



ASX 24 Exchange Traded Derivatives and OTC Interest Rate Derivatives Client Clearing

Response to Consultation Feedback on Draft Operating Rules



12 December 2013

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Executive summary

In the second half of 2013 ASX released two Consultation Papers seeking comment on the draft Operating Rules for a new client clearing service (“**Client Clearing Service**”) for ASX 24 Exchange Traded Derivatives and OTC Interest Rate Derivatives. The first Consultation Paper was published on 28 August 2013 and focused on the client account segregation and portability features of the Client Clearing Service. The second Consultation Paper was published on 17 October 2013 and focused on certain aspects of ASX’s default management processes. This document presents the results of the public consultation undertaken in those two papers.

ASX received a total of 18 formal submissions from Clearing Participants, financial institutions, fund managers and professional and industry associations in response to the two Consultation Papers. ASX has published the non-confidential submissions at <http://www.asx.com.au/services/otc-clearing.htm>.

ASX is taking the following steps to address comments made on the proposals outlined in the first Consultation Paper:

Australian legal opinion to confirm no impact on close-out netting with Client	ASX has commissioned an external Australian law legal opinion to confirm that the proposed changes to ASX’s clearing model (Client Protection Model) will not affect the application of the Payment Systems and Netting Act 1998 (Cth) to close-out netting of obligations owed between a Clearing Participant and its Client under a close-out netting contract between them. ASX will make this legal opinion available to Clearing Participants.
Nominated Person for Individual Client Account facilitates multi level client structures	ASX has modified the draft Operating Rules so that the benefits of individual account segregation can be made available to end user clients, without the Operating Rules requiring those clients to contract with a Clearing Participant. Under the modified rules, a person or entity who is not a client of a Clearing Participant may be nominated (as the ‘Nominated Person’) in respect of an Individual Client Account. In the event of the Clearing Participant’s default, ASX will refer to the Nominated Person rather than the Client for porting instructions in respect of the Individual Client Account, and pay to the Nominated Person any residual initial margin associated with positions in the account that could not be ported.
Client Fact Sheet distribution limited to Clients of Clearing Participant	ASX has modified the draft Operating Rules so that only a Clearing Participant’s Clients (i.e. immediate clients with whom the Clearing Participant has a client agreement) must be provided with, or directed to, the Client Fact Sheet by the Clearing Participant. ASX has clarified that only those Clients who have an open position in a class of financial products at the time at which the Client Clearing Service commences in respect of that class, or who seek to open a new position in that class subsequently, must be provided with, or directed to, the Client Fact Sheet. ASX has also withdrawn its original proposal to require Clearing Participants to obtain and retain evidence of each Client’s written acknowledgment of the fact sheet.
Treatment of positions and monies of Affiliated Clients	ASX will not proceed with proposed rule amendments relating to the House/Client classification of positions of related bodies corporate of Clearing Participants and segregation of related monies at this time. The existing Operating Rules in relation to those matters will continue to apply.

ASX received broad support for the proposals outlined in the second Consultation Paper and ASX does not intend to make any significant changes to those proposals. In response to feedback from OTC Participants and Foundation Customers, ASX proposes to modify its Default Management Group (DMG) Procedures so that members of the DMG may participate in DMG meetings either in person at ASX’s offices or by electronic communication from a location approved by ASX.

The revised draft Operating Rules that ASX has submitted for regulatory clearance are available at <http://www.asx.com.au/services/otc-clearing.htm>.

Consultation process

In the second half of 2013 ASX released two Consultation Papers seeking comment on draft Operating Rules for the Client Clearing Service:

- [First Consultation Paper](#) published 28 August 2013: This paper set out the draft Operating Rule framework for client clearing for ASX 24 Exchange Traded Derivatives and OTC Interest Rate Derivatives, including:
 - Client Protection Model – an agency-style clearing model, that will replace ASX’s existing ‘principal model’;
 - Client account structure – individual and omnibus client account options; and
 - Porting – conditions and processes for different client account options.
- [Second Consultation Paper](#) published 17 October 2013: This paper set out draft Operating Rules to refine certain aspects of ASX’s default management processes for OTC Interest Rate Derivatives and portfolio margined ASX 24 Exchange Traded Derivatives. Those refinements related primarily to the following matters:
 - Composition of the default portfolio;
 - Default auction process;
 - Allocation of default losses between House and Client accounts; and
 - OTC Commitment juniorisation.

ASX received a total of 18 formal submissions from Clearing Participants, financial institutions, fund managers and professional and industry associations: 11 in response to the first Consultation Paper and 7 in response to the second Consultation Paper. Of the total number of submissions received 15 were confidential. Schedule 1 contains a list of non-confidential submissions, which ASX has published at <http://www.asx.com.au/services/otc-clearing.htm>.

ASX is making a number of significant changes to its original proposals in response to stakeholder input. Those changes are outlined in this document.

ASX thanks all those who shared their views and expertise during the consultation process.

Consultation feedback and ASX responses

Substantive feedback

ASX received a significant amount of substantive feedback on the draft Operating Rules. A summary of unattributed feedback, and ASX's responses, is set out in Schedule 2.

ASX is taking the following steps to address comments made on the proposals outlined in the first Consultation Paper:

(i) *Impact of Client Protection Model on Clearing Participant close-out netting with Client*

'Client Protection Model' is the name ASX applies to the agency-style clearing model that it is introducing to support the Client Clearing Service. It refers to the legal relationships established by proposed Part 10 of the Futures Rules between a Client (whether utilising an Omnibus Account or Individual Client Account), its Clearing Participant and ASX, and the related arrangements for segregation and portability of client positions and associated initial margin.

Schedule 3 contains a brief FAQ with respect to the Client Protection Model.

The key feature of the Client Protection Model, which distinguishes it from the existing 'principal model' utilised by ASX, is that the Clearing Participant clears transactions as agent of its Client, binding the Client to cleared contracts through the authority which the Client has given the Clearing Participant to act on its behalf. As is the case with other 'agency-style' clearing models, the Clearing Participant remains responsible to ASX for the performance of the Client's obligations in respect of the cleared contracts.

Some respondents to the first Consultation Paper sought clarification on whether ASX's introduction of the Client Protection Model would affect Clearing Participants' ability to net obligations pursuant to close out netting contracts with Clients. ASX has commissioned an external Australian law legal opinion to confirm that the Client Protection Model will not affect the application of the Payment Systems and Netting Act 1998 (Cth) to close-out netting of obligations owed between a Clearing Participant and its Client under a close-out netting contract between them. ASX will make this legal opinion available to Clearing Participants.

(ii) *Accommodating multi-level client structures*

Some respondents expressed concern about ASX's original proposal that an end user client (i.e. a person or entity that does not deal directly with a Clearing Participant, but instead with an intermediary which is itself a client of the Clearing Participant) would need to enter into a client agreement with the Clearing Participant in order to take up the Individual Client Account option (in effect making the end user client a 'Client' of the Clearing Participant for the purposes of the Operating Rules). Respondents cited a potential lack of licence authorisations on the part of some Clearing Participants to deal directly with end user clients, the accrual of Know-Your-Customer (KYC) obligations by Clearing Participants as a result of this change, and the cost of documenting those client arrangements.

ASX has modified the draft Operating Rules so that the benefits of individual account segregation can be made available to end user clients, without the Operating Rules requiring those clients to contract with a Clearing Participant. Under the modified rules, a person or entity who is not a 'Client' of a Clearing Participant may be nominated (as a 'Nominated Person') in respect of an Individual Client Account. In the event of the Clearing Participant's default, ASX will refer to the Nominated Person rather than the Client for porting instructions in respect of the Individual Client Account, and pay to the Nominated Person any residual initial margin associated with positions in the account that could not be ported.

Schedule 4 contains an overview of the Nominated Person option.

(iii) *Distribution of the Client Fact Sheet*

Some respondents expressed concern about ASX's original proposal that Clearing Participants would be required to give the Client Fact Sheet to end user clients, with whom the Clearing Participant has no direct relationship.

ASX has modified the draft Operating Rules so that only a Clearing Participant's Clients (i.e. immediate clients with whom the Clearing Participant has a client agreement) must be provided with, or directed to, the Client Fact Sheet by the Clearing Participant. ASX has also clarified that only those Clients who have an open position in a class of financial products at the time at which the Client Clearing Service commences in respect of that class, or who seek to open a new position in that class subsequently, must be provided with, or directed to, the Client Fact Sheet.

ASX has committed to the regulatory agencies (ASIC and the Reserve Bank) that it will assess market awareness among Australian end user clients about ASX's client account segregation options 12 months after the launch of the Client Clearing Service for ASX 24 Exchange Traded Derivatives. Subject to the results of that assessment, ASX will revisit if necessary the distribution requirements with respect to the Client Fact Sheet under the Operating Rules.

In order to minimise the administrative burden on Clearing Participants, ASX has withdrawn its original proposal to require Clearing Participants to obtain and retain evidence of each Client's written acknowledgment of the Client Fact Sheet. Instead, ASX may require a Clearing Participant to attest annually whether it has directed Clients to the Client Fact Sheet in accordance with the Operating Rules.

(iv) Treatment of positions and monies of Affiliated Clients

Some respondents expressed concern about potential inconsistency between ASX's proposed rules with respect to the treatment of positions and monies of related bodies corporate of Clearing Participants, and the client money provisions of the Corporations Act and Market Integrity Rules for the ASX 24 market.

Given the significance of the potential inconsistencies and the need for regulatory reform of client money rules identified by stakeholders, ASX does not wish to pre-empt the outcome of future reform and risk further complicating an already complex area by proceeding with its proposed rule amendments at this time. The existing Operating Rules will continue to apply to position designation.

ASX has modified the draft Operating Rules to recognise that cash collateral returned by ASX to OTC Clearing Participants may include monies referable to client positions in OTC Interest Rate Derivatives which the law may require to be paid into a client money account that is not an ASX 24 Clients' Segregated Account.

ASX received broad support for the proposals outlined in the second Consultation Paper and ASX does not intend to make any significant changes to those proposals. In response to feedback from OTC Participants and Foundation Customers, ASX proposes to modify its Default Management Group (DMG) Procedures so that members of the DMG may participate in DMG meetings either in person at ASX's offices or by electronic communication from a location approved by ASX. The DMG will comprise representatives of OTC Participants and will advise ASX on certain matters related to the default of an OTC Participant. The proposed modification to the DMG Procedures seeks to address concerns expressed by some OTC Participants and Foundation Customers that in order to meet their obligation to nominate primary and alternate DMG members, and to manage the impact of this commitment on their own operations, they may need to draw on resources in the Asian region.

Drafting feedback

ASX received a number of drafting comments on the draft Operating Rules. ASX has incorporated those drafting comments where possible.

Feedback on Operating Rules that are not the subject of proposed change

ASX received a number of comments on Operating Rules that are already operative and not the subject of a change proposal under either of the client clearing Consultation Papers. These comments are separately identified in Schedule 2. Many of those Operating Rules were the subject of consultation by ASX in the first half of 2013 in connection with the implementation of ASX's dealer to dealer clearing service for OTC Interest Rate Derivatives.

ASX has reviewed all comments and incorporated those it has been possible to accommodate without unduly increasing the timeframe for regulatory clearance of the draft Operating Rules that are required to implement the Client Clearing Service.

Client Fact Sheet

The Client Fact Sheet has been revised to incorporate stakeholder input, and substantially reworked following externally-conducted consumer testing. ASX will publish a revised and final version of the Client Fact Sheet in January 2014.

Porting legal opinion

Some respondents to the first Consultation Paper sought clarification on whether actions taken by ASX under the Client Protection Model to port Client positions and associated initial margin could be reversed or unwound. ASX has commissioned an external Australian law legal opinion to confirm the validity and enforceability of porting of Client property in accordance with ASX's Operating Rules on Clearing Participant default. ASX will make this legal opinion available to Clearing Participants and Clients on request.

OTC Supplement

ASX foreshadowed in the first Consultation Paper that it would publish a sample OTC Client Clearing addendum that could be utilised by Clearing Participants and their Clients in conjunction with either a Futures Agreement or an ISDA Master Agreement. Subsequently, ASX undertook informal consultation on the form of the addendum with OTC Clearing Participants, OTC Foundation Customers and selected buy-side institutions and fund managers that have an interest in centrally clearing A\$ OTC Interest Rate Derivatives through ASX.

Taking into account all feedback received, ASX has finalised and published the ASX Cleared OTC Derivatives Supplement, available at <http://www.asx.com.au/services/otc-clearing.htm>. This document is not mandated for use, but is a sample which Clearing Participants and Clients might find useful in documenting the relationship between them with respect to clearing OTC derivatives through ASX.

Risk Committee

ASX received a number of comments in response to consultation questions that related to the nomination and selection process for Client representatives on the Risk Committee. ASX welcomes that input and will conduct a separate consultation process on detailed nomination and selection procedures in 2014.

Product Committee

The revised draft Operating Rules that ASX has published with this Response to Consultation Feedback contain a number of changes in relation to the Product Committee:

- The mandate of the committee has been extended to encompass consultation on exchange traded as well as OTC product development;
- Representatives of both Futures and OTC Participants will be entitled to participate in the committee;
- Representatives of Clients will be invited to participate in the committee. Nomination and selection procedures for Client representatives will be included in the 2014 consultation foreshadowed above in relation to the Risk Committee.

Eligible collateral

The revised draft Operating Rules that ASX has published with this Response to Consultation Feedback omit the lists of eligible collateral that currently appear in the schedules to the Futures Rules and in the OTC Handbook. This is to minimise the administrative overhead associated with amendments to the eligible collateral lists. ASX will maintain the eligible collateral lists on its website and notify Clearing Participants of changes. Eligible collateral will be a standing agenda item of the Risk Committee.

ASX's nomination of eligible collateral is subject to the requirements of the Reserve Bank of Australia's Financial Stability Standards for Central Counterparties (FSS) that require CCPs to accept only collateral that has low credit, liquidity and market risks and to set and enforce appropriately conservative haircuts and concentration limits (refer FSS, Standard 5).

Technology changes

In conjunction with the introduction of the Client Clearing Service, ASX will upgrade its clearing system to Genium INET Clearing in 2014. A number of amendments to the Operating Rules are proposed for the purpose of replacing references to particular software with generic terms.

Revised Operating Rules

The revised draft Operating Rules, incorporating changes made by ASX in response to consultation feedback, are available at <http://www.asx.com.au/services/otc-clearing.htm>.

A comparison of the revised draft Operating Rules against the draft rules annexed to the two Consultation Papers is available at <http://www.asx.com.au/services/otc-clearing.htm>. Those comparison documents highlight the changes made by ASX in response to consultation feedback.

The proposed amendments to the Operating Rules remain subject to the usual regulatory clearance process by ASIC and RBA.

