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OTC Derivatives – Exposure Draft Single-Sided Trade Reporting Regulations

The Financial Services Council (**FSC**) represents Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advisory networks, trustee companies and public trustees. The FSC has over 125 members who are responsible for investing more than \$2.4 trillion on behalf of 11 million Australians.

1. We welcome the opportunity to make a submission on the Exposure Draft *Corporations Amendment (Central Clearing and Single-Sided Reporting) Regulation 2015* (the **Single-Sided Trade Reporting Regulations**). The FSC supports the broad G-20 agenda in relation to OTC derivatives reform and Australia is well progressed in many respects in relation to the implementation of the G-20 requirements.
2. FSC in particular welcomes the Government's decision in relation to providing relief from the OTC derivative trade reporting requirements for organisations that undertake small amounts of OTC derivative activity by allowing 'single-sided' reporting for certain smaller Phase 3 entities. As noted in the Government's 12 December 2014 announcement, this means that the trade reporting compliance burden will mainly fall on larger financial institutions that are systemically important, while still providing regulators with information they need to effectively supervise over-the-counter derivatives markets.
3. It is important that the Single-Sided Trade Reporting Regulations achieve this result, namely that the single sided trade reporting exemption is, as a practical matter, available for these smaller entities. This submission contains necessary changes to the draft Single-Sided Trade Reporting Regulations so as to ensure, particularly in relation to offshore reporting, that smaller entities are not subject to an excessive compliance burden (that is, to ensure the smaller entities – as intended by the Government's policy – will be able to practically avail of the single-sided trade reporting exemption). The feedback from many of our members is that changes are required to the current "ASIC designation/tagging" condition for transactions with foreign counterparties to make the single-sided exemption workable in practice and, in

practice, able to be availed of. **The feedback from many FSC members is that the “ASIC designation” condition (for offshore reported trades), without changes, undermines the practical utility of the single-sided trade reporting exemption.** If this is not rectified, this could force these smaller entities to “over report” and incur the cost of this (the very cost that the Government’s policy seeks to avoid by providing the exemption).

Executive Summary

4. FSC broadly supports the Single-Sided Trade Reporting Regulations except to the extent the ASIC “designation/tagging” requirement for trades with foreign counterparties undermines the practical benefit of the Single-Sided Trade Reporting exemption for trades with foreign counterparties.
5. **The requirement for reporting entities to have trades “tagged/designated” as an ASIC reportable trade, for trades with foreign counterparties, should be removed.** Rather, ASIC should liaise direct with the offshore Prescribed TRs to operationalise whatever ASIC needs for ASIC to be able to access on request trades which otherwise take the benefit of the single-sided trade reporting regime. This is much simpler than requiring small Australian reporting entities to attempt to dictate to major global counterparties the form of reporting that the global counterparty will make (under offshore law) to the offshore Prescribed TR.
6. We applaud Treasury and ASIC for the sensible phase-in/phase-out arrangements (via the use of consecutive qualifying quarters or disqualifying quarters) in relation to assessing whether a Phase 3 entity can avail of the single-sided reporting exemption (i.e. the \$5 billion threshold).

Detail

7. FSC agrees that, in light of the policy, ASIC should have access to single-sided trade reporting data. FSC and our members consider that rather than requiring every smaller Phase 3 reporting entity, for every trade, with every offshore counterparty, for each Prescribed (offshore) trade repository, to ensure that trades reported to the offshore Prescribed TR are “tagged/designated” as an “ASIC” reportable trade, instead ASIC should designate which Prescribed (offshore) trade repositories meet ASIC’s requirements in that regard and then dispense with the “tagging/designation” condition for trades reported to that trade repository. This could be implemented by a prompt amendment to the regulations after ASIC confirms to Treasury that ASIC is satisfied with the arrangements it has in place with the offshore prescribed trade repository to enable ASIC to obtain ASIC reportable trades benefitting from the single-sided trade reporting exemption. Other implementation matters (such as MOUs and any other requirements) would be a matter for ASIC consistent with other OTC derivatives reform ASIC has progressed.
8. **We strongly urge the tagging/designation requirement for trades reported to an offshore Prescribed TR be removed as a condition of the Single Sided Trade reporting exemption. This condition risks severely undermining the utility and benefit of the single-sided reporting**

