ISDA Safe, Efficient Markets

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The Australian Securities and Investments Commission's Consultation Paper 231 on Mandatory central clearing of OTC interest rate derivative transactions, May 2015

The International Swaps and Derivatives Association, Inc. (ISDA)[1] welcomes the opportunity to provide comments on the Australian Securities and Investments Commission's (ASIC) Consultation Paper 231 Mandatory central clearing of OTC interest rate derivative transactions (Consultation Paper). Individual ISDA members may have their own views on the Consultation Paper, and may provide their comments to ASIC independently.

We appreciate the efforts ASIC, and all of the members of the Council of Financial Regulators, have taken to work with market participants to develop the mandatory clearing requirements. All stages of the process have been conducted through transparent and interactive dialogue. As a result, the Consultation Paper covers ground familiar to market participants and provides greater clarity into how ASIC's objectives will be accomplished through the rule making. ISDA and its members support the clearing of eligible OTC derivatives as a way to make markets safer and more efficient and supports ASIC's efforts to enforce mandatory clearing, where appropriate, while also recognizing that there are many OTC derivative trading scenarios where mandatory clearing might increase risk or lead to less efficient markets. We therefore support the Council of Financial Regulators' considered and evidence-based approach to identify the appropriate time and conditions for clearing, through the its ongoing market assessments. We support and

[1] Since 1985, ISDA has worked to make the global over-the-counter (OTC) derivatives markets safer and more efficient. Today, ISDA has over 840 member institutions from 64 countries. These members include a broad range of OTC derivatives market participants including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure including exchanges, clearinghouses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's web site: www.isda.org.

encourage continued dialogue between ASIC and the industry to work together to address any implementation issues that may arise from mandatory clearing.

Response to specific questions

The remainder of this letter sets out our comments in relation to the specific questions posed in the Consultation Paper. Our response is set out underneath each question. The headings used below correspond to the headings used in the Consultation Paper.

QUESTIONS

B1Q1 Do you agree with the proposed scope of entities that may be subject to mandatory central clearing?

We believe that the proposed scope covering ADIs, AFS licensees, Foreign clearing entities and trusts and registered schemes that exceed the clearing threshold is appropriate. However, we wish to point out that the definition of Financial Entity in the draft rules does not include reference to a Foreign ADI whereas this is referred to in the Consultation Paper as an entity category.

The draft rules cover only those foreign entities that, in addition to being an ADI, Exempt Foreign Licensee or financial services license holder, are also a Part 5B.2 registered or required to be registered foreign company. We understand that it is not necessarily the case that every ADI, Exempt Foreign Licensee or financial services license holder will also be a Part 5B.2 registered or required to be registered foreign company. Irrespective of any overlap between the requirement to be registered as a Part 5B.2 company and an entity's licensing status, these remain two distinct regimes (the former being subject to analysis based on common law principles (in addition to any statutory tests)). Therefore ASIC may wish to consider whether one should be conditional upon the other as forming part of the definition of Foreign Clearing Entity.

While some of our members are neutral, the majority feel strongly that the extra-territorial scope of the clearing mandate should be limited in nature and should only apply to OTC derivative transactions booked in Australia. In other words, where a Foreign Clearing Entity (FCE) is involved, only in-scope G4 or AUD-IRD transactions that are booked in its Australian branches (or potentially guaranteed by an Australian entity?) should be subject to the clearing mandate.

The inclusion of transactions 'entered into' in Australia (i.e. those with a trader or salesperson nexus) is not in line with international standards and international commitments, nor is it

consistent with the previously emphasized policy objective of increased efficiency, integrity and stability of financial markets. OTC derivative transactions 'entered into' in Australia but not booked in Australia do not impinge on Australia's financial stability, as the risk for these transactions does not reside in Australia, but in the jurisdiction in which they are booked.

The following table and notes highlight how ASIC's proposals are inconsistent with the approach taken in the US and the EU. The table assumes that the in-scope trade is booked outside of Australia by both entities. A "tick" highlights where there would be a clearing obligation under the current Australian mandate.

