

## COMMENT LETTER

December 22, 2014

# ICI Global Comment Letter to HK Authorities on Further Consultation on Reporting and Recordkeeping Obligations for OTC Derivative Transactions (pdf)

December 22, 2014 Via email Financial Stability Surveillance Division Hong Kong Monetary Authority 55/F Two International Finance Centre 8 Finance Street, Central Hong Kong Supervision of Markets Division The Securities and Futures Commission 35/F Cheung Kong Center 2 Queen's Road Central Hong Kong Dear Sir or Madam: ICI Global<sup>1</sup> appreciates the opportunity to provide comments on the further consultation issued by the Hong Kong Monetary Authority ("HKMA") and the Securities and Futures Commission ("SFC") on the mandatory reporting and related recordkeeping requirements for OTC derivatives.<sup>2</sup> The Consultation Paper includes a summary of comments received on the proposals for the mandatory reporting and related recordkeeping requirements for OTC derivatives,<sup>3</sup> the HKMA and the SFC's responses to those comments, their conclusions, and a request for further comment on three particular matters. In this letter, ICI Global addresses one of the matters raised by the HKMA and the SFC for further consultation – the proposal to define products traded on US swap execution facilities ("SEFs")

<sup>1</sup> The international arm of the Investment Company Institute, ICI Global serves a fund membership that includes regulated funds publicly offered to investors in jurisdictions worldwide, with combined assets of US\$18.9 trillion. ICI Global seeks to advance the common interests and promote public understanding of regulated investment funds, their managers, and investors. Its policy agenda focuses on issues of significance to funds in the areas of financial stability, cross-border regulation, market structure, and pension provision. ICI Global has offices in London, Hong Kong, and Washington, DC.

<sup>2</sup> Consultation Conclusions and Further Consultation on the Securities and Futures (OTC Derivative Transactions – Reporting and Record Keeping Obligations) Rules (November 2014), available at <http://www.sfc.hk/edistributionWeb/gateway/EN/consultation/conclusion?refNo=14CP6> ("Consultation Paper").

<sup>3</sup> Consultation Paper on the Securities and Futures (OTC Derivative Transactions – Reporting and Record Keeping) Rules (July 2014), available at <http://www.sfc.hk/edistributionWeb/gateway/EN/consultation/openFile?refNo=14CP6> ("Original Consultation").

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and EU multilateral trading facilities ("MTFs") as "OTC derivatives," which would subject these products to the Hong Kong ("HK") reporting and recordkeeping rules. Our members – US funds that are regulated under the Investment Company Act of 1940 ("ICA") and similar

