

**立法會**  
**Legislative Council**

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(These minutes have been seen  
by the Administration)

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**Subcommittee on Securities and Futures (Futures Contracts) Notice 2012**

**First meeting on**  
**Tuesday, 22 May 2012, at 2:30 pm**  
**in Conference Room 2B of the Legislative Council Complex**

- Members present** : Hon James TO Kun-sun (Chairman)  
Hon Audrey EU Yuet-mee, SC, JP  
Hon CHIM Pui-chung  
Hon KAM Nai-wai, MH
- Public officers attending** : Mr Anthony LI  
Principal Assistant Secretary for  
Financial Services and the Treasury (Financial Services) 2
- Mr Daryl HO  
Head, Market Development Division  
Hong Kong Monetary Authority
- Attendance by invitation** : Mr Rico LEUNG  
Senior Director, Supervision of Markets Division  
Securities and Futures Commission
- Ms Daphne DOO  
Director, Supervision of Markets Division  
Securities and Futures Commission

Mr Gerald D GREINER  
Chief Operating Officer  
Hong Kong Exchanges and Clearing Limited

Mr Kelvin LEE  
Vice President, Platform Development and Strategy Department  
Hong Kong Exchanges and Clearing Limited

**Clerk in attendance** : Ms Anita SIT  
Chief Council Secretary (1)5

**Staff in attendance** : Miss Evelyn LEE  
Assistant Legal Adviser 10

Mr Hugo CHIU  
Council Secretary (1)5

## **I Election of Chairman**

Mr James TO, the member with the highest precedence among those present at the meeting, presided over the election of the Chairman of the Subcommittee. He invited nominations for the chairmanship of the Subcommittee.

2. Mr James TO was nominated by Mr KAM Nai-wai and the nomination was seconded by Mr CHIM Pui-chung. Mr James TO accepted the nomination. There being no other nomination, Mr James TO was elected Chairman of the Subcommittee.
3. Members agreed that there was no need to elect a Deputy Chairman.
4. Members noted and accepted the application for late membership from Ms Audrey YU.

## II Meeting with the Administration

*(issued on 2 May 2012)*

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|------------------------------|--|
|                              | — Legislative Council Brief on Securities and Futures (Futures Contracts) Notice 2012 issued by the Financial Services and the Treasury Bureau, Hong Kong Monetary Authority and Securities and Futures Commission |
| L.N. 81 of 2012              | — Securities and Futures (Futures Contracts) Notice 2012   |
| LC Paper No. LS60/11-12      | — Report of the Legal Service Division on subsidiary legislation gazetted on 4 May 2012  |
| LC Paper No. CB(1)1933/11-12 | — Background brief prepared by the Legislative Council Secretariat)  |

### Discussion

5. The Committee deliberated (Index of proceedings attached at **Appendix**).

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### Follow-up actions to be taken by the Administration

6. The Administration was requested to provide the following information:
- (a) In respect of the proposed voluntary clearing of over-the-counter ("OTC") derivatives transactions, to provide information on –
    - (i) the steps to be taken for the establishment of a local central counterparty ("CCP") for the voluntary clearing of OTC derivatives transactions, and the expected timeframe;
    - (ii) the procedures for the Securities and Futures Commission to approve a local CCP and authorize the latter to provide clearing service for specific types of OTC derivatives, and the relevant considerations and criteria involved;

