



Australian Government

The Treasury

Parliamentary Joint Committee on Corporations and Financial Services

Inquiry into the Corporations Legislation Amendment (Derivative Transactions) Bill 2012

Submission by the Australian Treasury

The Australian Prudential Regulation Authority, the Australian Securities and Investments Commission, the Reserve Bank of Australia, and the Department of Resources, Energy and Tourism have been consulted in the preparation of this submission

October 2012

CONTENTS

INTRODUCTION	2
Scope of this Submission	2
PART ONE: PROVISIONS OF THE BILL.....	3
Timing of legislation	4
PART TWO: THE UNDERLYING POLICY FRAMEWORK	4
Application to the financial sector	6
Application to the energy sector	8
PART THREE: THE CONSULTATION PROCESS	11
Consultation and analysis conducted by the Council prior to 2011.....	11
The 2011 Council consultation on central clearing of OTC derivatives.....	11
Consultation on the Government's proposed legislative framework.....	12
Consultation on the draft legislation	12
CURRENT AND FUTURE CONSULTATION PROCESSES	12
Introduction.....	12
Checks and balances, and proper process.....	14
Current consultation and market analysis.....	15
APPENDIX.....	17
Respondents to the May 2009 APRA-ASIC-RBA OTC derivatives market survey	17
Public Submissions to the 2011 Council consultation on central clearing of OTC derivatives.....	18
Public submissions to the Government 2012 consultation paper - <i>Implementation of a framework for Australia's G-20 OTC derivatives commitments</i>	19
Public submissions on the exposure draft - <i>Corporations Legislation Amendment (Derivative Transactions) Bill</i>	20

INTRODUCTION

At the G-20 summit in Pittsburgh in 2009, the Australian Government joined other jurisdictions in committing to substantial reforms to practices in the over the counter (OTC) derivatives market. The three key G-20 commitments related to:

- the reporting of OTC derivatives to trade repositories;
- the clearing of standardised OTC derivatives through central counterparties; and
- the execution of standardised OTC derivatives on exchanges or trading platforms, where appropriate.

These commitments are intended to:

- increase transparency in the OTC derivatives market for regulators, market participants and the public; and
- reduce counterparty credit risks and operational risks associated with OTC derivatives.

The Corporations Legislation Amendment (Derivative Transactions) Bill 2012 ('the Bill') amends the *Australian Prudential Regulation Authority Act 1998*, *Australian Securities and Investments Commission Act 2001*, the *Corporations Act 2001*, the *Mutual Assistance in Business Regulation Act 1992*, and the *Reserve Bank Act 1959* to provide a legislative framework to implement Australia's G-20 commitments in relation to OTC derivatives reforms.

Scope of this Submission

1. This submission is in three parts:

- The first section provides additional information on the provisions of the Bill;
- The second section provides further information on the underlying policy framework and provides some further clarity around the timetable for consideration of future mandates; and
- The third section provides information on the consultation process so far and the process for future consultations.

PART ONE: PROVISIONS OF THE BILL

2. The Bill introduces a legislative framework into the *Corporations Act 2001* that would allow the Minister to prescribe certain classes of derivatives as subject to an Australian Securities and Investments Commission (ASIC) rule making power in regards to trade reporting, central clearing and trade execution.
3. Once a class of derivatives is prescribed, ASIC will have the power to issue rules to establish one or more specified mandatory obligations (reporting, clearing or execution) for transactions in that class.
4. The Australian Prudential Regulation Authority (APRA), ASIC and/or the Reserve Bank of Australia (RBA) may be requested to, or voluntarily, advise the Government on whether various classes of derivative transactions should be made subject to trade reporting, central clearing and on-platform execution requirements. Prior to making any decision to mandate reporting, central clearing or use of trading execution venues, the Government must engage with stakeholders further and consider any advice from the three agencies mentioned above.
5. The definition of 'derivative transaction' covers entry into a derivative arrangement, modification, assignment or termination of such an arrangement. The definition also allows for other types of transaction to be included through regulations. This flexibility is, in part, required to ensure that the Act can potentially apply to transactions dealt with in the laws of other jurisdictions – to enable rules that facilitate compliance with foreign laws and mutual recognition under foreign laws of compliance with our requirements.
6. The Bill also provides flexibility in implementing trading, clearing and on-platform trading mandates. This flexibility is necessary to ensure the regime can be implemented in a proportional and targeted way in Australia, and can be readily adapted to overseas regulatory developments so as to ensure a coordinated approach to the regulation of global OTC derivatives markets between Australia's financial regulators and their international counterparts.
7. Consistent implementation by all major economies is important to reduce systemic risk and the risk of regulatory arbitrage that could arise if there are significant gaps in implementation. International cooperation and flexibility will also help to avoid unintended consequences of national laws such as the burden on businesses of duplicated or conflicting rules and the costs of reduced access to international markets.
8. The Bill contains a range of checks and balances in relation to this rule making power, including a requirement that ASIC consult and obtain ministerial consent for any new rules. The scope of rules and other technical features of the scheme will be further limited by Regulation.
9. It is contemplated that ASIC may be required by regulation, made under the new section 900J, to consult with energy regulators and relevant bodies prior to making any derivative transaction rule.

