

রেজিস্টার্ড নং ডি এ-১

বাংলাদেশ



গেজেট

অতিরিক্ত সংখ্যা  
কর্তৃপক্ষ কর্তৃক প্রকাশিত

মঙ্গলবার, অক্টোবর ৮, ২০১৩

[ বেসরকারি ব্যক্তি এবং কর্পোরেশন কর্তৃক অর্থের বিনিময়ে জারীকৃত বিজ্ঞাপন ও নোটিশসমূহ ]

## CHITTAGONG STOCK EXCHANGE LIMITED

### NOTIFICATION

Dated: October 03, 2013

In accordance with the section 7(gha) of the এক্সচেঞ্জস ডিমিউচুয়ালাইজেশন আইন, 2013 (Exchanges Demutualization Act, 2013), Chittagong Stock Exchange Limited hereby publishes the following Demutualization Scheme of Chittagong Stock Exchange Limited approved by the Bangladesh Securities and Exchange Commission in exercise of the power conferred by section 6 of the এক্সচেঞ্জস ডিমিউচুয়ালাইজেশন আইন, 2013 (Exchanges Demutualization Act, 2013):

( ৮৬৯১ )

মূল্য : টাকা ৪০.০০

**DEMUTUALIZATION SCHEME OF CHITTAGONG STOCK EXCHANGE LIMITED****DISCLAIMER**

Approval of the Bangladesh Securities and Exchange Commission has been obtained to the attached Demutualization Scheme of Chittagong Stock Exchange Limited under section 6 of the এক্সচেঞ্জস ডিমিউচুয়ালাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013). It must be distinctly understood that in giving approval the Commission does not take any responsibility for the financial soundness of the Chittagong Stock Exchange Limited, value of any of its assets, number of shares to be issued, price of the share or for the correctness of any of the statements made or opinion expressed with regard to the scheme. such responsibility lies with the Chittagong Stock Exchange Limited, its directors, Chief Executive officer/Chief Financial officers, valuer and/or auditors.

**Declaration by Chittagong Stock Exchange Limited**

It is hereby declared that the assets including land and building as shown in the Demutualization Scheme are currently un-encumbered and owned by Chittagong Stock Exchange Ltd. No shareholder of Chittagong Stock Exchange Ltd. or any other person has any right in terms of ownership, permanent possession or otherwise except tenancy. Chittagong Stock Exchange Ltd. has absolute legal right to terminate or modify the tenancy agreement whenever they desire.

The new board of Chittagong Stock Exchange Ltd. after demutualization may review the conditions of its tenancy agreement including current rent structure.

On behalf of the Board of Directors

President

Chittagong Stock Exchange Ltd

## 1. INTRODUCTION

The Board of Directors of Chittagong Stock Exchange has approved this Scheme of Demutualization as required under the এক্সচেঞ্জেস ডিমিউচুয়ালাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013).

The Board of CSE recognizes that a demutualized and corporatized Exchange is expected to be more transparent and function as a responsible public interest institution. In today's competitive environment, a stock Exchange needs to be responsive to the needs of its many stakeholders, including participating organizations, listed companies, and institutional and retail investors. Separating Exchange ownership from its trading rights is the best way to affect such a shift and resolve conflicts of interest in the functioning of the exchanges. Furthermore, the demutualization also affords an opportunity to position the Exchange as a vibrant and efficient marketplace for the investors of the country.

It is with the above recognition that the under mentioned Scheme of Arrangement has been prepared by the CSE which adequately focuses on improvement in all areas of functioning of the institution. The Board believes that the demutualization of our domestic exchanges would be the critical first step to position our domestic capital market as a serious channel for the mobilization of capital in support of the economy.

## 2. CSE's Objectives of demutualization

While Demutualization is a process of separating the ownership interest of the members of an Exchange from the trading rights, however broadly the process also enables the Exchange to position itself as a strong business entity following the transition to a for profit entity. It is under this recognition that the CSE Board has also assigned the following distinct objectives as the outcomes of the exercise of Demutualization:

- To implement one of the best regulatory frameworks for enhancing fairness of the market;
- To put in place a balanced governance and ethics structure;
- To use the process of Demutualization for the strategic advantage of CSE and position the Exchange as a multi-product platform;
- To improve market access and outreach through a regulated and efficient network;
- To resolve the problem of fragmentation and poor price discovery for the benefit of common investors;
- To position CSE for integration of its market with domestic, regional and global markets.

### 3. DEMUTUALIZATION OF CHITTAGONG STOCK EXCHANGE LTD.

The Demutualization process of CSE has been planned in the following manner:

#### a) Changes in the Memorandum and Articles of Association

##### i. Memorandum of Association (MoA)

CSE will adopt a new Memorandum of Association in line with the demutualization objectives of the Exchange to convert itself from a company limited by guarantee to a company limited by shares and from not-for-profit to a for-profit structure. The Memorandum of Association provides for the following:

- To continue functioning as a securities exchange after demutualization of the Exchange and perform all other ancillary acts;
- To be able to distribute any excess earnings of the Exchange by way of dividend;
- To establish any separate entity for undertaking new lines of business such as the clearing and settlement corporation, commodity exchange business and technology sales etc;
- To become a multi-product exchange provide trading in new asset classes such as commodities, currencies, debt, derivatives, SMEs etc.;
- To enable CSE for any possible integration with another Exchange in the future;
- To support the broker and investors associations for promoting self regulation and transparency in the market;
- To provide for indemnification of Directors, officer and employees.

##### ii. Articles of Association (AoA)

The AoA set out the parameters for the improved management and governance structure of CSE. The revised AOA provide for a modus operandi for the appointments on the Board of the CSE post demutualization. In order to address the issues relating to the conflicts of interest, regulatory powers of the Board have been vested in the Regulatory Review Committee (RRC). Relevant clauses relating to the indemnification of Directors, officers and employees, and Capitalization of Profits and Reserves have also been introduced to bring the same at par with international jurisdictions, whilst keeping in view the local needs and requirements.

**b) Changes in Authorized and Paid up Capital:****AUTHORIZED SHARE CAPITAL:**

1,000,000,000	shares of Tk. 10 each	<u>Tk.: 10,000,000,000</u>
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**PAID-UP SHARE CAPITAL:**

634,524,840	shares of Tk. 10 each	<u>Tk.: 6,345,248,400</u>
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**SHARES TO BE ISSUED IN DEMATERIALIZED FORM (100%)**

634,524,840	shares of Tk. 10 each	<u>Tk.: 6,345,248,400</u>
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**SHARES TO BE ALLOTTED TO EXISTING SHAREHOLDERS (40%)**

253,809,936	shares of Tk. 10 each	<u>Tk.: 2,538,099,360</u>
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**SHARES TO BE KEPT IN BLOCKED ACCOUNT WITH CDBL (60%)**

380,714,904	shares of Tk. 10 each	<u>Tk.: 3,807,149,040</u>
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**c) Valuation of CSE and Revaluation of its Assets and Liabilities**

- I. **Valuation methodology and approach:** As required by the এক্সচেঞ্জের ডিমিউচুরালাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013) and Terms of Reference (ToR) provided by CSE M/S HodaVasi Chowdhury & Co, Chartered Accountants was appointed for the exercise of the revaluation of Assets and Liabilities of the Exchange. The following methods of valuation have been considered to find out the fair value of CSE.

- Discounted Cash Flow (DCF)
- Enterprise Value Method
- Present value of Future Earnings Method
- Multiple Valuations Method

The above methods are most commonly used methods for valuation of an entity. As agreed by CSE, we have not considered the 'Sum of net asset value of members' method of valuation in our calculation.

- i. **Discounted cash flow (DCF):** We have adopted the Discounted Cash Flow (DCF) method as first method for valuation of CSE. The DCF method is based upon an explicit forecast of the likely free cash flows to be generated by the CSE over a defined projection period. The returns are estimated as a stream of cash flows expected to be

received by CSE in the future. The risk is then quantified by means of the capitalization rate, discount rate or discount factor. The terminal value is then calculated applying an appropriate growth rate and capitalization rate to the forecasted cash flow for the year immediately following the end of the cash flow period. Justifications of considering free cash flow, discount rate and terminal value growth rate under DCF method are described as under:

- **Determination of free cash flow:** For the purpose of valuation under DCF method, we have computed free cash flow of CSE for the projected 7.75 years period through following ways:

FCF = Net income available to common shareholders

*Plus:* Net non-cash charges (Depreciation, amortization etc.)

*Plus:* Interest expenses  $\times$  (1-tax rate) *Less:* Capital expenditure

*Add/less:* Changes in working capital

- **Determination of discount rate:** In determining discount rate or capitalization rate for discounting future cash flows, we have considered average return of 10 years Bangladesh Government Treasury Bond (BGTB) for the last 10 years as risk free rate of return. While considering Beta ( $\beta$ ) of CSE, we assumed that stock of CSE is directly linked with index return, i.e. Beta ( $\beta$ ) equals to 1.

