



## **EXPOSURE OF SUNDRY AMENDMENTS TO THE RULES AND REGULATIONS OF THE COMMISSION**

### **Major Amendment**

1. Proposed amendment to Part C15 – Securities Clearing and Settlement Company

### **Sundry Amendments**

2. Proposed Amendment to the Rule 40(5) on type of Public Company that may file earnings forecast
3. Proposed amendment to Rule 41(4)- Rules Relating to Publication of Interim Financial Statement (Re-Exposure)
4. Proposed amendment to Schedule II of the Commission's Rules and Regulations- Insertion of penalty for diversion/misapplication of Issue Proceeds (Re-Exposure)

Details of the proposals are as follows:

### **Major Amendment**

1. **Proposed Amendments to Part C15 - Securities Clearing and Settlement Company – Rule 176-177**

The proposed rules below seek to replace the entire Part C15:

#### **New title of Part C15 – Central Counter Parties Rules (CCP)**

1. Definitions
2. Applicability
3. Registration requirements
4. Additional requirements
5. Functions
6. Governance
7. Composition of the Board
8. Appointment of Chief Executive and other Principal Officers
9. Code of conduct
10. Legal basis
11. CCP Rules



12. Access and Participation
13. Outsourcing
14. Efficiency and transparency
15. Investment policy
16. Framework for the comprehensive management of risks
17. Risk Committee
18. Liquidity risks
19. Operational risks
20. Business risks
21. Credit risks
22. Collateral requirements
23. Margin requirements
24. Default fund
25. Additional financial resources
26. Default waterfall
27. Default management procedure
28. Stress testing
29. Interoperability arrangement
30. Physical deliveries
31. Segregation and portability
32. Reports to be filed
33. Record keeping
34. Recovery and resolution

## **DEFINITIONS**

**CCP** means an entity registered by the Commission to clear derivatives contracts by adopting processes and procedures that ensure counterparties do not default on their obligations arising from performance of their contracts. A CCP can be a central counterparty CCP or a non-central counterparty CCP.

**CCP Rules** means its constitution, Articles of Incorporation, by-laws, or rules.

**Central Counterparty (CCP)** is a CCP that interposes itself between counterparties to contracts traded in one or more financial markets, becoming the buyer to every seller and the seller to every buyer and thereby ensuring the performance of open contracts.

**Clearing Member** means an entity authorized by a CCP to perform clearing services either on its own account or on behalf of other trading members or clients.



**Clearing Services** means services offered and activities performed by a clearing member in terms of the exchange rules or CCP rules, as the case may be, to facilitate clearing of derivatives contracts.

**Client** means any person or entity to which a regulated person provides securities services, and includes a person that acts as an agent for another person in relation to those services in which case it will include the agent or exclude the other person if the contractual arrangement between the parties indicates this to be the intention.

**Close link** means a situation in which two or more natural or legal persons are linked in any of the following ways: (a) participation in the form of ownership, direct or by way of control, of 20% or more of the voting rights or capital of an undertaking; (b) control; or (c) the fact that both or all are permanently linked to one and the same third person by a control relationship.

**Close-out Period** means the period which a CCP is reasonably expected to close out or transfer open positions of a defaulting clearing member.

**Collateral** means cash and other highly liquid, low risk securities collected by a CCP to protect itself and other clearing members from potential exposures that could arise as a result of default of a clearing member.

**Current exposure** means losses that a central counterparty would immediately face once a clearing member defaults. It also implies losses incurred by clearing members due to price movement.

**Defaulting Clearing Member** means a clearing member who has defaulted in the performance of its open contracts.

**Default Fund** is fund managed by the CCP, contributed to by clearing members and the CCP to protect against exposures resulting from default.

**Default Waterfall** refers to the financial safeguards available to a CCP to cover losses arising from a clearing member ("CM") default ("Default Losses"), and the order in which they would be expended.

**Derivatives** means any financial instrument or contract that creates rights and obligations and whose value depends on or is derived from the value of one or more underlying asset, rate or index, on a measure of economic value or on a default event.



**Exchange Traded Derivatives** means standardised derivatives contracts traded on a recognised exchange and cleared through a CCP.

**Extreme but Plausible Market Conditions** include the most volatile periods that have been experienced by the markets for which the CCP provides its services and a range of potential future scenarios. They shall take into account sudden sales of financial resources and rapid reductions in market liquidity.

**Financial Market Infrastructure** includes central securities depositories, central counterparties, securities settlement systems, payment systems and trade repositories.

**Futures Contract** means an agreement to buy or sell securities or commodities on an exchange at a pre-agreed price, quantity, quality and time.

