

Capital treatment of participating margins posted for the purposes of the Swap Connect

1. As discussed with the OTC Clearing Hong Kong Limited (“OTCC”), it is agreed that—
 - (a) participating margins (“PMs”) posted by authorized institutions (“AIs”) that are OTCC’s clearing members (“CMs”) for the purposes of the Swap Connect will be treated in the same manner as default fund contributions under Division 4 of Part 6A of the Banking (Capital) Rules (“BCR”); and
 - (b) the Shanghai Clearing House (“SHCH”) will be treated as if it were a CM of OTCC for the purpose of the calculation of the hypothetical capital (K_{ccp}) under Basel Framework CRE54.28 to CRE54.35¹.

2. Capital treatment of default fund contribution made by an AI to OTCC

An AI, *regardless of whether it has participated in the Swap Connect or not*, must calculate the capital charge for its default fund contribution made to OTCC in accordance with Formula 23K in section 226X(4) of the BCR as set out below:

- (a)
$$K_{AI_{CMs}} = \max \left(K_{ccp(CM)} \cdot \left(\frac{DF_{AI}^{funded}}{DF_{CCP} + DF_{CM}^{funded}} \right); 8\% \cdot 2\% \cdot DF_{AI}^{funded} \right)$$
 - (i) $K_{AI_{CMs}}$ is the capital charge for an AI’s usual default fund contribution (i.e. excluding PM in cases where the AI has participated in the Swap Connect);
 - (ii) $K_{ccp(CM)}$ is the hypothetical capital for OTCC’s trade exposures to all its CMs (including those CMs that have participated in the Swap Connect). The value of $K_{ccp(CM)}$ will be provided by OTCC; and
 - (iii) DF_{CCP} , DF_{AI}^{funded} and DF_{CM}^{funded} are as defined in section 226X(4). Any additional collateral or resources contributed by OTCC, the AI and other CMs for the purposes of the Swap Connect must be excluded as they will be accounted for in the calculation discussed below.

3. Capital treatment of participating margin posted by an AI to OTCC for the AI’s participation in the Swap Connect

If an AI has participated in the Swap Connect, the AI must, in addition to the capital charge for its usual default fund contribution calculated under paragraph 2, calculate a capital charge for its PM made to OTCC in accordance with Formula 23K in section 226X(4) of the BCR as set out below:

- (a)
$$K_{AI_{SHCH}} = \max \left(K_{ccp(SHCH)} \cdot \left(\frac{PM_{AI}}{ICM_{OTCC} + ICM_{SHCH} + PM_{CM}} \right); 8\% \cdot 2\% \cdot PM_{AI} \right)$$
 - (i) $K_{AI_{SHCH}}$ is the capital charge for an AI’s PM;

¹ https://www.bis.org/basel_framework/chapter/CRE/54.htm?inforce=20230101&published=20200327

- (ii) $K_{ccp(SHCH)}$ is the hypothetical capital for OTCC’s trade exposures to SHCH;
 - (iii) ICM_{OTCC} is OTCC’s own resources contributed to the inter-CCP margin. For application of Formula 23K, ICM_{OTCC} will be treated as the DF_{CCP} defined in paragraph (c) of Formula 23K;
 - (iv) ICM_{SHCH} is SHCH’s half of the inter-CCP margin. For application of Formula 23K, this will be treated as part of the DF_{CM}^{funded} defined in paragraph (d) of Formula 23K;
 - (v) PM_{AI} is the amount of PM contributed by the AI. For application of Formula 23K, this will be treated as the DF_{AI}^{funded} defined in paragraph (b) of Formula 23K; and
 - (vi) PM_{CM} is the total amount of PMs contributed by OTCC’s CMs. For application of Formula 23K, this will be treated as part of the DF_{CM}^{funded} defined in paragraph (d) of Formula 23K.
- (b) OTCC will disclose the value of a c-factor (“c”) to enable AIs to calculate the capital charges for their PMs in accordance with paragraph (a), where—

$$c = \frac{K_{ccp(SHCH)}}{ICM_{OTCC} + ICM_{SHCH} + PM_{CM}}$$

- (c) Currently under Basel Framework CRE54.29, the minimum risk-weight assigned to a qualifying CCP’s trade exposures to its CMs is 20%. In order to comply with the requirement set out in paragraph (a) of Formula 23K in section 226X(4) of the BCR, OTCC is required to apply a 20% risk-weight to its trade exposure to SHCH in calculating $K_{ccp(SHCH)}$ although this is not reflective of the lower credit risk of SHCH. As such, the HKMA will consider amending section 226X to allow for the application of a 2% risk-weight by OTCC in calculating $K_{ccp(SHCH)}$.

4. CAR return Part IIIe - reporting arrangement

Part IIIe: Risk-weighted Amount for Exposures to Central Counterparties (CCP)

(in HK\$'000)

Division A: Default Fund Contribution

	Default fund contribution (A1)	Capital Charge (A2)	Risk-weight % (A3)	Risk-weighted Amount (A4)
1. Qualifying CCPs				
2. Non-qualifying CCPs			1250	
SUBTOTAL				

An AI that is a CM of OTCC and has participated in the Swap Connect should report its default fund contribution and PM made to OTCC under item 1 in Division A of Part IIIe of the CAR return in the following manner—

(a) Item 1 - Column (A1) - Default fund contribution

The amount reported in respect of OTCC should be the sum of—

- DF_{AI}^{funded} (see paragraph 2(a)(iii) above); and
- PM_{AI} (see paragraph 3(a)(v) above).

(b) Item 1 - Column (A2) - Capital Charge

The amount reported in respect of OTCC should be the sum of—

- K_{AICMS} (see paragraph 2(a)(i) above); and
- K_{AISCH} (see paragraph 3(a)(i) above).

(c) Item 1 - Column (A4) – Risk-weighted Amount

The AI should report the risk-weighted amount of its default fund contribution and PM made to OTCC in column (A4), which is calculated by multiplying the sum of the two capital charges reported in column (A2) by 12.5.