25 November 2016

BY E-MAIL and HAND

Chief General Manager,
Reserve Bank of India,
Financial Markets Regulation Department,
Mumbai 400 001

E-mail: fmrdfx@rbi.org.in

Dear Sirs

Consultation on the Draft Guidelines for Centralised Hedging for Indian Subsidiaries of Non-Resident Companies

Introduction

The International Swaps and Derivatives Association, Inc. (**ISDA**)[1] is grateful for the opportunity to respond to the Consultation on the Draft Guidelines for Centralised Hedging for Indian Subsidiaries of Non-Resident Companies (**Consultation**) published on 4 November, 2016.

We welcome the initiative taken by the Reserve Bank of India (**RBI**) to provide greater flexibility for hedging the currency risk arising out of current account transactions of Indian subsidiaries of multinational companies (**subsidiary**) by the parent or any non-resident group entity (**non-resident entity**).

We had submitted an email dated 10 November 2016 requesting an extension of the submission date, and are grateful for the extension that was granted in your email on 15 November 2016. We may also have further feedback to provide to RBI on this Consultation. ISDA hopes to continue the constructive ongoing dialogue between the RBI and derivatives market participants to consider, for example, the practical concerns and risks surrounding the implementation of the draft guidelines set out in the Consultation. Our members may have feedback which they may wish to provide separately to RBI.

[1] Since 1985, ISDA has worked to make the global over-the-counter (OTC) derivatives markets safer and more efficient. Today, Today, ISDA has over 850 member institutions from 67 countries. These members comprise of a broad range of derivatives market participants, including corporations, investment managers, government and supranational entities, insurance companies, energy and commodities firms, and international and regional banks. In addition to market participants, members also include key components of the derivatives market infrastructure, such as exchanges, intermediaries, clearing houses and repositories, as well as law firms, accounting firms and other service providers. Information about ISDA and its activities is available on the Association's web site: www.isda.org.

General comments

Whilst our members agree that the draft guidelines are a welcome step in providing greater flexibility for hedging the currency risk arising out of current account transactions of Indian subsidiaries of multinational companies by the parent or any non-resident group entity, we would like to highlight certain areas which require further clarification.

Requirement for a multilateral agreement – clause 4(v)

As you know, derivatives are typically traded under the market standard ISDA Master Agreement (either the 1992 or 2002 versions). The ISDA Master Agreement contributes to the key objective of risk management and risk reduction by offering market participants a standardized agreement to document derivative transactions. In short, the ISDA Master Agreement is the building block for the documenting these transactions. Opinions such as the industry netting opinions are also available with respect to the ISDA Master Agreement and are relied on by ISDA members.

We note that clause 4(v) provides that if this activity needs to be conducted under a multilateral agreement, a new bespoke agreement specific to this type of hedging activity will need to be introduced. We seek clarification as to what this requirement entails, and what the purpose of this requirement would be. We note that as market participants are already using the ISDA Master Agreement to document derivatives transactions, there would be no further need for a multilateral agreement. Apart from helping market participants manage their risk, the ISDA Master Agreement also offers the advantage of reducing the time and expense in preparing and reviewing documentation prepared by another party.

An onshore subsidiary would be in a position to ensure that it complies with the rules of this particular regulation as well as any rules, regulations and directions issued under FEMA 1999, which is covered under clause 4(iv) of the draft guidelines. As the parent company of the onshore subsidiary, the offshore parent should also be in a position to procure that its onshore subsidiary ensures that such rules, regulations and directions are complied with and, as a counterparty to the AD Cat-I bank on the hedging transaction, confirm to the AD Cat-I bank of such compliance.

Therefore if the purpose of the multilateral agreement is for the AD Cat-I bank to get comfort on the Indian subsidiary's compliance with the relevant rules, regulations and directions, it would not be necessary for a multilateral or multiple party agreement as the individual counterparties would have already entered into an ISDA Master Agreement to document their derivative transactions.

We would be happy to discuss this further with you.

Requirement for accounting of P&L of the hedge – clause 4(vi)

With respect to the accounting treatment of the hedge, we respectfully submit that this requirement is solely within the purview of the subsidiary and non-resident entity to manage. A third party, such as the onshore bank in India, will not be in a position to influence or manage this requirement on behalf of the subsidiary or non-resident entity. We therefore would request that this requirement be removed. Alternatively, this requirement may be amended to clarify that the obligation to ensure this accounting treatment rests on the non-resident parent entity and/or its Indian subsidiary, and that the obligation of the AD Cat-I bank is to obtain confirmation from its non-resident counterparty for the trade that this requirement is complied with.

Monitoring of hedge transactions – clause 4(viii)

We refer to the requirement under clause 4(viii) for the AD Cat-I bank to monitor hedge transactions and ensure that the Indian subsidiary has the necessary underlying exposure for the hedge transactions. We respectfully submit that since a non-resident entity is allowed to deal with multiple AD Cat-I banks in respect of its hedging activities, it would not be possible for any single AD Cat-I bank to have total clarity on the total hedging positions of its counterparty.

We note the RBI's desire to ensure there is appropriate underlying exposure for hedging transactions also applies to purely onshore FX transactions between AD Cat-I banks and Indian resident entities. In that context, the issue is addressed by requiring AD Cat-I banks to take declarations from its counterparty on the counterparty's hedging status. This approach recognizes that the ability to ensure and confirm existence of necessary underlying exposure ultimately rests with the counterparty. We therefore ask that RBI considers following this same approach in respect of the proposed centralized hedging activity.

Reporting hedge contracts to CCIL – clause 4(x)

With respect to the requirement for transactions booked under this facility to be reported to CCIL's trade repository with a special identification tag, we respectfully submit that this requirement is inconsistent with current trade reporting requirements. Onshore OTC derivative trades are already reported to CCIL's trade repository, and the reporting of offshore trades will not be useful and may lead to possible duplication and confusion. It is also important to note that as the draft guidelines allows both OTC as well as exchange-traded trades for hedging purposes, reporting exchange-traded transactions to CCIL's trade repository seems counterintuitive as the trade would have already been recorded by an exchange.

We welcome further dialogue with the RBI on the points raised above, and would be grateful for the opportunity to engage with the RBI on any specific clarification that may be required when the final guidelines are drafted.

ISDA thanks the RBI for the opportunity to respond to the Consultation and welcomes dialogue with the RBI on any of the points raised. Please do not hesitate to contact Keith Noyes, Regional Director, Asia Pacific at (knoyes@isda.org at +852 2200 5909), Erryan Abdul Samad, Assistant General Counsel at (eabdulsamad@isda.org at +65 6653 4172) or Rahul Advani, Assistant Director, Public Policy at (radvani@isda.org at +65 6653 4171).

Yours sincerely,

For the International Swaps and Derivatives Association, Inc.

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