Next steps

ASX is continuing to engage with ASIC and the Reserve Bank of Australia (RBA) on the proposed rule changes and is awaiting an invitation from ASIC to formally lodge the revised Operating Rules for regulatory clearance. Subject to regulatory clearance, the rules will take effect in the first quarter of 2014, ahead of the commercial launch of the Client Clearing Service for OTC Interest Rate Derivatives (expected end Q1 2014) and ASX 24 Exchange Traded Derivatives (expected end Q2 2014).

Schedule 1: List of non-confidential submissions

The following non-confidential submissions are available at <http://www.asx.com.au/services/otc-clearing.htm>

First Consultation Paper

- ISDA
- AFMA

Second Consultation Paper

- ISDA

Schedule 2: Substantive feedback and ASX responses

ASX 24 ETD and OTC IRD Client Clearing - Summary of responses to Consultation Paper 1

Sub-issue	Comment	ASX Response
A1 ASX proposes not to require Clearing Participants to offer both account types to Clients. Do you agree with ASX's proposed approach? If not, why not?		
Account Types	<p>Yes - Support the ASX approach not to require Clearing Participants to offer both account types to Clients for reasons including the following:</p> <ul style="list-style-type: none"> - Choice can be achieved via a range of Clearing Participants - Costs involved in offering two methods may be too high for some Clearing Participants. - Significant increase in accounts increases operational risk and compliance costs. - Gives Clearing Participants the option not to invest in the operational system, and as a result, fee structures for clients may differ across Clearing Participants according to the investment in systems required. - Regulatory issues may prevent Clearing Participants from offering Individual Client Accounts to certain clients e.g. retail where only wholesale licence is held and regulatory requirements in offshore jurisdictions where clients are located. 	While different views have been expressed to ASX on this matter, the balance of consultation feedback favours allowing a Clearing Participant to maintain flexibility in the account types it offers its Clients. ASX will proceed on this basis.
Account Types	<p>No - Support an approach that <i>requires</i> Clearing Participants to offer both account types for reasons including the following:</p> <ul style="list-style-type: none"> - There is no incentive for Clearing Participants to offer both account types. - There is a danger Clearing Participants won't offer the service due to costs. 	
Account Types	Is there a sense from the market of what will be offered if ASX does not require Clearing Participants to offer both account types?	Feedback received by ASX from Clients and Clearing Participants indicates that there will be sufficient demand for an Individual Client Account structure to warrant Clearing Participants offering that structure.
Account Types	Object to rule 115 (and procedure) that does not appear to allow a Clearing Participant to provide the Individual Client Account to some clients (or types of clients) but not others. There may be commercial or regulatory reasons that prevent a Clearing Participant from offering both account types to <u>all</u> clients even if it offers both structures.	ASX has amended Procedure 115 so that a Clearing Participant may offer an Individual Client Account to selected Clients.
A2 Will the Individual Client Account structure enable ASX's indirect customers that are ADIs to gain the optimal capital treatment of their cleared trade exposures to ASX under APRA Prudential Standard 112? If not, why not?		
Capital Treatment	No - Individual Client Account structure will not enable ADI Clients to gain optimal capital treatment (2% risk weighting) on the basis that it is unlikely that all of the conditions in APS 112 will be satisfied – in particular, under Option 2, there is no provision for segregation and porting of collateral.	ASX has engaged with APRA to explain its reasons for expecting that the Individual Client Account structure will achieve optimal capital treatment for an ADI Client's cleared trade exposures under APS 112. APRA has indicated that regulated entities should liaise with APRA directly in relation to

Sub-issue	Comment	ASX Response
Capital Treatment	Yes – Individual Client Account structure will enable ADI Clients to gain optimal capital treatment.	capital treatment of cleared trade exposures under APS 112.
APRA	Has ASX liaised with APRA to gain feedback or attestation that the Individual Client Account model aligns or partially aligns with APS112?	
Opinion	What opinions (if any) is ASX going to commission in relation to the satisfaction of APS 112?	Regulated entities should liaise with APRA directly. ASX will not commission a legal opinion in relation to APS 112.
A3 ASX's Client Clearing Service will not offer a "bankruptcy remote" collateral holding structure initially. Feedback is requested, especially from Clients, on the relative priority of such arrangements, taking into account the incremental benefits and costs of implementation as well as other service enhancements that may be desirable (such as a "with excess" individual client account option).		
Bankruptcy remote collateral	Please clarify what is meant by a "bankruptcy remote" collateral holding structure.	ASX expects that collateral will be held by a CCP under a "bankruptcy remote" collateral holding structure if the claims of a Clearing Participant to collateral provided by it to that CCP have priority over the claims of third-party creditors of the CCP.
Bankruptcy remote collateral	Would like ASX to implement a bankruptcy remote structure or explain why it cannot.	ASX intends to implement a bankruptcy remote collateral holding structure and will consult stakeholders on options for implementing this structure in 2014.
Options 3 & 4	Require further clarification on costs and timing of current model proposed and Options 3 (LSOC with excess) and 4 (Full Individual Segregation).	ASX intends to consult stakeholders on the design and implementation of Options 3 (Individual Client Account "with excess") and 4 (Full Individual Segregation) in 2014.
Eligible Collateral	ASX should consider expanding collateral to include semi-governments and high grade corporates.	ASX maintains and frequently reviews the list of high quality collateral that it accepts from Clearing Participants. Additions to this list are undertaken on a case-by-case basis and ASX welcomes suggestions from market users. Subject to regulatory review, ASX will shortly be expanding eligible non-cash collateral to include a variety of Australian State Government Bonds and further additions are likely in due course.
B1 The porting windows for ASX 24 Exchange Traded Derivatives and OTC Interest Rate Derivatives are up to 24 and 48 hours respectively. Are the porting windows appropriate? If not, why not?		
Porting windows	Yes - Support porting windows proposed by ASX on the basis that: <ul style="list-style-type: none"> - Periods proposed are reasonable and appear to align with periods at other clearing houses. - Allowing any longer may make Clients nervous about the robustness of the porting process upon a Clearing Participant default. 	While different views have been expressed to ASX on this matter, the balance of consultation feedback supports porting windows for ASX 24 Exchange Traded Derivatives and OTC Interest Rate Derivatives up to 24 hours and 48 hours respectively. ASX has maintained the need for flexibility

Sub-issue	Comment	ASX Response
	<p>- it does not require the express consent of the client at the time of the default, especially for clients not located in Asia-Pacific time zone.</p>	<p>in order to manage the unique circumstances of each default event. ASX acknowledges the need to review the porting window for OTC where the OTC service is extended beyond Australian clients. However, ASX notes that longer porting windows may result in higher initial margin requirements. ASX strongly recommends that Clients nominate an Alternate Clearing Participant before any default in order to maximise the chances of porting in the event of a Clearing Participant default.</p>
Porting windows	<p>No - Do not support porting windows proposed by ASX.</p> <p>24 hours (for Futures) is insufficient time for a Clearing Participant to take over a portfolio (internal risk and due diligence requirements).</p> <p>A porting window of 72 hours is more reasonable.</p>	
Porting windows	<p>May require longer window (e.g. 72 hours) when foreign OTC Clients are admitted because of time delay in contacting offshore counterparties.</p>	
Porting windows	<p>A tighter timeframe or alignment with the ASX24 in the future may be necessary.</p>	
Margin	<p>If the proposed timeframes are adopted consideration should be given as to whether the CCP needs to take over margining process while the positions are under consideration for porting.</p>	<p>ASX does not propose to offer a 'direct funding' model (where the client pays margin directly to the CCP) at this time but will consider this as a potential enhancement of the service in future, subject to Client demand.</p>
Margin	<p>There is a risk that a Client, which is being ported, may have insufficient IM as a result of this. In such an instance, will the Client be expected to reimburse the Alternate Clearing Participant for the shortfall in IM? Will the shortfall in IM, in such an instance, be allocated out amongst the various Clients of the defaulting Clearing Participant?</p>	<p>During the porting window, ASX will not margin the defaulting Clearing Participant (or its Clients), however, ASX will continue to pay/receive VM to/from non-defaulting Clearing Participants on a timely basis. Once the positions are ported, the Alternate Clearing Participant will be called/paid VM in respect of the period from the last end-of-day VM settlement prior to default, up to the time of the VM call.</p>
Margin	<p>Require guidance as to the required timeframe for the receipt of VMs from the porting client by the Clearing Participant – currently these are outlined in the ASIC MIRs for Futures. ASX will need to add wording to address who is expected to make any required calls and the time for receipt. The proposed approach appears to assume that margining is not carried out while the portable positions are in limbo.</p>	<p>A Client whose positions are ported will be required to meet IM calls from the Alternate Clearing Participant, taking into account monies for IM that have been ported with its positions from the defaulting Clearing Participant.</p>
Porting windows	<p>Could ASX please explain how it arrived at these periods and how they compare to other similar CCPs.</p>	<p>The chosen porting periods are in line with industry practice, although many other CCPs are not as prescriptive in their rules on these periods. It is important that the porting periods are not so long as to potentially create unacceptable risks to the CCP and its non-defaulting Clearing Participants but also provide sufficient time for the Alternate Clearing Participants to perform the necessary checks and procedural steps. ASX strongly recommends that clients using Individual Client Accounts have an agreement in place with an Alternate Clearing Participant to expedite the porting process.</p>

Sub-issue	Comment	ASX Response
Porting windows	Clarity on porting window required for cross-margined positions.	The porting window for cross margined ASX 24 ETD positions is up to 48 hours.
Porting windows	The appropriateness of porting windows is impacted by the speed at which an Alternate Clearing Participant can receive information from ASX and their ability to assess the positions to be reported. System requirements for informing Clearing Participants need to be settled with regard to what format clients' exposures will be provided and, in addition to the IM and the positions, how VM exposure information on positions would be provided.	ASX will provide files to a nominated Alternate Clearing Participant detailing positions, last settlement price and Initial Margin. ASX is conscious that the timeliness of receipt of this data is critical for the Alternate Clearing Participant's deliberation and will design the distribution mechanism and file formats with this front of mind.
B2 ASX proposes not to require Clients utilising Individual Client Accounts to maintain a nominated Alternate Clearing Participant. Do you agree with ASX's proposed approach? If not, why not?		
Alternate Clearing Participant	<p>Yes – Support ASX proposal not to require Individual Client Account Clients to appoint an Alternate Clearing Participant for reasons including the following:</p> <ul style="list-style-type: none"> - As long as a Client is aware of the risks, a Client should be allowed freedom to choose account model that best suits their needs. - Not all Clients may be able to find an institution willing to act as its Alternate Clearing Participant. - Clients may value segregation over porting and appointment of an Alternate Clearing Participant only adds operational burden and additional costs. - Overall the commercial viability of providing porting is uncertain, and is likely to vary significantly from client to client and between Clearing Participants - The splitting of their books could mean some margin inefficiency, and will also potentially increase the overhead in connecting to multiple counterparties - The concept of 'guaranteed portability' does not exist. - Nominating an Alternate Clearing Participant will incur cost so they should be able to elect to do so only if they desire. 	There was unanimous support for ASX's proposed approach not to require Clients utilising Individual Client Accounts to maintain a nominated Alternate Clearing Participant. ASX will proceed on this basis.
Preconditions to porting	Client positions should only be ported if Client owes no further obligations to current defaulting Clearing Participant. How will defaulted Clearing Participant recover IM it has funded?	Porting will occur if a Client using an Individual Client Account satisfies the specified preconditions, whether or not the Client owes obligations to its defaulting Clearing Participant. Neither the porting process nor the legislative protections for porting given by the <i>Payment Systems and Netting Act 1998</i> (Cth) extinguish accrued rights and obligations between the Clearing Participant and Client (for example with respect to margin funded by the Clearing Participant).
Inconsistent porting rules	Unclear interaction between porting of Client positions under Rule 74 (Clients not in Default to Clearing Participant in Default) and Rules 119 and 120.	Rule 74 is relevant outside of the Client Protection Model. Rules 119 and 120 are relevant when the Client Protection Model applies.

Sub-issue	Comment	ASX Response
Excess collateral	Excess collateral will become more relevant when foreign clients are admitted for OTC. ASX's current position on excess collateral is a disincentive to clients posting excess giving rise to an operational burden on Clearing Participants	ASX plans to consult stakeholders on the design and implementation of the Individual Client Account "with excess" account option in 2014.
Collateral	IM and VM are usually calculated at same level – the consultation paper suggests VM is calculated at trade level and IM at book level. Does this make gross VM "excess collateral"?	Variation margin is not excess collateral: it is passed through by ASX.
C1 Unlike ASX's existing client clearing arrangements, which are based on the principal model, the Client Protection Model creates a direct legal relationship between ASX and the Client. Do you consider this may have any unintended consequences for Clients or Clearing Participants ? If so, why?		
Triparty relationship/ Client liability	<p>Is the effect of Rule 113.1(e) that ASX "waives" or "agrees not to sue" the Client, despite the Client's joint and several liability? Are there any circumstances in which, on current drafting of the Rules, ASX would proceed against the Client?</p> <p>If not, what is ASX's action in these circumstances?</p>	<p>ASX agrees not to sue the Client, despite the Client's joint and several liability.</p> <p>There are no circumstances in which, on current drafting of the Rules, ASX would proceed against the Client. ASX seeks to make the Client a party to Open Contracts under the Client Protection Model so that the Client has a direct legal relationship with ASX and may enforce its rights to segregation and portability under the Rules. ASX looks to the Clearing Participant exclusively to perform obligations under Open Contracts.</p>
Triparty relationship	Uncertainty in relation to when the agency relationship applies and when principal relationship applies and what rights and obligations a Clearing Participant, a Client and ASX will have.	<p>Under the Rules (and consistent with principles of agency law):</p> <ul style="list-style-type: none"> • The Clearing Participant clears transactions on behalf of a Client as its agent with the effect that each of the Client, Clearing Participant and ASX are parties to the cleared transactions and bound by the applicable Rules. • The Clearing Participant remains liable to ASX for Client transactions as principal obligor. • ASX agrees not to take action against a Client personally for the performance of any obligation owing in relation to the Client's cleared transactions. • In the ordinary course, ASX deals with the Clearing Participant only. However, upon the default of the Clearing Participant, ASX will deal with the Client in relation to porting. <p>We refer you to the Client Protection Model FAQ in the Response to Consultation for further details.</p>
Triparty relationship/ Client Protection Model	Is there any precedent for this sort of legal arrangement in Australia, in any other comparable area (ideally that has been considered by courts)?	The Client Protection Model applies general principles of agency law, which can be modified by contract. The Rules are a contract.

