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Hong Kong Monetary Authority  
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8 Finance Street, Central  
Hong Kong

Supervision of Markets Division  
The Securities and Futures Commission  
35/F Cheung Kong Center  
2 Queen's Road Central  
Hong Kong

August 18 2014

Dear Sirs,

**Consultation paper on the Securities and Futures (OTC Derivative Transactions – Reporting and Record Keeping) Rules**

This letter provides the submission of LCH.Clearnet Ltd ("LCH.Clearnet") to the above consultation paper.

LCH.Clearnet is a subsidiary of the LCH.Clearnet Group, the world's leading clearing house group, which services major international exchanges and platforms, as well as a range of OTC markets. It clears a broad range of asset classes including interest rate swaps, foreign exchange derivatives, credit default swaps, bonds and repos, cash equities, exchange traded derivatives, and commodities, energy and freight derivatives. The Group's central counterparties ("CCPs") have over 190 clearing members and over 600 clients across 22 countries.

As the HKMA and SFC are aware, LCH.Clearnet is already clearing OTC derivative transactions where a counterparty is a Hong Kong incorporated entity. LCH.Clearnet's current expectation is that it will apply to be an ATS provider under section 95 of the SFO. We have the following comments on specific questions:

*Question 1: Do you have any comments or concerns about the proposed definition of "Hong Kong person", "RCH" and "ATS-CCP"?*

Paragraph 56 states that it is proposed that "the reporting obligation in respect of CCPs will only apply when the entity in question is acting in its capacity as a CCP, e.g. it will not apply in respect of transactions entered into for proprietary trading purposes." We would like it to be made clear that transactions entered into as part of a CCP's default management are not included within that definition ("in its capacity as a CCP"), and are seen in effect as proprietary trading. We have concerns about any reporting of hedging/auction activity that leads to public dissemination of a CCP's actions.

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*Question 2: Do you have any comments or concerns about the proposed types of IRS and NDF that will be subject to the mandatory reporting obligation in the initial phase of implementation?*

We would like it to be clarified in Part 3 of Schedule 1 that Forward Rate Agreements are included within the definition of an “interest rate swap agreement”.

*Question 7: Do you have any comments or concerns about how the reporting obligation in respect of CCPs has been cast?*

We support the proposal that an ATS-CCP will only need to report reportable transactions where the other counterparty is a Hong Kong incorporated company.

As we understand it, the obligations on an ATS-CCP will be:

- a) under the principal model, to report only transactions with a clearing member where that clearing member is a “company” as defined in section 2(1) of the Companies Ordinance (Cap. 622);
- b) under the agency model, to report only transactions with a client where that client is a “company” as defined above, including an identification of the clearing member as a “client clearing services provider” under Schedule 2(5)(c); and
- c) not, under any circumstances, to report trades between clearing members and clients.

Transactions already entered into between a prospective ATS-CCP and a Hong Kong incorporated entity prior to its authorisation will, as we understand it, become reportable on the ATS-CCP’s “Starting day” (para 114 (e)), at which point historical transactions will need to be backloaded (para. 17), subject to the concession and grace periods (para. 119). At the moment, there being no licencing regime in place for an OTC ATS-CCP, overseas CCPs are not yet able to make an application to become an OTC ATS-CCP. Therefore it is anticipated that they will be covered by the provisions outlined in paragraph 124 (c) (“Entity attains regulated status after concession period”). It will be important both

- d) that once the reporting obligation is in place, no restrictions on clearing with an overseas CCP are placed on Hong Kong incorporated entities pending that overseas CCP receiving authorisation as an ATS-CCP, and
- e) that no clearing obligation is imposed before overseas CCPs currently providing relevant clearing services to Hong Kong incorporated entities have received both authorisation as ATS-CCPs and designation for the purposes of the clearing obligation (subject to regulatory approval and provided that an application is made within a reasonable timeframe).

*Question 20: Do you have any comments or concerns about how the concession period and the grace period are proposed to operate?*

We have a concern that a grace period of three months may be too short under certain circumstances e.g. should more complex products fall under a clearing obligation in future. These might require the definition of additional fields to correctly capture all of the characteristics of the instruments. Six months would be an appropriate period.

*Question 22: Do you have any comments or concerns about the proposed types of transaction information required to be reported for the purposes of the reporting obligation, or as to how these have been expressed in Schedule 2?*

We would like it to be made clear that the “confirmation” referred to in paragraph 4 of Schedule 2 refers to confirmation of the original trade, and not in the case of cleared trades, confirmation by the CCP that the trade has been accepted for clearing.

*Question 28: Do you have any comments or concerns about the proposed record keeping requirements in relation to mandatory reporting?*

The record keeping requirements appear to imply that the messages sent to the HKMA need to be stored rather than the data about the trade that needs to be provided to the HKMA. LCH.Clearnet does not believe that record keeping obligations should include storage of messages sent to trade repositories. Trade repositories should be obliged to report outstanding positions to each participant and to retain that data. As such, participants can use this data to validate that all relevant trades have been reported correctly and it should not then also be necessary to have to store each message sent to the repository. We would expect compliance with a reporting obligation to be demonstrated through a comparison of the HKTR’s records with the participant’s core records concerning the business they have transacted.

Additionally, Rule 33(a) seems to us to conflict with the limitation on an ATS-CCP’s obligation only to report transactions with Hong Kong entities.

In Part 1 of Schedule 3, greater clarity is needed in paragraphs 2 and 3. For example, LCH.Clearnet currently stores the time it receives a trade sent for clearing and the time it was accepted for clearing, i.e. when LCH.Clearnet became the counterparty – these being the key points in the process, which we believe should be sufficient.

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We hope that the Authority and the Commission find this submission useful and we look forward to engaging further as proposals are refined. Please do not hesitate to contact  
regarding any questions  
raised by this submission or to discuss these comments in greater detail.



Yours faithfully