Via e-mail:
financialmarkets@treasury.gov.au

Re: Implementation of a framework for Australia's G20 over-the-counter derivatives commitments - Consultation Paper, April 2012

Dear Sirs,

TriOptima AB ("**TriOptima**") is pleased to submit the following comments in connection with the Australian Treasury's (the "**Treasury**") consultation paper on the options for the implementation of a legislative framework for OTC derivatives regulation (the "**Consultation Paper**"). As discussed below in further detail, TriOptima is a provider of post-trade services to major market participants within the OTC derivatives markets.

Any defined terms used herein have the meaning prescribed to them in the Consultation Paper, unless otherwise specified herein.

TriOptima

TriOptima offers post-trade services on the OTC markets, primarily in relation to OTC derivatives. TriOptima has its headquarters in Stockholm and also conducts its business through its four subsidiaries in New York, London, Singapore and Tokyo, respectively. The company's client base is made up of major broker/dealer banks and other financial institutions globally.

TriOptima currently offers three post-trade services for the OTC markets:

- triReduce: a service for early termination of OTC derivatives, so called portfolio compression;

- triResolve: a service revolving around the reconciliation of counterparty positions in OTC derivatives; and

- triBalance: a service mitigating portfolio risk imbalances across bilateral and cleared OTC derivative exposures (as further detailed below).

TriOptima responses to the Consultation Paper

As background, TriOptima supports the stated policy aims of the G20 nations from their meeting in Pittsburgh in 2009, as referred to in the Consultation Paper, in terms of reduced counterparty risks, improved general market transparency and protection against market abuse, and improved abilities for regulators to assess, limit and manage systemic risks in the OTC markets.

TriOptima finds that the Treasury has taken a pragmatic approach in the legislative framework proposed in the Consultation Paper, and TriOptima has opted only to respond to the specific Consultation Paper question 18.1, and has not taken any view on the remaining questions.

We agree with the Treasury's observation in the Consultation Paper that it may not be appropriate for a clearing obligation to apply to all types of transactions. As we will show in the following, it would for example be inappropriate to apply a

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clearing obligation to the component transactions of a “compound transaction” (as defined below) entered into as part of participation in post-trade risk reduction services.

The objective of the G20 commitments is to mitigate systemic risk, and the actions supported by the G20 (including mandatory clearing) are means toward that end. While many OTC derivatives will be suitable for central clearing, some OTC derivatives will remain bilateral and not be cleared, and the combination of cleared and uncleared components in a portfolio may create risk imbalances within such portfolios. The portfolio imbalance can however be effectively rebalanced by lowering portfolio risk/DV01 characteristics of the portfolio and, thus, systemic risks, by appropriate injections of new bilateral non-cleared trades. Injections of off-setting trades which are not cleared can help to rebalance and stabilize the portfolio by eliminating risk sensitivities in the portfolio. In a multilateral context, these trades can be identified, while the overall compound transaction is market risk neutral for each of the participants.

TriOptima offers this type of post-trade risk reduction service under the name triBalance. The compound transaction package of trades suggested in a triBalance cycle is market risk and funding risk neutral as a whole for each participant. In order to be effective, however, the new risk off-setting trades must enter into the netting sets from where the risk they are off-setting arose. In order to off-set bilateral risks these new trades must thus remain bilateral and non-cleared themselves.

As mandatory clearing requirements are primarily aimed at reducing systemic risk, it is important that they are not applied in a way which effectively limits the opportunity for market participants to reduce such risk through the use of compound transaction post-trade risk reduction services. If portfolio risk reducing/off-setting trades are to fulfil their purpose, it is essential that they are not made subject to mandatory clearing requirements.

We would therefore encourage the Treasury to make clear that any class of OTC derivatives (as prescribed by the Minister) that will be subject to mandatory clearing requirements through a DTR should not include those OTC derivatives (i) the sole purpose of which is to reduce systemic risk and portfolio risk between more than two counterparties and (ii) which do not change the overall market risk for the counterparties. Such compound transaction derivatives should accordingly be outside the potential reach of the rule-making power.

Compound transactions

For your reference, we set out below an explanation of the concept of "compound transactions". This is the type of multiparty transaction that is the result of the type of risk reducing service described above, and other similar post-trade risk reduction services; and it is the "component transactions" which collectively make-up such compound transactions which accordingly should not be subject to mandatory clearing requirements.

The differences between compound transaction services and traditional trading are:

- A compound transaction is market risk neutral for each of the compound transaction participants:

- o Participants are indifferent to the price at which the components in the compound transaction are concluded;
- o Participants do not submit bids and offers to enter into a specific position, but rather indicate tolerances (e.g., maximum change in counterparty credit exposure) which the compound transaction must satisfy; and
- o The compound transaction and its components are not price-forming events. Normally, the compound transaction is effected several hours after the marks-to-market or the pricing curves are determined and, consequently, a compound transaction is calculated on basis of old and irrelevant market data.

- A compound transaction is designed to reduce second order risks emerging from existing OTC derivatives, such as counterparty credit risk, operational risk and/or basis risk.

- A compound transaction is multilateral and not bilateral (i.e. there are more than two parties to the transaction).

- All participants in the compound transaction must accept the transaction in full or it will not be executed. Unlike traditional trading activities, it is an "all or nothing" proposal, arranged by the post-trade risk reduction service provider (e.g., TriOptima), where several thousands of individual transactions are components of the overall compound transaction and the individual transactions are irrelevant in their own right and cannot be executed separately to achieve the desired risk reduction effect. If one party fails to accept, the entire proposal is declared null and void and no changes to the participants' portfolios take place.

- Periodicity of arranging a compound transaction is not continuous, but rather cycle-based and a cycle extends over more than a trading day.

- The service provider is not party to the compound transaction; nor is it involved in settlement of the compound transaction.

We are happy to provide further information on the above, if and as required.

Yours faithfully,

TriOptima AB

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