Sub-issue	Comment	ASX Response
Triparty relationship/ Trustee	Seeking clarification on ASX's view of trusts and trustee duties under Client Protection Model – think there are conflicting views put in Consultation Paper and rules (refer rule 4.9, 113.2, 124.4 and diagram of legal relationships in consultation paper). Note, Corporations Act does not impose any obligation in relation to margin being held on trust by Clearing Participants (some brokers specifically state there is no fiduciary relationship in their documentation)	ASX does not seek to impose additional trustee duties on a Clearing Participant that are not already contemplated under the Clearing Participant's client agreement. As a party to the Rules, a Clearing Participant will hold the rights and entitlements a Client has against ASX set out in the Client Protection Model Provisions on behalf of the Client (FR113.2). This is intended to facilitate enforcement against ASX of these rights and entitlements by the Client.
Triparty relationship/ Multi-level client structure	Does not address a multi-level client structure where an end user may be the client of a broker that is itself a client of a Clearing Participant.	<p>ASX has modified its approach to better accommodate multi-level client structures: end user clients that seek individual segregation may either (i) contract directly with a Clearing Participant (i.e. as the 'Client'), or (ii) be nominated by an entity (e.g. broker) that is itself a 'Client' of a Clearing Participant.</p> <p>In the latter case (ii), in the event of the Clearing Participant's default, ASX will:</p> <ul style="list-style-type: none"> • Take porting instructions from the Nominated Person in respect of the Individual Client Account; and • If the Client's positions and IM value in respect of the Individual Client Account cannot be ported, will remit the residual IM directly to the Nominated Person's bank account. <p>We refer you to Schedule 4 in the Response to Consultation for further details.</p>
ASX dual role	There may be a need for ASX to address its role as both the service provider and counterparty to the transactions (e.g. any conflicts and what complaints handling procedures are available).	<p>There is no conflict between ASX's role as service provider and central counterparty. ASX is required to have conflict handling arrangements under its CS Facility Licence (s821A(c) Corporations Act). More information on this can be found at the following website:</p> <p>http://www.asx.com.au/regulation/regulatory-compliance/asx-corporations-act-obligations.htm. ASX's compliance with these conflict handling arrangements is subject to annual assessment by ASIC.</p>

Sub-issue	Comment	ASX Response
ASX Clearing Participant and Client dispute	ASX needs to consider the possible scenarios where there is a dispute between the Clearing Participant and the Client, and these two parties give different instructions to ASX with regard to any Open Transactions or the treatment of any collateral. For example, one party may claim that the other party is in default, but the other party may dispute this; or each party may claim that the other is in default, but each party denies the occurrence of a default with respect to itself.	Prior to a Clearing Participant default, ASX will: (i) only accept instructions from a Clearing Participant in relation to Open Contracts and Open Positions (FR 113.2); and (ii) not seek to independently verify the Clearing Participant's instructions that a Client is in default. Where the Clearing Participant is in default, ASX will accept porting instructions from the Client of an Individual Client Account (FR 119). If the Clearing Participant is in default, ASX may determine that the Client is in default in accordance with FR 118.3.
ASX Reg/AML	The service performed by ASXCF in response to client requests for porting would need to be assessed as to whether they are designated services and therefore require ASXCF to undertake AML due diligence with respect to the client.	ASX is not subject to AML requirements in respect of the service.
Clearing Participant /Close-out netting	Further legal clarity will be needed on the question of whether the proposed change from Principal to Client Protection Model will have any adverse consequences for a Clearing Participant in being able to close out positions and liquidate collateral to protect itself. Do the rules together with client agreements constitute close out netting contracts? Seek an opinion on enforceability of close-out netting.	ASX has commissioned an external Australian law legal opinion to confirm that the proposed changes to ASX's clearing model (Client Protection Model) will not affect the application of the <i>Payment Systems and Netting Act 1998</i> (Cth) to close-out netting of obligations owed between a Clearing Participant and its Client under a close-out netting contract between them. ASX will make this legal opinion available to Clearing Participants.
Legal/Operating Rules as a contract under s822B	May need to amend s822B Corporations Act to clarify Rules take effect as a contract under seal in relation to Clients as well. The position of Client Protection Model Clients is unclear under Rule 1.3 and needs to be reconsidered.	No amendment of s822B is required. Clients are not, and are not required to be, parties to the Rules under FR 1.3. However, a Clearing Participant ensures that its Clients agree to be bound by the Rules for Client Protection Model under FR 112.2. This is already a required term of the client agreement (FR 4.14(j)). Section 822B of the Corporations Act is not an exclusive description of those to whom ASX has obligations and Clients are able to compel ASX's performance of its obligations.
Legal/Netting	Please explain how netting is supposed to work under Handbook 4.16. This seems limited to netting pairs of contracts which are identical. Is this facilitating closing out a cleared position by trading an opposite one and clearing it? What are the "other detailed procedures to be provided"?	Yes - trade netting facilitates closing out a cleared position by trading an opposite one and clearing it. We refer you to the revised Rules package for the operational procedures.
Legal/Portability arrangements	NSW legal opinion required confirming the enforceability of portability arrangements.	ASX has commissioned an external Australian law legal opinion, which will be made available to Clearing Participants, to confirm the validity and enforceability of porting of a CPM Client's property in accordance with ASX's Rules on Clearing Participant default.

Sub-issue	Comment	ASX Response
Legal/Insolvency set-off	Concerned that tri-party nature of open contract and open positions interferes with mutuality requirement for insolvency under s553C Corporations Act in the case of Client, Clearing Participant or CCP. Query whether an amendment to CA is required to preserve such set-off. Request that ASX provide a clean set-off opinion.	ASX has commissioned external Australian law legal opinions with respect to close out netting and porting. In each of these two cases there is an objective reference on which a general opinion can be based, being the definition of "close-out netting contract" in the PSNA and the porting and termination provisions contained in the ASX Clear (Futures) Rules. ASX is not able to take the same approach with collateral provisions and set-off clauses which particular Clearing Participants have agreed with their Clients. ASX understands that collateral provisions and set-off provisions (which are often are linked) differ from Clearing Participant to Clearing Participant and also between Client and Client. As the effectiveness of collateral and set-off arrangements depends on the exact nature of the obligations agreed between client and Clearing Participant ASX is not able to provide a general opinion applicable to the customised arrangements which Clearing Participants have put into place. However, although it is a matter on which Clearing Participants should take their own expert advice, ASX understands that it is possible for an agent and principal to establish mutual obligations between each other which may be sufficient to establish a set-off. As noted above, this is heavily dependent on what actually is agreed between Clearing Participant and Client.
Legal/Conflict of Laws	Uncertainty as to whether the Rules may be enforceable under non-Australian laws, particularly in the insolvency of a non-Australian Client. Conflict rules amplified by the Client Protection Model due to potential for Rules to interfere with client agreements governed by non-Australian laws. What steps is ASX taking to minimise conflicts of law issues as part of implementing the Client Protection Model?	The insolvency of a Client, whether Australian or not, is not a matter covered by the Rules. The Rules do not require Clearing Participants to manage Client insolvency in any particular way. The Clearing Participant -Client agreement should deal with Client insolvency in a way that is consistent with applicable law. However, despite this, the enforceability of the Rules under Australian law is protected by the <i>Payment Systems and Netting Act 1998</i> (Cth).
Client Default	Currently there is no obligation on a Clearing Participant to notify ASX that a client has defaulted. Under the Client Protection Model provisions, is it necessary to make such a notification? If so, under what rule and in relation to what?	It is not necessary for a Clearing Participant to notify ASX that a Client has defaulted (unless the Client's default threatens the Clearing Participant's ability to meet its obligations to ASX), however, the Clearing Participant may choose to do so.
Client Default	If a client defaults and Clearing Participant takes the decision to close out the client, wouldn't all that happens be that any client sub-account relating to that client is closed? Presumably ASX's intention is not to require that the positions are transferred to the House Account first?	If a Client defaults and the Clearing Participant takes the decision to close out the Client, the Clearing Participant may request the Client's positions be transferred to the House Account for this purpose; however, ASX does not require the Clearing Participant to do so. As noted above, the Rules are not prescriptive about the way in which a Clearing Participant manages a Client default.

Sub-issue	Comment	ASX Response
Client Default	Why would ASX need to make a determination under rule 118.3 whether the client will be able to meet its obligations with respect to Open Positions when the client won't have any such obligations? (refer rule 113.1(e))	Although ASX will not take action to enforce obligations with respect to Open Positions against a Client those obligations still exist. If the Clearing Participant is in default and a Client is not in a position to meet its obligations to the Clearing Participant (or an Alternate Clearing Participant), ASX has the discretion under FR 118.3 to treat the Client as being in default for the purposes of Clearing Participant default management.
Client Default	Is ASXCF prescribing under what circumstances will a Client have defaulted or is this left to the discretion of the Clearing Participant's relevant Client Agreement?	ASX is not prescribing in the Rules what circumstances amount to a Client default. Whether there has been a Client default will be determined by the Clearing Participant with reference to the relevant Client Agreement.
Client Default	There is no limitation on ability of a Clearing Participant to declare a client in default and request a transfer of positions to its House Account. Should require Clearing Participant notifying ASX of a Client default to act in good faith, or a commercially reasonable manner, or in consideration of the best interests of the Client (118.1). Concerned about minor or technical defaults.	ASX does not propose to amend the Rules to limit the ability of a Clearing Participant to declare a Client in default. ASX cannot introduce standards of good faith or reasonableness in the Rules that would interfere with the default mechanism negotiated between the Clearing Participant and Client under their client agreement.
Client Default	Concerned that in a Client default all Open Positions are transferred to the Clearing Participant's House Account. "All or nothing" transfer is inconsistent with MIR 7.2.8(1) which contemplates that if a client is in default by failing to pay a margin call then the TP is to close out positions to the extent necessary to counter the call. Total loss of segregation may be uncommercial if default is minor, technical or subsequently cured.	ASX has amended FR 118.1(b) to acknowledge that a transfer may only be in part. Please refer to the revised Rules package.
Client Default	Not clear what credit a Client must be given for the value of its Open Positions transferred to House Account. Will monies be returned to defaulting Client?	No - The rights of a Client in a Client default are governed by the client agreement with the Clearing Participant, not the Rules.
Client Default	Not certain whether approach to Client default is compatible with client segregation rules in foreign client jurisdictions to which Clearing Participants may be subject.	The Rules provide a non-prescriptive framework under which a Clearing Participant may manage a Client default. It is the Clearing Participant's responsibility to comply with the laws and regulations that apply to it.
Representations	Are the representations in Futures Rule 112 being made by all clients or just clients that opt for an Individual Client Account?	<p>The Client Protection Model Provisions will apply to all Clients by mid-2014 – a Client cannot choose to opt out. Subject to regulatory clearance, the Client Protection Model will take effect at the time of commercial launch of the Client Clearing Service for OTC Interest Rate Derivatives (expected end Q1 2014) and ASX 24 Exchange Traded Derivatives (expected end Q2 2014).</p> <p>The representations in FR 112 are made by all Clients (Omnibus Account and Individual Client Account).</p>

Sub-issue	Comment	ASX Response
Representations	Clearing Participant and Client will not be able to determine whether ASX may breach rules or regulatory requirements under Futures Rule 112.1(k). There are considerable uncertainties as the implementation of many rules is not yet finalised and the extraterritorial aspects are often contentious and problematic. Representation should be removed or qualified by the reasonable knowledge of Clearing Participants and Clients.	ASX has qualified FR 112.1(k) by the reasonable knowledge of Clearing Participants and Clients. Please refer to the revised Rules package.
Representations	Why isn't the new representation in Futures Rule 112.1 (k) necessary currently in relation to ASX 24? Is this a consequence of the introduction of the legal modelling underlying the Client Protection Model?	FR 112.1(k) is required as a result of changes to the international regulatory landscape, not the Client Protection Model.
Representations	Why should a Clearing Participant have to make the representation in Futures Rule 112.1 (k) in addition to the client? The Clearing Participant will not know – particularly if the Client is a client of a client. Rule should instead require client to make representation to both ASX and Clearing Participant.	The Clearing Participant will only need to make the representation in respect of its Client (i.e. its direct clients, not a client of a client). The Clearing Participant completes due diligence on its Clients (e.g. Know Your Client (KYC)) and therefore has the knowledge to give this representation.
VM representations	Are the representations in Handbook 5.8 (about VM) needed if the Client's trading is in an omnibus account? What about OTC is different to futures in relation to this sort of representation?	Yes – the representations are required if the Client's trading is in an Omnibus Account. Price Alignment Interest is only paid for OTC not Futures.
Records	What is meant by “appropriate records identifying all relevant information in respect of Clients” (FR 115.6)?	The records ASX expects Clearing Participants would already maintain – identifying Client name and contact details, margin paid and positions.
Records	Is the data set out in Procedure 115 required in relation to omnibus account clients? If so, why is it necessary?	No - the data set out in Procedure 115 is not required in relation to Omnibus Accounts. Procedure 115 has been amended. Please refer to the revised Rules package.
Records	The enormity of the task of validating information relating to every single client on a yearly basis under FR 115.6 is of concern. Clearing Participants may have thousands of direct actual clients alone.	ASX does not seek to be prescriptive about the Clearing Participant's own internal validation process. However, ASX does require confirmation from Clearing Participants annually that Client details submitted to ASX are up to date.
Cross-margining	A client could have an Individual Client Account that has a different broker for ASX 24 contracts as for OTC, but still has the same Clearing Participant. Then offsets shouldn't be permitted to work.	Portfolio margining will be available if the Individual Client Accounts have the same Clearing Participant, the same Client and (if applicable) the same Nominated Person. Please refer to the revised Rules package. Clearing Participants retain control over allocation of ASX 24 ETDs for portfolio margining.

