

ASX OTC Interest Rate Derivatives Clearing

Consultation on OTC Rule and Handbook amendments
related to the Client Clearing API and Multilateral
Compression Service

CONSULTATION PAPER

MARCH 2017



Invitation to comment

ASX is seeking submissions on the matters canvassed in this paper by 5 May 2017.

Submissions should be sent to:

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Office of General Counsel ASX Limited
20 Bridge Street Sydney NSW 2000

Attention: Tegan Jones

ASX prefers to receive submissions in electronic form. Submissions not marked as 'confidential' will be made publicly available on ASX's website

If you would like your submission, or any part of it, to be treated as 'confidential', please indicate this clearly in your submission. ASX is available to meet with interested parties for bilateral discussions on the matters under consultation.

Contacts

For general enquiries, please contact:

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Introduction

Overview

ASX Clear (Futures) Pty Limited (“**ASX**”) proposes to introduce a best practice OTC client clearing workflow for trade submission (“**Client Clearing API**”) and a multilateral compression service (“**Multilateral Compression Service**”) in the second quarter of 2017.

ASX’s proposed amendments to the OTC Rules and Handbook to support these new services are outlined in this Consultation Paper and available [here](#).

OTC Participant responses to this Consultation Paper should be submitted to ASX by 5 May 2017.

Client Clearing API

ASX proposes to introduce a Client Clearing API for OTC clients that will enable pre-clearing credit limit checks by means of a credit token issuer (either the client’s OTC Participant or a third party credit hub notified to ASX by the OTC Participant) and request for consent workflows initiated by ASX. The service will be launched in May 2017 (indicative). The Client Clearing API will:

- support clearing certainty for OTC counterparties;
- facilitate compliance by participants with foreign regulations that require cleared OTC Transactions concluded on a trading venue to be checked against client credit limits prior to execution: *17 CFR 1.73 (Dodd-Frank Act)*; *Draft RTS 26 under Regulation (EU) No 600/2014 Article 29(3)*; and
- deliver international best practice in OTC client workflows.

Using the Client Clearing API, OTC Participants may consent to the registration of client OTC Transactions with ASX using two new methods:

- **Credit token** – This will apply where an OTC Participant manages the utilisation of a client’s credit limit through a credit token issuer prior to trade submission. The credit token issuer may be the OTC Participant itself or a third party credit hub notified to ASX by the OTC Participant. The credit token issuer will be ‘pinged’ by an electronic trading venue at the point of trade to determine if the client has sufficient limit with their OTC Participant for the OTC Transaction to be executed. If sufficient limit is available, the OTC Transaction will be executed on the electronic trading venue and a credit token will be included in the transaction details of the OTC Transaction submitted to ASX through an Approved Trade Source System. Under the proposed amendments to the OTC Rules and Handbook, ASX will treat the inclusion of a credit token in the transaction details of a client OTC Transaction as the OTC Participant’s consent to registration of that OTC Transaction with ASX; and
- **Request for Consent** – Where an Approved Trade Source System submits a client OTC Transaction to ASX without a valid credit token, ASX will send a ‘request for consent’ message to the client’s OTC Participant or a third party credit hub notified to ASX by the OTC Participant. The recipient of the ‘request for consent’ message must provide consent to ASX (via an FpML message) within 10 seconds of receipt or the OTC Transaction will be rejected by ASX.

A diagram of the two consent processes described above is set out in **Attachment A**.



These new consent processes will not apply to OTC Transactions of OTC Affiliates that are cleared into the OTC Participant's House Account. Under ASX's proposed amendments to the OTC Rules and Handbook, an OTC Participant will continue to be taken to have consented to the submission of an OTC Transaction to ASX by an OTC Affiliate where the OTC Transaction is reported to ASX by an Approved Trade Source System.

In all cases, an OTC Transaction will only be registered by ASX after the OTC Participant consents (or is taken to have consented) and the OTC Transaction passes existing ASX trade and risk eligibility criteria.