10. As well as facilitating the possible introduction of trade reporting requirements, the legislation sets out a new licensing regime for trade repositories. Trade repositories will record derivative trade data and make it available to relevant regulators. This information can be used by regulators for monitoring market integrity and stability and enhance the supervision of banks and other market participants. Trade repositories also have the potential to facilitate efficiency improvements in post-trade processing and production of high-level statistical data for market use.
11. This licensing regime is based upon existing licensing regimes for financial markets and clearing and settlement operators, but adapted for the different role that this new form of market infrastructure entity will play. A key aspect of the regime is the strong protections against improper use and disclosure of reported derivative trade data.
12. The Bill also contains consequential amendments to the *Australian Prudential Regulation Authority Act 1998*, the *Australian Securities and Investments Commission Act 2001*, the *Mutual Assistance in Business Regulation Act 1992*, and the *Reserve Bank Act 1959*. These amendments relate largely to information sharing between, and the protection of the confidentiality of information held by, regulators.

Timing of legislation

13. In order to ensure that Australia implements its G-20 commitments on a timeframe consistent with their adoptions by other G-20 countries, the legislation would be required to pass in the Spring 2012 sittings, with licensing and rule making commencing immediately thereafter.

PART TWO: THE UNDERLYING POLICY FRAMEWORK

14. Derivative contracts are financial instruments that grant rights to some future payment or other consideration that is defined with reference to the value or amount of some underlying asset, rate or index.
15. Derivatives allow banks and other financial and non-financial institutions to mitigate risk and generate tailored exposures to variables, such as interest rates, or events, such as the credit default of a corporation.
16. While derivatives are a valuable tool in managing or hedging against risk, they are also a source of counterparty credit risk. Derivative contracts bind counterparties together for the duration of the contract. Throughout the lifetime of a contract, counterparties build up claims against each other, as the rights and obligations contained in the contract evolve as a function of changing circumstances.
17. The management of derivatives contracts may also be a source of operational risk.
18. Importantly, derivatives may also be a channel for financial contagion between market participants.
19. While many derivatives are traded on exchanges, such as the ASX 24 market, others are negotiated bilaterally 'over-the-counter' (OTC) between the buyer and the seller.

20. OTC derivatives often incorporate bespoke terms to allow the contracting parties to manage specific risks. This is in contrast to exchange traded derivatives that are typically highly standardised. OTC derivatives markets have traditionally been subject to less direct regulation than exchange-based markets.
21. The global OTC derivatives market is of a significant size, as at end-2011 the total notional amount outstanding for OTC derivatives worldwide was \$648 trillion. The Australian market is small by comparison, comprising around 2 per cent of the global market. But as is the case in most countries, Australian-located OTC derivatives market participants participate extensively in overseas markets.
22. The technology supporting financial markets and the nature of derivatives means that a participant located in Australia can very easily transact with a participant located offshore. The ability of locally-based market participants to participate in global markets reduces transaction costs and increases the range of available counterparties and products, in turn enhancing the depth and breadth of the Australian market.
23. However the financial crisis in 2008 highlighted structural deficiencies in the global OTC derivatives market and the systemic risks that those deficiencies can pose for wider financial markets and the real economy.
24. In many countries, these structural deficiencies contributed to the build-up of large, insufficiently risk-managed, counterparty exposures between some market participants in advance of the global financial crisis; and to the lack of transparency about those exposures for market participants and regulators.
25. The deficiencies may also contribute to market inefficiency, uncertainty, loss of confidence and loss of market liquidity, particularly when the market comes under stress.
26. At the G-20 summit in Pittsburgh in 2009, following the global financial crisis, the Australian Government joined other jurisdictions in committing to substantial reforms to practices in OTC derivatives markets.
27. Three of the key G-20 commitments in this area related to:
 - the reporting of OTC derivatives to trade repositories;
 - the clearing of standardised OTC derivatives through central counterparties; and
 - the execution of standardised OTC derivatives on exchanges or trading platforms, where appropriate.
28. These commitments aim to bring transparency to OTC derivative markets and improve risk management practices.
29. The implementation of the G-20 commitments is being coordinated and monitored by the Financial Stability Board (FSB). The FSB membership is made up of the major financial centres around the world and in our region, including: China, Hong Kong, India, Indonesia, Japan, the Republic of Korea and Singapore.