- (iii) the types of products that are intended to be covered under the voluntary clearing regime;
  - (iv) how the risks associated with OTC derivatives transactions can be reduced through the establishment of a local CCP for voluntary clearing;
  - (v) what are the risks associated with a local CCP for voluntary clearing and what risk management measures will be put in place by and for the local CCP under contemplation;
  - (vi) the role and possible liability of the HKSAR Government under the voluntary clearing regime;
  - (vii) the estimated volume of OTC derivatives transactions and the percentage of such volume out of the global transaction volume of OTC derivatives;
  - (viii) the benefits of the establishment of a local CCP for voluntary clearing; and
  - (ix) the consequences of not establishing a local CCP for voluntary clearing.
- (b) In respect of the mandatory clearing obligation to be imposed on market participants in the proposed regulatory framework for the OTC derivative market, to provide information on –
- (i) whether it is mandatory for Hong Kong to follow the "G20 requirements" and pursue mandatory clearing of OTC derivatives through CCPs;
  - (ii) if the answer to (i) above is affirmative, what are the risks (if any) that may be faced by the financial system of Hong Kong and whether Hong Kong can stand such risks; and
  - (iii) what will be the loss to or impact on Hong Kong, should Hong Kong choose not to follow the said "G20 requirements" and/or not providing a local CCP.
- (c) To consider imposing a cap (say, on a daily basis or otherwise) on the transaction volume of OTC derivatives to be handled under the proposed voluntary clearing regime and/or specifying a cap on the face value of each OTC derivative transaction that is to be regarded as a futures contract that may be cleared through a local CCP.

7. The Subcommittee agreed that the Chairman should move a motion at the Council meeting on 30 May 2012 to extend the scrutiny period of the Securities and Futures (Futures Contracts) Notice 2012 to 27 June 2012.

### **III Any other business**

#### Date of next meeting

8. The Chairman remarked that the next meeting would be held upon the receipt of written response from the Administration.

9. There being no other business, the meeting ended at 3:44 pm.

Council Business Division 1  
Legislative Council Secretariat  
11 September 2012

**Proceedings of the  
Subcommittee on Securities and Futures (Futures Contracts) Notice 2012  
First meeting on Tuesday, 22 May 2012, at 2:30 pm  
in Conference Room 2B of the Legislative Council Complex**

Time Marker	Speaker	Subject(s)	Action Required
000700 – 001017	Mr James TO Mr KAM Nai-wai Mr CHIM Pui-chung	Election of Chairman  Ms Audrey YU's application for late membership	
001018 – 001623	Administration Securities and Futures Commission (SFC)	Briefing by the Administration and the Securities and Futures Commission ("SFC") on the Securities and Futures (Futures Contracts) Notice 2012 ("the Notice"). SFC added that the Hong Kong Exchanges and Clearing Limited ("HKEx") would establish a local central counterparty ("CCP"). This local CCP would need to be approved by SFC as a recognized clearing house ("RCH") before it could commence operation.	
001624 – 002356	Mr CHIM Pui-chung Administration SFC	<p>Mr CHIM enquired:</p> <p>(a) about the types of futures products and derivatives products that were currently subject to the Administration's regulation and their relevant clearing arrangements; and</p> <p>(b) whether Loco London gold investment and foreign exchange trading would be covered in the proposed regulatory framework for the over-the-counter ("OTC") derivatives market.</p> <p>The Administration replied that:</p> <p>(a) the Notice would neither affect the existing clearing arrangements for futures products nor extend the coverage of the Securities and Futures Ordinance (Cap. 571)("SFO") to Loco London gold investment;</p> <p>(b) The aim of the Notice was to enable OTC derivatives transactions cleared through a local OTC CCP to enjoy insolvency override protection.</p> <p>SFC added that it employed the following means to regulate futures trading in Hong Kong:</p>	

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		<p>(a) A futures exchange must obtain the approval of SFC before it could commence operation; and</p> <p>(b) A party engaged in dealing in futures contracts must apply for the relevant licence from SFC.</p> <p>SFC also pointed out that the Notice was a provisional arrangement to pave the way for the implementation of the mandatory clearing requirement (whereby market participants would be obligated to centrally clear certain OTC derivatives through a designated CCP approved by SFC) under the proposed full-fledged regime for the OTC derivatives market in Hong Kong.</p>	
002357 – 002732	Mr CHIM Pui-chung Chairman Hong Kong Monetary Authority (HKMA)	<p>Mr CHIM enquired whether the proposed regulatory regime for the OTC derivatives market in Hong Kong would cover foreign exchange trading.</p> <p>The Hong Kong Monetary Authority ("HKMA") responded that foreign exchange was not recognized as a type of OTC derivatives and thus would not be covered under the proposed regime for the OTC derivatives market. The proposed regime for the OTC derivatives market would initially cover interest rate swaps and non-deliverable forwards.</p>	
002733 – 003322	Mr CHIM Pui-chung Chairman Hong Kong Exchanges and Clearing Limited (HKEx) Administration	<p>Mr CHIM remarked that the Administration should:</p> <p>(a) set out the respective types of products to be covered by the proposed voluntary clearing arrangement and the proposed mandatory clearing regime;</p> <p>(b) clarify which party would bear the operation costs of the local OTC CCP; and</p> <p>(c) explain the objective of the proposed voluntary clearing arrangement and the proposed mandatory clearing regime, and explain how central clearing could protect the interests of both investors and market participants.</p>	

