

AUSTRALIAN DERIVATIVES REFORM - NEW CLEARING REQUIREMENT

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Legal Briefings - By **Steven Rice** and **Thomas McClintock**

New rules have been introduced in Australia about the clearing of OTC derivatives.

- The rules commence on 4 April 2016 and apply to OTC derivatives where larger banks in Australia are a counterparty
- If the rules apply, then OTC derivatives need to be cleared through a licenced or prescribed clearing facility
- The rules contain a regime for substituted compliance where OTC derivatives have been cleared under foreign clearing rules
- Failure to comply with the rules may result in a civil penalty

On 14 December 2015, the Australian Securities and Investments Commission made the *ASIC Derivative Transaction Rules (Clearing) 2015 (Clearing Rules)*. The Clearing Rules implement Australia's mandatory central clearing regime for OTC derivatives, and contain a regime for substituted compliance where clearing has been done under clearing requirements in a foreign jurisdiction. The clearing requirement in Australia will commence on 4 April 2016. Failure to have a relevant transaction centrally cleared could result in a civil penalty of AUD180,000.

The new rules will apply to transactions in OTC interest rate derivatives denominated in Australian dollars, US dollars, euros, British pounds and Japanese yen. The clearing requirement is imposed where a counterparty to an OTC derivative is an 'Authorised Deposit-taking Institution' (eg. a bank) in Australia, or the holder of an Australian financial services licence, which has notional exposure to OTC derivatives of AUD100 billion or more. This means that the clearing requirement will, in practice, apply to OTC derivatives entered into with the larger banks operating in Australia. Entities may also opt in to be clearing entities.

Unless an exception applies, all transactions which are subject to the clearing requirement must be cleared through a 'clearing facility'. This is achieved by each side of the clearing transaction being replaced by novation by a contract between the operator of a clearing facility and a participant in that facility. The clearing must occur as soon as reasonably practicable after the transaction is entered into. A 'clearing facility' is one which is licenced as such or specifically prescribed.

The Clearing Rules require entities subject to a clearing requirement to maintain records (for five years) showing that they have complied with the Clearing Rules. If ASIC makes a written request, an entity with a clearing obligation must provide such records to establish their ongoing compliance with the Clearing Rules.

The Clearing Rules will be relevant to all counterparties to derivatives with the larger banks operating in Australia. A counterparty with such an institution can require confirmation of the institution's clearing entity status in order to determine their obligations under the Clearing Rules.

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