**Haircut** is a risk control measure applied to underlying assets whereby the value of those underlying assets is calculated as the market value of the assets reduced by a certain percentage. Haircuts are applied by a collateral taker in order to protect itself from losses resulting from declines in the market value of a security in the event that it needs to liquidate that collateral.

**Indirect Clearing** means clearing services provided by a clearing member to a trading member or a client, through a set of contractual arrangements between the central counterparty, the clearing member and trading member/client.

**Individual Client Segregation** means a form of accounts segregation where individual client's funds are deposited in different accounts as opposed to a single omnibus account.

**Initial margin** means cash or collateral deposited by clearing members on open positions, typically representing a deposit against short term price movement. It also covers potential future exposure for the expected time between the last variation margin exchange and the liquidation of positions on the default of counterparty.

**Interoperability** means an arrangement between two or more CCPs whereby each CCP has a link with another CCP to enable two counterparties use different CCPs to clear the same derivatives contract.

**Interoperable CCP** means a CCP that has interoperability arrangement with another CCP.

**Intraday Variation Margin Calls** means requesting for replenishment of margin accounts by clearing members before the end of a business day.



**Margin Calls** means requesting for replenishment of margin accounts by clearing members at the end of a business day.

**Netting** means offsetting the value of multiple positions or payments due to be exchanged between two or more parties.

**Non-Central Counterparty CCP** is a CCP that does not operate as a counterparty to clearing members.

**Novation** means the act of replacing one party in a derivatives contract with another.

**Omnibus Client Segregation** means a form of account segregation where clients' funds are deposited in a single omnibus account in order to separate the funds from clearing members' fund.

**OTC Derivatives** means derivatives contracts agreed between parties directly without going through an exchange. The parties may agree to clear the contracts through a CCP.

**Portability** means transferring a client's accounts and funds from a defaulting member to non-defaulting member.

**Potential future exposure** means losses that a central counterparty could potentially face between the period a clearing member defaults and the time it would be reasonably expected to close out or transfer a defaulting member's open positions.

**Principal Officer** means the chief executive officer or a member of the executive management team of a CCP.

**Recovery** means the actions of a CCP, consistent with its rules, procedures and other ex ante contractual arrangements, to address any uncovered loss, liquidity shortfall or capital inadequacy, whether arising from clearing members' default or other causes (such as business, operational or other structural weaknesses), including actions to replenish any depleted pre-funded financial resources and liquidity arrangements, as necessary to maintain the FMI's viability as a going concern and the continued provision of critical services.

**Reserves** means appropriation of retained earnings for a designated purpose which is not available for dividends to the shareholder and is of a permanent nature and able to absorb losses in going concern situations.



**Resolution** refers to processes and procedures that allow for orderly winding down of a CCP to ensure minimum disruption to the financial system.

**Securities** are as defined in the Investments and Securities Act.

**Stress Market Scenario in relation to a CCP that operates in a single jurisdiction** refers to a market condition that results in default of a clearing member to which it has the largest exposure to in extreme but plausible market conditions.

**Stress Market Scenario in relation to a CCP that operates in a multiple jurisdiction** refers to a market condition that results in default of at least two clearing members to which it has the largest exposure to in extreme but plausible market conditions.

**Third-party** means a service provider whom a clearing service has been outsourced to.

**Third-Party Pricing Services** means entities/institutions that provide prices which are not readily available from exchanges.

**Trading member** means a member of an exchange who is not authorised to clear trades through a CCP.

**Value date** means the day on which the payment, transfer instruction, or other obligation is due and the associated funds and securities are typically available to the receiving participant.

**Variation margin** means margin that is transferred between clearing members to reflect current exposures resulting from actual changes in market prices of underlying securities.

## **APPLICABILITY**

These rules shall apply to entities registered by the Commission as CCPs.

## **REGISTRATION REQUIREMENTS**

1. An application for registration of a CCP shall be made in Form S.E.C. 5C contained in Schedule III to these Rules and Regulations and accompanied by:
  - a) copy of certificate of incorporation certified by the company secretary;
  - b) two copies of the Memorandum and Articles of Association certified by the Corporate Affairs Commission;



