

Joint consultation paper on proposed amendments to the Clearing Rules for over-the-counter derivative transactions pursuant to global interest rate benchmark reform

March 2023



HONG KONG MONETARY AUTHORITY
香港金融管理局



SECURITIES AND
FUTURES COMMISSION
證券及期貨事務監察委員會

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FOREWORD

In line with global efforts, the Hong Kong Monetary Authority (HKMA) and Securities and Futures Commission (SFC) have been working with the Government of the Hong Kong Special Administrative Region and other stakeholders to implement a regulatory regime for the over-the-counter (OTC) derivatives market in Hong Kong. The regime, which is now in effect, provides for reporting, clearing, trading and record-keeping obligations in respect of OTC derivative transactions, among other things.

This consultation sets out our proposed changes to the mandatory clearing regime, which is governed by the Securities and Futures (OTC Derivative Transactions – Clearing and Record Keeping Obligations and Designation of Central Counterparties) Rules (Clearing Rules). We propose to remove the requirement to clear certain OTC derivative transactions referencing interbank offered rates (IBORs) that are or will no longer be published or considered representative by the relevant regulators and administrators, and instead to require clearing of those that reference alternative reference rates (ARRs) as identified by the relevant regulators in the jurisdictions concerned. These proposals should be read together with papers relating to earlier consultations on the implementation of the OTC derivatives regulatory regime in Hong Kong, particularly those on mandatory clearing. All the papers can be viewed on the websites of the HKMA and SFC.

Interested parties are invited to submit written comments on the proposed changes to either the HKMA or SFC on or before 11 April 2023 by any of the following methods:

- Online submission at: <http://www.sfc.hk/edistributionWeb/gateway/EN/consultation/>
- Email to: fss@hkma.gov.hk or otconsult@sfc.hk
- Fax to: (852) 2878 7297 or (852) 2521 7917
- Post to one of the following:

Financial Stability Surveillance Division
Hong Kong Monetary Authority
55/F, Two International Finance Centre
8 Finance Street, Central
Hong Kong

Supervision of Markets Division
Securities and Futures Commission
54/F, One Island East
18 Westlands Road
Quarry Bay, Hong Kong

If you are submitting comments on behalf of an organisation, please provide details of the organisation whose views you represent.

Please note that the names of commenters and the contents of their submissions may be published by the HKMA and SFC on their respective websites and in other documents to be published by them. In this connection, please read the Personal Information Collection Statement attached to this consultation paper.

If you do not wish your name or submission to be published by the HKMA and SFC, please state when submitting your comments that you would like to withhold your name, your submission or both from publication.

March 2023

PERSONAL INFORMATION COLLECTION STATEMENT

1. This Personal Information Collection Statement (**PICS**) is made in accordance with the guidelines issued by the Privacy Commissioner for Personal Data. The PICS sets out the purposes for which your Personal Data¹ will be used following collection, what you are agreeing to with respect to the HKMA's and SFC's use of your Personal Data and your rights under the Personal Data (Privacy) Ordinance (Cap. 486) (**PDPO**).

Purpose of collection

2. The personal data provided in your submission in response to this consultation paper may be used by the HKMA or SFC for one or more of the following purposes:
 - (a) to administer –
 - (i) the provisions of the Banking Ordinance (Cap. 155) and guidelines published pursuant to the powers vested in the HKMA; and
 - (ii) the relevant provisions² and codes and guidelines published pursuant to the powers vested in the SFC;
 - (b) to perform statutory functions under the provisions of the Banking Ordinance (Cap. 155), the Securities and Futures Ordinance (Cap. 571) and relevant provisions;
 - (c) for research and statistical purposes; or
 - (d) for other purposes permitted by law.

Transfer of personal data

3. Personal data may be disclosed by the HKMA or SFC to members of the public in Hong Kong and elsewhere as part of this public consultation. The names of persons who submit comments on this consultation paper, together with the whole or any part of their submissions, may be disclosed to members of the public. This will be done by publishing this information on the HKMA and SFC websites and in documents to be published by the HKMA and SFC during the consultation period or at its conclusion.

Access to data

4. You have the right to request access to and correction of your personal data in accordance with the provisions of the PDPO. Your right of access includes the right to obtain a copy of your personal data provided in your submission on this consultation paper. The HKMA and SFC have the right to charge a reasonable fee for processing any data access request.

¹ Personal data means personal information as defined in the Personal Data (Privacy) Ordinance (Cap. 486).

² The term "relevant provisions" is defined in section 1 of Part 1 of Schedule 1 to the Securities and Futures Ordinance (Cap. 571) and refers to the provisions of that Ordinance together with certain provisions in the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32), the Companies Ordinance (Cap. 622) and the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance (Cap. 615).

