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TO:
Financial Infrastructure Department
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Re: HKTR Consultation

The Global Foreign Exchange Division (GFXD) welcomes the opportunity to comment on HKMA's consultation. On behalf of its members, the GFXD would like to take the opportunity to comment on a number of issues around the implementation of a trade repository for foreign exchange transactions and to continue our recent discussions with you in more detail with the aim of aligning and coordinating development work as closely as possible to the benefit of both regulators and industry.

The GFXD was formed in co-operation 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 22 global FX market participants[1], collectively representing more than 90% of the FX market[2]. Both the GFXD and its members are committed to ensuring a robust, open and fair market place.

1. Overview and current FX industry initiatives

The GFXD welcomes the goals of enhancing regulatory oversight and promoting greater transparency. It is working with its members to implement a trade repository for the FX industry that aims, to the greatest extent possible, to meet global regulatory needs.

Its members recently announced their recommendation to partner with DTCC and Swift to develop a global foreign exchange trade repository. This selection was the result of an extended evaluation, Request for Information (RFI) and public Request for Proposal (RFP) process that began back in December 2010, with the RFP issued in April 2011.

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[1] Bank of America Merrill Lynch, Bank of New York Mellon, Bank of Tokyo Mitsubishi, Barclays Capital, BNP Paribas, Citi, Credit Agricole, Credit Suisse, Deutsche Bank, Goldman Sachs, HSBC, JP Morgan, Lloyds, Morgan Stanley, Nomura, RBC, RBS, Société Générale, Standard Chartered Bank, State St., UBS, and Westpac

[2] According to Euromoney league tables

The project is currently in the scoping phase and key work areas will cover overall functionality, technology, connectivity, messaging and data formats amongst other areas. However, this must crucially be framed in the context of understanding how the needs of multiple regulators can be met. The GFXD would welcome the opportunity to discuss this in more detail with you.

A common, global approach to trade repositories

The selection of a preferred partner for trade repository services arises from the general preference of the industry for the use of global trade repositories, rather than multiple, fragmented local repositories. This is because they provide the chief benefits of enhanced regulatory oversight and efficiency of data capture. This is particularly the case for the FX market which is characterised by vastly higher number of transactions and participants when compared to other asset classes given its position as the basis of the global payments system.

Comprehensive oversight

Trade repository information must be consistent, complete and as non-duplicative as possible in order for it to be meaningful, both for market surveillance and systemic risk monitoring. Global trade repositories provide a centralised point for submission of data, giving regulators access to both on and offshore trades and allowing them to build a complete picture regarding the positions of overseen entities. Since local regulators may typically only exert jurisdiction over local firms, currencies traded offshore by offshore entities would not be subject to regulation. They would therefore not be reported to the local repository, limiting the usefulness of that subset of data. Building an accurate picture of systemic risk or trade activity becomes significantly more difficult where the trade population is fragmented across a number of localised trade repositories, particularly considering the volume of participants and transactions present in the FX market, and in the absence of standardised global formats. The value of a comprehensive data set can also extend to implementation of other regulatory initiatives, for example, in analysing whether to mandate clearing for particular products and in establishing block trade sizes and appropriate reporting delays.

Efficiency

There are a number of efficiency arguments for global trade repositories from all market participants' perspectives.

- Cost – global trade repositories reduce the implementation costs related to building out and connecting to relevant trade repositories for both regulators and market participants alike. For reporting parties, global trade repositories allow a centralised reporting channel with common technology, messages and trade formats. Given the number of market participants engaging in cross-border transactions, local repository reporting may add significant costs for both buy and sell side participants as they are required to report to a number of repositories. Hardest hit might be the smaller, regional banks that would likely be expected to undertake the burden of international reporting on behalf of their clients. Centralised client due diligence would also produce significant savings.
- Data consistency and common standards – agreed global data formats and standards for LEIs and product and trade identifiers would also promote significant benefits for all

users. The industry is making progress in this regard and we fully support the comments made in the Coalition of Financial Services Firms and Trade Associations letter dated 8 September regarding LEI development and submitted in response to your consultation. Where local repositories prevail, regulators will need to be able to interpret and aggregate data across a number of differently formatted outputs, which can be inefficient at best. Timely access to and interpretation of a comprehensive data set will be important in times of market crisis and this will be hindered if regulators are required to seek trade and position data from a number of repositories.

- Implementation – global trade repositories may also help to minimise the risks of conflicting implementation deadlines and reduce time to market.