30. The FSB recently called on all jurisdictions to put legislation and regulations in place promptly, and in a form flexible enough to ensure that reforms are implemented consistently.
31. In the FSB's third progress report on OTC derivatives implementation, it noted that full and consistent implementation by all FSB members is important to reduce systemic risk and the risk of regulatory arbitrage that could arise if there are significant gaps in implementation.
32. The Bill provides a legislative framework, based on analysis and consultation conducted by Australia's financial regulators, to allow for industry-led solutions, driven by appropriate regulatory incentives, to be the primary method of increasing the use of centralised infrastructure for derivatives transactions.
33. The Bill also establishes laws that allow for mandated outcomes, where required to ensure the adoption of industry practices within a timeframe that is acceptable to the Australian Government and financial regulators, and is consistent with the international implementation of the G-20 OTC derivatives commitments. Decisions to mandate will be based on ongoing assessments by Australia's financial regulators.
34. Implementing these reforms in a globally coordinated way will not only ensure that the risk of regulatory arbitrage is avoided, and that Australia's financial system is protected, but also ensure that Australian businesses can continue to participate in global markets while remaining primarily regulated in Australia.

Application to the financial sector

35. As mentioned above, the legislative framework will allow the Minister for Financial Services to prescribe obligations so Australia can fulfil its G-20 commitments in relation to:
 - Trade reporting obligations;
 - Central clearing of standardised OTC derivatives obligations; and
 - Trade execution of standardised OTC derivatives obligations.
36. This framework gives the Government flexibility in responding to developments overseas and in the Australian OTC derivatives market. This flexibility is important as implementing the commitments in a globally coordinated way will not only ensure that the risk of regulatory arbitrage is avoided, and that Australia's financial system is protected, but also ensure that Australian businesses can continue to participate in global markets while remaining primarily regulated in Australia.
37. If the framework is not put in place this year, Australian entities participating in overseas markets may be forced to comply with conflicting layers of international obligations. The potential for mutual recognition of domestic requirements provides a means of minimising regulatory duplication and resolve conflicting requirements.
38. This is of particular importance in relation to OTC derivative requirements in the United States (US), due to its broad extraterritorial reach. In July 2012, the Commodity Futures Trading Commission (CFTC) issued draft interpretative

guidance and exemptive order setting out how it intends to apply the Dodd-Frank Act 2010 (DFA) to non-US based entities and their derivatives activities. The guidance provides that the CFTC may permit non-US swap dealers (who may be otherwise caught under the extra-territorial reach of Dodd-Frank) to rely on 'substituted compliance', that is, if CFTC is satisfied there is 'comprehensive and comparable regulation' in Australia for each rule, with specific entity-level and transaction-level requirements.

39. Before any obligations are imposed, the legislation requires further consultation with stakeholders to be conducted. In addition, the Minister for Financial Services and Superannuation will consult relevant Government departments, where appropriate, before approving DTRs.
40. Financial market stakeholders have generally supported the legislative framework.

Trade Reporting Obligations

41. Once the legislative framework has been enacted, the agencies will advise the Minister on whether to impose a reporting mandate. Trade reporting may be mandated in relation to a broad range of OTC derivatives contracts. Any mandates may be accompanied by Regulations that specify the reporting mandates do not apply to specified persons or instruments. If such a mandate is issued, ASIC would be expected to develop, in consultation with industry and subject to the Minister's consent, derivatives trading rules (DTRs) to implement the trade reporting commitments.
42. The timing of the introduction of trade reporting will in part depend on the development of a licensing framework for trade repositories, and licensing of trade repositories by ASIC. At this stage, we expect that, if a decision was made to mandate trade reporting, phased commencement of reporting obligations would commence in late 2013.

Central Clearing Obligations

43. APRA, ASIC and the RBA are currently undertaking a market assessment to identify derivative classes for which central clearing might be a priority (Australian dollar denominated interest rates swaps have previously been considered a potential candidate asset class). The agencies are also monitoring the impact of capital incentives and other initiatives to ensure that central clearing becomes standard industry practice in Australia within a timeframe that is acceptable to the Government and regulators, and that is consistent with international implementation of the G-20 commitments.
44. The agencies expects to provide advice by end-2012 on the suitability of specific derivatives classes for central clearing. The Council has earlier advised that capital incentives may be sufficient to ensure that central clearing becomes standard industry practice without the need to mandate central clearing.
45. However, there may be a case to impose mandatory clearing obligations should progress by market participants be inadequate, or should international developments including the need to ensure Australia's regulatory regime is recognised as 'equivalent' or 'comparable' with key overseas regimes, warrant this. At this stage if

a mandate for central clearing was to be imposed, it would most likely be imposed in late 2013 at the earliest.

