

Annex: Jurisdictions’ authority and process for exercising deference in relation to OTC derivatives regulation

Part A: With respect to the **authorisation and supervision of:** OTC derivatives market participants; TRs; CCPs; and exchanges or electronic trading platforms:

<p>A.1 What legal capacity, if any, do authorities in your jurisdiction have to defer to another jurisdiction's regulatory framework and/or authorities? Which authorities can exercise this capacity? Please also indicate if/when ‘partial’ or ‘conditional’ deference decisions can be made.</p>	<p>The authorisation and supervision of entities under the OTC derivatives regime in Hong Kong do not apply to overseas entities unless they wish to offer or market their services or carry on their business in Hong Kong, or, in the case of market infrastructures, to be used for fulfilling the mandatory obligations under the OTC derivatives regime in Hong Kong. In general, there is limited extra-territorial implication in relation the OTC derivatives regulation in Hong Kong. Therefore, there are limited circumstances where deference of rules to other jurisdictions would be required. Under the Securities and Futures Ordinance (SFO), amended to provide for the regulatory framework for the OTC derivatives market , provisions have been introduced to enable regulators to avoid conflicting or duplicating requirements from applying to market participants in cross-border transactions. We are now in the process of finalising the rules. In practice, reliance may be placed on the home regulator for the day to day supervision of certain overseas entities which are required to be authorised in Hong Kong.</p> <p>Please see below for a more detailed description of Hong Kong’s approach in authorisation and supervision:</p> <p><u><i>OTC Derivatives Market Participants:</i></u></p> <p>Hong Kong is in the process of implementing the regulation of the OTC derivatives market. The new regime will be jointly overseen and regulated by the SFC and the Hong Kong Monetary Authority (HKMA), with the HKMA regulating the OTC derivative activities of authorized institutions (AIs), generally known-as banks, and approved money brokers (AMBs), and the SFC regulating such activities of licensed corporations (LCs) and other prescribed persons.</p> <p>Institutions, locally or overseas incorporated, engaging in the banking or depositing taking business are required to be licensed by the HKMA as AIs. AIs are permitted to carry out OTC derivative dealing, which forms part of their mainstream businesses. In addition, institutions engaging in the money broking business must be licensed by the HKM A as AMBs. The business of money broking, however, does not involve position taking in OTC derivative transactions. Both AIs and AMBs are regulated under the Banking Ordinance.</p> <p>Under the new regime, persons that are not AIs or AMBs, and who carry on a business in dealing in, advising on, or providing client clearing services in OTC derivative transactions will be subject to licensing requirements unless otherwise exempted under the legislation. In general, licensed entities under the Hong Kong</p>
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licensing regime are Hong Kong incorporated companies and the SFC will be the primary regulator. Overseas entities generally will not be granted a licence in Hong Kong except in special circumstances that are permitted under the SFO. (see note below)

(Note: One such special circumstance is that the overseas entity may get a temporary licence to carry on regulated activities in Hong Kong for a limited period of time if it has been authorised to carry on such activities in another jurisdiction by an authority in the jurisdiction concerned which performs a function similar to the functions of the SFC and is empowered under the law of the jurisdiction concerned to investigate, and, where applicable, to take disciplinary action for, the conduct of such entity in Hong Kong.)

TRs

With respect to TR, authorization deference is not applicable as the local trade reporting regulation only accepts reporting to the TR operated by the HKMA.

CCPs

Locally incorporated CCPs will be subject to the rules and regulations set out in the SFO. As they are domestic entities and the SFC is the primary regulator, there will not be deference of rules to other jurisdiction's regulatory framework and/or authorities even if they are also licensed, registered or authorised in another jurisdiction.

An overseas CCP is not required to be authorised by the SFC in Hong Kong unless –

- a) its services are actively marketed to persons in Hong Kong; or
- b) when the mandatory clearing requirements are in place, it wishes to become a designated CCP to provide services to market participants in Hong Kong for meeting the mandatory clearing requirements in Hong Kong.

