



Banking and Capital Markets Regulation Unit
Corporations and Capital Markets Division
The Treasury
Langton Crescent
PARKES ACT 2600

31st August 2014

Dear Mr. Lim,

Treasury proposals paper: AUD-IRD central clearing mandate - submission

1. Do you have any comments on the specific benefits and costs of complying with a mandatory central clearing obligation for AUD IRD, from the point of view of your business and/or that of your customers?

In particular, do you agree that the additional compliance costs of complying with a central clearing mandate for AUD IRD would be low for internationally active dealers?

We request that, in commenting, you quantify compliance costs as far as possible, including whether costs are likely to change over time, are transitional or projected ongoing costs. For example, costs may include:

- *legal costs;*
- *staff costs – for example number of staff hours and training costs;*
- *IT costs; and/or*
- *increased costs of managing risks or funding projects.*

Response to question 1: GreySpark Partners thanks the Australian Treasury for the opportunity to comment on its G4-IRD central clearing mandate proposals paper.

GreySpark Partners is a global capital markets consultancy firm, with offices in London, Hong Kong and Sydney. GreySpark provides expertise in risk, e-trading and market structure and offers business, management and technology consulting services. In Australia, GreySpark offers the aforementioned services alongside additional services within the market structure remit in OTC reforms, to assist clients in preparing for the impacts of regulatory change. In this deeply client focussed role, GreySpark feels it has both a duty and an obligation to respond to the Treasury's request for comments and feedback.

GreySpark's general view on this question is that the large dealers who are internationally active would certainly have minimal compliance, legal and operational costs in addition to their existing costs, in complying with an AUD IRD mandate. We feel that the specific question of quantifying associated costs would be better answered by Australia's dealer banks.

2. With respect to benefits, do you have views on whether the imposition of a central clearing mandate for AUD IRD would be likely to lead to substituted compliance benefits for dealers? If



so, what would these benefits be, and would you be able to provide an estimate of the savings to your firm?

- *If possible, please provide the same details as requested above with respect to the detailed breakdown of savings estimates.*

Response to question 2: GreySpark welcomes the proposed AUD-IRD clearing mandate and views this as a positive development in ensuring Australia is consistent with the changes taking place in the U.S. and the EU. The incremental cost for the dealer community in implementing changes to prepare for clearing will be minimal, due to the fact that the local banks who are already registered as swap dealers with the CFTC are already clearing OTC derivatives trades frequently and have built out significant technology platforms to support clearing. Most dealer banks are clearing AUD IRD already so the mandate should have a negligible impact on their day to day processes and operations.

There is benefit in opening up the dealer-to-dealer clearing mandate to AUD-IRD at the same time as the G4-IRD mandate as well - the key benefit being international consistency and economies of scale for banks in preparing for these changes from an operations and technology standpoint. The AUD-IRD mandate would not require significantly more spend from the large dealer banks as they currently already clear AUD-IRD with international counterparties. Mandating both G4-IRD and AUD-IRD to go live at the same time would allow the dealer banks to mobilise their internal project teams and external consultants, where necessary, to plan and execute the project to go live. There will be significant cost benefits in enabling banks to go live with both mandates ahead of the same deadline, as in all likelihood, the banks will prepare internally for go live at the same time anyway to make this a scalable exercise.

In the interest of international consistency and ensuring that Australia is not seen to be falling behind in its G20 commitments, it is important that AUD-IRD is mandated locally in Australia, before it is mandated in other jurisdictions. This will ensure not only substituted compliance benefits in the future, but also show that Australia is taking ownership of it's own path in adhering with the G20 commitments and not just following the U.S. and EU in it's methodologies.

3. Could you please comment on the incremental costs and benefits of merging the timing and the determinations for G4 and AUD IRD?

Response to question 3: We feel that the approach by the regulators in Australia has so far been measured and cautious. The phased approach taken by ASIC to mandating reporting to trade repositories has certainly been viewed by Australian market participants as reasonable and practical, as opposed to the "big bang" method applied by the European regulators in implementing the European Market Infrastructure Regulation ("EMIR"), which mandated trade reporting on a singular start date for all market participants.

In terms of the global OTC derivatives clearing landscape, mandatory clearing is already live in the U.S. and is widely expected to commence in EU in early 2015. From GreySpark's extensive discussions with Australian industry participants, a reasonable deadline for mandatory clearing for the G4 dealers for AUD-IRD would also be in early 2015, aligning with the proposed G4-IRD mandatory clearing commencement date, which impacts the 13 firms identified as G4 dealers in the Treasury proposals paper. There is benefit in opening up the dealer-to-dealer clearing



mandate to AUD-IRD at the same time as the G4-IRD mandate, with the key benefit being international consistency. The AUD-IRD mandate would not require significantly more spend from the large dealer banks as they currently clear AUD-IRD with international counterparties. Therefore, the incremental effort and cost for dealers to comply with an AUD-IRD mandate is anticipated to be minimal.

4. Do you agree with the proposal to restrict ASIC rulemaking to entities that are considered to be dealers?

Response to question 4: GreySpark agrees with the current proposal to restrict the clearing mandate to dealers only. However, our view is that non-dealers, predominantly the buy-side (and hedge funds) should be mandated to clear shortly after the dealers. A lack of clearing mandate would pose significant risk to buy-side firms trading OTC derivatives in Australia. While the Australian regulators have indicated that they are keen for the market to naturally move to clearing prior to setting a mandate for central clearing of OTC derivatives, it has been GreySpark's firsthand experience that the buy-side is largely delaying their commitment to and preparation for clearing until a mandate is announced by regulators. The lack of clear direction for the buy-side on when a clearing mandate will affect them raises the risk that when liquidity for OTC derivatives inevitably shifts from bilateral to cleared markets, firms who are unprepared for this change may lose access to liquidity if they have not already secured access to clearing via a clearing broker - this scenario is plausible due to the fact that the clearing brokers who are currently operating in the Australian market cannot guarantee that they will on-board every client who wishes to clear with them and will certainly pick and choose which clients they will take on. Therefore, GreySpark's view is that it would be prudent on the part of Treasury and the Australian regulators to provide buy-side firms with an indicative timeline of when an OTC derivatives clearing mandate is expected to impact them, in order to ensure that the market is best prepared in a timely manner for this change.