Key Operating Rules:

OTC Rules – Rule 4.3 (Registration of OTC Transactions)

OTC Handbook Paragraphs 1.4, 2.15, 4.3

Consultation Questions:

- (1) Is the Client Clearing API aligned with OTC Participant regulatory obligations? For example, under the 'request for consent' process, is 10 seconds an appropriate timeframe within which ASX should require an OTC Participant or Approved Credit Hub to provide consent before rejecting the OTC Transaction?
- (2) Under the proposed rule amendments, the 'credit token' and 'request for consent' processes will not apply to OTC Transactions of OTC Affiliates that are cleared into the OTC Participant's House Account. Should the consent processes apply to OTC Affiliate transactions for regulatory or other reasons?

Multilateral Compression Service

ASX proposes to introduce a Multilateral Compression Service commencing in June 2017 (indicative). Multilateral compression is the process by which ASX terminates OTC Open Contracts which have been nominated for trade compression and simultaneously registers new OTC Open Contracts which have a combined notional value less than the terminated OTC Open Contracts. The new OTC Open Contracts represent the multilateral net exposure under the terminated OTC Open Contracts. Multilateral compression reduces exposures in an OTC Participant's portfolio, allowing for improved capital efficiency and a reduction in operational and systemic risk.

ASX's processes for multilateral compression will align with similar services operated by other OTC swap central counterparties. OTC Open Contracts registered in House Accounts (including contracts of OTC Affiliates) and Individual Client sub-accounts may be nominated for inclusion in a multilateral compression 'cycle'. Multilateral compression cycles will be available on the dates and times specified by ASX. Each multilateral compression cycle will be coordinated by a compression service provider approved by ASX (an "**Approved Compression Service Provider**").

An OTC Participant who wishes to participate in a multilateral compression cycle will need to be a party to, and adhere to, compression documentation with ASX and an Approved Compression Service Provider. Following the nomination of OTC Open Contracts for multilateral compression, the Approved Compression Service Provider will generate a proposed set of terminating OTC Open Contracts and resulting OTC Open Contracts (an "**Unwind Proposal**") which will be made available to each participating OTC Participant. ASX and all relevant parties as specified in the compression documentation must accept an Unwind Proposal for a compression cycle to proceed.

Prior to effecting an Unwind Proposal, ASX may make a call for additional margin to OTC Participants based on the outcomes of the Unwind Proposal. Following unanimous acceptance of the Unwind Proposal, ASX



will effect a multilateral compression and will notify OTC Participants once this has been completed. OTC Participants will be responsible for notifying their clients and OTC Affiliates once the cycle has been effected.

A diagram of the process described above is set out in **Attachment B**.

Key Operating Rules:

OTC Rules – Rule 4.14 (OTC Portfolio Compression)

OTC Handbook Paragraphs 1.4A and 4.14

Next steps

ASX seeks OTC Participants' views on the draft amendments to the OTC Rules and Handbook. Submissions should be made by 5 May 2017.

