
OTC DERIVATIVES TRADING IN HONG KONG FREQUENTLY ASKED QUESTIONS

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WHAT IS AN LEI?

The Legal Entity Identifier (LEI) is a unique global identifier of legal entities involved in financial transactions. These can be either companies or government entities that take part in financial transactions. The identifier is used in reporting to financial regulators. All financial companies and funds are required to have an LEI.

The identifier is formatted as a 20-character, alpha-numeric code based on the ISO 17442 standard developed by the International Organization for Standardization (ISO). It connects to key reference information that enables clear and unique identification of legal entities involved in financial transactions. Each LEI contains information about an entity's ownership structure and thus answers the questions of 'who is who' and 'who owns whom'. Simply put, the publicly available LEI data pool can be regarded as a global directory of participants in the financial market.

ARE LEIS OR COMPANY INCORPORATION NUMBER MANDATORY?

Having an LEI (first priority) or a company incorporation number (second priority) is a requirement for the Hong Kong Monetary Authority (HKMA) and Hong Kong Trade Repository (HKTR) in Hong Kong for OTC transaction reporting. If you have not applied for an LEI yet, we encourage you to do so as soon as possible and to provide us with your LEI once you have it.

For clients who do not have LEIs, the HKMA expects reporting entities like Banque Pictet & Cie SA, Hong Kong Branch ("the Bank"), to have a process in place to inform clients about the necessity to obtain an LEI and encourage or assist them to obtain one. Reporting entities should also ensure that the LEIs they obtain pertain to the entities concerned and are included in the Global LEI System.

The Bank, by being a branch of Banque Pictet & Cie SA, which is subject to FMIA laws in Switzerland, must obtain LEIs (first priority) or company incorporation number (second priority) from its clients before providing services that would trigger reporting obligations in respect of transactions carried out for those clients and use this information in its transaction reports. This requirement applies to all types of mandates.

Consequently, not providing an LEI or the incorporation number to the Bank within the stipulated timeframe will mean that no further transactions in any financial instruments will be allowed. This, in turn, may result in financial consequences.

In other words, no LEI / Incorporation number means no trade.

FOR WHAT PURPOSES ARE LEIS OR COMPANY INCORPORATION NUMBER REQUIRED WORLDWIDE?

Currently, LEIs are used in Hong Kong for reporting OTC derivative to the HKTR operated by the HKMA. LEIs may also be required for other regulatory purposes such as FMIA.

ARE LEIS CONFIDENTIAL?

No. LEIs are not confidential. There is an international database of LEIs and related companies accessible on the internet: <https://www.gleif.org/en/>.

OTC DERIVATIVES TRADING IN HONG KONG FREQUENTLY ASKED QUESTIONS

WHERE CAN I GET AN LEI?

There are a number of LEI issuers around the world that issue and maintain the identifiers and act as primary interfaces to the global directory. These are, typically, financial exchanges or financial data vendors, who are accredited by the Global Legal Entity Identifier Foundation (GLEIF) to issue LEIs.

LEI issuers authorized by Depository Trust & Clearing Corporation (DTCC) include:

In Asia

www.leicode.sg/lei-registration/

www.leicode.hk/

www.lei-worldwide.com

[/?gclid=EAIaIQobChMIto3DkKrY5wIVSbDtCh2xcgRIEAAAYASAAEgIycPD_BwE](https://www.gs1hk.org/our-services/legal-entity-identifier/?gclid=EAIaIQobChMIto3DkKrY5wIVSbDtCh2xcgRIEAAAYASAAEgIycPD_BwE)

<https://www.gs1hk.org/our-services/legal-entity-identifier/>

Outside Asia

lei.bloomberg.com

www.lei.direct

www.rapidlei.com

www.luxcsd.com/luxcsd-en/

Please note that there is also an upfront and annual cost for registering and maintaining an LEI.

The Bank does not recommend any LEI issuer specifically; the list above is merely indicative. Clients may select their preferred LEI issuers to register for an LEI. However, Relationship Managers may help clients to register for LEIs. Registering an LEI is a straightforward process requiring questions to be answered online.

WHAT IS A LEGAL ENTITY AND WHO NEEDS AN LEI?

An LEI enables clear and unique identification of legal entities (natural persons excluded) who participate in financial transactions issued under the Global LEI System. All unique parties that are legally or financially responsible for the performance of financial transactions or that have the legal right in their jurisdiction to enter independently into legal contracts are required to obtain LEIs, regardless of whether they are incorporated or constituted in some other way (e.g. trust, partnership, contractual). Therefore, even if an offshore company does not, for example, engage in any operations at all, if they are entering into a financial transaction and are legally bound by it, they should apply for an LEI.

