Finance and Treasury Association

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Re Implementation of Australia's over-the-counter derivatives commitments
- Response to December Treasury consultation paper by Finance and Treasury Association.

The Finance and Treasury Association welcomes this opportunity to once again consult with Australia's financial regulators on proposed regulation of OTC derivatives transactions.

This will be FTA's fifth submissions on OTC derivative regulations starting in September 2011 with a response to the Council of Financial Regulars (via RBA), then June 2012 (Treasury), September (Treasury), October (Parliament of Australia), and now March 2013 (Treasury).

FTA recognises that this consultation forms part of the necessary work designed to ensure that Australia meets commitments made at the 2009 G-20 Summit in Pittsburgh that over-the-counter (OTC) derivatives will be capable of being reported, centrally cleared, exchange traded.

We note that the current stage is laying the ground work for a pending Ministerial determination that may require all five derivative classes (interest rate, foreign exchange, credit, equity and commodity) to be reported to a licensed trade repository where one is available. And it had been planned that the trade reporting regime at least for major financial institutions would be in place by mid-2013.

In prior submissions, FTA has taken comfort that Treasury has acknowledged FTA's key message "some stakeholders argued that their use of derivatives was primarily for the hedging of business risk and questioned the systemic importance of their derivatives trading activities". We reiterate that point.

We furthermore noted that there may be a negative real economy impact from the direct application of these OTC derivative regulations on the corporate sector. A common experience with regulation is that any extra costs and complications end up being borne by the end user, and so dampen economic activity; policy-makers and regulators need to be mindful of this very real impact when they impose these regulations. Hence FTA asked that regulators first seek to determine the full cost-benefit equation of the proposed reforms.

FTA recognises Australia is obliged to act quickly to ensure Australian businesses and investors are "able to demonstrate that they are subject to an equivalent regulatory regime and so be able to continue to participate in the major derivatives markets of the world while still being primarily regulated in Australia".

FTA reiterates that non-financial corporations ("corporates") are large users of financial derivatives and that these transactions are primarily used to manage financial risk positions created through on-going business operations or funding activities. FTA is particularly concerned to ensure its Australian corporate treasurer members will continue to be able to use flexible OTC instruments such as forward foreign exchange contracts and cross currency swaps and these vital tools not be made prohibitively expensive nor administratively unworkable. FTA considers that deals done by non-financials are a tiny part of the derivatives markets here and abroad, and are not material in their impact on systemic risk and hence should be exempted from the proposed rules. We reiterate our offer to work with the regulators on developing a robust definition of hedging to support such an exemption.

Overview

With the late finalisation of our submission, FTA has had the benefit of reviewing submissions by a number of parties including the Australian Swap Dealer banks, AFMA, other significant industry and professional associations, and a major global corporate treasury with an offshore parent which has chosen not to make a public submission. (Refer - http://financialmarkets.tspace.gov.au/ for public submissions.)

We have also consulted with peer treasury associations offshore, notably the Association of Corporate Treasurers (UK) which has had experience in recent months with the issues being addressed in this current consultation.

With this slight advantage FTA has a few insights. A key reinforcement from consulting with our own members and surveying these submissions is that Australia's policy makers and financial regulators are doing well in taking advantage of the lessons already learnt in offshore jurisdictions.

For instance, a key lesson would appear to be that there is minimal additional benefit, and substantial additional cost, from Australia adopting the European (EMIR) approach to trade reporting where corporates get dragged unnecessarily into the net.

In FTA's view, there are two key decisions to be made at this juncture.

Firstly, appropriately defined end users such as non-financial corporations engaged in the activity of hedging should be exempted from all OTC reporting requirements via activity and size thresholds. In so doing there needs to be an exemption for intra-group hedging transactions.

Secondly, Australia ought to adopt single-sided reporting i.e. the US reporting hierarchy principle that only one party to each derivative reports the transaction and the reporting party will be the financial institution with the highest level of registration (i.e. Swap Dealer or Major Swap Participant under the Dodd-Frank Act). From an efficiency and domestic market integrity standpoint, it would be optimal if Australian banks were able to use the process and systems investments that they have already made in addressing the requirements of the Dodd-Frank Act while continuing to be primarily regulated by APRA and ASIC as rules are developed and refined globally.

Provided these two decisions are made, FTA would have a higher degree of comfort with the more flexible approach advocated by the Australian banks registered as Swap Dealers in their submission to this consultation.

