

AIX Central Securities Depository

Market Notice 2019-01-30_01

AIX CSD Management of Settlement Fails

Date	30/01/2019
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Pursuant to Rule 7.1.2 of AIX CSD Business Rules, AIX CSD hereby informs:

1 Purpose

The purpose of this Market Notice is to detail the mechanism and procedures of AIX CSD for the management of settlement fails.

2 Definitions

Definitions used in these procedures are identical to definitions in AIX CSD Business Rules.

Annual Guarantee Cap means the total amount that AIX CSD may pay during a calendar year to cover losses that occur during the performance of either Buy-in / Sell-out or Cash Compensation.

Available Guarantee means the lower amount of Event Guarantee Cap and Annual Guarantee Cap less any amounts paid (and not yet recovered) for events in the current calendar year.

Buy-in / Sell-out means the process described in 4.4.

Cash Compensation means the process described in 4.5.

Cash Compensation Amount means the amount that the Failing Participant shall pay to AIX CSD and amount that AIX CSD shall pay to Non-Failing Participants following Cash Compensation.

Event Guarantee Cap means the total amount that AIX CSD may pay upon any single event to cover losses that occur during the performance of either Buy-in / Sell-out or Cash Compensation.

Failing Participant means the participant causing a settlement to fail due to not delivering the required funds or securities.

Fair Price means the price used by AIX CSD for the purposes of calculating the Cash Compensation Amount. Fair Price would generally be the mid-price of the best bid and ask at 17:05 pm on T+3. In case bid and ask are absent at 17.05, the last traded price would be considered as Fair price. The Fair Price may also be adjusted by Valuation Adjustment as described in 4.5.3.

Non-Failing Participant means the counterparty of a settlement transaction with a **Failing Participant**.

Spread Rate means the information used to adjust the Fair Price. This is to take into account differences in bid and offer prices on the market.

Valuation Adjustment means an adjustment of the Fair Price that AIX CSD may apply at its own discretion. It would be applied in cases where AIX CSD assess that performing the buy-in or sell-out on the market of the failed settlement would significantly impact trading prices.

3 Identifying settlement fails

- 3.1** Settlement fails are any delivery obligations (securities and/or cash) that are not delivered on the intended settlement date (ISD) (which equals trade date + 2 **Business Days**).
- 3.2** Participant is not deemed Failing Participant if it fails to deliver securities or cash due to the failure of another participant to deliver securities or cash in AIX CSD.
- 3.3** All settlement fails may give rise to monetary penalties as set out in Market Notice 2018-12-11_01 on “AIX CSD Fees for unsettled Transactions”.

4 Management of settlement fails

- 4.1** AIX CSD manages settlement fails through the process of Buy-in / Sell-out, as described in 4.5.
- 4.2** Notwithstanding section 4.1, AIX CSD manage settlement fails through the process of Cash Compensation in the following cases:
 - a) sufficient amount of securities is not available for purchase;
 - b) the liquidity strain of the transaction for AIX CSD is too important
 - c) the market losses may exceed the Available Guarantee Amount.
- 4.3** For settlement fails that is rectified within or on ISD + 1 business day, the further 4.5 – 4.6 do not apply.
- 4.4** For settlement fails that are not rectified at end of day on ISD + 1 business day, the following items 4.5 to 4.6 shall apply.
- 4.5** Buy-in / Sell-out procedure includes:
 - 4.5.1** AIX CSD cancels the failing settlement transactions in the AIX CSD system.
 - 4.5.2** AIX CSD enters into transactions on AIX via AIX Trading Members (other than the Failing Participant and Non-Failing Participant) which are the opposite of the transactions entered into by the Failing Participant.
 - 4.5.3** AIX CSD replace the settlement transactions cancelled (as per 4.5.1). They then create settlement transactions where AIX CSD replace the Failing Participant as counterparty to the transaction.

- 4.5.4** Transactions where AIX CSD are buying securities on the market are referred as Buy-in Transactions. Transactions where AIX CSD are selling securities on the market are referred to Sell-out transactions.
- 4.5.5** Description of a buy-in transaction is specified in Annex 2.
- 4.6** Cash Compensation procedure includes:
- 4.6.1** AIX cancel the failing settlement transactions in the AIX CSD system.
- 4.6.2** AIX calculate one or more Cash Compensation Amounts that are:
- 4.6.2.1 to be paid by the Failing Participant to AIX CSD within 7 working days of invoice issuance accompanied by specifications of the amount;
- 4.6.2.2 to be paid by AIX CSD to the Non-Failing Participant.
- 4.6.3** Procedure for calculation of Cash Compensation Amounts includes:
- 4.6.3.1 AIX CSD calculate Cash Compensation Amount separately for each cancelled settlement transaction.
- 4.6.3.2 For transactions where the Failing Participant is the buyer of securities:
- 4.6.3.2.1 Cash Compensation Amount is calculated in accordance with the following formula:
number of securities * (original transaction price – Fair Price * (1 – Spread Rate))
- 4.6.3.3 For transactions where the Failing Participant is the seller of securities:
- 4.6.3.3.1 Cash compensation Amount is calculated in accordance with the following formula:
number of securities * (Fair Price * (1 + Spread Rate) – original transaction price)
- 4.6.3.4 Positive amounts are payable by the Failing Participant to AIX CSD and by AIX CSD to the Non-Failing Participant. Negative amounts are treated as zero.
- 4.6.3.5 If AIX CSD assess that the size of the transaction would drive the market price down, AIX CSD may apply downward Valuation Adjustments to the Fair Price. Maximum of such Valuation Adjustments is specified in Annex 1.
- 4.6.4** AIX CSD sum the Cash Compensation Amounts of all transactions into one amount for each participant.
- 4.7** Description of Cash Compensation is specified in Annex 3.