46. The imposition of a mandatory clearing obligation would need to take into account how this might change the counterparty exposures of market participants. A decision to mandate central clearing would need to have regard to industry developments and regulatory considerations relating to collateral management and the protection of posted collateral.

Trade Execution Obligations

47. The agencies have advised that, to date, it has not been apparent that there is an immediate case for a trading platform mandate to be imposed. This approach has generally been supported in subsequent consultation.
48. However, this advice may change, subject to further analysis of the volume and liquidity characteristics of markets for particular derivative classes and the emergence of suitable trading platforms. Additionally, there may need to be further consideration of reform to Australia's market licensing regime to better accommodate wholesale professional markets that may emerge to facilitate the execution of derivative transactions on trading platforms.

Application to the energy sector

49. The consultation paper on the legislative framework, *Implementation of a framework for Australia's G20 over-the-counter derivatives commitments*, released in April 2012, proposed that a broad range of derivatives be mandated for reporting but for further considerations to be undertaken before mandating any derivatives for central clearing or trading on exchange.
50. While these proposals have been generally supported, energy market participants in particular have raised concerns about the inclusion of electricity derivatives in future reporting obligations. They submitted that:
 - the electricity derivatives market was not a cause of the global financial crisis;
 - the Australian electricity derivatives market is not an international market and therefore not globally systemically important; and
 - the Australian electricity derivatives market is overwhelmingly used for managing risks in the national electricity market (NEM) so any increase in costs of using OTC derivatives through reporting obligations could make the NEM more risky and increase retail electricity prices.

The Government has no plans to make rules relating to the energy sector, however it is important that electricity derivatives be included in the legislative framework

51. The Government has no plans to prescribe derivative classes used particularly by the energy sector or mandate rules in relation to those classes.
52. The Government will further ensure that should any future decision be taken by the Minister for Financial Services in relation to either the making of regulation, the

mandating of a derivative or the consent to an ASIC rule, this will require the written approval of the Minister for Resources and Energy, where that decision relates to the energy sector.

53. Removal of electricity derivatives from the legislation may also undermine Australia's approach to implementing the G-20 reforms, and potentially raise barriers for Australian entities in participating in global financial markets.
 - 53.1. Australian entities participating in overseas markets may be forced to comply with obligations in relation to electricity derivatives by foreign regulations. The legislation will enable rules to be tailored to ensure that Australian entities have the protection of Australian law in fulfilling these requirements, while leaving the rest of the energy sector unaffected.
 - 53.2. There is a strong likelihood that international regulations applying to electricity derivatives will have extraterritorial effect and will require a future domestic legislative response. Removing electricity derivatives from the Bill will add to uncertainty facing the industry because the procedure for dealing with the international laws in the future will not be clear.
 - 53.3. Any pre-emptive exclusion may threaten Australia's ability to demonstrate the equivalency of its regulatory approach to other jurisdictions and therefore inhibit Australian entities to participate in global markets while remaining primarily regulated in Australia.
54. It also should be noted that current or proposed clearing mandates in foreign jurisdictions are generally subject to exceptions for derivatives transactions for 'bona fide' hedging purposes or for hedging commercial risk
55. There are three processes currently underway that will further the understanding of the Australian OTC derivatives energy market.
 - 55.1. The AEMC has been asked to provide advice to the Standing Council on Energy and Resources (SCER) on the resilience of the financial relationships and markets that underpin the operation of the National Electricity Market (NEM). The AEMC expects to consider OTC electricity derivatives markets as part of this assessment in the first half of 2013.
 - 55.1.1. The AEMC released an issues paper on 8 June 2012. While the AEMC states that their initial view is that financial relationships in the NEM are generally robust, there may be risks to system security created through the financial interdependencies between market participants.
 - 55.2. APRA, ASIC and the RBA initiated a targeted survey of derivatives markets participants on 6 July 2012, as part of a market assessment of Australia's derivative markets. This survey is expected to provide for increased understanding of the bilateral risk management practices and exposures of derivatives markets participants. This survey extends to electricity derivative markets.
 - 55.3. On 4 May 2012 ASIC commenced consultation on revised financial requirements for market participants in wholesale electricity markets dealing in

OTC derivatives, to ensure that they make adequate provision for expected expenses and carry sufficient financial resources to mitigate against operational risk that could lead to unexpected losses or expenses.

