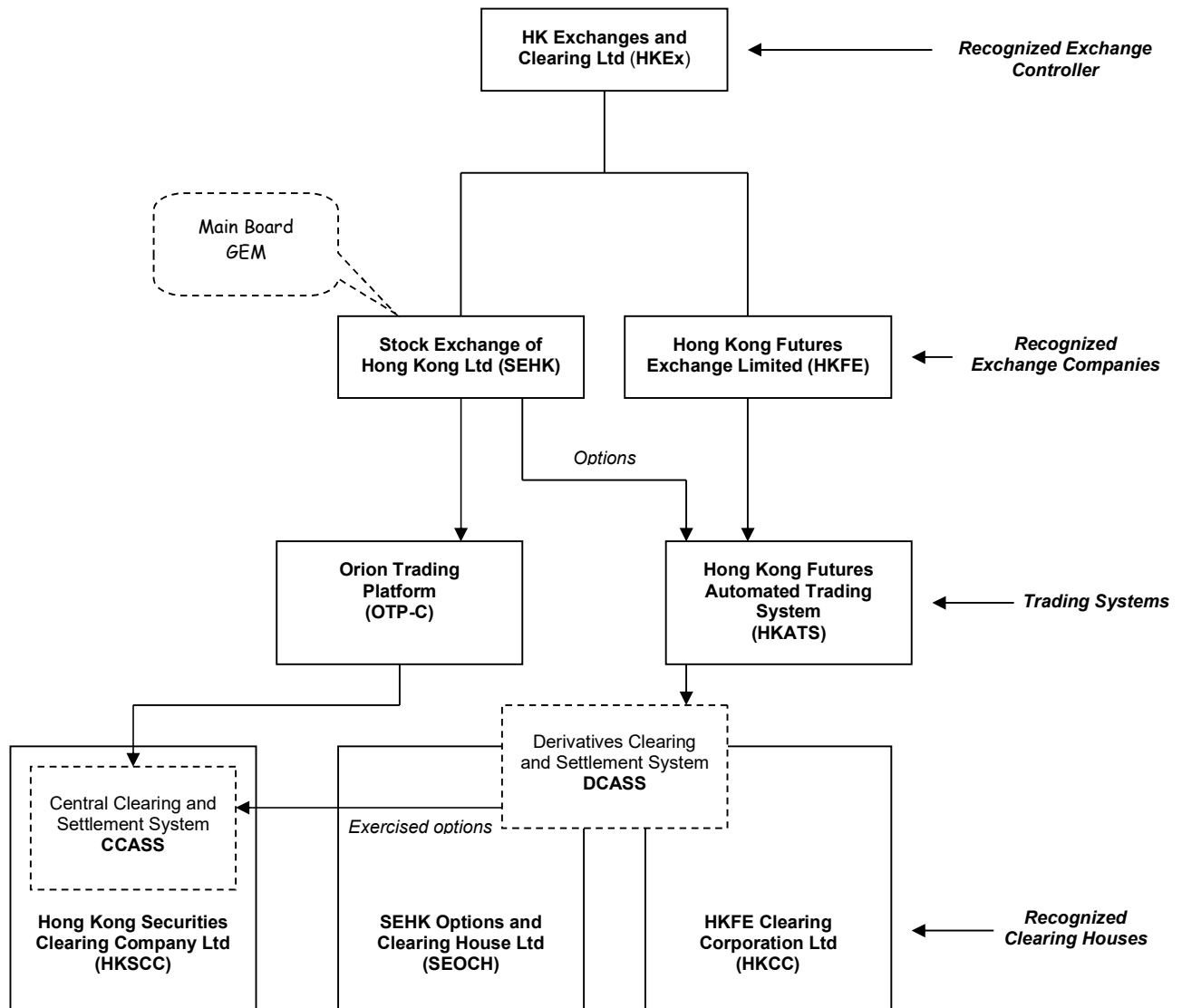
1. MARKET PARTICIPANTS IN HONG KONG SECURITIES MARKET

- The following can deal in securities which are listed on the SEHK:
 - **Exchange participants** (SEHK participants), who will be subject to SFC licensing requirements
 - Non-exchange participants holding Type 1 licenses, including **intermediaries that are subsidiaries of or controlled by foreign firms** and have a business presence in Hong Kong, who will be subject to SFC licensing requirements
 - **Overseas intermediaries who do not have a physical presence in Hong Kong** and trade through the above and will not be subject to SFC licensing requirements

