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Near Final Hong Kong Rules on Margin and Risk Mitigation Standards for Non-Centrally Cleared OTC Derivatives

Introduction

On 6 December 2016, the Hong Kong Monetary Authority (the "**HKMA**") published to the industry the near final version of the draft module in the HKMA Supervisory Policy Manual on margin and risk mitigation standards for non-centrally cleared OTC derivatives (the "**SPM Margin Module**"), together with the HKMA's response to comments from the various industry bodies on the HKMA consultation response from 22 August 2016[1]. The HKMA announced the implementation timeline for initial margin ("**IM**") and variation margin ("**VM**") requirements in Hong Kong. On the same day, the Australian Prudential Regulation Authority ("**APRA**") and the Monetary Authority of Singapore ("**MAS**") also announced to the market the implementation timelines for margin requirements for non-centrally cleared derivatives in Australia and Singapore; final margin rules were released by APRA and MAS on that day.

The three Asian regulators have aligned the implementation timelines in their respective jurisdiction with each other: margin requirements will commence in all three jurisdictions on 1 March 2017, with a six months' transition period provided in Hong Kong and Singapore for IM and VM and in Australia for VM.

With margin requirements commencing shortly on 1 March 2017, we have included a quick summary at the back of this Bulletin on the Hong Kong VM provisions[2] for your ease of reference.

Contents

[1] See our client bulletin HKMA Responses to the Consultation on Proposed Margin and Risk Mitigation Standards for Non-Centrally Cleared OTC Derivatives for our discussion on the August 2016 HKMA consultation response and our client bulletin Hong Kong Proposes Margin and Risk Mitigation Standards for Non-Centrally Cleared OTC Derivatives for our discussion on the December 2015 HKMA consultation paper.

[2] It is expected that IM requirements will practically only come into effect a few years later for AIs given the size of the IM thresholds.

Near final Hong Kong margin rules – points to note

We highlight in this Bulletin the major deviations and clarifications that we see in the near final version of the SPM Margin Module from the position set out in the HKMA's August consultation response.

In-scope entities and covered entities

Margin requirements will apply to both Hong Kong incorporated AIs (irrespective of where the trades are booked) and overseas incorporated AIs (with respect to trades booked in its Hong Kong branch only) when they enter into in-scope non-centrally cleared derivatives with a covered entity. "Covered entities" are "financial counterparties"[3] and "significant non-financial counterparties"[4] which are not excluded entities[5].

Financial counterparties

Threshold: The HKMA has made a significant change to the scope of the covered entities by introducing a HK$ 15 billion threshold for "financial counterparties". An entity that belongs to one of the types of financial counterparties will be a covered entity if it has (either on an individual or a group basis) an average aggregate notional amount ("**AANA**") of non-centrally cleared derivatives exceeding HK$ 15 billion. This will be determined for a one year period from 1 September each year to 31 August of the following year by reference to the average of the total gross notional amount of month-end positions of non-centrally cleared derivatives for March, April and May preceding the 1 September starting date in the relevant year. The

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[3] "Financial counterparties" refers to an entity for a one-year period from 1 September each year to 31 August of the following year, if the entity itself or the group to which it belongs has an average aggregate notional amount of non-centrally cleared derivatives exceeding HK$ 15 billion and means:

(i) an AI;
(ii) a Type 1, 2, 3, 4, 5, 6, 8, 9, 11 or 12 licensed corporation;
(iii) a Hong Kong-registered mandatory provident fund scheme;
(iv) a Hong Kong-registered occupational retirement scheme;
(v) a Hong Kong-authorised insurer;
(vi) a Hong Kong-licensed remittance agent or money changer;
(vii) a Hong Kong-licensed money lender;
(viii) a securitisation special purpose entity as defined in the Banking (Capital) Rules ("**BCR**") (unless the special purpose entity enters into derivatives for the sole purpose of hedging);
(ix) a collective investment scheme;
(x) a private equity fund; and
(xi) an entity that carries on a business outside Hong Kong and is engaged predominantly in any one or more of the following activities: (1) banking, (2) securities business, (3) management of retirement fund schemes, (4) insurance business, (5) operation of a remittance or money changing service, (6) lending, (7) securitisation (unless the related special purpose entity enters into derivatives for the sole purpose of hedging), (8) portfolio management and (9) activities that are ancillary to the conduct of these activities.