56. It is expected that each of these market assessments will be completed by the end of the first half of 2013 and together they should provide for a greater understanding of the bilateral risk management practices and exposures in the OTC electricity derivatives markets.
57. Currently commercial trade repositories offering services in respect of Australian electricity derivatives are not operational; however these are being developed in other jurisdictions.
58. ASIC is also currently consulting on financial requirements for electricity market participants and the Government will also take into account any possible interplay between financial resource requirements and potential G-20 mandates.
59. There has been no pre-emption of this assessment process in the terms of the Bill. No particular derivative market has been written out of the regime that will be supported by the proposed amendments.
60. The Bill establishes the legislative underpinnings of what will be an ongoing process. Over time reassessments may occur in response to changing regulatory or market environment. The appropriateness of any regulatory approach that has been adopted may be reassessed and adjusted accordingly. The Bill seeks to set up a regime that does not merely reflect industry practice or regulatory arrangements at one point in time.
61. Although the electricity derivative market, based on information currently available, is currently traded largely between electricity generation, transmission and retailing entities, this may change in the future. For instance, in some other jurisdictions (such as the United States or Europe) financial institutions play a role in intermediating or holding electricity derivatives positions. It will therefore be important to have the capacity to better understand and respond to any changes in the market for electricity derivatives.
62. Applying the legislative framework to all derivatives (including electricity derivatives) ensures that the on-going market assessment being conducted by the financial regulators is on clear legislative footing.
63. The framework would also provide a legislative basis for mandatory information gathering if voluntary surveys are unsuccessful. The voluntary survey currently being conducted by APRA, ASIC and the RBA requested response by 31 August. However, as at 24 September, the information sought from some participants had not been received, including that of a major energy market participant. At this stage there is some cause for concern that the voluntary survey may not be sufficient to develop the analysis necessary to make recommendations on the imposition of future mandates in the energy sector or to demonstrate the accuracy of assertions made about the electricity derivatives market by the Energy sector, in particular that it does not create systemic risk and is primarily in use to hedge underlying positions.

PART THREE: THE CONSULTATION PROCESS

64. In response to the turbulence in financial markets, the international regulatory community has paid increasing attention to developments in the OTC derivative space. In April 2008, the Financial Stability Forum (now the FSB) recommended that regulators take action to ensure a sound legal and operational infrastructure for the OTC derivatives market.
65. At the G-20 summit in Pittsburgh in 2009, the Australian Government joined other jurisdictions in committing to reforms to practices in the OTC derivatives market. Following the commitment, the Council consulted extensively on central clearing of OTC derivatives.

Consultation and analysis conducted by the Council prior to 2011

66. In May 2009 APRA, ASIC, and the RBA conducted a survey of the OTC derivatives market in Australia. The report identified areas in which operational and risk-management practices could be enhanced.
67. Twenty-eight firms including key participants in the Australian OTC derivatives market responded to the survey providing information in three areas: institutional details; risk management and infrastructure; and products and counterparties. The written survey responses were followed up with face-to-face meetings with a number of respondents.
68. The survey was undertaken with close engagement with AFMA, who were involved in the survey design, and participated in numerous post-report discussions.
69. The survey data provided a useful insight into the scope of market activity and key legal and operational practices, and allowed a number of conclusions to be drawn. An industry workshop was also convened, in which the regulators discussed the findings of the report and discussed next steps with key stakeholders. Representatives of the regulatory agencies also discussed the issues coming out of this report at a number of industry forums over 2009 and 2010.

The 2011 Council consultation on central clearing of OTC derivatives

70. In June 2011 the Council issued a discussion paper that sought to better understand how greater use of central counterparties (CCPs) might be promoted in the Australian OTC derivatives market. The paper set out some of the advantages and disadvantages of central clearing.
71. The Council received 25 submissions to the discussion paper from a range of domestic and foreign banking institutions, clearing houses and other market facilities, industry groups, and legal firms.
72. Council agencies also conducted round-table and bilateral discussions with 50 stakeholders as part of the consultation process for the discussion paper, with in-person meetings in Brisbane, Melbourne and Sydney. Representatives of agencies also engaged with stakeholders through participation in industry meetings and conferences.

Consultation on the Government's proposed legislative framework

73. Following the Council's 2011 consultation, the Council provided a report to the Government on 20 March 2012, setting out advice and recommendations on implementing reforms in the Australian market.
74. On 18 April 2012, the Government announced it will be developing a legislative framework to ensure the implementation of the G-20 commitments. On the same date the Government released a consultation paper seeking stakeholder views on the detailed design of a framework to implement Australia's G-20 commitments in relation OTC derivatives. Consultations on the paper concluded on 15 June 2012.
75. A wide ranging consultation process was conducted on the proposed framework for the implementation of Australia's G-20 OTC derivative commitment. The Council agencies conducted 53 stakeholder meetings, either face-to face or via teleconference, with stakeholders. The Government received 37 submissions to the consultation paper, including 7 confidential submissions (see appendix).
76. Stakeholders were generally supportive (with the notable exception of electricity market organisations) of the proposed legislative framework for the implementation of the G-20 OTC derivatives reforms. A wide range of stakeholders understood the need and supported the flexible approach taken by the Government in implementing the reforms.