OTC DERIVATIVES TRADING IN HONG KONG FREQUENTLY ASKED QUESTIONS

IS AN LEI REQUIRED FOR TRUST ENTITY THAT IS A CONTRACT RATHER THAN AN ENTITY?

Yes, except if the trust of legal arrangement is registered and can provide a company's incorporation number. All unique parties that are legally or financially responsible for the performance of financial transactions or have the legal right in their jurisdiction to enter independently into legal contracts are required to obtain LEIs, regardless of whether they are constituted in some other way (e.g. trust, partnership, contract). As per Switzerland rules, the trustee must be identified rather than the trust itself, for reporting purposes. The trustee can be either an individual or a company, for the latter identified with LEI or company incorporation number. This is the preferred solution. The Bank may also accept that an LEI for the trust itself is provided, especially if this already exists. In such a case, this must be mentioned in the onboarding form (i.e. the LEI identifies the trust itself and not the trustee).

CAN A COMPANY HAVE MORE THAN ONE LEI?

No. In general, a legal entity shall have only one LEI.

WHAT HAPPENS IF A LEGAL ENTITY DOES NOT PROVIDE THE BANK WITH AN LEI OR ITS INCORPORATION NUMBER?

HKMA issued a circular on 19 February 2019 to communicate the first phase ordering the use of LEIs to take effect on 1 April 2019. Pursuant to the Joint Consultation Conclusions Paper on Enhancements to the OTC Derivatives Regime for Hong Kong published in June 2018, the first phase applies only to a reporting entity's side of a transaction, in which all reporting entities are required to use an LEI to identify themselves when reporting to the HKTR effective from 1 April 2019.

In addition, HKMA reminded all reporting entities (including the Bank in this case) to put in place a process to request LEIs from clients after 1 April 2019. For clients who do not already have LEIs, this process includes informing clients about the necessity to obtain an LEI and to encourage or assist them to obtain it.

As a branch of a Swiss financial institution, the Bank should comply with Swiss legislation (such as FMIA). Therefore, transactions on the securities covered by these transactions will be blocked for entities that do not have a valid LEI or the entities' incorporation number.

WHAT ABOUT 'NO LEI EQUALS NO TRADE' IN HONG KONG?

The Bank must obtain LEIs or Incorporation number from its clients before providing services that would trigger reporting obligations in respect of transactions carried out for those clients and use this information in its transaction reports.

Consequently, not providing an LEI or Incorporation number to the Bank within the stipulated timeframe will mean that no transactions in any financial instruments are allowed. This, in turn, may result in financial consequences.

In other words, no LEI or Incorporation number means no trade.

OTC DERIVATIVES TRADING IN HONG KONG FREQUENTLY ASKED QUESTIONS

WHO DOES THE BANK REPORT OTC TRANSACTIONS TO?

The Bank reports its transactions to the HKTR, operated by the HKMA.

As the HKTR is a centralized registry that maintains an electronic database of records of OTC derivatives transactions. By collecting and providing OTC derivatives transaction information to regulatory authorities, the HKTR plays a vital role in helping authorities to carry out their market surveillance responsibilities. This will help maintain the stability of the financial systems. It also helps increase transparency in the market, promotes standardisation and provides a level of consistency in the quality and availability of transaction data.

As a branch of Banque Pictet & Cie SA, the Bank is subject to the Swiss legislation FMIA. Therefore, when it is counterparty to a transaction that falls within the scope of the regulations, it triggers FMIA reporting obligations.

For further information governing FMIA reporting obligation, please refer to the FAQs online at www.group.pictet/market_regulations.

HOW DOES DERIVATIVES REPORTING WORK IN SWITZERLAND AND HONG KONG?

All openings, daily valuation, modifications and closures of OTC derivatives trades within the scope of Swiss or Hong Kong OTC regulations need to be reported to a Swiss trade repository and a Hong Kong Trade repository by the end of the day after the execution (or maximum two days after the execution to the HKTR).

This includes the conclusion, modification and termination of any derivative contract within the scope with any counterparty (including individuals and third-country entities). The transmitted data include both transaction and counterparty data. The report must indicate the other counterparty of the trade. This is done via the Legal Entity Identifier (LEI) or company incorporation number.

For natural persons an internal code number (anonymised) will be used both in Switzerland and in Hong Kong.

The Bank will perform this reporting on the entity behalf both in Hong Kong and Switzerland.

WHAT DO OTC DERIVATIVE TRANSACTIONS COVER?

Over-the-counter ("OTC") derivatives cover the followings:

- Any interest rate derivatives contracts (e.g. interest rate swaps)
- Any credit derivatives contracts (e.g. credit derivatives swaps or index)
- Any foreign exchange derivatives contracts (e.g. forwards, swaps, options, non-deliverable forwards (NDF), non-deliverable options (NDO), accumulator/decumulator (ACDC))
- Any commodity derivatives contracts (e.g. ACDC, pivots, forwards, options)
- Any equity derivatives contracts (e.g. options, ACDC)

OTC DERIVATIVES TRADING IN HONG KONG FREQUENTLY ASKED QUESTIONS

Options may consist of vanilla options or exotic options such as single/ double options.

