

20 May 2016

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Dear Pat

Discussion Paper: Margining and risk mitigation for non-centrally cleared derivatives

The Australian Bankers' Association (**ABA**) welcomes the opportunity to provide feedback on APRA's Discussion Paper *Margining and risk mitigation for non-centrally cleared derivatives (CPS 226)*.

With the active participation of its members, the ABA provides analysis, advice and advocacy for the banking industry and contributes to the development of public policy on banking and other financial services. The ABA works with government, regulators and other stakeholders to improve public awareness and understanding of the industry's contribution to the economy and to ensure Australia's banking customers continue to benefit from a stable, competitive and accessible banking industry.

The ABA is aware that APRA will receive comprehensive submissions on the proposals from both the Australian Financial Markets Association (**AFMA**) and the International Swaps and Derivatives Association (**ISDA**). The ABA shares common members with AFMA and ISDA and given their particular skills and expertise it was agreed between ABA members that the AFMA submission would be the primary domestic submission to APRA in response to CPS 226.

Given this, the ABA generally supports the comprehensive and detailed submissions of both AFMA and ISDA. The ABA and its members do have some specific comments on CPS 226 which are of particular importance to members.

The ABA feedback relates specifically to the:

- 1) Entity level scope of the proposed margin requirements.
- 2) Implementation timeframe of the risk mitigation standards.
- 3) Timeframe for APRA's jurisdictional comparability assessments.
- 4) Minimum qualifying level of AUD 3 billion for variation margining.
- 5) Definitions contained in CPS 226

At this point the ABA would like to acknowledge APRA's open engagement to date, we note that AFMA and APRA continue to discuss the margining requirements and the ABA would like our members' concerns to form part of that ongoing work.



1. The entity level scope of the proposed margin requirements

The ABA and AFMA are generally aligned in their concern regarding APRA's proposed application of margin requirements to every entity in a Level 2 group. APRA's proposed approach is inconsistent with the BCBS/IOSCO framework in that it fails to consider the systemic nature of non-financial entities that it captures, and there is no connection between the clearing mandate and the margining requirements. APRA's approach is also inconsistent with the approaches taken by other comparable jurisdictions, such as the European Union and United States. Members are also concerned that the application of the rules to the Level 2 group would give CPS 226 an inappropriate extra-territorial application. The rules would potentially place Level 2 entities at a competitive disadvantage in jurisdictions where no equivalent requirements are imposed.

Both the AFMA and ISDA submissions discuss in great detail the concerns of the industry, which the ABA will not repeat here, other than to reiterate that the approach proposed by APRA is too broad and imposes a significant and unnecessary burden on Australian Authorised Deposit-taking Institutions (ADIs).

The ABA notes that its members' views to the APRA proposal understandably differ on the basis of the impact the proposals would have depending on members' particular group structure and the form of their extra-territorial operations.

The view of a majority of ABA members is that the margin requirements should only apply to transactions involving the entities within a margining group that meet the 'APRA covered entity' definition.

2. Implementation timeframe of the risk mitigation standards

The ABA supports in full the AFMA and ISDA recommendation that APRA de-couple the implementation of the risk mitigation standards from the implementation of the margin requirements. The ABA has received consistent feedback from our members that a 1 September 2016 go-live date for the implementation of risk mitigation standards is simply not enough time for such a large, complex and resource intensive task.

The ABA supports the ISDA recommendation that APRA consult specifically on the risk mitigation standards as set out in paragraphs 70-92 of the draft CPS 226. Decoupling the implementation of the margin rules from the proposed risk mitigation standards would be a sensible outcome for both APRA and industry. A 12 month standalone implementation for finalised risk mitigation standards would be a logical decision and in line with current government policy that requires all agencies to increase the time available for industry to implement complex regulatory change¹.

The ABA fully supports the ISDA recommendations regarding the scope and phasing-in of the risk mitigation standards, as well as supporting ISDA's proposed amendments, in order to make those standards practically achievable without detriment to APRA's prudential objectives and IOSCO's principles.

3. Timeframe for APRA's jurisdictional comparability assessments

The ABA also supports the comments set out by AFMA and ISDA on the pressing need on the industry for APRA's comparability assessment, and for there to be sufficient notice of this prior to the implementation date of the margin rules. This is because a majority of our membership are directly subject to multiple offshore regime's margin rules. It is essential that a workable cross-border framework is facilitated so that implementation approaches and decisions, which are in the process of being made now, can be undertaken on a streamlined and efficient basis.

¹ FSI Recommendation 31, [Improving Australia's financial system](#): Government response to the Financial System Inquiry, Page 25, Dec 2015.



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The ABA strongly supports the ISDA recommendation that if APRA is unable to finalise its comparability assessments before 1 June 2016, that it considers issuing a two-year transitional comparability determination during which the margin rules will not apply to in-scope derivatives where either or both of the APRA covered entity or the covered counterparty is subject to the margin requirements of the relevant foreign regime.

4. Variation margining

In regards to the minimum qualifying level of AUD 3 billion for variation margin requirements (Paragraph 12) the ABA's view differs, in one aspect, to that contained in AFMA's submission. The ABA supports APRA's proposed inclusion of the AUD 3 billion threshold for variation margin on the basis that entities that transact in a *deminimis* amount of non-centrally cleared derivatives do not pose a systemic risk and so do not warrant the additional costs that would be imposed. Imposing a variation margin requirement in these circumstances could result in such counterparties, including end-user counterparties, from engaging in legitimate hedging activities. The ABA understands that APRA is not alone in setting a variation margin threshold, for example, there is a similar threshold under the Japanese margin rules, set at JPY300 billion.

The ABA's support for retaining the threshold is subject to a request for APRA, before the finalisation of CPS 226, to confirm with its foreign counterparts that the threshold will not impact or prevent substituted compliance determinations.

5. Definitions in CPS 226

Paragraph 10 of the draft CPS 226 defines certain key terms. The AFMA and ISDA submissions detail a number of concerns and recommendations in regard to the current definitions (e.g. Derivatives, Financial Institution, etc.) The ABA agrees with both AFMA and ISDA that the proposed definitions require further refinement, and supports their suggestions. The ABA strongly supports the view of AFMA that more specific discussion, between APRA and the industry on this topic, is critical before APRA finalises CPS 226.

Finally, the ABA appreciates the considerable efforts of APRA, to date, in working with the industry to find an appropriate balance between the objectives of the global reforms and the requirements of the Australian financial system, with particular regard to supporting the ongoing efficient access to derivative markets for Australian ADIs.

The ABA and its members look forward to ongoing dialogue with APRA, and will continue to work with both AFMA and ISDA to ensure an efficient and effective implementation

Yours sincerely

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