non-US regulated funds publicly offered to investors, such as UCITS (collectively, "Regulated Funds") – use derivatives in a variety of ways. Derivatives are a useful portfolio management tool in that they offer Regulated Funds flexibility in structuring their investment portfolios. Uses of derivatives include, for example, hedging positions, equitizing cash that a Regulated Fund cannot immediately invest in direct equity holdings, managing a Regulated Fund's cash positions more generally, adjusting the duration of a Regulated Fund's portfolio, or managing a Regulated Fund's portfolio in accordance with the investment objectives stated in a Regulated Fund's prospectus. To employ derivatives in the best interests of fund investors, our members strongly support ensuring that the derivatives markets are highly competitive and transparent. ICI Global members, as market participants representing millions of investors, generally support the goal of providing greater oversight of the derivatives markets. As an initial matter, we applaud the HKMA and the SFC for recognizing the concerns expressed in our comment letter on the Original Consultation. In particular, we support the HKMA and the SFC's determination not to require, in the first phase of the implementation, authorized institutions ("AIs") and licensed corporations ("LCs") to report OTC derivative transactions that they have entered into on behalf of a counterparty in their capacity as a person registered/licensed to carry on Type 9 RA (asset management) services for that counterparty. We agree that the HKMA and the SFC should take the time necessary to address the difficulties for these entities to report and will provide further feedback when the HKMA and the SFC consult on these issues at a later stage. In addition, we appreciate the clarification provided by the HKMA and the SFC with respect to the requirement to report transactions "conducted in Hong Kong." As noted by the HKMA and the SFC in the Consultation Paper, the "reporting requirement in respect of transactions 'conducted in Hong Kong' is not aimed at catching fund managers." We understand that asset managers would be subject to the reporting requirements only as AIs and LCs in their capacity to carry on Type 9 services. In the Consultation Paper, the HKMA and the SFC request further comment on three specific matters. In this letter, we are providing our views with respect to the definition of "OTC derivatives" and whether products traded on US SEFs or EU MTFs should be included within the definition. We believe that US SEFs should be included in the list of markets based outside of Hong Kong for which products traded on these markets would be excluded from the definition of "OTC derivative." As the HKMA and the SFC are fully aware, a majority of derivatives transactions are conducted on a cross-border basis, and many Regulated Funds may be trading (or are required to trade)<sup>4</sup> certain derivatives. Section 2(h)(8) of the Commodity Exchange Act ("CEA") mandates that a swap that is cleared on a derivatives clearing organization be traded on a board of trade designated as a designated contract market ("DCM") or SEF unless no DCM or SEF makes a swap available to trade or the swap is subject to a clearing exemption. In other words, once a swap is subject to the trading requirement, bilateral trading of such a swap is prohibited. Similarly, the EU Markets in Financial Instruments Regulation ("MiFIR") Article 24 mandates that derivatives that are subject to a clearing obligation be traded on a trading venue. ICI Global Letter to HKMA and SFC December 22, 2014 Page 3 of 6 on SEFs. We do not believe that these types of transactions should be included in the definition of "OTC derivatives" and be subject to the HK reporting requirements for the reasons discussed below. SEFs Satisfy the Criteria Set Forth by HKMA and SFC In the Consultation Paper, the HKMA and the SFC state that only stock/futures markets and clearinghouses that meet certain criteria should be included on the proposed list. The criteria are as follows: (1) the markets operate in jurisdictions whose securities or futures regulator is a member of the International Organization of Securities Commissions ("IOSCO"); (2) the markets are regulated in their home jurisdictions and their regulatory status is comparable to that of a recognized exchange company or recognized clearinghouse under the Securities and Futures Ordinance; and (3) the markets are