5 Guarantee fund and AIX CSD liability limitations

5.1 AIX CSD, upon settlement fails, cancel the original settlement transactions and either perform necessary trades on the AIX market or calculate cash compensation to be paid to Non-Failing Participants.

5.2 AIX CSD guarantee funds for such purpose up to total amounts of:

- KZT 740 million per calendar year (Annual Guarantee Cap); and
- KZT 370 million per any single event (Event Guarantee Cap)

5.2.1.1 A single event may comprise several settlement instructions in several securities traded over several days, however, limited to one participant.

5.2.1.2 Available Guarantee is the available amount for any single event. Available Guarantee shall be defined as the lower amount of the Event Guarantee Cap and the Annual Guarantee Cap less any amounts paid (and not recovered) for events in the current calendar year.

5.2.1.3 The date on which AIX CSD initiate buy-in / close-out or the Cash Compensation processes is the relevant date for determining the year when an event occurred.

5.3 If the compensation amounts to be paid to Non-Failing Participants exceed the Available Guarantee:

5.3.1 AIX CSD reduce the compensation amounts for all Non-Failing Participants pro rata;

5.3.2 AIX CSD ensure that the Cash Compensation paid out in total does not exceed the Available Guarantee;

5.3.3 AIX CSD advance any funds received from the Failing Participant (or the administrator of the Failing Participant in case of bankruptcy / insolvency / unwinding) pro-rata to Non-Failing Participants until the original Cash Compensation amount has been paid in full.

Annex 1

Spread rates and Maximum Valuation Adjustments on AIX listed and traded securities

Security	Spread Rate	Max Valuation Adjustment
All AIX listed securities	1%	10%

Annex 2

Example of Buy-in transaction AIX Transaction:

Date	Buying Broker	Buying Broker Account	Selling Broker	Selling Broker Account	ISIN	Quantity	Price (KZT)	Amount (to be settled)
1	Broker A	Client 1	Broker B	Client 2	KZ001	100	8000	80.000

Broker B failed to deliver the securities on ISD (day 3) and on ISD +1 (day 4).
At the end of day 4 the last traded price is 9000,00.

On day 4 (end-of-day):

AIX CSD cancel the settlement transaction in the AIX CSD system.

AIX CSD transfer KZT 100.000 to Broker X for the purchase of the shares (as we do not know what the actual transaction price will be the next day).

AIX CSD order Broker X (with which AIX CSD has a client account) to buy 100 KZ001.

AIX CSD enter a settlement transaction into its system where AIX CSD (from its client account with Broker X) deliver 100 KZ001 to Broker A (the sub-account of Client 1) for KZT 8000 per share.

AIX CSD notify both parties that it will perform a buy-in of 100 KZ001 at the risk and expense of Broker B.

On day 5:

Broker X successfully buys 100 KZ001 on behalf of AIX CSD at a price of 9200 per share. To be settled on day 7.

AIX CSD sends invoice to Broker B where it should pay to AIX CSD within 7 working days:

KZT 12.000 (to cover the market loss incurred by AIX CSD)

KZT amount to cover the brokerage fees levied by Broker X to AIX CSD

KZT equivalent of USD 1,000 as a service charge payable to AIX CSD for the execution of the buy-in.

On day 7:

The AIX CSD purchase of 1000 KZ001 (at a price of 9200) settles.

The AIX CSD sell of 1000 KZ001 to Broker A (client 1) settles.

AIX CSD requires Broker X to return the KZT 80.000 to AIX CSD's account.

The Available Guarantee is now KZT 159.988.000 (160 million less the 12.000 which has not yet been recuperated).

Within day 12:

Broker B pays its invoice to AIX CSD.

Available Guarantee is again KZT 160 million.

Annex 3

Example of Cash Compensation

AIX Transaction:

Date	Buying Broker	Buying Broker Account	Selling Broker	Selling Broker Account	ISIN	Quantity	Price (KZT)	Amount (to be settled)
1	Broker A	Client 1	Broker B	Client 2	KZ001	50.000	8.000	400.000.000

Broker B failed to deliver the securities on ISD (day 3) and on ISD +1 (day 4).

At the end of day 4 the last traded price is 9000,00. Best Bid / Ask are 8.950 and 9.050 respectively.

The liquidity needed (for the purchase of the securities) of estimated 450 million is more than the Available Guarantee. Therefore AIX CSD proceed with Cash Compensation.

Available ask orders towards the end of trading hours totaled 10.000 securities and, in AIX CSD assess a purchase of 50.000 securities in the market would have a significant impact on the trading price.

Maximum Valuation Adjustment is 10% for KZ001. Spread Rate is 1%.

On day 4 (end-of-day):

AIX CSD cancel the settlement transaction in the AIX CSD system.

AIX CSD perform calculation of Cash Compensation:

Fair price in the market (9.000) is adjusted upwards by 10% to 9.900.

Number of shares * (Fair Price * (1 + Spread Rate) – original transaction price)) becomes:

$$50.000 * (9.900 * (1 + 0,01) - 8.000) = 99.950.000$$

AIX CSD notify both parties that the settlement transaction in AIX CSD has been cancelled and that AIX CSD has proceeded to calculate Cash Compensation due to the size of the transaction. Also that the estimated current market price of the securities has been adjusted upwards by 10% from KZT 9.000 to KZT 9.900.

With a Spread Rate of 1%, original share price of 8.000 and volume of 50.000 securities, the cash compensation is calculated to be 99.950.000.

AIX CSD to send an invoice to Broker B of this amount payable within 7 business days.

AIX to credit Broker A, as the Non-Failing Participant, the equal amount.

Should you have any questions in relation to this letter please feel free to contact AIX Post-Trade Department at ptd@aix.kz.