Sub-issue	Comment	ASX Response
Proportionate liability	Have you considered how the proportionate liability regimes might impact on this relationship? Should they, where possible, be disapplied?	The proportionate liability regimes should not be applicable to the contractual allocation of liability to the Clearing Participant of the obligations which are owed to ASX. However, it is possible for a Clearing Participant and Client to agree allocation of risk and contribution between each other in respect of those liabilities which the Clearing Participant owes to ASX.
Client Ag Contribution rights	Do you envisage that in the client agreement between the Clearing Participant and the Client the Clearing Participant would seek to expressly cover contribution rights? For example, if ASX proceeds against, and recovers from, the Clearing Participant, the Clearing Participant might then seek contribution from the Client.	Contribution rights are a matter for the Clearing Participant and Client to agree. Inclusion of a provision dealing with contribution rights in the client agreement would not be inconsistent with the Client Protection Model.
Block trading and allocation	Clarification required around how block trading and post trade Allocations operate under the Client Protection Model.	The Client Protection Model does not change the existing procedures with respect to block trading and post trade Allocations.
Transfers	BAU transfers happen now and presumably all parties act in an appropriate commercial manner. Is there a particular concern that ASX has noted in the legal market?	ASX has not identified a particular concern around BAU transfers.
Preservation of existing Futures model	Clearing Participants want ability to opt-in to the Client Protection Model (rather than have it mandatorily apply) so they have maximum flexibility to structure their clearing business as they wish.	ASX is moving from a Principal Model to the Client Protection Model in response to client feedback that favours explicit recognition by ASX, and in a way that preserves optionality for Clearing Participants with respect to their business arrangements; the Client Protection Model does not require Clearing Participants to change their clearing business model, and the decision to offer one or multiple account options will be the Clearing Participant's decision.
Porting	Why does ASX need the flexibility to port without Guaranteed Initial Margin Value under FR 120.2?	In the event of a Clearing Participant default, ASX may wish to port the individual positions of a Client in an Omnibus Account without margin to an Alternate Clearing Participant if that Client consents. It may be important to a Client in an Omnibus Account for its positions to be preserved even if it has to recollateralise those positions with an Alternate Clearing Participant.
D1 Do you agree with the primary operational role of the Clearing Participant under the Client Clearing service or should clients have more direct operational engagement with ASX? Why, and what form would that take?		
Clearing Participant primary role	Support ASX proposal that Clearing Participant have primary operational role under the Client Clearing Service for reasons including: <ul style="list-style-type: none"> - The risk that a more direct operational engagement between Client and ASX will become too complicated and potentially confuse the rules and obligations of everyone else. - If Clients had more operational engagement with ASX, then the liability of the Clearing Participant cannot be absolute because the Clearing Participant is principally liable to the ASX. 	There was unanimous support for ASX's proposed approach for Clearing Participants to maintain the primary operational role under the Client Clearing service. ASX will proceed on this basis.

Sub-issue	Comment	ASX Response
	<p>- A Clearing Participant is best placed to face the client from an operational basis because it is the Clearing Participant (rather than the CCP) that completes KYC process, credit checks, and has visibility to positions on other exchanges as well as other asset classes.</p>	
ASX contact for clients	Suggest ASX provides direct 'helpdesk' type contact for Clients in addition to enabling transparency of client positions, IM calculations, fees, interest, valuations, haircuts, collateral holdings.	Any questions or concerns in relation to data provided by ASX to Clients should first be directed to the Client's Clearing Participant. If a Client's questions or concerns cannot be addressed by the Clearing Participant, ASX expects Clearing Participants to escalate these matters to ASX.
ASX contact for clients	The ASX is making position and guaranteed initial margin value reports available to Clients. Would the ASX make data available direct to clients utilising the Individual Client Account? Are clients able to query these direct with the ASX? Similarly, can clients query the Fact Sheet direct with the ASX as well?	ASX will provide prescribed data to Clients to enable them to effectively reconcile their positions and accounts against that provided by their Clearing Participant. Any questions or concerns in relation to this data should first be directed to the Client's Clearing Participant. If a Client's questions or concerns cannot be addressed by the Clearing Participant, ASX expects Clearing Participants to escalate these matters to ASX. ASX will respond to Client queries on the Fact Sheet.
E1 Do you have any comments on the restrictions that apply to Clients in relation to OTC Client Clearing?		
Due diligence	Due diligence of clients in some form should be implemented as part of good governance by the ASX. Need to strengthen acceptance criteria for Clients.	In the ordinary course of business, ASX does not take counterparty exposures to Clients and it is therefore the Clearing Participant that has primary responsibility for risk management due diligence on the Client. However, ASX does monitor Client exposures and in some circumstances, the nature of the Client and/or its exposure may result in ASX taking action to mitigate any unacceptable risks.
Jurisdictional restriction	Concerned that approach will limit the scope of clients that can enter into the cleared market in Australia which may have an impact on liquidity and scale. Please provide guidance on timing around restrictions. When does ASX expect these to be broadened? These restrictions create some inefficiency from a capital and operational perspective and a need for additional documentation and due diligence procedures.	ASX will seek to expand the range of eligible OTC Clients as regulatory clearances become available in other jurisdictions. ASX is investigating Singapore and Hong Kong initially.
Wholesale restriction	Why must an OTC client be a wholesale client – is ASX providing a financial service?	This requirement does not relate to whether or not ASX is providing a financial service. This requirement reflects the wholesale nature of the OTC market.
Jurisdictional restriction	Is the "connected with Australia" requirement prompted by tax (IWHT) or foreign regulations?	The requirement that a Client be "connected with Australia" is driven by the need to ensure that ASX does not operate the service without necessary foreign regulatory approvals.

Sub-issue	Comment	ASX Response
Representations	If ASX has a direct contractual connection with the client, why must the Clearing Participant also represent that the client is wholesale and has an Australian connection? (OTC Rule 2.16)	The Clearing Participant completes due diligence on its Clients (e.g. KYC) and therefore has the knowledge to give the representation that the Client is wholesale and has an Australian connection.
<p>F1 Where a Client that is a RBC of the Clearing Participant acts as principal or as agent for other RBC only, ASX proposes to permit the Client's positions to be designated as 'Client' positions, on condition that the positions are allocated to an Individual Client Account that is maintained for the Client, and the Clearing Participant maintains a separate Clients' Segregated Account (outside the clearing facility) for funds in respect of those positions. Is it desirable to permit positions of a RBC of the Clearing Participant in these circumstances to be designated as 'Client' positions? Why or why not? Are the conditions to designation of such positions as 'Client' positions, as proposed by ASX, appropriate?</p>		
Designation of RBC positions	<p>Support ASX proposal to permit group positions of an RBC to be treated as Client for reasons including:</p> <ul style="list-style-type: none"> - Consistent with European position that provides for affiliated positions to be designated as Client - It will enable RBCs of defaulting Clearing Participants to port their positions to an Alternate Clearing Participant - Proposal does not detract from existing client protections under Corporations Act - Consistent with Corporations Act which does not distinguish between clients that are RBCs and those who are not 	<p>Submissions have identified inconsistencies in relation to the treatment of positions and money of related bodies corporate between the Corporations Act, Market Integrity Rules and ASX's proposal. Given the significance of these inconsistencies and the need for regulatory reform of client money rules identified by stakeholders, ASX has decided that it should not pre-empt the outcome of regulatory reform and risk further complicating an already complex area by proceeding with its proposed changes at this time. Accordingly, ASX will not proceed with these changes as part of the revised Rules package.</p>
Designation of RBC positions	Do <u>not</u> support ASX proposal that RBC group positions be treated as Client. RBC group positions should remain house, consistent with current ASX rules.	ASX has modified the draft Rules to recognise that cash collateral returned by ASX to OTC Clearing Participants may include monies referable to client positions in OTC Interest Rate Derivatives which the law may require to be paid into a client money account that is not an ASX 24 Clients' Segregated Account.
Designation of RBC positions	Appears to be an acceptable approach as long as the appropriate rules are in place to ensure integrity in the market and client protection is maintained as intended. These rules should extend to appropriate monitoring by the ASX, regulators and Chinese walls being in place to ensure preferential treatment is not given with the Clearing Participant's related entities.	
Designation of RBC positions	What legal analysis has been undertaken to assure Clearing Participants that if a RBC is treated as 'house', the Clearing Participant will not be in breach of the Corporations Act?	
Designation of RBC positions	Please explain the relationship between how RBC positions are designated and Account levels. Where does the RBC and unrelated end-user sit in this account structure?	
Designation of RBC positions	Can a Clearing Participant really be said to be acting as "agent" of an unrelated third party in a chain of intermediated entities, even if this is said to be indirect? Does it matter?	

Sub-issue	Comment	ASX Response
Designation of RBC positions	Is it sufficient for the Clearing Participant to obtain a representation from its RBC that the RBC is acting for unrelated third parties or is it intended that the Clearing Participant undertake due diligence to ascertain whether or not the RBC's clients are in fact unrelated?	
RBC definition	How will ASX define RBC? Will it include subsidiaries that are 100% owned by the Clearing Participant or will it be limited to entities within the same group and with the same parent entity?	
RE / Trustee	REs / Trustees. What is the situation where the RBC of a Clearing Participant is a responsible entity or trustee? Does this fall within the end user client category or principal category. Legally, it would be in the principal category, which should not be the result we suspect.	
Transition	Transitional. How is this to apply to ASX24 when only omnibus accounts are allowed?	
ASIC MIRs	How does this sit with the ASIC Market Integrity Rules which treat RBC as non clients?	
Condition/Designation of RBC positions	The requirement for Individual Client Accounts to be used for RBC group positions represents additional accounts, additional operational risk and additional compliance costs. The splitting between RBC group positions and RBC unrelated third party positions adds a great level of complexity which may not be justified by the perceived benefits to clients.	
Condition/RBC monies	If the "house" option is chosen, is it still permissible to have any money received from the client placed in the CSA?	
Condition/RBC monies	Why is it necessary for ASX to impose these requirements on Clearing Participants when the Corporations Act already regulates handling of client money?	
Condition/RBC monies	Corporations Act does not require AFS licensee to treat money of an RBC that is a client differently from money received from a non-RBC. How will ASX's proposal interact with Corporations Act?	
Condition/RBC monies	CSA rules have apparent effect of changing the way a licensee deals with its clients in relation to potentially only one small part of its business through its trading on ASX. For the rest of the licensee's business, there is no obligation to treat money received from clients that are related bodies corporate differently depending on who they are acting for. This adds complexity and risk for global brokers.	
Condition/RBC monies	Is it intended that an ASX24 Clearing Participant must run separate CSAs for RBCs (on one hand) and non RBCs and RBCs acting for UTPs (on the other)? Does this cause any technical issues when settling?	

Sub-issue	Comment	ASX Response
Condition/RBC monies	<p>Concerned by constraints imposed by Corporations Act, MIRs and proposed ASX rules</p> <ul style="list-style-type: none"> ASX 24 MIRs require that only client money received from clients in relation to ASX 24 is to be placed into the CSA. RBCs are not clients under MIRs. However, Corporations Act still regards RBC money as client money so this has to go into a separate trust account. Corporations Act contemplates a CSA which can contain client money from all sources. However, ASX 24 MIRs require that only money received in relation to ASX 24 activities be placed in CSA. Monies for the same clients in relation to other exchanges or OTC have to go in separate CSA. ASXCLF will require a separate CSA for monies of RBCs clearing for themselves or other RBCs. Is this 2 additional accounts? (i.e. one for OTC and one for ASX 24) 	
Condition/RBC monies	Proliferation of CSAs increases risk Clearing Participant will make a mistake in managing client money and represents significantly more work for Clearing Participants without commensurate additional protection for clients.	
Condition/RBC monies	The CSA requirements for each such underlying client are unduly burdensome and have significant netting implications.	
Condition/RBC monies	In order for proposed CSA changes to work, ASX would need to have the ability to see and monitor CSAs outside of the ASX clearing facility. This would involve addressing client confidentiality across multiple clearing houses and locations.	
Audit report	Divergent approach under MIRs and ASX Rules as to who the audit report must go to.	
Audit report	Where is the obligation that audit report covers client money as per MIR 2.3.5?	
Audit report	MIR's auditor's report is to cover compliance with rule 2.2.6 of the MIRs (i.e. CSA obligation). How will this be handled under ASX rules?	
Multiple CSAs	There is a requirement for multiple CSA accounts. We currently have ASIC/ASX approval for a single Client Segregated Trust Account.	

Sub-issue	Comment	ASX Response
F2 Do you consider there may be any unintended consequences of the proposed amendments to the definitions of 'Client' or 'Clients' Segregated Account' in Futures Rule 1.1?		
Client definition	Why have ASXCF chosen to define a client on the basis of the Clearing Participant entering into, acquiring or disposing of a market contract? This is the role of the Trading Participant, it may be the case that a Clearing Participant does none of these things.	ASX has amended the definition of 'Client'. Please refer to the revised Rules package.
Client definition	How do we work out who a Client is (i.e. the entity we need to sign the 4.14(j) agreement and who we send the notice to under Rule 112 in the Procedures)? Is the definition of "Client" capable of picking up anyone that is not currently our actual client (i.e. reach further into the "end user" territory than our immediate client)? Clients should be restricted to persons on-boarded with ASX as Clients by a Clearing Participant. This will avoid potential issues arising between a Clearing Participant and end users the Clearing Participant does not wish to treat as clients.	The definition of 'Client' is intended to identify, and has been modified to identify, only the person or entity who is the Clearing Participant's immediate client (i.e. the person with whom the Clearing Participant has a Client Agreement and for Individual Client Account, the person on-boarded at ASX as the 'Client'). Please refer to the revised Rules package.
CSA definition	Is the definition of 'Clients' Segregated Account' correct? There are no rules requiring a Trading Participant to maintain a CSA in the Exchange Operating Rules. Should this be a reference to the ASIC MIRs?	ASX has amended the definition of 'Clients' Segregated Account' to refer to the ASIC MIRs. Please refer to the revised Rules package.
Significant % of business operations	A client clearing model under which Clearing Participant has a related body corporate as its Client which faces end-users will likely find such a Client represents a significant percentage of its business operations. Clarification on scope of rule 4.14(l) is desired in relation to the Client Protection Model.	For the purpose of managing Client concentration risk, ASX currently uses Daily Beneficial Ownership Reports to provide information about the beneficial owners of Client positions. Accordingly, it is not expected that the scope of rule 4.14(l) will change with the implementation of the Client Protection Model.
Timing of payments	The close out/portability arrangements of CSA funds do not take into account timing of transfers of payments such as initial margin. For example, initial margin is paid by the Clearing Participant from its operating account and then an adjustment made to the CS(T)A (and also from the underlying account bookings).	Neither the porting process nor the legislative protections for porting given by the <i>Payment Systems and Netting Act 1998</i> (Cth) extinguishes accrued rights and obligations between the Clearing Participant and Client (for example with respect to margin funded by the Clearing Participant).
F3 In order for an end user client to gain the protection of the Individual Client Account option, where the Clearing Participant chooses to offer it, the end user client would need to have entered into a client agreement with the Clearing Participant on terms consistent with the minimum terms prescribed by ASX. What consequences flow from the requirement for a client agreement in these circumstances? Please provide details of any financial or regulatory implications of a Clearing Participant contracting directly with end user clients that wish to take up the Individual Client Account option. Are those implications (if any) likely to affect Clearing Participants' ability to offer the Individual Client Account option or end user client demand for it? If so, why?		
Need for legal agreement	Could the legal need for an agreement between a Clearing Participant and an end-user (or any entity other than our actual client) be explained? It is also not clear whether or not such terms are required from a Clearing Participant's actual client, or just the client of their client (presumably both, but perhaps this could be made clear)?	ASX has modified its approach to better accommodate multi-level client structures: end user clients that seek individual segregation may either (i) contract directly with a Clearing Participant (i.e. as the 'Client'), or (ii) be nominated by an entity (e.g. broker) that is itself a 'Client' of a Clearing Participant.