Entity 1 / Entity 2	Australia Clearing Entity ("ACE")	Foreign Clearing Entity ("FCE")	Foreign International Active Dealer ("FIAD")
ACE	√	√	√
FCE	√	√ [where 'entered into' in Australia][1]	√ [where 'entered into' in Australia][2]
FIAD	√	√ [where 'entered into' in Australia][2]	×

1. In a US context, currently if both FCEs were non-US Swap Dealers then the trade would not be subject to the US clearing obligation. This position is subject to final guidance from the CFTC on footnote 513/13-69. In an EU context, the trade would only be subject to the EU clearing obligation if the trade had a direct, substantial and foreseeable effect within the EU (which equates, in this context to being guaranteed by an EU entity or booking to a branch in the EU).
2. In a US context, assuming the FCE is a non-US Swap Dealer and the FIAD a foreign internationally active dealer, currently the trade would only be subject to the US clearing mandate if the FIAD was a guaranteed affiliate of a US entity or a US Swap Dealer. This position is subject to final guidance from the CFTC on footnote 513/13-69. In an EU context, the trade would only be subject to the EU clearing obligation if the trade had a direct, substantial and foreseeable effect within the EU (which equates in this context to being guaranteed by an EU entity or booking to a branch in the EU).

For these reasons, the inclusion of 'entered into' in Australia transactions within the mandate is an inappropriate extraterritorial reach. Market surveillance policy objectives were the driving force behind the inclusion of nexus transactions within the reporting mandate, but the clearing mandate has always been justified in policy terms on the basis of increased efficiency, integrity and stability of financial markets; not market surveillance. As such our members strongly believe that including nexus transactions in the mandate is a significant policy overreach by ASIC and any extension should be limited to where one of the foreign entities is guaranteed by an Australian entity.

To include 'entered into' in Australia transactions in the mandate increases the potential for the Australian mandate to conflict with the rules in other jurisdictions, will significantly increase the

compliance and build costs associated with the mandate for FCEs, and have a number of potentially negative outcomes.

By way of example, where a FCE is trading with a FIAD across multiple time zones, a situation could arise where 2 identical transactions (both booked outside Australia) entered into by the FIAD with the FCE have different clearing requirements under the Australian mandate. This could occur where the first transaction is conducted during New York (NY) trading hours and involves a NY salesperson or trader, and the second transaction is conducted during Australian trading hours and involves an Australian salesperson or trader. The risk profile of both transactions to the Australian market will be identical, however the second transaction will be subject to the Australian clearing mandate yet first transaction will not.

Where the above situation occurs, the first transaction may have been subject to an EU or US clearing requirement and therefore the parties would be able to clear through the full spectrum of central counterparties (CCPs) permitted under either the EU or US regulations. This list of available CCPs is much wider than the limited list of CCPs licensed or intended to be prescribed in Australia. The second transaction would be required to only be cleared through one of the limited list of Australian licensed CCPs or 4 CCPs intended to be prescribed.

The above issue becomes even more complex where the first transaction is not required to be cleared – that is, it relates to an Australian-clearable transaction not yet subject to mandatory clearing in the EU or US, or is with a FIAD not yet mandated to clear under EU or US requirements. If the second transaction was actually priced during NY hours by a NY trader (i.e. as a non-cleared transaction) but was finalized by an Australian salesperson, it would have to be re-priced and adjusted at the point of trade to reflect the fact that it is now subject to the clearing mandate.

The complexities described above will significantly increase compliance and build costs for FCEs and FIADs, while also affecting competition and the efficiency of the market. The complexities created by the inclusion of nexus transactions could further potentially result in an increase in systemic risk in Australia, as FCEs may be forced to consider reducing the scope of transactions they arrange or execute from Australia, resulting in reduced liquidity within the Australian market. In addition, given that expectations are for the EU and US clearing mandates to be expanded in due course to include interest rate swaps (IRS) denominated in AUD, there would appear to be little justification for the overlap on the grounds of preventing regulatory arbitrage.

B1Q2 Do you agree with the proposed definitions of 'Australian clearing entity', 'foreign clearing entity', 'opt-in Australian clearing entity' and 'opt-in foreign clearing entity'?

Our members have raised the concern that a Foreign Clearing Entity should only be in-scope if "registered", as opposed to "registrable", as otherwise this creates uncertainty for the clearing entity to determine which counterparties are and are not in-scope for mandatory clearing. If an entity prefers to clear its trades, but it is not considered as an Australian or Foreign Clearing Entity, it can still do so on a voluntary or opt-in basis.

B1Q3 What is the likely impact of our proposals?