Consultation on the draft legislation

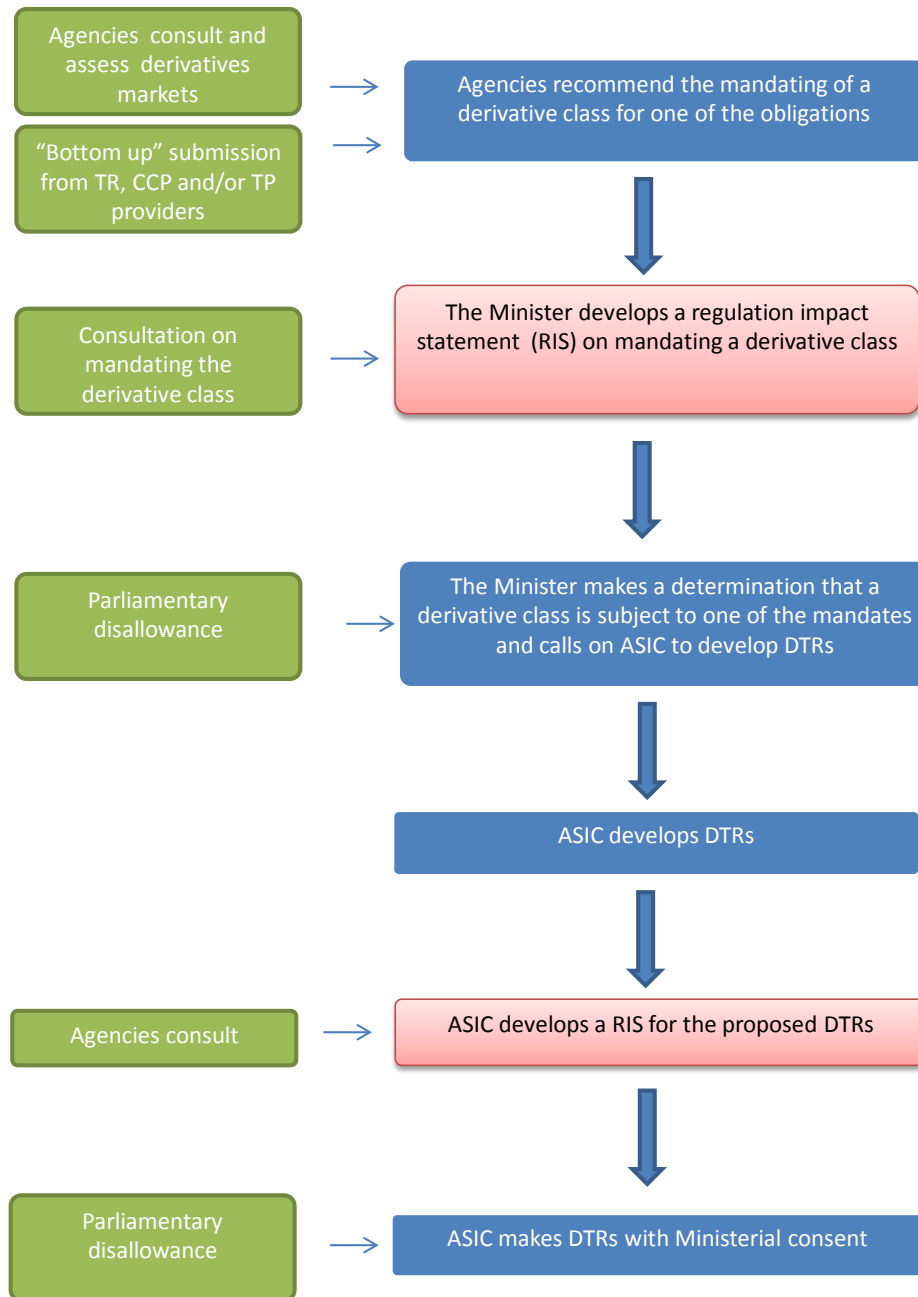
77. An exposure draft of legislation designed to implement the legislative framework was released for public consultation on 25 July. The Government received 17 submissions, including 1 confidential submission.
78. Additional meetings with interested stakeholders were conducted during the exposure period to discuss the legislation.
79. Financial market stakeholders generally supported the Bill.

CURRENT AND FUTURE CONSULTATION PROCESSES

Introduction

80. During the consultation on the proposed framework in 2012 a proposal for on-going consultation was provided for public comment. Figure 2 in that consultation illustrated future steps for consultation and market assessment.