regulated by the relevant market regulator, banking regulator or government agency in that jurisdiction. We believe SEFs satisfy all of these top-level criteria. In particular, we note that (1) the Commodity Futures Trading Commission ("CFTC"), the US regulator of SEFs, is a member of IOSCO; (2) SEFs are regulated in the United States, must complete a CFTC registration process, and, as discussed in further detail below, possess a regulatory status that is comparable to a recognized exchange company or recognized clearinghouse under the Securities and Futures Ordinance; and (3) SEFs have been required to register with and to comply with CFTC regulations since October 2013. With respect to a SEF's regulatory status, similar to requirements imposed on The Stock Exchange of Hong Kong Limited under the Securities and Futures Ordinance, SEFs are under a duty to ensure an orderly, informed and fair market in securities/derivatives contracts that are traded on it or through its facilities and to ensure that risks associated with its business and operations are managed prudently.<sup>5</sup> As with a recognized exchange company,<sup>6</sup> a SEF, in discharging its duties, must minimize conflicts of interest in its decision-making process. In addition, as required for recognized exchange companies,<sup>7</sup> each SEF is required (A) to formulate and implement appropriate procedures for ensuring that its participants comply with the rules of the facility; and (B) to provide and maintain, at all times, for the conduct of its business (i) adequate and properly equipped premises, (ii) competent personnel, and (iii) automated systems with adequate capacity, facilities to meet contingencies or emergencies, security arrangements, and technical support. A more comprehensive comparison of regulations applicable to Hong Kong recognized exchange companies and to SEFs is included as Appendix A to this letter. <sup>5</sup> Hong Kong Securities and Futures Ordinance, Section 21(1). <sup>6</sup> Hong Kong Securities and Futures Ordinance, Section 21(2). <sup>7</sup> Hong Kong Securities and Futures Ordinance, Section 21(4) and (6). ICI Global Letter to HKMA and SFC December 22, 2014 Page 4 of 6 SEFs Should Be Treated Similarly to DCMs for Purposes of HK Rules In the Consultation Paper, the HKMA and the SFC take the view that DCMs regulated by the CFTC should be included in the list of markets and that the products traded on DCMs would not be considered "OTC derivatives." We agree and believe that products that are traded on SEFs should be provided the same treatment because the regulation of SEFs by the CFTC is comparable to the regulation of DCMs. SEFs and DCMs share many similarities and provide functions that are comparable to traditional exchanges. The CFTC has noted that SEFs and DCMs are intended to provide market participants with "the prices of available bids and offers" and "transparent and competitive trading systems or platforms."<sup>8</sup> Any platform that offers market participants the ability to execute or trade swaps with more than one other market participant on the platform must register as either a SEF or DCM.<sup>9</sup> SEFs must register with the CFTC on Form SEF and, following approval, are subject to substantive regulation by the CFTC. By definition, a SEF must give multiple participants the ability to accept bids or offers made by multiple potential counterparties on the platform, which sets them apart from bilateral OTC transactions. Similar to DCMs, SEFs are required to operate pursuant to statutory "Core Principles" a majority of which are similar in purpose to the Core Principles of DCMs. SEFs must comply with 15 Core Principles as a condition of registration.<sup>10</sup> Similar to DCMs, Core Principle 2, among other things, requires a SEF to: (1) establish and enforce compliance with its rules; (2) establish and enforce trading, trade processing, and participation rules to deter abuses; and (3) have the capacity to detect, investigate, and enforce those rules (in this respect, a SEF is similar to a traditional exchange in that it acts as a self-regulatory organization). Similar to DCMs, SEFs are required by Core Principles 3 and 4 to permit trading only in swaps that are not readily susceptible to manipulation and to establish and enforce rules for trading procedures and trade processing that monitor for market manipulation. Both DCMs and SEFs must adopt position limits as necessary to prevent manipulation or congestion (as required by SEF Core Principle 6). Core Principle 9 requires a SEF to make public timely information on price,