ISDA notes that the majority of in-scope "sell-side" institutions are already clearing on a voluntary basis and therefore, we do not anticipate significant impact on them. We do however have some concerns about how "buy-side" institutions that are above the threshold may be impacted. This is because the number of client clearing service providers currently remains limited, and it would be easy to envision scenarios under which buy-side firms are unable to contract client clearing service providers at a price that makes economic sense. If this scenario were to play out, these institutions might reduce or cease their derivatives trading activity.

The inclusion of nexus transactions in the mandate increases the scope for conflict with foreign rules, increases the compliance and build costs for clearing entities and will result in FCEs having to reconsider the services they are able to offer FIADs with respect to in-scope products from Australia. We note that the Monetary Authority of Singapore (MAS) recently published a consultation paper on its proposed mandatory clearing regime, which does not include the nexus test.

B2Q1 Do you agree with our proposal to adopt the clearing threshold set by the Australian Government of $100 billion gross notional outstanding in OTC derivatives, for entities other than those acting in a representative capacity?

Most members are supportive of the proposed clearing threshold. However, there is a countervailing view that believes that the threshold is too high and disagrees with the policy intent behind the clearing mandate. Under this view, the clearing mandate should be broader in application, to capture all risk in the financial system. The draft rules reflect current market practice (rather than imposing any additional requirements) – namely, the largest financial institutions are already centrally clearing – and therefore the better approach would be to reduce the threshold and extend the scope of the clearing mandate to capture medium and smaller-sized institutions, consistent with the approach taken across other major G20 jurisdictions such as the EU and US. Setting a clearing threshold at such a high level will operate to exclude a significant

amount of the medium and smaller-sized financial markets (and therefore the risk that such participants bring to the system).

Those members supportive of the proposed threshold believe that it meets the objective of channeling the credit risk of systemically-important institutions into central clearing and appropriately regulated clearinghouses, and avoids burdening smaller, non-systemic financial institutions with costs that could be disproportionately high relative to their size and the amount of risk reduction achieved. Furthermore, they support Australia's policy of using an incentives-based approach and believe that capital charges under the Basel III regulatory framework will drive voluntary central clearing for entities below the gross notional threshold.

Members supportive of the proposed threshold have also pointed out that the clearing threshold calculation should be based on OTC derivative transactions 'booked in' Australia only. One of the main policy intentions of the clearing mandate communicated previously has been to increase efficiency, integrity and stability of the financial markets in Australia, however the 'entered into' concept was introduced to assist ASIC meet its market surveillance and transparency objectives. It is therefore not appropriate for inclusion in a mandate based on increasing efficiency, integrity and stability of the financial markets in Australia, and members would argue that the market surveillance and transparency objectives have been achieved by the introduction of transaction reporting.

However, if ASIC is to continue to include nexus transactions within the threshold calculation (which our members do not support), it is of critical importance that it amends the current proposal to exclude "entered into" transactions entered into before 25 February 2015. As ASIC is aware from its work with the industry earlier this year on ASIC Instrument 15/0067 (Instrument), reporting entities have faced significant challenges in identifying historical nexus transactions, as the logic has required enhancements to the trade data being captured by firms which cannot be applied retrospectively. This was one of the main reasons for a back loading period with respect to nexus transactions under the Instrument being limited to those executed after 25 February 2015. For the same reason, we believe that only nexus transactions executed after 25 February 2015 should be included in the calculation of the clearing threshold.

Additionally, members have asked for clarity as to, in the event that a client of an investment manager (i.e. a fund or institutional client) becomes subject to the central clearing mandate as it individually has over AUD100 billion in gross notional OTC derivatives exposure, whether it would be able to delegate its central clearing obligation to agents such as its investment managers who enter into the relevant trades on its behalf, as these entities currently do in respect of reporting under delegation agreements. We also query whether any safe harbour provisions would be equally applicable to a delegated clearing obligation.

Members have also pointed out that the method for determining whether or not an entity exceeds the clearing threshold may arguably be subject to distortion. This is because the threshold is

calculated on the basis of any derivative exposure and not specific to a clearable instrument/product. For instance, an entity may have derivative exposure in credit derivatives of $102 billion thereby exceeding the threshold, yet only have an exposure of $1 million in IRS which is a proportionally very small portfolio. Yet in these circumstances the relevant entity would have to put in place relevant systems, controls and documentation to centrally clear the small portfolio of trades. In the same way, the converse can apply to a smaller entity which proportionally could have up to $900 million derivatives exposure in IRS and $1 million in credit derivatives, yet not be caught by the clearing mandate (nor have to put in place relevant systems, controls and documentation to manage the financial risk arising), despite having a much larger portfolio of clearable trades compared to a larger entity that exceeds the clearing threshold.