In the absence of these two decisions, however, FTA would ask Australian regulators to avoid expeditious introduction of trade reporting (and repository licencing) and not wish to impose changeable interim reporting obligations.

FTA considers it vital that there be no disruption to the ability of Australian corporate treasurers to be able to hedge currency and interest rate risk associated with their offshore borrowing programs and further to be able to access a full suite of risk management products at competitive rates. We conclude that in the absence of liquid markets for non-vanilla products that valuation protocols must be established. And we question whether investing in the processes and systems to capture and report on the OTC trade activity by non-financial organisations will be in the economic interest of all but the largest corporates. The derivative regulation in Europe is already law, with the implementation dates for trade reporting phased in over the next year. As companies start to grapple with the all-encompassing reporting obligations it has become ever more apparent to the ACT in the UK that that reporting by non-financials is "a pointless and unnecessary burden".

FTA feels strongly that the activities of typical non-financial corporation end-users do not pose a systemic risk to the Australian nor global financial system.

Throughout the consultation process, FTA has sought more information about how (the next day) data collected by trade repositories will be used, and by whom, and the protections for commercial-in-confidence corporate activity that will be in place. We have received no detailed response to these questions from local or international regulators and see these answers as a foundation for any licencing process of new market utilities, or for Australian entities reporting trades offshore.

There may be long term benefits from the collection and subsequent analysis of this data set. But there are other ways to analyse the structure, conduct and performance of the OTC derivatives market which do not rely on ever-more sophisticated and costly algorithms and “big data”.

While taking a pragmatic perspective, and recognising Australia’s G20 commitments, FTA has also questioned the very rationale for centralised clearing and exchange-trading, in raising concerns that they may in fact exacerbate the concentration risk that is present, but less of a concern, under a traditional diffused over-the-counter regime.

Arguably, the centralised reporting, clearing and exchange trading regime rather than overcoming the “Too Big To Fail” conundrum merely recreates it in another form. Some of the existing offshore market utilities that will be licenced to receive the trade information, and later conduct clearing and potentially provide exchange trading platforms, are owned by the same big banks whose stability lies at the very centre of the post-GFC regulatory push.

It has been argued the mandating of centralised utilities in this light may be another way which these big banks will be over time able to extract monopoly rents from lesser capitalised and well-connected/located competitors. In this instance, those paying the bill would be Australian banks, and mostly by extension, their customers, including FTA members’ companies and their shareholders.

Intrinsic as the providers of central infrastructure will be to the entire G20-inspired OTC regulation regime, FTA encourages Australia’s financial regulators as part of the licencing process to analyse the business models of these entities and put in place protections against monopolistic pricing practices.

Specific responses to questions in Consultation Paper

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?**

FTA understands broadly the reasons why financial regulators wish to collect the OTC derivative trade data and has no objections in principle provided data is secure and commercial sensitivity is respected.

FTA recognises that in the wake of the collapse of Lehman Brothers, it became apparent to regulators that not even market-making participants could confidently ascertain the quantum of outstanding derivative positions and hence the counterparty credit risk concentrations. Furthermore, efforts to contain risk to a few institutions were frustrated by the interconnectedness of counterparties in the OTC derivative market.

But FTA strongly recommends that the Australian financial regulators do <u>not</u> adopt the trade reporting rules proposed in the European Markets and Infrastructure Regulation (EMIR).

In Europe the reporting requirements cover even very small companies and require around 40 reporting fields for every deal. The Association of Corporate Treasurers (ACT) report that any company in Europe undertaking derivative transactions, even just FX forwards, will be affected. Moreover, intra-group deals will also need to be reported in the same detail.

FTA is not comfortable for non-financial corporations to have to report to central trade depositories that do not yet exist, which is the situation in the UK and Europe. Reporting in advance of the introduction of these central trade depositories will be a major administration burden; in Europe all derivatives outstanding on 16th August 2012 and executed since then will eventually have to be reported to trade depositories that do not yet exist.

Should there be no exemption for corporate hedging activity, and/or a decision to adopt one-sided reporting by the entity with the highest level of registration, as discussed in our response to Questions 4 and 5, FTA would seek from Australia's financial regulators a floor by size of deal reported and size of company reporting.

The ACT has published a briefing note *European regulation of OTC derivatives: Implications for non-financial companies* to help non-banks understand the specific implications for them. Refer: http://www.treasurers.org/node/8649. Decision-makers on the regulation of OTC derivatives in Australia are encouraged to go to this page and associated documents.

