



afme/

asifma

sifma

Global Foreign Exchange Division  
St Michael's House  
1 George Yard  
London  
EC3V 9DH

**By Email ([fss@hkma.gov.hk](mailto:fss@hkma.gov.hk)/[otcconsult@sfc.hk](mailto:otcconsult@sfc.hk))**

**TO:**

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

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

14 August 2014

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

The Global Foreign Exchange Division (GFXD) of the Global Financial Markets Association (GFMA) welcomes the opportunity to comment on behalf of its members on the Consultation Paper issued by the Hong Kong Monetary Authority (HKMA) and the Securities and Futures Commission (SFC) on 18 July 2014.

The GFXD was formed in cooperation with the Association for Financial Markets in Europe (AFME), the Securities Industry and Financial Markets Association (SIFMA) and the Asia Securities Industry and Financial Markets Association (ASIFMA). Its members comprise 23 global Foreign Exchange (FX) market participants,<sup>1</sup> collectively representing more than 90% of the FX inter-dealer market.<sup>2</sup> Both the GFXD and its members are committed to ensuring a robust, open and fair marketplace and welcome the opportunity for continued dialogue with global regulators.

\*\*\*\*\*

**Introduction**

The FX market is the world's largest financial market. Effective and efficient exchange of currencies underpins the world's entire financial system. Many of the current legislative and regulatory reforms have had, and will continue to have, a significant impact upon the

---

<sup>1</sup> Bank of America Merrill Lynch, Bank of New York Mellon, Bank of Tokyo Mitsubishi UFJ, Barclays, BNP Paribas, Citigroup, Credit Agricole, Credit Suisse, Deutsche Bank, Goldman Sachs, HSBC, JP Morgan, Lloyds, Morgan Stanley, Nomura, Royal Bank of Canada, Royal Bank of Scotland, Société Générale, Standard Chartered Bank, State Street, UBS, Wells Fargo and Westpac

<sup>2</sup> According to Euromoney league tables

operation of the global FX market, and the GFXD wishes to emphasise the desire of our members for globally co-ordinated regulation which we believe will be of benefit to both regulators and market participants alike.

The global FX market presents some unique challenges for trade reporting when compared with other asset classes. FX forms the basis of the global payments system and as such both the number of market participants and the volume of transactions are high. Notional turnover, as recently reported by the Bank of International Settlements, is US\$5.3 trillion/day.<sup>3</sup>

The high number and diversity within the participants of the global FX market presents many practical challenges in ensuring that the market participants that are required to report actually can do so. As the FX market is global in nature, the reporting of a transaction will often be required to multiple jurisdictions, and any variation in the trade reporting requirements will be required to be adopted by either one or both parties to the transaction, resulting in increased costs and increased operational risks.

The GFXD has consistently promoted and supported efforts to align global trade reporting standards as we believe that consistent trade reporting requirements offer regulators the best opportunity to oversee trading practices and market transparency.

We note the recent consultation performed by the CFTC on its swap data reporting and record keeping requirements<sup>4</sup> to which the GFXD responded, requesting that the CFTC should help to define a (globally consistent) standardised minimum data set which would allow convergence with other global regulatory trade reporting obligations, allowing for more effective regulatory oversight.

We also note the recent Financial Stability Board's (FSBs) Consultation Paper<sup>5</sup> on data aggregation, which promotes the desire and requirement to standardise the reporting of swaps data, and identified 4 key challenges facing the market today, namely:

- Inconsistencies still exist in trade identifier construct and other key reporting fields
- Inconsistencies exist as to when reporting is required to be submitted to the trade repository (trade date v trade date+)
- Inconsistency remains in who is required to report, including dual v single sided requirements
- Inconsistency in the global treatment of participant confidentiality

Concluding, the GFXD respectfully requests that trade reporting requirements in Hong Kong are aligned with those obligations that are currently live, such as the US and, Europe as well as the pending trade reporting obligations in Singapore, Australia and Canada.

---

<sup>3</sup> <https://www.bis.org/publ/rpfx13fx.pdf>

<sup>4</sup> <http://gfma.org/correspondence/item.aspx?id=598>

<sup>5</sup> <http://gfma.org/correspondence/item.aspx?id=575>

## **Executive Summary**

### **➤ FX Security Conversions are not FX Derivatives**

- We request that transactions entered into to fund the purchase/sale of a foreign security are considered to be a bona fide FX spot contract in situations where the settlement period is greater than T+2 banking days and that it will not be subject to reporting obligation
- Such a proposal would bring Hong Kong in-line with the US and Canada (and the GFXD notes that there are on-going regulatory discussions in Europe where the GFXD has requested that FX security Conversions are also considered to be bona fide FX spot contracts)