1.1 The Hong Kong Exchanges and Clearing Limited

- The Hong Kong Exchanges and Clearing Limited (“HKEx”) is:
 - A company listed on the SEHK
 - The exchange controller as defined in the SFO
 - Regulates listed companies, trading on the exchanges and the related clearing and settlement functions
 - Owns subsidiaries operating the 2 exchanges:
 - **Stock Exchange of Hong Kong Limited (“SEHK”)** with the Main Board (securities and options of established companies with profitable operating track record) and the Growth Enterprise market (“GEM”) (securities of growth companies)
 - **Hong Kong Futures Exchange Limited (“HKFE”)** (futures contracts)
 - Owns subsidiaries operating the 3 clearing houses
- The 4 clearing houses are:
 - **The Hong Kong Securities Clearing Company Limited (“HKSCC”)**, an independent corporation, which operates the Central Clearing and Settlement System (“CCASS”) for cash business
 - **The SEHK Options Clearing House Limited (“SEOCH”)**, a wholly owned subsidiary of the SEHK, for options
 - **The HKFE Clearing Corporation Limited (“HKCC”)**, a subsidiary of HKFE, for the futures business
 - **OTC Clearing Hong Kong Limited (OTC Clear)** – see below
- Note that the SFC regulates intermediaries engaged in trading, not the HKEx
- See below for diagram

HONG KONG EXCHANGES AND CLEARING LIMITED



- In November 2013, OTC Clearing Hong Kong Limited (**OTC Clear**) started operations. It was established to provide clearing services for over-the-counter (OTC) derivatives. It is 75% owned by HKEx with the remainder owned by 12 financial institutions, being the founding shareholders
- On 31 August 2016, SFC designated OTC Clear as a central counterparty (CCP) for certain mandatory OTC derivative clearing obligations under the SFO (see Topic 2)

2. SEHK EXCHANGE PARTICIPANTS AND TRADING RIGHTS

2.1 Participants - General

- To trade through the exchanges, an intermediary must become an **exchange participant** and hold at least one **stock exchange trading right**
- **Trading rights are non-transferable** (since 2010)
- An exchange participantship is **NOT** transferable
- To clear trades you must become a clearing participant of the relevant clearing house
- Deposits and subscriptions must be paid to the relevant exchange and clearing house by participants
- Membership of HKEx is no longer needed to trade on the exchanges nor to clear trades

2.2 SEHK Participants

- An **Exchange Participant** must always:
 - be of good financial standing and integrity
 - observe at all times all provisions of SFO, subsidiary legislation, codes of conduct, guidelines, rules and regulations administered by SFC and exchange
 - be a holder of a stock exchange trading right
 - be licensed for Type I activity under the SFO
 - be a corporation limited by shares and incorporated in Hong Kong

2.3 Representatives and Responsible Officers

- All licensed representatives of an Exchange Participant who are Type 1 SFC-approved Responsible Officers shall be registered with the SEHK as Responsible Officers
- An Exchange Participant must have at least one executive director registered with the SEHK as a Responsible Officer at all times
- An Exchange Participant is responsible for the acts of its representatives

2.4 SEHK Trading Rights

- A trading right allows the holder to trade on SEHK and to be entered into a register kept by the SEHK
- A holder must be authorized as an exchange participant before any trading is done
- Trading rights are non-transferable
- Each trading right entitles its holder to connect to the SEHK trading system via a trading device in the Exchange Participant's office

3. PRODUCTS TRADED ON THE SEHK

3.1 Products

3.1.1 Equity Securities

- Ordinary shares (most of SEHK turnover) and preference shares
- Securities listed on overseas exchanges traded under pilot programmes
- Securities traded under the pilot programme for trading US securities are different to Main Board and GEM traded securities and are:
 - listed on NASDAQ or AMEX
 - may also include a number of exchange traded funds
 - have no public offering in Hong Kong
 - not regulated as listings on SEHK's Main Board or GEM
 - admitted to SEHK for trading only
 - regulated by Hong Kong laws and SEHK rules
- Shares of companies incorporated in PRC and approved by CSRC for listing in Hong Kong ("H-shares")
- Shares of companies ("Red Chip") where:
 - Mainland China entities hold more than 30% of capital and are single largest shareholder (in aggregate), or
 - Mainland China entities hold more than 20% of capital and there is strong influential presence of Mainland China-linked individuals on company's Board of directors
- GEM targets growth companies and has lower listing requirements to accommodate growth companies without a track record

3.1.2 Debt Securities

- Bonds or notes where the entity promises to repay the holder the total amount borrowed at maturity, with a fixed or floating rate interest payment (coupon) during the term
- Holders are creditors not owners of equity
- Examples are exchange fund notes issued by the HKMA and by the HK Mortgage Corporation Limited