[4] "Significant non-financial counterparties" are entities other than financial counterparties which have (either on an individual or a group basis) an average aggregate notional amount of non-centrally cleared derivatives exceeding HK$ 60 billion. Whether an entity is a significant non-financial counterparty is determined for a one year period from 1 September to 31 August of the following year by reference to the average of the total gross notional amount of month-end positions of non-centrally cleared derivatives for March, April and May preceding the 1 September starting date in a relevant year.

[5] Excluded entities are: sovereigns, central banks, public sector entities, multilateral development banks and the Bank for International Settlements.

HK$ 15 billion threshold will be useful for smaller financial counterparties (such as funds) with less significant activities in non-centrally cleared derivatives by excluding such entities from the entity scope.

The types of entities which fall under the definition of "financial counterparties" have changed slightly in the SPM Margin Module:

Special purpose entities (SPEs): In the August consultation response, the HKMA indicated that they are willing to exclude traditional securitisation SPEs (but not synthetic securitisation SPEs) from the definition of "financial counterparty", provided that the SPE enters into the derivative transactions for the sole purpose of hedging. The HKMA has now excluded both traditional and synthetic securitisation SPEs from the definition of financial counterparty, but only if the SPE enters into non-centrally cleared derivatives for the sole purpose of hedging.

Overseas financial entities: Previously, one of the limbs in the definition of financial counterparties referred to entities carrying on business outside Hong Kong that would require licensing under one of the enumerated categories of Hong Kong regulated entities[6] if it were carrying on business in Hong Kong. Taking into account industry comments on the difficulty with applying Hong Kong authorisation, licensing and registration requirements to overseas entities, the HKMA has revised the definition to refer to the following list of activities undertaken by an overseas financial entity:

> Banking;

> Securities business;

> Management of retirement fund schemes;

> Insurance business;

> Operation of a remittance or money changing service;

> Lending;

> Securitisation (except where and to the extent that the related special purpose entity enters into non-centrally cleared derivative transactions for the sole purpose of hedging);

> Portfolio management (including asset management and funds management); and

> Activities that are ancillary to the conduct of these activities.

Overseas financial entities:

The list of activities set out in the revised definition is broad-brushed and do not necessarily correspond to the activities performed by the enumerated categories of Hong Kong regulated entities in the previous draft. An example is the activity of "management of retirement fund schemes": it appears to catch overseas pension fund managers although the corresponding Hong Kong regulated entities are the Hong Kong-registered mandatory provident schemes and occupational retirement schemes (i.e. the pension funds themselves). The activity of "lending" also appears to be very broad and it is unclear if one should look to the corresponding Hong Kong ordinance (the Money Lenders Ordinance) to ascertain the scope of the activity.

[6] These were:
(i) AIs;
(ii) Type 1, 2, 3, 4, 5, 6, 8, 9, 11 or 12 licensed corporations;
(iii) Hong Kong-registered mandatory provident fund schemes;
(iv) Hong Kong-registered occupational retirement schemes;
(v) Hong Kong-authorised insurers;
(vi) Hong Kong-licensed remittance agents or money changers; and
(vii) Hong Kong-licensed money lenders.

An overseas financial entity which carries on a business outside Hong Kong and is engaged predominantly in any one or more of the above activities will, subject to the crossing of the HK$ 15 billion threshold as described above, will be a financial counterparty for the purpose of the SPM Margin Module.

Significant Non-Financial counterparties

The definition of significant non-financial counterparties has not changed from the previous draft SPM Margin Module. The HKMA now permits an AI to not exchange IM or VM with a significant non-financial counterparty that predominantly uses non-centrally cleared derivatives for hedging purposes. AIs wishing to do so will have to obtain a declaration from the significant non-financial counterparty that it predominantly uses the non-centrally cleared derivatives for hedging purposes. AIs also have to put in place appropriate internal limits and risk management policies and procedures commensurate to its risk appetite, as to monitor and control the risks of relevant exposures. There is no regulatory guidance on what “hedging” or “predominantly” mean.

Significant non-financial counterparties

The inclusion of significant non-financial counterparties as a category of covered entities makes the Hong Kong regime broader in scope than that of the other major Asian jurisdictions (Japan, Singapore and Australia). The practical implication of this is that AIs will have to do more in their client outreach exercise to make sure that their non-financial clients are aware of the new requirements (and how to categorise themselves with industry-developed self disclosure letters).
The hedging exemption may come in handy although AIs will have to consider how to obtain the relevant representation and how continuously the representation will have to be made by their non-financial clients.