exemption for trades with offshore counterparties. Instead we request that ASIC liaise direct with offshore Prescribed TRs and once ASIC is satisfied as to an identifier which the Prescribed TR receives under the reporting regime applicable for its jurisdiction and which identifies the trade as being referable to an Australian (Phase 3) entity, that ASIC inform Treasury with a view to Treasury promptly updating the regulations to note that Prescribed TR as a TR for which no tagging/designation condition is imposed in respect of the Single Sided Trade Reporting exemption in respect of transactions with foreign entities.

9. Some detailed comments are in the table below. Most of our comments relate to the single-sided trade reporting exemption as it relates to transactions involving foreign entities and in particular the tagging requirement **which we seek be achieved instead by ASIC** dealing direct with the offshore Prescribed TR and/or offshore regulators as appropriate (rather than imposing this burden on all smaller reporting entities). We agree ASIC should be able to retrieve the single-sided reporting data but this should be achieved by ASIC negotiating this with the offshore TR and agreeing with the offshore TR the applicable identifier/tag to enable the TR to retrieve ASIC reportable trades.

ED Regs Reference	Requirement	Comments	Practical Solutions
Schedule 1, Part 2, 7.5A.71 (3) (pages 10-11 of the ED Regulations)	<p>Exemption – single-sided transaction reporting</p> <p><i>Transactions involving foreign entities</i></p> <p>(b)(ii) reports information about the transaction to a facility prescribed by or under subregulation 7.5A30(2); and</p> <p>(b)(iii) designates the information to that facility as information that has been reported to ASIC under the Derivative Transaction Rules (Reporting)</p>	<p>We understand that the prescribed TRs under 7.5A30 will expire on 30 June 2015 and that ASIC is currently analysing the TRs for re-prescription. While a matter under ASIC consideration, if ASIC only intends to re-prescribe one of the three US TRs being DTCC Data Repository (U.S.) LLC, this impacts on the practical application of the exemption under (b)(ii) for Phase 3 entities.</p> <p>The “tagging” requirement under (b)(iii) raises a number of practical compliance issues:</p> <ul style="list-style-type: none"> - Our members inform FSC that it is not a given that foreign counterparties will agree to tag trades as ASIC trades (even if the offshore TR fields did facilitate that, which is also not a given). Therefore it may not be operationally possible to meet the “tagging” requirement. 	<p>1) Remove the tagging/designation condition for offshore reported trades.</p> <p>2) By way of a safe harbour (in availing of the Single-Sided Trade Reporting Exemption), the Phase 3 entity should be able to rely on a representation by the foreign reporting entity that it is subject to reporting requirements in the foreign jurisdiction and is reporting the transactions (i.e. through ISDA Amend). There should NOT be a condition imposed on the Australian Phase 3 entity to have to ensure the trade which is reported – is tagged/designated as an ASIC trade. We consider it is more appropriate, simpler, efficient and consistent with the policy design, that ASIC work with offshore TRs directly to ensure ASIC is satisfied it can access trade</p>