Whilst an overseas CCP that wishes to be authorised must comply with Hong Kong law, Hong Kong requirements are predominantly based on international standards, and Hong Kong relies heavily on the home regulator of the CCP for day to day supervision. Further, the authorisation of an overseas CCP is based on an assessment by the SFC that the overseas CCP is subject to regulation in its home country comparable to the regulation of CCPs in Hong Kong and consistent with international standards.

Exchanges or Electronic Trading Platforms

There is no requirement for an additional licence with respect to AIs in Hong Kong who wish to provide electronic trading platform services to customers. The HKMA supervises these trading platforms as part of the AIs' electronic banking services. Non-AI entities that wish to provide electronic trading platforms to banks may require approval as MBs and there is no deference mechanism with respect to the regulation of their services to other authorities.

Exchanges and electronic trading platforms for OTC derivatives products not operated by an AI/AMB are regulated by the SFC. Locally incorporated exchange or electronic trading platforms will be subject to the rules and regulations set out the SFO. As they are

	<p>domestic entities and the SFC is the primary regulator, there will not be deference of rules to other jurisdiction’s regulatory framework and/or authorities even if they are also licensed, registered or authorised in another jurisdiction.</p> <p>An overseas exchange or overseas electronic trading platform is not required to be authorised by the SFC in Hong Kong unless –</p> <ol style="list-style-type: none"> a) it actively markets its services to persons in Hong Kong; or b) when the mandatory trading requirements are in place, it wishes to be a designated trading platform to provide services to meet the mandatory trading requirements in Hong Kong. <p>Whilst an overseas exchange or electronic trading platform that wishes to be authorised must comply with Hong Kong law, Hong Kong requirements are predominantly based on international standards, and Hong Kong relies heavily on the home regulator of the exchange or overseas electronic trading platform for day to day supervision. Further, the authorisation is based on an assessment by the SFC that the exchange or overseas electronic trading platform is subject to regulation in its home country comparable to the regulation in Hong Kong and consistent with international standards.</p>
<p>A.2 Please provide a brief description of the standards that need to be met in coming to a decision as to whether to exercise any such deference, and the criteria/inputs used in assessing whether these standards have been met (e.g. whether “similar outcomes” is the standard used; whether an analysis of enforcement regimes or authority is included as part of the assessment; whether reference is made to implementation of international standards; etc.).</p>	<p><u>OTC Derivatives Market Participants</u></p> <p>AIs and AMBs: Please see answer to A.1.</p> <p>LCs: Please see answer to A.1..</p> <p><u>TRs</u></p> <p>As the reporting requirements impose the reporting to be made to the TR operated by the HKMA only, deference determination is not relevant.</p> <p><u>CCPs</u></p> <p>The SFC has adopted the “<i>Principles for financial market infrastructures</i>” (“PFMIs”) issued by the IOSCO in April 2012 as benchmarks against which to assess clearing houses in the course of carrying out its function to supervise, monitor and regulate clearing houses.</p> <p>For overseas CCPs, Hong Kong relies heavily on the home regulator of the CCP for day to day supervision. As Hong Kong’s requirements are predominantly based on international standards, for purposes of assessing whether the standards that an overseas CCP is subject to is comparable to that of a Hong Kong CCP, the SFC intends to adopt a “similar” regulatory outcome approach in the assessment, including consideration of the following -</p> <ul style="list-style-type: none"> - effective monitoring and supervision of the overseas CCPs, - effective and comparable enforcement regime and authority, and - expectation that the home regulators of the overseas CCPs have also implemented the international standards.