3.1.3 Unit Trusts/Mutual Funds

- Invests contributions from investors in a portfolio of securities and issues units to the investors

3.1.4 Exchange Traded Funds (“ETFs”)

- ETFs hold portfolios of securities to correspond to the price and yield performance of their designed theme (such as the Hong Kong Tracker Fund (TraHK) designed to reflect the performance of the Hang Seng Index)
- Holders can create block-sized units (“creation units”) in cash or in kind and redeem for securities approximating the composition of the underlying portfolio

3.1.5 Leveraged and Inverse Products

- Such products structured as ETFs are traded on the stock market and authorised by the SFC as collective investment schemes (CISs)
- **Leveraged products** aim to deliver a daily return equal to a multiple of the underlying index return that they track
- **Inverse products** aim to deliver the opposite of the daily return of the underlying index that they track

3.1.6 Real Estate Investment Trusts

- Portfolios of income generating properties such as shopping malls, hotels and service apartments
- Pays at least 90% of net income after tax to investors as dividends

3.1.7 Structured Products

Equity Warrants

- Equity warrants carry the right to subscribe for equity securities of an issuer or any of its subsidiaries at a pre-determined price at any time before maturity (US style) (European style can only subscribe at maturity)
- Minimum term of 1 year, maximum of term of 5 years

Derivative Warrants

- Derivative warrants are similar to equity warrants but are issued by a party that is independent of the issuer of the underlying securities of the company and its subsidiaries
- Majority in Hong Kong are settled in cash
- Can be call or put warrants
- May be issued over assets other than securities (such as currencies or commodities)

Inline Warrants

- Inline warrants give investors the opportunity to receive a pre-determined fixed payment at the expiry of the warrant, depending on whether the price of the underlying asset falls within or outside the upper and lower strike prices chosen by the investor
- They may be bought and sold prior to their expiry or be settled at expiry in cash
- Usually issued by investment banks, independent of HKEx and the underlying asset
- Lifespan of six months to five years

Callable Bull/Bear Contracts (CBCBs)

- Leveraged investments tracking the performance of an underlying asset
- Issued by a third party such as an investment bank
- Cash settled with a life span of 3 months to 5 years and can be called by the issuer if the underlying asset reaches a pre-specified level

Equity Linked Instruments (ELIs)

- Structured product issued by banks and financial institutions
- Investor in ELI indirectly writes an option on the underlying stock
- If market moves as investor expects, earns a fixed return mainly from premium received on writing option
- If market moves against investor's view, may lose some or all of investment or receive shares worth less than initial investment
- 3 different types of ELI (bull, bear and range) to match investors' directional view of underlying securities

3.2 Characteristics of Hong Kong Listed Companies

- The **Listing Rules** are intended to ensure:
 - Suitability of applicants for listing
 - Fair and orderly issue and marketing of securities
 - Provision of sufficient, material and timely information which might concern the issuer and affect the price
 - Fair and equal treatment of shareholders
 - Directors act in the interests of all shareholders

3.3 Main Board Listing Criteria (Chapter 8 of SEHK Listing Rules)

- The **basic criteria for an initial listing** is as follows:
 - Must be incorporated, but not a private company
 - Both issuer, and its business, must in the opinion of SEHK be suitable for listing (eg a company consisting primarily of cash or near cash would not be deemed suitable)
 - Issuer must satisfy one of the following tests:
 - **Profits test:** Profits for the most recent year must not less than HK\$20 million **and those of the two preceding years in aggregate must not be less than HK\$30 million**; or
 - **Market Capitalisation/Revenue/Cash Flow Test:** The issuer must have a market capitalization at the time of listing of at least HK\$2 billion, revenue for most recent audited financial year of at least HK\$500 million and positive cash flow for the preceding three financial years of at least HK\$100 million; or
 - **Market Capitalisation/Revenue Test:** The issuer must have a market capitalization at time of listing at least HK\$4 billion and revenue for the most recent audited financial year of at least HK\$500 million
 - New applicants must have a **trading record** of at least three years under substantially the **same management**, while **ownership** should be substantially the same for at least the most recent audited financial year.
 - “**Continuous ownership and control**” refers to voting rights by a controlling shareholder or, where there is no controlling shareholder, the single largest shareholder
 - For a new applicant, the **latest financial period** reported on by the reporting accountants must be within the six months before the date of listing document
 - At least 25% of the issuer’s total number of shares must be **held by the public** and the public holding of shares must be **at least HK\$125 million** – for issues over HK\$10 billion, the SEHK may accept a lower percentage of between 15% and 25%
 - For new listings that involve placings, the **placing tranche** must not be less than HK\$25 million, and not less than 25% of the placing tranche must be made available by the lead broker to the general public