The following are not considered as OTC derivatives under HKMA rules:

- Dual currency investments (DCI), dual currency deposits (DCD) and dual currency deposit notes (DCN) fall under the definition of structured deposits rather than derivatives contracts.
- Structured products or notes, FX spots, securitised products and certificates.
- The Bank is not authorized to trade exchange-traded derivatives, i.e. futures and options.

WHAT IS FMIA?

FMIA (Swiss Federal Act on Financial market Infrastructure and Market Conduct in Securities and Derivatives Trading) enhance the transparency on derivatives and securities transactions, reduce counterparty risk and improve market integrity and supervision. Provisions of FMIA are largely similar to those from OTC derivatives regulations applicable locally in Hong Kong under the supervision of HKMA and / or SEC. The main difference from a client perspective between Hong Kong and Swiss regulation, is that Swiss regulation requires additionally a reporting on Securities traded or admitted to trade on a Swiss exchange, in addition to the reporting of OTC derivatives to a trade repository (similar to HKTR in Hong Kong). The relevant brochure is available on our website:

<https://www.group.pictet/wealth-management/market-regulations>

WHAT IS MEANT BY SECURITIES?

FMIA Securities are standardised certificated and uncertificated securities, derivatives and intermediated securities, which are suitable for mass trading

HOW DOES SECURITIES REPORTING WORK IN SWITZERLAND?

CBPSA in Geneva, as a participant admitted to a Swiss trading venue (mainly SIX exchange in Zürich) shall report all transactions they execute involving securities admitted to trading on a Swiss trading venue.

The Bank, as a foreign branch of Swiss securities dealers (BPSA) will fulfil its reporting obligation under the membership of their Swiss parent company BPSA.

In particular, the following must be reported: the name and number of purchased or sold securities, the volume, date and time of the transaction; the price; the details necessary to identify the beneficial owner.

The reporting duty also applies to transactions in derivatives whose underlying instruments are securities admitted to trading on a Swiss trading venue.

The reporting duty applies not only to transactions on own account, but also to transactions executed on behalf of a client.

BPSA will perform this reporting on behalf of the Bank in Switzerland.

OTC DERIVATIVES TRADING IN HONG KONG FREQUENTLY ASKED QUESTIONS

WHAT IS MEANT BY 'CENTRALLY CLEARED OTC'S'?

Central clearing is currently a requirement mostly applicable to large financial institutions. As a client of the Bank, you are not concerned by central clearing.

WHAT ARE THE INITIAL AND VARIATION MARGINS REQUIREMENTS?

In some cases (depending on the client's classification), OTC derivative trading regulations require the bilateral exchange of margining or collateral to cover market and credit risk.

Determining the client's classification and potential need for margining requirements is covered by section 4 of the OTC client onboarding form.

Variation margin is aimed at protecting the Bank against market movements while initial margin seeks to protect the Bank against default by the counterparty.

Margining requirements will be dealt with directly by the Bank without your being involved.

The Bank seeks your acknowledgment to collect the above information and to inform us in due course should there be a change in circumstance, such as a change in threshold for margining. This applies to all types of mandates.

WHAT ARE COVERED ENTITY OR FOREIGN COVERED ENTITIES IN THE CONTEXT OF MARGINING?

Covered Entity (CE) means a financial counterparty, a significant non-financial counterparty, or another entity designated by the HKMA, but excludes a sovereign (i.e. central government of a country), central bank, public-sector entity, multilateral development bank and the Bank for International Settlements.

Financial counterparty refers to any 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 HKD 15 billion. For significant non-financial counterparties, an aggregate notional amount of non-centrally cleared derivatives exceeding HKD 60 billion is used to assess the need for margining using the same phase-in period defined for financial counterparty.

The margin provisions apply to the Bank only when it enters into transactions with a CE that are booked in the Bank's book. However, the Bank will be subject to initial margin (IM) requirements if (i) the counterparty is a covered entity and (ii) both the Bank and the covered entity have an average aggregate notional amount of non-centrally cleared OTCD exceeding the threshold stipulated in the phase-in schedule.

Foreign Covered Entity (FCE) refers to an entity operating outside of Hong Kong which, if operating in Hong Kong, would be classified as a Covered Entity.

Some information is quoted from Source:
https://en.wikipedia.org/wiki/Legal_Entity_Identifier.

Non official translation – If there is any inconsistency or ambiguity between the English version and the Chinese version, the English version shall prevail.

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