

**RECOGNISED INVESTMENT EXCHANGES AND
RECOGNISED CLEARING HOUSES SOURCEBOOK
(AMENDMENTS TO RECOGNITION REQUIREMENTS) INSTRUMENT 2009**

Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of section 157 (Guidance) of the Financial Services and Markets Act 2000.

Commencement

- B. This instrument comes into force on 15 June 2009.

Amendments to the Handbook

- C. The Glossary of definitions is amended in accordance with Annex A to this instrument.
- D. The Recognised Investment Exchanges and Recognised Clearing Houses sourcebook (REC) is amended in accordance with Annex B to this instrument.

Citation

- E. This instrument may be cited as the Recognised Investment Exchanges and Recognised Clearing Houses Sourcebook (Amendments to Recognition Requirements) Instrument 2009.

By order of the Board
28 May 2009

Annex A

Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text.

- market contract* a market contract as described in section 155 of the Companies Act 1989 or article 80 of the Companies (No 2) (Northern Ireland) Order 1990 which is in summary:
- (a) a contract entered into by a *member* or *designated non-member* of an *RIE* which is either:
- (i) a contract made on the exchange or an exchange to whose undertaking the exchange has succeeded; or
 - (ii) a contract in the making of which the *member* or ~~designated non-member~~ *designated non-member* was subject to the rules of the exchange or of an exchange to whose undertaking the exchange has succeeded;
- (b) a contract entered into by an *RIE* or *RCH*, in its capacity as such, with one of its , or with an *RCH* or with an *RIE*, for the purpose of:
- (i) enabling the rights and liabilities of that *member*, or clearing house or other investment exchange, under transactions in a transaction, to be settled; or
 - (ii) providing central counterparty clearing services (as described in section 155(3A) of the Companies Act 1989) to that *member* or clearing house or other investment exchange.

Annex B

Amendments to the Recognised Investment Exchanges and Recognised Clearing Houses sourcebook (REC)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

2.17 Recognition requirements relating to the default rules of UK recognised bodies

2.17.1 G The text of part of regulation 3 (Interpretation) of and Parts II and IV of the Schedule to the Recognition Requirements Regulations is set out below.

2.17.1A UK Regulation 3 (Interpretation) of the Recognition Requirements Regulations:

...

“default fund” means the sum of the default fund contributions by the members or designated non-members of a [recognised investment exchange] to that exchange or by one [recognised investment exchange] to another or by the members of a [recognised clearing house] to that clearing house or by one [recognised clearing house] to another to the extent those contributions have not been returned or otherwise applied;

“default fund contribution” has the same meaning as in section 188(3A) of the Companies Act [1989];”

...

2.17.2 UK Schedule to the Recognition Requirements Regulations, Part II

Paragraph 10 (Default rules in respect of market contracts)	
...	
(4)	<u>Sub-paragraph (5) applies where the exchange has arrangements for transacting business with, or in relation to common members of, a [recognised clearing house] or another [recognised investment exchange].</u>
(5)	<u>A [UK RIE] must have [default rules] which in the event of the clearing house or the investment exchange being or appearing to be unable to meet its obligations in respect of one or more [market contracts], enable action to be taken in respect of unsettled [market contracts] to which that person is a party.</u>
Paragraph 11 (Content of rules)	

...	
Paragraph 12 (Content of rules)	
(1)	This paragraph applies as regards contracts falling within section 155(2)(b) or (c) of the Companies Act [1989].
(2)	The [<i>default rules</i>] must provide -
(a)	...
(b)	for the sums so payable by or to the defaulter in respect of different contracts <u>entered into by the defaulter in one capacity for the purposes of section 187 of the Companies Act [1989]</u> to be aggregated or set off so as to produce a net sum;
(bb)	<u>if relevant, for that sum to be aggregated with, or set off against, any sum owed by or to the investment exchange by or to AP under an indemnity given or reimbursement or similar obligation in respect of a margin set off agreement in which the defaulter chose to participate so as to produce a net sum;</u>
(e)	for that sum-
(i)	if payable by the defaulter to the [UK RIE], 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 [UK RIE] 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
(c)	<u>for the net sum referred to in [(2)](b) or, if relevant, the net sum referred to in [(2)](bb) -</u>
(i)	<u>if payable by the defaulter to the exchange, to be set off against -</u>
(aa)	<u>any property provided by or on behalf of the defaulter as cover for margin (or the proceeds of realisation of such property);</u>
(bb)	<u>to the extent (if any) that any sum remains after set off under (aa), any default fund contribution provided by the defaulter remaining after any application of such</u>