- c) latest copy of audited accounts or statement of affairs signed by its auditors and management accounts that are not more than thirty (30) days old as at the time of filing with the Commission;
  - d) two copies of existing or proposed rules and regulations, and code of conduct;
  - e) sworn undertaking to promptly furnish the Commission with copies of any amendment to the rules of the CCP;
  - f) information relating to clearing facilities, including settlement procedure;
  - g) fidelity bond representing 25% of minimum required capital;
  - h) sworn undertaking to keep such records and render such returns as may be specified by the Commission from time to time;
  - i) sworn undertaking to comply with and enforce compliance by its members with the provisions of the Act and the Commission's rules and regulations;
  - j) an application for registration of all principal officers and compliance officers on Forms SEC 2 and 2D;
  - k) information memorandum on the company, including the organizational and shareholding structure, profile of promoters, members of the board and principal officers;
  - l) evidence of publication of a notice of filing the application in at least two national newspapers;
  - m) evidence of minimum capitalization of N5 billion;
  - n) filing fee of N50,000;
  - o) processing fee of N200,000;
  - p) registration fee of N1,000,000;
  - q) registration fee of N10,000 for each of the sponsored individuals and the compliance officer;
  - r) any other documents required by the Commission from time to time.
2. An entity applying for registration as a CCP shall publish in two national newspapers and on its official website concurrently a notice of an application for such registration,



a copy of which shall be submitted to the Commission and contain the following among others:

- a) Brief information about the entity;
  - b) Name and registered addresses of the entity;
  - c) Places where the entity may be operated;
  - d) Where the CCP's proposed rules may be inspected by members of the public;
  - e) The period within, and the process, by which objections to the application may be lodged with the Commission. Such period shall not exceed 21 days from the date of publication.
3. The Commission may, after consideration of any objection received and subject to the conditions which it may consider appropriate, register the applicant to perform the functions of a CCP if the applicant complies with the relevant requirements of the Act and the rules made pursuant to it.

### **ADDITIONAL REQUIREMENTS**

A registered CCP shall have:

1. Sufficient assets and resources, which include financial, management and human resources with appropriate experience, to perform its functions as set out in these Rules;
2. An effective and reliable infrastructure to facilitate its clearing operations or services;
3. A comprehensive risk management process;
4. Appropriate systems, controls and procedures that are reliable and secure and have adequate scalable capacity;
5. Adequate mechanisms for the purpose of reviewing, monitoring and evaluating its internal controls;
6. Proper arrangements for security and back-up procedures to ensure the integrity of the records of transactions cleared through its facilities;
7. Arrangements for the efficient and effective supervision of clearing members to ensure compliance with its rules and directives.
8. Consistent communication procedures and standards relating to securities, futures contracts and member identification.





## **FUNCTIONS**

The functions of a registered CCP shall be to:

1. Interpose itself between counterparties to contracts traded in one or more financial markets through the process of novation, legally binding agreement or open offer system;
2. Facilitate post trade management functions;
3. Implement a margin system that establishes margin levels commensurate with the risks and particular attributes of each product, portfolio and the market;
4. Collect and manage collateral held for the due performance of the obligations of clearing members;
5. Establish and maintain a default fund to mitigate the risk of default by a clearing member and to ensure, where possible, that the obligations of that clearing member continue to be fulfilled;
6. Have a clearly defined default management system and waterfall where the obligations of the defaulting clearing member, other clearing members and the CCP are legally and clearly managed;
7. Provide for portability in the case of default of a clearing member;
8. Perform any other function as may be determined by the Commission from time to time.

## **GOVERNANCE**

1. A CCP shall have:
  - a) Rules and procedures that support financial stability, safety and efficiency of its clearing activities;
  - b) A charter for the Board and Management that clearly stipulates responsibility and accountability which should be made publicly available;
  - c) Standard operating procedures that stipulate its entire business processes and operations and must be duly approved by management;



- d) Processes to identify, assess, and manage potential conflicts of interest of members of the Board, principal officers, employees or any person directly or indirectly linked to the Board.
2. The Board and Management of a CCP shall have the required mix of skills and competence to discharge their duties;
3. The Board of a CCP shall consider the interest of relevant stakeholders before making critical decisions.

### **COMPOSITION OF THE BOARD**

1. A CCP shall have a Board, which should be independent of Management;
2. Appointment of Board members shall be subject to approval of the Commission;
3. The Board shall comprise of:
  - a) A Chairman;
  - b) A Chief Executive Officer;
  - c) At least one Independent Director;
  - d) At least one clearing member;
4. The majority of Board members shall be Non-Executive Directors;
5. The Board shall have all the relevant Board Committees, including a Risk Management Committee.

