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Mr Daniel McAuliffe
Manager
Financial Markets Unit
Corporations and Capital Markets Division
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Mr McAuliffe,

Council of Financial Regulators – Implementation of a framework for Australia's G20 over-the counter derivatives commitments

ASX welcomes the approach the Government and Council of Financial Regulators have taken in developing its policy to implement Australia's G20 commitments on OTC derivatives.

We look forward to participating in the stakeholder consultation meetings that the Council will be holding with interested parties. ASX believes such a process will enable an effective airing of the wide range of complex issues that arise when considering policy settings in this area.

Australia needs a robust regulatory framework for managing OTC Derivatives

The decisions with regard to these important issues will not only impact the systemic stability of the Australian financial sector but will also heavily influence the structure of our capital markets going forward. These decisions will also determine if Australia will be able to achieve its regional financial centre aspirations or whether its key financial sector infrastructure will increasingly be located and regulated overseas.

ASX recognises the current approach of providing an opportunity for economic incentives to drive a market led 'solution' to deliver on the Government's objectives and meet its G20 commitments. For its part, ASX is already actively engaging in that process through discussions with its clients and other key stakeholders.

The truncated timeline within which to deliver on the Government's G20 commitments, the wide range of different stakeholder perspectives on these issues, and the desirability of ensuring that foreign financial market dislocation does not negatively impact systemically important Australian financial markets, may make it necessary for the Government to mandate an outcome if it is to achieve its policy objectives. If that is the case then we believe the legislative framework articulated in the paper provides a robust structure to consider and enact regulatory change in relation to OTC derivatives.

ASX notes that the proposed framework is intended to promote regulatory flexibility, for example, to apply different approaches to different classes of derivative product and to allow for regulatory obligations applying to some service providers to vary (potentially significantly) as circumstances change. However, where the trigger for a change in obligations (for example the imposition of location requirements) is not clearly defined, the resulting

regulatory uncertainty can affect the timely and effective provision of financial market infrastructure services. It may affect the willingness of service providers to invest to establish operations, or customers to commit to a service where the regulatory obligations may change and make the business model uneconomic. ASX therefore believes that the outcomes from the consultation proposed by the Council on the scenarios where these requirements may be imposed in a 'proportional and graduated manner' are critical to providing the certainty necessary for the effective implementation of the regulatory framework.

The formal requirement for substantive stakeholder consultation (both at the level of Ministerial determination and the more detailed obligations imposed through ASIC's Derivative Transaction Rules) will be a key factor in ensuring that policy settings deliver efficient and cost-effective solutions to achieve the Government's objectives. This includes appropriate transitional arrangements that allow for operational and technology arrangements to be put in place.

ASX has previously provided detailed feedback to the Council in response to its June 2011 discussion paper on clearing of OTC derivatives as well as in response to Government's April 2012 release relating to the regulation of financial market infrastructure.

A suitable, detailed regulatory regime is outlined in ASX's original OTC Derivatives Clearing submission

In relation to centralised clearing of significant OTC derivative products, we would refer the Council to the earlier submission by ASX Clearing Corporation (dated 1 September 2011) which provided greater detail.

Some of the key points made in that submission were:

- Uncertainty surrounding Australian regulatory requirements has meant that participants trading Australian OTC derivatives have not been able to commit to an appropriate market-led solution;
- Delays in setting regulatory requirements, or setting of a regulatory framework that encourages offshore provision of clearing services, could see a larger and perhaps dominant share of Australian denominated and traded product cleared offshore;
- An outcome where most clearing of systemically significant products is conducted offshore could significantly limit the ability of domestic regulators to manage systemic risk in the Australian financial system, particularly at times of crisis;
- ASX believes \$A denominated OTC interest rate products can be centrally cleared (e.g. interest rate swaps, overnight index swaps and forward rate agreements) but other products are unlikely, at this stage, to require or be suitable for central clearing.
- ASX is confident that a cost effective and timely, domestically-based, solution for the Australian market can be developed, subject to regulatory clarity being provided.

Case by case consideration is required for Trade Reporting mandating

ASX recognises the important role trade reporting can play in generating essential information about the size, characteristics, and operation of some relatively opaque OTC markets. We agree that having robust and detailed information on these markets is a critical pre-requisite to determining whether there is a need to mandate centralised clearing or electronic trading of those products.

This suggests that the class of derivatives subjected to mandated trade reporting may well be wider than that for any mandated centralised clearing. However decisions on the precise coverage of derivative products and reporting parties will raise complex issues and potentially impose significant implementation costs in establishing reporting systems. Any detailed consideration of data coverage needs to be conducted on a case by case basis so the cost of collection can be assessed against the benefits of the data being collected.

ASX also submits that the capital investment which is needed to develop the trade repositories and to provide stakeholders with data must be underwritten by legislative recognition and protection of the right of those repositories to commercialise such trade data on reasonable terms.

Any mandatory electronic trading of OTC derivative products is most likely to be linked to central clearing.

In relation to the mandating of trade execution facilities for standardised derivative products we believe a case by case approach is required. We agree that where centralised clearing is mandated, the availability of transparent and reliable pricing is very important to enable CCPs to effectively manage risks.

Competitive neutrality is an important element of any regulatory regime

The consultation paper also raises questions around a proposed licensing regime for trade repositories based on the models already in place for the licensing of market and clearing and settlement facility operators. We agree that such a system would provide appropriate regulatory oversight of this important financial market infrastructure and enable key standards for service delivery to be established.

We note that it is proposed that alternative arrangements would be applied to potential overseas trade reporting facilities, where they are subject to equivalent regulatory arrangements in their home jurisdiction. However, we believe that competitive neutrality between potential domestic and overseas service providers should be preserved and is consistent with the need to provide sufficient risk management controls to Australian regulators.

As we indicated in our submission to the Council's Review of Financial Infrastructure Regulation, decisions in relation to licensing and location requirements will play a key role in determining whether critical financial infrastructure services will be conducted in Australia. This applies regardless of whether the specific facility is providing trade reporting, clearing or trade execution services.

ASX considers that it is in Australia's national interest to maintain a world-class regulatory system and systemically significant market infrastructure in Australia to provide Australian authorities with sufficient powers to intervene in times of crisis.

We would once again like to thank the Government for the opportunity to provide our initial feedback on some of these important issues and look forward to further engagement with Council as the details of the policy framework is further developed.

If you would like to discuss further detail on our submission please contact:

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Yours sincerely



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