ISDA Safe, Efficient Markets

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3 July 2015

Dear Sirs,

Exposure Draft of the Corporations Amendment (Central Clearing and Single-Sided Reporting) Regulation 2015 – Comments on Single-Sided Reporting

The International Swaps and Derivatives Association, Inc. ("**ISDA**") appreciates the opportunity to provide comments on the exposure draft of the Corporations Amendment (Central Clearing and Single-Sided Reporting) Regulation 2015 ("**Regulation**") published by the Treasury on 28 May 2015.

Since 1985, ISDA has worked to make the global over-the-counter ("**OTC"**) derivatives markets safer and more efficient. Today, ISDA has over 800 member institutions from 67 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.

ISDA is actively engaged with providing input on regulatory proposals in the United States (the "**US**"), Canada, the European Union (the "**EU**") and Asian jurisdictions, including Singapore and Hong Kong, among others. Our comments are derived from this international experience and constant dialogue, and reflect the views of both firms in the Asia-Pacific region and from further afield. As OTC derivatives tend to be cross-border in nature, we wish to highlight the importance of ensuring that regulatory proposals have a consistent domestic and cross-border effect, so as to not disproportionately impact any one sector of what is a

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global market. Noting also that the intent of the regime is to have an overall deregulatory impact, our members feel that amendments to certain elements of the Regulation would assist in ensuring that the regulatory benefits of a simplified reporting regime clearly outweigh the regulatory burden that such a regime creates.

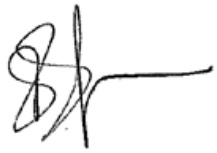
In the spirit of consistent reporting requirements, we also wish to note recent industry efforts to promote data harmonisation on a global basis through the release of the ISDA white paper, *Improving Regulatory Transparency of Global Derivatives Markets: Key Principles*, which was recently endorsed by 10 other global trade associations in a letter to 18 international regulators and legislatures. We would encourage the Treasury to give further thought to ways in which it could maximise harmonisation of its intended regime with other reporting regimes globally, particularly through Principle 1, which states that 'Regulatory reporting requirements for derivatives transactions should be harmonised within and across borders' through the issuance of consistent reporting requirements across jurisdictions.

We are appreciative of the opportunity to provide input on the Regulation, which will assist reporting entities in preparing for compliance with their reporting obligation. We aim to continue to facilitate the dialogue between the industry and regulatory authorities in Australia to address implementation issues that may arise from single-sided trade reporting. In this regard, ISDA is undertaking an initiative to assist reporting entities to make representations as to their classification under the regime, to enable a smooth identification and adoption of reporting mechanics in various trading scenarios.

Our comments in this letter only address the aspects of the Regulation relevant to single-sided reporting and not the aspects pertaining to central clearing, which will be sent by way of letter to the Treasury and the Australian Securities and Investments Commission (**"ASIC"**). We set out our response along thematic lines followed by recommendations, with some specific drafting comments in addition. We would be happy to discuss this letter further.

Yours faithfully

For the International Swaps and Derivatives Association, Inc.



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COMMENTS ON THE EXPOSURE DRAFT OF THE REGULATION

GENERAL COMMENTS

1. Intended Deregulatory Nature of the Regime

1.1. While appreciating that the intent of the proposed regime is to result in an overall deregulatory impact, particularly for phase 3 reporting entities, our members remain concerned that in practice, preparation for implementation of the regime as proposed will result in a complex array of counterparty representations, transaction-level mechanics, legal risks, considerations and agreements, and uncertainty regarding whether the exemption is applicable on an ongoing basis. Phase 3 reporting entities may also experience difficulties in reporting position information generally, despite the 6-month grace period for complying with this proposed requirement.

1.2. Because availability of the exemption is determined by the counterparty's status (as opposed to the status of the phase 3 reporting entity), this may have the effect of actually creating a greater amount of regulatory burden for these entities than what may have been experienced if they were required to report the entirety of their transactions under a regime that further incentivised and promoted delegated reporting. On that basis, as a general comment, we would urge the Treasury to give consideration to redrafting the Regulation in a way that results in a simple, easy-to-implement, effective regime. We set out our rationale below.