Members have also queried what the foreign exchange (FX) conversion rate should be, if they are converting their outstanding trades into AUD for the purpose of calculating the clearing threshold. ISDA notes that exchange rate fluctuations could cause entities to be above the threshold for one quarter and below the next, or vice versa.

B2Q2 Do you agree with the proposed application of the clearing threshold in relation to transactions entered into on behalf of a trust or registered scheme?

Members have noted that an investment manager would manage investment portfolios and execute transactions with counterparties in an agency capacity on behalf of (i) funds; and (ii) institutional clients. We request that ASIC clarify whether the proposed central clearing mandate would apply to trades that such an investment manager enters into in an agency capacity on behalf of its clients. For instance, if the investment manager's aggregate derivatives exposure in respect of transactions it enters into for Client A and Client B in an agency capacity crosses the AUD100 billion threshold, would it become subject to the central clearing obligation? It would be helpful to have this explicitly carved out in the rules if that is not the intention.

B2Q3 Do you agree with the proposed derivatives that must be included when calculating the clearing threshold?

We are of the view that "true" OTC derivatives only should be included in the threshold calculation and as such derivatives that are traded on or cleared through a Financial Market (as defined in Pt 7.2A of the Corporations Act) or a foreign market (whether or not a Regulated Foreign Market (as defined in Rule 1.2.4 of the ASIC Derivative Transaction Rules (Reporting) 2013)) should not be included in the calculation However, we would ask for greater clarity around the definition of "entered into in Australia" used to calculate the threshold for foreign financial entities in line with our comments above.

B2Q4 Do you agree with our proposals for determining whether an Australian financial entity or foreign financial entity is a clearing entity, and when a clearing entity ceases to be a clearing entity?

Some members have suggested that the proposal may create the incentive for a clearing entity to close out trade positions on the last day of a quarter, in order to remain below the threshold. Though more complicated to track, calculating the notional outstanding as the average over a period of time may be a more effective anti-avoidance measure that discourages entities from closing out positions on the last day of the quarter.

Please see also the response to B2Q1with regard to nexus concerns.

B2Q5 Do you agree with our proposal to apply the clearing requirements on the first Monday three months on or after the second calculation date?

Members have no objection to this timeline, although buy-side firms may feel pressured to conclude client clearing arrangements within this time frame.

B2Q6 What is the likely impact of our proposals?

Members are concerned that certain entities may actively trade around quarter-end positions to remain below the threshold.

B3Q1 Do you agree with the proposal to apply the clearing requirements in each of the circumstances listed in proposals B3(a)(i)–B3(a)(v)?

ISDA members disagree with proposals B3(a)(iii) and B3(a)(v) to include nexus derivatives transactions as part of mandatory clearing. The inclusion of nexus transactions in ASIC's proposed mandated is unprecedented and is internationally inconsistent. It would introduce conflicts with other mandatory clearing regimes, and create unnecessary complexity and regulatory burden.

As written, the proposal covers transactions entered into by two FCEs, where either one of the entities books the trade in Australia, enters the trade in Australia or, if it has opted-in to the nexus test, conducts a nexus derivative. This means whenever an FCE enters into a trade with another FCE, in order to determine whether the trade falls within the mandatory clearing scope, it will not only have to determine whether the trade was "entered into" by itself in Australia, but will also need to establish whether the trade is "entered into" in Australia by its counterparty. Practically, the only way in which a foreign clearing entity can establish the latter aspect is through reliance on its counterparty's determination. This does however mean that the

FCE will be exposed to regulatory breach if the determination of its counterparty is incorrect, which is a highly undesirable outcome from a compliance perspective. . Accordingly, we strongly request that the scope is restricted such that a trade between two FCE's will only be in-scope where either party books the trade into Australia.

If this is not acceptable to ASIC, we request that ASIC includes a "safe harbour" provision to protect against where an FCE has relied on a representation from another FCE that a trade was not entered into in Australia (i.e. where two FCEs have entered into an in-scope trade together and one of the FCEs ("**FCE One**") has relied on a representation from the other FCE ("**FCE Two**") that the trade was not entered into in Australia by FCE Two but then FCE One finds out post trade that FCE Two did in fact enter into the trade in Australia).

