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ANNEXURE 2
PROPOSED AMENDMENTS IN RELATION TO THE
PROPOSED FRAMEWORK FOR DISCRETIONARY TRADING

RULES AND DIRECTIVES OF BURSA MALAYSIA DERIVATIVES BERHAD (“BMD RULES AND DIRECTIVES”)

PROPOSED AMENDMENTS TO THE BMD RULES AND DIRECTIVES
IN RELATION TO THE PROPOSED FRAMEWORK FOR DISCRETIONARY TRADING

| AMENDMENTS TO THE BMD RULES | | | | |
|-----------------------------|---|------|--|--|
| RULE | EXISTING PROVISIONS | RULE | AMENDED PROVISIONS | RATIONALE |
| 1.01 | New provision | 1.01 | <p>Definition</p> <p><u>Discretionary Account</u> An account for trades executed by a Trading Participant on behalf of a Client pursuant to an arrangement where the Client authorises the Trading Participant to trade on the Client’s behalf on a discretionary basis.</p> | To set out the definition of “Discretionary Account” for clarity and consequential to the prescription of the framework for discretionary trading. |
| 4.17 | <p>Discretionary Account</p> <p>(1) A Trading Participant must not operate a discretionary account on behalf of a Client unless written authorisation of the Client has been obtained, and the account has been approved in writing by a person appointed by the Trading Participant to approve such accounts. Where a Trading Participant is properly authorised in writing by a Client to operate a discretionary account on behalf of that Client, it must:</p> | 4.17 | <p>Discretionary Account</p> <p>(1) —A Trading Participant <u>or a Registered Representative must not operate when operating a Discretionary Account</u> on behalf of a Client unless written authorisation of the Client has been obtained, and the account has been approved in writing by a person appointed by the Trading Participant to approve such accounts. Where a Trading Participant is properly authorised in writing by a Client to operate a</p> | Propose to amend Rule 4.17 on Discretionary Account to take a less prescriptive approach in the Rules and to set out the obligations with respect to Discretionary Account in the TP’s Directives No. 2.01(2)-002 (Directive on Readiness Audit – Self Assessment Approach, Declaratory Approach and Green Lane), No. 3.36-001 (Directive for Compliance |

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| | <p>(a) maintain full and complete records of each exercise of that discretionary authority showing the name of the Client, the details of the Contract and the date and time the transaction is effected and the name of the Registered Representative executing the order;</p> <p>(b) ensure that in the exercise of the discretion no trading is entered into which is excessive having regard to the financial resources of that Client; and</p> <p>(c) ensure that in the exercise of the discretion, no conflict of interest arises.</p> <p>(2) A Trading Participant, Head of Dealing and Registered Representative must not, in relation to a discretionary account, execute any orders for the sale or purchase of Contracts which are excessive in size or frequency in view of the financial resources and nature of such account.</p> | | <p>discretionary account on behalf of that Client, it must comply with the requirements the Exchange prescribes in respect of Discretionary Accounts.</p> <p><i>[Refer to Directives No. 2.01(2)-002, 3.36-001 and 4-001]</i></p> <p>(a) maintain full and complete records of each exercise of that discretionary authority showing the name of the Client, the details of the Contract and the date and time the transaction is effected and the name of the Registered Representative executing the order;</p> <p>(b) ensure that in the exercise of the discretion no trading is entered into which is excessive having regard to the financial resources of that Client; and</p> <p>(c) ensure that in the exercise of the discretion, no conflict of interest arises.</p> <p>(2) A Trading Participant, Head of Dealing and Registered Representative must not, in relation to a discretionary account,</p> | Officers) and No. 4-001 (Directive on Conduct of Business) instead. |

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| | <p>(3) A Compliance Officer must review the acceptance of each discretionary account to determine that the person appointed by the Trading Participant to accept the account had a reasonable basis for believing that the Client is able to understand and bear the risks of the strategies or transactions proposed, and he must maintain a record of the basis for his determination.</p> <p>(4) Each discretionary order must be reviewed by a Compliance Officer and identified as a discretionary order at the time of entry.</p> | | <p>execute any orders for the sale or purchase of Contracts which are excessive in size or frequency in view of the financial resources and nature of such account.</p> <p>(3) A Compliance Officer must review the acceptance of each discretionary account to determine that the person appointed by the Trading Participant to accept the account had a reasonable basis for believing that the Client is able to understand and bear the risks of the strategies or transactions proposed, and he must maintain a record of the basis for his determination.</p> <p>(4) Each discretionary order must be reviewed by a Compliance Officer and identified as a discretionary order at the time of entry.</p> | |