Accommodating different jurisdictional requirements

Of course, any global trade repository must meet the needs of the multiple regulators that it serves. In order to do that, the GFXD and its members support the efforts being made across international forums to standardise both data formats and reporting requirements. The current implementation status of global regulation does mean that final requirements have not yet been set and so any moves to implement trade repositories should be done so with flexibility in mind. It is important to stress that the development of the FX trade repository is being done so with global regulatory reporting in mind and not simply with a focus on the US's Dodd-Frank rules. This extends to reviewing the options for the legal entity structure to address any indemnity requirements, building data centres in location-neutral venues and submitting the FX trade repository for regulation in multiple jurisdictions.

Whilst the industry would prefer global data repositories to be implemented for the reasons set out above, the GFXD understands that certain jurisdictions prefer to mandate the use of a local trade repository. A number of operating models are being considered and it may be possible to implement a local trade repository within a global framework without necessarily ceding physical control to an offshore location. Such a local instance might even be operated by the regulator under licence from a global provider. In instances where a separate local repository is conceived and built, for the reasons outlined above, it would be preferable for the local repository to utilise agreed global formats and parameters to facilitate reporting, and better still to allow trade data to be fed from a global trade repository to a local repository and possibly vice versa.

2. General comments on the consultation paper

2.1. Entities subject to the mandatory reporting requirement

The Consultation Paper discusses allowing reporting through an agent. We believe there are various scenarios that would make this beneficial. Non financial intermediaries executing a low-volume of trades, for instance, may not have, or desire to build, the necessary infrastructure to fulfil the reporting requirements. Such participants may find the build-out costs to be prohibitive, or will prefer to avoid them. This will be particularly prevalent given the number of market participants in FX.

We therefore agree that third party facilitation of trade reporting should be permitted. TR members, and trade confirmation and matching vendors etc could all be potential providers of information to a trade repository. Perhaps more importantly, we agree with the proposal that institutions may delegate reporting to a third party global trade repository. Ideally, the HKTR would allow a two-way feed with a global trade repository in order to ensure that any locally fed trades could be combined with a global data set, which the HK regulators would have access to.

2.2. Products subject to mandatory reporting requirements

We understand that only certain types of interest rates swaps and non-deliverable FX forwards (NDFs) will be required to be reported during the initial phase with reporting taking effect from start of 2013. Furthermore the consultation proposes that transactions with a Hong Kong nexus will be required to be reported. We would welcome further clarification of exactly which trades and by which counterparty would be subject to the reporting requirements. As discussed above, we believe that ensuring connectivity between the HKTR and the proposed FX global trade repository will ensure that HKMA has access to both onshore and offshore NDF trades that are of interest.

One area in which work is ongoing relates to client confidentiality issues. A number of jurisdictions place restrictions on the counterparty details that may be reported to a trade repository. Reporting participants may therefore face legal conflicts where counterparties are located in jurisdictions which do not permit such disclosure. The final reporting requirements should recognise these potential conflicts.

2.2.1.Interaffiliate trades

Given the high volume of transactions in FX compared to any other asset class, we believe that only transactions settling with an un-affiliated third party should be reported. Many millions of trades occur daily between different affiliates of the same institution which are not relevant to that institution's external market positioning and would increase ticket volumes at any trade repository significantly. We would also point out that FX is used to manage balance sheet and foreign asset exposures for income attribution, which under this rule would be subject to reporting. We do not believe that reporting inter-affiliate trades will achieve the goals of reducing systemic risk and increasing transparency. Inter-affiliate trades represent allocation of risk within a corporate group and do not give rise to the same systemic risk issues that are raised by trades by one corporate group with another. Also, reports about inter-affiliate FX trades will not give meaningful indications about the overall FX market or the overall exposure of the relevant corporate group.

2.2.2.Aggregation of trades below a certain notional threshold

Given the sheer volume of trades in the FX market, we have previously suggested to regulators the concept of setting a notional threshold (subject to periodic revision) so that the noise of small scale FX transactions is filtered out. This will leave trade repositories to focus on materially significant transactions. In the absence of such a threshold, the global data set is likely to be overwhelming. A notional threshold of USD1m or equivalent would be a reasonable, initial starting point.