Fig 1: Ongoing future consultation and market assessment



Checks and balances, and proper process

81. The flow chart set out above demonstrates the extensive processes that are contemplated to ensure that proper consideration is given to the circumstances of each derivative market and the views of stakeholders.
82. It should also be noted that the Bill:
 - 82.1. mandates the consideration of certain issues by decision makers at both the product prescription and rule making stage;
 - 82.2. mandates regulatory impact analysis at both the product prescription and rule making stage (precluding the possibility of non-compliance with government regulatory impact policies or the obtaining of a RIS exemption under that policy);
 - 82.3. mandates consultation at the rule making stage (including public consultation);
 - 82.3.1. The regulations may mandate consultation with specified bodies.
 - 82.4. mandates consultation at the product prescription stage;
 - 82.4.1. Public consultation is not mandated by the Bill given that public consultation on possible prescription of a product class will occur as part of market assessments. All rule making and product prescription will in any event be subject to consultation requirements as imposed under Part 3 of the *Legislative Instruments Act 2003*. This should ensure that public consultation on product prescriptions would need to occur if this had not occurred as part of a market assessment.
83. Product prescriptions and rules are legislative instruments, which are subject to review and potential disallowance by Parliament.
84. Rules may only be made by ASIC with the consent of the Minister (or in the case of emergency rules, are subject to disallowance by the Minister).
85. The proposed framework will work within the ordinary policy development and approval process of Government. Any product prescription will need to obtain policy approval before being made and therefore be subject to the processes of Government directed at ensuring proper analysis and decision making on policy proposals. Under this process, non-Treasury Ministers and agencies decisions would be required to be consulted in relation to proposals that impact upon their portfolio responsibilities. Where appropriate, the agreement of Ministers whose portfolio responsibilities are impacted would need to be obtained.
86. In relation to the energy sector, as was outlined above, the Government will ensure that regulations created under the proposed legislative framework provide electricity regulators and bodies with a formal consultative role in the mandating of any possible requirements, where appropriate.
87. The Government will also ensure that any decision taken by the Minister for Financial Services in relation to either the making of regulation, the mandating of a

derivative or consent to an ASIC rule will also involve the Minister for Resources and Energy, where that decision relates to the energy sector.

88. It is contemplated that ASIC may be required by regulation, made under the new section 900J, to consult with energy regulators and relevant bodies prior to making any derivative transaction rule.

Current consultation and market analysis

89. Council agencies are continuing to monitor derivatives markets and will provide ongoing reports to the Government with recommendations for the inclusion or extension of any of the obligations to additional derivatives classes.
90. Recommendations for mandating derivative classes will be provided in conjunction with a report on derivatives markets. These reports will examine derivatives market practices for each derivative class and could consider the following factors:
- The extent to which mandating could address systemic risk posed by that derivative class.
 - The competitiveness or reasonable terms of access to trade repositories, CCPs or trading platforms for that derivative class.
 - Availability of access to trade repositories, CCPs and trading platforms for Australian entities and investors, either as direct members or as indirect clients for that derivative class.
 - The impact of mandating and not mandating on competition among participants in the markets for that derivative class.
 - The extent of voluntary take-up of trade repositories, CCPs and/or trading platforms in a derivative class.
 - The extent of development of improved bilateral risk management practices in that derivative class, such as collateralisation, default handling procedures and improved back-office functions.
 - Relevant international regulatory and market developments.
 - Potential costs of compliance.
91. Assessments may consider whether a facility has indicated that it is willing to provide particular reporting, clearing or trading services. In that case, the assessment process could operate along the lines of the 'bottom up' approach being established in the US and EU. Alternatively, agencies may seek indications of interest from operators of relevant facilities to offer a service, as in the 'top down' approach of these jurisdictions
92. The key objectives of this report are to:

- document and analyse the current state and trends in OTC derivatives markets;
 - summarise material changes in the OTC derivatives regulatory environment;
 - identify risks and concerns in OTC derivatives markets;
 - lay the groundwork for possible future regulatory action and recommended; and mandates, if/where necessary; and
 - serve as a tool for ongoing industry engagement.
93. A core part of the assessment report will be a quantitative and qualitative discussion of the state-of-play in the Australian OTC derivatives market. To that end, APRA, ASIC and the RBA have undertaken a voluntary survey of around 60 market participants, covering large domestic and international banking groups, smaller ADIs, funds managers, government borrowing agencies, corporate treasuries and electricity companies. The survey has asked a wide range of questions around risk management practices, many of which are similar to those asked in the 2008–09 survey, so it is expected that some useful discussion of progress in risk management practices will be possible.
94. The Council intends to use the data to better understand market liquidity, since this will be an important factor in any future consideration of mandatory requirements around clearing and trade execution. This data might also be useful in calibrating any thresholds for exemptions from mandatory obligations.
95. Developments in financial market infrastructure will also be reviewed, again to provide an input into thinking about any future mandatory obligations. The report will review existing and prospective infrastructure availability for Australian market participants, as well as discussing any challenges (such as operational issues) and likely costs.
96. The voluntary survey closed on 31 August and the regulatory agencies have been able to obtain data to establish an understanding of all markets except the electricity derivatives sector. As of 24 September the agencies were waiting on contributions from a number of energy market participants, including one major participant, so the ability to assess the electricity derivatives market through the voluntary survey is not certain.