	<p><u><i>Exchanges or Electronic Trading Platforms</i></u></p> <p>As Hong Kong’s requirements are predominantly based on international standards, for purposes of assessing comparability, the SFC intends to adopt a “similar” regulatory outcome approach, and will also look at the following key considerations</p> <ul style="list-style-type: none"> • effective monitoring and supervision of the exchange or overseas trading platforms, and • effective and comparable enforcement regime and authority.
<p>A.3 Please provide a brief description of the process by which a decision to defer to another jurisdiction is taken, including any action that needs to be initiated to begin the process (e.g. an application from a jurisdiction or an entity), the general time frame for coming to a decision, any processes in place for reviewing a decision, and whether any other agreements or conditions need to be met in order for an affirmative decision to be taken (e.g. confidentiality agreements, supervisory cooperation, or reciprocal arrangements).</p>	<p><u><i>OTC Derivatives Market Participants</i></u></p> <p>Please refer to A.1.</p> <p><u><i>TRs</i></u></p> <p>Please refer to A.1.</p> <p><u><i>CCPs</i></u></p> <p>In general, there is not a process to determine equivalence of standards for deference of regulation on a jurisdiction level. The assessment on whether an overseas CCP is subject to comparable standards and supervision as local CCPs is normally triggered by an application for authorisation made by the CCP to the SFC. As set out above, SFC intends to use PFMI as a guiding principle.</p> <p>Further, SFC will normally wish to see a Memorandum of Understanding (MOU) or other information sharing and co-operation arrangement has been entered into between the SFC and the home regulator of the overseas CCP before the authorisation is granted.</p> <p><u><i>Exchanges or Electronic Trading Platforms</i></u></p> <p>In general, there is not a process to determine equivalence of standards on a jurisdiction level. The assessment on whether an overseas exchange or electronic trading platform is subject to comparable standards and supervision as local exchange or electronic trading platform is normally triggered by an application for authorisation made by the overseas exchange or trading platform to the SFC.</p> <p>The SFC will normally wish to see a MoU or other information sharing and co-operation arrangement has been entered into between the SFC and the home regulator of the overseas exchange or electronic trading platform before the authorisation is granted.</p>
<p>A.4 Please provide copies of, or weblinks to, any documentation or forms that have been developed for sharing with jurisdictions or entities as part of the comparability or equivalence assessment.</p>	<p>Since we are still in the process of finalising our rules, there are currently no documents that can be shared.</p>

<p>A.5 Please provide a list of jurisdictions that you have already determined to be comparable or equivalent, if any (and for what regulatory purposes), and please note any jurisdictions for which a determination is pending.</p>	<p>As explained above, SFC does not have a process to determine equivalence of standards on a jurisdiction level.</p>
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Part B: With respect to **requirements on market participants** related to: reporting to TRs; clearing transactions through CCPs; capital, margin and/or other risk mitigation requirements; and executing transactions on exchanges or electronic platforms:

