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25 November 2011

By email: [baselcommittee@bis.org](mailto:baselcommittee@bis.org) & post

Secretariat of the Basel Committee on Banking Supervision  
Bank for International Settlements  
CH-4002 Basel  
Switzerland

Dear Sirs

**Consultation on Capitalisation of Bank Exposures to Central Counterparties**

We refer to the Consultative Document “Capitalisation of bank exposures to central counterparties” published by the Basel Committee on Banking Supervision (BCBS) in November 2011. On behalf of our members, we would like to set out our views on the Consultative Document as follows:

**General Comments**

We note the second consultative document has accepted some of our comments on the first consultation proposal published by BCBS in December 2010. We welcome the changes that clarify the required capital calculation rules on bank exposures to central counterparties (CCPs).

We are pleased to provide our further response to the revised consultative document. We believe further clarification of the final rules would be very helpful for the expeditious implementation of the new rules.

Our specific comments are as follows:

**1. Credit exposures**

In February 2011, we sought clarification on the calculation of credit exposures for each kind of exchange traded derivatives, exchange traded futures and options. In response, we note the newly revised rules have provided more guidelines on the product coverage, and the credit exposures for option products. For instance,

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- (i) Annex 6, Section II, 6(i) “exposures arising from the settlement of cash transactions (equities, fixed income, spot FX and spot commodities) are not subject to this treatment.”
- (ii) Para. 116(i), “The PFE calculation under the CEM for options and swaptions that are transacted through a CCP is adjusted by multiplying the notional amount of the contract by the absolute value of the option’s delta, which is calculated according to Annex 4 paragraph 77 and 78.”

However, it is still unclear as to how the monetary value of futures products is to be determined. Exchange traded warrants (e.g. Callable Bull / Bear Contracts traded in Hong Kong) are cash settled transactions and there is no counterparty credit risk from the exchanges. Should these products and other similar cash-settled exchange traded products be exempted from this credit risk capital requirement?

## 2. Determination of Qualifying CCPs

We continue to urge the BCBS to provide a list of qualifying CCPs and their respective supervisors, and to clarify whether local regulators have the discretion to modify this list.

As mentioned before, multiple CCPs from varying jurisdictions are often used for most of the banking portfolios in international financial centers, such as Hong Kong. The determination of whether a specific CCP is qualified as a “Qualifying CCP” for the purpose of capital calculation may not be a straight-forward exercise.

While we understand it is the clearing member’s responsibility to perform independent credit risk assessment to all of its counterparties, including CCPs, it is not cost-effective for individual clearing members to perform their individual qualifying CCP analysis for the same pools of CCPs, based on the same set of CCP rules. In particular the capital treatment on a ‘qualifying’ and ‘non-qualifying’ CCP can vary a lot, it is therefore essential that BCBS provide an ongoing list of frequently-used qualifying CCPs and non-qualifying CCPs to standardize and facilitate for such assessment.

If the determination of qualifying CCP is to be determined by each banking supervisor, the timeline for implementation by January 2013 could be challenging and the original intention to provide incentives for banks to use of qualifying CCPs may be undermined.

## 3. Reporting Frequency for CCP capital charge

The reporting frequency for the proposed CCP capital charge is not mentioned in the document. While we understand the reporting frequency is normally determined by local bank supervisors, the current practice in different jurisdictions requires

different reporting frequencies (e.g. quarterly for Hong Kong Monetary Authority (HKMA) but monthly for FSA).

Given the international nature of most of the banking portfolios in the World's financial centers, including Hong Kong, multiple CCPs from varying jurisdictions are often used. If a normally qualifying CCP would not provide the necessary data frequent enough for the calculation of default fund capital charge, it could be deemed as a non-qualifying CCP based on the newly proposed rule. Also, given the default fund capital charge can range from 0.16% to 120%, untimely data of CCP may potentially distort the capital charge calculation. It is therefore essential for BCBS to provide a clear reporting standard so that there is one standardized reporting frequency for all CCPs to comply with.

#### 4. **Applying Standardised Approach on Non-qualifying CCPs**

In para. 118, "Banks must apply the Standardised Approach for credit risk in the main framework, according to the category of the counterparty, to their trade exposure to a non-qualifying CCP."

Annex A in this consultative document proposes to revise para. 256 in Basel II as:

##### *"3. Adoption of the IRB approach across asset classes*

*256. Once a bank adopts an IRB approach for part of its holdings, it is expected to extend it across the entire banking group, **with the exception of the banking group's exposures to CCPs treated under Annex 4, Section IX.***

We would seek permission to use the IRB approach where appropriate to avoid ambiguity in Basel 2.5 implementation in Hong Kong where the HKMA disallows the application of non-IRB guarantors being recognized for credit risk mitigation to IRB credit risk exposures and vice versa.

#### 5. **Client Trades**

Paragraph 30 states that "When a client of a clearing member enters into a trade which is centrally cleared, it will be able to capitalise the exposures arising from such a trade under the proposed framework for CCPs only if certain segregation and continuity requirements are met."

Please provide more explanation on the segregation and continuity requirements.

#### 6. **Capital treatment for potentially 'unlimited' default contributions**

For some CCPs, the default contributions would not be a fixed amount. In the case a clearing member default, the remaining clearing members may be asked to increase

their default contribution.

How is the RWA/capital requirement calculated for such unlimited default contribution commitment?

**7. Risk weighting for qualifying CCPs**

Will there be any national discretion to deviate from the proposed 2% weighting? For exposures risk weighted at 2%, are they exempted from the IRB coverage calculation consistent with the exposures to non-qualifying CCPs?

**8. Exposures categorization of trade exposures**

Annex A provides as follows:

*« (iii) Client exposures*

*112. Where a bank is a client of a clearing member, and enters into a transaction with the clearing member acting as a financial intermediary (ie the clearing member completes an offsetting transaction with a CCP), the client's exposures to the clearing member may receive the treatment in paragraph 110 above if the following two conditions are met: "*

We would suggest the final rules state clearly the rules of exposure categorisation for the client's trade exposures to the clearing member acting as a financial intermediary, ie. Should this kind of exposures be categorized as "exposures to banks" or "exposures to CCP/corporate" for purposes of capital adequacy ratio reporting?

We hope you would find our above comments useful. If you have any questions or require any clarification, please do not hesitate to contact us.

Yours faithfully



Eva Wong  
Secretary

c.c. Ms. Karen Kemp, Executive Director (Banking Policy),  
Hong Kong Monetary Authority