Retention

5. Personal data provided to the HKMA and SFC in response to this consultation paper will be retained for such period as may be necessary for the proper discharge of their functions.

Enquiries

6. Any enquiries regarding the personal data provided in your submission on this consultation paper, requests for access to personal data or correction of personal data should be addressed in writing to:

HKMA

Personal Data Privacy Officer
Hong Kong Monetary Authority
55/F, Two International Finance Centre
8 Finance Street
Central, Hong Kong

SFC

Data Privacy Officer
Securities and Futures Commission
54/F, One Island East
18 Westlands Road
Quarry Bay, Hong Kong

7. A copy of the Privacy Policy Statement adopted by the HKMA and SFC is available upon request.

A. Introduction

1. To meet the G20 commitments to reform over-the-counter (OTC) derivatives markets, the HKMA and SFC have implemented a regulatory regime for OTC derivatives in Hong Kong. Among other things, the regime introduces reporting, clearing, trading and record-keeping obligations in respect of OTC derivative transactions.
2. To date, we have implemented rules for mandatory reporting and mandatory clearing. Mandatory clearing took effect on 1 September 2016 to capture specified standardised interest rate swaps (IRS) between major dealers if certain conditions under the Clearing Rules³ are met. At present, three types of IRS denominated in HKD and G4 currencies (i.e. USD, EUR, GBP and JPY) are subject to mandatory clearing as tabled in Schedule 1 to the Clearing Rules (Product Tables).
3. In 2014, the Financial Stability Board (FSB) was commissioned by the G20 to:
 - (a) undertake a fundamental review of major interest rate benchmarks and to plan for reform; and
 - (b) ensure that interest rate benchmarks are robust and appropriately used by market participants.
4. Since then, various jurisdictions and regulators have been working to identify, develop and implement alternative reference rates (ARRs) which could be used instead of certain interbank offered rates (IBORs) that have either ceased (or will cease) to be published by their respective administrators, or ceased (or will cease) to be representative; and to enable an orderly transition from the IBORs to the ARRs. In the context of the Clearing Rules, the following ARRs and IBORs are relevant to the mandatory clearing regime in Hong Kong:

<i>Currency</i>	<i>IBOR</i>	<i>Identified ARR</i>	<i>Designated CCPs⁴ offering clearing services for IRS referencing ARRs</i>
USD	LIBOR	Secured Overnight Financing Rate (SOFR)	CME, LCH, OTC Clear
GBP	LIBOR	Sterling Overnight Index Average (SONIA)	CME, LCH
EUR	EONIA	Euro Short-Term Rate (€STR)	CME, LCH, OTC Clear
JPY	LIBOR	Tokyo Overnight Average Rate (TONA)	CME, JSCC, LCH

³ The Securities and Futures (OTC Derivative Transactions – Clearing and Record Keeping Obligations and Designation of Central Counterparties) Rules.

⁴ These refer to the four central counterparties (CCPs) designated under section 101J of the SFO for the purposes of providing clearing services for compliance with mandatory clearing under the Clearing Rules, namely Chicago Mercantile Exchange Inc (CME), Japan Securities Clearing Corporation (JSCC), LCH Limited (LCH) and OTC Clearing Hong Kong Limited (OTC Clear).

HKD	HIBOR	Hong Kong Dollar Overnight Index Average (HONIA)	LCH, OTC Clear
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5. The following benchmarks have ceased or will cease to be representative or published from the dates below:
- (a) EUR EONIA (all tenors) (after 3 January 2022)
 - (b) GBP LIBOR (all tenors) (after 31 December 2021)
 - (c) JPY LIBOR (all tenors) (after 31 December 2021)
 - (d) USD LIBOR (tenor of one week and two months) (after 31 December 2021)
 - (e) the remaining USD LIBOR (tenors of overnight, one, three, six and 12 months) will cease to be representative or published immediately after 30 June 2023.
6. In Hong Kong, whilst HONIA has been identified as an alternative to HIBOR, there is no plan to discontinue HIBOR as market participants still widely recognise it as a credible and reliable benchmark.
7. With a view to keeping our OTC derivatives clearing regime relevant and appropriate as the market evolves, we support international efforts to transition from IBORs to ARR. This consultation proposes various amendments to the Product Tables of the Clearing Rules to reflect global interest rate benchmark reforms. The proposed IBOR-to-ARR transition and related amendments in respect of each of the prescribed products set out in paragraphs 10 and 11 below are in line with the proposed / implemented IBOR-related changes in the mandatory clearing regimes in other major jurisdictions, including the United States (US), the United Kingdom (UK), the European Union (EU), Japan and Australia. They also reflect a policy intent to keep the scope of current clearing obligation in Hong Kong broadly unchanged.