### **APPOINTMENT OF CHIEF EXECUTIVE AND PRINCIPAL OFFICERS**

1. The Chief Executive Officer of a CCP shall hold office for a period of five (5) years in the first instance and may be re-appointed for a further period of five (5) years and no more;
2. The appointment of a Chief Executive Officer and Principal Officers of a CCP shall be subject to the prior approval of the Commission;
3. The Chief Executive Officer and the other Principal Officers of a CCP shall be registered by the Commission as sponsored individuals;



4. The Chief Executive Officer and other Principal Officers of a CCP shall:
  - a) Be persons of proven integrity with no record of criminal conviction;
  - b) Hold at least a university degree or its equivalent;
  - c) Have at least ten (10) years cognate experience in the financial markets;
  - d) Not have been found complicit in the operation of an institution that has failed or been declared bankrupt or has had its operating license revoked as a result of mismanagement or corporate governance abuses;
  - e) Not have been found liable for financial impropriety or any other misdemeanor by any court, panel, regulatory agency or any professional body or previous employer;
  - f) Comply with any other criteria which the Commission may, in the public interest, determine from time to time.

## **CODE OF CONDUCT**

A CCP shall have a Code of Conduct, approved by the Commission, for its staff and clearing members provided that they shall also be required to comply with the Code of Conduct for Capital Market Operators approved by the Commission as contained in the Schedule of these Rules and Regulations.

## **LEGAL BASIS**

1. A CCP shall have:
  - a) Rules, procedures, and contracts that are clear, understandable, enforceable and consistent with relevant laws and regulations;
  - b) Clearly defined default management procedures that are legally binding and enforceable;
2. The legal basis of a CCP shall provide high level of certainty with respect to the following in case of default by a clearing member:
  - a) Rights to use and dispose of, collateral;
  - b) Authority to transfer ownership rights or property interests; and
  - c) Rights to make and receive payments.
3. A CCP shall have legal basis that is clear and made available to relevant stakeholders.



## **CCP RULES**

1. A CCP shall make rules pursuant to the Act and these Rules to govern its operations and clearing members;
2. The rules of CCP shall:
  - a) Be clear, transparent and enforceable for all its operations and activities;
  - b) Have a high level of certainty.
  - c) Provide for settlement finality
3. The rules shall provide for:
  - a) Membership criteria which should be fair and transparent
  - b) Effective regulation of members to ensure compliance with laid down rules and regulations
  - c) Complaints management process for disputes resolution
  - d) Disciplinary proceedings against erring members
  - e) Process of communicating with clearing members
  - f) Margin requirements and management of collateral
  - g) Default management process

## **ACCESS AND PARTICIPATION**

A CCP shall:

1. Ensure fair and transparent access to its services and put in place the necessary controls against the risks to which it is exposed by its clearing members;
2. Have membership criteria that are:
  - a) Fair and allow open access to all members and where applicable members' clients;
  - b) Risk-based, publicly disclosed and adequate to ensure that its clearing members meet appropriate operational, financial, and legal requirements to allow them to fulfill their obligations in a timely manner.
3. Ensure that its clearing members and other FMIs to which it has interoperability arrangement have the necessary operational capacity, legal powers and risk management measures to prevent risks which it may be exposed to;



4. Monitor compliance by its clearing members with the laid down regulations and require members to provide information on their activities and any developments on their inability to comply with the laid down regulations.

## **OUTSOURCING**

1. Where a CCP outsources any of its functions, services or activities, it shall take full responsibility for the functions, services and activities outsourced.
2. A CCP that outsources any of its functions, services or activities shall ensure that the outsourcing does not affect the discharge of its obligations to clearing members and clients.
3. A CCP shall:
  - a) Ensure that outsourcing of functions, services and activities does not change the terms and conditions of its registration with the Commission;
  - b) Ensure that outsourcing its functions, services and activities does not affect its effective management of risks;
  - c) Not outsource its major risk management functions without the prior approval of the Commission.
4. Where a CCP outsources any of its functions, services and activities to a third-party, it shall ensure that the Commission has oversight and supervisory functions over the third-party;
5. A CCP shall ensure that a third-party to which it outsources any of its functions, services or activities has the necessary business continuity arrangement;
6. A CCP shall have the necessary expertise and resources to evaluate the functions, services and activities provided by a third-party;
7. A third-party shall protect any confidential information of the CCP, clearing members and clients.

## **EFFICIENCY AND TRANSPARENCY**

1. A CCP shall:



- a) Design its operations and processes to meet the need of its clearing members and the market in general. The design shall include:
  - i. specific clearing and settlement arrangements;
  - ii. operating structure;
  - iii. scope of products cleared;
  - iv. use of technology
- b) Ensure that the objectives of the design in (a) above are measurable in terms of minimum service standards;
- c) Carry out a review of the efficiency of its operations and processes at least once in a year.

## **INVESTMENT POLICY**

### 1. A CCP shall:

- a) Have an investment policy that is consistent with its overall risk-management strategy which should be fully disclosed to clearing members;
- b) Not prioritize pursuit of profit over financial soundness and liquidity risk management;
- c) Consider its overall credit risks exposure to a single obligor;
- d) Invest its cash collateral in liquid assets with low credit, liquidity and market risks.

