

Head of Secretariat
Financial System Inquiry
The Treasury
Langton Crescent
PARKES ACT 2600

August 26 2014

Dear sirs,

FINANCIAL SYSTEM INQUIRY – FINAL SUBMISSION

This letter provides the final submission of LCH.Clearnet Ltd (“LCH.Clearnet”) to the Government’s Financial System Inquiry.

LCH.Clearnet is a subsidiary of the LCH.Clearnet Group, the world’s leading clearing house group, which services major international exchanges and platforms, as well as a range of OTC markets. It clears a broad range of asset classes including cash equities, exchange traded derivatives, commodities, energy, freight, interest rate swaps, credit default swaps, bonds, repos, and foreign exchange derivatives. The Group’s central clearing counterparties (“CCPs”) have over 190 clearing members and over 600 clients across 22 countries.

LCH.Clearnet is the only non-Australian CCP to have been granted an Australian Clearing and Settlement Facility Licence and is currently providing clearing services for over-the-counter (“OTC”) interest rate swaps (“IRS”) to a number of major Authorised Deposit-taking Institutions through its SwapClear service. LCH.Clearnet is also licenced in Australia to clear for the FEX commodities and energy exchange. LCH.Clearnet is supervised directly by both ASIC and the RBA. In addition to its Australian licence, LCH.Clearnet Ltd is regulated in the EU, US, Singapore, Quebec and Ontario. LCH.Clearnet SA is regulated in the EU and the US. LCH.Clearnet LLC is regulated in the US, and has applied for recognition in the EU.

Access to CCPs such as LCH.Clearnet is important and integral to the implementation of Australia's G20 commitments, and LCH.Clearnet is delighted to be given the opportunity to provide its submissions to assist the Inquiry in its deliberations.

Your review could not come at a better time to help inform not only the long-term future of Australian financial markets, but also the nearer-term implementation of G20 market reforms in Australia. LCH.Clearnet provided exchange clearing services in Australia

for a number of years (as ICCH) prior to its recent re-entry, and is the only foreign organisation to have been granted a licence to provide clearing services directly to the Australian market. LCH's SwapClear OTC clearing service has been highly instrumental in enabling Australia to fulfil its G20 commitments to CCP clearing of OTC products. We are committed to making further investments in Australia and expect to use our presence in Australia to serve our growing activities in the Asia-Pacific region.

The objectives of the Inquiry resonate strongly with LCH.Clearnet, especially that *“Recommendations will be made that foster an efficient, competitive and flexible financial system, consistent with financial stability, prudence, public confidence and capacity to meet the needs of users.”* A pro-competitive stance in financial infrastructure regulation could make to a significant positive contribution to these objectives, and to the Australian financial system overall.

As the world's largest open, horizontal CCP, LCH.Clearnet can bring unique expertise, experience and connectivity to Australia's financial markets. Recent adoption of the LCH.Clearnet SwapClear platform is evidence of the confidence Australian banks and their clients have in the system. Membership enables them to gain direct access to global liquidity pools in all major currencies, realise optimal netting efficiencies and enjoy value-added services such as trade compression. Where we have provided clearing services elsewhere, these have been followed by lower charges, faster innovation and enhanced capacity. Some of these benefits have recently been evidenced in Australia itself as a result of competitive pressure in clearing. Our comments relate therefore to the topic of Competition in financial market infrastructure discussed on pp 2-35 and 2-36 of the Interim Report.

The advantages of competition in the clearing sector should never result in a reduction in risk management standards. It is a fundamental belief at LCH.Clearnet that CCPs should never differentiate themselves by compromising on risk management standards as this could lead to potentially catastrophic consequences in the event of a significant default. LCH.Clearnet operates its clearing services at a prudent level of risk, calibrated to exceed any regulatory minimum and international market standards such as CPSS-IOSCO's PFMI (Principles for Financial Market Infrastructures).

We believe that the requirement that a CCP must be an Australian incorporated entity if it provides services which are considered to be “systemically important” with a “strong domestic connection” in Australia runs contrary to the Financial Systems Inquiry's objective of *‘balancing competition, innovation, efficiency, stability and consumer protection’*. Enabling LCH.Clearnet to clear directly for additional markets in Australia subject to the supervision of Australian regulators could benefit the market by increasing financial stability, bringing innovation and lowering fees for Australian firms. This has already been enabled for OTC IRS through the approval of LCH.Clearnet's SwapClear service in accordance with the CFR's policy. However, maintaining a requirement for CCPs to domestically incorporate for other activities would deny them further such benefits.

LCH.Clearnet has demonstrated a strong commitment and willingness to adhere to the high standards of Australia's clearing regulatory regime without being domestically incorporated. Through the license we hold in relation to the FEX and SwapClear services, we are subject to the RBA's Financial Stability Standards in addition to ASIC's requirements. We have also demonstrated our commitment to Australia in practical ways by setting up a local office, increasing our staff presence and establishing a local OTC User Group.

We would like to propose to the Financial Systems Inquiry that the right balance between stability and competition can be achieved by allowing a strong, locally-regulated though foreign-incorporated CCP to offer clearing services more broadly in Australia. That is contingent on the Australian regulators being satisfied with the home oversight and risk management regimes, as has already been proven and implemented in OTC derivative markets, and the agreement of cross-border resolution arrangements. We would welcome the opportunity to discuss this further, if it was helpful to the Inquiry.

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We hope that the Inquiry finds this submission useful and we look forward to engaging further as policies are developed. Please do not hesitate to contact me at rory.cunningham@lchclearnet.com regarding any questions raised by this letter or to discuss these comments in greater detail.

Yours faithfully



Rory Cunningham
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