

SCHEDULE

PART II

Recognition requirements for investment exchanges: default rules in respect of market contracts

Default rules in respect of market contracts

10.—(1) The exchange must have default rules which, in the event of a member of the exchange being or appearing to be unable to meet his obligations in respect of one or more market contracts, enable action to be taken in respect of unsettled market contracts to which he is a party.

(2) The rules may authorise the taking of the same or similar action in relation to a member who appears to be likely to become unable to meet his obligations in respect of one or more market contracts.

(3) The rules must enable action to be taken in respect of all unsettled market contracts, other than those entered into by a recognised clearing house for the purposes of or in connection with the provision of clearing services for the exchange.

Content of rules

11.—(1) This paragraph applies as regards contracts falling within section 155(2)(a) of the Companies Act.

(2) The rules mentioned in paragraph 10 must provide—

- (a) for all rights and liabilities between those party as principal to unsettled market contracts to which the defaulter is party as principal to be discharged and for there to be paid by one party to the other such sum of money (if any) as may be determined in accordance with the rules;
- (b) for the sums so payable in respect of different contracts between the same parties to be aggregated or set off so as to produce a net sum; and
- (c) for the certification by or on behalf of the exchange of the net sum payable or, as the case may be, of the fact that no sum is payable.

(3) The reference in sub-paragraph (2) to rights and liabilities between those party as principal to unsettled market contracts does not include rights and liabilities—

- (a) in respect of margin; or
- (b) arising out of a failure to perform a market contract.

(4) The rules may make the same or similar provision, in relation to non-members designated in accordance with the procedures mentioned in sub-paragraph (5), as in relation to members of the exchange.

(5) If such provision is made as is mentioned in sub-paragraph (4), the exchange must have adequate procedures—

- (a) for designating the persons, or descriptions of person, in respect of whom action may be taken;
- (b) for keeping under review the question which persons or descriptions of person should be or remain so designated; and
- (c) for withdrawing such designation.

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- (6) The procedures must be designed to secure that—
 - (a) a person is not, or does not remain, designated if failure by him to meet his obligations in respect of one or more market contracts would be unlikely adversely to affect the operation of the market; and
 - (b) a description of persons is not, or does not remain, designated if failure by a person of that description to meet his obligations in respect of one or more market contracts would be unlikely adversely to affect the operation of the market.
- (7) The exchange must have adequate arrangements—
 - (a) for bringing a designation or withdrawal of designation to the attention of the person or description of persons concerned; and
 - (b) where a description of persons is designated, or the designation of a description of persons is withdrawn, for ascertaining which persons fall within that description.

12.—(1) This paragraph applies as regards contracts falling within section 155(2)(b) of the Companies Act.

- (2) The rules mentioned in paragraph 10 must provide—
 - (a) for all rights and liabilities of the defaulter under or in respect of unsettled market contracts to be discharged and for there to be paid by or to the defaulter such sum of money (if any) as may be determined in accordance with the rules;
 - (b) for the sums so payable by or to the defaulter in respect of different contracts to be aggregated or set off so as to produce a net sum;
 - (c) for that sum—
 - (i) if payable by the defaulter to the exchange, to be set off against any property provided by or on behalf of the defaulter as cover for margin (or the proceeds of realisation of such property) so as to produce a further net sum;
 - (ii) if payable by the exchange to the defaulter, to be aggregated with any property provided by or on behalf of the defaulter as cover for margin (or the proceeds of realisation of such property); and
 - (d) for the certification by or on behalf of the exchange of the sum finally payable or, as the case may be, of the fact that no sum is payable.
- (3) The reference in sub-paragraph (2) to the rights and liabilities of a defaulter under or in respect of an unsettled market contract includes (without prejudice to the generality of that provision) rights and liabilities arising in consequence of action taken under provisions of the rules authorising—
 - (a) the effecting by the exchange of corresponding contracts in relation to unsettled market contracts to which the defaulter is party;
 - (b) the transfer of the defaulter's position under an unsettled market contract to another member of the exchange;
 - (c) the exercise by the exchange of any option granted by an unsettled market contract.
- (4) A "corresponding contract" means a contract on the same terms (except as to price or premium) as the market contract but under which the person who is the buyer under the market contract agrees to sell and the person who is the seller under the market contract agrees to buy.
- (5) Sub-paragraph (4) applies with any necessary modifications in relation to a market contract which is not an agreement to sell.
- (6) The reference in sub-paragraph (2) to the rights and liabilities of a defaulter under or in respect of an unsettled market contract does not include, where he acts as agent, rights or liabilities of his arising out of the relationship of principal and agent.

Notification to other parties affected

13. The exchange must have adequate arrangements for ensuring that—

- (a) in the case of unsettled market contracts with a defaulter acting as principal, parties to the contract are notified as soon as reasonably practicable of the default and of any decision taken under the rules in relation to contracts to which they are a party; and
- (b) in the case of unsettled market contracts with a defaulter acting as agent, parties to the contract and the defaulter's principals are notified as soon as reasonably practicable of the default and of the identity of the other parties to the contract.

Cooperation with other authorities

14. The exchange must be able and willing to cooperate, by the sharing of information and otherwise, with the Secretary of State, any relevant office-holder within the meaning of section 189 of the Companies Act, and any other authority or body having responsibility for any matter arising out of, or connected with, the default of a member of the exchange or any non-member designated in accordance with the procedures mentioned in paragraph 11(5) above.

Margin

15.—(1) Where the exchange provides clearing services, the rules of the exchange must provide that in the event of a default, margin provided by the defaulter for his own account is not to be applied to meet a shortfall on a client account.

(2) This paragraph is without prejudice to the requirements of any rules relating to clients' money made by the Authority under sections 138 and 139 of the Act.