

March 21, 2014

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Chief Risk Officer
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BY E-MAIL

Dear Sirs,

Consultation Paper: Segregation and Portability related Changes & Clearing Member Structure

1. Introduction:

The International Swaps and Derivatives Association, Inc. (“ISDA”)¹ welcomes the opportunity to respond to the Consultation Paper on *Segregation and Portability Related Changes & Clearing Member Structure* (“**Consultation Paper**”) issued by The Clearing Corporation of India Ltd. (“CCIL”) on February 28, 2014.

2. Consultation Paper:

We commend CCIL for taking steps to propose a Clearing Member (“CM”) structure and the portability and segregation of indirect participants. We support CCIL’s efforts to meet Principle 14 of the Principles for financial market infrastructures (“**PFMI Principles**”)² issued by the Committee on Payment and Settlement Systems (“CPSS”) and the International Organization of Securities Commission (“IOSCO”). We would like to provide our comments on the proposed CM structure; the proposed approach towards margining and collateral handling; and the proposed approach towards shortfall and default handling.

3. Clearing Member Structure:

In the Consultation Paper, it is proposed that clearing members (“CMs”) may allow indirect participants to trade, within limits set by the CM, in trading systems run by the Clearcorp Dealing Systems (India) Limited or any other trading system as specifically permitted by the CM. As this is similar in concept to an electronic trading platform, we have no major issues as long as the CM and CCP are in a position to

¹ Since 1985, ISDA has worked to make the global over-the-counter (OTC) derivatives markets safer and more efficient. Today, ISDA has over 800 member institutions from 64 countries. These members include a broad range of OTC 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 including exchanges, clearinghouses 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.

² <http://www.bis.org/publ/cpss101a.pdf>, Committee on Payment and Settlement Systems and the International Organization of Securities Commission, Principles for financial market infrastructures, April 2012.

monitor the counterparty risk of its indirect participant at all times irrespective of the trading venue or market access used by this indirect participant. It is equally important that the limits set by the CM for a particular indirect participant, regardless of the trading venue or market access used by the indirect participant, is strictly enforced, monitored and the CCP will notify the CM immediately, if and when, the indirect participant's limit is breached.

One of the key considerations of Principle 14 of the PFMI Principles states that “a CCP should maintain customer positions and collateral in individual customer accounts or in omnibus customer accounts”³. We raise attention to other CCPs, such as LCH.Clearnet, the Australian Securities Exchange (**ASX**) and the Singapore Exchange (**SGX**), that offers or plans to offer both an individual segregated account and omnibus account as part of their OTC clearing service. It should also be noted under paragraph 5 of Article 39⁴ of the European Market Infrastructure Regulations (“**EMIR**”), that a CM should offer its clients a choice between omnibus client segregation and individual client segregation. As the Consultation Paper only proposes offering the omnibus client segregation for the Securities Segment, we seek further understanding on the rationale for limiting the other segments in CCIL, such as the Forex Forward Segment, to individual client segregation only. We believe the omnibus client segregation and the individual client segregation should be offered to all segments of CCIL and not limited to the Securities Segment only.

Paragraph 3.14.5 of the PFMI Principles states that “in order to achieve fully the benefits of segregation and portability, the legal framework applicable to the CCP should support its arrangements to protect and transfer the positions and collateral of a participant's customers”⁵. Accordingly, we seek assurance that the proposed segregation and portability in the Consultation Paper will be upheld under Indian law thereby allowing an indirect participant to port its positions (should it choose to do so) and its margin protected from loss, in the event of a CCP or CM default, according to the account structure it has selected. We also seek assurance that settlement finality applies and there will be no claw-back risks under Indian law in relation to any payments that have been made by an indirect participant.

