29 August 2025

To: ASX Limited (Attn : Key-Yong Tee)

Dear Sirs/Madams

ASX Clear (Futures) Dynamic Default Fund Framework Consultation

FIA[1] appreciates the opportunity to provide comments to ASX's "Dynamic Default Fund Framework Consultation".

We commend ASX's efforts to strengthen its default fund structure and risk management practices. The proposed framework reflects a step forward in adapting to evolving market conditions. We support the intent of the reforms and recognise their potential to enhance ASX's risk management approach.

Please find below our comments to the specific questions raised in the consultation. Unless otherwise specified, capitalised terms follow the definitions provided in the consultation paper.

PROPOSED DYNAMIC DEFAULT FUND

4.1. ASX Commitment / Skin-In-The-Game
Question 4.1.1: Do you have any feedback or comments on ASX's commitment to ASXCLF's default fund under the proposed framework?
We are supportive of the direction and intent behind ASX's proposed changes to the ASXCLF default fund framework. The proposed enhancements represent, on balance, a positive step forward from the current framework and better address evolving risk management needs. The proposed framework offers ASX greater flexibility to respond to changing market conditions and strengthens the integrity of the clearing ecosystem.

[1] FIA is the leading global trade organization for the futures, options and centrally cleared derivatives markets, with offices in Brussels, London, Singapore and Washington, D.C. FIA's membership includes clearing firms, exchanges, clearinghouses, trading firms and commodities specialists from about 50 countries as well as technology vendors, law firms and other professional service providers. FIA's mission is to support open, transparent and competitive markets, protect and enhance the integrity of the financial system, and promote high standards of professional conduct. As the principal members of derivatives clearinghouses worldwide, FIA's clearing firm members play a critical role in the reduction of systemic risk in global financial markets. Further information is available at www.fia.org.

At the same time, we see opportunities for the proposal to be more closely aligned with international best practices and prevailing market norms. We would welcome continued engagement with ASX to explore potential refinements in support of this goal.

We also believe it would be beneficial to incorporate additional measures to reduce the impact of extreme or outlier data points that may otherwise distort default fund sizing outcomes under the proposed dynamic model.

4.2. Default Fund Sizing Methodology

Question 4.2.1: Please provide your feedback or comments on the proposed methodology for calculating the total default fund size.

1. **Look-Back Period**
   Concerns have been raised about the sizing methodology, particularly the inclusion of the 3-month period ending nine months ago in the lookback. This does not appear to capture evolving risk. A more appropriate approach would be to extend the observation window to ideally 6 months, or at a minimum of 3months, to better reflect current risk dynamics and promote a more stable default fund size over time.

   While we acknowledge that ASXCLF already uses its Credit Stress Test (CST) framework to size the default fund against Cover-2 exposures, we believe additional clarity around the CST scenario design process would help participants better assess the robustness of the methodology. In particular, more transparency on the key parameters, risk factors, and scenario construction principles (with a non-exhaustive set of illustrative scenarios) would provide comfort that the framework adequately captures a wide spectrum of extreme but plausible market conditions.

   Greater visibility into the CST design would also help clearing participants understand how the proposed sizing approach interacts with stress testing, particularly in periods of market dislocation not covered by the proposed lookback window. Such disclosures, even at a high level, would enhance confidence in the resilience of the framework while still respecting the confidentiality and sensitivity of scenario design.

2. **Sizing Metric**
   We believe the use of average exposures as the core sizing metric warrants further reconsideration. Instead, we recommend that the total default fund size be based on the maximum exposure observed over the lookback periods rather than the average.

   Default funds are designed to cover extreme but plausible scenarios, and a peak exposure approach is better suited to achieve this than relying on averages. For instance, in a rising equity market environment, averaging exposures from the most recent three-month period and from nine months ago may significantly understate prevailing risks, resulting in an inappropriately sized default fund.

While a peak-based methodology may lead to a larger default fund, it reduces the likelihood of having to rely on additional initial margin to absorb stress losses above IM during periods of market volatility. This, in turn, supports predictability and enhances systemic resilience.

This approach also aligns more closely with peer CCP practices, which typically calibrate their default funds to cover extreme but plausible stress events using peak exposures or high-confidence measures.

Should ASX prefer to maintain an average-based sizing approach, we suggest it clearly articulate the underlying risk appetite and provide appropriate backtesting and disclosures to demonstrate that the methodology performs adequately under a range of adverse scenarios.