Sub-issue	Comment	ASX Response
Offshore clients	Clients (particularly offshore Clients) will need to consider any tax and regulatory implications in connection with (i) being 'on boarded' as a Client at the ASX in Australia and (ii) signing and agreeing to certain minimum terms with the Clearing Participant, if such steps constitute any business activity in Australia for that Client.	<p>In the latter case (ii), in the event of the Clearing Participant's default, ASX will:</p> <ul style="list-style-type: none"> • Take porting instructions from the Nominated Person in respect of the Individual Client Account; and • If the Client's positions and IM value in respect of the Individual Client Account cannot be ported, will remit the residual IM directly to the Nominated Person's bank account. <p>ASX's revised approach will enable broking firms to offer end user clients the benefits of ASX's individual segregation option without the Clearing Participant needing to contract directly with end user clients.</p> <p>We refer you to Schedule 4 in the Response to Consultation for further details.</p>
Offshore clients	Regulatory issues may prevent Clearing Participants from contacting directly with end clients e.g. where end client is retail and Clearing Participant only holds a wholesale AFSL, where Clearing Participant only deals with RBCs and does not have an AFSL, and regulatory requirements in offshore jurisdictions where end clients are located.	
RBC clients	Documentary steps required for clients of RBCs as Clearing Participant will be responsible for having clients of its RBCs agree to the minimum terms prescribed by ASXCF and onboarded.	
Onboarding	Problems may arise with onboarding requirements (e.g. KYC and credit assessment)	
Increased Clearing Participant risk	Concerned about risk of claim by end user against Clearing Participant (e.g. if we close out positions of immediate client who has defaulted). Court may find Clearing Participant owes obligations as broker to end-client, in conflict with obligations we owe actual client.	
Alternative proposal	If end result that ASX is seeking to achieve is to have end user client bound to the rules so that ASX will be in a direct contractual relationship with the client for the purpose of porting the client's positions to a new Clearing Participant this can be achieved in another way. Propose an alternative model similar to RHCCA forms on ASX Clear under which Clearing Participant arranges for client to provide necessary authorisations to ASX to deal with collateral lodged with ASX in event of Clearing Participant default. The rules could provide that where an end user client wishes to set up an Individual Client Account, the Clearing Participant must provide a copy of the disclosure and also obtain from that end user client an agreement (in ASX standard form) undertaking to be bound by the rules on the default of the Clearing Participant and making the necessary representations. Under this model, the Clearing Participant would not need to enter into an agreement with end user client. The Clearing Participant would simply be facilitating the relationship between ASX and end user client.	
Alternative proposal	Alternative approach would be for the ASX to allow RBC accounts to be established as individual numbered client accounts held by the Clearing Participant on behalf of the RBC's end clients (i.e. not omnibus).	

Sub-issue	Comment	ASX Response
Representations	What are consequences for a Client of representations being “fundamental conditions” (r 112.1)? Do the Rules intend to evoke the doctrine of fundamental breach? This reference should be removed. A breach of Rule 112.1 by a client should be treated as a Client default under r118.	ASX has removed the reference to “fundamental” in Rule 112.1. Please refer to the revised Rules package.
G1 What impact will the introduction of ASX’s Client Clearing service have on existing client documentation, both for ASX 24 ETD and OTC IRD?		
Addendum	The new FIA ISDA addendum could be used with the new ASX Client Protection Model, although the US references are unnecessary. This is why some Australian clients have asked the ASX to provide a sample Australian agreement, we would expect this to be consistent with FIA.	ASX’s sample Cleared OTC Derivatives Supplement incorporates features of both the FIA and FOA addendums. ASX has sought to simplify and express in plain language these features in a manner suited to client documentation in use in the Australian market.
Documentation review	The recognition by ASX Clear Futures of a Client as principal and not as trustee, as agent or as acting in any other capacity, will require both Clearing Participants and existing Clients to review existing Client documentation and, for those Clients opting for the Individual Sub-Account, ensure consistency with the Client on boarded at ASX.	Futures Rule 113.5, that ASX is entitled to deal with a Client as principal, should not require existing client agreements to be reviewed. The Rule is simply to ensure that, as between ASX and the Client, ASX may rely on porting instructions given by the Client (or third person nominated by the Client in accordance with the Rules) and need not take notice of instructions that any other third party may purport to give to ASX.
Documentation review	The ASX does not prescribe any additional documentation for the Client Protection Model. From a Clearing Participant’s perspective for regulatory capital we need provisions outlining the Clearing Participant will not guarantee the performance of the CCP. We’re not aware of any provisions in Part 10 which cause Clearing Participants to guarantee the performance of the ASX.	There is no such guarantee in the Rules. Clearing Participants have no obligation to replenish Commitments (FR7.6).
Repapering	The clearing documentation for most Clearing Participants is predicated on the principal model. The references to Rules etc may not require a change to documentation. However, the change to the nature of the relationship between client and Clearing Participant, the affiliate arrangements, client segregation trust account implications, acknowledgement of the receipt of the fact sheet and the security interest implications will require a re-papering for clients.	<p>It should not be necessary for those Clearing Participants who (or whose related brokers) do not intend to offer Clients the individual segregation option to amend the terms of existing client agreements.</p> <p>Those Clearing Participants who (or whose related brokers) do intend to offer Clients the individual segregation option will need to satisfy themselves that existing client agreements do not require amendment – the cost of making any necessary amendments would be factored into the Clearing Participant’s commercial decision to offer individual segregation.</p>

Sub-issue	Comment	ASX Response
Inconsistency	Rule 112.1(m) that provides that the Client Protection Model Rules prevail over client agreements in the event of any inconsistency is too broad and unduly interferes with client agreements by interfering with the risk allocation in contracts between the Client and its Clearing Participant. Suggest scope of rule 112.1(m) is narrowed so Rules only override agreements between the Clearing Participant and Client to the extent necessary to ensure the effectiveness of these Rules. The Rules should only prevail where there is a clear and direct inconsistency, such that effect cannot be reasonably given to both clauses.	<p>ASX 24 ETD Clearing Participant client agreements typically contain a provision to the effect that the CCP's Rules as in force from time to time prevail to the extent of any inconsistency with the client agreement; the Client Protection Model Provisions go no further than this usual contractual stipulation.</p> <p>The Client Protection Model Provisions are intended to give protections to Clients and Nominated Persons (where applicable). These protections cannot be contracted out of.</p> <p>Based on the common law meaning of inconsistency, the Client Protection Model Provisions will only prevail in circumstances where there is a direct inconsistency.</p>
Return of IM	Concerned return of IM directly to Client counter to documentation between Clearing Participant and Client. In Futures segment, there is a Liquidation Amount which uses IM as part of calculation. If IM has been paid by ASX IM will need to be removed from calculation of Liquidation Amount.	Any Clearing Participant evaluating the commercial risks and returns of offering the Individual Client Account option will need to factor in changes to documentation that recognise that on a Clearing Participant default ASX will remit Guaranteed Initial Margin for Individual Client Accounts directly to the Client if porting is not achieved. It is the Clearing Participant's choice whether to make Individual Client Account available or not.
G2 ASX has sought to avoid taking a more prescriptive approach to documentation between Clearing Participant and Clients. Should ASX be more prescriptive, e.g. by prescribing the form of clearing agreement to be used?		
No	Support ASX providing sample clearing agreement on the basis that this is likely to reduce legal costs and negotiation time but do not think sample should be made mandatory.	While different views have been expressed to ASX on this matter, the balance of consultation feedback favours ASX not taking a more prescriptive approach to documentation between Clearing Participant and Clients.
Yes	ASX should be more prescriptive and mandate a standard client clearing agreement for use in ASX OTC clearing. This approach offers advantages in terms of cost savings, efficiency, may enable more efficient porting, improve the ability to appoint Alternate Clearing Participants and minimise negotiation time.	Submissions in favour of further prescription have not highlighted advantages that would outweigh the disadvantages arising from the inability of Clearing Participants and Clients to negotiate their own arrangements. Accordingly, ASX intends to continue prescribing minimum terms rather than a form of client agreement. ASX has sought to assist Clearing Participants and Clients by providing a sample Cleared OTC Derivatives Supplement that can be utilised with either a Futures Agreement or an ISDA Master Agreement.
International consistency	Clearing annexes and addendums should be consistent, where possible, with addendums in other jurisdictions.	ASX's sample Cleared OTC Derivatives Supplement incorporates features of both the FIA and FOA addendums.

Sub-issue	Comment	ASX Response
G3 Should the minimum terms for client agreements in Rules 4.14(j)(v) (Margins) and 4.14(j)(ix) (Right to refuse to deal) be disapplied for OTC Client Clearing on the basis that these terms would be expected to be superseded by any bilateral documentation in place between Clearing Participant and Clients?		
No	We favour the retention of these provisions as minimum terms. From the perspective of the Clearing Participant, these provisions should be basic and uncontentious and provide key protections (from a risk, credit and legal perspective) for the Clearing Participant given that it is fully liable as principal. Their inclusion as minimum terms means they have the imprimatur of the ASX, thereby facilitating negotiation with Clients.	ASX will disapply 4.14(j)(v) (margins) for OTC Client Clearing on the basis that terms related to provision of margin by Clients are heavily negotiated in the OTC market. ASX does not intend to disapply 4.14(j)(vi) (Appointment of Attorney) or (ix) (Right to refuse to deal) for OTC Client Clearing.
Yes	4.14(j)(v) (margins) should be disapplied due to risk of inconsistency with margining arrangements in place between Clearing Participant and Client. 112.1(m) (client reps) may also affect margining arrangements. 4.14(vi) (Appointment of attorney) can be disapplied because of overlap with 10.9. No need to disapply 4.14(j)(ix) as this is just an acknowledgement.	
ASX 24 ETD vs OTC IRD	What is the basis for distinguishing between Futures and OTC in relation to margin provisions? The "Right to Refuse to Deal" provision seems inappropriate for OTC generally.	
G4 Does ASX's proposed approach to client agreements provide adequate legal certainty for Clearing Participant and Clients? Do you consider that further or alternative steps could be taken to give greater certainty, and would that require client agreements to be modified?		
NSW legal opinions	Suggest greater legal certainty could be provided if ASX provided a NSW legal opinion to all Participants confirming the enforceability of the close-out netting, the portability and the bankruptcy remote arrangements.	ASX has commissioned external Australian law legal opinions, which will be made available to Clearing Participants, to confirm: <ul style="list-style-type: none"> that the proposed changes to ASX's clearing model (Client Protection Model) will not affect the application of the <i>Payment Systems and Netting Act 1998</i> (Cth) to close-out netting of obligations owed between a Clearing Participant and its Client under a close-out netting contract between them; and The validity and enforceability of porting of Client property in accordance with ASX's Rules on Clearing Participant default. As indicated in the consultation paper, ASX's Client Clearing Service will not offer a "bankruptcy remote" collateral holding structure initially.

Sub-issue	Comment	ASX Response
More details around Settlement Finality	New Rule 103.2 relates to Settlement Finality. Suggest this rule is not sufficiently detailed to address the requirements of Standard 8 of FSS for CCPs. Consideration should be given to more provisions dealing with revocability and more detail on when a payment is “made”.	FR 103.2 is consistent with FSS8. Payments will be “made” in accordance with the rules of the relevant payment facility (e.g. Austraclear Regulations).
G5 Is the Client Fact Sheet sufficiently clear and does it contain enough detail? What other information should be included?		
Requirement for Client Fact Sheet	<p>Where does the requirement for a client fact sheet come from? Was this a regulator requirement?</p> <p>Rule 112.1(g) goes beyond the requirements of Financial Stability Standard 13.4. We are not clear on how this Standard can be relied on to impose an end user disclosure obligation on RBC Clients.</p>	The purpose of the Client Fact Sheet is to discharge ASX’s obligation under the FSS to disclose its rules, policies and procedures relating to the segregation of a participant’s customers’ positions and related collateral, including whether customer collateral is segregated on an individual or omnibus basis and any constraints, such as legal or operational constraints, that may impair its ability to segregate or port a participant’s customers’ positions and related collateral.
Provision of Client Fact Sheet	<p>Concerned (that under r 112.1(g)) Clearing Participant (or RBC) will have to give Client Fact Sheet to all end clients of an RBC. This is impractical as there may be thousands of end-user clients, the majority of whom are outside Australia.</p> <p>Obligation should be limited to Clearing Participant’s own clients. This is consistent with approach ASX has taken in other areas such as margin calculation and participation in the Risk Committee.</p>	<p>In response to feedback, ASX will require Clearing Participants to direct only Clients (i.e. immediate clients with whom the Clearing Participant has a client agreement) to the Client Fact Sheet. Please refer to the revised Rules package.</p> <p>Twelve months after launch of the Client Protection Model, ASX intends to assess market awareness among Australian end users about the account segregation options available under Client Protection Model and reconsider whether there is a need for a more extensive distribution obligation.</p>
Provision of Client Fact Sheet	The Clearing Participant should be able to direct its Client to provide the statement to the Client’s client as the Clearing Participant won’t have a relationship with them. There are various regulatory restrictions on the Clearing Participant dealing with end-user clients that may restrict its ability to provide the client fact sheet itself.	
Provision of Client Fact Sheet	Futures Rule 112.1(g) contemplates that the Fact Sheet be sent two-levels down the chain. Not all end users will be reached if the fact sheet is distributed merely two levels down.	
Provision of Client Fact Sheet	Rule 112.1(g) goes beyond the requirements of Standard 13.4. We are not clear on how this Standard can be relied on to impose an end-user disclosure obligation on RBC Clients.	
Provision of Client Fact Sheet	Should there be an obligation on an investment manager opening clearing accounts on behalf of Clients to inform the Clients of this Fact Sheet also?	The Client Fact Sheet must be given to the ‘Client’, which may be the investment manager or the trustee(s) of the relevant fund(s), depending on choice at account setup.