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| PARAGRAPH | EXISTING PROVISIONS | PARAGRAPH | AMENDED PROVISIONS | RATIONALE |
| Directive on Readiness Audit – Self Assessment Approach, Declaratory Approach and Green Lane (No. 2.01(2)-002) | | | | |
| 2(2) | An applicant wishing to commence new activities requiring the Exchange's approval only must also first undertake a readiness audit in accordance with this Directive. These activities are: (a) the relocation or change of business address of its Principal Office; (b) the offering of discretionary account trading facilities to clients; and (c) the commencement of proprietary trading. | 2(2) | An applicant wishing to commence new activities requiring the Exchange's approval only must also first undertake a readiness audit in accordance with this Directive. These activities are: (a) the relocation or change of business address of its Principal Office; (b) the offering of e Discretionary a Account trading facilities to e Clients; and (c) the commencement of proprietary trading. | Proposed amendment is consequential to the insertion of the definition of Discretionary Account. |
| 4.2 | Activities Subject to paragraph 4.3, the Exchange may apply the Green Lane Policy to the following types of activities: (a) the relocation or change of business address of its Principal Office 2; | 4.2 | Activities Subject to paragraph 4.3, the Exchange may apply the Green Lane Policy to the following types of activities: (a) the relocation or change of business address of its Principal Office 2; | Proposed amendment is consequential to the insertion of the definition of Discretionary Account. |

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| | (b) the offering of discretionary account trading facilities to clients; and (c) the commencement of proprietary trading. | | (b) the offering of e Discretionary a Account trading facilities to e Clients; and (c) the commencement of proprietary trading. | |
| Directive for Compliance Officers (No. 3.36-001) | | | | |
| Annex 1 (c)(xiv) of Appendix 1 on Guidelines for Compliance Functions | <p>DUTIES AND RESPONSIBILITIES OF THE COMPLIANCE OFFICER</p> <p><i>to review, monitor and supervise other supervisory measures to ensure compliance</i></p> <p>review discretionary accounts to ensure compliance with rules and that transaction are not in excess of clients' financial resources;</p> | Annex 1 (c)(xiv) of Appendix 1 on Guidelines for Compliance Functions | <p>DUTIES AND RESPONSIBILITIES OF THE COMPLIANCE OFFICER</p> <p><i>to review, monitor and supervise other supervisory measures to ensure compliance</i></p> <p>review eDiscretionary aAccounts <u>for the following:</u></p> <p><u>(a) to ensure compliance with Exchanges' business rules, the Rules and Directives and that transaction are not in excess of clients' financial resources;</u></p> <p><u>(b) the acceptance of Discretionary Accounts and to ensure that prior written authorisation from the client has been obtained;</u></p> | In view of streamlining the compliance obligations in operating a Discretionary Account for both BMS Rules and Directives and BMD Rules and Directives and to reflect the obligations set out in Rule 4.17 of BMD Rules and Appendix 1 of Directive 3.36-001 of the BMS Rules with respect of the execution of Discretionary Accounts, we propose to insert the following compliance obligations for Compliance Officer: |

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| | | | <p><u>(c) to ensure that the Trading Participant has entered into a written agreement with the Client which sets out the terms and conditions for the operation of the Client's Discretionary Account, including adequate and accurate disclosure of the risks involved;</u></p> <p><u>(d) to ensure each discretionary order must be identified as a discretionary order at the time of the entry;</u></p> <p><u>(e) to review the trades done in a Discretionary Account regularly;</u></p> <p><u>(f) to ensure that in operating a Discretionary Accounts, the Trading Participant must at all times act in the best interest of the Client. In this regard, the review must include the assurance that there is a mechanism in place to prevent the churning of such accounts purely to generate commission;</u></p> <p><u>(g) to ensure that all discretionary trades are executed within the proper discretionary authority granted to the Trading Participant and that such trades are properly</u></p> | <ul style="list-style-type: none"> • ensuring that prior written authorisation from Client has been obtained; • ensuring that an agreement is entered into between the Trading Participant and the Client and that the Client is informed of the risk of the strategies or transactions proposed; • ensuring that each discretionary order must be identified as a discretionary order at the time of the entry; • amending the frequency of review of the trades done in a Discretionary Account in view of ensuring rules are more principle-based and less prescriptive |