Separately, we welcome and view the inclusion of the 10% buffer as prudent, and suggest it should apply to both lookback periods, not just the most recent one.

3. Polluter Pays Approach

Members have also noted that if ASX intends to adopt a polluter-pays approach for stress losses above IM, the mechanism should allow these losses to be allocated directly to the clients that generate the exposure.

At present, stress add-ons are often borne only by clearing members, who cannot always pass them through. This creates an uneven outcome. Allowing direct allocation to clients would better align costs with the source of risk and reduce the need for higher default fund contributions from clearing members. Without such a mechanism, the default fund size becomes somewhat artificial, as risk is ultimately covered either through mutualisation or through add-ons applied solely to clearing members.

Question 4.2.2: Do you have any feedback or comments on the proposed selection of the look-back period under the proposed Framework?

We note that most peer CCPs typically rely on recent market observations when sizing their default funds.

While ASX's proposed approach includes a recent three-month window, the additional use of a three-month period ending nine months prior potentially introduces a structural cycle. Specifically, this pairing creates a repeating annual pattern. For example, on 1 April 2025, both lookback periods would be January–March 2025 and January–March 2024. This could unintentionally amplify or mute recurring seasonal effects (e.g. commodity cycles, agricultural harvests, or economic data releases), as these events would consistently appear in one comparison window but not the next.

To mitigate this, we suggest ASX consider adopting a rolling 6-12-month consecutive lookback. While slightly longer, this approach would still reflect recent market conditions while reducing the risk of cyclical distortion and improving the robustness of the sizing methodology.

In addition, we would welcome further clarity from ASX on whether the inclusion of the three-month period ending nine months ago materially alters the calculated default fund size in backtesting results. Framed another way, is the activity during that earlier period (particularly in the commodities segment, where seasonality may play a significant role) sufficiently material to warrant its inclusion? If so, we would suggest ASX provide evidence of its impact to support the proposed methodology.

Question 4.2.3: Do you have any feedback or comments on the approach to sizing the default fund as the average CST pre-AIMs Cover-2 exposure over the lookback period?

We strongly recommend using maximum stress exposure rather than averages for a more robust and risk-sensitive default fund sizing approach.

Additionally, while using peak CST (rather than average) would increase CPs' default fund contributions, it would yield 98% pre-AIMs coverage. We ask whether ASX considered using a higher confidence level of stress loss exposure (e.g. the second-highest peak CST in its assessment), and what the rationale was for not incorporating it.

Question 4.2.4: What is your view on setting an explicit cap on the total default fund size and the associated review processes?

We have no objection to the proposed cap. Implementing a cap, alongside a clear monitoring and alerting process, introduces a prudent layer of risk control.

In that regard, we recommend that ASX develop internal policies and consult the RCC on when it may be appropriate to raise the cap, particularly if the default fund approaches the limit. We also note that ASX's ongoing commitment to contribute at least 20% of the default fund could constrain future increases to the cap.

Additionally, CPs should be given clear and timely information on how any decision to increase the cap would be communicated, including when any resulting increase in contributions would be due.

Finally, it would be helpful for ASX to explain how the cap is intended to apply in recovery or assessment scenarios involving single versus multiple defaults—specifically, whether the cap operates as a 1x or 3x multiple under such circumstances.

FIA.org

4.3. Default Fund Resizing Frequency
Question 4.3.1: What is your view on the proposed monthly resize of the total default fund at every month-end under the proposed Framework?
We consider this to be appropriate and consistent with market standards. Regular recalibration ensures the default fund remains responsive to changes in market risk and participant activity, supporting the robustness of the risk management framework.

4.4. Default Fund Allocation Methodology
Question 4.4.1: Is the proposed approach of using Credit Stress Tests (CST) pre-AIMs Cover-1 exposure to allocate the default fund to each CP a fair approach? If not, what alternatives would you suggest and why?
The approach is appropriate and consistent with market standards, helping to minimise volatility by avoiding overly frequent adjustments. Some listed CCPs, particularly in the U.S., use a blended allocation method. They typically allocate 10-20% based on volume to better capture CPs that are active in trading but hold minimal end-of-day risk. For example, CME allocates 90% based on stress loss and 10% based on volume.
Question 4.4.2: Is the proposed approach of using the average CST pre-AIMs Cover-1 exposure over the most recent 3- calander-month period to allocate default fund to the CPs a fair approach? If not, what alternatives would you suggest and why?
We recommend aligning the allocation period with the sizing methodology. If ASX retains the two separate lookback periods, then the default fund allocation should reflect each CP's CST pre-AIMs exposure during the relevant period and not only the most recent three months. In addition, ASXCLF should clearly communicate which lookback period is driving the default fund size as part of the monthly default fund resizing notifications.