			<u>contribution;</u>
		(ii)	<u>to the extent (if any) that any sum remains after set off under (i), to be paid from such other funds, including the default fund, or resources as the exchange may apply under its default rules;</u>
		(iii)	<u>if payable by the exchange to the defaulter, to be aggregated with -</u>
		(aa)	<u>any property provided by or on behalf of the defaulter as cover for margin (or the proceeds of realisation of such property);</u>
		(bb)	<u>any default fund contribution provided by the defaulter remaining after any application of such contribution; and</u>
	(d)	...	
(2A)	<u>In sub-paragraph (2), “margin set off agreement” means an agreement between the exchange and AP permitting any eligible position to which the Participant Member is party with the exchange and any eligible position to which the Participant Member is party with AP to be taken into account in calculating a net sum owed by or to the Participant Member to either the exchange or AP and/or margin to be provided to, either or both, the exchange and AP.</u>		
(2B)	<u>In sub-paragraph (2) -</u> <u>“AP” means a [recognised clearing house] or another [recognised investment exchange] of whom a Participant Member is a member;</u> <u>“eligible position” means any position which may be included in the set off calculation;</u> <u>“Participant Member” means a person who</u> <u>(a) is a member of the exchange;</u> <u>(b) is a member or participant of AP; and</u> <u>(c) chooses to participate, in accordance with the rules of the exchange, in such agreement.</u>		
(2C)	<u>The property, contribution, funds or resources referred to in (2)(c), against which the net sum is to be set off (or with which it is to be aggregated) are subject to any unsatisfied claims arising out of the default of a defaulter before the default in relation to which the calculation is being made.</u>		

...	
<u>Paragraph 12A (Content of rules)</u>	
<u>The rules of the [UK RIE] must provide that, in the event of a default, any default fund contribution provided by the defaulter shall only be used in accordance with paragraph 12(2)(c)(i) or (ii).</u>	
...	
<u>Paragraph 14 (Cooperation with other authorities)</u>	
<u>The [UK RIE] must be able and willing to cooperate, by the sharing of information and otherwise, with the Secretary of State, any <i>relevant office-holder</i> and any other authority or body having responsibility for any matter arising out of, or connected with, the default of a <i>member</i> of the [UK RIE] or any [<i>designated non-member</i>] or the default of a [<i>recognised clearing house</i>] or another [<i>recognised investment exchange</i>].</u>	
<u>Paragraph 15 (Margin)</u>	
(1)	<u>Where the [UK RIE] provides clearing services, the [<i>default rules</i>] of the [UK RIE] 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 <i>client</i> <i>client</i> account <u>other than a client account of the defaulter.</u></u>
(2)	...
(3)	<u>For the purposes of this paragraph, “client account of the defaulter” means an account held by the [UK RIE] in the name of the defaulter in which relevant transactions effected by the defaulter have been recorded.</u>
(4)	<u>In sub-paragraph (3) “relevant transaction” has the same meaning as in regulation 16(1) of the Financial Markets and Insolvency Regulations 1991.</u>

2.17.3 UK Schedule to the Recognition Requirements Regulations, Part IV

<u>Paragraph 24 (Default rules in respect of market contracts)</u>	
...	
(3)	<u>Sub-paragraph (4) applies where the clearing house has arrangements for transacting business with, or in relation to common members of, a [<i>recognised investment exchange</i>] or another [<i>recognised clearing house</i>].</u>
(4)	<u>A [UK RCH] must have [<i>default rules</i>] which in the event of the investment exchange or the clearing house being or appearing to</u>

	be unable to meet its obligations in respect of one or more [<i>market contracts</i>], enable action to be taken in respect of unsettled [<i>market contracts</i>] to which that person is a party.	
Paragraph 25 (Content of rules)		
(1)	The [<i>default rules</i>] must provide -	
	(a)	...
	(b)	for the sums so payable by or to the defaulter in respect of different contracts entered into by the defaulter in one capacity for the purposes of section 187 of the Companies Act [1989] to be aggregated or set off so as to produce a net sum;
	(bb)	if relevant, for that sum to be aggregated with, or set off against, any sum owed by or to the clearing house by or to AP under an indemnity given or reimbursement or similar obligation in respect of a margin set off agreement in which the defaulter chose to participate so as to produce a net sum;
	(e)	for that sum—
	(i)	if payable by the defaulter to the [<i>UK RCH</i>], 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 [<i>UK RCH</i>] 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
	(c)	for the net sum referred to in [(1)](b) or, if relevant, the net sum referred to in [(1)](bb)
	(i)	if payable by the defaulter to the clearing house, to be set off against -
	(aa)	any property provided by or on behalf of the defaulter as cover for margin (or the proceeds of realisation of such property);
	(bb)	to the extent (if any) that any sum remains after set off under (aa), any default fund contribution provided by the defaulter remaining after any application of such contribution;