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| | | | <p><u>recorded;</u></p> <p><u>(h) to ensure the maintenance of full and complete documentation of every transaction undertaken under any Discretionary Account; and</u></p> <p><u>(i) to review the Discretionary Account transactions to ensure there is no conflict of interest in the execution of Client trades and proprietary trades.</u></p> | <p>and a daily review might not be operationally efficient;</p> <ul style="list-style-type: none"> • reviewing trades done in a Discretionary Account regularly; • ensuring that in executing Discretionary Accounts, a Trading Participant must at all times act in the best interest of the Client and there must be a mechanism in place to prevent the churning of such accounts purely to generate commission; • ensuring that discretionary trades are executed within the proper discretionary authority granted to |

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| | | | | <p>the Trading Participant and that such trades are properly recorded;</p> <ul style="list-style-type: none"> • ensuring the maintenance of full and complete documentation of every transaction undertaken under any Discretionary Account; and • reviewing of Discretionary Account transactions to ensure there is no conflict of interests in the execution of Client trades and proprietary trades. <p>We do not propose to insert the obligation in the current Rule 4.17 of BMD Rules on ensuring that the transactions are not in excess of client's financial resources as the term 'excess' is vague.</p> |

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| | | | | We propose to state instead that a TP must at all time act in the best interest of a client and that there must not be churning of the Discretionary Account. |
| (c)(xv) of Appendix 1 on Guidelines for Compliance Functions | <p><i>to review, monitor and supervise other supervisory measures to ensure compliance</i></p> <p>review of all proprietary account and discretionary accounts transactions, and ensure there is no conflict of interests during the execution of client trades and house trades;</p> | (c)(xv) of Appendix 1 on Guidelines for Compliance Functions | <p><i>to review, monitor and supervise other supervisory measures to ensure compliance</i></p> <p>review of all proprietary account and discretionary accounts transactions, and ensure there is no conflict of interest during the execution of client trades and house proprietary trades;</p> | Propose to delete reference to discretionary accounts in this paragraph in view of the insertion of compliance obligations with respect to Discretionary Account above. |
| Directive on Conduct of Business (No. 4-001) | | | | |
| 10.1 | Arrangement with Clients | 10.1 | Arrangement with Clients | |
| | A Trading Participant, Head of Dealing and Registered Representative must not: | | A Trading Participant, Head of Dealing and Registered Representative must not: | Since a TP, Head of Dealing (“HOD”) and Registered Representative (“RR”) are generally not allowed to accept a share in the profits of a client’s |
| | | | (a) accept a share in the profits of a Client’s accounts or have any | profits of a client’s |

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| | <p>(a) accept a share in the profits of a Client's accounts or have any arrangement with a Client to share in the profits of the Client's account;</p> <p>(b) have any arrangement with a third party to allocate profits or losses in a Client's account; or</p> <p>(c) lead a Client to believe that the Client will not suffer loss as a result of opening an account or dealing in derivatives.</p> | | <p>arrangement with a Client to share in the profits of the Client's account <u>unless it is in accordance with the provisions on operating a Discretionary Account under Rule 4.17;</u></p> <p>(b) have any arrangement with a third party to allocate profits or losses in a Client's account; or</p> <p>(c) lead a Client to believe that the Client will not suffer loss as a result of opening an account or dealing in derivatives.</p> | <p>accounts and have any arrangement with a Client to share in the profits of the Client's account under paragraph 10.1 of Directive No. 4-001, a carve out in the provision is inserted to permit TP, HOD and RR to have an arrangement with clients for the share of profits in relation to discretionary trading.</p> |
| 12 | New provision | 12 | <p><u>Rule 4.17</u></p> <p><u>(1) Rule 4.17 provides that a Trading Participant or a Registered Representative when operating a Discretionary Account on behalf of a Client must comply with the requirements the Exchange prescribes in respect of Discretionary Accounts.</u></p> <p><u>(2) In discharging the obligations under the said Rule, a Trading Participant or a Registered Representative must, amongst</u></p> | <p>Insertion of new provision on Discretionary Account to set out the requirements that a TP or a RR is required to comply with in executing a Discretionary Account on behalf of a client.</p> |

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| | | | <u>others, comply with the requirements set out below.</u> | |
| 12.1 | New provision | 12.1 | <p><u>Eligibility criteria for Registered Representative</u></p> <p><u>A Trading Participant must ensure that a Registered Representative operating a Discretionary Account on behalf of a Client must have:</u></p> <p><u>(a) a minimum of 5 years' experience in dealing in derivatives; or</u></p> <p><u>(b) a minimum of 5 years' direct experience in fund management; and</u></p> <p><u>(c) no adverse findings or enforcement proceedings or actions commenced or taken against the Registered Representative under the Rules and Directives or Securities Laws.</u></p> | <p>Insertion of requirements to be fulfilled by a RR to operate a Discretionary Account as follows:</p> <p>(a) minimum of 5 years' experience in dealing in derivatives; or</p> <p>(b) minimum of 5 years' direct experience in fund management; and</p> <p>(c) no adverse findings or enforcement proceedings or actions commenced or taken against the Registered Representative under the Rules and Directives or the Securities Laws.</p> |