B. Proposed amendments to Schedule 1 to the Clearing Rules

8. The major amendments proposed to the Product Tables are:
- (a) to remove specified OTC derivatives transactions referencing certain IBORs that have ceased or will cease to be published, or are no longer representative; and
 - (b) to replace those transactions with specified Overnight Index Swaps (OIS) referencing the relevant ARRs as tabled under paragraph 4 above.
9. The proposed IBOR-to-ARR changes are in line with global developments under the IBOR transition, and further ensure that the Hong Kong mandatory clearing regime remains relevant and appropriate. The proposal set out in paragraphs 10 and 11 below further take into account:

- (a) **Experiences of other jurisdictions:** The experiences of other jurisdictions over the past two years could help reduce the implementation, compliance and monitoring burden on prescribed persons and market participants;
- (b) **International consistency and convergence:** Reference was made to related amendments to the clearing obligations in other major jurisdictions such as Australia, the EU, Japan, the UK and the US (and these consistency considerations have underlined our proposed amendments to the tenor ranges for certain existing product types). In this respect, other than the proposed amendment relating to transactions referencing HONIA, the other proposed IBOR-to-ARR changes relating to transactions denominating in GBP, JPY, EUR and USD would be aligned with the requirements in the aforementioned jurisdictions;
- (c) **Availability of designated CCPs:** There are at least two CCPs designated under the Clearing Rules that currently provide clearing services for each of the proposed new types of OIS (see column 4 of the table under paragraph 4) such that specified persons are not expected to encounter significant difficulties in accessing the necessary clearing services for these types of OIS; and
- (d) **Impact on prescribed persons and market participants:** Notably, other aspects of the Clearing Rules remain unchanged, including the clearing threshold, the frequency of the calculation periods and prescribed day, the availability of designated CCPs, etc. Relevant data from the HKMA's Trade Repository also showed that participants in the Hong Kong OTC derivatives market were already voluntarily submitting the bulk of some of the proposed types of OIS for central clearing. We therefore do not anticipate a substantive compliance burden on the market to comply with the proposed amendments.

10. In line with the IBOR-to-ARR changes in other major jurisdictions, we propose:

(a) Transactions referencing GBP LIBOR

- (i) to remove the requirement to clear transactions referencing GBP LIBOR for basis swaps (item 3 of Table 1 in Schedule 1 to the Clearing Rules) and fixed-to-floating swaps (item 3 of Table 2 in Schedule 1 to the Clearing Rules); and
- (ii) to revise the requirement to clear transactions referencing GBP SONIA for OIS with tenors ranging from the current "seven days to two years" to "seven days to 50 years" (item 3 of Table 3 in Schedule 1 to the Clearing Rules).

(b) Transactions referencing JPY LIBOR

- (i) to remove the requirement to clear transactions referencing JPY LIBOR for basis swaps (item 4 of Table 1 in Schedule 1 to the Clearing Rules) and fixed-to-floating swaps (item 4 of Table 2 in Schedule 1 to the Clearing Rules); and

- (ii) to add a requirement to clear transactions referencing JPY TONA for OIS with tenors ranging from “seven days to 30 years” (new item 4 of Table 3 in Schedule 1 to the Clearing Rules).

(c) Transactions referencing EUR EONIA

- (i) to remove the requirement to clear transactions referencing EUR EONIA for OIS (item 2 of Table 3 in Schedule 1 to the Clearing Rules); and
- (ii) to add a requirement to clear transactions referencing EUR €STR for OIS with tenors ranging from “seven days to three years” (item 2 of Table 3 in Schedule 1 to the Clearing Rules).

(d) Transactions referencing HKD HONIA

- (i) to add a requirement to clear transactions referencing HONIA for OIS with tenors ranging from “seven days to 10 years” (new item 6 of Table 3 in Schedule 1 to the Clearing Rules).

The proposed addition of OIS in HKD referencing HONIA for mandatory clearing along with the retention of the current transaction types referencing HIBOR is consistent with the HKMA’s “multi-rate approach” to maintaining both HIBOR and HONIA.

(e) Transactions referencing USD LIBOR

- (i) to remove the requirement to clear transactions referencing USD LIBOR in basis swaps (item 1 of Table 1 in Schedule 1 to the Clearing Rules) and fixed-to-floating swaps (item 1 of Table 2 in Schedule 1 to the Clearing Rules); and
- (ii) to add the requirement to clear transactions referencing USD SOFR in OIS with tenors ranging from “seven days to 50 years” (new item 5 of Table 3 in Schedule 1 to the Clearing Rules).