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		<p>The Chairman pointed out that the Legislative Council Brief provided by the Administration did not specify the products to be covered by the proposed voluntary clearing arrangement, and requested the Administration to provide written information on this matter.</p> <p>The Administration and HKEx replied that:</p> <ul style="list-style-type: none"> <li>(a) interest rate swaps and non-deliverable forwards would be covered under the proposed mandatory clearing regime and the proposed voluntary clearing arrangement; and</li> <li>(b) upon commencement of operation of the Notice, HKEx would establish a local OTC CCP, and any local CCP would need to be approved by the SFC as an RCH before it could commence operation. In addition, the local OTC CCP had to obtain the authorization of SFC for each type of OTC derivatives product covered by its clearing service.</li> </ul>	
003323 – 004802	Chairman SFC Administration HKEx HKMA	<p>The Chairman requested the Administration to provide, in respect of the proposed voluntary clearing of OTC derivatives transactions, information on:</p> <ul style="list-style-type: none"> <li>(a) the types of products that were intended to be covered under the voluntary clearing regime;</li> <li>(b) the steps to be taken for the establishment of a CCP for the voluntary clearing of OTC derivatives transactions, and the expected timeframe; and</li> <li>(c) the procedures for the SFC to approve a local CCP and authorize the latter to provide clearing service for specific types of OTC derivatives, and the relevant considerations and criteria involved.</li> </ul> <p>The Chairman queried whether it would be more appropriate for the Notice to be made after (a) the OTC CCP established by HKEx had been approved by SFC as an RCH; and (b) the OTC CCP had obtained authorization from SFC to</p>	The Administration to take action as per paragraph 6 of the minutes.

Time Marker	Speaker	Subject(s)	Action Required
		<p>provide clearing service for the OTC derivatives products concerned.</p> <p>SFC advised that it would take a few months for SFC to process the application for approval of the OTC CCP established by HKEx as an RCH and to authorize such RCH to provide clearing service for specific products. If the Notice did not come into operation as scheduled, SFC would not, under the existing SFO, have the authority to regulate the clearing of OTC derivatives transactions.</p> <p>In reply to the Chairman's enquiry, the Administration confirmed that if the Notice came into operation as scheduled, SFC would have the power to approve the OTC CCP established by HKEx as an RCH and authorize the CCP to provide clearing service for specific types of OTC derivatives. A key consideration of SFC in approving a CCP as an RCH was the robustness of the CCP's risk management measures based on the relevant international standards.</p> <p>The Chairman expressed concern that the transaction volume to be handled by the local OTC CCP might be huge and beyond its risk capacity. As such, the Administration should provide detailed information on the proposed voluntary clearing and mandatory clearing of OTC derivatives transactions for members' consideration, in particular information on the risk management measures.</p>	
004803 – 005009	Mr CHIM Pui-chung Administration	Mr CHIM concurred with the Chairman, and remarked that the Administration should send higher ranking officials to explain the policy and provide further information. Otherwise, it would be difficult for him to support the Notice.	
005010 – 010130	Chairman Administration SFC HKEx	<p>HKEx made the following remarks:</p> <p>(a) HKEx was currently operating three clearing houses and had extensive experience in risk management;</p> <p>(b) The main purpose of the establishment of a clearing house was to reduce risks through netting;</p>	