### **➤ Trade identifier construct**

- We support the ESMA UTI construct as being the global trade identifier standard (and that HKMA/SFC could consider the suggestions as made by the ISDA working group in respect of the fields structure)

### **➤ Conducted in Hong Kong**

- We generally support the HKMA/SFC approach to “Conducted in Hong Kong” under the 4 major criteria as stated in the Consultation paper, and would like to suggest that a consistent approach be implemented in Singapore and Australia

### **➤ Implementation timing**

- We suggest a 6 months gap between the finalisation of the rules and implementation of such to be provided for the industry

## (A) Specified Derivatives Contracts

While The HKMA/SFC have provided a list of OTC Derivative Product Class to be subject to mandatory reporting in phase 1 as set out in this consultation, which is primary NDF and IRS, the consultation states that "the obligation will be extended subsequently, and in phases, to cover other interest rate derivatives and foreign exchange derivatives...". GFXD would like to recommend that the HKMA/SFC also consider an FX transaction that is entered into solely to effect the purchase or sale of a foreign security – commonly referred to as an “FX Security Conversion” – to be a bona fide FX spot contract in situations where the settlement period is greater than T+2 banking days, and that any such contract is not a foreign exchange derivative.

For these purposes, we suggest that an FX Security Conversion Transaction be defined as the purchase, sale or exchange of a foreign currency for the sole purpose of effecting a purchase or sale of a security denominated in a foreign currency when the settlement period for such FX transaction is within the settlement cycle for such security.

Many of our members act as custodian for the securities of, in the case of broker-dealers, their customers and, in the case of banks, for their customers and those of their affiliated broker-dealers. Due to the increased access and investor interest in foreign markets, growing numbers of these customers are invested in foreign securities. To facilitate the purchase or sale of these foreign securities, bank custodians and broker-dealers, as part of their duties, often enter into a FX transaction that is incidental to and for the sole purpose of effecting the foreign securities transaction. For example, when a non-US customer wishes to purchase a US dollar-denominated security, its broker-dealer or bank custodian will enter into a corresponding FX transaction to have US dollars on hand to meet the cash currency requirements necessary for the customer to complete its purchase of the securities. These FX transactions are an integral part of the settlement process. Typically, the settlement cycle for most non-EUR denominated securities is trade date plus three days (T+3).<sup>6</sup> Accordingly, the bank custodian or broker-dealer would enter into a FX transaction on a T+3 basis as well. In some securities markets, for example in South Africa, the settlement cycle can take up to seven days (T+7).

To date, regulatory authorities in each of the United States and Canada have defined transactions used solely to fund the purchase or sale of a foreign security where the settlement period is greater than T+2 days as an FX spot contract and are thus outside the scope of OTC derivatives regulation within those jurisdictions. Hence, we consider the HKMA/SFC will apply the same treatment to these transactions and not considering them as foreign exchange derivatives.

Subjecting these transactions that are incidental to related securities transactions to OTC derivatives regulation would expose bank custodians, broker-dealers and their customers to needless operational, price, credit and other risks. As a result, participants may restrict FX Security Conversions to T+2 FX spot contracts, even when the securities settlement takes longer, thereby exposing the customer to FX risk while exposing the bank to certain operational risks and changing – and disrupting – the long-standing and well-functioning settlement processing for the systemically relevant securities markets that exists today.

OTC derivatives regulation simply should not be applied to the types of incidental transactions at issue here and will not provide any meaningful protection to participants (in the form of disclosures) or meaningful information to the regulatory authorities (in the form of regulatory reporting). Inconsistent treatment of these transactions globally should be avoided to ensure that the lack of an exclusion for FX Security Conversions from OTC derivatives regulation in some jurisdictions (e.g. Hong Kong) doesn't create unnecessary disincentives from transacting in securities in those jurisdictions by raising their transactional costs relative to other jurisdictions which have excluded them (e.g. in the United States and Canada).

---

<sup>6</sup> See [www.sec.gov/investor/pubs/tplus3.htm](http://www.sec.gov/investor/pubs/tplus3.htm)

## **(B) Conducted in Hong Kong**

The GFXD welcomes the clarification in the Consultation Paper on tying “the conducting of the transaction by the trader”, rather than “salespersons” nor the previous “origination” requirement, further proposing to consider that any transaction that is executed by a trader who is generally employed in Hong Kong, and is employed or engaged by a licensed entity in Hong Kong or perform a substantial part of his or her duties in Hong Kong (i.e. booked in Hong Kong and traded in Hong Kong) would be considered to be reportable in Hong Kong.