The lack of access to a common, recognized clearing house between two offshore entities to clear AUD derivatives may also result in compliance issues and AUD derivatives market activity being reduced or gravitating offshore to service foreign based clients, who would not be impacted by the nexus clearing obligation. Mandating clearing for these transactions should fall under the responsibility of relevant regulators in the jurisdiction into which they are booked. The ability to enforce and supervise mandatory clearing of two offshore entities may also prove challenging. (See also our response to B1Q1.) Additionally, there may be timing issues, for example if some jurisdictions have not completed the implementation of their mandatory clearing regimes by the commencement of central clearing in Australia.

B3Q2 Do you agree with our proposed definition of 'foreign internationally-active dealer'?

Members have inquired as to the rationale for including swap dealers or security-based swap dealers in the scope, in addition to clearing entities, as their position is that the clearing mandate should only apply to transactions between Australian clearing entities and foreign clearing entities where they are above the clearing threshold. However, if Treasury and ASIC continue to push for the requirements to extend to OTC derivative transactions entered into between FCEs and FIADs then they should only do so where the in-scope transaction is booked in Australia by the FCE.

B3Q3 Do you agree with our proposed approach to defining 'nexus derivative', and to allow foreign clearing entities to opt-in to centrally clear nexus derivatives?

With respect to approach defining 'nexus derivative' please refer to our response to B3Q1 above. In addition we would ask ASIC to clarify which entities it will expect will rely on the opt-in-arrangements and how will members have comfort that the ASIC opt-in arrangements will be sufficiently equivalent to gain the benefit of substituted compliance and not have to clear under

two separate jurisdictions (since we understand that the opt-in arrangements have been included for the purposes of allowing members to have the benefit of substituted compliance provisions with overseas jurisdictions). There may be practical challenges with foreign entities opting into arrangements under the Australian clearing rules to benefit from substituted compliance provisions in respect of nexus derivatives.

B3Q4 Do you see any practical challenges for clearing entities trying to determine whether they are trading with an entity that is subject to the clearing requirements in each of the circumstances listed in proposals B3(a)(i)–B3(a)(v)?

ISDA members foresee potential challenges in determining whether their counterparties are subject to the clearing requirements or not, given that the entities subject to the clearing requirements may change over time (based on quarterly eligibility or entities may voluntarily opt-in). We believe tracking of this 'active' list will be operationally challenging. To resolve this challenge, some ISDA members would prefer ASIC to allow legal reliance on ASIC's published list of which entities are subject to mandatory clearing only. This places the obligation to clear on each individual entity. The practical challenges of ensuring the clearing status of the counterparty at the point of trade (which impacts pricing) may also need to be addressed through such industry-led solutions as ISDA Amend.

However, even if there was a public list of FCEs and ACEs, due to the current inclusion of nexus transactions, it will not be straight forward for FIADs to determine on a pre-trade basis which of its in-scope transactions with an FCE will be subject to the Australian clearing mandate and which will not. This may necessitate significant changes to global practices for global banks.

B3Q5 What is the likely impact of our proposals?

Please refer to our response to B3Q1.

B4Q1 Do you agree with the proposed definitions for 'swap', 'fixed-to-floating swap', 'basis swap', 'forward rate agreement' and 'overnight index swap' in the draft derivative transaction rules (clearing) attached to this paper?

ISDA agrees with the proposed definitions in the draft derivative transaction rules.

B4Q2 Do you agree with the proposed asset class specifications in proposal B4(a)and Table 2?

ISDA does not believe it is appropriate to designate AUD denominated FRAs as clearable at this stage given no licensed CCPs are clearing this product and there is limited development of pre-existing voluntary clearing in this product. We are of the view that to market participants should

at least have two licensed or prescribed CCPs upon which to clear a product, prior to it being mandated for clearing.

In addition, we do not believe it is appropriate to designate OIS denominated in AUD as clearable at this stage, as clearing of this product is only possible via one licensed CCP and members have stated that they consider it anti-competitive to mandate a product where there is only one CCP available to meet the clearing obligation. Furthermore, only those products that are clearable in at least two CCPs is crucial to business continuity, and recovery and resolution considerations relevant to CCPs. From this perspective, it is important that in the event of CCP default that there are other CCPs which will be offering clearing of the same products.