- Expected market capitalisation of a new applicant must be at least HK\$500 million at time of listing and there must be a **sufficient spread of shareholders** with a minimum of 300
- Not more than 50% of the securities **in public hands** at the time of listing can be beneficially owned by the **largest 3 public shareholders**
- If a new applicant has a **controlling shareholder** with an interest in a business that competes (or may compete), this must be disclosed
- A new applicant for a primary listing must have **sufficient management presence** in Hong Kong (at least 2 executive directors resident in Hong Kong)
- The securities must be **freely transferable**
- A new applicant must appoint **an approved share registrar** in Hong Kong to maintain register of members
- Proposed directors must meet certain requirements
- SEHK may accept a shorter trading period and/or may waive the profit or financial standards requirements

3.4 GEM Listing Criteria

- Targets growth companies from all industries and of all sizes
- Qualifications for listing generally lower, to accommodate companies without a performance track record
- Operates on the philosophy of “buyer beware” and “let the market decide” - based on strong disclosure
- Requirements for listing:
 - **Performance track record** only required for 2 years with a positive cash flow from operating activities of at least HK\$30m for those two years
 - The applicant must show that it has been **focused on one line of business** under substantially same management
 - Shorter periods for trading, ownership and management continuity may be acceptable for newly-formed project companies
 - **Market capitalization** at time of listing must be at least HK\$150 million
 - **Public ownership** must be at least 100 persons at time of listing
 - At least 25% of the issuer’s total number of shares must be **held by the public** and the public holding of shares must be at least HK\$45 million – at least 10% of all securities offered must be offered to the public

4. TRADING MECHANISM AND RULES

4.1 Automatic Order Matching and Execution System

- Orion Trading Platform (OTP-C) (trading system used by SEHK) allows for direct interface with intermediary's systems
- Supports trading for over 20 hours per day and trading in multiple markets
- Orders can be placed by internet, cell phones or other technology
- Most on-exchange transactions use OTP-C system

4.2 Trading Methods

- OTP-C system is “**order-driven**” with participants for buyers finding participants for matching sellers
- All transactions concluded by auto matching **except**:
 - Non-automated trades (which are concluded as odd lot transactions and must be reported to SEHK so that information on trades can be given to all participants in market to ensure transparency)
 - Cross trades (direct business transactions)
 - Isolated trades to effect a buy-in
 - Orders exceeding the maximum order size limit
 - Transactions intentionally concluded outside OTP-C
- An Exchange Participant may choose between one of the following to connect to OTP-C:
 - **New Securities Trading Device (NSTD)**: is a multi-workstations front-end trading device, developed by an independent software vendor. Compatible with the SEHK's core platforms, it is offered to Exchange Participants (EPs) under the brand name “ET Trade Speed Station”
 - **Broker-supplied systems (BSS)**: developed by individual participants for their needs (following Open Gateway specification design from SEHK)

4.3 Trading Sessions

- In the **pre-opening session**, maximum automatch order size is 3,000 board lots. Orders are matched at an order matching period in order type, price and time priority at the final Indicative Equilibrium Price. In the **Continuous Trading Session**, maximum automatch order size is 3,000 board lots. Orders are continuously executed by price and time priority

4.3.1 Closing Auction Session (CAS)

- Market participants interested in trading at the closing price may input buy and sell orders. CAS covers the Hang Seng Composite LargeCap and MidCap Index constituent stocks, Hang Seng Composite SmallCap Index constituent stocks, H shares and all ETFs
- A reference price is determined from several nominal prices during the continuous trading session (CTS). A CAS order should not deviate by more than 5% from the reference price
- Most developed markets have a CAS to enable trading at closing prices, which is a key investment mandate of some funds such as index trackers
- The CAS covers all equities as well as funds (including ETFs and REITs) traded on the SEHK.
- Structured products, leveraged and inverse products, equity warrants, rights and debt securities are currently excluded
- Short selling is allowed in the CAS with the limitation that the prices cannot be lower than the CAS reference price

4.3.2 Volatility Control Mechanism (VCM)

- A **five-minute cooling-off period** will be imposed for a particular stock/contract if the market price moves by more than 10%/5% from its last traded price 5 minutes before. **Normal continuous trading will resume when the 5-minute cooling-off period ends** - there is a maximum of one trigger per continuous trading session
- VCM applies to certain Hang Seng Index and Hang Seng China Enterprises Index constituent stocks and index futures contracts
- VCM does not apply to the first 15 minutes of morning and afternoon continuous trading sessions and the last 15 minutes of the afternoon session