FTA observes Australian financial regulators and their peers offshore have provided little detail about how the reported OTC trade data is to be used. <u>How the data is to be used and by whom goes to the heart of the value of assessing the particular benefits of end-users, and particularly non-financial corporations.</u>

FTA considers that OTC derivatives used by non-financial corporation end-users for hedging do not pose any systemic risk to the domestic nor global financial system. Moreover, it is core business for banks to provide a risk intermediation and transformation products and services. All risks that a corporate would be seeking to manage via a derivative contract are entirely capable of being on-sold to another party where there are not natural offsets within a bank's own balance sheet.

There are currently no trade reporting requirements for corporations. How will corporates capture data in useful formats? In the absence of information about what is to be reported and how, it is not feasible to provide a detailed estimate of costs except initial set up, particularly if these costs were be repeated each time new fields are added.

FTA is particularly concerned that corporates might be required to provide next day trade reporting. This is only really feasible for larger entities which have the capacity to invest in a treasury management system (TMS). For those companies that cannot afford a TMS, the compliance with the trade reporting regulation would require a manual work-around i.e. manual entry into spreadsheets. Inevitably there would be keying errors which if unaddressed would undermine the fidelity of the data. On the other hand, validating this data plus restructuring existing controls and reporting functions would produce additional layers of cost. (And FTA would not want underprepared and resourced corporates to be held legally responsible for any errors in data reported.)

And as addressed in other submissions to this consultation, for the data to be most useful to whoever will be tasked to analyse it, it would need to be captured standard formats. Manual work-arounds are by their nature, non-standard.

Furthermore, if there were to be an onus on corporations having to provide next day valuations this would add extra layers of complexity and cost as data feeds from arms-length, independent third parties (as distinct from the counterparty banks) are additional to the TMS, and expensive.

Finally, it is worth reiterating that OTC derivatives used for hedging are not already exchange-traded because they are at some level bespoke. They are bilateral contracts where the counterparties agree terms specific to the needs of the end user.

Liquid markets are not only useful to make central clearing and exchange-trading worthwhile, they are also a necessary pre-requisite for accurate pricing and valuation as the only true value for any financial instrument is what someone else will pay for it. If there is not liquid market then valuations must be produced via models which are only as good as the assumptions that are input. In short, a requirement for daily reporting and valuations of non-standard OTC derivative positions, by a corporate or a financial institution, rather than producing a set of objective data that may be analysed in aggregate may in fact contain a series of assumptions which will distort the overall picture.

Coupled with other risk management initiatives such as electronic trade confirmations, trade compression etc which Australia's financial regulators have endorsed and which FTA considers being in line with best practice, <u>FTA does not see a net benefit for corporates in reporting directly to trade repositories.</u> So in Question 9, FTA does not support expeditious introduction of OTC data reporting by non-financial corporations.

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?**

Here FTA observes potentially opposing views from key respondents to this consultation.

On the one hand, ISDA (International Swaps and Dealers' Association) the primary international association for OTC market participants believes for practical technical and resourcing reasons, "a big bang approach in which all five derivative classes are required to be reported by a specified deadline, may not be practicable."

For the Australian Swap Dealer banks, the "primary concern is that the range of derivatives captured by the Australian regime is sufficiently broad, and the exemptions sufficiently narrow, so that foreign regulators such as the CFTC (US) and ESMA (Europe) will be satisfied that Australian industry participants can be primarily subject (to) the Australian regime rather than the foreign regime. "

FTA considers that there are different issues across the asset classes with reporting of even the most generic OTC derivatives, and so is wary of a blanket approach being taken.

Spot foreign exchange transactions settle within two days but are technically OTC derivative trades. What would be the benefits of reporting them?

And many of these trades are done internally by corporates. FTA quotes from the unreleased submission from a major global corporate treasury with an offshore parent.

"An exemption for end user to end user transactions should be considered where both parties are part of the same corporate group. Many corporates centralise their market activity in order to reduce risk and better manage the financing requirements of global operations. This can result in internal derivative transactions between legal entities of the same corporate group. We can see no benefit in reporting these internal transactions."

And, regulators should "eliminate or minimize the need to report on derivatives between end-users, in particular where these derivatives are demonstrably for the purposes of hedging an underlying exposure. The alternative imposes a significant reporting burden on one or both of the end-users to the intra-group derivative and it is not clear how the reporting of such transactions would help to reduce systemic risk in the Australian financial system."