APPENDIX

Respondents to the May 2009 APRA-ASIC-RBA OTC derivatives market survey

The following 54 organisations were invited to participate, of which 28 submitted survey responses.

ABN Amro Bank NV	Airservices Australia
Alcoa of Australia Ltd	AMP Capital Investors Ltd
Arcadia Energy Trading	Australia and New Zealand Banking Group Limited
Australian Super Pty Ltd	AWB Ltd
Bank of America NA	Bank of Tokyo - Mitsubishi UFJ Ltd
Bendigo and Adelaide Bank Ltd	BNP Paribas Australasia
Brisbane City Council	BT Funds Management Ltd
CBH Group Ltd	Citibank N.A. Sydney
CMC Markets Asia Pacific Pty Ltd	Colonial First State Global Asset Management
Commonwealth Bank of Australia	Credit Suisse Sydney Branch
Deutsche Bank Aktiengesellschaft (Sydney Branch)	Goldman Sachs JBWere Pty Ltd
Host-Plus Pty Ltd	HSBC Bank Australia Limited
IG Markets Ltd	Industry Funds Management Pty Ltd
Investec Bank (Australia) Limited	JP Morgan Chase Bank National Association
Kaiser Trading Group Pty Limited	Lion Nathan Ltd
Macquarie Bank Limited	Macquarie Investment Management Ltd
MF Global Australia Limited	MLC
Morgan Stanley Australia Securities Limited	National Australia Bank
NSW Treasury Corporation	QIC Limited
QIC Properties Pty Ltd	Royal Bank of Canada
Santos Ltd	Société Générale Australia Branch
Standard Chartered Bank	State Street Bank and Trust Company
Sumitomo Australia	Suncorp-Metway Ltd
The Toronto Dominion Bank	Tower Australia Group Ltd
Treasury Corporation of Victoria	UBS AG, Australia Branch
Wesfarmers Ltd	Westpac Banking Corporation
Worley Parsons Ltd	xStrata Holdings Pty Limited

Public Submissions to the 2011 Council consultation on central clearing of OTC derivatives

ANZ Global Markets, Institutional Division; Commonwealth Bank of Australia Markets; Macquarie Bank Limited; Westpac Institutional Bank Financial Markets	ASX Clearing Corporation
Barclays Capital	CLS Bank International
Mr Satyajit Das	d-cyphaTrade
Deutsche Bank AG Australia and New Zealand	Global Foreign Exchange Division
International Swaps and Derivatives Association, Inc.	J.P.Morgan
LCH.Clearnet Group Limited	Mallesons Stephen Jaques
National Australia Bank, Wholesale Banking	Reval.com, Inc.
Mr Manmohan Singh - International Monetary Fund	RBC Capital Markets
Vanguard Investments Australia Ltd	Australian Bankers' Association Inc.
Australian Bureau of Statistics	Australian Financial Markets Association
Colonial First State Global Asset Management	Finance and Treasury Association

**Public submissions to the Government 2012 consultation paper -
*Implementation of a framework for Australia's G-20 OTC derivatives
commitments***

ASX Group	Australian Bankers Association
Australian Energy Regulator	Australian Financial Markets Association
CME Group	Colonial First State Global Asset Management
The Depository Trust and Clearing Corporation	Deutsche Bank
Energy Supply Association of Australia	Finance and Treasury Association
Financial Services Council	Global Financial Markets Association
HSBC	IG Markets
International Power-GDF Suez Australia	International Swaps and Derivatives Association
King and Wood Mallesons	LCH.Clearnet
Major Australian Banks	Markit
MarkitSERV	National Generators Forum
Norton Rose	Private Electricity Generators
Rate Validation Services	State Street Global Markets
TriOptima	TRUenergy
Vanguard	Yieldbroker

Public submissions on the exposure draft - *Corporations Legislation Amendment (Derivative Transactions) Bill*

AGL	Alinta Energy
ASX	Australian Bankers Association
Australian Financial Markets Association	The Depository Trust & Clearing Corporation
Energy Supply Association of Australia	Finance and Treasury Association
Henry Davis York	Industry Super Network
International Power-GDF Suez Australia	International Swaps and Derivatives Association
King and Wood Mallesons	National Generators Forum
Norton Rose	Origin Energy