Paragraph 7 of the Consultation Paper requires “suitable documentation”⁶ for porting. In such an instance, we seek clarification on what will be considered suitable documentation. We believe the choice of porting should reside with the indirect participant. The indirect participant should be given the choice to decide if it wishes to setup and maintain an on-going arrangement with an alternative CM or if it would seek an alternative CM only in the event of a CM's default. As there are associated costs with setting up and maintaining an alternative CM arrangement, an indirect participant should be allowed to decide what best suits their needs.

³ <http://www.bis.org/publ/cpss101a.pdf>, Committee on Payment and Settlement Systems and the International Organization of Securities Commission, Principles for financial market infrastructures, Principle 14, Page 82, April 2012.

⁴ <http://www.bis.org/publ/cpss101a.pdf>, Committee on Payment and Settlement Systems and the International Organization of Securities Commission, Principles for financial market infrastructures, Paragraph 3.14.5, Page 83, April 2012.

⁵ <http://www.bis.org/publ/cpss101a.pdf>, Committee on Payment and Settlement Systems and the International Organization of Securities Commission, Principles for financial market infrastructures, Paragraph 3.14.5, Page 83, April 2012.

⁶ <https://www.ccilindia.com/Lists/LstDiscussionForum/Attachments/7/Intra-day%20MTM%20Collection-All%20segments-18022014.pdf>, The Clearing Corporation of India Ltd., Mumbai, Consultation Paper on *Intra-day Mark to Market Margin Collection in CCIL's CCP Cleared Segments*, Paragraph 3(b), Page 3, 18 Feb 2014.

If and when the client structure proposed in the Securities segment is extended out to the other segments within CCIL, we would like to suggest that if a CM's affiliates are considered as clients, these CM's affiliates should be identifiable and an additional option within the client account structure be allowed for a CM's affiliates, i.e., CMs may place their affiliates transactions in a separate account from their proprietary account. Netting of margin and collateral should be applied for all affiliates in such an account. We seek clarification on the meaning behind the sentence "for identified small clients, margins on their trades could be carried out in a group"⁷. As an indirect participant would have selected a client account that is appropriate to their risk appetite, we seek clarification on how an identified client group account will be constructed and who will make the determination of which clients will be placed in an identified client group account instead of an omnibus account. As both the CM and the CCP will be bound by the principles of segregation, both the CM and CCP will not be able to move a client's positions to another account type without its consent. Further we seek clarification on how the CCP will determine when an individual client will be required, subject to agreed parameters, to only opt for the segregated client account model. As the CM will have no visibility over a particular client's aggregated portfolio, when the CM on-boards this client, the decision on what type of client account structure will be decided by the client. The choice of what type of client account structure should be left to the client.

Paragraph 9⁸ of the Consultation Paper proposes that an indirect participant may be allowed to clear through multiple CMs. It should be noted in Principle 19 of the PFMI Principles that "an FMI should identify, monitor, and manage the material risk to the FMI arising from tiered participation arrangements"⁹. As a CM will not have an overview of the aggregate position of such an indirect participant, the CCP will need to be in a position to identify, monitor and manage any material risk to the CCP that may arise in such a situation.

4. Margin Shortfall:

In the event of a margin shortfall by an indirect participant, we acknowledge that the CM will be responsible for providing the required margin to cover the indirect participant's shortfall.

5. Settlement Shortages:

In the event of a settlement shortage by an indirect participant, we acknowledge that the CM will be responsible for providing the required monies to cover the indirect participant's shortage.

⁷ <https://www.ccilindia.com/Lists/LstDiscussionForum/Attachments/7/Intra-day%20MTM%20Collection%20All%20segments%2018022014.pdf>, The Clearing Corporation of India Ltd., Mumbai, Consultation Paper on *Intra-day Mark to Market Margin Collection in CCIL's CCP Cleared Segments*, Paragraph 3(b), Page 3, 18 Feb 2014.

⁸ <https://www.ccilindia.com/Lists/LstDiscussionForum/Attachments/7/Intra-day%20MTM%20Collection%20All%20segments%2018022014.pdf>, The Clearing Corporation of India Ltd., Mumbai, Consultation Paper on *Intra-day Mark to Market Margin Collection in CCIL's CCP Cleared Segments*, Paragraph 3(b), Page 4, 18 Feb 2014.