Hence FTA argues there should be an exemption for intra-group hedging transactions - which are core activity of significant corporate treasuries.

The US reporting hierarchy principle where only one party to each OTC trade reports the transaction and the reporting party is the most sophisticated financial institution (by level of registration) does away with costly duplicate reporting while maintaining transparency over end-user transactions.

Should Australia adopt the US reporting hierarchy principle, FTA is more comfortable with ASIC making this determination reflecting offshore developments and the readiness of Australian banks.

To the degree that Australia can control its own destiny, FTA is aligned with the view expressed by Finsia in their submission. "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."

Furthermore, as the FSC suggest it would be sensible that "more complex derivatives (e.g. exotic/multi-leg) should have a longer phase-in time for mandatory trade reporting". Foremost among these instruments for Australia treasurers are cross-currency interest rate swaps (CCIRS).

The companies represented by our members enter into cross currency interest rate swaps in conjunction with the issuances of foreign currency debt into the global capital markets. This is done with one overriding objective of securing a sufficient quantity, diversity and tenor of funding to enable the company to meet its business objectives, while protecting the strength of the balance sheet and therefore the interests of all stakeholders, including investors and lenders. With this in mind, the choice of whether to issue in domestic currency, or in foreign currency and hedge is based primarily on a comparison of the net cost of funds of a foreign currency issuance, inclusive of all hedge costs, against the domestic borrowing rate. These transactions are typically done by contracting to receive under the CCIRS a stream of cash flows that exactly match the cash flow obligation under the foreign currency debt, and committing to pay domestic currency cash flows at the current prevailing fixed or floating market rate.

FTA made similar comments to these in a recent letter to the International Accounting Standards Board and Australian Accounting Standards Board which contributed to a change in the proposed accounting treatment of currency hedging.

Currency hedging is more important to Australian non-financial corporations, and the Australian economy at large, than for the United States and the countries of Europe which are driving much of this regulation. Hence it is FTA's view that particular care must be taken not to make it unnecessarily costly.

Moreover, FTA considers that whatever decisions are made that Australia's financial regulators actively represent the Australian position with their offshore peers.

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

A pre-determined timetable with further scheduled stages of public consultation prescribed in regulation might be considered better practice for change of this magnitude which imposes substantial costs on market participants to produce a public good outcome, the value of which is difficult to quantify.

And AFMA remind us that while trade reporting can really only commence in a meaningful way when a trade repository is licensed, "past experience with financial market infrastructure licensing suggests that the application approval process can be quite protracted and subject to considerable uncertainty until a ministerial decision is made." So it may not be appropriate to wait for licences to be issued before commencing the regime.

However, the Government's over-riding commitment to its G20 obligations, unpredictable developments in other jurisdictions and the industry's need to demonstrate "substituted compliance" to offshore regulators to meet extra-territorial requirements, means there is a stronger need for flexibility and for ASIC to be delegated rule making authority.

Most of the submissions to date recognise this point and FTA is in accord assuming engagement with industry through further stages of consultation from ASIC.

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?**

The timetable which this question addresses proposes three separate phases with staged commencement dates.

Phase 1: major financial institutions: these would be required to commence reporting of trades in the first phase.

Phase 2: domestically focused financial institutions: Australian deposit taking institutions (ADIs) and larger AFSL holders (and those exempt from holding AFSLs under relevant ASIC class orders for foreign financial services providers) which are not within phase 1, would be required to report starting in Phase 2.

Phase 3: end users: end users (including corporates), and other financial institutions not commencing reporting in Phase 2, would be subject to reporting in phase 3.

FTA does not take issue with the broad timetable for Phases 1 and 2 as it can be made consistent with our recommendation of the adoption of US single-sided reporting hierarchy principle in that only one party to each derivative reports the transaction and the reporting party will be the financial institution with the highest level of registration.

As FTA would expect that with single-sided reporting, the operation of activity thresholds and size proxies would rule out most non-financial corporations, FTA is then comfortable that with Phase 3 following Phase 2 with the proposed six month lag i.e. for implementation at the end of 2014.

FTA notes that “within each phase, there would be scope for further differentiating between instrument classes. “ As addressed in our response to Question 2, non-financial corporations are primary users of multi-leg multi-asset class derivatives such as cross currency swaps the hedge accounting for which has only been settled in 2013 after more than a decade of iterations by accounting standard-setters. We suggest such common but admittedly complex instruments be left to last for implementing the trade reporting obligation.