B4Q3 Do you agree with our proposal that mandatory central clearing should only apply to the entry of an arrangement that is a derivative (other than in the circumstances outlined in proposal B7)?

Members are supportive of this proposal.

B4Q4 Do you agree with our proposal to mandate central clearing of AUD-denominated forward rate agreements? If not, why not?

Members have noted that mandatory clearing of AUD-denominated forward rate agreements is inconsistent with ESMA mandatory clearing requirements which do not mandate AUD and JPY FRAs. ISDA understands that AUD FRA is not currently cleared at any CCPs. We are of the view, therefore, that it would be better to exclude AUD FRA from the current scope, since there is no clarity as to how and when AUD FRA would be made mandatorily clearable by ASIC once a CCP has offered to clear this product. We also note that if only one CCP is able to clear AUD FRA, there will be some industry participants who may not have a clearing relationship with that CCP and require additional time to adapt to mandatory clearing. . We also highlight the consideration raised in B4Q2 with regard to business continuity and CCP recovery and resolution such that mandated for clearing products are available to clear n at least two CCPs.

B5Q1 Do you agree with our proposal to require clearing entities to clear each clearing transaction through a clearing facility?

Members are in general agreement with the requirement. This is predicated on ASIC continually endeavoring to ensure that there is always a minimum of two clearing facilities able to clear each mandatorily clearable transaction and that each clearing facility would be treated as a QCCP for regulatory capital purposes.

B5Q2 Do you agree with the proposed definition of 'cleared through' a clearing facility in the draft derivative transaction rules (clearing) attached to this consultation paper. Do you agree with our proposal to allow direct, indirect or client clearing arrangements to be used?

The "cleared through" definition should accommodate clearing arrangements in foreign jurisdictions that adopt an agency model for clearing (for example the FCM model in the US). Our understanding from the Consultation Paper is that ASIC does intend this to be the case (however this does not appear to be reflected in the draft rules). Confirmation of this should be provided specifically for those foreign jurisdictions in which the Treasury has prescribed CCPs and jurisdictions that ASIC intends to prescribe CCPs for the purposes of alternative clearing under the draft rules. Without such confirmation, the clearing entity will not be able to satisfy the requirement to clear and be considered in breach of the clearing provision (as a consequence of the clearing model being used). Draft rule 2.1.1 covers clearing based on the principal model (as opposed to agency) where each Clearing Entity is a participant at the CCP and where each Clearing Entity is not a participant at the CCP but instructs a participant to clear on its behalf.

B5Q4 Should the derivative transaction rules (clearing) impose a prohibition on derivative transactions being de-cleared after they have been centrally cleared? If so, are there any circumstances where a mandatorily-centrally cleared derivative transaction should be permitted to be de-cleared?

ISDA and the industry strongly believe that CCPs should run regular compression cycles to reduce the volume of economically redundant trades in the clearing house and to reduce margin burdens and capital charges for clearing members. The process of portfolio compression can require the de-clearing of certain trades in order to achieve the greatest compression efficiency. ISDA believes that the greater good achieved through this risk reduction justifies the possibility of de-clearing a comparably small number of trades.

B6Q1 Do you agree with our proposed deadline of T+1 for the clearing of clearing transactions?

The time given to clear a trade to comply with ASIC clearing and alternative clearing in a foreign jurisdiction should be consistent. (Currently T+1 compared to T+3). If nexus trades continue to remain in-scope, there needs to be additional thought given towards the clearing timeline when the trades are being booked on a foreign balance sheet.

B6Q2 Do you agree with our proposal that the deadline for clearing be calculated according to business days and AEST or AEDT, as applicable in Sydney, Australia?

Members have some concerns that if nexus trades continue to remain in-scope, these trades would likely be booked to a US or EU balance sheet and, if cleared at one of the alternative clearing facilities in a foreign jurisdiction, it may be more appropriate for the deadline to be calculated according to the T+1 business day close in the jurisdiction of the clearing facility. This obviates the scenario in which there is a public holiday in the jurisdiction of the clearing facility, but not in Sydney, on T+0 or T+1 that could result in the Sydney deadline passing before the trade can be cleared.