trading volume, and other trading data on swaps to the extent prescribed by the CFTC and requires that the SEF have the capacity to capture and transmit electronically trade information with respect to transactions executed on the facility. The CFTC rules specify that SEFs must report swap data, and both the requirements for real-time reporting to the public and regulatory reporting to the CFTC for SEFs are identical to the corresponding requirements imposed on DCMs. 8 CFTC, Core Principles and Other Requirements for Swap Execution Facilities, 78 FR 33477 ( June 4, 2013) at 5-6. 9 17 CFR 37.3. 10 The Core Principles are: (1) Compliance with Core Principles; (2) Compliance with Rules; (3) Swaps Not Readily Susceptible to Manipulation; (4) Monitoring of Trading and Trade Processing; (5) Ability to Obtain Information; (6) Position Limits or Accountability; (7) Financial Integrity of Transactions; (8) Emergency Authority; (9) Timely Publication of Trading Information; (10) Recordkeeping and Reporting; (11) Antitrust Considerations; (12) Conflicts of Interest; (13) Financial Resources; (14) System Safeguards; and (15) Designation of Chief Compliance Officer. ICI Global Letter to HKMA and SFC December 22, 2014 Page 5 of 6 Products Traded on SEFs Should not be Subject to HK OTC Derivatives Regime The HKMA and the SFC state that markets included in the list are subject to regulation under the laws of their home jurisdiction and that it is therefore unnecessary for products traded and cleared through them to be subject to the HK derivatives regime as well. In particular, the HKMA and the SFC expect these markets to provide a higher level of transparency than OTC markets, including both pre-trade transparency on quotes and orders for transaction as well as post-trade transparency on completed transactions through public and regulatory reporting. We believe this higher level of transparency is provided by SEFs. US SEFs are subject to regulation by the CFTC (as discussed above) and provide a level of transparency that would make it unnecessary for the products traded through them to be subject to the HK derivatives regime. Currently, most transactions on SEFs are executed through request-for-quote ("RFQ") systems. Under a RFQ system, a market participant must send out a request for a quote to at least three other market participants.<sup>11</sup> A market participant could typically execute using any of the quotes obtained. As with DCMs, SEFs also must provide pre-trade transparency through "order book" capability: prior to execution of a transaction, a SEF must furnish a market participant with all executable bids or offers for the same instrument. The market participant would then be permitted to execute against any of those bids or offers, if desired. Although pre-trade transparency is limited to market participants, SEFs are required to provide access to any eligible participant (this requirement applies both to entities with trading rights and/or access to data).<sup>12</sup> As a result, any transaction executed on a SEF would be more transparent than a traditional OTC transaction that is transparent only to the two executing parties and at least as transparent as a DCM.<sup>13</sup> SEF Core Principal 9 requires timely publication of trading information, including price, trading volume and other trading data as prescribed by the CFTC.<sup>14</sup> The CFTC intends that such data be disseminated to the public in "real time."<sup>15</sup> The data required for both public dissemination and regulatory reporting to the CFTC (specified by parts 43 and 45 of the CFTC regulations, respectively) are the same as the data specified for DCMs. Publicly available data includes the execution timestamp, start date, end date, underlying asset(s), price notation, rounded notional amount, payment frequency, reset frequency, details regarding whether the transaction is customized, and collateralization details. <sup>11</sup> This requirement may be reduced to two other market participants during an initial implementation stage. <sup>12</sup> 17 CFR 37.202(a): "A swap execution facility shall provide any eligible contract participant and independent software vendor with impartial access to its market(s) and market services, including any indicative quote screens or any similar pricing data displays [....]" <sup>13</sup> As noted above, although orders on SEFs are typically executed through RFQ systems, SEFs also must provide order book transparency, even if participants do not execute using the order book capability. <sup>14</sup> 17 CFR 37.900. As noted

above, both DCMs and SEFs are subject to similar post-transaction transparency requirements. 15 CEA Section 2(a)(13(A) defines “real-time public reporting” as reporting of “data relating to a swap transaction, including price and volume, as soon as technologically practical after the time at which the swap transaction has been executed.” ICI Global Letter to HKMA and SFC December 22, 2014 Page 6 of 6 HKMA and SFC Should Carefully Review EU Rules Being Developed for MTFs Under the Markets in Financial Instruments Directive (“MiFID”), a MTF is a multilateral system operated by an investment firm or market operator that brings together multiple third-party buying and selling interests in financial instruments in the system, in accordance with non-discretionary rules, in a way that results in a contract.<sup>16</sup> It is expected that the European Union (“EU”) will adopt rules shortly with respect to execution on MTFs that may be comparable to US regulation of SEFs. The definition of MTFs is similar to the CFTC definition of SEFs, and the CFTC has issued conditional “no-action” letters recognizing the comparability of qualifying MTFs to SEFs.<sup>17</sup> When the EU adopts final rules governing MTFs, we urge the HKMA and the SFC to consider carefully whether MTFs also should be included in the list so that products traded on MTFs will not be considered “OTC derivatives.” \* \* \* We appreciate the opportunity to provide further comments on the proposed reporting rules for OTC derivatives. We urge the HKMA and the SFC to include US SEFs in the list of markets so that products traded on those markets would not be considered “OTC derivatives.” If you have any questions on our comment letter, please feel free to contact the undersigned, Susan Olson at +1-202-326-5813, Sarah Bessin at +1-202-326-5835, or Jennifer Choi at +1-202-326-5876.