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?**

On balance, FTA has a preference for threshold of activity, however we consider it would be best structured based on averages over a period of time (e.g. more than 1 year) and lagged, so that if a corporate has a one-off large transaction they are not suddenly ‘tipped in’ when they would not be set up for it.

Our second preference would be for a size proxy combined with an activity threshold. We note that you can be a large corporate with very little activity or sophisticated systems, and vice-versa e.g. specialist trading houses.

FTA agrees with the Financial Services Council in issuing “a note of caution against adopting legal status as the trigger for reporting. Such a regime could lead to entities creating alternate entity types to circumvent the requirement to report. For this reason we would be more supportive of a threshold trigger for reporting requirements."

Furthermore we agree that "threshold triggers linked to market activity are more likely to reflect the level of risk and regulatory cost related to the participant." Like FSC we ask that ASIC should consult with stakeholders on various threshold trigger ranges prior to finalisation.

6. **& 7.** FTA will not be commenting on Questions 6 & 7 concerning electricity derivatives.

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?

FTA notes that it is expected that the regulations may prescribe consultation with other specified bodies where the underlying assets upon which a derivative is based fall with the regulatory responsibilities of that body such as with the electricity regulator AEMCO. Hence FTA recognizes that the financial regulators wish to consult as widely as possible.

FTA notes that bilateral commodity trading is conducted between significant commodity producers such as coal and petroleum companies and with major trading companies. And in more recent times a spot and futures market has evolved in iron ore. These are bilateral OTC deals conducted as commercial contracts but often under the auspices of derivative market agreements which are pro-forma versions of OTC market standard ISDA Master Agreements. That corporates enter commodity hedging arrangements is often required by banks as a condition of project financing.

There may not yet be bodies with regulatory responsibility in this area but FTA encourages policy-makers to seek out those commercial organisations likely to be affected.

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?

The trade repository licencing should not be rushed. Issues including reporting formats, data management, confidentiality and rights to data access security concerns must first be addressed.

FTA is not comfortable for non-financial corporations to have to report to central trade depositories that do not yet exist, which is the situation in Europe. (Reporting in advance of the introduction of these central trade depositories will be a major administration burden; in Europe all derivatives outstanding on 16th August 2012 and executed since then will eventually have to be reported to trade depositories that do not yet exist.)

In order to reduce duplication and support harmonisation, a key consideration is ensuring that the final reporting requirements are fully known before the reporting is required so that all required information is being captured.

To maximise the future utility of the information to Australian policy-makers, regulators and market participants, it is highly important that Australian financial regulators are clear what information they require and why, and that they represent those preferences clearly and early to international peers.

As previously stated, FTA considers OTC trade repository information on corporate hedging should only become publicly available with a significant lag and on a basis where names could not be determined by the nature of data released. And FTA considers that there is a risk of breaching of commercial-in-confidence arrangements.

FTA understands that the preference of Australian regulators is for trade data to be reported on a next day basis, rather than same day; for corporate hedging activity neither is desirable.

Beyond the likely inconsistency with privacy laws we still maintain that it might risk breach of commercial confidentiality because funding positions can be taken in advance of underlying transactions e.g. for market-sensitive mergers and acquisition (M&A) activity. FTA would favour 72 hour window for these activities to take place before being disclosed.

FTA notes AFMA's suggestion that to meet extraterritorial requirements and demonstrate substituted compliance it may be necessary "subject to cross border confidentiality issues being effectively addressed" and "as a short term expedient" to implement interim reporting drawing on existing offshore repositories.

FTA would wish to consult with ASIC should this temporary solution be considered.

Here FTA also notes the comment by the Australian swap dealer banks: "There is a high probability that a material number of counterparties will refuse to provide their consent, giving rise to civil or criminal liability under Australian law if the international reporting obligation is adhere to."

FTA members are the counterparties of banks. The process of negotiating the release of confidential information may push some users from borrowing at least cost on offshore markets or from implementing economically sensible risk management. Some users will leave the market and this is one area where real economic costs of this regulation will be evident.

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?

FTA agrees with the proposal to not impose central clearing obligations at this stage.

No move to mandate clearing should be taken absent the licencing of clearing and settlement providers. However FTA notes broad banking industry agreement to first have central clearing of AUD interest rate swaps.