B6Q3 If you believe the deadline should be based on the time the derivative transaction was entered into (e.g. 24 hours after the derivative transaction was entered into), how should the deadline for clearing be determined if the derivative transaction is entered into on a cross-border basis by two counterparties located in different time zones?

Some members put forward an alternative proposal to use the later in the day time zone as the location and time from which the clock starts ticking to clear the trade in order to facilitate compliance.

B6Q4 Do you agree with our proposal that the clearing requirements will not be breached if a clearing transaction is not cleared and is terminated before T+1?

We are in agreement with this proposal.

B7Q1 Do you agree with our proposal that mandatory central clearing be applied in the circumstances outlined above?

We are in agreement with the anti-avoidance objective of the proposal, although some members have pointed out that there are no similar requirements under the regulations of other jurisdictions that if a legacy, non-centrally cleared derivatives transaction between two clearing entities that would otherwise have been subject to the clearing mandate is amended after the commencement date of mandatory clearing such that the maturity of the transaction is extended by 12 months or more beyond the maturity of the transaction at the time it was entered into, then that amended transaction should be subject to the application of mandatory clearing. Members further believe that it would be relatively costly to adapt IT systems to capture such changes.

B7Q2 Do you agree with our proposal that a derivative transaction that is extended for 12 months (or more) should become subject to the clearing requirements? If you believe the

period should be longer, please give reasons why a derivative transaction would need to be extended for a period of 12 months or more.

Please refer to B7Q1 above.

C1Q1 Do you agree with our proposal to allow clearing entities to be cleared through licensed CS facilities or prescribed CCPs?

We would strongly encourage ASIC and the Treasury to work on prescribing as many CCPs as possible to allow for sufficient competition and prevent risk being focused through a small number of CCPs. Our comments regarding business continuity, recovery and resolution considerations described above equally apply here to highlight the importance of mandating products for clearing that are offered in at least two CCPs.

D1Q1 Do you agree with our proposal to allow any clearing entity to comply with mandatory central clearing by using alternative clearing? If not, do you think the scope of our proposal should be narrower (e.g. restricted to foreign clearing entities)?

We are supportive of this proposal and note that the list of prescribed CCPs is currently set out in the draft regulation together with a mechanism for ASIC to prescribe further CCPs. ASIC should ensure that when making such determinations, there is sufficient choice for market participants as part of the exercising these powers of prescription. If ASIC has a list of additional CCPs it is intending to prescribe, these would be useful for industry to know as much as possible in advance. As highlighted by ASIC, it agreed along with others in April 2013 that clearing requirements should generally not apply to derivative transactions already subject to mandatory clearing in another jurisdiction except where:

a) a category of counterparty or products are exempt from mandatory clearing in one jurisdiction but not another; and
b) a product is subject to mandatory central clearing in one jurisdiction but not another.

This principle does not accord with the additional requirement proposed by ASIC that the transaction also has to be cleared via a prescribed or licensed CCP. The inclusion of this additional requirement undermines including an alternative clearing provision. This is especially true given the limited number of CCPs licensed or prescribed under the regulations. We also note it is not consistent with the approach taken in EMIR under Article 13. Article 13 equivalence looks at the equivalence of the clearing requirements and does not include further specific venue requirements.

At a minimum the Australian clearing requirements should allow for a foreign entity that is required to clear a particular transaction under substantially equivalent rules to be able to clear such transaction on any CCP permitted under such substantially equivalent rules.

D1Q2 Do you believe that access to alternative clearing would assist clearing entities to meet their clearing requirements?

Please refer to D1Q1 above.

D1Q3 What is the likely impact of our proposals?

Many FIADs and FCEs incorporated in jurisdictions that Australia considers equivalent may not have access to the limited list of prescribed or licensed CCPs. By mandating that these entities clear on a smaller number of CCPs than they are currently able to clear on under the equivalent foreign legislation will effectively prevent them trading with ACEs or FCEs. This will not result in a competitive environment and potentially increased costs / reduced liquidity.

D2Q2 Do you agree with our proposal that derivative transactions using alternative clearing must be cleared through a licensed CS facility or prescribed CCP?

Please refer to our response to D1Q1 above.

E1Q1 Do you agree with our proposal to allow an exemption from the clearing requirements for intra-group derivative transactions?

The flexibility that the exemption offers is welcomed.