Sincerely, /s/ Dan Waters Dan Waters Managing Director ICI Global +44-203-009-3101 16 MiFID I Directive, Article 4(15). 17 “Conditional No-Action Relief with respect to Swaps Trading on Certain Multilateral Trading Facilities Overseen by Competent Authorities Designated by European Union Member States,” CFTC No-Action Letter No. 14-46 (April 9, 2014).

#### APPENDIX COMPARISON OF SFO REQUIREMENTS APPLICABLE TO A RECOGNIZED EXCHANGE COMPANY AND CFTC REQUIREMENTS APPLICABLE TO SWAP EXECUTION FACILITIES

Securities and Futures Ordinance CFTC Regulations – 17 CFR Part 37 (Swap Execution Facilities) Section 21(1) It shall be the duty of a recognized exchange company to ensure-

- (a) so far as reasonably practicable, an orderly, informed and fair market-
- (i) in the case of a recognized exchange company which operates a stock market, in securities that are traded on that stock market or through the facilities of that company; or
- (ii) in the case of a recognized exchange company which operates a futures market, in futures contracts that are traded on that futures market or through the facilities of that company; and

To be registered and maintain registration as a swap execution facility, a SEF must comply with various rules aimed at maintaining an orderly, informed and fair market, including the core principles contained in the Commodity Exchange Act of 1936, as amended (the “Act”) (e.g., Core Principle 1, Section 37.1000).

- (1) A SEF must create an orderly market through “establish[ing] and enforce[ing] compliance with any rule of the swap execution facility, including the terms and conditions of the swaps traded or processed on or through the swap execution facility and any limitation on access to the swap execution facility.” (Core Principle 2). In particular, the SEF must enforce compliance of rules with respect to: -the terms and conditions of the swaps on the SEF; -access to the SEF; -trade practice rules; -audit trail requirement; and -disciplinary rules (Section 37.201)
- (2) A SEF must establish an informed market. A SEF is subject to several substantive requirements with respect to transparency. At a minimum, a SEF must establish a system through which all market participants have “the ability to enter multiple bids and offers, observe or receive bids and offers entered by other market participants, and transact on such bids and offers.” (Section 37.3(a))
- (3) SEFs are subject to various requirements with respect to maintaining a fair market: -Access must be fair: access to the market must be granted impartially to all qualified participants; criteria governing access must be “impartial, transparent, and