ED Regs Reference	Requirement	Comments	Practical Solutions
		<ul style="list-style-type: none"> - It would be very resource intensive for Phase 3 entities to ascertain, implement and monitor “tagging” for each foreign entity. - There is the added difficulty for initial and ongoing monitoring when it comes to external investment managers transacting with foreign entities in relation to the “designation/tagging” requirement. - We are not sure that it is possible for Phase 3 entities to check with an offshore Trade Repository (TR) directly that transactions have been reported by the other (foreign) counterparty to the transaction. - What is the result if it is identified that the other party has not reported a transaction? The Phase 3 Entity would not be able to report itself within T+1 to a Licenced TR as required by the Derivative Transaction Rules (Reporting). - There is an added layer of complexity when a Phase 3 entity outsources investment management to an external investment manager. Investment Management Agreements may need to be amended to restrict an external investment manager’s use of counterparties to those that are required to and do report transactions to a Prescribed TR and tag/designate the trade as an ASIC trade (otherwise the Phase 3 entity will need to report to a Licenced TR). 	<p>information from the offshore TR.</p> <ul style="list-style-type: none"> 3) ASIC should work with foreign TRs and regulators to enable transaction information of Australian entities to be reported to ASIC (or be able to be obtained by ASIC). 4) If “tagging” is an issue, the Legal Entity Identifier (LEI) (or some other appropriate identifier) may potentially be used to identify transactions with an Australian entity that need to be reported to ASIC (and this is a matter we urge ASIC to scope out directly with the offshore Prescribed TR). We urge ASIC to work with offshore TRs and offshore regulators (as required) to ascertain an identifier in relation to trades reported under the single-sided trade reporting exemption which enable the TR to identify the trade as an ASIC reportable trade (rather than requiring every Phase 3 entity availing of the single sided exemption to request every foreign counterparty to tag/designate to the offshore TR the trade as an “ASIC” reportable trade).

ED Regs Reference	Requirement	Comments	Practical Solutions
Schedule 1, Part 2, 7.5A.72 (pages 11-12)	Exemption – single-sided position reporting <i>Transactions involving foreign entities</i>	The same general comments above apply in respect of the exemption for single-sided <i>transaction</i> reporting involving foreign entities.	The same practical solutions above apply in respect of the exemption for single-sided <i>transaction</i> reporting involving foreign entities.

10. **As set out above, our members are very concerned about the limiting application of the exemption as it relates to offshore reported trades.** Under the regulations, the Phase 3 entity is held accountable for the counterparty reporting offshore (and tagging/designating the trade as an ASIC reportable trade). We think there should be a safe harbour under which the single sided trade reporting exemption is available provided the Phase 3 entity contracts with the offshore counterparty to report the trade (but not with an ASIC tagging/designation condition). So long as the Phase 3 entity has an agreement with the counterparty and monitors the counterparty as appropriate, that should suffice as a condition for the Phase 3 entity to be able to avail of the single sided reporting exemption.

11. That is, in relation to transactions involving foreign entities, we request a safe harbour for Phase 3 entities relying on the Single Sided Trade Reporting exemption where:

- (a) the Phase 3 entity has an agreement in writing with the offshore counterparty to report trades to an offshore Prescribed TR (but with no condition requiring an offshore reported trade be tagged/designated as an “ASIC trade” – see our submissions elsewhere that instead ASIC work with Prescribed TRs as to what ASIC may require in order to have access to trade information for trades reported to the offshore Prescribed TR); and
- (b) the Phase 3 entity makes regular enquires reasonably designed to determine whether the foreign counterparty is discharging its obligations under the agreement with the Phase 3 entity.

We note this request for a safe harbour to avail of the single sided trade reporting *exemption* simply mirrors the existing safe harbour for *delegation* of reporting under *Derivatives Transaction Rules (Reporting) 2013*, Rule 2.2.7.

12. Where the Phase 3 entity has met the above requirements (under our requested safe harbour above), the Phase 3 entity should have no liability if the offshore counterparty omits to report the trade, provided the Phase 3 entity takes steps to request the counterparty to report such trades which the Phase 3 entity becomes aware has been omitted to be reported. Alternatively, the Phase 3 entity could be able to inform ASIC of this circumstance (rather than be required to connect to an Australian TR to report the omitted trade).

7.5A.71 & 7.5A.72

Australian Entities

13. We would like to see more details and/or separate guidance on what the requirements are in order to qualify for the reporting exemption. For example, can Phase 3 entities eligible for the single-sided trade reporting exemption, make their own assessment as to whether a counterparty is required to report to ASIC or would the Phase 3 entity need to obtain written confirmation of this from the counterparty? It may make sense to leverage the ASIC safe harbour requirements with regards to delegated reporting. We request that the requirements be kept as simple as possible in order not to erode the efficiencies gained from the single-sided approach.