	(ii)	<u>to the extent (if any) that any sum remains after set off under (i), to be paid from such other funds, including the default fund, or resources as the clearing house may apply under its [default rules];</u>
	(iii)	<u>if payable by the clearing house to the defaulter, to be aggregated with</u>
	(aa)	<u>any property provided by or on behalf of the defaulter as cover for margin (or the proceeds of realisation of such property);</u>
	(bb)	<u>any default fund contribution provided by the defaulter remaining after any application of such contribution; and</u>
	(d)	...
(1A)		<u>In sub-paragraph (1), “margin set off agreement” means an agreement between the clearing house and AP permitting any eligible position to which the Participant Member is party with the clearing house and any eligible position to which the Participant Member is party with AP to be taken into account in calculating a net sum owed by or to the Participant Member to or by either the clearing house or AP and/or margin to be provided to, either or both, the clearing house and AP.</u>
(1B)		<u>In sub-paragraph (1A) -</u> <u>“AP” means a [recognised investment exchange] or another [recognised clearing house] of whom a Participant Member is a member;</u> <u>“eligible position” means any position which may be included in the set off calculation;</u> <u>“Participant Member” means a person who -</u> <u>(a) is a member of the clearing house;</u> <u>(b) is a member or participant of AP; and</u> <u>(c) chooses to participate, in accordance with the rules of the clearing house, in such agreement.</u>
(1C)		<u>The property, contribution, funds or resources referred to in (1)(c), against which the net sum is to be set off (or with which it is to be aggregated) are subject to any unsatisfied claims arising out of the default of a defaulter before the default in relation to which the calculation is being made.</u>

(2)	The reference in sub-paragraph (1) ... includes ... authorising -
(a)	the effecting by the [market contracts] <i>UK RCH</i> of corresponding contracts in relation to unsettled <i>market contracts</i> to which the defaulter is party;...
...	
...	
<u>Paragraph 25A (Content of rules)</u>	
<u>The rules of the [UK RCH] must provide that in the event of a default, any default fund contribution provided by the defaulter shall only be used in accordance with paragraph 25(1)(c)(i) or (ii).</u>	
...	
<u>Paragraph 27 (Cooperation with other authorities)</u>	
The [UK RCH] must be able and willing to cooperate, by the sharing of information and otherwise, with the Secretary of State, any <i>relevant office-holder</i> and any other authority or body having responsibility for any matter arising out of or connected with the default of a <i>member</i> of the [UK RCH] or the default of a [<i>recognised investment exchange</i>] or another [<i>recognised clearing house</i>].	
<u>Paragraph 28 (Margin)</u>	
(1)	The [<i>default rules</i>] of the [UK RCH] 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 <i>client</i> <u>client account other than a client account of the defaulter.</u>
(2)	...
(3)	<u>For the purposes of this paragraph, “client account of the defaulter” means an account held by the [UK RCH] in the name of the defaulter in which relevant transactions effected by the defaulter have been recorded.</u>
(4)	<u>In sub-paragraph (3) “relevant transaction” has the same meaning as in regulation 16(1) of the Financial Markets and Insolvency Regulations 1991.</u>

- 2.17.4 G *UK RIEs* which, under their rules, have *market contracts* and *UK RCHs* which, under their rules, enter into *market contracts* are required to have *default rules*. The *default rules* must enable the *UK recognised body* to take action in relation to a *member* ~~or~~, an interoperating *RIE* or *RCH* and, for an *RIE*, a *designated non-member*, who appears unable, or likely to become unable to meet his obligations in respect of one or more unsettled

market contracts.

- 2.17.5 G This action is to provide for all rights and liabilities of the defaulter (including a recognised investment exchange or a recognised clearing house) and any counterparty to an unsettled *market contract* to be discharged and for there to be paid between the defaulter and each counterparty one sum representing the net amount of all the contracts between them. ~~Where property has been~~ Property provided by the defaulter as cover for margin, (or any relevant sum owed under a margin set-off arrangement), or any remaining default fund contribution provided by the defaulter, ~~that property~~ may be set off against any amount owing by the defaulter. ...