

19 May, 2014

Regulatory & Public Policy
ASX Ltd
20 Bridge Street
SYDNEY NSW 2000

By email: regulatorypolicy@asx.com.au

Attention: Ms Diane Lewis

Dear Ms Lewis

ETO Expiry Date - Automatic Exercise and other Proposals

I refer to the ASX Consultation Paper entitled *ASX Exchange Traded Options: Consultation on Automatic Exercise on Expiry Date and Approach for Exercise Errors*. The Stockbrokers Association of Australia is pleased to provide the following comments on the Questions set out in the Consultation Paper.

Q1

Do you agree that ASX Clear should change its current policy and provide for automatic exercise as the default position for all in-the-money cash settled option contracts on the expiry date? Please set out your reasons.

There was general support for the proposal that in-the-money cash settled options should be exercised automatically. This was regarded as eliminating any risk of failure to set up an account for auto exercise as a default, or of an inadvertent failure to exercise a particular position. The change will also remove the requirement for a number of manual processes required for exercise and for account set-up.

There was a suggestion that the definition of “in-the-money” for XJO options should factor in the cost of exercise. The calculation of whether the position is in profit should factor in a minimum of 0.05 to cover exercise costs.

Q2

If ASX Clear were to implement the proposal for automatic exercise as the default position for all in-the-money cash settled options contracts, do you support ASX Clear providing the ability for clearing participants to exclude automatic exercise for a specific option position? Please set out your reasons.

Members without exception supported the retention of the ability to exclude automatic exercise for specific positions. Members referred to the specific example of where the economic value of a position was negative due to the cost involved in settlement, including all applicable fees.

Some members at present set up all accounts to default to expiry, and provide for clients to be able to specifically request this default to be overridden. Those members have stated that retaining the ability to override the default was regarded as important.

There was a suggestion from one member that the ability to exclude options exercise should be limited to the nearest in-the-money option only.

Q3

Do you agree that ASX Clear should change its current policy and provide for the automatic exercise as the default position for all in-the-money deliverable option contracts on the expiry date? Please set out your reasons.

There was general support for this proposal for the same reasons as outlined in the answer to Question 1 above. There was a suggestion that the in-the-money position should have a minimum value of at least 0.01 for it to be considered to have a positive economic value.

There was however a different perspective held by some members, that deliverable options should not necessarily be viewed in the same light as cash settled options. They preferred the existing framework where brokers could make the decision to set up accounts for automatic exercise.

Q4

If ASX Clear were to implement the proposal for automatic exercise as the default position for all in-the-money deliverable options contracts, do you support ASX Clear providing the ability for clearing participants to exclude automatic exercise for a specific option position? Please set out your reasons.

There was a general view that the ability to exclude automatic exercise should exist for the same reasons as outlined in the answer to Question 2 above. There may be reasons not to want automatic exercise that are known to the Participant and/or client and not known to ASX Clear.

Q5

Do you agree that ASX Clear should change its current approach to addressing participant exercise errors notified to ASX Clear? Please set out your reasons.

Members regarded that operational errors regarding exercise had the potential to damage the ETO market, and hence, there was support for a change to the current approach and the adoption a clearly defined procedure for addressing exercise errors. There was support for ASX Clear having the power to reverse certain manual errors on the basis of the detriment that such errors had the potential to cause.

There was general support for the approach outlined in the Consultation Paper. Some members support there stipulation of a very clear framework regarding the time lines and responsibilities to remove uncertainty and to enhance the integrity of the market and its Participants.

There was also a suggestion that the errors framework should also make provision for errors regarding American style options prior to a corporate action. However, in this respect, the framework should provide protections against any incentives to “game” the error process.

Members indicated that further detail about these proposals would be needed in order to comment more fully on this.

Q6

Should ASX Clear change its current approach so that it does not in any circumstances take steps which may facilitate the correction of exercise errors? Please set out your reasons.

Members preferred that ASX Clear have the ability to facilitate the correction of errors as set out in the answer to Q5 above.

Q7

Should ASX Clear impose a notification cut-off time in order for a participant to be able to seek that an erroneous exercise or failure to exercise be addressed, and if so what time should apply? Please set out your reasons.

Members supported a requirement that, when ASX Clear decides to reverse an error, this should be made known to all Participants before the opening of the market on the next business day. This would allow the whole day for any resulting action necessary to

be taken , such as by way of close-out, including obtaining VWAP where that is a consideration. Some members indicated 10.00am as a suitable cut-off time, while others preferred 9.00am to allow time for any communications between client and broker to occur prior to market opening.

Q8

Should ASX Clear identify the counterparty participant to the requestor regardless of whether the counterparty participant has consented to their identity being revealed? Please set out your reasons.

Members did not see there being any reason why it was necessary for ASX Clear to identify the counterparty participant to the requestor in the absence of any consent by the counterparty participant. Although it was noted by a member that the identity of the counterparty participant is likely to be revealed in the DCA system in any event, albeit this would not be until a later point in time.

There was a minority view expressed supporting the position that counterparty identity should be revealed and that the counterparties negotiate error situations between themselves in preference to an ASX mandated regime.

We appreciate the opportunity to provide comments in respect of this Consultation Paper. Should you require any additional information or wish to discuss further any of the matters raised in this Submission, please contact me or Peter Stepek, Policy Executive on pstepek@stockbrokers.org.au

Yours sincerely,



David W Horsfield
Managing Director/CEO