

SECTION 8

MINIMUM STANDARDS APPLICABLE TO A CLEARING MEMBER

The minimum standards set out below shall be complied with by all Self Clearing Members and Professional Clearing Members on an ongoing basis, upon admission in terms of these Rules.

8.1. Capital Requirements

8.1.1 (a) Minimum Capital Requirements applicable to Clearing Members:

Clearing Members shall maintain the minimum capital requirements as set out below:

For a Self Clearing Member;

- (i) If a Trading Participant of the CSE; a minimum liquid capital of Rs. 50 Million and a minimum shareholders' equity of Rs. 125 Million or 50% of the stated capital, whichever is higher.
- (ii) If a Custodian Bank a minimum total shareholders' equity of Rs. 500 Million.

For a Professional Clearing Member;

- (i) If a Trading Participant of the CSE; a minimum total shareholders' equity of Rs. 500 Million or 50% of the stated capital, whichever is higher and an additional shareholders' equity of Rs. 50 Million for each Limited Clearing Member Client in respect of whom a clearing and settlement services are provided.
- (ii) If a Commercial Bank licensed by the CBSL or a Non-Banking Finance Company licensed by the CBSL, a minimum total shareholders' equity of Rs.500 million and an additional shareholders' equity of Rs. 50 Million for each Limited Clearing Member Client in respect of whom clearing and settlement services are provided.

For the purposes of this Rule 8.1.1 (a);

'liquid capital' shall have the same meaning as defined in Annexure 2 of the Trading Participant Rules of the CSE.

'total shareholders' equity' shall be computed in accordance with the applicable Sri Lanka Accounting Standards.

- (b) Periodic Updates on the compliance with the capital requirements by Clearing Members who are Trading Participants

Clearing Members who are Trading Participants of the CSE shall submit to the Clearing House on a quarterly basis, together with the Quarterly Statements as required in terms of Rule 8.1.2 (i) (a), a written confirmation confirming that it is in compliance with the relevant capital requirements specified in Rule 8.1.1 (a) above.

(c) Non-compliance with Rule 8.1.1 (a)

(i) In the event a Clearing Member fails to meet the capital requirements set out in Rules 8.1.1 (a) (as applicable), such Clearing Member shall immediately notify the Clearing House, in writing, and take necessary steps to comply with the applicable minimum capital requirement/s within a period of thirty (30) calendar days from the date of non-compliance.

A Professional Clearing Member which fails to meet the capital requirements shall also notify all its Limited Clearing Member Clients with whom the Professional Clearing Member has entered into written agreements in terms of Rule 7.2.2 above.

(ii) In the event a Self Clearing Member fails to meet the applicable minimum capital requirement/s within the period referred to in Rule 8.1.1 (c) (i) above, the Self Clearing Member shall comply with the following requirements with regard to its Clients:

(aa) The Self Clearing Member shall, on the date of expiration of the thirty (30) calendar day period referred to in Rule 8.1.1(c)(i) above, issue a written notice to all its Clients, with a copy to the Clearing House, notifying them of the non-compliance and providing such Clients of a period of up to [thirty (30)] calendar days from the date of such written notice to engage a Trading Participant or a Depository Participant that has an appropriate arrangement for the clearing and settlement of Trades;

(bb) Notwithstanding anything to the contrary in these Rules, the Self Clearing Member shall continue to and be obliged to clear and settle any Trades executed by such Self Clearing Member on behalf of its Clients on or before the [thirtieth (30th)] calendar day from the from the date of such written notice.

On the expiration of the said thirty y (30) calendar day period referred to in items (aa) and (bb) above, if the Self Clearing Member has not rectified the non-compliance, the Clearing House shall prohibit such Self Clearing Member from carrying out the clearing functions through the Clearing House in relation to CCP Settled Trades and a notice will be simultaneously published by the CSE Clear on its website setting out the non-compliance with applicable minimum capital requirements upon the clearing member being informed of the same by CSE Clear.