Question 4.4.3: Please provide feedback or comments on the processes and timelines for ASXCLF notifying CPs of the default fund commitments, and for CPs meeting their respective default fund commitments.
Some members have queried why CPs are notified of default fund requirements only on the 5th business day when ASXCLF calculates this on the 1st business day of the month. To address this, we suggest considering a shortened cycle of three business days' notice followed by two business days for funding. This could help reduce the likelihood of relying on AIMs and enhance liquidity planning for clearing participants.

4.5. Default Waterfall
Question 4.5.1: Please provide feedback or comments on the proposed default waterfall structure.
We are opposed to the proposed changes that effectively reduce the number of tranches from three to two and rebalance the seniority of ASX's SITG, and question the need for any change to the current structure. ASXs proposal to remove the segregation between the F&O and OTC cleared services, with the second ASX tranche eliminated, would leave CPs who only use one service exposed to losses arising from defaults in the other. Under all scenarios, a CP active only in Futures would be worse off in the event of an OTC-only default, and vice versa, compared to the current setup. Members expressed strong support for retaining the ASX tranche between the two clearing services. This would maintain ASX's incentive to manage available resources before relying on the second tranche, an incentive that disappears under the proposal. In reality, this increases ASX last tranche protection as it must go through both clearing services prefunded resources before being used. While before, that fund was much at risk, as only 1 clearing service prefunded would act as a buffer before ASX tranches would be used. While ASX cites peer practice, we are not aware of a similar approach at other large global CCPs. If a two-tranche structure is ultimately preferred, we would encourage ASX to maintain its industry-leading commitment to a robustly sized SITG by calibrating the first tranche to match the combined size of the current first and second tranches (i.e. approximately AUD 270 million).

4.6. Stress Test Exposure Limit and Additional Initial Margins Approach
Question 4.6.1: Do you support the considerations given for retaining STEL and AIMs under the Dynamic Default Fund Framework?
Yes. As noted, these tools are necessary to meet regulatory standards, particularly when the default fund approaches its cap. They also provide ASX with valuable optionality for managing intra-month default fund resizing (versus AIM calls). To support participants in assessing the impact of retaining STEL, it would be helpful for ASX to provide each member with illustrative figures under the new framework. As mentioned in our response to Question 4.2.4, ASX's policy on resizing the cap should also take into account the number of clearing participants being impacted by AIM calls. This will ensure that the framework remains risk-sensitive and proportionate.

4.7. Recovery Assessments
Question 4.7.1: Due to ASX's high SITG, under ASXCLF's proposed Dynamic Default Fund Framework the recovery assessments will need to be adjusted. What is your view on the analysis presented and the adjustments proposed?
SITG Replenishment Members have raised strong objections to this, as they believe that assessments should continue to be capped at CPs' contributions. Under the proposal, the default fund would be defined to include both ASX's SITG and CP contributions. ASX has clarified during discussions that, in a recovery scenario, CPs' replenishment obligations would apply to both components. This approach diverges from standard practices at peer CCPs, where SITG is typically excluded from replenishment requirements. At the same time, with the default fund size and CP contributions already increasing, ASX's available resources are already expanding. As currently proposed, ASX's recovery assessments are set at exceptionally high levels[2] that are well above prevailing industry norms (typically 1–2x CP contributions). The main driver of these inflated

[2] Under the current proposal, recovery assessment multipliers are at 3.25x for a single default and up to 10x for multiple defaults. By way of numerical example - a default fund of AUD 650m with SITG contributions of AUD 270m and AUD 180m, and CP contributions of AUD 200m, would currently imply assessments of 650m (32.5x CP

levels is the inclusion of SITG within CPs' replenishment obligations. Such levels risk creating severe liquidity strains during stress events and could ultimately trigger disorderly market exits. We would also note that several CCPs cap assessments at less than 1x the default fund size. In light of the potentially significant size of SITG and the concerns around excessive replenishment, we recommend that ASX review its approach and exclude SITG from the definition of the default fund. Doing so would remove much of the rationale for imposing materially elevated replenishment obligations on CPs, and help ensure that replenishment requirements remain appropriately calibrated and aligned with industry practices. **<u>Request for Clarification</u>** Some members have queried what the course of action would be if losses exceed even 3x the default fund size. While such a scenario is highly unlikely, greater clarity on this point would support effective risk management planning and help participants assess the full extent of their potential exposures under the proposed framework.