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		<p>(c) It was envisaged that the volume of OTC derivatives transactions to be handled by the local OTC CCP would not be huge;</p> <p>(d) The fees of the local OTC CCP would be competitive in comparison with overseas CCPs;</p> <p>(e) HKEx would be prepared to brief members on the risk management measures of the local OTC CCP; and</p> <p>(f) HKEx had discussed with major banks in Hong Kong and they indicated keen interests to use the service of the local OTC CCP.</p> <p>The Chairman suggested the Administration consider imposing a cap (say, on a daily basis or otherwise) on the transaction volume of OTC derivatives to be handled under the proposed voluntary clearing regime and/or specifying a cap on the face value of each OTC derivative transaction that was to be regarded as a futures contract that may be cleared through a local CCP. Amendments to the cap should be subject to the vetting of LegCo.</p> <p>SFC responded that if a cap was set on the transaction volume of OTC derivatives to be handled under the proposed voluntary clearing arrangement, market participants might choose to use the CCPs in other jurisdictions instead. There would also be technical difficulty in determining the cap.</p> <p>The Chairman remarked that the cap could be revised if needed.</p> <p>HKMA advised that the establishment of a local OTC CCP would not bring additional risks to the financial market of Hong Kong as the risks concerned would be borne by the local CCP and its members. The netting effect of the CCP's clearing services would actually reduce the risks of the OTC derivatives transactions concerned. HKMA also pointed out that one of the causes of the financial tsunami in 2008 was that OTC derivatives transactions were not cleared by CCPs.</p>	<p>The Administration to take action as per paragraph 6 of the minutes.</p>

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010131 – 011409	Mr CHIM Pui-chung Chairman Administration SFC	<p>Mr CHIM remarked that the Administration, SFC, HKMA and HKEx should provide further information to let the public and industry know the purpose of the proposed voluntary clearing arrangement, the proposed mandatory clearing obligation and the establishment of a local OTC CCP. He was also concerned about (a) which party would bear the operation costs of the local OTC CCP; and (b) whether the local OTC CCP had the capability to handle OTC derivatives transactions of huge size.</p> <p>At members' request, the Administration undertook to:</p> <p>(a) in respect of the proposed voluntary clearing of OTC derivatives transactions, provide information on:</p> <ul style="list-style-type: none"> <li>(i) how the risks associated with OTC derivatives transactions could be reduced through the establishment of a local CCP for voluntary clearing;</li> <li>(ii) what were the risks associated with a local CCP for voluntary clearing and what risk management measures would be put in place by and for the local CCP under contemplation;</li> <li>(iii) the role and possible liability of the HKSAR Government under the voluntary clearing regime;</li> <li>(iv) the estimated volume of OTC derivatives transactions and the percentage of such volume out of the global transaction volume of OTC derivatives;</li> <li>(v) the benefits of the establishment of a local CCP for voluntary clearing; and</li> <li>(vi) the consequences of not establishing a local CCP for voluntary clearing.</li> </ul> <p>(b) in respect of the mandatory clearing obligation to be imposed on market participants in the proposed regulatory framework for the OTC derivative market, provide information on:</p>	The Administration to take action as per paragraph 6 of the minutes.

<b>Time Marker</b>	<b>Speaker</b>	<b>Subject(s)</b>	<b>Action Required</b>
		<p>(i) whether it was mandatory for Hong Kong to follow the "G20 requirements" and pursue mandatory clearing of OTC derivatives through CCPs;</p> <p>(ii) if the answer to (i) above was affirmative, what were the risks (if any) that might be faced by the financial system of Hong Kong and whether Hong Kong could stand such risks; and</p> <p>(iii) what would be the loss to or impact on Hong Kong, should Hong Kong choose not to follow the said "G20 requirements" and/or not providing a local CCP.</p>	
011410 – 011510	Chairman Administration	Extension of the scrutiny period and date of next meeting	

Council Business Division 1  
Legislative Council Secretariat  
11 September 2012