- (iii) In the event a Professional Clearing Member fails to rectify the non-compliance within the period referred to in Rule 8.1.1 (c) (i) above, the Professional Clearing Member shall comply with the following requirements with regard to its Clients, including the Limited Clearing Member Clients with whom the Professional Clearing Member has existing written agreements entered into in terms of Rule 7.2.2 above:
- (aa) The Professional Clearing Member shall, on the date of expiration of the thirty (30) calendar day period referred to in Rule 8.1.1(c)(i) above, issue a written notice to all its Clients, with a copy to the Clearing House, notifying them of the non-compliance and providing such Clients of a period of up to [thirtieth (30)] calendar days from the date of such written notice to engage the services of another Trading Participant or a Depository Participant that has an appropriate arrangement for the clearing and settlement of Trades, which shall, in the case of Limited Clearing Member Clients, mean the services of another Professional Clearing Member.
 - (bb) The Limited Clearing Member Clients shall enter into written agreements in terms of Rule 7.2.2 with other Professional Clearing Member to engage the services of such Professional Clearing Members to clear and settle the CCP Settled Trades of the Limited Clearing Member Clients, within thirty (30) days from the issue of the written notice referred to in item (aa) above.
 - (cc) Notwithstanding anything to the contrary in these Rules, the Professional Clearing Member shall continue to and be obliged to clear and settle any Trades executed by such Professional Clearing Member on behalf of its Clients, other than Limited Clearing Member Clients, on or before the [thirtieth (30th)] calendar day from the from the date of such written notice referred in (aa) above.
 - (dd) Notwithstanding anything to the contrary contained in these Rules, the Professional Clearing Member shall continue to and be obliged to clear and settle the Trades executed by Limited Clearing Member Clients on or before the earlier of (A) the thirtieth (30th) calendar day from the from the date of such written notice, or (B) the effective date of the written agreement by the Limited Clearing Member Client with a new Professional Clearing Member (which effective date shall be notified by the Limited Clearing Member Client to the Clearing House), whichever comes first.

On the expiration of the said thirty (30) calendar day period day period referred to in items (aa), (bb), (cc) and (dd) above, if the Professional Clearing Member has not rectified the non-compliance, the Clearing House prohibit such Professional Clearing Member from carrying out the clearing functions through the Clearing House on behalf of its Clients, including Limited Clearing Member Clients and a notice will be simultaneously published by the CSE Clear on its website setting out the non-compliance with applicable minimum capital requirements upon the clearing member being informed of the same by CSE Clear.

- (iv) The written agreement between the Professional Clearing Member which has failed to rectify the non-compliance within the period referred to in Rule 8.1.1 (c) (i) above and a Limited Clearing Member Client shall be in force until the full settlement of the Trades referred to in this item (cc) above and shall be deemed to be terminated, ipso facto, upon the full and final settlement of all such Trades in accordance with these Rules. If the Limited Clearing Member Client has entered into a written agreement with a new Professional Clearing Member before the full and final settlement of such Trades, the new Professional Clearing Member which enters into a written agreement with the Limited Clearing Member Client in terms of this Rule 8.1.1(c)(iii) shall, notwithstanding any provision to the contrary contained in Rule 7.2.4 above, be entitled to clear and settle Trades of the Limited Clearing Member Client executed on or after the effective date of such written agreement (which effective date shall be notified by the new Professional Clearing Member to the Clearing House in writing), even though the written agreement of the Limited Clearing Member Client with the Professional Clearing Member which has failed to rectify the non-compliance referred to in Rule 8.1.1 may still be in force.

The termination of the written agreement shall be immediately notified by the Professional Clearing Member and the Limited Clearing Member Client to the Clearing House.

- (v) In the event any Limited Clearing Member Client does not enter into a written agreement with a new Professional Clearing Member within thirty (30) days from the issue of the written notice referred to in item (iii)(aa) above, the Clearing Member status of the Limited Clearing Member Client shall be suspended by the Clearing House immediately upon the expiration of such thirty (30) day period, and the Clearing House immediately notify the CSE of such suspension.
- (vi) The prohibition imposed on the Clearing Member shall be lifted upon such Clearing Member meeting the applicable minimum capital requirement/s.

In the case of a Professional Clearing Member which opts to become a Self Clearing Member in terms of Rule 7.3 of these Rules, pursuant to the failure to meet the capital requirements for a Professional Clearing Member, by fulfilling all relevant entry requirements for a Self Clearing Member, the prohibition imposed on the carrying out of clearing functions through the Clearing House on behalf of Clients (other than Limited Clearing Member Clients) shall be lifted upon the change of status becoming effective.

- (vii) In the event the Clearing Member fails to rectify the non-compliance within three (3) months from the date of prohibition referred to in Rule 8.1.1 (c) (ii) or Rule 8.1.1(c)(iii) above, as the case may be, the Clearing House shall terminate the Clearing Member status of such Clearing Member.
- (viii) The Clearing House shall publish a notice on its website stating the non-compliance with the applicable Rules and the enforcement action initiated by the Clearing House in respect of the Clearing Member concerned.

- (ix) The Clearing House shall notify the CSE, CDS and the SEC regarding the enforcement action initiated against the Clearing Member.

8.1.2 Financial Statements of Clearing Members:

- (i) The Self Clearing Members and Professional Clearing Members shall submit to the Clearing House, certified copies of the following:
 - a) quarterly financial statements of such Clearing Member within two (02) months from the end of the respective quarter, provided however that where the Clearing Member publishes its annual audited financial statements within three (03) months from the end of the financial year, such Clearing Member shall be exempt from publishing its quarterly financial statement for the fourth quarter of the respective year; and,
 - b) audited financial statements of the Clearing Member within five (05) months from the end of the financial year.