We note that the current exemptions from the clearing requirements do not contemplate or exempt derivative transactions entered into by sovereigns, central banks, international multilateral development banks or the Bank for International Settlements. In view of the governmental, policy and developmental functions of such public bodies, we believe that it would be appropriate for ASIC to exempt sovereigns, central banks, international multilateral development banks (e.g. Asian Development Bank, World Bank, European Bank of Reconstruction and Development) and the Bank for International Settlements from the clearing requirements, and such exemption would be consistent with the approach of other jurisdictions such as the European Union, the United States and Singapore.

E1Q2 Do you have any feedback on the notification requirements?

Where the intra-group exemption is relevant such that notice is to be provided, we do not think that such notice should have to be provided 1 Business Day prior to the transaction. Instead, to retain the ability to hedge or execute trades if and when needed, providing a notification on a post- transaction basis would be the better approach. This also gives certainty to ASIC that one transaction has occurred (and an intention that others will follow in the future) as opposed to before the event/first transaction where a change of circumstances could mean that the clearing transaction does not proceed.

E2Q1 Do you agree with our proposal to allow an exemption from the clearing requirements for transactions that are created as part of a multilateral trade compression cycle? Are there any conditions that should be placed on this proposed exemption?

Referring to B5Q4 above, we are extremely supportive of this exemption and request that the exclusion is expanded to also cover bilateral compression processes.

New and amended trades that result from systemically risk-reducing processes such as compression, be it via a multilateral trade compression cycle or a bilateral compression processes, should not be subjected to the clearing mandate where the original trades were themselves not subject to the clearing mandate. If these post-trade risk reduction trades are not exempted this would act as a significant disincentive for firms to participate in both multilateral and bilateral compression exercises, and introduce new pricing risks for market participants. In addition, subjecting resultant trades to the clearing obligation could also undermine other risk mitigation requirements faced by foreign clearing entities such as under EMIR.

E2Q2 Do you agree with our proposal not to allow an exemption from mandatory central clearing for bilateral compression exercises?

We disagree with the proposal and believe that an exemption from mandatory clearing is justified. Bilateral compression exercises also accomplish the greater good of reducing the amount of risk in the system and should be encouraged. We note further that the types of counterparties that would enter into bilateral compression are also likely to be the types of entities subject to BCBS-IOSCO OTC margining requirements so new OTC trades coming out of bilateral compression exercises will still be subject to collateral requirements.

F1Q1 Do you agree with our proposal to require entities to notify us when they become, or cease to be, a clearing entity? If not, why not?

We are supportive of this proposal.

F1Q2 If proposal F1(a) is implemented, should ASIC publish a list of clearing entities on an ongoing basis, based on the notifications provided to us? Are there any practical benefits in ASIC publishing a list based on notifications from clearing entities (taking into account existing industry mechanisms for providing notifications about an entity's regulatory status)?

Referring to B3Q4 above, members believe that it is imperative that ASIC publish on an ongoing basis a list that can be relied upon of clearing entities.

F2Q1 Do you agree with our proposal to require clearing entities to maintain records demonstrating compliance with the clearing requirements for a period of five years?

We are supportive of this proposal.

F2Q2 Do you agree with our proposal to require clearing entities to provide us with these records upon our request? If not, why not?

We are comfortable with this proposal on the basis that it allows for records to be provided in a reasonable time frame. However, members would like to understand the scope of the obligation and are concerned about duplicative obligations under existing rules and legislation and where ASIC has access to records through its license conditions with CCPs.

F2Q3 What is the likely impact of our proposals?

G1Q1 Do you agree with the proposed commencement date of 7 March 2016 for mandatory central clearing (for those entities that are at or above the clearing threshold as at 30 September 2015 and 31 December 2015)?

EEA entities would seek a relief period until EMIR IRS clearing obligations are enforceable for the same product scope and the same clearing entities in order to be consistent with the alternative clearing principles. EMIR clearing obligations are expected to be applicable later than ASIC clearing obligations. As such we would request that if EMIR timelines are delayed that ASIC looks to align its effective date for the clearing requirement. We note also that the draft timeline calls for commencement 3 months following the clearing threshold calculation date. For 31 December 2015, this would be 31 March 2016, which may be closer to the start date for EMIR clearing obligations.

ISDA®

Once again, ISDA is grateful for the opportunity ASIC has given us to respond to the consultation paper and welcome further dialogue with ASIC on any of the points we have raised.

Yours faithfully

For the International Swaps and Derivatives Association, Inc.

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