11. A summary of the proposed amendments to the Product Tables is tabled below, and in a draft of the Securities and Futures (OTC Derivative Transactions—Clearing and Record Keeping Obligations and Designation of Central Counterparties) (Amendment) Rules 2023 as set out in Appendix A of this Consultation Paper.

Table 1 – Basis Swaps

Item	Currency	Floating rate index	Tenor	Optionality	Constant notional
1.	USD	LIBOR	28 days to 10 years	No	Yes
2.	EUR	EURIBOR	28 days to 10 years	No	Yes
3.	GBP	LIBOR	28 days to 10 years	No	Yes

Item	Currency	Floating rate index	Tenor	Optionality	Constant notional
4.	JPY	LIBOR	28 days to 10 years	No	Yes
5.	HKD	HIBOR	28 days to 10 years	No	Yes

Table 2 – Fixed-to-Floating Swaps (except Overnight Index Swaps)

Item	Currency	Floating rate index	Tenor	Optionality	Constant notional
1.	USD	LIBOR	28 days to 10 years	No	Yes
2.	EUR	EURIBOR	28 days to 10 years	No	Yes
3.	GBP	LIBOR	28 days to 10 years	No	Yes
4.	JPY	LIBOR	28 days to 10 years	No	Yes
5.	HKD	HIBOR	28 days to 10 years	No	Yes

Table 3 – Overnight Index Swaps

Item	Currency	Floating rate index	Tenor	Optionality	Constant notional
1.	USD	Fed Funds	7 days to 2 years	No	Yes
2.	EUR	EONIA €STR	7 days to 2 years 3 years	No	Yes
3.	GBP	SONIA	7 days to 2 years 50 years	No	Yes
4.	JPY	TONA	7 days to 30 years	No	Yes
5.	USD	SOFR	7 days to 50 years	No	Yes
6.	HKD	HONIA	7 days to 10 years	No	Yes

Q1. Do you have any comments regarding our proposed changes as set out in paragraphs 10 and 11 above? If so, please provide details and justifications for your comments, as well as suggestions on how best to address them.

C. Way forward

12. We invite comments on the above proposed changes. Comments should reach the HKMA or SFC no later than 11 April 2023.
13. Thereafter, we aim to table the necessary subsidiary legislation for effecting the proposed changes before the Legislative Council for negative vetting in 2023, and subject to legislative process, aim to implement the proposed changes between Q4 2023 and Q1 2024.

APPENDIX A - Securities and Futures (OTC Derivative Transactions—Clearing and Record Keeping Obligations and Designation of Central Counterparties) (Amendment) Rules []

(Made by the Securities and Futures Commission under sections 101N and 101P of the Securities and Futures Ordinance (Cap. 571) with the consent of the Monetary Authority and after consultation with the Financial Secretary)

1. Commencement

These Rules come into operation on [].

2. Securities and Futures (OTC Derivative Transactions—Clearing and Record Keeping Obligations and Designation of Central Counterparties) Rules amended

The Securities and Futures (OTC Derivative Transactions—Clearing and Record Keeping Obligations and Designation of Central Counterparties) Rules (Cap. 571 sub. leg. AN) are amended as set out in rule 3.

3. Schedule 1 amended (Specified OTC Derivative Transactions for the Purposes of Clearing Obligation and Record Keeping Obligation)

(1) Schedule 1, section 2, Table 1—

Repeal

"1.	USD	LIBOR	28 days to 10 years	No	Yes
3.	GBP	LIBOR	28 days to 10 years	No	Yes
4.	JPY	LIBOR	28 days to 10 years	No	Yes".

(2) Schedule 1, section 2, Table 2—

Repeal

"1.	USD	LIBOR	28 days to 10 years	No	Yes
3.	GBP	LIBOR	28 days to 10 years	No	Yes
4.	JPY	LIBOR	28 days to 10 years	No	Yes".

(3) Schedule 1, section 2, Table 3—

Repeal item 2

Substitute

“2. EUR €STR 7 days to No Yes”.
3 years

(4) Schedule 1, section 2, Table 3, item 3—

Repeal

“2 years”

Substitute

“50 years”.

(5) Schedule 1, section 2, Table 3, after item 3—

Add

“4. JPY TONA 7 days to No Yes
30 years

5. USD SOFR 7 days to No Yes
50 years

6. HKD HONIA 7 days to No Yes”.
10 years