Discount rate element	Risk value	Justification
Risk free rate of return (Rf)	10.02%	Average of 10 years BGTB for last 10 years
Beta ( $\beta$ )	1.00	Directly linked with index return
Expected return on the market (Rm)	15.03%	
Equity risk premium (Rp) = $\beta$ (Rm - Rf)	5.01%	An equity risk premium (Rm-Rf) of approximately 5.01% is regarded as appropriate by us in the current Bangladesh investment climate
<b>Discount rate</b>	<b>15.03%</b>	Sum of the risk free return and equity risk premium

- **Determination of terminal value growth rate:** We needed to determine the terminal value growth rate of the free cash flow after the ending of projected horizon. In that case, we have considered the average GDP growth rate of Bangladesh Economy for the last ten years to find out terminal value growth rate. In this case, the average GDP growth rate stands for 6.11 percent. Considering the CSE as a service sector

company, we have assumed that the company will grow at a rate of 2 percent higher than the GDP growth rate for perpetuity. Thus, the terminal value growth rate would stand at 8.11 percent. The given table summarizes the calculation of GDP growth rate.

Year	GDP growth rate (%)
2003	5.26
2004	6.27
2005	5.96
2006	6.63
2007	6.43
2008	6.19
2009	5.74
2010	5.83
2011	6.70
2012	6.30
<b>Average GDP growth rate</b>	<b>6.11</b>

- ii. **Enterprise value method:** We have adopted the Enterprise Value (EV) method for valuation of CSE. Enterprise value represents the entire economic value of an entity. More specifically, it is a measure of the theoretical takeover price that an investor would have to pay in order to acquire an entity. Enterprise value represents a company's economic value-the minimum someone would have to pay to buy the entity outright. Though it is known that market capitalization (the current stock price multiplied by the number of shares outstanding) serves as a price tag for a company, it ignores debt. In some companies debt is substantial and changes the picture significantly. Enterprise value is a modification of market capitalization, incorporating debt. Enterprise value can be computed by following formula:

Enterprise value = **Market capitalization** (Current share price x total number of shares outstanding)

*Plus:* Debt (long-term debt + short-term debt)

*Less:* Cash and cash equivalents

- iii. **Present value of future earnings method:** The present value of future earnings method is based upon an explicit forecast of the likely net profit to be generated by the CSE over a defined forecast period. The returns are estimated as a stream of net profit expected to be received by CSE in the future. The risk is then quantified by means of the capitalization or discount rate. The terminal value is then calculated applying an appropriate growth rate and capitalization rate to the forecasted cash flows for the year immediately following the end of the projected earnings horizon. In undertaking the valuation of CSE under present value of future earnings method, we have also applied the same growth rate and discount rate as we considered in Discounted Cash Flow method.
- iv. **Multiple valuations method:**
- o **Price-Earnings (P/E) multiple:** The price-earnings ratio (P/E) is the best known of the investment valuation indicators. The P/E ratio has its imperfections, but it is nevertheless the most widely reported and used valuation by investment professionals and the investors. For Price-Earnings (P/E) multiple valuations, we have considered 10 stock exchanges which were demutualized and subsequently listed in stock exchanges. Since there is no precedence of demutualized listed stock exchange in our country and even in the neighbouring countries, we have considered the global demutualized listed stock exchanges as similar stock.
  - o **Price-Book value (P/B) multiple:** Price to book value is a useful measure where tangible assets are the source of value generation. Because of its close linkage to return on equity (price to book is PE multiplied by ROE), it is useful to view price to book value together with ROE. For Price-Book value (P/B) multiple valuations, we have considered data of 11 global demutualized listed stock exchanges.

## II. Revaluation of Assets and Liabilities to Determine CSE's Equity Capital

As per the requirement of the এক্সচেঞ্জ ডিমুটিউয়ালাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013) (the Act), M/S HodaVasi Chowdhury & Co, Chartered Accountants was appointed for the exercise of the revaluation of Assets and Liabilities of the Exchange. Accordingly, the firm has valued the Exchange at the following cumulative value, which will serve as the basis for paid up capital of CSE:



## Net asset Value of CSE (in BDT)

Particulars as of 31 <sup>st</sup> Mar 2013	Pre-Valuation Amount	Re-valuation Amount	Post- Revaluation Amount
Net assets	4,771,673,190	1,573,575,210	6,345,248,400

## Summarized Asset Position (Historical &amp; Revalued at 31 March 2013)

Particulars	Notes	Value as per audited statement as at 31.03.2013	Surplus /(deficiency)	Revalued amount
		Tk.	Tk.	Tk.
<b>Non-current Assets</b>				
Properties, Plant and Equipment	4.1, 4.2, 4.3 & 4.4	281,574,157	1,352,013,568	1,633,587,725
Automation		359,968,535		359,968,535
Investment with CDBL	4.5	384,300,440	228,264,535	612,564,975
Advance against Car Scheme(Long term)		13,015,000		13,015,000
<b>A. Total Non-current assets</b>		<b>1,038,858,132</b>	<b>1,580,278,103</b>	<b>2,619,136,235</b>
<b>Current Assets</b>				
Accounts Receivable - Clearing		94,241,476		94,241,476
Accounts Receivable - Others		130,692,338		130,692,338
Advances, deposits and pre-payments	4.6	60,020,279	(6,702,893)	53,317,386
Investment in FDRs		3,500,000,000		3,500,000,000
Cash and cash equivalents		203,010,721		203,010,721
Miscellaneous Adjustments		5,675		5,675
<b>B. Total Current assets</b>		<b>3,987,970,489</b>	<b>(6,702,893)</b>	<b>3,981,267,596</b>

<b>C. TOTAL ASSETS (A+B)</b>	<b>5,026,828,621</b>	<b>1,573,575,210</b>	<b>6,600,403,831</b>
Current liabilities			
Accounts Payable- Clearing	176,274,564	-	176,274,564
Liability for expenses	55,948,735	-	55,948,735
Liability for other finance	21,880,312	-	21,880,312
Deferred revenue	1,051,820	-	1,051,820
<b>D. Total Current liabilities</b>	<b>255,155,431</b>	<b>-</b>	<b>255,155,431</b>
<b>Net Assets</b>	<b>4,771,673,190</b>	<b>1,573,575,210</b>	<b>6,345,248,400</b>

### III. Paid up and Authorized Capital of the Exchange

Paid up Capital of the Exchange	Authorized Capital of the Exchange
BDT 6,345,248,400	BDT 10,000,000,000

### IV. Calculation of Allotment of Shares to Initial Shareholders

After the re-valuation of the assets and liabilities, the Act required the allotment of shares in other than cash consideration to all the existing members of the CSE. Accordingly, the Exchange has determined the following shares to be allotted to each shareholder:

Particulars	Unit	Value
Paid up Capital (Revaluation Amount)	BDT	6,345,248,400
Face Value per Share	BDT	10.00
Total Shares	No	634,524,840
No of Initial Shareholders	No	148
Shares to be Allotted to Each Initial Shareholder	No	4,287,330
Total Face Value of Shares per Initial Shareholder	BDT	42,873,300

**d) Initial Shareholders and their Shares**

- i. Within 30 (thirty) days of receiving approval of the scheme from BSEC, CSE shall
  - a) Adopt special resolution in a general meeting regarding approval of the scheme, amendments in the memorandum and articles of association and list of directors of the first Board of Directors of the demutualized exchange as per requirements of Section 8(ka) of the এক্সচেঞ্জস ডিমিউচুয়ালাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013);
  - b) Allot 42,87,330 shares to each of the existing members of CSE, who will be the initial shareholders of the Exchange after demutualization, in dematerialized form, which shall not, at any time or for any reason, be converted into rematerialized form;
  - c) Deposit not less than 60 (sixty) percent of the shares allotted to the initial shareholders in a blocked account till disposal of the same in accordance with section 14 of the এক্সচেঞ্জস ডিমিউচুয়ালাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013);
  - d) Issue a certificate to each of the initial shareholder mentioning its number of shares held in the blocked account.
  - e) Issue a trading right entitlement certificate to each initial shareholder entitled thereto.
- ii. Entitlement of the shares deposited in the blocked account shall be following:
  - a) Initial shareholders shall be entitled to the dividends, bonus shares, rights shares and sale proceeds against those shares;
  - b) Bonus shares and right shares earned against those shares shall be added to the shares held in blocked account and shall be disposed off along with the blocked shares;
  - c) Rights to maintain and off-loading of the shares preserved in the blocked account shall vest upon the Board of Directors;
  - d) The board shall distribute the sale proceeds of the shares preserved in the blocked account to each of the initial shareholders pro-rata basis, upon realization of the sale proceeds in part or full after a periodic interval as decided by the board.

