Subcommittee on Three Pieces of Subsidiary Legislation Relating to Over-the-counter Derivative Transactions

The Administration and Regulators' Response to the Submission of the Hong Kong Association of Banks

Purpose

This paper sets out the Administration and regulators' response to the matters raised in the submission of 22 June 2015 of the Hong Kong Association of Banks ("HKAB").

Response

Reporting of valuation transaction information

2. Regarding the proposed reporting timeframe and valuation methodology for the purpose of reporting valuation transaction information, it should be noted that the first phase of implementation of reporting requirements does not cover this aspect. The Hong Kong Monetary Authority ("HKMA") and the Securities and Futures Commission ("SFC") will consult the market on expanded reporting for the next phase of implementation of the over-the-counter ("OTC") derivatives regulatory regime, and will continue to maintain close dialogue with the industry to address their concerns.

Masking relief

3. The HKMA and the SFC have provided further guidance to the industry by issuing a set of Frequently Asked Questions ("FAQs") on the Securities and Futures (OTC Derivative Transactions – Reporting and Record Keeping Obligations) Rules ("Reporting Rules") on 10 July 2015. In particular, QA43 of the FAQs provides guidance as to what specific action an institution is required to take in order to verify the existence of a prohibitive legal or regulatory limitation pursuant to Rule 26(1)(a)(i) of the Reporting Rules. The reasonable due diligence that an institution should carry out does not necessarily entail obtaining a formal legal opinion each time to support masking in a particular case, but would, at a minimum, require it to keep abreast of developments that might trigger changes which effectively allow reporting of counterparty identifying

particulars in a particular case. If further clarification is needed, the FAQs can be enhanced from time to time to give further guidance.

Prescribed stock/futures markets and clearing houses

4. The two entities proposed by the HKAB will not be included in the list of prescribed markets and clearing houses for the purposes of section 1B(2)(c) of Part 1 of Schedule 1 to the Securities and Futures Ordinance at this stage because the services provided by these entities involve OTC derivative products. Products traded or cleared through these entities are therefore not suitable to be excluded from the definition of "OTC derivative product". This has previously been explained to the HKAB.

Reporting of unique transaction identifiers ("UTIs")

5. The requirement to report UTIs is in principle consistent with international standards. The International Organization of Securities Commissions plans to issue such standards later this year, which most jurisdictions are expected to follow. In practice, transaction reporting must carry a UTI so that reported transactions can be matched and aggregated for the purpose of regulatory data analysis. Without this critical data element, a substantial part of the reported data may be subject to duplication or double-counting, which will severely compromise the accuracy and validity of regulatory data analysis for purposes of monitoring risks in the market. It is therefore important that every transaction reported, regardless of whether it is cleared or not, should carry a UTI.

6. We understand that it will take time for the industry to get their system ready in order to comply with the requirement. We therefore have provided a concession such that the UTI requirement will only come into effect in February 2016. The HKMA and the SFC will continue to communicate with the industry with a view to facilitating their compliance with the reporting requirements.

Financial Services and the Treasury Bureau
Hong Kong Monetary Authority
Securities and Futures Commission
13 July 2015