1.3. We note that Treasury has limited scope within which it can grant exemptions for phase 3 reporting entities – that is, where the counterparty is required to report, or does report, the relevant transaction. However, due to the fact that the Regulation does not grant an overall exemption from reporting, phase 3 reporting entities will need to ascertain, from each counterparty they transact with, on a trade-by-trade basis, whether that counterparty:

- is also a phase 3 reporting entity or not;
- is subject to an Australian reporting requirement, or has in fact reported the relevant transaction;
- is willing to, and has otherwise, reported the relevant transaction under the ASIC Derivative Transaction Rules (Reporting) 2013 ("**Australian trade reporting rules**"); or
- is subject to reporting requirements in one or more foreign jurisdictions that are substantially equivalent to requirements under the Australian trade reporting rules, has reported the relevant transaction to a trade repository

prescribed under Regulation 7.5A.30 of the Corporations Regulations or ASIC Prescribed Trade Repositories Determination 15-0591, and has 'tagged' the transaction as being reportable under the Australian regime.

1.4. At the trading relationship level, this requires, at the very least, the phase 3 reporting entity to engage with every trading counterparty (both domestic and international) to ascertain whether in fact that counterparty meets one of the criteria above, and to create systems, processes and procedures to account for both the circumstances when its counterparty has reported a relevant transaction, and when the phase 3 reporting entity retains the requirement to report a relevant transaction. This may potentially discourage phase 3 reporting entities from trading with counterparties who do not meet one of the criteria above, prejudicing best execution.

1.5. At the transaction level, this also means that if even one of the phase 3 reporting entity's counterparties were unable to satisfy any of the above criteria, the phase 3 reporting entity would retain the requirement to report. This would necessitate costly investment in reporting systems, processes and procedures, trade repository onboarding and human resources for compliance. This would seem to be at odds with what we understand forms at least part of the intent of the regime – to relieve phase 3 reporting entities of the regulatory burden of reporting to the maximum extent possible, under a simplified reporting regime for these entities.

1.6. Investment in reporting systems, processes and procedures, trade repository onboarding and human resources are sunk costs that are incurred once, as soon as a transaction is required to be reported by a phase 3 reporting entity, and cannot be recovered. Therefore, in order to avoid these implementation costs, we request that consideration be given to designing a regime which has the practical effect of reducing outlays (current and projected) and regulatory burden for phase 3 reporting entities, and to this effect we set out our suggestions in section 4 below.

1.7. Even if a phase 3 reporting entity's counterparty did report transactions, provisions of the Regulation as drafted would appear to require the phase 3 reporting entity to conduct checks on each of those transactions, to ensure that they had in fact been successfully reported. At a practical level, this may require the phase 3 reporting entity to incur the costs of onboarding with the trade repository used by its counterparty, and to employ resources (both human and IT) to conduct the necessary verifications. This again would seem to place undue burden on a phase 3 reporting entity. We recommend, as stated in section 4, that phase 3 reporting entities instead be permitted to rely on an undertaking by its counterparty to report, by way of written arrangement or representation.

2. Level Playing Field Considerations

2.1. We wish to note that a phase 3 reporting entity's counterparty (usually a bank or dealer) may have difficulty in taking on reporting obligations, particularly when that counterparty does not have an obligation to report under the Australian regime (either by virtue of not being a reporting entity under the Australian trade reporting rules, or by virtue of a particular transaction not being reportable under the Australian trade reporting regime). In the case of a foreign entity that does not have an obligation to report under the Australian trade reporting regime, ensuring that its phase 3 reporting entity client can benefit from the exemption (which would only occur if the foreign entity did report the transaction in compliance with the requirements in the Regulation) may require:

- onboarding at a trade repository prescribed under Regulation 7.5A.30 of the Corporations Regulations or ASIC Prescribed Trade Repositories Determination 15-0591;
- entering into a delegated reporting agreement with the phase 3 reporting entity (or agreeing to 'voluntarily report');
- incurring the potential doubled cost of reporting the relevant transaction under the requirements of a foreign jurisdiction and also 'tagging' the relevant transaction as being reportable under the Australian trade reporting rules; and
- managing trade repository validation processes, including potential numerous error reports where the trade repository is only able to validate a transaction report against the foreign jurisdiction's data requirements (and not the Australian trade reporting data requirements).

2.2. Particularly for transactions which neither bear any Australian nexus nor are booked in Australia by a foreign entity with no Australian reporting obligations, the above requirement for these transactions to be 'tagged' presents a significant degree of operational complexity and difficulty, and one that potentially places foreign entities at a competitive disadvantage to firms that have Australian reporting obligations – so much so that in current circumstances in may make more practical sense to invest in direct reporting to a licensed trade repository, under the Australian trade reporting rules. But for the competitive distortion that the Regulation potentially generates, these arrangements and large costs would not need to be borne by these entities.