<p>B.1 What legal capacity, if any, do authorities in your jurisdiction have to defer to another jurisdiction's regulatory framework and/or authorities? Which authorities can exercise this capacity? Please also indicate if/when 'partial' or 'conditional' deference decisions can be made.</p>	<p>The Securities and Futures (Amendment) Ordinance 2014 (Amendment Ordinance) provides for the framework for reporting, clearing and trading of OTC derivative transactions.</p> <p>The requirements on reporting, clearing and trading are imposed on prescribed persons. Prescribed persons are AIs, AMBs, LCs, and such persons as prescribed under the respective reporting rules/clearing rules/trading rules (as appropriate) as being subject to those obligations.</p> <p><u>Requirement to report to TRs</u></p> <p>The Amendment Ordinance provides that a Prescribed person must report those OTC derivative transactions as specified in the rules to the TR operated by the HKMA. There is no mechanism for deference in this regard, although the rules allow reporting can be made by an agent, such as a global TR, to the HKMA.</p> <p><u>Requirements to clear transactions through CCPs</u></p> <p>The Amendment Ordinance provides that a Prescribed person must clear certain OTC derivative transactions with a designated CCP, and in accordance with the clearing rules. The Amendment Ordinance provides for a rule making power to prescribe circumstances in which the requirement to clear with a designated CCP is taken to have been complied with.</p> <p>In this regard, the clearing rules will be developed at a later stage with a view to avoiding any conflicts or duplication for cross-border transactions. Consideration will be given to including transactions cleared at CCP supervised by a competent overseas authority as one of the prescribed circumstances where our clearing obligation may be taken to have been complied with. In the meantime, we will closely monitor international development before finalising our cross border proposals on clearing.</p> <p><u>Requirements to execute transactions on exchanges or electronic platforms</u></p> <p>The Amendment Ordinance provides that a Prescribed person must execute certain OTC derivative transactions only on a designated trading platform, and in accordance with the trading rules. The Amendment Ordinance provides for a rule making power to prescribe circumstances in which the requirement to trade only on a designated trading platform is taken to have been complied with.</p> <p>In this regard, we will carefully study our local market</p>
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	<p>in order to determine how best to implement the trading obligation. Consideration will be given to including transactions traded on a trading platform supervised by a competent overseas authority as one of the prescribed circumstances where our trading obligation may be taken to have been complied with. In the meantime, we will closely monitor international development before finalising our cross border proposals on trading obligation.</p> <p><u>Capital, margin and/or other risk mitigation requirements for non-centrally cleared derivatives</u></p> <p>For locally incorporated AIs, capital requirements consistent with the Basel III framework are set out in the Banking (Capital) Rules. Overseas incorporated AIs will be subject to the capital requirements under their home jurisdiction. A framework to defer to the capital requirements of another jurisdiction is not applicable.</p> <p>Margin and other risk mitigation requirements for non-centrally cleared derivatives are being developed, Hong Kong intends to update the relevant prudential regimes for respective derivatives market participants to align with the international standards recommended by the BCBS-IOSCO Working Group on Margining Requirements and the IOSCO Working Group on Risk Mitigation Standards where appropriate. We will also closely monitor international developments in the implementation of those standards before finalising our policy proposals for the treatment of cross-border derivatives transactions.</p>
<p>B.2 Please provide a brief description of the standards that need to be met in coming to a decision as to whether to exercise any such deference, and the criteria/inputs used in assessing whether these standards have been met (e.g. whether “similar outcomes” is the standard used; whether an analysis of enforcement regimes or authority is included as part of the assessment; whether reference is made to implementation of international standards; etc.).</p>	<p>Whilst we have not yet finalised our decision on deference in respect of cross-border derivatives transactions, Hong Kong would intend to adopt a “similar” regulatory outcome approach where appropriate as recommended by the international standards, and the deference framework would likely take into account the following factors:</p> <ul style="list-style-type: none"> - the quality of the relevant regulatory and enforcement regimes for derivatives market participants, and - the equivalence and comparability of the relevant rules or requirements (including whether the home/host regulators have put in place a regulatory regime for non-centrally cleared derivatives consistent with the international standards).
<p>B.3 Please provide a brief description of the process by which a decision to defer to another jurisdiction is taken, including any action that needs to be initiated to begin the process (e.g. an application from a jurisdiction or an entity), the general time frame for coming to a decision, any</p>	<p>We have not yet determined a process for deference in respect of cross-border derivatives transactions. We will closely monitor the development of such process by other jurisdictions when considering an appropriate deference process for Hong Kong.</p>

<p>processes in place for reviewing a decision, and whether any other agreements or conditions need to be met in order for an affirmative decision to be taken (e.g. confidentiality agreements, supervisory cooperation, or reciprocal arrangements).</p>	
<p>B.4 Please provide copies of, or weblinks to, any documentation or forms that have been developed for sharing with jurisdictions or entities as part of the comparability or equivalence assessment.</p>	<p>N/A since we are still in the process of considering an appropriate deference framework for Hong Kong in respect of cross-border derivatives transactions.</p>
<p>B.5 Please provide a list of jurisdictions that you have already determined to be comparable or equivalent, if any (and for what regulatory purposes), and please note any jurisdictions for which a determination is pending.</p>	<p>N/A since we are still in the process of considering an appropriate deference framework for Hong Kong in respect of cross-border derivatives transactions.</p>