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| 12.2 | New provision | 12.2 | <p><u>Obligations of a Trading Participant with respect to Discretionary Accounts</u></p> <p><u>In order for a Trading Participant to exercise discretionary authority in a Client's Discretionary Account, the Trading Participant must ensure compliance with the following requirements:</u></p> <p><u>(a) before any discretionary authority can be exercised, prior written authorisation from the Client must be obtained. Comprehensive records of such authorisation must be maintained;</u></p> <p><u>(b) the Trading Participant must enter into a written agreement with the Client which sets out the terms and conditions for the operation of the Client's Discretionary Account, including adequate and accurate disclosure of the risks involved;</u></p> <p><u>(c) full and complete records of every transaction undertaken under any Discretionary Account must be documented and maintained including the details of the</u></p> | <p>Propose to insert TP's compliance obligations in view of streamlining the compliance obligations in operating a Discretionary Account for both BMS Rules and Directives and BMD Rules and Directives.</p> <p>Kindly note that the newly inserted provisions on compliance obligations for a TP is reflective of the obligations set out in Rule 4.17 of BMD Rules and Appendix 1 of Directive No. 3.36-001 of the BMS Rules with respect of the execution of Discretionary Accounts.</p> |

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| | | | <p><u>Contract, the date and time the transaction is effected and the name of the Registered Representative who executed the transaction;</u></p> <p><u>(d) in operating a Discretionary Account, the Trading Participant must at all times act in the best interest of the Client. In this regard, there must be a mechanism in place to prevent the churning of Discretionary Accounts purely to generate commission; and</u></p> <p><u>(e) there must be no conflict of interest arising from such transactions.</u></p> | |
| 12.3 | New provision | 12.3 | <p><u>Requirements pertaining to trading in a Discretionary Account</u></p> <p><u>A Trading Participant and a Registered Representative must comply with the following requirements in operating a Discretionary Account:</u></p> <p><u>(a) trading in a Discretionary Account must be confined to the Contracts</u></p> | <p>Insertion of provision on requirements to set up a Discretionary Account as follows:</p> <p>(a) trading in a Discretionary Account is limited to contracts which are traded on Bursa</p> |

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| | | | <p><u>which are traded on the Exchange.</u></p> <p><u>(b) trading in a Discretionary Account must commence with a cash transfer from a Client instead of a transfer of Open Positions or other types of collateral in lieu of cash;</u></p> <p><u>(c) trading in a Discretionary Account must be carried out separately from trades in a non-Discretionary Account and must be on a cash upfront basis; and</u></p> <p><u>(d) funds in a Client's Discretionary Account must be segregated from the funds in the Client's non-Discretionary Account.</u></p> | <p>Malaysia Derivatives Berhad;</p> <p>(b) trading in a Discretionary Account must commence with a cash transfer from a Client and not by transfer of open positions or other types of collateral;</p> <p>(c) trading in a Discretionary Account must be carried out separately from trades in a non-Discretionary Account and must be on a cash upfront basis; and</p> <p>(d) funds in a Client's Discretionary Account must be segregated from the funds in the Client's non-Discretionary Account.</p> |

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| 12.4 | New provision | 12.4 | <p><u>Profit-sharing or fee arrangement</u></p> <p><u>(1) A Trading Participant or a Registered Representative may charge a Client in the following manner for the service of operating a Discretionary Account on behalf of the Client:</u></p> <p><u>(a) a Trading Participant or a Registered Representative may accept a share in the profits from a Client's Discretionary Account or have an arrangement with a Client to share in the profits from the Client's Discretionary Account; or</u></p> <p><u>(b) a Trading Participant or a Registered Representative may charge a fee calculated based on a percentage of the total value of margin managed under a Client's Discretionary Account.</u></p> <p><u>(2) A Trading Participant or a Registered Representative must not share in the profits under paragraph 12.3(1)(a) and</u></p> | <p>Insertion of a new provision to set out the fee models applicable for trades executed under a Discretionary Account.</p> <p>A Trading Participant or a Registered Representative is only permitted to charge a client either on the basis of profit-sharing or fee arrangement, not both.</p> |

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| | | | <u>concurrently charge a fee under paragraph 12.3(1)(b).</u> | |

[End of Proposed Amendments to the BMD Rules and Directives]