4.4 Order Types

- **At-the-market orders:** buy or sell at best available price
- **Limit orders:** sets specific price (or better price) at which transaction can be executed (limits highest and lowest price)
- **Enhanced limit orders:** matches up to 10 price queues at the same time. The input order price of an enhanced limit order can be matched up to 9 spreads better than the best price on the other side of the market. Unfilled quantities will be converted into a limit order.
- **Special limit orders:** matches up to 10 price queues (the best price queue and the next 9 queues each at one-spread away) as long as traded price is not worse than input price limit. Any unfilled quantity after matching will be cancelled.
- **At-auction orders:** order input during pre-opening session without a specified price and has higher priority for matching than an at-auction limit order
- **At-auction limit orders:** order input during pre-opening session with a specified price. Any unfilled quantity after matching will be converted to a limit order at the input price and carried forward to continuous trading (as long as input price is not 9 times or more from prevailing nominal price)

4.5 Quotation Rules

- Quotation rules ensure there is no sudden dramatic fluctuations in the share price for the maintenance of orderly trading
- First order entered into the trading system each day, if it is a bid, must be at a price higher than or equal to the previous closing price minus 24 spreads
- First order entered into the trading system each day, if it is an ask, must be at a price lower than or equal to the previous closing price plus 24 spreads
- Spread of a security depends on its price range

Price Range (HK\$)			Spread (HK\$)
All securities other than debt:			
0.01	-	0.25	0.001
>0.25	-	0.50	0.005
>0.50	-	10.00	0.010
>10.00	-	20.00	0.020
>20.00	-	100.00	0.050
>100.00	-	200.00	0.100
>200.00	-	500.00	0.200
>500.00	-	1,000.00	0.500
>1,000.00	-	2,000.00	1.000
>2,000.00	-	5,000.00	2.500
>5,000.00	-	9,995.00	5.000
Specified SEHK securities and other debt securities:			
0.50	-	9,999.95	0.050

4.6 Direct Business (Crossing of Trades) Rule

- Direct business (crossing of trades) is where the **SEHK participant acts for both the buyer and the seller**, whether as principal or agent
- Focus of the rules is prompt and accurate reporting to ensure market transparency and that the SEHK has up to date information on current trading activity to be aware of unusual activity or improper trades
 - Details of transactions executed through an automated trading system provided by an Exchange Participant must be input to system within 1 minute of concluding a transaction
 - Details of all other transactions must be reported within 15 minutes of transaction conclusion
 - Details of transactions conducted outside the Pre-opening Session and the trading hours must be reported within the first 15 minutes of the next trading session
 - Trades cannot be cancelled once reported in system

5. TRADING HALT, SUSPENSION, CANCELLATION AND WITHDRAWAL OF LISTING

- The SEHK may halt/suspend a listing where it considers it necessary for the protection of the investor or **maintenance of an orderly market**
- **Suspension or a trading halt can be initiated by:**
 - The listed company
 - SEHK or GEM
 - SFC for untoward movements in prices or volumes
- **A trading halt** (which cannot be for more than 2 days) will be necessary when the issuer:
 - Has material information to be disclosed to avoid a false market under the MBLR;
 - Needs to disclose inside information
 - Is to issue an announcement regarding market commentaries or rumours
- **SEHK may call a trading halt/suspension if:**
 - There are insufficient shares in the hands of the public;
 - The issuer does not have a sufficient level of operations or sufficient assets to warrant a continued listing; or
 - It considers that the issuer is no longer suitable for listing
- Listed securities **should be continuously traded** save in exceptional circumstances and therefore, the SEHK requires an issuer-requested suspension to be kept as short as possible
- An issuer must have a **sufficient level of operations or tangible assets** to warrant continued listing on the SEHK. A listing may be cancelled if the issuer fails to:
 - Take adequate action to restore its listing for a prolonged period
 - Address matters identified by the SEHK within the specified time
- **SEHK can also cancel a listing where** it has been suspended for a continuous period of 18 months
- An issuer may **not voluntarily withdraw its listing** without shareholder approval
- An Exchange Participant **must not deal in suspended securities** except:
 - Where the suspension is due to insufficient shares held by the public (dealing must be reported to the SEHK)
 - To return borrowed securities
 - For the purpose of completing a market-maker short selling transaction concluded before the suspension
 - Where the securities are suspended for “placing” on behalf of the issuer or for “offer for subscription” or “rights issue” under the Listing Rules

