**Return of Large Exposures**
**MA(BS)1D**

**<u>Summary of Changes</u>**

**1. "Default risk exposures arising from OTC derivative transactions and credit derivative contracts"**
(Return – Column (4) of Parts I, II and III; Completion Instructions - Section A paragraphs 5(vi)-(xii), (xiv), (xvi), (xix)-(xxi), (xxiii), 6-10)

AIs are now required to report their default risk exposures to individual counterparties arising from <u>all</u> their OTC derivative transactions and credit derivative contracts ("derivative exposures"), instead of reporting their exposures arising from outstanding foreign exchange and interest rate contracts to individual counterparties only if they use internal models to measure such exposures (as required in the last version of this Return).

A locally incorporated reporting institution (a) is required to calculate its derivative exposures as the sum of (i) the current exposure and (ii) the potential exposure of the relevant OTC derivative transactions and credit derivative contracts by using the current exposure method ("CEM") under the capital adequacy framework, and (b) should NOT (any longer) calculate such exposures by use of internal models for the purposes of reporting under this Return.

An overseas incorporated reporting institution may, instead of using the CEM, adopt an internal approach for reporting its derivative exposures under this Return, subject to meeting certain conditions (see paragraph 10 of the Completion Instructions for details). This is a transitional arrangement that will last until the new Standardized Approach for Counterparty Credit Risk under the Basel III capital framework is implemented in Hong Kong.

Consistent with the above changes, the Completion Instructions for reporting exposures under credit derivative contracts in this Return have been revised to provide for -

(i) the requirement to report exposure to the counterparty of a credit derivative contract if:

- the reporting institution is a protection buyer and the credit derivative contract concerned is a credit default swap or total return swap which is not recognised as a protection for the underlying asset for capital adequacy purposes (Completion Instructions - Section A paragraph 11(A)(b));

- the reporting institution is a protection seller and the credit derivative contract concerned is a credit default swap which is subject to close-out upon the insolvency of the protection buyer whilst the reference entity is still solvent (Completion Instructions - Section A paragraph 11(B)(b)); and

- the reporting institution is a protection seller and the credit derivative contract concerned is a total return swap (Completion Instructions - Section A paragraph 11(B)(d)); and

(ii) the reporting requirements under other specified circumstances (Completion Instructions - Section A paragraph 11(A)(c), 11(B)(c) and 11(B)(e)).

**2. Transitional arrangement**
(Completion Instructions – Section A paragraph 20)

Reporting institutions are allowed to report their derivative exposures based on quarter-end positions (instead of the maximum of such derivative exposures during each reporting period) until the first quarter of 2016. This means that, on an interim basis, the value to be reported by reporting institutions in column (1) (maximum exposure in reporting period) of Part I, II or III should be the sum of their maximum exposures (excluding derivative exposures) during the reporting period and their derivative exposures at the reporting date of the period concerned. From the second quarter of 2016 onwards, reporting institutions should report their maximum exposures (including the maximum of their derivative exposures) during each reporting period.

**3. "Exposures"**
(Completion Instructions – Section A paragraph 5(xv))

The definition of this term has been rewritten to enhance clarity and to cover explicitly exposures arising from OTC derivative transactions and credit derivative contracts.

4. **Reporting treatment of exposures to joint account**
(Completion Instructions – Section A paragraph 14)

Instructions provided for purposes of clarification.

**5. Reporting treatment of exposures to central counterparties**
(Completion Instructions – Section A paragraph 17)

Instructions provided for reporting derivative exposures subject to central clearing.

**6. Editorial changes**

Minor editorial changes have been made throughout the Completion Instructions without altering the essence of the reporting requirements.

The order of paragraphs has been rearranged to improve the logical flow of the Completion Instructions.

**7. Changes consequential to legislative amendments**
(Completion Instructions – Section A paragraph 5(iii) and (iv))

References to the Banking Ordinance or its related subsidiary legislation have been updated to reflect the latest version.

Hong Kong Monetary Authority
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