Provided however, this Rule 8.1.2 (i) shall not be applicable to Clearing Members that have its Securities listed on the CSE and have published its financial statements in accordance with the Listing Rules of the CSE.

- (ii) If the Clearing Member fails to submit certified copies of such financial statements within the respective timelines set out in Rule 8.1.2 (i) above, the Clearing House shall impose a fine of Rupees Twenty-Five Thousand (Rs. 25,000/-) for every month of delay from the expiry of the stipulated time period.
- (iii) Additionally, the Clearing House shall have the right to suspend the Clearing Member status of a Clearing Member for continuous non-submission of quarterly/audited financial statements. In such event, the Clearing House shall notify the SEC, CSE and the CDS of such suspension.

8.2 Systems and Operations of a Clearing Member

A Self Clearing Member or a Professional Clearing Member shall ensure that:

- (i) its systems and connectivity to the Clearing and Settlement system and facilities operate properly at all times and have adequate redundancy and scalable capacity to accommodate current and anticipated settlement volumes; and
- (ii) it complies with the terms and conditions in any agreement with, and any other requirements imposed by, the Clearing House for accessing the Clearing or Settlement system and facilities or in relation to settlement under these Rules.
- (iii) its back office systems operate smoothly and properly at all times and have adequate redundancy and scalable capacity to accommodate all current depository functions and future enhancements; and

- (iv) it complies with the terms and conditions in any agreement with, and any other requirements imposed by the CSE Clear in relation to systems and operations required to support and facilitate depository functions to the extent stipulated in these Rules.
- (v) A Clearing Member shall maintain complete and accurate records, which enable it to identify at all times, specific amounts of such monies and assets deposited with it by each client in connection with such clients' trades which are or are to be, cleared or settled through CSE Clear.
- (vi) Clearing Members shall maintain sufficient, qualified and competent employees at all times to perform business operations in terms of these Rules and applicable requirements.
- (vii) A Clearing Member shall ensure segregation of key functions of the Clearing Members to minimize and manage conflict of interests among these functions.

8.3 Business Continuity Requirements

- 8.3.1 The Self Clearing Members and Professional Clearing Members shall, at all times, have in place, review and maintain disaster recovery and business continuity arrangements that are adequate to ensure the timely recovery of its usual operations having regard to the nature and extent of the business carried on by that Clearing Member and any matters as may be specified by the Clearing House from time to time.
- 8.3.2 The Clearing House may, at any time, require a Clearing Member to undertake testing of its disaster recovery and business continuity arrangements at such times and in such manner as may be specified by the Clearing House.
- 8.3.3 A Clearing Member shall, at all times maintain adequate back up procedures to ensure the integrity and recoverability of its records and locate its disaster recovery hardware and related facilities off site.

8.4 Other Risk Management Requirements

- 8.4.1 The Self Clearing Members and Professional Clearing Members shall be responsible for the monitoring and management of risk, including determination of the nature and extent of the significant risks which the Clearing Member can reasonably undertake.
- 8.4.2 The management of the Clearing Member shall oversee the Clearing Member's risk management framework and policies and ensure that the management maintains a sound system of risk management and internal controls including but not limited to maintaining adequate staff and facilities for monitoring its cash flows and funding requirements and maintaining sufficient liquidity for its day to day operations.
- 8.4.3 The Clearing Member shall, upon the request of the Clearing House, make available details which include the following;

- (a) information needed by the Clearing House to make an informed assessment of the Clearing Member's risk management and internal control systems;
- (b) a description of the principal risks (including liquidity, financial, operational, compliance, information technology, legal, environmental, social or political risk categories) applicable to the Clearing Member and the manner in which such risks are being managed or mitigated;
- (c) an explanation of the Clearing Member 's approach towards identifying, measuring and monitoring its key and emerging risks, and an elaboration of its approach towards the governance and management of these risks; and,
- (d) an explanation of the manner in which the management of the Clearing Member has assessed the prospects of the company, together with the period under consideration and the justification/s for selection of such time period.

8.5 Internal Audit Requirements

A Clearing Member which clears and settles CCP Settled Trades shall cause its internal auditors to conduct an internal audit of its operations annually or at such times and within such scope as prescribed by the Clearing House and to submit a report of each internal audit conducted and the follow-up actions taken to the Clearing House by such time as may be specified by the Clearing House.

8.6 Submission of Compliance Report

A Self Clearing Member or Professional Clearing Member shall submit a compliance report annually to the Clearing House setting out in detail, the manner in which the Clearing Member has complied with, or the steps taken by the Clearing Member to comply with these Rules.