2.3. Where the foreign entity is a foreign reporting entity, the requirement for transactions which do not constitute 'Reportable Transactions' under the Australian trade reporting rules to nevertheless be reported under the conditions in the Regulation in

order to gain the benefit of the exemption similarly presents significant operational challenges. Such trades would not necessarily be within the oversight or reach of the foreign reporting entity's operations in Australia, falling outside of what is required to be reported under the Australian trade reporting rules. Therefore, expanding the scope of what the foreign reporting entity must report in order for the exemption to be fulfilled would appear to counter the rationale and efficacy of the existing Australian trade reporting regime and the express application to the scope of Reportable Transactions based on counterparty type and connection to Australia.

2.4. A separate example of limitations to the Regulation includes the international clearing context. Phase 3 reporting entities wishing to clear OTC derivative transactions at overseas clearing houses will be dependant on the clearing model, and in some cases, the clearing house, to report transactions. In most cases, such international clearing houses are not subject to the Australian trade reporting rules and may not undertake reporting obligations on behalf of the client.

2.5. A phase 3 reporting entity would be exempted from reporting if its foreign entity counterparty was willing to offer a 'delegated' or 'voluntary' reporting service (by reporting additional trades as an additional obligation), but this is a commercial proposition that must be considered alongside the regulatory and legal risk and characterisation of such a service. In particular, we note that 'delegation' of reporting to a foreign entity with no Australian reporting obligations carries a degree of legal risk, whereby sufficient comfort does not currently exist to mitigate the risks that the foreign entity faces in circumstances where it may not be able to report a particular transaction, or it breaches Australian trade reporting requirements. We discuss this in further detail in section 3 below.

2.6. In practice, this complexity for foreign firms to report in compliance with the various limbs and conditions of the Regulation means that phase 3 reporting entities may find it operationally simpler to transact only with counterparties who have direct Australian reporting obligations and are required to report all transactions, thereby having certainty of the ability to avail themselves of the exemption from reporting. This may prejudice best execution and in any case may not be practicable in the case of a global investment mandate, resulting in a similar situation whereby either the phase 3 reporting entity is required to build infrastructure to report, or must otherwise ensure that the foreign entity does report under the Australian trade reporting rules.

2.7. Indeed, we have been advised by some of our members that this may already be happening in practice, ahead of finalisation of the regime. Feedback received indicates that some phase 3 reporting entities, particularly domestically-domiciled funds, are amending (or actively considering amending) their mandates such that their investment managers will only permitted to deal with counterparties that have

Australian reporting obligations under the Australian trade reporting rules. Thus, the Regulation as drafted could operate to restrict and redirect the activities of phase 3 reporting entities, incentivised by factors that are less relevant to the operation, liquidity and efficiency of the financial markets, the economy and doing business.

2.8. We submit that this potential competitive distortion would not be a desirable outcome, nor be in the interests of maintaining a level playing field for all entity types under the Australian trade reporting regime. Aside from the potential competitive distortions, market distortions may also occur through concentration of risk into domestic entities, as phase 3 reporting entities may be incentivized to make trading decisions based on counterparty type, to enable their continuous reliance on the exemption. On a broader scale, this may have the effect of restricting access of international liquidity to phase 3 reporting entities, and vice-versa. Such pooling and fragmentation of liquidity along geographic lines, following the trade reporting obligations of the counterparty, should be avoided at all costs.

3. Safe Harbour for Foreign Entities and Phase 3 Reporting Entities

3.1. We understand that in relation to preliminary feedback, the Treasury is willing to consider adding 'safe harbour' provisions in the Regulation to give phase 3 reporting entities comfort when their counterparty to a transaction reports or agrees to voluntarily report. Our members are supportive of this proposal, however we would also note that one roadblock to a wider delegated reporting offering by firms (particularly larger financial institutions and dealers) remains the potential consequences of not being able to report a transaction on behalf of a delegating phase 3 reporting entity or inadvertently breaching the reporting requirements, which exposes the delegate itself to legal risks for which there do not appear to be any protections.

3.2. Delegated reporting risks are particularly pronounced in the case of foreign entities offering a commercial, voluntary service to their phase 3 reporting entity clients, as following the requirements as currently proposed in draft subregulation 7.5A.71(3) may require a delegated reporting agreement to be concluded between the two entities. However, legal characterisation and allocation of legal risk and liability of such delegation arrangements remains unclear (particularly where trades are not reported or reported in breach of the requirements).