### 3.1 Demutualization Date

- i. Within seven days of the adoption of special resolution in a meeting of the shareholders regarding amendments of the memorandum and articles of association, CSE shall submit the following documents to the Commission and the Registrar:
  - a) Copy of the adopted memorandum and articles of association;
  - b) Copy of the special resolution by which the amendments in the memorandum and articles of association have been adopted;
  - c) Copy of the particulars of directors of its first board of directors;
  - d) Copy of its return of allotment of shares;
  - e) Certificate issued by its auditors certifying that all shares have been allotted to the initial shareholders in dematerialized form; and
  - f) Certificate from the depository that at least 60 (sixty) percent of the shares allotted to the initial shareholders have been deposited in a blocked account.
- ii. The Registrar, within 14 (fourteen) days of receipt of the information as mentioned above, if satisfied that the requirements of the concerned rules-regulations have been complied with, shall
  - a) Issue a certificate of registration registering the adopted memorandum and articles of association; and
  - b) Issue a certificate of re-registration to CSE as evidence of conversion of its status from a public company limited by guarantee to a public company limited by shares.
- iii. CSE shall stand demutualized at the date of issuance of the certificate of registration as mentioned above as per Section 10 of the এক্সচেঞ্জস ডিমিউচুয়ালাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013).

#### 4. Governance Structure:

##### 4.1 Board of Directors

###### a. General Requirements:

- Majority of the members of the Board of Directors of the Exchange, including the Chairman, shall be Independent Directors.
- Board of Directors of the demutualized exchange shall elect Chairman from the Independent Directors.
- The Nomination and Remuneration Committee shall nominate the names of Independent Directors and Managing Director in accordance with the fit and proper criteria.
- Directors other than the Independent Directors and the MD shall be elected by shareholders in accordance with the provisions of the Articles of Association.
- Directors other than shareholder Directors are not required to hold any qualification shares.
- Any vacancy in any particular category of Directors shall not affect the continuation of the Board and the Board shall be entitled to carry out its functions and otherwise act in accordance with its powers under the Articles of Association and in law notwithstanding such vacancy.
- Subject to the provisions of the Articles, all Directors other than the Independent Directors and the MD shall be liable to retire by rotation in accordance with the provisions of the Companies Act, 1994.

###### b. In accordance with the above requirements, Board structure of CSE shall be the following:

Until otherwise determined in a General Meeting of the Exchange with prior approval of the Commission, number of Directors shall be 13 (thirteen) with the following composition:

- i. 7 (seven) Independent Directors. The Board of Directors of the Exchange, as per recommendation of the "Nomination and Remuneration Committee" will propose at least 2 (two) names against each post of Independent Director and then submit to the Commission for approval through the Board, provided that if the Commission does not approve the proposed names of Independent Directors, then CSE has to re-submit a fresh list of candidates (two names against each post) of Independent Director;

- ii. 5 (five) Directors from amongst the Shareholders and Strategic Investor(s) among which at least 1 (one) post will be reserved for Strategic Investor(s), provided that 1 (one) post of Director from the Strategic Investor(s) shall remain unfilled pending the entrance of Strategic Investor(s);
- iii. Managing Director and CEO as Ex-Officio member of the Board with voting rights.

**C. Quorum :**

The quorum shall be one-third members of the Board of Directors of which majority of the Directors present shall be Independent Directors. Quorum for any committee constituted by the Board shall be three members, of which majority shall be Independent Directors.

**4.2 Fit and Proper Criteria for Directors**

- a) A Director elected by the Shareholders shall hold office for no more than 2 (two) consecutive terms and shall be eligible to be elected as Director after a gap of 1 (one) year;
- b) An Independent Director shall be nominated for a term of 3 (three) years and may be renewed for another term by the Commission on recommendation of the Exchange. Thereafter however, he/she shall not be eligible to be nominated as an Independent Director until after a gap of 1 (one) year;
- c) The Managing Director shall be nominated for a term of not more than 3 (three) years and may be renewed for another term by the Commission on recommendation of the Board.
- d) No person shall be eligible to be elected or appointed as, or continue to occupy the office of a Director if:—
  - i. He is found lunatic or becomes of unsound mind or incapable of efficient attention to business; or
  - ii. He remains absent in three consecutive meetings of the Board of Directors or in all meetings of the Board of Directors for a continuous period of three months, whichever is the longer, without leave of absence from the Board of Directors; or
  - iii. He is convicted of any criminal offence and sentenced to imprisonment;

- iv. He is a loan defaulter as per CIB report of Bangladesh Bank.
- v. He has entered into any business transaction with the Exchange.
- vi. Without prejudice to the above he fails to pass "Fit and Proper" criteria as may be framed by the Commission from time to time.

e) In addition to the above, a person shall not be considered as an Independent Director if:

- i. He is or has been an employee of the Exchange, any of its subsidiaries or holding company within the preceding 3 (three) years of his proposed date of appointment;
- ii. He is or has been the CEO/MD of any subsidiary, associated company, associated undertaking or holding company of the Exchange within the preceding 3(three) years of his proposed date of appointment;
- iii. He has, or had within the preceding 3 (three) years of his proposed date of appointment, a material business relationship with the Exchange either directly, or indirectly as a partner, substantial shareholder or director of a body that has such a relationship with the Exchange;
- iv. He has received remuneration within the preceding 3 (three) years of his/her appointment as a director or receives additional remuneration, excluding retirement benefits from the Exchange apart from a director's fee or has participated in the Exchange's share option or a performance-related pay scheme;
- v. He is a family member or connected person, as defined in the এক্সচেঞ্জ ডিমুচুয়ালাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013), of any of the Directors, TREC holders or shareholders of the Exchange or the Exchange itself;
- vi. He has or had any relationship with any of the TREC holders or Shareholders of the Exchange or Directors thereof;
- vii. He is or has been an employee or director of any capital market intermediary including Merchant Banker or Asset Management Company within the preceding 3 (three) years of his proposed date of appointment;
- viii. He acts as a Director of any other exchange;

- ix. He is an employee of any shareholder of any exchange;
  - x. He is an employee of any regulatory organization;
  - xi. He is a director or holds any office of a listed company.
- f) An Independent Director must have at least any of the following educational qualification and professional experience:
- i. Master in business, economics, statistics, computer science, mathematics, public administration or law including not less than 10 (ten) years professional experience;
  - ii. Bachelor in business, economics, statistics, computer science, mathematics, public administration or law including not less than 15 (fifteen) years professional experience ;
  - iii. Professional designation like CFA, CA, CMA, CS, CPA etc, including not less than 10 (ten) years professional experience;
  - iv. Persons with at least Bachelors degree having 20 (twenty) years of management experience.

### 4.3 First Board of CSE and Subsequent Activities

Formation of the First Board of CSE and its subsequent activities shall be as per the provisions of the এক্সচেঞ্জস ডিনিউচ্যুয়লাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013).

### 4.4 Code of Conduct and Code of Ethics for the Board and its Members

There shall be a set of appropriate code of conducts and code of ethics for the Board which shall be incorporated in the proposed Chittagong Stock Exchange (Board and Administration) Regulations, 2013 to ensure fair and ethical functioning of the Board.

#### 4.4.1 Code of Conduct

##### a. Meetings & Minutes

- Meeting of the Board of Directors and General Meetings, notices, agenda, minutes of the meetings shall be in accordance with the Companies Act, 1994.
- In the event that a Director is of the view that his dissenting note has not been satisfactorily recorded in the minutes of a meeting of the Board, he may refer the matter to the Company Secretary. The relevant Director may require the note to be appended to the minutes during confirmation of the minutes.



- Director(s) shall not participate in the discussion on a matter in which any conflict of interest exists or arises, whether pecuniary or otherwise, and in such cases the same shall be disclosed and recorded in the minutes of the meeting.

**b. Regulatory Compliances**

- The Directors shall ensure that the Exchange abides by all the provisions of securities laws, rules and regulations framed there under and circulars, directions issued by the BSEC and other authorities as the case may be.
- The Directors shall ensure compliance at all levels so that the regulatory system does not suffer any breaches.
- The Directors shall ensure that the Exchange takes commensurate steps to honour the time limit prescribed by BSEC for corrective action.
- The Directors shall not support any decision in the meeting of the Board which may adversely affect the interest of investors and the Managing Director shall report forthwith any such decision to BSEC.

**c. General Responsibility**

- The Directors shall ensure performing activities of the Exchange to uphold the interest of public, i.e. the investors; and give priority to the interest of public, i.e. the investors, even it appears to be conflicting with the interest of the Exchange or its shareholders.
- The Directors shall place priority for redressing investor grievances and encourage fair practices in dealings and trading in securities and matters ancillary thereto.
- The Directors shall carry out their fiduciary duties with a sense of objective judgment and independence in the best interests of the Exchange and investors.
- The Directors shall submit necessary disclosures/statement of holdings/dealings in securities as required by the Commission and the Exchange from time to time as per their rules, regulations and bye-laws.