Sub-issue	Comment	ASX Response
Client acknowledgement	What form of acknowledgement of receipt of the Fact Sheet is a Clearing Participant required to obtain? That the client was directed to a copy of the Fact Sheet? The requirement to procure an acknowledgement of receipt of the Client Fact Sheet will be very burdensome for Clearing Participants and global brokers. The representation in the rules should be enough.	In response to feedback, no form of acknowledgement will be mandated. However, a Clearing Participant will need to implement whatever compliance controls it believes are sufficient to discharge its obligation to provide or direct Clients to the Client Fact Sheet in accordance with the Rules. ASX may require a Clearing Participant to attest annually that it has provided or directed Clients to the Client Fact Sheet in accordance with the Rules.
Provision of Client Fact Sheet	There should be a defined look-back period in relation to who constitutes an end client for the distribution of the Client Fact Sheet.	<p>Upon the commencement of the Client Protection Model Provisions with respect to classes of Market Contracts, Open Contracts, Clearing Participants or Clients (as applicable), a Clearing Participant must:</p> <ul style="list-style-type: none"> (a) In respect of each of its existing Clients for which it holds an open position to which the Client Protection Model Provisions apply; and (b) In respect of each of its other existing Clients not covered by (a), before, or if not practicable as soon as practicable after it next holds an open position to which the Client Protection Model Provisions apply (for example, where the Clearing Participant is not the executing broker), provide the Client Fact Sheet to such person or direct such person to a copy of the Client Fact Sheet. <p>Once the Client Protection Model Provisions have commenced, a Clearing Participant must provide each new Client with the Client Fact Sheet or direct such person to a copy of the Client Fact Sheet before the Clearing Participant holds an open position for that Client.</p> <p>A Clearing Participant will only be required to provide a Client Fact Sheet to a particular Client or direct that Client to a copy of the Client Fact Sheet once.</p> <p>Accordingly, there will be no need for a defined look-back period. We refer you to Futures Procedure 112 of the revised Rules package.</p>
Provision of Client Fact Sheet	<ul style="list-style-type: none"> - Does the obligation exist for clearing clients only? - What documentation and record keeping requirements are there? - What format does the direction to the client to the Fact Sheet have to take? - It is assumed that only direct clients trading ASX 24 products need to be directed to the fact sheet. Is this correct? 	<ul style="list-style-type: none"> - The Client Fact Sheet only applies to clearing Clients. - The Client Fact Sheet does not need to be provided to Clients in paper form. Clients may be directed to the Client Fact Sheet on the ASX website. - The Client Fact Sheet applies to Clients trading ASX 24 ETDs or OTC IRDs.

Sub-issue	Comment	ASX Response
H1 Under the FSS for CCP, ASX's Risk Committee must comprise representatives of indirect participants "depending on the scale and nature of client clearing activity." In your view, what scale and nature of activity warrants Client representation?		
Transaction volume	Representatives should include Clients whose business volume could reasonably be considered to have a material impact on the good functioning of the market as a whole. For example, complex/exotic but small volume business would not reasonably be qualifying. ASX should value "scale" over "nature" in determining client participation in the Risk Committee.	<p>ASX acknowledges 4 key themes from the responses to this question:</p> <ul style="list-style-type: none"> - Volume in addition to IM should be the measure of scale of client clearing activity. - There should be a cross-section of client types represented on the Risk Committee. - The Client representatives should not be related to the Clearing Participants. - Client representatives on the Risk Committee should have the relevant risk skill set. <p>Nomination and selection procedures for Client representatives on the Risk Committee will be the subject of further consultation and a rule proposal in 2014.</p>
Transaction volume	Qualification should be based on volume of transactions (as a proportion of either the Clearing Participant's transactions, or gross ASX transactions) and perhaps diversity across types of trades. The Risk Committee should represent the different legal and entity types of Clients (and the end user clients they may represent), e.g. life insurance, superannuation funds, hedge funds, custodian banks, investment managers, as each have different requirements regarding the collateral it is required to post and the consequential structure of the client accounts.	
Transaction volume, gross notional and level of IM	Assessment of potential indirect members should be based off volume, gross notional, level of IM.	
2 nd tier banks	We firmly believe 2 nd tier bank representation is required outside of the majors and international banks. A cross section of representation is required to appropriately address risks at different levels of client types.	
Industry bodies	This approach is recognised as incorporating non-broker representation. Rather than assigning scale, would it be appropriate to invite representation from relevant industry bodies that represent the Australian market?	
Query criteria	Reliance on "scale" to assess participation of clients in Risk Committee may be difficult if measured using IM because this could potentially include clients who have only a few very long-dated large notional OTC contracts and exclude clients who have a flat book because of portfolio margining.	
Criteria	We would like to see the following requirements for indirect participants (IP's): □ IP's should not be related entities of the Clearing Participant; □ IP's should be wholesale/professional parties; □ There should be a limit on how many clients of the same Clearing Participant are allowed as IP's; There should be a mix of broker, fund manager and proprietary trader IP's on the committee.	
Criteria	Representation should be extended to sophisticated clients with large trading volume who have the necessary risk skill set.	

Sub-issue	Comment	ASX Response
	Fundamental question whether clients should be represented on Risk Committee given they have no skin in the game.	
H2 What nomination and selection procedures should be put in place to select Client representatives for the Risk Committee?		
Description of procedures	Open and transparent, based on rules and a process agreed by the governing regulatory bodies as this would apply to all key nominations of risk governance.	Nomination and selection procedures for Client representatives on the Risk Committee will be the subject of further consultation and a rule proposal in 2014.
Aim of procedures	<p>The nature and composition of the Risk Committee should reference that Committee's mandate and be subject to consideration regarding the powers that the Committee may wield and the basis upon which any such powers can be invoked.</p> <p>The Committee will need to be knowledgeable and have appropriate experience but also be fair and balanced with respect to its members and their interests. Procedures need to address the appointment of Committee members, their ongoing suitability (fitness and properness)</p>	
Aim of procedures	Need to ensure a cross section of clients are always represented. A transparent nomination process is also required to ensure a level playing field.	
Proposed nomination and selection procedures	<p>Potentially take the top 3 for each category of transaction volume, gross notional and level of IM to make an eligible list of indirect clients to select Voting Client members and non voting client members. There needs to be accompanying qualifications in addition to the client requirements provided already (potential licences that need to be held, solvency etc...)</p> <p>Procedures would then be needed to:</p> <ol style="list-style-type: none"> 1. Select the first year client members (voting / non voting) 2. Designate clients in breach of the requirements to be a member and process for terminating their committee membership and appointing of replacement client member. 3. Selection process of new client members for year "n". Should be an element of "holdover" membership to ensure element of consistency in client views. 4. Process for handling disputes to termination of membership on the committee. 	
Proposed nomination procedures	Client representatives should be encouraged to nominate themselves and selection should be based on knowledge and experience	

Sub-issue	Comment	ASX Response
Proposed nomination and selection procedures	Nomination and selection procedure should be similar to the manner in which ASX selects or nominates representatives for the Risk Committee.	
Proposed selection procedure – rotation	Suggest a rotation schedule for Client representatives. Number of Client representatives should not exceed a predefined percentage of risk committee (e.g. offshore CCP – no less than 10% but no more than 50%). One representative per Client.	
Voting rights	Client representatives should have limited voting rights given they provide no Commitment.	
I1 Do you have any comments on the proposed security interest provisions in Part 11?		
Return of non-cash collateral	If a Clearing Participant posts non cash collateral, does the ASX undertake to return the same specific collateral to the Clearing Participant? The Clearing Participant may be obliged to return collateral to the Collateral identical to the collateral delivered by the client to the Clearing Participant, in which case the Clearing Participant would want to ensure it could receive identical collateral from the ASX.	ASX will return fungible rather than the same specific collateral to non-defaulting Clearing Participants.
Adjustments to Part 11 given the Client Protection Model	The Client has a direct legal relationship with ASX and may therefore be regarded as the security provider under the Client Protection Model. Query whether Part 11 must be further adjusted. For example, is it necessarily the case that the Clearing Participant (instead of the Client) which is the beneficial owner of the Secured Initial Owner (rule 124.2)? If the Client (and not the Clearing Participant) is correctly the chargor, should ASX require the assistance of the Client, rather than the Clearing Participant (rule 124.7)? Does ASX also need the consent of the Client (rule 124.6)?	The Clearing Participant (and not the Client) is required to provide collateral to ASX (FR 116.2). The rules do not contemplate the Client providing cash or non-cash collateral (whether by transfer or security) directly to ASX. The Clearing Participant must ensure it is the beneficial owner of non-cash collateral the subject of the security interest (FR 124.2).
Implications for Clearing Participant and client arrangements	If the ASX considers the possibility of taking a security interest in collateral rather than its absolute transfer, is there an intention that this should be mirrored by how the Clearing Participant takes collateral from its client? This would need broader review in terms of legal enforceability issues, PPSA registration administration and operational risk.	Part 11 may not affect the arrangements in the Client Agreement under which a Client provides margin to the Clearing Participant. However, if the Clearing Participant grants a security interest to ASX under Part 11 it must ensure it is the beneficial owner of the relevant non-cash collateral (FR 124.2).
Application of Part 11	ASX should provide clarity as to which (derivative) products it intends to apply the security interest provisions to.	ASX will clarify in due course which products it intends to apply Part 11 to. Part 11 will not be operative at commencement if the Client Clearing Service.

Sub-issue	Comment	ASX Response
Priority and security arrangements	If ASX has a secured interest over initial margins, and if Clearing Participant defaults, ASX's interest may affect our priority of interests in relation to the initial margin. Clearing Participant grants this security as a beneficial owner of initial margin which must not be subject to any encumbrance. Initial margin would be covered by our security deed so this 'non encumbrance' rule will cause a problem for Clearing Participant and its security interest under the security deed.	Part 11 creates a framework within which a Clearing Participant may meet its Initial Margin obligations by giving ASX a security interest in non-cash collateral rather than by absolute transfer. Clearing Participants may elect which method to use to meet their Initial Margin obligations.
CGT	An absolute transfer would be deemed a disposal for CGT purposes and financial accounting. Such a transfer should be made disposal exempt for the purposes of the ASX Operating Rules.	Non-cash collateral can currently only be provided by a Clearing Participant to ASX by absolute transfer. Part 11 creates a framework within which a Clearing Participant may elect to provide a security interest over non-cash collateral rather than an absolute transfer. This may result in a different CGT outcome for a Clearing Participant.
Disclosure	If CCP needs to register security on PPS register this may potentially lead to disclosure of part of the trade position, making it public information. This is likely to concern some clients.	ASX is not required to register its security under the <i>Personal Property Securities Act 2009</i> (PPSA) in order to have priority under the PPSA given the provisions in the <i>Payment Systems and Netting Act 1998</i> (Cth) (s16(2)(fa) and 16(3)) and PPSA (s256).
Foreign security interests	Need to consider foreign security interests in collateral outside Australia including lodged in foreign CSDs or subject to tri-party collateral management arrangements.	A Clearing Participant must ensure that it is the beneficial owner of non-cash collateral (FR 124.2).

ASX 24 ETD and OTC IRD Client Clearing - Summary of responses to Consultation Paper 2 (Default Management)

Sub-issue	Comment	ASX Response
A1 Do you agree with ASX's approach to the composition of the default portfolio? If not, why not?		
Composition of default portfolio	Combining house and client positions to utilize hedging benefits and reduce auction costs is viewed as advantageous and to the benefit of clearing members. Provided there is proper record /accounting of house and client positions /proceeds, ASX's approach seems justified and appropriate.	ASX will maintain records to ensure full attribution and reconciliation between House and non-ported Client positions that are combined as part of one or more portfolios for sale or auction.
Composition of default portfolio	Client and House positions would ideally remain segregated. We would like to understand the pros and cons ASX considered when making the decision to combine house and non-ported client positions for the purpose of a default auction.	Hedging default portfolios of terminated Client and House positions separately may create unnecessary costs and losses, and represent an additional operational burden. Similarly holding multiple auctions may reduce the overall likelihood of a successful conclusion to the Default Management Process. Accordingly, ASX proposes to implement processes that minimise the costs of a default and reduce the possibility of erosion of the default waterfall.
Composition of default portfolio	It is unclear from OTC Rule 6.8 that the Client Positions will be terminated and cease to be Client Positions before being combined with House Positions to form default portfolios. ASX should ensure that regulatory guidelines for segregation are not impacted when the non-ported Client Positions are combined with the House Positions.	Non-ported Client positions will be terminated and cease to be Client positions before being combined with terminated House positions to form one or more default portfolios (OTC Rule 6.6).
Loss allocation process	If hedging, sale or auction is part of the Default Management Process and Loss is attributed after that process has been activated, how will ASX take into account the cost of the hedges, sale or auction in its Loss allocation at the point of combining the Terminated Client Contracts since the hedging/sale/auction occurs after this combination? If Client Positions are closed out at the point of combination of the Client Positions and House Positions, what Termination Value will the Client receive since the final losses, costs, charges and expenses in connection with the process are not yet known?	The losses incurred by ASX in closing out the OTC and portfolio-margined ETD transactions comprising the default portfolio will be determined at the end of the default process. ASX will then allocate those losses to the House and non-ported Client accounts of the defaulting OTC Participant by reference to the initial margin relating to each account at the time of combination (OTC Handbook Schedule 6). ASX has further amended OTC Rule 6.8 to clarify this process.
Sale of non-cash collateral	The Rules should cover the sale of non-cash collateral of defaulting members/clients. Rules should require ASX to manage expenses and obtain cash values of non-cash collateral on a commercially reasonable basis.	ASX has the power to sell non-cash collateral of defaulting Clearing Participants: FR 72.1(b). ASX will exercise this power in accordance with its obligations as a CS Facility Licensee to provide services in a fair and effective way and to reduce systemic risk. Given that ASX has \$120M of its own capital at the front of the default waterfall, ASX is incentivised to manage expenses and obtain a reasonable price from the sale of non-cash collateral of defaulting Clearing Participants.

Sub-issue	Comment	ASX Response
Composition of default portfolio	Under what circumstance (if any) will the non-ported client transactions not be included in the default portfolio?	Non-ported Client positions comprising OTC IRD and portfolio-margined ASX 24 ETD will always be included in a default portfolio – whether or not House and Client positions are combined – for the purpose of being auctioned or sold bilaterally in accordance with the OTC Default Management Process.
Composition of default portfolio	In the case of multiple defaults, the number of non-ported client transactions would potentially be large. Is it feasible to combine them with House transactions? Under what circumstances will the non-ported transactions be closed out (for Individual Accounts)?	ASX reserves the flexibility to combine terminated Client and House positions across multiple defaults in a default portfolio (OTC Rule 6.8 and Schedule 3). Whether ASX will do so will depend on the particular circumstances. All non-ported Client positions will be terminated – OTC IRD and portfolio margined ASX 24 ETD will be auctioned or sold bilaterally in accordance with the OTC Default Management Process and non-portfolio margined ASX 24 ETD will be closed-out on market.
B1 Do you agree with the proposed refinements to the default auction process in the Operating Rules? If not, why not?		
Default management refinements	Generally support refinements to the auction process. Strongly believe ASX should consult with DMG prior to making any determinations regarding Default Management Process, such as hedging portfolio, the auction units, composition of auction portfolio, auction weights and the auctioning or sale of a portfolio.	ASX intends to consult the DMG on these matters (OTC Rules, Schedule 3, 1.4)
Auction methods	Support there being alternate auction methods. Expect ASX/DMG to use most appropriate method given conditions of market and its participants at the time.	ASX's expectation is that the Highest Bidder Wins is the most likely format to be used, however, flexibility to use other formats is reserved to ensure that the best tools can be available to deal with unforeseen circumstances. ASX will consult with the DMG on the appropriate format of the auction (OTC Rules, Schedule 3, 1.4 and 4.1). As it is in ASX's interest to ensure a successful outcome to the auction, it is also in ASX's interest to ensure that all Clearing Participants have a solid understanding of the format and rules of the auction, the underlying positions comprising the auction portfolio and the timing of the auction. ASX will take all reasonable steps to ensure Clearing Participants are in a position to participate actively in the auction.
Auction methods	Recommend removing ASX's discretion to use auction formats other than Highest Bidder Wins and Multi-Unit Auction format on the basis that a solid understanding of the method of auction prior to a Default Management Process is critical for Clearing Participants to be able to participate in a timely and meaningful way.	
DMG and Risk Committee	The Rules do not indicate how DMG actions will interact with a Risk Management Committee for the clearing fund.	In the event of a Clearing Participant default, ASX will consult the DMG, not the Risk Committee, in accordance with the Default Management Process. However, both the Risk Committee and the DMG will be consulted on changes to the Default Management Process described in Schedule 3.