### 2. A CCP investment shall:

- a) Be fully secured to mitigate against credit risk;
- b) Allow for quick liquidation with little, if any, adverse price effect;

## **FRAMEWORK FOR COMPREHENSIVE MANAGEMENT OF RISKS**

A CCP shall have a framework, policies and procedures for comprehensive management of risks which should cover:

1. Legal basis that is clear, transparent and enforceable for each material aspect of its operations;
2. Credit exposures to clearing members and those arising from its payments clearing, and settlement processes where applicable;



3. Collateral and margin management requirements that are adequate and risk based;
4. Maintenance of adequate liquid resources to ensure timely fulfillment of payment obligations with a high degree of confidence;
5. Risk management tools to effectively manage systemic risks arising from its interconnectedness with other CCPs and FMIs;
6. Identification of critical situations that may impact its going concern status in terms of operations as well as development of appropriate policies for business continuity, recovery plans or winding-down;
7. Establishment of effective information management system and control that allows it to promptly get information needed for comprehensive management of risks.

### **RISK COMMITTEE**

1. A CCP shall have a Risk Committee that will continuously identify, measure, monitor, and manage the range of risks that may arise.
2. The Committee:
  - a) Shall comprise representatives of clearing members, independent members of the Board and representative (s) of clients;
  - b) May invite employees and relevant stakeholders to attend meetings in a non-voting capacity;
  - c) Shall report directly to the Board.
3. None of the groups of representatives required in 2(a) above shall have a majority representation on the risk committee;
4. The Committee shall meet every quarter, and where there is an urgency to have a meeting, it shall not hesitate to convene.

### **LIQUIDITY RISKS**

1. A CCP shall:
  - a) have highly liquid resources and committed line of credit to enable it meet up with its financial obligations;



- b) have diversified portfolio of liquid resources and avoid undue concentration with respect to any relevant asset class and issuer;
  - c) monitor and control the concentration of its liquidity risk exposure to clearing members and other entities;
  - d) meet its obligations timely and with high degree of certainty in a stress market scenario
  - e) assess the liquidity risks it faces including the risks that its members may not be able to settle their obligations;
  - f) actively monitor and control its liquidity risk exposures and funding needs at the level of CCP as an entity or as part of a group structure;
  - g) periodically test the ability to convert its highly liquid securities into cash;
  - h) determine the amount and regularly test the sufficiency of its liquid resources through rigorous stress testing;
  - i) where an asset ceases to meet the criteria of highly liquid securities, remove the asset from its portfolio of highly liquid securities within 30 days;
2. No instruments borrowed in a securities lending transaction shall qualify as highly liquid securities;
  3. All highly liquid securities held by a CCP shall not be pledged, either explicitly or implicitly, to secure, collateralize or credit-enhance any transaction and cannot otherwise be subject to any further commitment.

## **OPERATIONAL RISKS**

A CCP shall:

1. Have clearly defined operational reliability objectives and policies designed to achieve those objectives.
2. Ensure that it has scalable capacity adequate to handle increasing stress volumes and achieve its service-level objectives.
3. Have comprehensive physical and information security policies that address all potential vulnerabilities and threats.
4. Have a business continuity plan to mitigate the risk of major disruptions.
5. Identify, monitor, and manage operational risks posed by its staff, clearing members, other FMIs and service utility providers.

## **BUSINESS RISKS**

1. A CCP shall:





- a) Have policies and procedures to identify, monitor and manage general business risks;
- b) Maintain a viable plan for raising additional equity should its equity fall close to or below the capital required;
- c) Hold sufficient liquid net assets to enable it operate as a going concern if it incurs general business losses. The net asset position shall be determined by:
  - i. its general business risk profile; and
  - ii. the length of time required to achieve a recovery or orderly wind down.

## **CREDIT RISKS**

### 1. A CCP shall:

- a) Have in place a comprehensive framework for managing its credit exposure to clearing members and their affiliates. The framework shall take into consideration the following:
  - i. current exposures;
  - ii. potential future exposures
- b) Identify different sources of credit risks and regularly measure its credit exposures, and use appropriate risk-management tools to control these risks;
- c) Closely monitor its exposure to individual clearing members and their clients;
- d) Monitor changes in creditworthiness of its clearing members;

2. A CCP may decide to place limits on its credit exposures irrespective of whether collateral has been provided.

## **COLLATERAL REQUIREMENTS**

### 1. A CCP shall:

- a) Only accept highly liquid assets with low credit, and market risks as collateral;
- b) Establish prudent valuation practices and develop haircuts that are regularly tested and take into account stressed market conditions;
- c) Ensure that it carries out mark to market valuation of collateral on a real-time basis as well as monitor credit, liquidity and market risks of all collateral regularly.