- The Directors shall unless otherwise required by law, maintain confidentiality and shall not divulge/disclose any information obtained in discharging their duties.
- The Directors shall not use any confidential information for his personal gain, directly or indirectly, received or obtained by him in his capacity as a member of the Board.
- The Directors shall perform their duties in an independent and objective manner and avoid activities that may impair, or may appear to impair, their independence or objectivity or official responsibilities.
- The Directors shall put in place for an annual evaluation of the Board's own performance.
- The Directors shall not, in any way, interfere in the activities of the management of the Exchange.

#### 4.4.2 Code of Ethics

##### a. Objectives and Underlying Principles

- The code of ethics for Directors of the Exchange intends to establish highest level of business/professional ethics to be followed for establishing a fair and transparent exchange. In discharging functions, the Directors shall adhere to the following fundamental principles:
  - i. Fairness and transparency in dealing with matters relating to the Exchange and the investors;
  - ii. Compliance with all laws/rules/regulations laid down by the Exchange and BSEC;
  - iii. Exercising due diligence in the performance of duties; and
  - iv. Avoidance of conflict of interest between self-interests of Directors and interests of the Exchange and investors.

##### b. Disclosure of Dealings in Securities by Directors of the Exchange

- Directors of the Exchange shall disclose on a periodic basis, with an interval of not more than one month, their trading activities including personal and institutional portfolio investment where such director has direct or indirect interest to the Conflict Mitigation Committee.

- Directors of the Exchange shall also disclose on a periodic basis as above, the trading conducted by firms/corporate entities in which they hold 10% or more beneficial interest or hold a controlling interest, to the Conflict Mitigation Committee.

**c. Avoidance of Conflict of Interest**

- No director of the Board or member of any committee of the Exchange shall participate in any decision making/adjudication process in respect of any person/matter in which he is in any way, directly or indirectly, concerned or interested.
- No director shall be involved in any business transaction with the Exchange except transaction related to the trading of securities;
- Any decision of the Conflict Mitigation Committee as to the existence of conflict of interest shall be final.

**d. Disclosures of Beneficial Interest**

All Directors shall disclose to the Conflict Mitigation Committee, upon assuming office and during their tenure in office, whenever the following arises:

- Any fiduciary relationship of self and family members and directorship/ partnership of self and family members in any issuer or with any capital market intermediary;
- Shareholding or any changes thereof, directly or through his family, in any listed company on the Exchange or in other entities related to the capital markets; and
- Any other business interests which may affect price movements of the listed securities.

**e. Access to Information**

- Directors shall not have access to any undisclosed price sensitive information, surveillance or any matter related to the market operation unless the matter is placed before a committee or board meeting, as the case may be;

- There shall be prescribed channels through which information shall move subject always to audit trail of the same. Any retrieval of confidential documents/information by any member of the Board or any Committee shall be properly recorded.
- All such information, especially which is non-public and price sensitive, shall be kept confidential and not be used for any personal gain.
- Any information relating to the business/operations of the Exchange, which may come to the knowledge of Directors during performance of their duties shall be held in strict confidence and shall not be divulged to any third party and shall not be used in any manner except for the performance of their duties.

#### 4.4.3 Management of the Exchange

The overall management of CSE will be looked after by the Board of Directors. The Managing Director ("MD"), as selected independently by the Nomination and Remuneration Committee, recommended by the Board and approved by the Commission shall have a tenure of not more than 3 (three) years, which may be renewed for another term with prior approval of the Commission. The MD shall have the authority to perform all administrative functions of the Exchange, give effect to the policies, directives, guidelines and orders issued either by the Commission or by the Board from time to time, to implement any provisions of laws, rules, regulations, Articles and bye-laws and to take such other actions as may be required for these purposes. He shall be a member of all Board committees except the Regulatory Affairs Committee.

The MD shall be responsible for -

- designing measures to protect the interest of investors and shareholders;
- free, fair, transparent and efficient management and operation of the Exchange;
- effective administration and efficient financial and general management of the Exchange including management of its human resource functions;

- market related information technology of the Exchange;
- controlling and directing the officers and staff of the Exchange;
- ensuring disclosure of all price sensitive/material information in the manner prescribed by the Commission or the Exchange;
- adopting necessary measures to pre-empt conflict of interest;
- providing extensive financial education to investors, general public, market intermediaries, listed companies and others related to the capital market;
- discharging all other duties and responsibilities delegated by the Board from time to time; and
- representing the Exchange before the Commission and any other authority concerned.
- In case of any conflict between any policy, directive, guideline or order issued by the board of directors of the Exchange and also by the Commission on any matter, the policy, directive, guideline or order issued by the Commission shall prevail and the Managing Director shall be bound to carry out the policy, directive, guideline or order issued by the Commission.

From the date of demutualization, all the employees of CSE shall still be the employees of CSE on the same terms and conditions as existing immediately prior to the date of demutualization. Seniority of the respective employees and their tenure of service, gratuity and other entitlement based on length of service shall be calculated as before demutualization.

Separate regulatory affairs division will be created to oversee the regulatory functions of the Exchange independently. It will be headed by the Chief Regulatory Officer, reporting directly to the Regulatory Affairs Committee, with administrative reporting to the MD. All other divisional heads will report to the MD.

#### **4.5 Committees**

##### **4.5.1 Committees to be formed**

The following Board Committees shall be formed and empowered to ensure superior corporate governance for CSE:

- a. Nomination and Remuneration Committee;
- b. Regulatory Affairs Committee;
- c. Audit and Risk Management Committee;
- d. Appeals Committee; and
- e. Conflict Mitigation Committee.

#### 4.5.2 General Principles of Board Committees

The Board committees shall be duly formed and empowered to ensure superior corporate governance for Chittagong Stock Exchange Limited. All such committees will adhere to the following general principles in discharging their functions and responsibilities:

- a. Unless otherwise stated, each Committee shall be comprised of 5 (five) members including ex-officio member, out of which at least 3 (three) members including the Chairman shall be Independent Directors.
- b. All the members of the Regulatory Affairs Committee (RAC) shall be Independent Directors except the ex-officio member;
- c. All members of the Audit and Risk Management Committee should be "financially literate" and at least 1 (one) member shall have accounting or related financial management experience.
- d. Chairman of the Audit and Risk Management Committee or any member of the Audit and Risk Management Committee appointed by the Chairman shall remain present in the Annual General Meeting (AGM).
- e. Chairman of the RAC shall not be eligible for becoming member of any other Committee.
- f. MD of the Exchange shall be the ex-officio member of all Board Committees except the RAC and the Appeal Committee with voting right.
- g. CRO shall be the ex-officio member of RAC without voting right.
- h. If any Committee has reported to the Board about anything having material impact on the activities of the Exchange and that any rectification is necessary and if such recommendation has been unreasonably ignored or the Board has failed to discuss on the report in its 2 (two) consecutive meetings from the date of reporting by the committee, the MD shall report such finding to the Commission,
- i. When the term of service of the Committee members expires or there is any circumstance causing any Committee member to be unable to hold office until expiration of the term of service, thus making the number of the Committee members to be lower than the prescribed number, the Board of Directors shall appoint new Committee member(s) to fill up the vacancy(s) immediately or not later than 1 (one) month from the date of vacancy(s) in the Committee to ensure continuity of the performance of work of the Committee.

- j. All terms of reference for the committees shall be approved by the Board of Directors and circulated to all respective committee members and disclosed on the Exchange's website.
- k. These committees shall have the authority to hire independent external consultants to obtain expert opinions in advisory capacity and incur necessary expenses subject to prior approval of the Board;
- l. Despite delegation of the various tasks to the Committees as per the assigned terms of reference, the Board shall be ultimately accountable for the performance/ progress of committees.
- m. The Chairman of each committee shall be the coordinator for the respective committee while the company secretary shall be responsible for all matters relating to convening the meeting, proceedings, agenda and preparation of minutes and the Managing Director shall be responsible for execution of the committee decisions as may be approved by the board.
- n. The secretarial functions of each committee constituted by the Board shall be discharged by the Company Secretary or by a nominee of the Secretary unless otherwise stated in the Regulations or decided by the Board.
- o. The members of each committee shall strictly adhere to all applicable rules, regulations and any other securities laws in discharging their functions, duties and responsibilities.
- p. Tenure of each committee shall be a period of one year from the date of constitution. Unless otherwise decided by the Board, each committee shall continue to operate notwithstanding expiry of their tenure until a new committee is constituted by the Board. The Board shall have the authority to reconstitute any committee or to replace any member of a committee from time to time as it deem fit regardless of the tenure of the respective committee or its members.
- q. Unless otherwise provided herein, the committees shall meet at least once in every quarter of the financial year. Additional meetings may be held, as and when deemed necessary.
- r. In addition to the scheduled meetings approved by the Board, the committee may regulate its own procedures and in particular the calling of meetings, the notice to be given of such meetings, the voting and proceedings thereat. The Secretary shall, on the requisition of a member, summon a meeting of the members.

