

15 February 2013

Financial Markets Unit Corporations and Capital Markets Division The Treasury Langton Crescent PARKES ACT 2600 Australia

To whom it may concern,

## Response to Consultation Paper: Implementation of Australia's G-20 over-thecounter derivatives commitments

Finsia represents 16,000 members from corporate finance & wholesale banking, financial markets, managed funds & superannuation, private wealth management and retail banking, and has a long history of contributing to higher standards of professionalism among industry participants.

Finsia appreciates the opportunity to respond to the consultation paper on a proposed approach for implementing the Australian Government's G-20 Commitments in relation to over the counter (OTC) derivatives. Feedback has been provided under each relevant question below.

1. Do you have comments on the costs and benefits of complying with the trade reporting obligation, as outlined above, from the point of view of your business and/or that of your customers?

The reporting of over-the-counter derivative trades to trade repositories is supported by Finsia. The trade repositories could add to the transparency and surveillance capability of regulators and monitoring systemic risks (near to real-time as possible).

Under bilateral OTC trading, the characteristics of trading activity, financial innovation and, most importantly, exposures arising from trading, are regarded as being opaque to regulators and market participants. During the Global Financial Crisis, regulators and market participants were not fully abreast of market exposures, the interconnections between counterparties arising from trading, and the levels and timing of exposure concentration by counterparty. They were thus constrained in their ability to effectively supervise the OTC market and monitor trading activity.

By requiring all OTC derivative transactions to be reported to trade repositories, comprehensive data regarding all OTC derivatives can be made available publicly and to regulators. Increasing the transparency of trading goes some way to addressing the above issues and simultaneously decreases both the potential for

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moral hazard on the part of participants and information asymmetries arising from trading.

For the data collected by trade repositories to be useful to regulators, ongoing work needs to be completed on the scope of data needed by authorities and on technical issues, such as reporting formats, the legal entity identifier (LEI) and data aggregation.

Whilst the use of trade repositories is supported by Finsia uncertainty exists regarding the following aspects of the use of trade repositories:

- Data management the data stored in the repository will be highly sensitive to institutions and its confidentiality and privacy is critical. Therefore adequate controls will need to be implemented by trade repositories to manage their operations.
- > Data accessibility it is not clearly understood as to which market participants and stakeholders will have access to data stored in trade repositories, for what purposes will the data be assessable, and will it be available more broadly to all market participants in a summarised manner or made available for academic and industry research (not just available to regulators).

Compliance with the regulatory obligation of reporting trades to trade repositories will increase operating and compliance costs for financial institutions. The cost impost of treasury systems obtaining derivatives data and the frequency with which that data will need to be captured will be significant, particularly for participants who do not have this technology already in place. These costs will involve the initial implementation work and the ongoing process of capturing and reporting trades on a frequent basis. Although we cannot make specific comments relating to the nature or level of the costs, we do note that many financial institutions currently use multiple internal systems for their trading, risk management and reporting purposes. Therefore many financial institutions will need to further modify existing controls and reporting functions accommodate the trade reporting. These costs will be reflected into operating costs and could increase the cost of transacting in financial markets.

OTC derivatives are two-way transactions and it is not clear whether the obligation to report a trade to the repository applies to both parties. If obligations apply to both parties, there could be needless duplication of reporting that may result in an inefficiency impost. Should the reporting requirements be divided between the real users or the providers of these transactions or should both counterparties be responsible?

Many Australian OTC market participants trade across multiple geographic areas and regulatory jurisdictions. So far as possible, the Australian framework should be aligned with those offshore to ensure compliance costs are contained. Regulators could develop a broad understanding of international trade repository regulatory requirements to ensure this alignment of reporting requirements.

2. Do you have comments on the proposal to mandate a broad range of derivatives subject to the phase in and exceptions outlined below? Or is there another option you prefer? If so why?

We are supportive of this approach and believe that the phasing in of new regulations is the appropriate manner of implementation. The capturing of interest rate swap contracts in the first instance is beneficial because this will capture most of Australia's derivative contracts and the long term nature of these contracts will make it easier for institutions to collate their own data. This approach will also ensure teething problems for trade reporting, both from a regulatory and institutional viewpoint, can be handled appropriately.

3. Do you have a preference for the timetable being prescribed in regulation or implemented by a phased approach to ASIC rule making?

We are supportive of ASIC determining the phased approach as they can consider all stakeholders when prescribing the timing and implementation.

4. Do you have comments on the proposal timetable for implementing the trade reporting obligation? Or is there another option you prefer? If so, why?

We are supportive of implementing trade reporting regulations in the proposed phased order. It is important that a significant proportion of all OTC derivatives are captured through the trade reporting process to assist with the transparency of trading activity.

5. For Phase 1, do you have a preference for referencing legal status, thresholds of activity, or size proxies? For Phases 2 and 3, do you prefer activity thresholds or size proxies?

Finsia does not have a preference however would prefer consistency across institutions so that no institution obtains a regulatory advantage through the reporting framework.

6. Do you have comments on the proposed regulations at Attachment A? Or is there another option you prefer? If so why?

We are supportive of Attachment A and the delay to the treatment of electricity market derivatives. We note that unlike other OTC derivative markets, the electricity market operates as part of a different regulatory framework to other OTC derivative instruments and regulatory changes could impact on reallocation settlement activities by market participants.

7. Do you have comments on the proposal to wait until after review processes before making a decision on mandating trade reporting of electricity derivatives? Or is there another option you prefer? If so, why?

Please refer to the answer under question 6.

8. Are there other bodies with responsibility for underlying assets upon which a derivative is based that should be also be specified under section 901J?

None that Finsia is aware of.

9. Do you have comments on the proposal to implement the trade reporting and trade repository licensing regime expeditiously, but not to impose interim reporting obligations ahead of this? Or is there another option you prefer? If so, why?

Finsia supports the proposed approach provided the issues discussed in question 1 have been considered as part of any expeditious move towards trade repository licensing. Key issues here will involve the issues discussed in question 1 and the standardization of reporting obligations.

10. Do you have comments on the proposal to not impose central clearing obligations at this stage? Or is there another option you prefer? If so, why?

The delay to impose central clearing obligations is a sensible position at this stage.

Finsia believes care needs to taken with central clearing as it will include margining. Margining would make derivatives less effective as a hedging tool as it would shift the timing and impact the cash flows for a transaction, from the maturity of the hedge to any time from the inception of the hedge. This more than likely will not match the timing of the cash flows for the exposure being hedged.

It is also important to note that since 2008 the majority of Australian institutions trading in OTC derivatives use ISDA master agreements incorporating a credit support annex or other collateral arrangements. Finsia believes the widespread use of ISDA master agreements among Australian institutions also supports the position to delay central clearing obligations until further consultation has taken place.

11. Do you have comments on the proposal to not impose trading obligations at this stage? Or is there another option you prefer? If so, why?

Finsia notes that international regulators are still looking to implement a global Legal Entity Identifier (LEI) system that will uniquely identify parties to financial transactions. Currently many institutions have multiple LEI's and this means it can

be difficult to track counterparties. A uniform system for identifying entities will improve risk management in firms; facilitate orderly resolution measures; contain market abuse and reduce financial fraud; and enable higher quality and accuracy of financial data overall.

Finsia is grateful for this opportunity to respond and is willing to be involved in any further consultations on these matters. If you have any further questions please contact Samuel Bell, Senior Policy Advisor on (02) 9275 7953 or email s.bell@finsia.com.

Yours sincerely,

Russell Thomas F Fin

**CEO and Managing Director**