applied in a fair and nondiscriminatory manner;" (Section 37.202) -Trading must be fair: prohibitions include inter alia trading ahead of customer orders, trading against customer orders, improper cross trading, front- running, wash trading, pre-arranged trading (other than certain block trades), fraudulent trading, as well as any other manipulative or disruptive trading practices prohibited by the Act. (Section 37.203(a)) -Fairness Must Be Enforced: a SEF must make arrangements and resources for effective enforcement of rules, including sufficient compliance staff and resources. (Section 37.203(b)-(c)) (b) that risks associated with its business and operations are managed prudently. A SEF must "establish and maintain a program of risk analysis and oversight to identify and minimize sources of operational risk, through the development of appropriate controls and procedures, and automated systems." This includes emergency procedures, backup facilities, and disaster recovery. (Core Principle 14, Section 37.1400) A SEF must establish certain systems to monitor market-related risks, including an automated trade surveillance system and real-time market monitoring. (Section 37.203(d)-(e)) In addition, a SEF must establish and maintain risk control mechanisms to prevent and reduce the potential risks of market disruptions. (Section 37.405) A SEF is further required to have "adequate financial, operational, and managerial resources to 3 discharge each responsibility" that it has. (Core Principle 13, Section 37.1300) Section 21(2) In discharging its duty under subsection (1), a recognized exchange company shall- (a) act in the interest of the public, having particular regard to the interest of the investing public; and (b) ensure that the interest of the public prevails where it conflicts with the interest of the recognized exchange company. Section 37.1200 Core Principle 12 – Conflicts of interest The swap execution facility shall: (a) Establish and enforce rules to minimize conflicts of interest in its decision-making process; and (b) Establish a process for resolving the conflicts of interest. A SEF must designate a "chief compliance officer" (Core Principle 15, Section 37.1500). The chief compliance officer's duties include resolution of conflicts that arise between business considerations and compliance requirements, as well as conflicts between business considerations and the requirement that the SEF provide fair, open and impartial access. The chief compliance officer must also take reasonable steps to ensure compliance with the Act and promote compliance with a code of ethics designed to prevent ethical violations and to promote honesty and ethical conduct. (Section 37.1501(d)) Section 21(3) A recognized exchange company shall operate its facilities in accordance with the rules made under section 23 and approved under section 24. SEFs are subject to CFTC regulations and required to comply with the substantive rules contained in Part 37 of the CFTC's rules as well as other CFTC regulation and the Act generally. Section 21(4) A recognized exchange company shall formulate and implement appropriate procedures for ensuring that A SEF must have a "rule enforcement program" coupled with the capacity to detect and investigate rule violations, compliance staff and resources, and sufficient enforcement staff and resources to effectively and promptly prosecute possible rule 4 its exchange participants comply with the rules of the company. violations. (Section 37.203(a)-(c); Section 37.206(a)) Section 21(5) A recognized exchange company shall immediately notify the Commission if it becomes aware- (a) that any of its exchange participants is unable to comply with any rules of the company or any financial resources rules; or (b) of a financial irregularity or other matter which in the opinion of the company may indicate that the financial standing or integrity of an exchange participant is in question, or that an exchange participant may not be able to meet his legal obligations. SEFs are subject to rules requiring that all participants meet certain minimum financial standards, including qualification as "eligible contract participants" (Section 37.702). SEFs must monitor the financial soundness of participants on an ongoing basis. (Section 37.703) Section 21(6) A recognized exchange company shall at all times, for the conduct of its business, provide and maintain- (a) adequate and properly equipped premises; SEFs are required to maintain an adequate infrastructure,

included automated trade surveillance systems (Section 37.203(d)), adequate operational resources (Section 37.1300(a)), and infrastructure and personnel resources of their own sufficient to meet various regulatory purposes. (Section 37.1401(c)) (b) competent personnel; and The credentials of a SEF's professional employees must be submitted to the CFTC for review as part of the SEF's registration process. (Form SEF, Exhibit E). SEFs are required to maintain sufficient compliance staff to ensure compliance with various rules (Section 37.203(c)), sufficient enforcement staff to effectively and promptly prosecute possible rule violations (Section 37.206(a)) and a chief compliance officer overseeing their conduct. (Section 37.1500) 5 (c) automated systems with adequate capacity, facilities to meet contingencies or emergencies, security arrangements and technical support. The SEF must have a program of risk analysis and oversight to identify and minimize sources of operational risk through the development of appropriate controls and procedures and automated systems. These systems must be reliable and secure, have adequate scalable capacity, and establish and maintain emergency procedures, backup facilities, and a plan for disaster recovery. (Section 37.1400) Section 23(1) Without limiting any of its other powers to make rules, a recognized exchange company may make rules for such matters as are necessary or desirable- (a) for the proper regulation and efficient operation of the market which it operates; (b) for the proper regulation of its exchange participants and holders of trading rights; (c) for the establishment and maintenance of compensation arrangements for the investing public. Section 37.200 Core Principle 2 – Compliance with rules A swap execution facility shall: (a) Establish and enforce compliance with any rule of the swap execution facility, including the terms and conditions of the swaps traded or processed on or through the swap execution facility and any limitation on access to the swap execution facility; (b) Establish and enforce trading, trade processing, and participation rules that will deter abuses and have the capacity to detect, investigate, and enforce those rules, including means to provide market participants with impartial access to the market and to capture information that may be used in establishing whether rule violations have occurred; (c) Establish rules governing the operation of the facility, including rules specifying trading procedures to be used in entering and executing orders traded or posted on the facility, including block trades; and (d) Provide by its rules that when a swap dealer or major swap participant enters into or facilitates a swap that is subject to the mandatory clearing requirement of section 2(h) of the Act, the swap dealer or major swap participant shall be responsible for compliance with the mandatory trading requirement under section 2(h)(8) of the Act. Section 37.203 Rule enforcement program A swap execution facility shall establish and enforce trading, trade processing, and participation rules 6 that will deter abuses and it shall have the capacity to detect, investigate, and enforce those rules. (a) Abusive trading practices prohibited. A swap execution facility shall prohibit abusive trading practices on its markets by members and market participants. Swap execution facilities that permit intermediation shall prohibit customer-related abuses including, but not limited to, trading ahead of customer orders, trading against customer orders, accommodation trading, and improper cross trading. Specific trading practices that shall be prohibited include front-running, wash trading, pre-arranged trading (except for block trades permitted by part 43 of CFTC regulations or other types of transactions certified to or approved by the Commission pursuant to the procedures under part 40 of CFTC regulations), fraudulent trading, money passes, and any other trading practices that a swap execution facility deems to be abusive. A swap execution facility shall also prohibit any other manipulative or disruptive trading practices prohibited by the Act or by the CFTC pursuant to CFTC regulation. (b) Capacity to detect and investigate rule violations. A swap execution facility shall have arrangements and resources for effective enforcement of its rules. Such arrangements shall include the authority to collect information and documents on both a routine and non-routine basis,