6. CLEARING AND SETTLEMENT SERVICES

6.1 Hong Kong Central Clearing and Settlement System (“CCASS”)

- CCASS is operated by Hong Kong Securities Company (HKSCC)
- HKSCC provides securities clearing and settlement services, as well as:
 - depository services
 - common nominee services
 - electronic securities application services
- CCASS is a computerized book-entry clearing and settlement system. Settlement is electronically recorded in the stock account balance of a participant without the physical movement of share certificates (which remain in HKSCC’s central securities depository)
- CCASS reduces scrip circulation by immobilisation of share certificates delivered by participants to the depository
- There are various categories of CCASS participants, including:
 - Direct Clearing Participants (DCPs)
 - General Clearing Participants (GCPs)
 - Clearing Agency Participants
 - Custodian Participants
 - Stock Lender Participants
 - Stock Pledgee Participants
 - Investor Participants

6.2 Clearing Participantship

6.2.1 Direct Clearing Participantship (DCP)

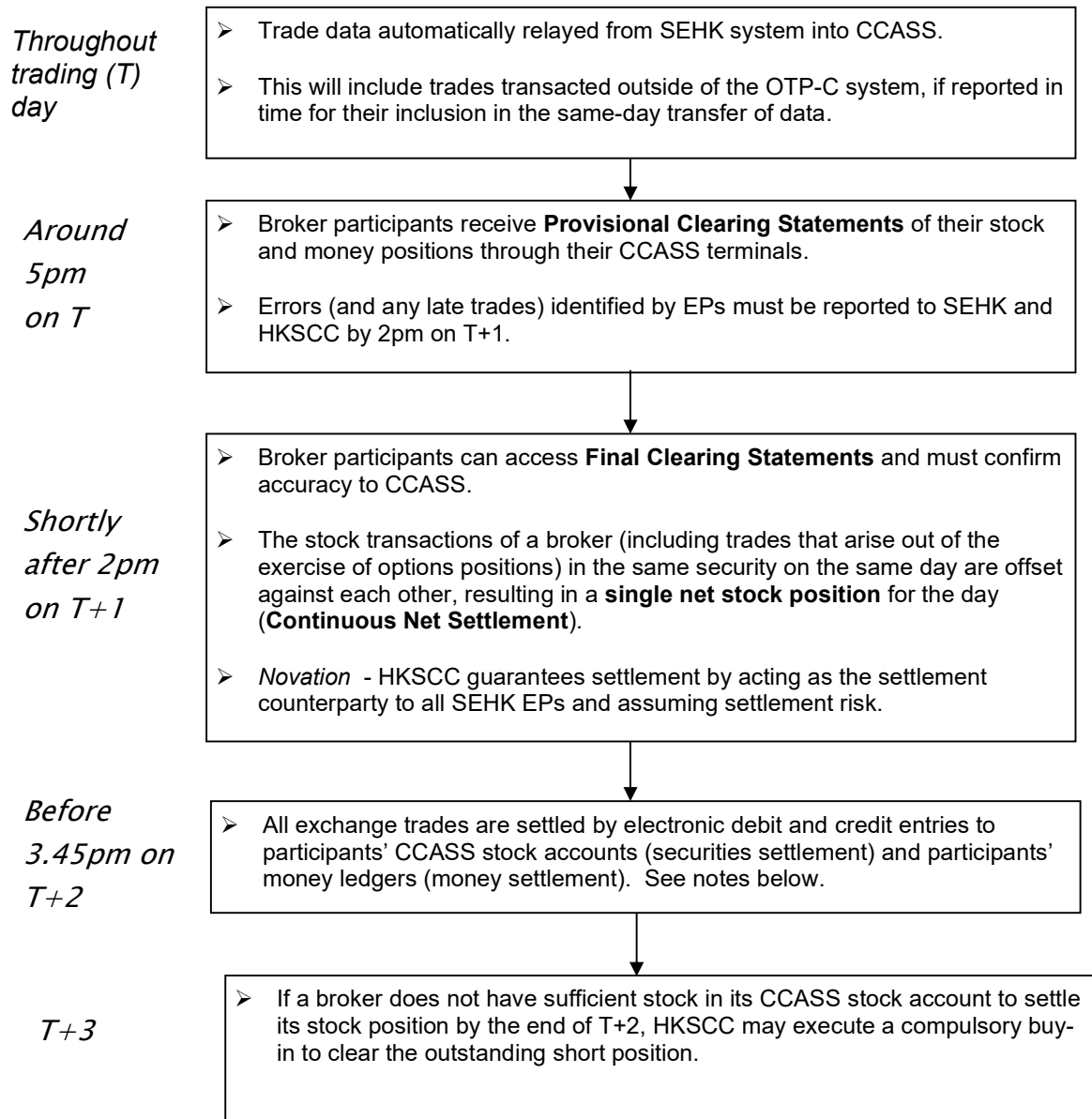
- A DCP can only clear its own trades
- A DCP applicant must:
 - Be an Exchange Participant
 - Be Type 1 licensed
 - Sign a participantship agreement and pay admission/contribution fees
 - Provide assurances on performance and obligations
 - Obtain an agreement from a designated bank for money settlement in CCASS

