



20 March 2008

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Dear Caroline

**Re: Draft Emissions Units, Settlement Systems and Futures Bill**

Thank you for the opportunity to make a submission on the above mentioned Bill. The New Zealand Financial Markets Association is a not for profit Incorporated Society and provides a range of member services to Banks and other organisations primarily active in the 'over-the-counter' Financial Markets operating within New Zealand.

The submission provided in this document is a collation of views, comments and opinions derived from our members who represent the Financial Markets activities within those organisations. Our comments relating to this Draft Bill are provided from a market perspective only.

The NZFMA is supportive in concept to the proposed regulatory reform. We do however have a number of concerns regarding the scope, implications and unintended consequences. Although we have not responded to all your specific questions, we have commented on those where we feel we have an informed perspective to give.

Our comments are as follows:

**1. Clarification of a Futures Contract**

Specifically, current uncertainty with regard to definitions of a 'futures contract' continues to detract from the obligation of some organisations to meet licensing requirements that serve to raise the professional standards of participants in the financial markets. The NZFMA is of the view that this Draft Bill, while clearly capturing emission units as futures contracts, does little to provide clarification on other financial instruments. Specifically Margin Foreign Exchange, Contracts for Difference, Options and Forward Foreign Exchange represent very large transaction volumes in the financial markets and yet still need clarification as to whether they are considered a futures contract. The NZFMA would welcome clarification of this issue within this Bill.

**2. OTC Market Implications**

Whilst this Draft Bill is focused on the Exchange Traded Market, the development of a complementary 'over the counter' (OTC) emissions market is important for its sustainability. Under Part 3 Section 37 (2) of the Securities Market Act 1988, currency and interest rate swaps and forwards to which a registered bank is a party are excluded from the definition of a futures contract. The NZFMA would be concerned if the Draft Bill inadvertently affected the ability of a registered bank to establish an associated OTC market by having to comply with a whole new set of regulatory requirements.



### 3. Authority of an Exchange to Licence Futures Dealers

The NZFMA is concerned that the intention of the Draft Bill is to provide a registered exchange with the ability to authorise futures dealers. We believe that change may prove a barrier for other entities looking to operate in or establish exchange traded markets in New Zealand. The existing exchange would have blanket power to authorise futures dealers including those that choose not to be an Exchange-regulated Futures & Options participant. The NZFMA would prefer that the Securities Commission retain their ability to authorise Futures Dealers with clearly defined financial resource requirements similar to those considered global best practise.

### 4. Priority over Collateral

The intention in the Draft Bill to provide certainty of a designated clearing house's ability to realise capital via an amendment to the PPSA has a range of implications for our members. Banks may be impacted through their negative pledge clauses leading to possible breaches of a banks covenant. Although the consultation document states these implications can be avoided, it is not clear to the NZFMA as to how. Further, the NZFMA would want certainty that the Draft Bill did not impact on other collateral arrangements. For example, that posted with the Debt Management Office to meet the terms of their ISDA.

### 5. Certainty of Title

Clause 33 of the Draft Bill details certainty of title. The NZFMA wishes to point out that this approach may preclude the establishment of a Repurchase Agreement (Repo) market which is potentially a natural extension of the emissions market.

### 6. Questions

The NZFMA has a number of questions relating to the Draft Bill it wishes to table:

- With regard to priority over collateral, what would happen if the margin call exceeded the collateral posted. Is it the intention of the Draft Bill to provide the clearing house with additional powers to seek a margin call beyond that covered by the collateral posted?
- The NZFMA would be interested in how Australia addresses the issue of priority over collateral.
- The NZFMA seeks clarity over what defines an Investment Security referred to in 7.7 of the discussion document. Does it extend to P Notes or is it restricted to sovereign securities and, if so, what type?

Thank you for the opportunity to make this submission and we acknowledge that this submission may be posted on your website. I would be happy to answer any queries you may have relating to these comments.

Yours sincerely

Paul Atmore  
Chief Executive Officer