Foreign Entities

14. We think that a similar requirement should apply to foreign entities as to those for Australian entities. That is, the exemption be available where the foreign counterparty is required to report, or does report, in a foreign jurisdiction that has requirements substantially equivalent to the ASIC reporting regulations. As set out above, with regard to ASIC being able to source the reporting provided in the foreign jurisdiction, we urge that ASIC arrange – directly - with the relevant foreign regulators and/or offshore prescribed TRs for this data to be made available to ASIC. To assist ASIC being able to access the relevant data, the Phase 3 reporting entity could supply ASIC with the relevant Legal Entity Identifiers (LEIs) for its reporting entities. This is preferable to having Phase 3 entities arrange counterparties to agree to tag/designate trades as “ASIC” reportable trades (which each Phase 3 entity would need to do on a counterparty by counterparty basis), which will limit the benefits of the single-sided reporting exemption.

Representative Capacity – instead use phrase “Trustee Capacity” and make it clear that an “agent” is not taken to be a party to a transaction

15. We suggest that the definition of *representative capacity* be amended to instead refer to *trustee capacity*. The phrase “representative capacity” may conflate concepts of agency and trusteeship and thereby possibly lead to confusion. By virtue of section 601FC(2) of the *Corporations Act* a responsible entity is to that extent always a trustee.
16. A suggestion is to use the following terminology (including the Note we have drafted) in the Single-Sided Trade Reporting Regulations instead of *representative capacity*:

trustee capacity: an entity is a party to an OTC derivatives transaction, or holds an OTC derivative position, in a *trustee capacity* if the entity is such a party, or holds such a position, in its capacity as the responsible entity for a registered scheme or as the trustee of a trust.

Note: To avoid doubt an investment manager which acts as an agent of a responsible entity or trustee is not taken to be a “party” to the derivative transaction; rather the “party” is the principal (not the agent) being the responsible entity or trustee.

17. FSC does not intend making a submission on the draft ASIC *Derivative Transaction Rules (Clearing) 2015 (Clearing Rules)* but the *representative capacity* point above applies equally to the concept of *representative capacity* in the Clearing Rules. We suggest that the definition of *representative capacity* in the Clearing Rules also be amended to instead refer to *trustee capacity*.

Miscellaneous

18. While FSC members strongly urge Treasury and ASIC to take a different approach in relation to the manner of ensuring ASIC has access to offshore reported data (see above), our members were not sure what suffices to satisfy the “designated” as information reported to ASIC under the Derivative Transaction Rules (Reporting) (e.g. 7.5A.71(3)(b)(iii)). For example if the overseas counterparty reports to an offshore Prescribed TR and the report to the TR included an LEI, can this be regarded as “designated” as an ASIC trade?
19. If the template for the offshore counterparty’s report to the offshore Prescribed TR includes a spare (free text) field, can the trade be designated as an ASIC trade by incorporating “ASIC” on the field?

Conclusion

20. **Nonetheless, our prime concern is that the designation condition (for offshore reported trades) be removed from the regulations and that ASIC instead satisfy itself, direct with the offshore Prescribed TR, as to how – as between that TR and ASIC – ASIC may obtain data on the single sided trade reporting transactions and the applicable identifier to enable that. Failing this, the reality is the benefit of the single-sided trade reporting exemption for smaller Phase 3 entities, when dealing with offshore counterparties, will be significantly undermined, which would be a very unfortunate outcome and inconsistent with the Government’s policy decision to relieve smaller Phase 3 entities from the significant compliance burden which would otherwise apply to them.**

Thank you for the opportunity to make this submission. If you have any questions on our submission, please contact Stephen Judge on (02) 9299 3022.

Yours sincerely



Stephen Judge
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