⁹ <http://www.bis.org/publ/cpss101a.pdf>, Committee on Payment and Settlement Systems and the International Organization of Securities Commission, Principles for financial market infrastructures, Principle 19, Page 105, April 2012.

Paragraph 10(ii) of the Consultation Paper also states that “any shortage on account of a participant however would have minimum impact on another participant even if margin for trades of such participant comes from the same collateral group”¹⁰. While we support the protection of indirect participants from fellow customer risk, indirect participants in an omnibus or an identified client group will be exposed to fellow client risk. It should be noted that any shortage on account of a participant may also be due to the default of a CM, in which case, all indirect participants within the same collateral group would be impacted. Although an indirect participant will face fellow client risk in the omnibus and identified client group account structures, an indirect participant should always be allowed to select the client account structure that meets its needs, cost and risk appetite.

We seek clarification if the indirect participant’s margins will be collected on a gross or net basis. CMs should be allowed the option of whether margins should be collected on a gross or net basis as the CMs are liable for any margin shortfalls or settlement shortages of its indirect participants.

6. Default on Account of Indirect Participants:

It should be noted that indirect participants in an omnibus account or identified client group account structures will be exposed to fellow client risk. As CCIL will be entitled to use the collaterals placed as margin by the CM for the defaulted indirect participant, we seek confirmation that there will be no conflict of law issues that may impede or prevent CCIL from using the collateral when the indirect participant is not located in India.

7. Clearing Member Default:

As porting of the omnibus or identified client group client account structures may be difficult to implement, when a CM defaults, the CCP may wish to consider granting the CM a grace period. This grace period will allow the CM sufficient time to port its indirect participants’ positions in an omnibus account or an identified client group account to another CM prior to a forced close-out of these positions by the CCP. The current proposal in the Consultation Paper of placing the responsibility with the indirect participants to ensure porting of their positions to an alternative CM within a day’s period may be difficult to implement. It may be beneficial for the CCP to be aware of the portability arrangements on an on-going basis, which may facilitate the CCP’s decision on whether or not to close-out the non-defaulting indirect participants’ positions. This decision should be made in conjunction with the default management process of each segment. The default management process should encompass the default of both a CM and an indirect participant. It should be clearly established and referenced in the CCP’s rules. In addition, the CCP’s rules should also contemplate the possibility of a default by the CCP and the procedure or default management process for such a scenario. Further we seek confirmation that CCIL has an established mechanism in place to facilitate the porting of the indirect participants’ positions and margins to another CM as per the porting agreements of the non-

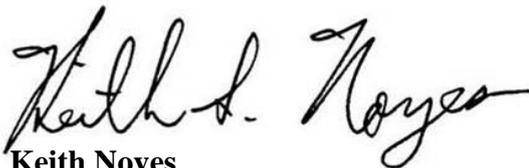
¹⁰ https://www.ccilindia.com/Lists/LstDiscussionForum/Attachments/7/Intra-day%20MTM%20Collection%20segments_18022014.pdf, The Clearing Corporation of India Ltd., Mumbai, Consultation Paper on *Intra-day Mark to Market Margin Collection in CCIL’s CCP Cleared Segments*, Paragraph 10(ii), Page 5, 18 Feb 2014.

defaulting indirect participants. This porting process should not be impeded by any conflict of laws that may arise when the CM is not incorporated in India.

ISDA appreciates the opportunity to provide comments on the Consultation Paper. If you have any questions on this submission, please contact Keith Noyes at (knoyes@isda.org, at +852 2200 5909) or Cindy Leiw at (cleiw@isda.org, at +65 6538 3879) or Erryan Abdul Samad (eabdulsamad@isda.org, at +65 6538 3879) at your convenience.

Yours sincerely,

For the International Swaps and Derivatives Association, Inc.



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