including the authority to examine books and records kept by the swap execution facility's members and by persons under investigation. A swap execution facility's arrangements and resources shall also facilitate the direct supervision of the market and the analysis of data collected to determine whether a rule violation has occurred. Section 23(2) Without limiting the generality of subsection (1), a recognized exchange company which may operate a stock market may make rules for-

Section 37.201 Operation of swap execution facility and compliance with rules (a) A swap execution facility shall establish rules governing the operation of the swap execution facility, including, but not limited to, rules specifying trading procedures to be followed by

7 (a) applications for the listing of securities and the requirements to be met before securities may be listed; (b) the entering into of agreements between the recognized exchange company and other persons in connection with the listing of securities, and the enforcement of those agreements by the company; (c) the cancellation and withdrawal of the listing of, and the suspension and resumption of dealings in, securities listed on the recognized stock market operated by the recognized exchange company; (d) the imposition on any person of obligations to observe specified standards of conduct or to perform, or refrain from performing, specified acts reasonably imposed in connection with the listing or continued listing of securities; (e) the admission of securities which are regulated in a jurisdiction outside Hong Kong to trading on a recognized stock market operated by the recognized exchange company; (f ) the penalties or sanctions which may be imposed by the recognized exchange company for a breach of rules made under this section; (g) procedures or conditions which may be imposed, or circumstances which are required to exist, in relation to matters which are provided for in the rules made under this section; (h) dealing with possible conflicts of interest that might arise where a relevant corporation or a relevant recognized exchange controller seeks to be or is a listed corporation; (i) such other matters as are necessary or desirable for the proper and efficient operation and management of the recognized exchange company.

members and market participants when entering and executing orders traded or posted on the swap execution facility, including block trades, as defined in part 43 of CFTC regulations, if offered. (b) A swap execution facility shall establish and impartially enforce compliance with the rules of the swap execution facility, including, but not limited to -

(1) The terms and conditions of any swaps traded or processed on or through the swap execution facility; (2) Access to the swap execution facility; (3) Trade practice rules; (4) Audit trail requirements; (5) Disciplinary rules; and (6) Mandatory trading requirements.

Section 37.1200 Core Principle 12 - Conflicts of interest The swap execution facility shall: (a) Establish and enforce rules to minimize conflicts of interest in its decisionmaking process; and (b) Establish a process for resolving the conflicts of interest.

Section 23(3) A SEF is required to implement any applicable CFTC regulations. (Section 37.2) 8 The Commission may, by notice in writing served on a recognized exchange company, request the company-

(a) to make rules specified in the request within the period specified in that request; or (b) to amend rules referred to in the request in the manner and within the period specified in that request.