Sub-issue	Comment	ASX Response
Risk Ratings	Can ASX provide guidelines or frameworks on the factors used to determine Risk Ratings?	Higher risk weightings will be given to Auction Pools that are assessed by ASX, in consultation with the DMG, as being less attractive to the market and therefore require another incentive via the application of the juniorisation arrangements to stimulate bidding in the Auction.
DMG	ASX will establish a DMG with respect to each OTC Transaction Type specified in the DMG Composition Table, provided that there are at least 5 OTC Participants having open contracts relating to such OTC Transaction Type. What happens when there are less than 5 participants?	ASX intends to establish a DMG with respect to each OTC Transaction Type unless it does not have a substantial size. Accordingly, ASX has removed the requirement for there to be at least 5 OTC Participants (OTC Handbook, Schedule 3, 3.2). See revised Rules package.
DMG	ASX may decide against establishing a DMG with respect to an OTC Transaction Type which does not have a substantial size – what is the definition of “substantial”? In such a scenario, who makes the decision on the risk weight assigned to an Auction Unit?	ASX expects that the Risk Committee will provide guidance on what amounts to an OTC Transaction Type of a “substantial size” for the purpose of establishing a DMG. ASX will decide on risk weights for Auction Units.
DMG	We believe that once the default portfolio has been hedged then the DMG members should be cleared and released, which is more consistent with other CCPs.	Some DMG members may be permitted to return to their organisations after completion of the hedging phase of the default. However, a subset of the DMG may be required to provide advice on the auction bids and auction outcome (ASX DMG Dealing Code of Conduct).
DMG	What is the estimated time that the DMG will be required in order to fulfil their obligations, in particular in a default situation?	DMG members will be required at least until completion of the hedging phase of the default. ASX is cognisant of the needs of the DMG member’s employers during a time of a Clearing Participant default and as such, DMG members will be released as soon as practicable.
Uneconomic Price and reserve price	How does the Uneconomic Price (and its use to determine the order of application of juniorisation) interact with the concept of the reserve price?	The reserve price is the minimum price at which an auction pool would be sold to a bidding Clearing Participant (OTC Handbook, Schedule 4, 8.2). The Uneconomic Price is a price determined by ASX, in consultation with the DMG, at or beneath which a bid will be taken to be uneconomic for the purpose of determining how Mandatory OTC Participants should be juniorised (OTC Rules, Schedule 3, 4.6). The reserve price and the Uneconomic Price are unrelated except that the Uneconomic Price is always less than or equal to the reserve price.
Default Fund Contribution	If a Clearing Participant gets into a “Guaranteed Portability” agreement with one of its clients, will it incur additional default fund contribution?	ASX will not call for additional Commitments from an Alternate Clearing Participant before positions are ported to that Alternate Clearing Participant. Commitments are calculated quarterly based on initial margin requirements in the prior 3 month period.

Sub-issue	Comment	ASX Response
C1 Do you agree with ASX's proposed approach to allocation of losses, costs and expenses? If not, why not?		
Allocation of default losses	Support ASX approach of using initial margin as a risk measure for allocation losses across Clearing Participants.	Noted.
Allocation of default losses	Do not think ASX's proposed approach to allocation of losses, costs and expenses is appropriate as each client account must be treated separately and not comingled.	Non-ported Client positions will be terminated and cease to be Client positions before being combined with terminated House positions to form one or more default portfolios (OTC Rule 6.6). Under a hedge then auction process, the positions in a default portfolio must be risk neutralised by entering into offsetting positions, whether these positions are combined or auctioned/sold separately. Combining terminated House and Client positions enables ASX to take advantage of natural offsets thereby minimising the cost of hedging and the absolute size of the default portfolio to be disposed of. Minimising the extent of the default losses is important because the losses to be allocated impact on the amount of Guaranteed Initial Margin Value that can be returned to Clients. Losses will be allocated by reference to the initial margin relating to each portfolio at the time of combination.
Allocation of default losses	Do not totally agree with combining House and Client positions. With the combining of house/client and proportioning losses against the initial IM there appears to be the possibility of the house benefiting from a client's favourable positions compared to its own. Is this the case? Does this mean the Client is taking on the risk appetite of the Clearing Participant? What alternatives were considered by ASX?	
Allocation of default losses / Default waterfall	Schedule 6 (Allocation of Loss Worked Example) contains no mention of the defaulted members default fund contribution. How should this be allocated to this loss structure?	The example in Schedule 6 assumes that the defaulting Clearing Participant has sufficient initial margin associated with each account to cover the losses allocated to each account. It is only if the initial margin together with any available excess collateral is less than the losses allocated to the account that the defaulting Clearing Participant's default fund contribution would be applied.
	Examples should clearly state that risk and apportionment relate to required margin only rather than temporary excess margin.	Clarification added.
D1 Do you have any comments on the draft Operating Rule amendments that give effect to OTC Commitment juniorisation?		
OTC Juniorisation	Support the creation of tranches to define the Priority Groups in the juniorisation process.	Noted.
OTC Juniorisation	Support incentivising good bidding behaviour through the juniorisation approach.	Noted.
Multiple tranche juniorisation	Considers multiple tranche juniorisation based on level of auction bid, is a particularly aggressive way of ensuring good bid prices. ASX may wish to consider the LCH & HKEx model in which there are also 3 tranches (1st non bidders 2nd bidders non winners 3rd winners). In this case less aggressive bidders share losses on a pro rata basis alongside other non winning bidders, rather than having their DF fully wiped out, by virtue of not trading a particular market segment.	ASX has undertaken extensive consultation with OTC Foundation Customers, the RBA and ASIC on the juniorisation design, taking international comparisons into account. ASX has concluded that the proposed model of juniorisation is the most appropriate and robust. If a non-defaulting OTC Clearing Participant does not have any open

Sub-issue	Comment	ASX Response
OTC juniorisation	Request ASX reconsider its stand on calculating losing bids by the distance from the winning bids. Having worked with other CCPs globally we are of the belief that the possibility of collusion among traders and gaming of results is remote.	positions in an OTC Transaction Type and currency the subject of an auction, the Clearing Participant will not be required to bid, if it not a Mandatory OTC Participant in any Auction Pool, and will be ranked equal to the winning bidder for the purpose of juniorisation. The Clearing Participant's Commitment would not be 'wiped out' by virtue of not trading a particular market segment.
OTC juniorisation	For the purpose of juniorisation, what is the ranking of an OTC Clearing Participant that is not a Mandatory OTC Participant with respect to any auction pool?	A non-defaulting OTC Clearing Participant that has no open positions in an OTC Transaction Type included in an auction pool will, if it is not a Mandatory OTC Participant in any Auction Pool, be ranked equal with the winning bidder.
Uneconomic Price	Do not believe an Uneconomic Price is necessary as the bid furthest from the winning bid, which may be above the Uneconomic Price, will still be ranked last in the Priority Group but above the Non-Contributing Participants. As all Mandatory Participants know very low bids will threaten the mutualised guarantee fund, this should be sufficient incentive for Mandatory Participants to bid sensibly.	Feedback from OTC Foundation Customers supported ASX including the concept of an Uneconomic Price. ASX will consult with the DMG with respect to determining the Uneconomic Price for a particular auction (OTC Rules, Schedule 3, 1.4(v) and 4.6).
Auction	What is the minimum number of Clearing Participants required for an auction to proceed? In case of only 2 bidders, does the juniorisation process remain unchanged?	The minimum number of Clearing Participants required for an auction to proceed is 2 bidders. In the case of 2 bidders the juniorisation process remains unchanged.
Submissions received on Rules that were previously subject to consultation in Q2 2013 and are not the subject of the October 2013 change proposal		
DMG	If ASX does not follow the DMG's recommendations in respect of the composition of the default portfolio (or any aspect of the default process), it should give its reasons why not.	If ASX does not follow the recommendations or advice of the DMG, ASX will provide reasons (OTC Rules, Schedule 3, 1.7).
Compulsory Settlement	The Rules aren't entirely clear that auction and re-auction will occur until positions are completely transferred, and do not preclude the possibility of "last resort" compulsory settlement to non-defaulting members (which Barclays would not support).	ASX does not have compulsory settlement powers in relation to OTC contracts (FR 72.1(k) and OTC Rules, Schedule 3, 3). Compulsory settlement powers for ASX 24 ETD contracts are capped at twice the non-defaulting Clearing Participant's Commitment (FR 102). ASX intends to consult on "last resort" options as part of its consultation on CCP recovery and resolution in 2014. This consultation will also consider whether compulsory settlement of ASX 24 ETDs should remain in place.

Sub-issue	Comment	ASX Response
Resignation	<p>Under the Rules, Clearing Members are obliged to bid in an auction if at the time of the default of the defaulting Clearing Member they had a relevant Open Contract.</p> <p>Does this mean practically that if there was a Default and a Clearing Member at that time had an relevant Open Contract and the next day the Clearing Member closed out all its Open Contracts and resigned it would nonetheless still be obliged to bid in the auction (thereby meaning it could not fulfil the resignation criteria set out in 11.1(b)(2)(C)). In times of multiple defaults this would effectively seem to operate to endlessly delay the effectiveness of the resignation</p>	<p>If Clearing Participant 1 has an OTC Open Position at the time of the default of Clearing Participant 2 then it will have an obligation to bid in the resulting auction even if it closes out all its Open Positions the next day. However, if Clearing Participant 3 defaults after Clearing Participant 1 has closed out all its Open Positions then Clearing Participant 1 has no obligation to bid in the auction of Clearing Participant 3's portfolio. Accordingly, multiple defaults do not endlessly delay the effectiveness of resignation.</p>
Mandatory OTC Participants	<p>Are there sufficient safeguard available for members not active in specific segments of the market? eg a predominately short-end member, bidding on a long end portfolio, a member without futures clearing , bidding for a portfolio that includes futures.</p>	<p>OTC Clearing Participants that are required by the default auction rules to bid in an auction pool – that is, where the Clearing Participant has at least one open contract in the relevant OTC Transaction Type and currency at the time of the default – have a legal obligation to bid. It is incumbent on Clearing Participants to ensure they have the capacity to bid where they are required to do so and to accept any portfolio they may win at auction. A failure to comply with this obligation is a breach of the rules (FR 4.11(f)) and itself an event of default (FR 71.3).</p> <p>ASX proposes to undertake pre-auction risk checks. Given that the default portfolio will be hedged at that stage, risks are more likely to relate to operational concerns than margin/exposure concerns. ASX retains a power to waive the requirement to bid (OTC Rules, Schedule 3, 4.5). That power may be exercised in exceptional circumstances (for example, where ASX is directed by regulators to excuse a financially distressed Clearing Participant from bidding).</p>
Mandatory OTC Participants	<p>Support fundamental basis of 'Best Bidder' to receive portfolios (or proportion of portfolios) and 'worst' bidders via bottom up, to lose commitment. However, ASX should take into account the ability of bidders to participate in auction due to impact of bidders positions and market conditions which may create financial stress for a bidder.</p>	
Mandatory OTC Participants	<p>Concerned about the concept of seniorising people in response to their inability to help mop up the mess caused by a default. Concerned entities may be accepted as participants without have the capacity to perform the role. The principle should be that all participants, without exception, must bid competitively if they want to avoid juniorisation.</p>	
	<p>If a participant has traded a contract in the last few months, surely it has demonstrated that it has the wherewithal to handle the contract type. Why should it then not be a Mandatory OTC Participant?</p>	<p>The principle that a Clearing Participant should not be required to bid in an OTC Auction if it does not have an open position in the auctioned contract type/currency is intended to give resigning Clearing Participants greater certainty regarding the timing of the return of their Commitment and their liabilities, while balancing the interests of continuing Clearing Participants.</p>
Mandatory OTC Participants	<p>Why can ASX waive the requirement that a Mandatory OTC Participant participates in an auction? What other CCPs offshore are entitled to intervene to alter loss allocation in this way?</p>	<p>ASX intends to retain the power to waive the requirement to bid. That power may be exercised in exceptional circumstances (for example, where ASX is directed by regulators to excuse a financially distressed Clearing Participant from bidding).</p>

Sub-issue	Comment	ASX Response
Reserve Price	Do not believe there should be a Reserve Price imposed in an auction as it may result in the auction failure even though all Mandatory Participants submit bids. The auction should set the price.	The setting of a reserve price requires the Clearing Participant to make an ex ante judgement about the lowest price it would be prepared to accept and therefore sets a boundary condition on the losses acceptable by virtue of the Auction process. In ASX's view this enhances the integrity of the auction process. ASX needs to retain the flexibility to set reserve prices. If a reserve price is not reached, ASX may seek to dispose of the default portfolio bilaterally or re-auction (in different auction pools) at a later date.
DMG	In times of stress (when a Clearing Participant defaults) the remaining Clearing Participants will require their experienced swaps traders to be active in managing their own risk. If the trader is a member of the DMG, due to the restrictions placed on their activity, it will conflict with their ability to act in the best interest of their own institutions and managing their risk in volatile times.	It is a condition of admission as an OTC Clearing Participant that an entity can demonstrate its ability to participate in ASX's Default Management Process, which includes adequately resourcing the DMG (OTC Rules 2.3(c)). The OTC Clearing Participant also has an obligation to procure the attendance of its DMG Member at the DMG meeting (OTC Handbook, Schedule 3, 5.3). In the event of a Clearing Participant default, ASX will rely on the skills and expertise of DMG members to assist ASX in reducing the risk posed by the default, such reduction being consistent with the interests of non-defaulting Clearing Participants. ASX will release DMG members from the DMG as soon as practicable following completion of the hedging phase of the Default Management Process.
DMG	Who exactly does ASX require to sit on the DMG? Through the ASX documents it mentions various terms for the criteria of the DMG candidates, i.e. trading, risk, or front office. What is the definition of these, and exactly what is the criteria?	The DMG members must be qualified with respect to the relevant OTC Transaction Type and must have expertise and experience in relation to the relevant DMG Matters (OTC Handbook, Schedule 3, 5.3(b)). DMG Matters include advice on and execution of hedging transactions (OTC Rules, Schedule 3, 1.4). ASX expects that DMG members are likely to be experienced traders.
Direct Sale vs Auction	Can ASX provide guidelines or frameworks on deciding between Direct Sale vs Auction?	ASX will only enter into a direct sale against the recommendation of the DMG prior to an auction if entering into the sale does not result in the application of the Commitments of non-defaulting OTC Participants and the terms and conditions of the sale are fixed (OTC Rules, Schedule 3, 3). Whether ASX would enter a direct sale would depend on factors such as how quickly such a sale could be effected, the terms and conditions applicable and the prevailing market conditions. ASX would take into account the advice of the DMG on deciding between Direct Sale vs Auction.