6.2.2 General Clearing Participants (GCP)

- A GCP can clear its own trades and provide third party clearing services to other non-clearing Exchange Participants
- A GCP applicant must meet same criteria as a DCP, plus:
 - Be licensed or registered for Type 1 activities
 - For a Licensed Corporation:
 - Be incorporated in Hong Kong
 - Minimum liquid capital of HK\$300m or RLC under FRR (whichever higher); OR paid-up share capital of at least HK\$300m and liquid capital of not less than HK\$100m or RLC under FRR (whichever is higher)
 - For a Registered Institution:
 - Minimum credit rating of A3 or a HK\$ note-issuing bank
 - Demonstrate operational and financial capabilities to satisfy CCASS requirements and to operate a securities clearing business

6.3 Summary of Facilities and Systems Offered

6.3.1 Settlement under the Continuous Net Settlement (CNS) System



- CCASS Stock Accounts:
 - No 01 accounts: stocks for settlement
 - No 02 accounts: handling of stock dividends
 - No 03 accounts: safe custody stocks, house investments and onwards securities collateral
 - No 20 account: stock collateral control account

- There are two categories of transactions:
 - Exchange trades (trades in eligible securities on SEHK) settled under CNS
 - Non- exchange trades (settlement instructions, clearing agency transactions and investor settlement instructions)

6.3.2 Exchange Trades using CNS

Settlement under CNS

- SEHK trades will all be settled through the CNS system unless they are isolated from the CNS system by the counterparty or the HKSCC

Settlement – Isolated Exchange Trades

- Isolated trades are settled on a trade-for-trade basis
- Trades can be isolated from CNS system by choice of SEHK participants or by HKSCC (for risk management reasons)
- Two SEHK participants can elect to have trade settled under isolated trade system of CCASS at time of trade
- Participants can make their own money settlement outside of CCASS, called free payment
- HKSCC does not become settlement counterpart for isolated trades therefore facilitates but does not guarantee settlement
- Participants may choose to settle on real-time delivery versus payment basis (shares are delivered on confirmation of payment) to eliminate credit risk

6.3.3 Non-exchange Trades

Settlement Instructions (SI)

- SIs relate to intermediary-custodian transactions, stock borrowing and lending, stock pledging and portfolio movements.
- Settlement is on a trade-for-trade basis.
- HKSCC does not become settlement counterpart for SIs and therefore facilitates but does not guarantee settlement
- 2 parties can match instructions through HKSCC facilities. Can be against payment or free of payment and may specify delivery date
- On due date HKSCC will attempt to make delivery of stock. If it fails, the instruction will be deleted from the system. If successful, message is sent to banks to transfer funds.

6.3.4 Investor Account with HKSCC

- Investor account service launched in 1998
- Depository account for safekeeping of stock while retaining legal protection and control
- Both individual and corporate investors may have accounts in CCASS and be investor participants
- Investors receive activity and monthly statements from HKSCC
- Can use system to subscribe for new shares, tender and settle for Stock Exchange Fund or HKMC Notes, and receive corporate communications from listed issuers

Investor Settlement Instructions (ISI)

- ISI moves stock out of a direct account opened by investor
- Investor instructs participant who confirms order in CCASS system or in person by submitting a form

6.4 Risk Management

6.4.1 Marks

- HKSCC is exposed to market risk from unfavorable price variations on unsettled stock positions of SEHK participants in CNS system
- HKSCC marks-to-market any unsettled stock position in CNS and will collect any adverse variance (marks)
- Marks normally collected as cash although may use securities used as collateral
- HKSCC can collect marks, even if stock position not due for settlement

6.4.2 Margin

- HKSCC is entitled to compute margin on all unsettled stock positions
- Margin is normally collected in cash, but HKSCC may accept securities as collateral in exceptional cases
- Intra-day margin may be collected in the following circumstances
 - Sudden fluctuations in the securities market
 - When major markets are open but SEHK is closed on public holidays
 - When HKSCC considers it appropriate

6.4.3 Collateral

- HKSCC may require SEHK participant to provide collateral if trading pattern creates excessive risks due to market contracts with participants
- Can be in form of cash, bank guarantees or collateral securities