For derivative classes that are to be centrally cleared, FTA is comfortable with the adoption of *de minimus* rules as in Europe, and a rule that says that hedging deals do not count toward the threshold test for mandatory clearing. We consider that this *may* provide a sufficiently big exemption that few non-financial companies would have to mandatorily clear their OTC derivatives. FTA strongly advises policy-makers to not commence a timetable for introduction of procedures for non-centrally cleared OTC trades – including margining - until the central clearing arrangements for the particular asset class and instrument have been bedded down.

FTA observes that starting 2015 prudential and securities regulators (Basel Committee and IOSCO) will require higher capital charges and margining to apply in future to bilateral OTC transactions not being centrally cleared. Without a broad exemption for corporates, this development would be potentially most damaging to both the ability of end-users to manage risks and also for them to productively employ precious liquidity and shareholder capital.

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?

FTA agrees with the proposal to not impose trading obligations at this stage.

Conclusion

In this paper, FTA reiterated the following points made in previous FTA submissions a Australia's commitment to implementing commitments made to G20 meeting in Pittsburgh in 2009.

- Corporations are large users of financial derivatives in Australia. These transactions are primarily used to manage financial risk positions created through their ongoing business operations or their funding activities.

- FTA is particularly concerned to ensure its Australian corporate treasurer members will continue to be able to use flexible OTC instruments such as forward foreign exchange contracts and cross currency swaps.
- FTA's primary concern is for such prudent corporate risk management tools to not be made prohibitively expensive nor administratively unworkable.
- Given the potential negative real economy impact, FTA recommends if regulators are considering imposing these OTC derivative regulations on the corporate sector that they first seek to determine the full cost-benefit equation of the proposed reforms. Any extra costs and complications end up being borne by the end user and dampen economic activity, so regulators need to be careful of what they impose.
- FTA considers deals done by non-financials are a tiny part of the derivatives markets here and abroad, and therefore not material in their impact on systemic risk and should be exempted from the proposed rules.
- FTA considers OTC trade repository information on corporate hedging should only become publicly available with a significant lag and on a basis where names could not be determined by the nature of data released.
- For Australian entities an appropriate exemption for corporate risk management would protect the non-standardised way corporate entities access OTC derivatives as a primary risk management tool.

In this submission, FTA builds on these arguments with the following points:

- FTA considers two key decisions need to be made at this juncture.
- Firstly, appropriately defined end users such as non-financial corporations engaged in the activity of hedging should be exempted from all OTC reporting requirements by activity and size thresholds. In so doing there needs to be an exemption for intra-group hedging transactions.
- Secondly, Australia ought to adopt single-sided reporting i.e. the US reporting hierarchy principle that only one party to each derivative reports the transaction and the reporting party will the financial institution with the highest level of registration.
- FTA strongly recommends that the Australian financial regulators do not adopt the trade reporting rules proposed in the European Markets and Infrastructure Regulation (EMIR).
- FTA is particularly concerned that corporates might be required to provide next day trade reporting.
- Coupled with other risk management initiatives such as electronic trade confirmations and trade compression which Australia's financial regulators have endorsed, and which FTA considers being in line with best practice, FTA does not see a net benefit for corporates in reporting directly to trade repositories.

- FTA does not take issue with the broad timetable for Phases 1 and 2 as it can be made consistent with our recommendation of the adoption of a single-sided reporting hierarchy principle.
- On balance, FTA has a preference for threshold of OTC derivative activity over a size proxy as a basis for exemption from the new derivative transaction rules. We caution about the use of legal status-based exemption.
- FTA is not comfortable for non-financial corporations to have to report to central trade depositories that do not yet exist. (FTA would wish to consult with ASIC should some form of trade reporting be required ahead of the licensing of a trade repository e.g. to ensure “substituted compliance” and maintain access for Australian institutions to international derivative markets.)
- FTA agrees with the proposal to not impose central clearing obligations at this stage.
- FTA agrees with the proposal to not impose trading obligations at this stage.

We look forward to working with the financial regulators on the next stages of the consultations and the design of the institutional framework.

Yours faithfully,

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About FTA

The Finance & Treasury Association (FTA) is a professional association for executives working across all aspects of treasury and financial risk management. The FTA provides training and skills development and access to current information, facilitates networking and builds a community in this specialised area of business. It seeks to increase recognition of the skills of members and to convey the views of members on key technical issues facing the profession to government, other associations and the wider community.