Schedule 3: Client Protection Model FAQ

What is the Client Protection Model?

'Client Protection Model' is the name ASX applies to the agency-style clearing model that it is introducing to support the Client Clearing Service. It refers to the legal relationships established by proposed Part 10 of the Futures Rules between a Client (whether utilising an Omnibus Account or Individual Client Account), its Clearing Participant and ASX, and the related arrangements for segregation and portability of client positions and associated initial margin.

When will the Client Protection Model take effect?

Subject to regulatory clearance, the Client Protection Model will take effect at the time of commercial launch of the Client Clearing Service for OTC Interest Rate Derivatives (expected end Q1 2014) and ASX 24 Exchange Traded Derivatives (expected end Q2 2014). ASX will confirm the commencement dates closer to commercial launch.

Who is a CPM Client?

A CPM Client is a Client with an Open Position in a financial product to which the Client Protection Model applies.

How does the Client Protection Model work?

Under the Client Protection Model, the Clearing Participant clears transactions as agent of its Client, binding the CPM Client to cleared contracts through the authority which the CPM Client has given the Clearing Participant to act on its behalf pursuant to the client agreement. In this respect, the Client Protection Model creates contractual relationships that are similar (though not identical) to those that arise under the so-called 'agency model' of central clearing, as applied to US Derivatives Clearing Organisations by CFTC regulations. The Client Protection Model under Australian law establishes a clear set of contractual relationships that, through Commonwealth legislation applicable to 'netting markets' such as ASX, give legal protection to arrangements for segregation and portability of client positions and associated initial margin under ASX's Operating Rules.

Under the Operating Rules which give effect to the Client Protection Model:

- The Clearing Participant remains fully liable for all obligations to ASX in connection with cleared contracts (referred to in the Operating Rules as 'Open Contracts');
- Each of the Clearing Participant, the CPM Client and ASX is a party to Open Contracts;
- ASX agrees not to take action against the CPM Client personally for the performance of any obligation owing by the Clearing Participant under Open Contracts;
- ASX recognises the interest of the CPM Client or CPM Clients (depending on whether an Individual Client Account or Omnibus Account is used) in the value of initial margin calculated by ASX with respect to the client account;
- If the Clearing Participant has defaulted:
 - a CPM Client that has elected to use an Individual Client Account has a right to require ASX to port its positions and associated initial margin to an alternate Clearing Participant, where the CPM Client has satisfied the porting conditions within the applicable porting window;
 - a CPM Client that has elected to use an Omnibus Account has a right to request, jointly with all other CPM Clients holding positions in the account, ASX to port the positions in the account and associated initial margin to an alternate Clearing Participant. Porting of positions in an Omnibus Account is at ASX's discretion;
 - a CPM Client has a right to communicate with ASX in connection with the porting process.

How does the Client Protection Model affect Clearing Participants relative to ASX's existing clearing model?

The key difference between the Client Protection Model and ASX's existing clearing model (commonly known as a 'principal model') is that under the Client Protection Model, the Clearing Participant clears transactions as agent of its Client, binding the CPM Client to cleared contracts through the authority which the CPM Client has given the Clearing Participant to act on its behalf under its client agreement. Under its existing clearing model ASX does not recognise any contractual relationship with the Client and treats the Clearing Participant as the principal with whom it is contracting.

In most other respects, the Client Protection Model and ASX's existing clearing model are identical in their practical effect on Clearing Participants. For instance, under both clearing models:

- The Clearing Participant is liable to ASX on its Open Contracts as principal obligor;
- In the ordinary course of business (i.e. unless the Clearing Participant is in default), ASX will communicate and deal with the Clearing Participant only, not its CPM Clients, in relation to Open Contracts;
- The Clearing Participant is responsible for agreeing the terms of its relationship ('client agreement') with its CPM Client. The client agreement, rather than the Operating Rules, governs the rights and obligations between the Clearing Participant and its CPM Client (refer Figure 1, below);
- The Clearing Participant is responsible for managing the risks arising from the default of its CPM Client, in accordance with the client agreement and applicable law. The Operating Rules are non-prescriptive about how the Clearing Participant manages those risks.

The main significance of ASX's implementation of the Client Protection Model is for the Clients of Clearing Participants: the Client Protection Model gives CPM Clients upon their Clearing Participant's default direct legal rights against ASX to segregation and portability of client positions and value of the associated initial margin, subject to and in accordance with ASX's Operating Rules. Clients do not have such rights under ASX's existing clearing model.

A diagrammatical depiction of the Client Protection Model is in Figure 1 below.

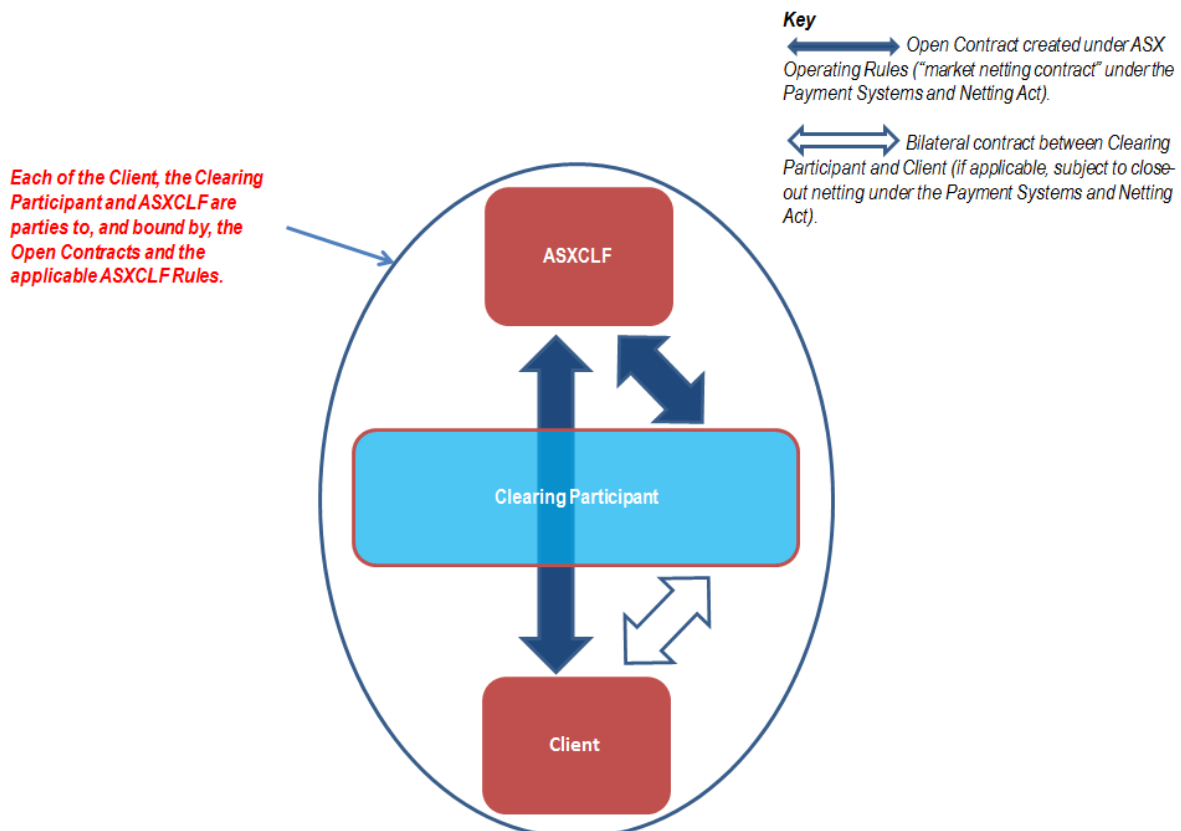


Figure 1: Client Protection Model – legal relationships overview

Does the Client Protection Model affect the Clearing Participant's close out netting rights with respect to its Clients?

ASX has commissioned an external Australian law legal opinion, which will be made available to Clearing Participants, to confirm that the Client Protection Model will not affect the application of the Payment Systems and Netting Act 1998 (Cth) to close-out netting of obligations owed between a Clearing Participant and its CPM Client under a close-out netting contract between them. Whether a bilateral contract between a Clearing Participant and its CPM Client is a 'close-out netting contract' is a matter on which Clearing Participants should seek their own legal advice.

Can actions taken by ASX to port CPM Client property be reversed or unwound?

ASX has commissioned an external Australian law legal opinion, which will be made available to Clearing Participants and CPM Clients on request, to confirm the validity and enforceability of porting of CPM Client property in accordance with ASX's Operating Rules on Clearing Participant default.

Schedule 4: Nominated Person for Individual Client Account

To better accommodate multi-level client structures, ASX has modified its original proposal so that an end user client that seeks the benefits of individual segregation may either: (i) contract directly with a Clearing Participant (and become the 'CPM Client') or (ii) be nominated by an entity (e.g. broker) that is itself a 'CPM Client' of a Clearing Participant (the 'Nominated Person option'). The Nominated Person option will not be available for Omnibus Accounts.

What is the Nominated Person option?

Under the Nominated Person option, a CPM Client may provide to ASX the contact and bank account details of its end user client (**Nominated Person**) in respect of an Individual Client Account opened by the CPM Client for the Nominated Person. Where a Nominated Person has been designated in respect of an Individual Client Account, and the CPM Client's Clearing Participant defaults, then:

- (a) ASX will, if necessary, contact the Nominated Person instead of the CPM Client for instructions relating to porting the positions in that Individual Client Account to an alternate Clearing Participant; and
- (b) if the positions in the Individual Client Account and the associated initial margin value cannot be ported, the CPM Client agrees that ASX will remit the residual initial margin directly to the Nominated Person's bank account.

The Nominated Person does not have any other rights or entitlements under the Client Protection Model or Operating Rules. In particular, the Nominated Person does not have any further protections in the event of the default of the CPM Client or any other intermediating entity. The Nominated Person is only protected from the default of the Clearing Participant to the extent outlined above.

How is a Nominated Person designated in respect of an Individual Client Account?

The CPM Client designates a Nominated Person in respect of its Individual Client Account by providing to ASX the contact, bank account and any other prescribed details of the Nominated Person. The CPM Client may also amend these details by notifying ASX. If the CPM Client makes such an amendment, ASX intends to notify the Nominated Person of the amendment by using the contact details recorded prior to the amendment.

The designation of the Nominated Person and any changes to the details of such Nominated Person are only effective if made prior to the default of the CPM Client's Clearing Participant.

The Nominated Person cannot provide their details to ASX directly.

What do the relationships look like if the Nominated Person option is used?

The Nominated Person option does not affect the structure of the relationships and contracts described in Figure 1 in Schedule 3. The CPM Client, Clearing Participant and ASX are still the only parties to the Open Contract and bound by the Operating Rules. The Nominated Person does not become a party to the Open Contract.

The Nominated Person is only entitled to communicate with ASX upon the default of the CPM Client's Clearing Participant in relation to the porting process for the Individual Client Account in respect of which it is the Nominated Person.

How does the position of the Nominated Person differ from that of a CPM Client?

Unlike the CPM Client, the Nominated Person will not have a direct relationship with ASX because it is not a party to the CPM Client's Open Contract. However, the Nominated Person will have some of the key benefits of a CPM Client, namely, on default of the CPM Client's Clearing Participant it may provide instructions to ASX in relation to porting and will receive the residual initial margin value where the positions in the Individual Client Account in respect of which it has been nominated are not ported.

The Nominated Person option is contrasted with the 'base case' (where the end user client deals directly with the Clearing Participant) in Figure 2 below.

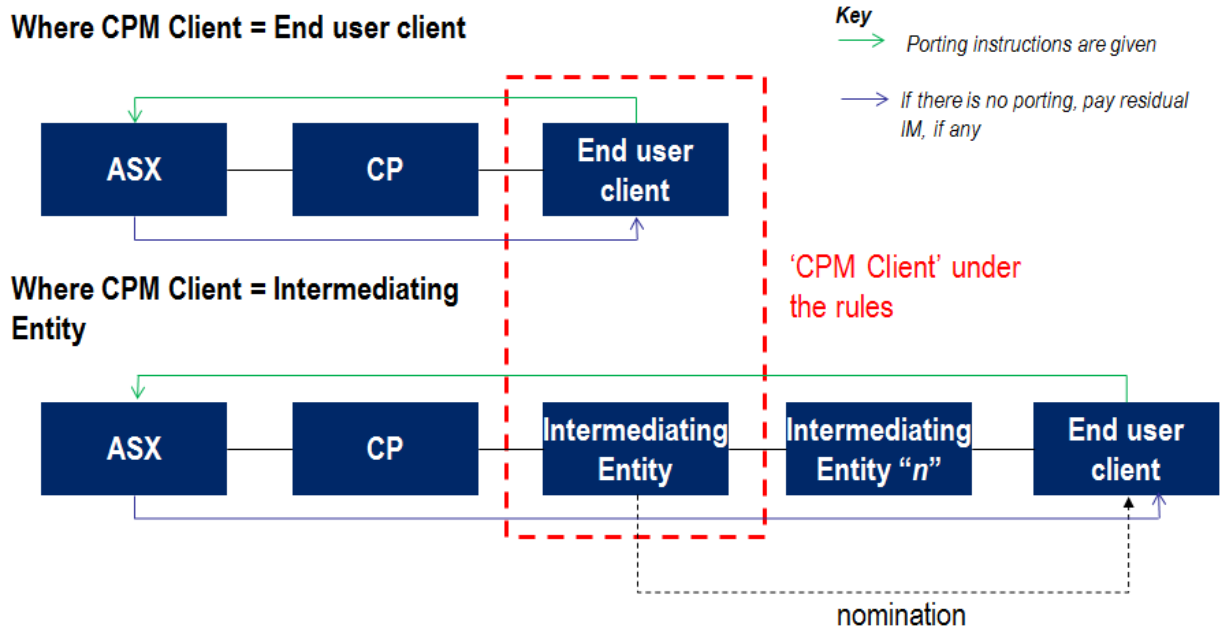


Figure 2: Nominated Person option for Individual Client Account