3.3. We note a number of situations where a trade may not be able to be reported, such as system or process failures (either at the dealer or trade repository level) or force majeure events. Inadvertent breaches of the reporting requirements may also present a large degree of legal risk of enforcement action, potentially even in situations where the foreign entity does not have any Australian reporting obligations.

3.4. Our members seek additional clarification on what legal obligations the delegate would retain as well as what legal obligations the phase 3 reporting entity would retain in the above circumstances, with the aim of ensuring that the proposed safe harbour provisions for phase 3 reporting entities do not result in an automatic transfer of legal risk to reporting delegates. Indeed, we propose that there would be value in a legal safe harbour provision not only for phase 3 reporting entities exempt from reporting, but also for the agents (including investment managers) they appoint to report on their behalf, as well as their foreign entity counterparties that actually do the reporting under this regime.

3.5. Such safe harbour should include substantial mitigation or removal of legal liability for a foreign entity for not reporting or incorrectly reporting despite reasonable efforts to avoid doing so, including specifically covering obligations arising through reporting additional transactions (that are not Reportable Transactions of a foreign reporting entity) and 'voluntary' transactions of a foreign entity. In this regard, we would also be grateful if the Treasury could make clear whether and how, in the context of the Regulation, the protections provided under s907C of the Corporations Act would apply to all entities, both Australian and foreign.

4. Recommendations

Foreign Entity Reporting

4.1. In order to alleviate phase 3 reporting entities of the regulatory burden and significant costs of trade repository onboarding, system connections, self and counterparty representations, and investment in human and compliance resources, we urge the Treasury to consider implementation of a regime whereby the conditionality of the exemption focuses more on the phase 3 reporting entity's status, as opposed to that of the counterparty. Lessening or even removing this conditionality within the exemption will greatly assist these entities to manage their costs and implementation arrangements to prepare for single-sided reporting.

4.2. In relation to this conditionality when transacting with a foreign entity (whether or not a foreign reporting entity), we consider that the goals of regulatory transparency and mitigating systemic risk will remain fulfilled where a transaction is reported to any prescribed trade repository globally, and the requirement for a transaction to be 'tagged' only relates to transactions 'booked' or 'entered into' in Australia.

4.3. However, due to the core functionality limitations at the trade repository level noted in paragraph 2.1, 'tagging' currently remains an unviable and unworkable solution for many foreign entities, due to the severe operational complexity of managing a large number of validation fails and error reports generated for each transaction designated as reportable under the rules of more than 1 jurisdiction. This may change

in the future, however as an interim measure we propose an alternative for these entities whereby they may choose to report these transactions 'booked' or 'entered into' in Australia to a licensed trade repository instead.

4.4. In other words, we propose that a phase 3 reporting entity be exempt from reporting where it transacts with a foreign entity (whether or not a foreign reporting entity) that:

i. is subject to reporting requirements in one or more foreign jurisdictions that are substantially equivalent to requirements under the Australian trade reporting rules, and:

ii. reports information about transactions to a facility prescribed under subregulation 7.5A.30(2) of the Corporations Regulations or ASIC Prescribed Trade Repositories Determination 15-0591 and designates transactions 'booked' or 'entered into' in Australia as information that has been reported under the Australian trade reporting rules; or;

iii. reports OTC derivative transactions 'booked' or 'entered into' in Australia to a licensed trade repository where 'tagging' is not undertaken.

4.5. Such a regime would better enable foreign entities to offer liquidity to phase 3 reporting entities (and equally, provide freedom of choice of liquidity sources to phase 3 reporting entities) on the same basis as Australian entities, and without potential competitive distortions.

4.6. We note that this proposal would mean that a subset of internationally-conducted transactions with phase 3 reporting entities would not be reported or 'tagged' under the Australian regime. However, providing an exemption on the basis of paragraph 4.4 above does not necessarily mean that these transactions remain unreported. There should remain a sufficient level of comfort (for phase 3 reporting entities and other interested parties) that systemic risk, market oversight and market integrity considerations in such a scenario would not be adversely impacted, as these transactions will in most cases be reported in a foreign jurisdiction considered to be 'substantially equivalent'by the foreign entity. The removal of the requirement to 'tag' or report transactions that are not 'Reportable Transactions' of foreign entities should therefore not automatically be construed as an accumulation of unreported systemic risk to the financial markets by foreign entities.

4.7. Providing an exemption on this basis would also save foreign entities the significant cost of managing Australian reporting and tagging architecture for their international trading desks, branches or subsidiaries which transact with phase 3 reporting entities.