- s. If, at any meeting, the Chairman is not present within 1 (one) hour after the time appointed for holding the meeting, the members present shall choose another member of the Committee to Chair the meeting.
- t. In case of an equality of votes, the Chairman of the meeting shall have a second or casting vote.
- u. A resolution in writing, signed by a majority of the members for the time being entitled to receive notice of a meeting of the committee (of which a majority shall be independent), shall be valid as effectual as if it had been passed at a meeting of the committee duly convened and held. Any such resolution may consist of several documents in like form, each signed by one or more member.
- v. The committees shall undertake any task assigned by the Board from time to time.

#### **4.5.3 Roles of Independent Directors**

Independent Directors shall play the most important role in the Board Committees by ensuring neutrality, improving corporate governance and enhancing business efficiency through their diverse experience and expertise. Independent Directors shall be majority in all the Board Committees including the Chairman in all the committees and thus their strong role will be ensured in decisions and functions of these committees.

#### **4.5.4 Role and Structure of Committees**

##### **A. Nomination and Remuneration Committee:**

###### **Functions:**

The Committee shall discharge such functions as may be vested to it by the Board from time to time. Without prejudice to the generality of the nature of functions of the committee shall be as follows:

- a. Scrutinize nomination papers that may be submitted by a candidate for the post of Director including Independent Directors according to "Fit and Proper Criteria" as described in this Scheme and the Regulations concerned. ;
- b. provide recommendation of remuneration and other facilities of the Directors for approval of the shareholders through the board;



- c. provide recommendation of remuneration for the Managing Director for approval of the shareholders through the board;
- d. carry out the function of searching qualified persons for the recruitment of the Managing Director;
- e. short-list candidates for the appointment of the Managing Director;
- f. recommend the appointment, compensation, succession planning and removal of the CRO to the Board in consultation with the RAC. Provided that CRO can only be appointed and removed upon recommendation by the RAC to the Board and with final approval of the Commission. For this purpose, non-renewal of the contract with CRO shall also be considered as removal;
- g. Recommend, review and/or make revisions of human resource management policies, including compensation and appraisal policies of CSE;
- h. ensure that compensation policy is not biased in favour or against any particular position or positions;
- i. recommend to the board the selection, evaluation, compensation (including retirement benefits) of COO, CFO, CTO and Company Secretary or any other position comparable with these roles;
- j. oversee proper implementation of all Human Resource policies; and
- k. submit written reports to the Board of CSE regarding activities and proceedings as and when requested by the Board.

**B. Regulatory Affairs Committee:**

The Regulatory Affairs Committee ("RAC") shall act as the vehicle for separation of business and regulatory activities of the Exchange. RAC shall ensure that the Regulatory Affairs Division ("RAD") functions effectively and take measures necessary to create and maintain an effective regulatory environment to improve investor confidence and market integrity. Functions of the RAC are described in details in chapter 5 'Separation of Business from Regulatory Functions'.

**C. Audit and Risk Management Committee:****Functions:**

- a. The Audit and Risk Management Committee shall assist the Board of Directors in ensuring that the financial statements reflect true and fair view of the state of affairs of the company and in ensuring a good internal monitoring system within the business;
- b. The Audit and Risk Management Committee shall be responsible for internal financial, cost and management audits of the Exchange periodically;
- c. The Audit and Risk Management Committee shall assess the risks related to investments and associated financial management of the exchange, perform benefit-cost analysis and advise the board to make financial decisions;
- d. Oversee the financial reporting process;
- e. Monitor choice of accounting policies and principles;
- f. Monitor Internal Control and Risk management process;
- g. Oversee hiring and performance of external auditors;
- h. Review along with the management, the annual financial statements before submission to the board for approval;
- i. Review along with the management, the quarterly and half yearly financial statements before submission to the board for approval;
- j. Review the adequacy of internal audit function;
- k. Review statement of significant related party transactions submitted by the management;
- l. Review Management Letters/ Letter of Internal Control weakness issued by statutory auditors;
- m. Advise the management in adopting appropriate accounting and investment policies; and
- n. Ensure that statutory statements are submitted to the regulators in time.

**Reporting of the Audit and Risk Management Committee****a. Reporting to the Board of Directors**

- i. The Audit and Risk Management Committee shall report on its activities to the Board of Directors.

- ii. The Audit and Risk Management Committee shall immediately report to the Board of Directors on the following findings, if any:
  - a) report on conflicts of interests;
  - b) suspected or presumed fraud or irregularity or material defect in the internal control system;
  - c) suspected infringement of laws, including securities related laws, rules and regulations;
  - d) any other matter which should be disclosed to the Board of Directors immediately.

b. Reporting to the Shareholders and General Investors

Report on activities carried out by the Audit and Risk Management Committee during the year, shall be signed by the Chairman of the Committee and disclosed in the annual report of the Exchange.

**D. Appeal Committee:**

**Functions:**

The Appeal Committee shall have the authority to decide on any appeal against decisions to take disciplinary action against officers/employees of the Exchange.

No member of the Appeal Committee shall be involved in the decision to take disciplinary action against the officer or employee lodging the appeal.

The Appeal Committee shall also review the operations of the "Disciplinary Procedures" on a continuous basis and propose improvements/inclusions as the committee considers necessary to the Board and ensure that the Exchange's disciplinary rules are appropriate to handle the disciplinary issues.

**E. Conflict Mitigation Committee**

The Conflict Mitigation Committee shall satisfy the Board of Directors ("Board") that any perceived or actual conflict of interest between the

Exchange's regulatory responsibilities and commercial interests is addressed. These functions include:

- a. Deal with perceived or actual conflict between regulatory responsibilities and commercial interests of the Exchange; and
- b. Review the adequacy of the arrangements within the Exchange for dealing with any perceived or actual conflict arising from/during:
  - i. the commercial interests of the Exchange to its shareholders, including any conflict of interest or potential conflict of interest arising as a result of the listing of the shares of the Exchange in its own bourse;
  - ii. supervision and monitoring disclosures made by the Directors of the Exchange in discharge of their obligation under the Code of Conduct and Ethics;
  - iii. recommending the course of action to be taken against the disclosing Director in case any concealment or omission of material information is detected;
  - iv. notifying the BSEC of all relevant facts, including any proposals for resolving the matter in a manner which assures the proper performance of any relevant regulatory functions; and
  - v. reviewing the regulatory implications and reputational risks of strategic initiatives requiring Board approval and are referred to the Committee, and to thereafter report its views to the Board.

## **5. Separation of Business from Self Regulation**

### ***5.1 Reasons for Separation***

Demutualization of stock exchanges raises new conflicts of interest in exchanges carrying out front line regulatory roles. It is generally perceived that performing a dual role of a commercial entity and a self regulating organization is the primary source of conflicts of interests. Globally, this is a highly debated area as to the best models that can be used to mitigate this risk. The solution often prescribed is the separation of an exchange's SRO functions from its commercial activities.

## 5.2 Proposed Process & Model for CSE

The suggested SRO model for CSE is *Strong Exchange SRO Model*.

Under this model, CSE's potential conflict of interest will be managed through setting up separate regulatory committees/divisions (i.e. Regulatory Affairs Committee, Regulatory Affairs Division) that will function totally independent from any committees/divisions of CSE involved in commercial functions.

The segregation will be envisaged through setting up of a Regulatory Affairs Division ("RAD") that will be headed by a Chief Regulatory Officer ("CRO"); the overall supervision of RAD will be vested with a Regulatory Affairs Committee ("RAC"), which will be comprised of independent directors of the board. The RAC will function as a 'Chinese Wall' between the regulatory functions and commercial activities of the exchange and will be responsible for developing and measuring RAD's effectiveness in implementing the overall regulatory plan, processing all regulatory amendments, recommending budget and staff allocations for the RAD, recommending appointment and removal of the CRO.

### 5.2.1 Regulatory Affairs Committee

RAC shall act as the vehicle for separation of business activities from self-regulation.

#### Composition:

- The RAC shall consist of 3 (three) Independent Directors. No shareholder Director shall be eligible to be a member of RAC.
- The Chairman of RAC shall not be eligible for becoming a member of any other Committee.
- The Managing Director of CSE shall not be a member of the RAC, instead the CRO shall be the ex-officio member of the RAC without voting right.