In-scope products

The HKMA has clarified in the SPM Margin Module that margin requirements will apply to all OTC derivative products not cleared through a central counterparty (“**CCP**”), not through a qualifying CCP as stated in the early draft of the rules.

Exempt products: More importantly, the HKMA is now exempting two types of products from VM (and IM) requirements: (i) physically-settled FX forwards and swaps (this would include FX security conversion transactions, i.e. physically settled FX forwards for the sale or purchase of a currency which are entered into for the purpose of settling a sale or purchase of securities, which were added by the HKMA to the list of exempt products in the August consultation response) and (ii) “FX transactions” embedded in cross-currency swaps associated with the exchange of principal. In the previous draft SPM Margin Module, these two types of products were exempt from IM requirements but not VM. This will bring Hong Kong more in line with most of the other major jurisdictions (e.g. Japan, Singapore, Australia and the United States).

Physically settled commodity forwards are a new type of exempt product (from both IM and VM requirements). As for the deferred products, the SPM Margin Module clarified that the three-year deferral period (from 1 March 2017 to 29 February 2020) applies to non-centrally cleared single-stock options, equity basket options and equity index options.

Substituted compliance

As indicated by the HKMA in the August consultation response, substituted compliance is permitted to be applied to cross-border transactions with (i) a deemed comparable jurisdiction until such time as a comparability assessment has been completed for that jurisdiction or (ii) a jurisdiction for which the HKMA has issued a comparability determination.

Deemed comparable jurisdictions

These are the following WGMR member jurisdictions (from the day such jurisdictions implement margin requirements):
Australia, Canada, the European Union, India, Japan, Republic of Korea, Mexico, Russia, Singapore, Switzerland and the United States.

Locally incorporated AIs: For AIs incorporated in Hong Kong, substituted compliance is available if the covered entity is required to comply with the margin requirements of a foreign jurisdiction for which the HKMA has issued a comparability determination or which is a deemed comparable jurisdiction. This means that the Hong Kong-incorporated AI may follow the margin requirements applicable to its counterparty instead of the Hong Kong margin requirements.

Overseas incorporated AIs: For AIs incorporated outside Hong Kong, three potential jurisdictions may be applicable for substituted compliance purposes:

> the foreign jurisdiction which margin requirements the covered entity is required to comply with;

> the AI's home jurisdiction; and

> a foreign jurisdiction other than the AI's home jurisdiction,

in all cases, if the foreign jurisdiction is one for which the HKMA has issued a comparability determination or which is a deemed comparable jurisdiction.

Note that the application of substituted compliance in the third case (i.e. complying with the margin standards of a foreign jurisdiction other than the AI's home jurisdiction) is available only in justified cases. The example cited in the SPM Margin Module is where substituted compliance is driven by genuine business presence and client base and not by opportunity for regulatory arbitrage of margin requirements. The foreign regime must be one which, in addition to being accepted by the HKMA as comparable, is accepted by the AI's home authority as a substitute with which the AI may comply. The AI may be requested by the HKMA to substantiate how and the extent to which the foreign standards are relevant to the AI's situation.

The HKMA has clarified that, in all cases of substituted compliance, compliance with the margin requirements of the comparable jurisdiction must be in its entirety, i.e., it is not possible to pick and choose different provisions from the applicable regimes for compliance purposes.

Substituted compliance

The HKMA has previously clarified that if the product scope of the comparable jurisdiction is narrower than that under the Hong Kong rules, AIs will only have to margin on the basis of the narrower product scope if they wish to apply substituted compliance and follow the rules of the comparable jurisdiction.

Of more interest is the case where the comparable jurisdiction (e.g. Singapore) only imposes margin requirements on trades booked in Singapore. It appears that Singapore-incorporated AIs choosing to comply with home rules will therefore not have to margin trades booked in the Hong Kong branch. It remains to be seen whether the HKMA will impose terms and conditions if it is being asked to make a comparability determination for the Singapore margin rules.

Non-netting jurisdictions and non-segregation jurisdictions

As concluded by the HKMA in the August consultation response, margin is not required to be exchanged when AIs trade with counterparties located in non-netting jurisdictions or non-enforceable collateral jurisdictions. Instead, AIs have to put in place appropriate internal limits and risk management policies and procedures, commensurate to their risk appetite, as to monitor and control the risks of relevant exposures. In the SPM Margin Module, the HKMA has helpfully clarified the requirements and refined the conditions for this exclusion to be relied on.