With respect to the entities included in the reporting obligation, the GFXD requests further clarity on the treatment of transaction “conducted in Hong Kong”, but are booked in global books (i.e. non-Hong Kong entities/foreign branches based in Hong Kong). The GFXD expects that such transactions would also be reported under the obligations of other jurisdictions (most likely Europe or the US) and suggests that the HKMA/SFC limits the obligation to Hong Kong entities or foreign branches based in Hong Kong. We specifically would like to request clarity on point 66 (d) of the Consultation Paper, in so much as the requirements for a trader who normally substantially performs his functions in Hong Kong but is subsequently required travel abroad to provide short-term cover for a colleague in another region on a non- Hong Kong entity (e.g. a Hong Kong trader travelling to New York to cover a US colleague on a US entity). Such a situation would result in any executed trades being reported under the local regulations to the local trade repository and the GFXD respectfully suggests that the HKMA is not looking to capture such activity within the Hong Kong trade repository.

The GFXD also request clarity on the treatment of transactions executed electronically by counterparties residing in Hong Kong, which are entered into a bank’s global e-trading book which naturally resides outside of Hong Kong. The GFXD suggests that these transactions would not be reportable by the bank, but could be by the counterparty, should they meet the required qualifications as a significant derivatives holder.

We also welcome the efforts to align the ‘trader location’ description with other peer regulators, such as the Monetary Authority of Singapore, and the Australian Securities and Investments Commission.

## **(C) Information to be Reported**

### Complex and Bespoke

Whilst appreciating the HKMA/SFC response to feedback gathered from previous rounds of consultations, the GFXD would like to re-iterate that there are still operation constraints on reporting complex and bespoke products. Complex and bespoke products are not traded electronically, cleared or confirmed through electronic matching platforms. We would like to re-state that there is limited standardisation of representation for these products in the marketplace and limited support in Financial products Markup Language (FpML) for trade reporting. Market participants are currently reporting these products using the Generic Product Template in FpML for US and European regulatory requirements.

The FX industry is continuing to work on standardising the representation of complex and bespoke products in FpML and the GFXD has recently commissioned work to develop the FpML representation of 20+ products. Once completed, these new FpML templates will be available to all market participants for implementation. It is however important to recognise the complexity of standardising such products and it is unlikely that any impact from this work will be seen before early 2016.

### Inter-affiliate trades

The GFXD requests clarity on the requirement to report inter-affiliate trades, i.e. back-to-back trades and trades executed at arm's length. The GFXD believes that the reporting of inter-affiliate trades does not provide any additional regulatory transparency but does incur increased operational risks and increased costs to those who report such transactions. The GFXD also believes that such transactions cause unnecessary volume to be reported to the trade repositories which could cause unnecessary spikes in volumes and potential performance issues.

#### Fields to be reported

Trade identifier: The GFXD believes that the European Unique transaction identifier (UTI) construct provides the most complete method in promoting the concept of a global UTI – such as the UTI construct being a 20 character Legal Entity identifier (LEI) followed by a 32 character trade reference number, or 10 LEI followed by 42 character trade reference number (and to be confirmed as per the development of the ISDA working group in this respect).

The GFXD suggest that the HKMA/SFC should define a UTI construct to prevent any confusion in the market place, such as that seen in Europe post the go live of trade reporting obligations under the European Markets infrastructure Regulation (EMIR).<sup>7</sup> Specifically, given the dual sided reporting requirements in Europe, trades with different UTIs cannot be matched at the trade repository, resulting in considerable reconciliation challenges, ultimately impacting the ability for the European Securities and Markets Authority (ESMA) and the National Competent Authorities in Europe to use the data as originally intended.

#### **(D) Implementation Timetable**

##### Phasing by entity type

The GFXD welcomes the proposal that licensed banks will still be entitled to concession period and grace period for transactions not covered by the interim reporting requirement (i.e. “conducted in Hong Kong”). On top of this, the GFXD would suggest HKMA/SFC to consider providing a minimum of 6 months between the date of the finalisation of the rules and the implementation of additional reporting obligation. This will allow the banks to implement and roll out all necessary works prior to their fulfilling of reporting obligations notwithstanding the concession and grace period provided.

\*\*\*\*\*

We appreciate the opportunity to share our views on this Discussion Paper. Please do not hesitate to contact, David Ngai at 852-5699 9976 / [dngai@gfma.org](mailto:dngai@gfma.org) or Andrew Harvey at +44 (0) 207 743 9312 / [aharvey@gfma.org](mailto:aharvey@gfma.org) should you wish to discuss any of the above.

Yours sincerely,



James Kemp  
Managing Director  
Global Foreign Exchange Division, GFMA

---

<sup>7</sup> Regulation (EU) No 648/2012