#### Functions:

- a. develop an overall regulatory plan and roles and responsibilities of each department of RAD;
- b. ensure adequacy and effectiveness of the exchange's regulatory plan and approve annual plans/targets for the RAD;
- c. recommend all required regulatory amendments to the Board;

- d. assess performance of the RAD in the light of regulatory program and take measures and where necessary make recommendations to the Board for improvements;
- e. recommend any allowance that may be paid to the personnel of RAD for proper and smooth functioning of the division;
- f. formulate and recommend to the Board for approval, budget and staff allocation for RAD;
- g. conduct hearings of any appeal against the enforcement actions/ arbitration awards of RAD;
- h. identify and manage potential conflicts of interest between commercial and regulatory functions regularly;
- i. train/educate employees of RAD in respect of conflict management and also develop the manual on conflict management policy and circulate to all employees of RAD;
- j. prepare an annual report of the RAD on the activities, conclusions, recommendations of the last year with special focus on the identification and mitigation of conflicts of interest and identify the targets for next year along with any other matters, for the Board and BSEC;
- k. all appointments and removals from RAD shall only be subject to the approval of RAC;
- l. establish criteria for evaluating candidates for the senior management of RAD including CRO; and
- m. carry out any other function that may be mutually agreed upon by the RAC and the Board.

### ***5.2.2 Chief Regulatory Officer***

- a. The CRO shall be the head of the RAD and shall oversee the efficient functioning of the division in accordance with the terms of reference approved by the Board on the recommendations of the RAC;
- b. The CRO shall report directly to the RAC but will also have an administrative reporting to the CEO;
- c. The CRO shall be appointed by the Board with approval from the Commission upon the recommendations of the Nomination and Remuneration Committee in consultation with the Chairman of the RAC;

- d. CRO can only be removed on the recommendations of RAC and approval from the Commission. The affairs relating to compensation, succession planning and removal of the CRO shall be recommended to the Board by Nomination and Remuneration Committee in consultation with the Chairman of RAC. For this purpose, non-renewal of the contract with CRO shall also be considered as removal;
- e. The CRO must not be a connected person with the MD/CEO, TREC holders and the strategic investor(s), or any financial institution holding more than 5% of the shares of the CSE;
- f. The CRO and his/her family member(s) shall not be engaged in any investment activity with reference to the shares of the Exchange or any listed company;
- g. CRO shall be a dedicated position and CRO must not have any other responsibility in the Exchange except the regulatory role;
- h. CRO shall also liaise between the Exchange and BSEC on regulatory affairs;
- i. CRO shall be responsible for taking disciplinary measures in appropriate cases against persons violating the Exchange regulations or bye-laws;
- j. CRO shall be responsible for securing surveillance of market activities and information technology relating to surveillance;
- k. CRO shall be the representative of the Exchange in respect of all external investigations, law enforcement, prosecution agencies and courts of law and related matters. However, the CRO may authorize any person from within the RAD or form legal department for any of the aforesaid purposes subject to intimation to the RAC;
- l. The CRO will submit a report on regulatory compliance status to the RAC with copy to the Commission every month, as per a format to be prescribed by RAC; and
- m. Compensation arrangement of CRO should be determined against the measurable criteria and should not be linked with the number of violations detected or the amount of fine recovered from the market participants.

### **5.2.3 Regulatory Affairs Division**

The RAD shall perform following functions through different departments. Exchanges may consolidate or re-allocate different tasks to departments according to their administrative requirements.

### 5.2.3.1 TREC Holder Affairs

- Set minimum admission standards and eligibility criteria for TREC holders;
- Formulate rules and regulations relating to proprietary and client level trading by the TREC holders;
- Create awareness about the code of conduct amongst the TREC holders;
- Process approvals/NOCs for changes in majority shareholding of brokerage houses;
- Formulate comprehensive guidelines for TREC holders to meet all obligations to investors in conformity with applicable laws; and
- Develop detailed system for TREC holders to keep proper records of all transactions and orders and client profile.
- Monitoring compliance of all the requirements for TREC holders in accordance with the securities laws and recommend/initiate enforcement actions in case of non-compliance.

### 5.2.3.2 Listing/Company Affairs

- Set listing standards and making efforts to continuously enhance the same;
- Ensure continuous and timely disclosure of material information by the listed companies;
- Ensure compliance of listing regulations;
- Take steps in case of non-compliance of listing regulations;
- Ensure compliance of corporate finance requirements by the listed companies;
- Ensure compliance with the Code of Corporate Governance by the listed companies; and
- Recommend / initiate enforcement action against non-compliant listed companies within the jurisdiction allowed under the securities laws.

### 5.2.3.3 Conduct Monitoring and Surveillance of the Market

- Ensure continuous monitoring and surveillance of trading activities;
- Investigate violations of trading rules and disciplinary requirements;
- Ensure that proper systems for detecting violations/ market malpractices are in place and in operation;



- Review and implement risk management standards;
- Ensure compliance with the capital adequacy regime;
- Conduct research of various jurisdictions in respect of risk management and developments therein; and
- Adopt and implement any international standard code of conduct with approval from RAC.
- Monitoring compliance of all the requirements related to trading in accordance with the securities laws and recommend/initiate enforcement actions in case of non-compliance.

#### **5.2.3.4 Enforcement and Compliance**

- Establish compliance procedures to ensure that the procedures reflect current laws and provide adequate guidance to the employees about what is permissible conduct;
- Supervise system audit of brokers/dealers and introduce a system of regular inspection of brokers/dealers;
- Continuously liaise between the Exchange/BSEC and the TREC holders etc. on compliance related issues;
- Ensure that adequate systems and procedures are in place and maintained by supervisory personnel;
- Ensure that all applicable rules/regulations/procedures/directives, code of conduct and any amendments therein are strictly adhered to by all personnel;
- Initiate enforcement actions or recommend enforcement actions to BSEC, whichever is applicable, such as imposition of penalties, suspensions etc. Cases requiring litigation shall be forwarded to the Litigation Wing;
- Dissemination of material disciplinary actions through website for the information of general public. Maintain and publication of a database of past enforcement actions in accordance with the dissemination policy approved by the Board; and
- Ensure that all post-trade information/reports are made available to investors by TREC holders in line with prescribed rules/regulations.

#### **5.2.3.5 Investors Complaints, Arbitration and Litigation**

- Establish a dispute resolution mechanism;
- Handle and process investor complaints;

- Conduct preliminary enquiries, hearings and mediations;
- Coordinate arbitration proceedings; ensure implementation of arbitration awards etc; and
- Initiate/defend legal proceedings in respect of enforcement actions of Enforcement and Compliance Wing.

#### 5.2.3.6 Other Functions

- Create awareness among market participants including TREC holders, regarding the Code of Conduct and other compliance issues through regular seminars, newsletters and workshops.

## 6. TRADING RIGHT

### 6.1 Trading Right Entitlement Certificate ("TREC")

The proposed demutualization of CSE provides for two completely de-linked assets to the existing members in the Exchange, namely (a) fully paid-up shares and (b) trading right. CSE shall have the authority to issue Trading Right Entitlement Certificate (TREC), as per the এক্সচেঞ্জস ডিমিউচ্যুয়ালাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013) and as outlined in this scheme, to provide the right to trade any securities enlisted in CSE to eligible brokers and dealers. Such TRECs will be totally separate from the ownership of the Exchange as there is no obligation for TREC holders to be or remain shareholders of the Exchange.

### 6.2 Issuance of TREC to Initial Shareholders

Within 30 days from the approval of this Demutualization Scheme, CSE shall issue one TREC in favor of each initial share holder under the following terms and conditions:

- (1) An initial shareholder who is issued with a trading right entitlement certificate, if not already registered under the Bangladesh Securities and Exchange Commission Act, 1993 or any Rules made there under, shall have to obtain registration certificate in accordance with the requirements of the said Act or Rules within 3 (three) years from the date of demutualization, and commence its business within 6 (six) months from the date of receiving such registration.
- (2) Any member whose membership is currently suspended and/or undergoing adjudication for forfeiture shall not be issued with TREC till final decision regarding the dispute.