Section 23(4) Before making a request under subsection (3), the Commission shall consult the Financial Secretary and the recognized exchange company to which the request relates. N/A

Section 23(5) Where the Commission is satisfied that a recognized exchange company has not complied with a request referred to in subsection (3) within the period specified in the request, the Commission may make or amend the rules specified in the request instead of the company. The CFTC has direct authority to make regulations that are binding on a SEF.

Section 23 (6) The following persons or anyone who seeks to become any such person shall, if required to do so by the rules of a recognized exchange company, make a statutory declaration concerning such matters as may be specified in the rules-

(a) an exchange participant or holder of trading rights of the company; (b) a director of a corporation which uses the facilities of the company; (c) a director of a corporation which is



seeking to have any of its securities listed; and (d) a director or adviser of a listed corporation. SEF members must provide the equivalent of a declaration regarding their eligibility to be a member of the SEF. (Section 37.202). Section 24(1) A SEF and its various policies, procedures and operating manuals are subject to review and 9 Subject to subsection (7), no rule (whether or not made under section 23) of a recognized exchange company or any amendment thereto shall have effect unless it has the approval in writing of the Commission. approval by the CFTC. The SEF must furnish to the CFTC such information in Form SEF. In Form SEF, a SEF is required to submit various exhibits containing references to and copies of its rules associated with compliance with all core principles, as well as technical manuals, guides or instructions. (e.g., Form SEF, Exhibits L and M) A swap execution facility shall submit a swap's terms and conditions, including amendments to such terms and conditions, new rules, or rule amendments pursuant to procedures under CFTC regulation. (Section 37.4) The CFTC retains the ability to require compliance with any rules that it promulgates. (Section 37.2) Section 24(2) - (7) (2) A recognized exchange company shall submit or cause to be submitted to the Commission- (a) for its approval the rules and every amendment thereto that require approval under subsection (1), together with explanations of their purpose and likely effect, including their effect on the investing public, in sufficient detail to enable the Commission to decide whether to approve them or refuse to approve them; and (b) for its information the rules which belong to a class the subject of a declaration under subsection (7) and every amendment to the rules, as soon as reasonably practicable after they have been made. (3) The Commission shall, not later than 6 weeks after the receipt of a submission under subsection (2)(a) from a recognized exchange company, by notice in writing served on the company, give its approval or refuse to give its approval (together with its reasons for the refusal) to the rules or amendment of the rules (as the case may be) or any part thereof, the subject of the submission. (4) The Commission may give its approval under subsection (3) subject to requirements which shall A SEF is required to submit an exhibit containing references to its rules associated with compliance with all core principles, as well as technical manuals, guides or instructions. (Form SEF, Exhibits L and M) Where amendments are necessary to a SEF's order of registration, the SEF must submit an amended Form SEF. With respect to specific terms of swaps traded on a SEF, Section 37.4 (Procedures for listing products and implementing rules) will apply. (a) An applicant for registration as a swap execution facility may submit a swap's terms and conditions prior to listing the product as part of its application for registration. (b) Any swap terms and conditions or rules submitted as part of a swap execution facility's application for registration shall be considered for approval by the Commission at the time the Commission issues the swap execution facility's order of registration. (c) After the Commission issues the order of registration, a swap execution facility shall submit a swap's terms and conditions, including amendments 10 be satisfied before the rules or amendment of the rules or any part thereof take effect. (5) The Commission may in a particular case, with the agreement of the recognized exchange company concerned, extend the time prescribed in subsection (3). (6) The Financial Secretary may, after consultation with the Commission and the recognized exchange company concerned, extend the time prescribed in subsection (3). (7) The Commission may, by notice published in the Gazette, declare any class of rules of a recognized exchange company to be a class of rules which are not required to be approved under subsection (1) and, accordingly, any rules of the company which belong to that class (including any amendment thereto) shall have effect notwithstanding that they have not been so approved. to such terms and conditions, new rules, or rule amendments pursuant to the procedures under part 40 of CFTC regulations.

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