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Mr Tony Richards
Head of Payments Policy Department
Reserve Bank of Australia
GPO Box 3947
Sydney NSW 2001

By email: pysubmissions@rba.gov.au

Dear Mr Richards

Consultation Paper – New Financial Stability Standards

The Australian Bankers' Association welcomes the opportunity to provide comments to the Reserve Bank of Australia (Bank) on the proposed new *Financial Stability Standards* (FSSs) for central counterparties (CCPs) and securities settlement facilities (SSFs).

We note the new FSSs will:

1. Align the Australian regime for clearing and settlement (CS) facilities with new international standards, namely, the Principles for Financial Market Infrastructures (FMIs) (the Principles), developed by the Committee on Payment and Settlement Systems (CPSS) and the Technical Committee of the International Organisation of Securities Commissions (IOSCO);
2. Uphold the standards to which licensed CS facilities are held under the current FSSs; and
3. Implement key elements of the Council of Financial Regulators' (Council) framework for ensuring that Australian regulators have appropriate influence over cross-border CS facilities.

Our submission sets out comments associated with these key aspects of the proposed FSSs.

1. Alignment with the Principles relevant to financial stability

The ABA understands the need for FMIs to be subject to regulatory safeguards to protect and promote the stability of Australia's financial stability. The ABA supports the efforts of the Bank to ensure that the regulatory framework in Australia is consistent with international efforts on regulatory harmonisation. We therefore welcome the Bank's proposal to fully adopt the Principles where those Principles are relevant to financial stability in the new FSSs. We also support the proposal to adapt the Principles to the Australian context where appropriate.

1.1. Risk controls

We note the proposal to require for CCPs to collect margin from participants must be met for all products cleared by a CCP¹, including cash equities². This is a notable change from current practices for clearing of cash equities, and may therefore result in higher transaction costs.

1.2. Default arrangements

The consultation paper notes that existing insolvency provisions may inhibit timely portability of customer positions in event of participant's default. As an alternative to legislative change, the CP notes a CCP could adopt an agency model for customers of its clearing participants, whereby the customers would form a contractual arrangement directly with the CCP and the clearing participants would act as agents for their customers in posting collateral (in contrast to principal-to-principal model currently used by the ASX i.e. no direct contractual relationship between an indirect participant and a CCP).

While portability is important, it is necessary to take into account broader considerations. For example, a direct model may be required in order to achieve derivatives clearing organisation (DCO) status from US regulators. It is likely that capital charges to clearing brokers will vary between the two models and the direct model may involve less capital charge and therefore lower clearing fees. While portability is desirable it is unlikely Clearing Brokers will commit to accepting future porting as they will seek to analyse the risk when the porting event actually arises. We therefore support AFMA's recommendation that this issue be sorted bilaterally between participants.

1.3. Participation and access

The ABA supports proposed CCP Standard 17 and SSF Standard 15, consistent with the Principle on tiered participation, noting that restrictions on access can result in highly tiered clearing arrangements and potentially give rise to concentration risks.

1.4. Additional requirements

Question 3 - Are there any potential obstacles to CCPs taking proposed steps to monitor the credit standing of participants and impose additional risk controls where a participant's credit standing is called into question?

The ABA notes that it may be difficult for CCPs to monitor participants other than they currently do via performance of obligations and to monitor participants on an ongoing basis.

Question 4 - In balancing the system wide impact of restricting collateral eligibility to High Quality Liquid Assets (HQLA) against the risk that lower quality or less liquid assets may not hold their value in a stressed market should any other collateral eligibility be considered?

The FSSs could encourage CCPs to accept a broader set of collateral assets than HQLA ('prefer collateral with low credit, liquidity and market risks'). However, there are practical limitations to the pool of liquid assets being broadened. For example, if the pool is widened much beyond Level 1 assets the potential for the collateral to fall short of being liquid at the time required is higher.

The primary purpose of CCPs is to manage counterparty risk. The ABA, therefore, questions whether there are unacceptable functional risks being taken on if a CCP is expected to manage risks more broadly, including credit and liquidity risk.

¹ Proposed CCP Standard 6

² Reserve Bank of Australia, *Consultation on New Financial Stability Standards*, August 2012, pg 12.

³ Proposed CCP Standard 4.3

⁴ Proposed CCP and SSF Standard 5

Question 6 - Should an SSF always be required to offer intraday or real-time settlement finality, or are there circumstances in which a minimum standard of end-of-day settlement finality would be acceptable⁵.

The ABA recommends a SSF should be required to offer real-time settlement finality in order to minimise the risk of settlement failing. The need to confirm execution as soon as technologically possible would ensure there was negligible idiosyncratic risk to CCP users.

Question 7 - Should settlement arrangements be allowed to settle using DvP model 2 where trade values are small and operational, or should all facilities be required to settle according to DvP model 1 or 3⁶?


The ABA suggests that while the standards should be defined, CS facilities and participants should bilaterally negotiate which settlement arrangements are to apply.

2. Influence over Cross-border Clearing and Settlement facilities

We note the Council recommended the imposition of graduated 'location requirements'⁷ to implement the policy objectives on cross-border provision of CS services, for example, to ensure continuity in the provision of services in times of stress. The graduated framework articulated by the Council recommended that the specific measures applied to a facility would reflect the nature and scope of its activities, and, in particular, its systemic importance in Australia and the strength of the domestic connection.

The ABA supports the use of the FSSs as the principal mechanism to implement the framework's stability relevant measures, including financial, governance, operational, regulatory and legal measures. We also support that the application of the requirements in a graduated and proportionate way to ensure that the regulatory approach is tailored to the specific circumstances of individual FMIs and the markets and participants they serve.

Yours sincerely,



Jade Clarke

⁵ SSF Standard 7

⁶ CCP Standard 11 and SSF Standard 10

⁷ Council of Financial Regulators, *Ensuring Appropriate Influence for Australian regulators over cross-border clearing and settlement facilities*, October 2012 .