In the absence of a carve-out for smaller trades, we would recommend allowing reporting counterparties the option of aggregating smaller trades to reduce the reporting burden. Trades could be aggregated by relevant criteria, for example, by currency-pair, trade-date, value-date, counterparty and / or direction (average buys / average sells; the average buys / average sells is used so to obtain a true FX trade without odd rates or amounts in either of the aggregated currencies). Aggregation might then occur by time of day (e.g. before end of day in each region), up to a pre-defined total notional exposure for each counterparty and / or for trades not greater than a pre-defined size e.g. USD 1m or equivalent (if an input ticket is too large it would be passed through without aggregation). It may also be possible to use number of tickets in the aggregate as a cut-off in order to accommodate the IT capabilities of the receiving systems. Note that the regulator would still have access to the underlying trades via a reporting counterparty's record keeping. Alternatively, a separate data store for micro-trades could be set up within the trade repository that would be used solely to store transactions whilst the aggregate was used for general reporting.

2.3. Matching and confirmation for local CCP clearing

We note that forwarding of trades to the HKEx CCP can only occur after trades have been matched at the HKTR and therefore that clearing flows are dependent upon reporting flows. We believe these should be independent of one another in order to remove the risk of delays in clearing.

2.4. Other services

We would welcome confirmation by the HKMA as to the ownership status of information submitted to the HKTR and assume that it is intended that reporting parties retain ownership of any data submitted. We also assume that any information submitted to the HKTR will be used solely for regulatory oversight purposes and not used or onward licensed or sold for any commercial purpose.

2.5. Life cycle approach

We note that the HKTR is adopting a life cycle approach to reporting and that other jurisdictions appear initially to be mandating snapshot reporting for the FX asset class. We believe that end of day reporting for all trades should be the appropriate initial step for capturing data for FX swaps. However, we would also suggest that given the importance of the data repository that an approach is not overly prescriptive and that the FX market develops the best approach over time.

2.6. Pairing and matching of trades

Given that trade matching occurs both through third party platforms and locally within banks (particularly for the foreign exchange market), pairing and matching of trades at the HKTR would seem to add unnecessary duplication of work flows. Trade repositories should pair data based on the provision of unique trade identifiers, with confirmation status being flagged as part of data reporting. We note the exception to this for trades submitted by both parties through the same confirmation and matching platform.

2.7. Backloading of outstanding trades

We agree with the proposal only to report trades that are unexpired as of a specified reference date and note that the paper suggests a grace period of three months within which to start backloading and a further month before the backloading cut off date allowing up to a total of four months to backload. However, we would ask that in order to allow parties to be able to report through an agent (in this case the global FX trade repository) that effort be taken to synchronise the reference date to allow backloading and reporting across both repositories.

2.8. Data submission formats, data templates and details to be reported

We welcome the use of FpML and CSV format reporting as this will provide flexibility for market participants to submit most standardised trades. However exotic trade reporting will require FpML templates to be developed and this will take some time. We therefore recommend that the industry be given time to develop these prior to setting the reference date for reporting those trades. Members are currently investigating this as part of the development work for the global FX trade repository.

As discussed above, we recommend that reporting to the HKTR be aligned with global standards for reporting and note the recent IOSCO-CPSS report on requirements for OTC derivatives data reporting and aggregation. Such alignment will facilitate connectivity between market participants and other market infrastructures including any global trade repositories. It will also make interrogation of data easier for the Hong Kong regulatory authorities should they need to link to multiple repositories.

2.9. HKTR system implementation timeline

As discussed, members of the GFXD have entered a scoping and development phase for a global trade repository for FX transactions. We would like to discuss with you the potential implementation timelines in order to allow third party reporting to the HKTR through the global trade repository. We believe this would be beneficial both for market participants and for the HKTR as it may in fact allow earlier reporting for trades envisaged for a later phase of work under the HK timeline.

2.10. Public reporting and block trades

We note from the FAQs that public disclosure of information would only be done on an aggregated basis and assume that care would be taken to ensure that no information is disclosed that would reveal the identity of any counterparties or that would allow position to be inferred from such data.

The FAQs comment that HKMA will refer to evolving local and international disclosure standards. Some international regulators are proposing that trade level pricing be publicly disseminated for market transparency purposes. Should the HKMA move forward in this manner, we would welcome the opportunity to comment on the appropriate mechanisms and delays that should be implemented for e.g. block trades as this will be critical for ensuring that liquidity is not damaged.

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We appreciate the opportunity to share our views on the HKMA's consultation paper. We would welcome the opportunity to discuss these in further detail with you and how to align the development of the global FX trade repository and the HKMA's trade repository. In the meantime, please do not hesitate to contact me at +44 (0) 207 743 9319 or at jkemp@gfma.org should you wish to discuss any of the above.

Yours sincerely,

James Kemp

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Global Foreign Exchange Division