2. A CCP shall ensure that:
  - a) Its haircuts are adequate to compensate the expected decline in value by the time the collateral is expected to be liquidated;
  - b) Its haircuts are stable and conservative enough to withstand period of stressed market conditions;
  - c) It is able to liquidate its collateral quickly following the default of a clearing member;
  - d) Its clearing members do not post their own debt or equity securities, or debt or equity of companies closely linked to them as collateral.
3. A CCP shall avoid concentrating its collateral in one class of asset.
4. Where a CCP accepts cross-border collateral, it shall:
  - a) Take steps to mitigate risks associated with its use and ensure that the collateral can be used in a timely manner;
  - b) Assess the foreign exchange risks and set haircuts to adequately compensate for the additional risks.
5. A CCP shall have a collateral management system that:
  - a) Is well-designed and operationally flexible;
  - b) Accommodates changes in the ongoing monitoring and management of collateral;
  - c) Allows for the timely calculation and execution of margin calls, the management of margin call disputes, and accurate daily reporting of levels of initial and variation margin;
  - d) Tracks the extent of reuse of collateral, both cash and non-cash;
  - e) Has functionality to accommodate the timely deposit, withdrawal, substitution and liquidation of collateral.

## **MARGIN REQUIREMENTS**

1. A CCP shall have a:
  - a) System that stipulates margin requirements proportionate to the risks and attributes of the relevant products and the markets;
  - b) Reliable source of timely price data for:



- i) Exchange traded products, contracts and derivatives to determine margin requirements;
  - ii) OTC derivatives contracts.
2. Where a CCP:
  - a) Utilizes data from third-party pricing services, it shall regularly evaluate the data's reliability and accuracy;
  - b) Uses its own valuation model, it shall validate the model under different market scenarios at least annually.
3. Where price data from an exchange and third-party pricing services are not readily available, a CCP shall have procedures and sound valuation techniques to determine the value of products, contracts and derivatives.
4. A CCP shall adopt:
  - a) More conservative margin models for OTC derivatives;
  - b) A risk-based initial margin requirement that is sufficient to cover potential future exposures to clearing members between the last margin call and expected close-out period arising from default of clearing members;
  - c) An appropriate close-out period for each product it clears which should consider:
    - i. Historical price of the products or derivatives;
    - ii. Liquidity;
    - iii. Impact of a clearing member's default on prevailing market conditions;
    - iv. Stressed market conditions;
    - v. Position concentrations.
5. The initial margin requirement of a CCP shall take into consideration changes in market conditions.
6. During periods of high volatility, a CCP shall increase its margin requirements to compensate for the additional risks.
7. A CCP shall:
  - a) Mark clearing member positions to market and collect variation margin at least daily;
  - b) Have the authority and capacity to make intra-day variation margin calls and payments;



- c) Regularly review the performance of its model and overall margin system taking into account a wide range of parameters and assumptions that reflect possible market conditions.

### **DEFAULT FUND**

1. A CCP shall:
  - a) Establish and maintain a default fund to cover losses not covered by margin requirements;
  - b) Set a minimum amount to which the fund must not go below;
  - c) Establish criteria for calculating clearing members' individual contributions to the fund which should be dependent on the level of exposure to clearing members.
2. A CCP may establish more than one default fund for different classes of instruments it clears.

### **ADDITIONAL FINANCIAL RESOURCES**

1. A CCP shall maintain additional financial resources which must:
  - a) cover potential losses not covered by margin requirements and the default fund;
  - b) be freely available to the CCP;
  - c) not form part of the minimum capital requirement of the CCP;
  - d) not be used for day to day operations of the CCP;
  - e) not be used for potential general business losses of the CCP.
2. A CCP shall ensure that its default fund and additional financial resources are adequate in a stress market scenario.
3. A CCP shall:
  - a) have documented process for measuring additional financial resources;
  - b) adopt a framework that defines extreme but plausible market conditions.

### **DEFAULT WATERFALL**

1. A CCP shall clearly stipulate the order of hierarchy of the financial resources to be utilized in covering the resultant losses in the event of default of a clearing member,
2. A CCP shall not use margins posted by clearing members to cover losses of a defaulting clearing member;



3. A CCP may require non-defaulting clearing members to provide additional funds in the event of a default of another clearing member.