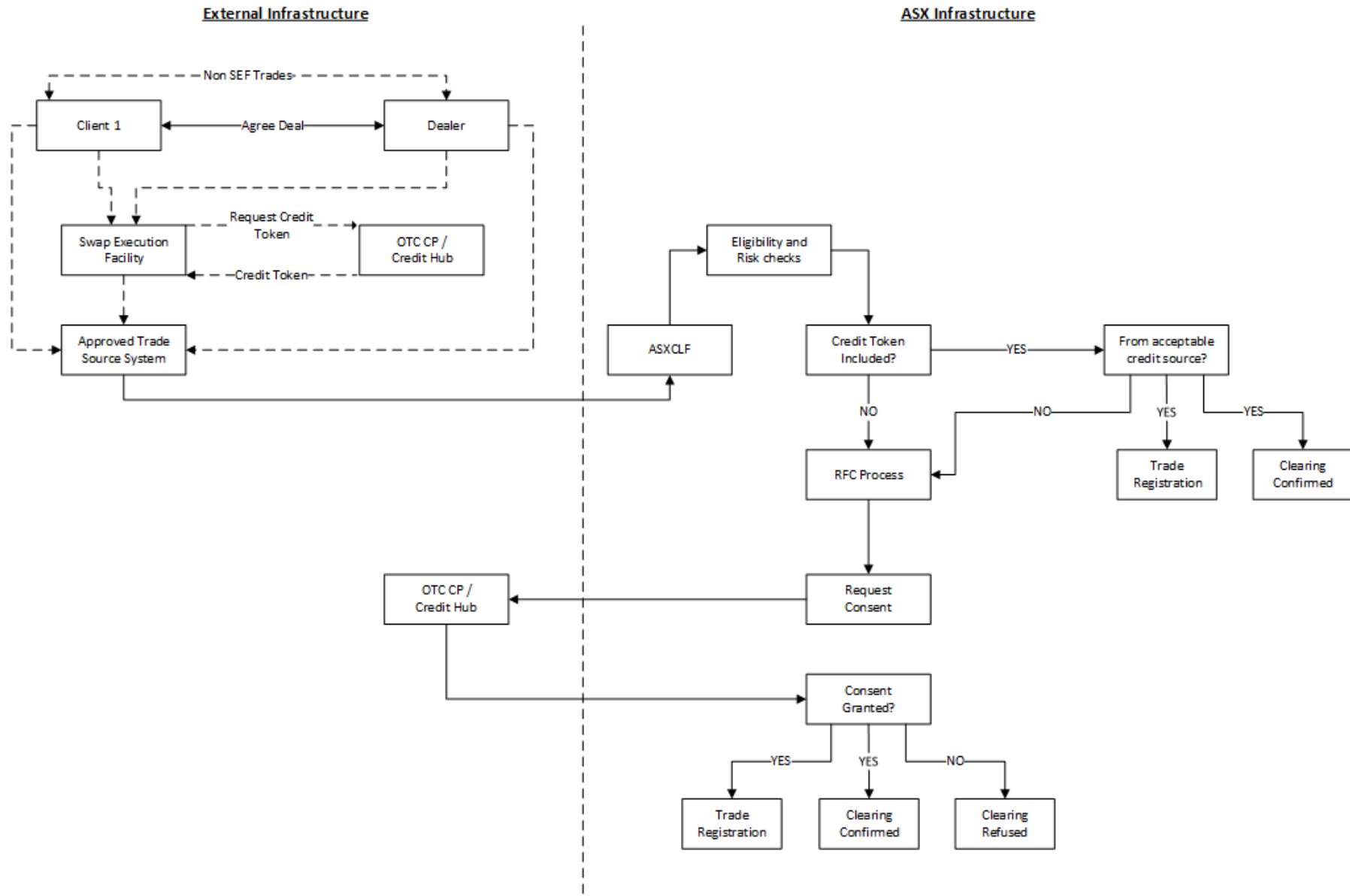
ASX welcomes the opportunity to discuss the draft amendments with interested parties (please refer to the contact details on page 2).

Subject to OTC Participant feedback and regulatory clearance, ASX intends to implement the proposals with effect as follows:

- Client Clearing API – 29 May 2017
- Multilateral Compression Service – 30 June 2017.