4.8. Default Fund Replenishment
Question 4.8.1: Please provide feedback or comments on the default fund replenishment approach presented above.
ASX's replenishment timelines should be more closely aligned with those of CPs. Members suggested reviewing this to ensure ASX's incentives remain aligned with participants' interests. A tighter timeline would also improve the credibility of ASX's recovery measures. Both the current and proposed replenishment timelines have been viewed by some members as slow relative to the potential severity of events that could lead to default fund depletion. ASX should look to recent precedent, such as the Nasdaq default event, where rapid replenishment was key to maintaining confidence. In the event of losses to the default fund, ASX must demonstrate that it can act swiftly to restore trust in the soundness and resilience of the CCP, including prompt replenishment of its SITG and default fund contributions. There are also concerns that requiring large contributions during periods of systemic market stress could create significant liquidity strain and inadvertently amplify broader market risks. These concerns are heightened in scenarios where ASX may call for both replenishment and recovery assessments simultaneously. Additionally, some members have requested further clarity on how the process would apply in cases where a member resigns or defaults during the replenishment window.

contributions, 3.25 X 200 = 650m) for a single CP default and nearly AUD 2bn (9.75x CP contributions, 9.75 X 200 = 1,950Bn) for multiple defaults.

Question 4.8.2: Under the proposed default fund replenishment approach, ASXCLF provides estimates of a CP's default fund contribution to the CP shortly after the completion of the last default management process. Do you view this provision as useful for CPs?
Yes, including this provision would be useful as it enables members to better estimate the associated costs and make timely arrangements for the necessary funding.

IMPLEMENTATION CONSIDERATIONS

5.1. Implementation Timelines
Question 5.1.1: Does the indicative implementation timeline provide sufficient time for you to prepare for the implementation of the Dynamic Default Fund Framework?
The proposal appears reasonable, though the implementation timeline could be accelerated. Providing three months' notice, along with indicative impact assessments for CPs, should be sufficient to support readiness and smooth adoption.
Question 5.1.2: If the timeline does not provide sufficient time for preparation, please provide the reasons and propose alternative timelines.
No comment.
Question 5.1.3: Is there other essential information you would like ASX to consider providing with regards to the implementation of the Framework?
1. We recommend that ASX provide CPs with a one- to two-year historical backtest to better understand historical hypothetical default fund sizes and how they would have varied over time under the proposed methodology. 2. While ASX has noted that AUD 790 million was the peak default fund size over an 18-month backtest, members would appreciate further impact analysis showing not only the total default fund contributions but also firm-level allocations under the new framework. 3. It would be helpful for ASX to provide CPs with specific details on how their individual contributions (such as for AIMs, STEL, and other components) would change under various test scenarios. This could include illustrative calculations to clarify the allocation methodology and ensure transparency.

5.2. Dress Rehearsals for Notifying CP Default Fund Commitment Change
Question 5.2.1: Do you think conducting the 3 dress rehearsals is useful for CPs?
Conducting rehearsals is useful and appropriate to support readiness. However, given that most clearing participants are already familiar with variable default fund frameworks, the number of dress rehearsals could potentially be reduced. ASX might consider making the first rehearsal mandatory, with the subsequent ones carried out on a voluntary basis.
Question 5.2.2: Is there other information you would like ASX to consider providing in the CP commitment notice on an ongoing basis?
To support transparency and participant understanding, ASX could consider providing a summary of the underlying data and methodology used to derive each CP's default fund commitment.

5.3. Other Implementation Considerations
Question 5.3.1: Are there other implementation considerations and issues that ASX should consider to ensure the successful implementation of the Dynamic Default Fund Framework?
We would appreciate further clarification on how ASXCLF currently manages the default fund assets held with its panel of banks. In particular, could ASX confirm whether any changes to this arrangement are planned in light of a potentially larger default fund size? It would be helpful to understand whether ASX intends to diversify these holdings further to mitigate concentration risk across its panel banks as the default fund grows.

We welcome the opportunity to work with ASX to address these comments. Please feel free to contact me at bherder@fia.org should you wish to further discuss.

Yours

Bill Herder
Head of Asia-Pacific