## **DEFAULT MANAGEMENT PROCEDURE**

1. A CCP shall have rules and procedures that enable it to continue to meet its obligations to non-defaulting clearing members in the event of a clearing member's default;
2. The rules and procedures shall:
  - a) clearly define what circumstances constitute default of a clearing member;
  - b) allow the CCP to use any financial resources it maintains according to the default waterfall to cover losses and contain liquidity pressures arising from default of a clearing member;
  - c) stipulate guidelines for replenishing financial resources maintained by the CCP over an appropriate time horizon following a default of a clearing member to enable the CCP continue operating in a safe and sound manner;
  - d) ensure that the application of previously provided collateral will not be subject to prevention, stay, or reversal by any applicable law;
  - e) facilitate prompt close out or transfer of defaulting clearing member's open positions.
3. Where clearing members agree to bid upfront for the open positions of a defaulting member, the CCP shall, upon default by any clearing member, auction the open positions of the defaulting clearing member;
4. Where a CCP is unable to immediately close out or transfer open positions of a defaulting member, it shall hedge the positions as an interim risk management tool;
5. A CCP shall involve its clearing members and other stakeholders in periodic review and testing of its default management procedure to ensure effectiveness and practicability.

## **STRESS TESTING**

1. A CCP shall:
  - a) regularly test the sufficiency of its total financial resources available in the event of a default in extreme but plausible market conditions;
  - b) test the models and parameters used to adopt margin requirements, default fund contributions, collateral requirements and other risk control mechanisms;
  - c) conduct reverse stress tests aimed at identifying the extreme scenarios and market conditions in which its total financial resources would not provide sufficient cover.



2. The result of stress testing shall be reported to the Commission;
3. The frequency of the tests shall be higher when the products cleared become more volatile, less liquid or when exposure to clearing members increases significantly;

### **INTEROPERABILITY ARRANGEMENT**

1. A CCP may enter into an interoperability arrangement with another CCP where applicable;
2. Where a CCP enters into an interoperability arrangement with another CCP, it shall:
  - a) Identify, monitor and manage all interoperability related risks;
  - b) Agree on their respective rights and obligations, including the applicable law governing their relationships where the CCPs operates in different jurisdictions;
  - c) Identify and manage potential spillover effects from the failure of interoperable CCP.
3. A CCP in an interoperability agreement shall be able to cover its current and potential future exposures through collection and application of margin.

### **PHYSICAL DELIVERIES**

1. Where a CCP clears transactions that involve physical delivery of instruments or commodities, it shall:
  - a) Make appropriate regulations and guidelines on its obligations and those of the clearing members;
  - b) Identify and manage all risks and costs associated with the delivery;
  - c) Identify and manage the specific risks associated with storage facilities taking into consideration the characteristics of the commodities involved;
  - d) Arrange and manage the possibility of alternative assets or location as well as timing of the delivery if necessary;
  - e) Arrange for deployment and training of relevant personnel to handle the delivery;
  - f) Arrange for insurance policy of the instruments or commodities;
  - g) Maintain accurate record management system that represent the actual holdings of the instruments;
2. A CCP shall:



- a) Stipulate in its regulations the various asset classes acceptable for clearing that end in physical delivery;
- b) Establish a system to monitor the performance of its clearing members to ensure that they have the resources and system to discharge their physical delivery obligations.

3. Where a CCP:

- a) Is required to warehouse and transport commodities, it shall make the necessary arrangement taking into consideration the type and characteristic of the relevant commodities;
- b) Adopts the system of matching clearing members with physical storage and delivery obligations of commodities from a risk management perspective, it shall:
  - i. Clearly state the legal delivery obligations of the clearing members;
  - ii. Stipulate if compensation would be sought from it in the event of loss by either the receiving clearing member or the delivering clearing member.

4. Where a clearing member is holding margin involving matched clearing members, it shall not release the margin until it confirms that both clearing members have satisfied their respective obligations;

5. In carrying out stress testing, the CCP shall take into consideration the impact of relevant stress scenarios in terms of both defaulters' positions and possible price changes during liquidation.

### **SEGREGATION AND PORTABILITY**

1. A CCP shall have a segregation and portability arrangement that distinguishes between positions and collateral of:

- a) one clearing member from another clearing member;
- b) clearing members from the assets of the CCP;
- c) clearing members from those of their clients in an omnibus account.

2. Clearing members shall have adequate segregation and portability arrangement to protect clients' positions and collateral in the event of default of a clearing member;

3. A clearing member shall offer its clients the choice between omnibus client segregation and individual client segregation;



4. A CCP shall maintain a portability arrangement that enables it transfer the positions and collateral of a defaulting clearing member's client to non- defaulting clearing member(s);
5. A CCP and clearing member shall publicly disclose protection and costs associated with individual account segregation;
6. A CCP shall disclose any legal or operational constraints, that may impair its ability to segregate or transfer a clearing member's client's positions and related collateral.