### 6.3 Transfer and Issue of TREC

- (1) TRECs issued to the initial shareholders can be transferred once within 5 years from the demutualization date to any eligible entity in accordance with the এক্সচেঞ্জ ডিমিউচ্যুয়লাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013) and payment of fees as may be determined with the Commission's approval from time to time.
- (2) Any TREC Holder desiring to transfer its TREC subject to requirements of the এক্সচেঞ্জ ডিমিউচ্যুয়লাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013) must submit to the Exchange a written application, signed by both the transferor and transferee, in such form and accompanied with such documents as may be prescribed by the Exchange.
- (3) Any company, who acquires the TREC as above, shall require to obtain registration certificate under the Bangladesh Securities and Exchange Commission Act, 1993 or any Rules made thereunder, not later than 12 (twelve) months of such acquisition, and shall require to commence its business within 6 (six) months from the date of registration.
- (4) All such transfers will be subject to payment of all outstanding dues to the Exchange, other relevant statutory duties and such conditions or payments as the Board of Directors of CSE or the Commission or any other competent authority may impose from time to time including, but not limited to, transfer fees/charges levied by the Exchange for execution of such transfer. Such transferor will have no outstanding payment to clients and no legal proceedings shall be pending. It is further provided that the requirements of the relevant laws, rules and regulations in respect of such transfer shall also have to be complied with.
- (5) All TREC shall become non-transferrable upon completion of 5 (five) years from the date of demutualization.
- (6) Within 5 (five) years of demutualization, an exchange may, by adopting special resolution in general meeting, increase the number of trading right entitlement certificates.
- (7) Upon completion of 5 (five) years from the date of demutualization, TREC shall be issued to an applicant by the exchange upon fulfilment of the qualifications and criteria prescribed in this scheme.

- (8) Any company, who acquires TREC as above, shall require to obtain registration certificate under the Bangladesh Securities and Exchange Commission Act, 1993 or any Rules made thereunder not later than 12 (twelve) months of such acquisition, and shall require to commence its business within 6 (six) months from the date of registration.
- (9) If any company or initial shareholder fails to obtain registration certificate or to commence business within the time as stipulated above, the respective TREC shall become cancelled.

#### **6.4 Criteria of Applicants for Obtaining New TRECs**

- a. An entity shall apply to the Exchange for issuance of new TREC in compliance with the requirements of the Chittagong Stock Exchange (Trading Right Entitlement and Trader Certificate) Regulations, 2013.
- b. The Exchange shall scrutinize the application, documents and eligibility requirements and upon satisfaction of fulfilment of the requirements as per the Regulations, shall issue TREC following the procedure and timeframe of the Regulations.
- c. Every TREC shall be liable to pay such fees for obtaining certificate and renewal thereof as may be determined by the Exchange from time to time.
- d. The Exchange shall have the authority to collect such amount of fees and charges as it may deem appropriate for providing training and other facilities.
- e. An entity shall not be eligible for obtaining TREC from the Exchange unless the following conditions are satisfied:
  - i. it has obtained or is in the process of obtaining a registration certificate as stock-dealer or stock broker under the concerned Rules of Bangladesh Securities and Exchange Commission. In the event that a registration certificate is not issued by the Commission within the timeframe stipulated in the এক্সচেঞ্জস ডিমিউচুয়ালাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013), the TREC shall be cancelled;
  - ii. it has a minimum paid up capital of Taka 10,000,000 (Ten Million) only and audited net worth of 75% of its paid-up capital;

- iii. it have adequate professional management including compliance officer, human resource, information technology infrastructure and financial capability as may be determined by the Exchange from time to time;
  - iv. its promoters, sponsors, MD/CEO, directors and key executives comply with the "Fit and Proper" criteria as may be specified by the Commission from time to time;
  - v. none of its directors has served as a director in a TREC holder or member entity of any Exchange which had been declared a defaulter or expelled as a member or its TREC has been cancelled by the Exchange; and
  - vi. it has adequate policies, procedures, systems and controls to handle conflict management, monitoring of unethical conduct and market abuse, resolve investor complaints, prevent money laundering and combat terrorist financing and ensure compliance with applicable laws.
- f. The Exchange may specify such standards for good governance, enhanced disclosures, investor protection, accountability, investor service and infrastructure requirements with regard to applicants as it may deem necessary from time to time.
- g. No applicant shall be issued a TREC of the Exchange if it or any of its directors:
- i. has been adjudged bankrupt or a receiver order in bankruptcy has been made against it or it has been proved to be insolvent even though it has obtained its final discharge;
  - ii. has compounded with its creditors for less than full discharge of debts;
  - iii. any of its directors has been convicted for any offence of moral turpitude;
  - iv. has been at any time expelled or declared a defaulter by any exchange, or its TREC has been cancelled or it has been debarred from trading in securities by any regulatory authority including the BSEC or any court having jurisdiction; and
  - v. incurs such disqualification under the provisions of any Securities law or Rules or Regulations or any other law for the time being in force, so as to disentitle such persons from seeking TREC of a stock exchange;

### **6.5 Power of the Exchange**

- a. The Exchange shall have the following powers in respect of TREC:
- i. Issuance of TREC: The Exchange shall issue TREC subject to terms and conditions as specified in the certificate with the power to renew, suspend and cancel.
  - ii. Suspension of TREC: The CRO of the Exchange shall have the power to suspend the trading operation of any TREC as he may deem fit and proper at anytime without prior notice in accordance with the Chittagong Stock Exchange (Trading Right Entitlement and Trader Certificate) Regulations, 2013. The Exchange shall have the power to suspend any TREC if there remain any unsettled dues owed by a TREC holder either to his customer, or to the Exchange till settlement of the dues.
  - iii. Cancellation of TREC: A TREC may be cancelled by the Exchange on the following grounds:
    - (a) If a TREC holder is found to be involved in any activity prohibited under any securities law;
    - (b) If a cancellation order is issued by BSEC or any other competent authority or any court of justice;
    - (c) If the TREC holder failed to comply with the requirements of the CSE (Settlement of Transactions) Regulations, 1998;
    - (d) If the TREC holder fails to comply with the requirements of the CSE (Member's Margin) Regulations, 1998;
    - (e) If the TREC holder is found to have acted in violation of these Regulations including change in the shareholding structure resulting in change of control without prior approval from the Exchange;
    - (f) If the TREC Holder fails to commence broking business within 6 (six) months of receipt of the brokerage registration from BSEC:

Provided that no TREC shall be cancelled without giving the TREC holder an opportunity of hearing.

- b. The management of the Exchange shall have the power to take such other steps in the interest of the Exchange and the capital market on behalf of the Exchange.

## **7. Conflict of Interest**

Post demutualization, an exchange shifts its strategies and objectives towards protecting interest of investors, establishing corporate governance, making profit and maximizing shareholder value through commercially oriented business practices and flexible decision making. Besides, the exchange shall also continue its role as SRO and market regulator post demutualization. The core issue remains whether the dual roles played by a demutualized exchange of business and regulator are manageable and the conflicts of interest that it raises

### **7.1 Areas of Conflicts**

Overviews of the types of conflicts of interest that exists post demutualization are given below:

- a. Conflict between dual roles of business and self regulation:
- b. Self listing:
- c. Conflict in sponsoring regulatory activities:
- d. Conflict in administration:
- e. Biasness in performing regulatory role:
- f. Conflict in remuneration of regulatory Staff:

### **7.2 Mitigation of Conflict of Interest and Preservation of Investors' Interest**

The following methods are proposed to manage and mitigate the conflicts and ensure preservation of investors' interest for Chittagong Stock Exchange Ltd:

#### **a. Empowering Independent Directors in the Board**

The Board shall be comprised of majority independent directors nominated by the Nomination and Remuneration Committee of CSE in accordance with "Fit and Proper" criteria and approved by the BSEC. Majority presence from the independent directors shall ensure fairness and transparency whenever any conflict arises.

In addition to their fiduciary duties, the independent directors will be responsible for providing managerial oversight, work for the protection of minority shareholders' rights, improving corporate credibility, governance standards and exercise independent judgment.

The Chairman of the Board shall be from the independent directors. All of the Board Committees shall be comprised of majority independent directors including the Chairman. It will ensure unbiased functioning of the committees.

**b. Code of Business and Code of Ethics**

There shall be a Code of Business and Code of Ethics for the Board which shall be outlined in details in the proposed Chittagong Stock Exchange (Board and Administration) Regulations, 2013. The codes shall constitute standards that are reasonably designed to avoid conflict, promote integrity and to deter wrongdoing.

**c. Separation of SRO Function from Commercial Activities**

CSE will follow a "Strong Exchange SRO Model" for separating SRO function from commercial operations. Under this model, CSE's potential conflict of interest will be managed through setting up separate regulatory committee and divisions (i.e. Regulatory Affairs Committee, Regulatory Affairs Division) that will function totally independent from any committees/departments of CSE involved in commercial functions.

Such separation will ensure the proper and unbiased functioning of the regulatory function of the exchange and thus help to avoid conflicts.

**d. Independent Internal Audit Department**

CSE will ensure strong internal control through having a separate Internal Audit Department, which shall have a direct reporting to the Audit and Risk Management Committee comprised of majority Independent Directors. Internal Audit will conduct regular audit to ensure all rules, regulations, bye-laws and policies are adhered to.



**e. Transferring regulatory functions during self-listing**

When CSE will go for self-listing, regulators shall perform the role which is generally performed by the Exchange, including approval of the listing and review of compliance to all listing requirements. BSEC shall be administering the listing rules. Subsequently, the trading of CSE will also be monitored by BSEC to ensure transparency and fairness. This will ensure avoidance of any potential conflict that may arise from listing in the own exchange.