Non-netting: In-scope AIs are not required to exchange IM or VM with a covered entity in circumstances where there is *reasonable doubt* as to the enforceability of the netting agreement upon insolvency or bankruptcy of the counterparty. In order to establish this, in-scope AIs are required to undertake an assessment on the enforceability of the netting agreement which should be supported by a legal opinion, taking into consideration relevant jurisdiction(s) and counterparty type. The assessment should consider the conditions required to qualify as a "valid bilateral netting agreement", as defined in section 2 of the BCR[7]. In particular, in-scope AIs do not have to provide IM and VM where the relevant netting agreement does not fulfil all the conditions, which are beyond the control of the AI, required to qualify as a valid bilateral netting agreement.

By focussing the assessment on the definition of "valid bilateral netting agreement" in the BCR, the determination should be consistent with treatment for regulatory capital purposes. The HKMA has clarified that AIs should make their own assessment on whether a counterparty is a non-netting counterparty. An uncertainty remains with whether AIs incorporated in a non-netting jurisdiction are required to exchange margin under the Hong Kong rules.

Non-enforceable collateral: In-scope AIs are not required to exchange IM in circumstances where arrangements for the protection of posted collateral are questionable or not legally enforceable upon default of a counterparty (i.e. where there is an issue with segregation of margin). In order to establish this, in-scope AIs are required to undertake an assessment on the collateral arrangements which should be supported by a legal opinion, taking into consideration relevant jurisdiction(s) and counterparty type. It is less than clear what the scope of the legal opinion should be; as currently worded the SPM Margin Module seems to envisage "negative" opinions to be provided in

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[7] A "valid bilateral netting agreements" in relation to an authorized institution is defined in Section 2 of the BCR to mean an agreement in respect of which the following conditions are satisfied:

(a) the agreement is in writing;

(b) the agreement creates a single legal obligation for all individual contracts covered by the agreement, and provides, in effect, that the institution would have a single claim or obligation to receive or pay only the net amount of the sum of the positive and negative mark-to-market values of the individual contracts covered by the agreement in the event that a counterparty to the agreement, or a counterparty to whom the agreement has been validly assigned, fails to comply with any obligation under the agreement due to default, insolvency, bankruptcy, or similar circumstance;

(c) the institution has been given independent legal advice in writing to the effect that in the event of a challenge in a court of law, including a challenge resulting from default, insolvency, bankruptcy, or similar circumstance, the relevant court or administrative authority would find the institution's exposure to be the net amount under-

  (i) the law of the jurisdiction in which the counterparty is incorporated or the equivalent location in the case of non-corporate entities, and if a branch of the counterparty is involved, then also under the law of the jurisdiction in which the branch is located;

  (ii) the law which governs the individual contracts covered by the agreement; and

  (iii) the law which governs the agreement;

(d) the institution establishes and maintains procedures to monitor developments in any law relevant to the agreement and to ensure that the agreement continues to satisfy this definition;

(e) the institution manages the transactions covered by the agreement on a net basis;

(f) the institution maintains in its files documentation adequate to support the netting of the contracts covered by the agreement; and

(g) the agreement is not subject to a provision that permits the non-defaulting counterparty to make only limited payment, or no payment at all, to the defaulter or the estate of the defaulter, regardless of whether or not the defaulter is a net creditor under the agreement;

order to confirm this, although we note that the HKMA will accept opinions obtained on an industry-wide basis.

Requirements for the legal opinion: the legal opinions to establish whether a counterparty is located in a non-netting jurisdiction or whether arrangements for the protection of posted collateral are questionable or not legally enforceable need to be a formal legal opinion in written form and may be obtained from an independent internal unit or an external independent legal counsel. Jurisdictional opinions obtained on an industry-wide basis by industry associations from external independent legal counsel are acceptable for this purpose.

Margin standards: variation margin

AIs are required to exchange VM with a covered entity on a net basis to collateralise the mark-to-market exposure of the non-centrally cleared OTC derivatives in a netting set. The SPM Margin Module requires the VM amount to be exchanged to "fully collateralise the current exposure of the non-centrally cleared derivatives". It remains to be seen whether the HKMA would be agreeable to the inclusion of non-regulatory independent amounts in counterparties' regulatory VM documentation.

Margin standards: Initial margin

IM standards have not deviated substantially from the August consultation response. Subject to the crossing of the relevant thresholds by both counterparties, AIs are required to exchange (i.e. post and collect) IM with a covered entity on a two-way gross basis to collateralise the potential future exposure that could arise from future changes in the mark-to-market value of the derivatives during the time it takes to close out and replace the position in the event of a counterparty default.