### **RECOVERY AND RESOLUTION**

1. A CCP shall have processes and procedures to achieve adequate recovery when its going concern status is threatened so that its critical operations and services can be sustained.
2. The processes and procedures shall clearly spell out pre-agreed obligations of clearing members and the CCP itself in the event of recovery.
3. Where recovery is no longer feasible, the processes and procedures shall provide for orderly winding down to avoid causing distress to the system.
4. The processes and procedures shall make arrangement for transferring critical operations of the CCP to another CCP where available.

### **REPORTS TO BE FILED**

1. A CCP shall file with the Commission:
  - a) A daily report of its clearing activities;
  - b) Its operational report within 5 working days after the end of each calendar month;
  - c) Its quarterly financial statements and operational report separately within 1 month after the end of every quarter. This report should include information on functions, services or activities it outsourced;
  - d) Its annual report and audited financial statement within 3 months after the end of each financial year;
  - e) Any other information which the Commission may require from time to time.

### **RECORD KEEPING**

A CCP shall:





1. Maintain records of its activities and services for a period of not less than 6 years;
2. Maintain records of all contracts cleared for a period of not less than 6 years from the termination of each contract;
3. Make available upon request by the Commission any record kept;
4. Keep its record safe, secured and in a manner which will make it easy for retrieval;
5. Ensure that records kept can be retrieved in their original form without alteration;
6. Upon request, provide the Commission with post trade and real-time access to transactions and or positions records.

### **Sundry Amendments**

#### **1. PROPOSED AMENDMENT TO RULE 40(5): RULE ON EARNINGS FORECAST**

##### **Full Text of Existing Rule**

Public companies may notify the relevant securities exchanges as soon as it is known that the forecast will not be realized and the reasons for the non-realization shall be stated.

##### **Proposed Amendment**

Public quoted companies shall notify the relevant securities exchanges as soon as it is known that the forecast will not be realized and the reasons for the non-realization shall be stated.

**Justification:** *The amendment aligns the rule to the provision of S.64 of ISA 2007*

#### **2. PROPOSED AMENDMENT TO RULE 41(4): PUBLICATION OF INTERIM FINANCIAL STATEMENT**

##### **Full Text of Existing Rule:**

All public companies shall publish their "signed" quarterly balance sheet, income statement and cash flow statements in at least one (1) national daily newspaper. However, the accounting policies, notes and other relevant information shall be posted on the company's website which address shall be disclosed in the newspaper publication. The publication shall be signed by the officers mentioned in (3) above.



**Proposed Amendment:**

All public companies shall publish their “signed” quarterly statement of financial position, income statement and cash flow statements in at least one (1) national daily newspaper; the publication shall not be later than thirty (30) days from the end of each quarter.

However, the accounting policies, notes and other relevant information to the quarterly report shall be posted on the company’s website which address shall be disclosed in the newspaper publication. The publication on the company’s website shall not be later than thirty (30) days from the end of each quarter and shall be on their website up to the end of the succeeding quarter. The publication shall be signed by the officers mentioned in (3) above.

Provided that public unlisted companies, companies listed on the alternative securities market or such other platforms approved by the Commission, may publish their “signed” quarterly statement of financial position, income statement and cash flow statements, accounting policies, notes and other relevant information on the company’s website and the relevant exchange’s website/platform where applicable.

**Justification:** *Some companies claim that the Rule does not give a specific time within which the publication is to be made. Also the proposed rule will reduce the cost of publication for small companies listed on the alternative securities market or such other approved platforms.*

**3. PROPOSED AMENDMENT TO SCHEDULE II OF THE COMMISSION’S RULES AND REGULATIONS: INSERTION OF PENALTY FOR DIVERSION/MISAPPLICATION OF ISSUE PROCEEDS**

**Proposed amendment: Addition to Schedule II**

Diversion/misapplication of Issue proceeds – Any Issuer in default shall be required to pay the ongoing Monetary Policy Rate +2% on the amount of proceeds diverted/misapplied.

Notwithstanding the above, the Issuer shall:

- i. Be suspended from accessing the capital market for such period as



may be determined by the Commission;

- ii. Be liable to a public censure (publication of the Issuer's default on the Commission's website).

**Justification:** *Arising from the comments received on the exposed Rule, other instances of misapplication of issue proceeds were disclosed. To curtail such diversion/misapplication of issue proceeds, the market recommended a stiffer penalty which has been reflected in the re-draft.*