In order to ensure that Australia does not fall too far behind the global timelines for clearing and not be seen as lagging behind in their G20 commitments, it would be judicious to not leave the buy-side clearing mandate until 2016 and instead implement this in late 2015 alongside, or shortly after, the AUD-IRD mandate. In the interest of only mandating systemically important counterparties to clear, it would be prudent for the regulators to impose a mandate for ADIs and AFSL holders, to whom this mandate should be made applicable should their OTC derivative activity exceed a pre-set threshold per asset class. This approach would be in line with the phased rollout method adopted by the U.S. regulator Commodity Futures Trading Commission ("CFTC") in implementing mandatory clearing and would certainly give buy-side firms in Australia enough time to prepare. Buy-side firms who are currently holding off moving forward with clearing arrangements would also then be able to firmly commit to kicking off their preparations for entering the clearing arena. Providing the buy-side with at least a tentative timeline would eliminate much of the uncertainty and confusion that such firms are facing today in relation to future Australian clearing timelines.

There are several benefits to onboarding buy-side firms onto mandatory clearing sooner rather than later. The key benefit is that it would allow Australian buy-side firms to access the increasingly growing pool of cleared liquidity in the U.S. and EU regions. It would also allow them the time to complete full cost/benefit analyses on their clearing models, allow sufficient time for them to do clearing broker selection and enable them to make the best choice of clearing technology, clearing brokers and clearinghouses that are on offer rather than be pushed into a last minute choice after having left their decision to clear too late in the game. In the present state

of the market, buy-side firms are largely unwilling to commit to clearing. However, once margin requirements are imposed on bilateral uncleared trades, they will find increased incentive to clear – but not many buy-side firms seem aware of the fact that this change is coming. Australian buy-side firms who are unprepared for this change may lose access to liquidity if they have not already secured access to clearing via a clearing broker - this scenario is plausible due to the fact that the clearing brokers who are currently operating in the Australian market cannot guarantee that they will on-board every client who wishes to clear with them and will certainly pick and choose which clients they will take on. Therefore, GreySpark's view is that it would be prudent on the part of Treasury and the Australian regulators to provide buy-side firms with an indicative timeline of when an OTC derivatives clearing mandate is expected to impact them, in order to ensure that the market is best prepared in a timely manner for this change. The lack of clear direction for buy-side firms from Australian regulators and the Treasury coupled with a cost-conscious, largely uninformed and nonchalant Australian buy-side is creating enormous uncertainty in the market and a clear proposal and timeline on client clearing from the regulators and Treasury would allay some of the uncertainty that is growing in the market.

5. What are your views on the two options presented above to define internationally active dealers? Do you have views on additional criteria that should be used, or do you think that one or more of the suggested criteria should not be used? Or would you prefer a different methodology and if so, which one and why?

Response to question 5: There are benefits to each option proposed in this paper. In our view, Option A would certainly be a more accurate measure of capturing significant levels of activity that are relevant to Australian regulators. This option would also mean more monitoring/surveillance on the part of regulators on market participants' trading levels to ensure that all participants falling into this category are clearing their trade volumes as required by the rules.

Option B presents an opportunity for regulators to more easily define the pool of market participants who should be clearing under the mandate. However, in our view, imposing the mandate on registered swap dealers may not pick up the full population of trades in the market that represent "significant levels of activity".

It would be prudent on the part of regulators to impose Option A for completeness and to cover a more comprehensive list of market participants required to clear in their mandate.

6. Do you have comments on a possible coordination of the AUD IRD mandate with similar overseas requirements? If so, to which key overseas jurisdictions should an Australian mandate be linked?

Response to question 6: Our view is that although key overseas jurisdictions (like the U.S.) are debating AUD-IRD clearing for next year, it will be in the best interest of Australian dealer banks to align the AUD-IRD mandate with the G4-IRD mandate rather than with any international requirements/deadlines. The reasoning behind this is that should Australian banks have any technology or operations work to do in complying with the G4-IRD mandate, the same work can be extended to the AUD-IRD mandate, thereby enabling them to take advantage of economies of scale and build out to hit both mandates at the same time.



7. Do you have comments on the proposed timetable for implementing the central clearing obligation?

Response to question 7: GreySpark's view is that the proposed timetable for implementation of the AUD-IRD mandate, aligning it with the G4-IRD mandate is both fair and reasonable. The proposal allows the banks enough time to prepare and will undoubtedly be a positive move by the Australian market towards being in line with the U.S. and EU in their rollout of clearing. The proposal leaves enough time for industry consultation and definition of the rules, in our view, and we expect that this mandate will result in non-banks taking notice of clearing and looking at clearing liquidity in more detail than at the present time.

About GreySpark Partners

GreySpark is a global consultancy providing services exclusively to Capital Markets businesses. We are the trusted advisors to the world's leading finance houses. We help the leaders to make substantial, lasting improvements to the performance of their organisations.

We assist our clients throughout business and project lifecycles, from inception to completion, offering services in:

- Business Consulting
- Management Consulting
- Technology

For any questions regarding this submission, please contact Malavika Shekar or Braian Szwarcberg-Poch on +61 2 9299 9298 or at sydney@greyspark.com.

For further information about GreySpark please visit our website: www.greyspark.com.