Legacy trades

Hong Kong margin requirements do not apply to non-centrally cleared derivatives entered into before the 1 March 2017 commencement date of the SPM Margin Module ("**legacy trades**"), although legacy trades may be included in the netting set if it is done on a continuous basis. The HKMA has indicated that there will also be no retrospective application of margining requirements in respect of any transactions which are entered into during the transition period (i.e. from 1 March 2017 to 31 August 2017).

Changes in covered entity status

As the definitions of financial counterparty and significant non-financial counterparty are determined on a yearly basis (from 1 September to 31 August of the following year) by reference to the AANA of the relevant counterparty or its group, the SPM Margin Module clarified that where a covered entity ceases to be subject to margin requirements in any one-year period from 1 September of that year to 31 August of the following year, the in-scope AI may cease to comply with the margin requirements for non-centrally cleared derivatives entered into with that covered entity after the covered entity changes its status (i.e. from 1 September of that year) as well as for any outstanding transactions entered into since the beginning of the applicable phase-in period.

Amendments and novations

The SPM Margin module clarified that genuine and non-material amendments to legacy trades will not be subject to margin requirements. New contracts resulting from portfolio compression or post-trade risk reduction exercises are not subject to margin requirements as long as the portfolio on which such exercise is performed consists exclusively of legacy trades. On the other hand, any amendment that substantially changes the terms and conditions of a trade needs to be considered as a new contract. Any amendment that extends a legacy trade for the purpose of avoiding the margin provisions needs to be considered as a new contract. Margin requirements also apply to any new contracts resulting from portfolio compression or post-trade risk reduction exercises if the portfolio on which such exercise is performed consists of legacy trades and new trades.

Calculation of AANA

AANA (average aggregate notional amount) is used for a number of purposes:

> To determine whether an entity that belongs to one of the types of financial counterparties has exceeded the HK$ 15 billion threshold such that it will become a covered entity;

> To determine whether a non-financial counterparty has exceeded the HK$ 60 billion threshold such that it will become a significant non-financial counterparty (hence a covered entity); and

> To determine whether an in-scope AI and a covered entity has exceeded the relevant threshold such that they will have to exchange IM and adopt risk mitigation standards for non-centrally cleared derivatives for a one year period (from 1 September to August of the following year).

AANA in respect of an entity or a group and a period from 1 September to 31 August of the following year means the average of the total gross notional amount of month-end positions of non-centrally cleared derivatives for March, April and May preceding the 1 September starting date in a relevant year. The SPM Margin Module clarified the following for the calculation of AANA:

> All non-centrally cleared derivatives are included in the calculation of AANA, including physically settled FX forwards, physically settled FX swaps, the “FX transactions” embedded in cross-currency swaps associated with the exchange of principal, physically settled commodity forwards, single-stock options, equity basket options and equity index options;

> AANA is calculated on a group level by including all non-centrally cleared derivatives of all entities within the group of companies (including those for which the in-scope AI faces no counterparty risk or that are entered into with exempt entities).

> Intragroup transactions are included once in the AANA calculation.

Effective date and Phasing-in schedule; Transition period

The commencement date of the SPM Margin Module is 1 March 2017. AIs are required to exchange VM for all in-scope non-centrally cleared derivatives entered into with a covered entity from 1 March 2017. For IM, the exchange of IM by AIs with covered entities will apply in a one-year period (from 1 September of a year to 31 August of the following year) where both the AI and the covered entity have an AANA of non-centrally cleared derivatives exceeding the following threshold:

	Period	AANA threshold
Phase-in	1 March 2017 to 31 August 2017	HK$ 24 trillion
	1 September 2017 to 31 August 2018	HK$ 18 trillion
	1 September 2018 to 31 August 2019	HK$ 12 trillion
	1 September 2019 to 31 August 2020	HK$ 6 trillion
Permanent	From 1 September 2020 onwards for each subsequent 12-month period	HK$ 60 billion

Transition period: VM and IM requirements are subject to an initial 6-month transition period (i.e. 1 March 2017 to 31 August 2017).

The expectation of the HKMA is that in-scope entities shall start exchanging margin as soon as possible after the 1 March 2017 commencement date and make reasonable and continuous progress during the transition period in order to achieve full compliance by the end of the period. Helpfully, the HKMA has indicated that no regulatory action will be taken in the case of non-compliance during the transition period and there will be no retrospective application of margin requirements in respect of any transactions which are entered into during the transition period.