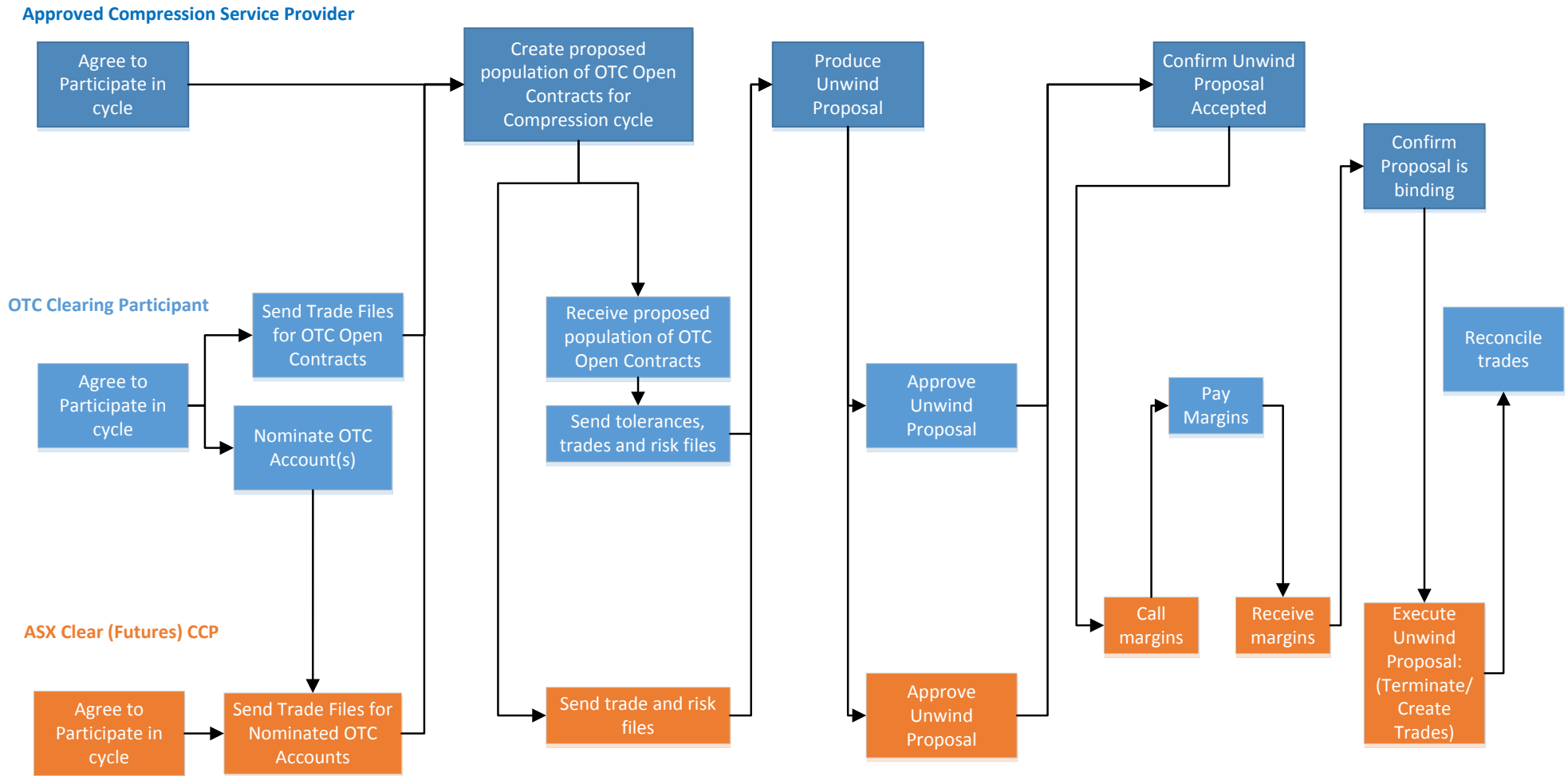


Attachment A – Client Clearing API Trade and Message Workflow



Attachment B – Multilateral Compression

Indicative High-Level Process Overview – Multilateral Compression for House Accounts



Indicative High-Level Process Overview – Multilateral Compression for OTC Affiliates and Clients

Approved Compression Service Provider

OTC Affiliate or Client

ASX Clear (Futures) CCP

ASX OTC Clearing Participant