Therefore,

i. the overwhelming majority of these transactions would not go unreported globally;

ii. foreign regulators would have and retain oversight and power to investigate such transactions for systemic risk, market oversight and market integrity considerations; and

iii. increased international cooperation between regulators would enable ASIC to investigate these transactions where it considers that systemic risk issues warrant further investigation.

4.8. Indeed, a precondition of prescription of a trade repository under Regulation 7.5A.30 of the Corporations Regulations is that adequate arrangements exist for cooperation between ASIC and an appropriate authority responsible for licensing, authorising or registering the facility as a derivative trade repository in the foreign jurisdiction, and therefore data relating to a relevant transaction could very likely be shared upon request, including data aggregated by counterparty name, Legal Identity Identifier (LEI) or domicile for systemic risk purposes.

Reliance on Written Arrangements

4.9. In place of the consequential requirement to verify the successfully reported status of each transaction, we submit that a regime where the phase 3 reporting entity is able to rely on a counterparty's documented representation regarding its status and the reporting of transactions (without having to exercise routine monitoring of whether the counterparty does in fact report the relevant transaction) will achieve a similar if not identical regulatory outcome, while lessening the compliance burden for phase 3 reporting entities. We therefore request that the Treasury give due consideration to amending the relevant provisions of the Regulation (relating to both transaction reporting and position reporting) to enable phase 3 reporting entities to be able to rely on such documented representations. We would be happy to discuss these proposed drafting amendments further.

Commercial End User Considerations

4.10. While noting the importance of trade reporting as a means of furthering OTC derivatives market transparency globally, concerns regarding market integrity should be also balanced against the fact that phase 3 reporting entities benefitting from the exemption are the smallest sub-category of reporting entities under the Australian trade reporting rules, and have characteristics that are more akin to corporate end-users rather than large financial institutions or banks. In this regard, we do not

consider that the proposed modifications to the construction and operation of the Regulation would give rise to systemic risk, market oversight or market integrity concerns.

Further Assistance

4.11. Generally, we remain open to discussing any of the above issues, as well as any other proposals or measures which would enable:

- foreign entities to continue trading with and offering liquidity to phase 3 reporting entities on similar commercial and legal terms to those of Australian reporting entities;
- the regime for phase 3 reporting entities to be further simplified, at both the regulatory and practical levels;
- the maximum possible reduction of costs associated with reporting; and
- all entity types to mitigate their legal and commercial risks of doing business as much as possible.

5. OTHER REQUESTS FOR CLARIFICATION

5.1. Our members would like to seek further clarification on whether the exemption must be complied with for phase 3 reporting entities, or whether the Regulation applies on a voluntary basis. By way of example, please confirm whether a phase 3 reporting entity would be able to enter into a delegated reporting or 'voluntary reporting' arrangement with a counterparty under which the counterparty would report all trades of the phase 3 reporting entity irrespective of whether those trades could be caught by the exemption and if so, whether this would amount to over-reporting by the phase 3 reporting entity.

6. SPECIFIC DRAFTING COMMENTS

6.1. We request the Treasury consider redrafting the reference to 'Australian entities' under Regulation 7.5A.71(2), and 7.5A.72(2). Our understanding is that paragraph (2)(b)(i) of each Regulation is not limited to Australian-incorporated reporting entities. We further understand that paragraph (2)(b)(ii) of each Regulation could equally apply to non-Australian entities which are not required to report under the Australian trade reporting rules, but choose to voluntarily do so by building direct reporting infrastructure to a trade repository licensed by ASIC and reporting the full set of ASIC data fields (instead of alternative reporting), in order for the phase 3 reporting entity exemption to be realised.

6.2. If the Treasury agrees, we would also urge reconsideration of the term ‘reporting entity’ in Regulation 7.5A.71(2)(b), as these foreign entities will not be reporting entities under the Australian trade reporting rules. We would further request additional clarification in the Explanatory Guide as to the application of Regulation 7.5A.71(2)(b)(ii) (such as whether this is limited to two phase 3 reporting entities transacting, or also extends to foreign entities and foreign reporting entities with no reporting obligation for all or a subset of their transactions with phase 3 reporting entities but who build direct reporting infrastructure to voluntarily report in accordance with the Australian trade reporting rules).

6.3. We would note that if the Treasury agrees with the above points, they would be equally applicable to the same provisions under Regulation 7.5A.72, and consequential amendments to the Explanatory Guide would also be beneficial – such as, for example, including the above circumstances in the guidance under Regulation 7.5A.71.