6.4.4 Securities-on-hold

- Money settlement is only confirmed by banks on day following delivery in CCASS, so HKSCC has risk exposure due to timing
- Title and property in securities does not pass to participant until payment has been received in full
- If participant wants to use securities allocated to stock account, needs to provide bank guarantee to HKSCC for sums owed
- Exchange participants may need to pay same-day available funds to HKSCC to reduce their monetary obligations. Equivalent discounted market value of on-hold securities will then be released

6.4.5 Evidence of Securities Available for Settlement

- If exchange contracts are subject to expiry (e.g. warrants), selling participant must provide evidence that there will be sufficient securities in account by expiry date

6.4.6 Closing Out

- If participant defaults, HKSCC may close out any or all obligations in CNS
- Result is that all obligations to deliver securities will be replaced by sums payable, with a net amount due
- The HKSCC thus can quantify its exposure and enable it to meet its obligations to other exchange participants

6.5 Clearing and Settlement of OTC Derivatives Transactions

- OTC Clear was established by HKEx to provide clearing and settlement of OTC derivatives transactions
- OTC Clearing and Settlement System (OCASS) is an integrated system which processes trade novation and registration, valuation, collateral and margin calculation, trade event management, market data storage and the user interface for day-to-day operations and reporting
- OTC Clear replaces the original trade between two Clearing Members with two separate trades between it and the clearing members

7. SEHK DISCIPLINARY PROCEDURES

- SEHK is only responsible for disciplinary matters relating to trading offences
- SFC is responsible for all disciplinary matters relating to breaches of SFO, statutory rules, regulation and codes of conduct
- SEHK Board and Chief Executive **may exercise disciplinary powers if exchange participant:**
 - Is or has been in breach of rules of SEHK or clearing houses
 - Is or has been in breach of statutory provisions in SFO and subsidiary legislation
 - Fails to report to SFC and exchanges inability to comply with financial resources rules and requirements
 - Fails to carry out its obligations
 - Charged with or convicted of fraud or dishonesty
 - In under investigation by SFC with auditor appointed
 - Is guilty of misconduct
- SEHK Board has the following **disciplinary powers:**
 - Expel an exchange participant
 - Request an exchange participant to resign
 - Suspend an exchange participant
 - Impose a fine on an exchange participant
 - Censure an exchange participant
 - Suspend or revoke registration of responsible officer of an Exchange Participant
 - Suspend, withdraw or revoke right of access to trading system

- **Disciplinary procedures** are:
 - Board of SEHK calls a meeting to determine if case exists for disciplinary action
 - Exchange participant requested to attend a meeting to explain conduct
 - Board can decide on action (even if exchange participants fails to attend meeting)
 - Board must inform SFC of action, so SFC can determine if exchange participant can retain license
 - Board must inform HKSCC and SEOCH, if relevant
 - Board can suspend exchange participant from trading during disciplinary process
 - Exchange participant can appeal against actions by Chief Executive within 14 days
 - If exchange participant is suspended, he must appoint another participant to execute client orders
 - If exchange participant is suspended, he loses right to trade on exchange

8. TRANSACTION COSTS

- **Commission (brokerage):** freely negotiable between exchange participant and client (investor). Brokerage for IPO transactions is set at 1% of application money
- **Trading fee:** 0.005% per side of the consideration of a transaction payable by buyer and seller to SEHK (other than options, pilot programme and certain other products and market making trades in designated Exchange Traded Funds)
- **Trading tariff:** HK\$0.50 payable by buyer and seller to SEHK on each and every purchase or sale transaction
- **Transaction levy:** 0.0027% of the value of each purchase or sale of securities per side of a transaction payable by buyer and seller to SFC
- **Investor compensation levy:** 0.002% per side of the consideration of a transaction payable by buyer and seller and collected for SFC. Suspended since 19 December 2005
- **Ad valorem stamp duty:** 0.1% (rounded up to nearest dollar) on the value of the transaction, payable by both buyer and seller. There is no stamp duty on derivative warrants, callable bull and bear certificates and options trading
- **Transfer deed stamp duty:** HK\$5.00 payable by the registered holder of the share certificates (the seller) to the Government on each new transfer deed (regardless of number of shares traded)
- **Transfer fee:** HK\$2.50 per share certificate payable by the registered holder for each new share certificate issued (the buyer) to the registrar of each listed company on each new certificate issued (regardless of number of shares on the certificate)
- **Others:** Intermediaries and custodians may pass on fees paid for using the clearing, settlement, custody and nominee services of the HKSCC