**f. Reinforcing Investors' Interest Mandate**

The এক্সচেঞ্জ ডিমিউচুয়ালাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013) clearly makes it binding that CSE must give priority to public cum investors' interest if any conflict arises. CSE will reiterate this spirit through documenting it under the code of conduct of the Board.

**g. Investors' Protection Fund:**

The Exchange shall maintain an "Investors' Protection Fund" to protect the interest of the investors in case of default by the TREC Holders. It shall also keep a provision which shall provide CSE the power to set-off the security deposit by any TREC if there remain any unsettled dues owed by a TREC Holder to its customers.

The Investors' Protection Fund shall consist of contributions from the Exchange and TREC Holders in the following manner:

- (a) Contributions already made by CSE and others which are currently lying with the Exchange.
- (b) An amount representing 0.50 % (point five zero per cent) of the listing fee received by the CSE during the immediately preceding quarter, which shall be placed in the Fund immediately after closure of each quarter.
- (c) Quarterly contribution at the rate of 1 (one) taka for every Taka 10 (ten) lac or part thereof of gross cumulative turnover (buy + sale) of each TREC holder immediately after closure of each quarter.

- (d) Taka 1 (one) lac from the TREC holders other than the initial TREC holders.
- (e) All benefits accrued against unclaimed shares shall be transferred to the Investors' Protection Fund of CSE after 5 years of such accrual.
- (f) Any amount received from such other sources as may be available at the discretion of the Board.

**h. Contribution to the Settlement Guarantee Fund:**

(1) The Fund shall comprise of contributions from the following sources:

(a) Initial contribution: The initial contribution shall comprise of contributions from the Exchange and Trading Participants as follows:

- (i) Taka 200,000,000 (Taka Twenty Crore) from the Exchange;
- (ii) Taka 500,000 (Taka Five lac) per Trading Participant as subscription in the Fund. Out of which Taka 250,000 (Taka two lac fifty thousand) only will be collected on call made by the management and rest Taka 250,000 (Taka two lac fifty thousand) only will be collected between second and third year of formation of the Fund.

(b) Regular contributions:

- (i) 5% of annual net profit of the Exchange will be transferred to the Fund as a regular contribution on annual basis.
- (ii) Any income generated from of the Fund shall be attributable to this fund.

The settlement guarantee fund will be reviewed at the time of the establishment of the new clearing house.

**i. Management of Conflict of Interest at Intermediaries' Level**

CSE shall outline the rules and regulations for the intermediaries to follow in order to manage the conflicts at intermediaries level, that Conflict at intermediary level arises mainly due to intermediaries putting forth their own interest at the cost of clients/market investors, and the internal conflicts within the intermediaries that stems from intermediary structure, its product offering and markets of operation. Conflict may also arise between intermediaries and different/various types of clients.

## 8. Widening Shareholder Base

### A. Shareholding Structure

On the date of demutualization, there shall be 148 shareholders of CSE, who were members of the exchange prior to demutualization. There can be three ways through which new shareholders may come and thus widen the shareholders base:

- Through transfer of 60% of the total initially allotted shares held in blocked account;
- Through transfer of 40% free shares held by initial shareholders; and
- Through issuance of new shares to raise capital.

The post demutualization shareholding structure of CSE shall be subject to the following conditions at all time:

- a. All shares of the Exchange equivalent to the paid-up capital at the date of demutualization shall be allotted to the initial shareholders, out of which sixty percent (60%) shall be held in a blocked account till disposal to strategic investor(s), institutional investor(s) and general public.
- b. Total shares held by the TREC holders together with their connected persons, other than the shares held temporarily in the blocked account, shall not be more than 40 (forty) percent of the total issued share capital of the Exchange at any time. A strategic investor may, with the approval of the Commission, hold up to 25 (twenty five) percent of its total issued share capital: provided that, the Commission, in the public interest, may permit any strategic investor to hold shares above this threshold.
- c. No person including his/her/its connected persons, other than strategic investors, shall hold above 5 (five) percent of its issued share capital.

## **B. Operation and Entitlement**

Initial shareholders shall be entitled to any dividend, Bonus Shares, Rights Shares and sale proceeds earned from the shares held in blocked account. Bonus Shares or Rights Shares earned against the shares in blocked account will be added to those shares and will be disposed off with the shares held in blocked account according to section 8.C. of this scheme.

Rights to maintain and transfer the shares preserved in the blocked account shall vest upon the board of directors

The right to exercise voting power attached to these shares shall remain suspended till the completion of transfer of these shares.

## **C. Off-loading of Shares held in Blocked Account**

Shares held in the blocked account can be sold in a manner:

- Not more than 25% of total issued shares shall be sold to any Strategic Investor. Additional shares may be sold to the strategic investor, if allowed by the BSEC in greater interest of the capital market.
- Except shares allotted in favour of strategic investors, shares held in blocked account shall be sold to general public and/or institutional investor(s).
- The decision as to whether to accept or reject any offer from a strategic investor shall be made by the Board of Directors subject to approval of the Commission.
- Shares held in blocked account, except the portion which is to be sold to the strategic investor, are planned to be off-loaded to general public including institutions within earliest suitable time after demutualization in a manner as decided by the board and approved by the Commission.
- Price of shares of such off-loading shall be determined under the book-building method as described in the relevant securities laws.

- The board shall distribute all the sale proceeds of shares held in blocked account to the initial shareholders pro-rata basis periodically as determined by the board.

#### ***D. Limit in Shareholding***

During the sale of shares to general public/institutional investor(s) and at all time, CSE shall ensure, as per the Section 12 (1) (Ga) of the এক্সচেঞ্জ ডিমিউচুয়ালাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013), that any person, except strategic investor(s), individually or collectively with related persons cannot hold more than 5% of the total issued shares

#### ***E. Transfer of Shares***

Shares acquired by general public or institutional investor, as per the এক্সচেঞ্জ ডিমিউচুয়ালাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013), can be transferred freely as per the prevailing law of the country. However, all such transfers must ensure that all limits and restrictions imposed by the এক্সচেঞ্জ ডিমিউচুয়ালাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013) are not violated at any time.

#### ***F. Strategic Investor:***

Strategic investor (s), subject to approval from commission, can acquire up to 25% of the total issued shares. But the Commission can, for public interest, approve any strategic investor to hold more shares than this limit.

##### ***i. Suitability of Strategic Investor:***

The foremost priority for CSE following its demutualization shall be to prepare a list of potential strategic investors from a list of global securities markets, depository and clearing institutions and as well as the international investment banking institutions. While CSE management engages itself in the implementation of the 7 year business plan to create value for its investors, the Board of CSE would embark upon a global hunt for some ideal strategic investor willing to become involved in managing a domestic market in Bangladesh.

CSE would constantly plan to follow the under-mentioned strategy to achieve the goal of wider ownership of the shares by remaining with the ownership restriction and the timelines prescribed under the Act:

- Sale to Strategic Investor: Under this priority option, CSE plans to take the following steps so that it can find the most suitable strategic partner:
  - i. Identification of Suitable Strategic Investors
  - ii. Arrange Meetings with Potential Strategic Investors
  - iii. Holding Road shows/Investment Conferences in Far East, Asia Europe and North America
  - iv. Considering Technology/Product Tie-ups with other Foreign Exchanges

#### ***ii. Transfer of Shares by Strategic Investors***

According to Section 15 of the এক্সচেঞ্জস ডিমিউচ্যুয়লাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013), if any strategic investor acquires any shares, shares can only be sold to other strategic investor with approval from the Commission. The Commission, through written order, can exempt the strategic investor from provisions related to share buying, selling, acquisition and take over.

### **9. CONCLUSION**

This scheme attempts to provide a detail outline and comprehensive proposal regarding, inter alia, board and management structures, different aspects of shareholding and trading right, governance issues, discipline and restrictions and other activities which are to be adopted and followed during the demutualization process and also after demutualization. All proposals made in this document seek to uphold the overall spirit of demutualization and the provisions of the এক্সচেঞ্জস ডিমিউচ্যুয়লাইজেশন আইন, ২০১৩ (Exchanges Demutualization Act, 2013). Hence this "Demutualization Scheme", shall act as the basic guiding document for the Exchange during their journey towards demutualization to become a model exchange.

In the event of any omission, uncertainty, misunderstanding and ambiguity the Bangladesh Securities and Exchange Commission (BSEC) would provide necessary guidance to resolve these issues.

BY ORDER OF THE BOARD OF DIRECTORS

SYED SAJID HUSAIN

CHIEF EXECUTIVE OFFICER

CHITTAGONG STOCK EXCHANGE LIMITED.

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