Risk Mitigation Standards (RMS)

The SPM Margin Module provides for the following RMS for non-centrally cleared derivatives:

> Execution of written trading relationship documentation;

> Confirmation of the material terms of the non-centrally cleared OTC derivative after the transactions are executed;

> Valuation of non-centrally cleared derivatives in an objective manner;

> Regular reconciliation of the material terms and valuations of all transactions in a non-centrally cleared derivatives portfolio; and

> Resolution of disputes in a timely manner.

Implementation timeline: An important change in the SPM Margin Module relates to the implementation timeline for RMS. The adoption of RMS will be phased-in on a similar schedule as IM. The RMS apply in a one-year period (from 1 September of each year to 31 August of the following year) where both the in-scope AI and the covered entity have an AANA exceeding the following threshold:

	Period	**AANA threshold**
Phase-in	1 March 2017 to 31 August 2017	HK$ 24 trillion
	1 September 2017 to 31 August 2018	HK$ 18 trillion
	1 September 2018 to 31 August 2019	HK$ 12 trillion
	1 September 2019 to 31 August 2020	HK$ 6 trillion
	1 September 2020 to 31 August 2021	HK$ 60 billion
Permanent	On a permanent basis from 1 September 2021	Zero

Conclusions

Margin requirements for non-centrally cleared derivatives are set to commence in Hong Kong, Singapore and Australia from 1 March 2017 with a six months' transition period from 1 March 2017 to 31 August 2017. The coordination by the three Asian regulators on the implementation timelines is very much to be welcomed and the transition period will give market participants the much needed time to prepare for the new regulatory requirements.

It is expected that the Securities and Futures Commission will in due course publish a corresponding set of margin rules for licensed corporations in Hong Kong. It remains to be seen when this will be done and how the rules will compare with the SPM Margin Module.

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Appendix

Hong Kong VM requirements – a summary	
In-scope entities	AIs under the Banking Ordinance, incorporated in Hong Kong or outside Hong Kong
Covered entities	Financial counterparties (HK$ 15 billion threshold) and significant non-financial counterparties (HK$ 60 billion threshold)
Booking location requirement	Hong Kong-incorporated AIs: Hong Kong margin rules apply on an entity basis (i.e. to all in-scope products booked in all branches). Overseas-incorporated AIs: Hong Kong margin rules only apply to in-scope products booked in its Hong Kong branch.
Exempt entities	Sovereigns, central banks, public sector entities, multilateral development banks, Bank for International Settlements.
In-scope products	Non-centrally cleared derivatives (i.e. OTC derivative products as defined in the Securities and Futures Ordinance) not cleared through a CCP.
Exempt products	Physically settled FX forwards and swaps, fixed physically settled FX transactions associated with exchange of principal of cross-currency swaps, physically settled commodity forwards, indirectly cleared derivatives, repos and securities lending transactions. Non-centrally cleared single-stock options, equity basket options and equity index options subject to three-year deferral period (from 1 March 2017 to 29 February 2020).
Broad product set	Permitted if done on a consistent basis.
VM calculation frequency	Daily.
VM threshold	Zero.
Timing for margin calls and transfers	Call by end of business day following trade date. Collect within two business days after call date.
Minimum transfer amount	HK$3,750,000 (cumulatively with IM).
Eligible collateral	Cash, gold, marketable debt securities issued by sovereigns, multilateral development banks, public sector entities and other issuers of credit quality grade 3 or above. Equities included in the Hang Seng Index or any other main index.

	Policies and procedures should be in place for the replacement of collateral when the credit quality grade falls below credit quality grade 3.
Ineligible collateral	Securities issued by AIs and foreign banks, securities exhibiting a significant correlation with the creditworthiness of the counterparty or the underlying non- centrally cleared derivatives (in particular, securities issued by the posting counterparty or its group entities)
FX haircut	8% on non-cash VM in a currency different from any currency contractually agreed by the parties.
Intragroup exemption	Available. No requirement to apply for exemption.
Substituted compliance	Available with respect to comparable jurisdictions. Deemed comparable jurisdictions are: Australia, Canada, EU, India, Japan, Republic of Korea, Mexico, Russia, Singapore, Switzerland, US
Non-netting jurisdictions	VM not required to be exchanged. In-scope entities should manage exposure by putting in place appropriate internal limits and risk management policies and procedures.