



The Directors
ASX Settlement Pty Limited and ASX Clear Pty Limited
Exchange Centre, 20 Bridge Street
SYDNEY NSW 2000

21 September 2016

Dear Directors,

1. Background

ASX Settlement Pty Limited and ASX Clear Pty Limited (together hereinafter referred to collectively as 'the ASX' or 'ASX') operate the sole licensed clearing and settlement facilities in Australia providing clearing and settlement systems and services for the Australian cash equity market. Clearing and settlement services are critical to the operation of Australia's financial markets, providing investors efficiency in equity transactions and reducing counterparty and systemic risk.

Through its commitment to the ongoing development of clearing and settlement services to ensure that the needs of users are met and that services provided are aligned with global standards, the ASX in consultation with industry stakeholders and Australian regulators developed a Code of Practice for the Clearing and Settlement of Cash Equities in Australia ("the Code").

This Code came into effect on 9 August 2013 with the aim of formalising the ASX's commitment of working with clearing and settlement users to ensure their needs are met and they are engaged in a timely and transparent manner in relation to the ongoing development of clearing and settlement services and infrastructure.

Following the Treasurer's announcement on 30 March 2016 that approval of any new equities clearing licence applications will not be recommended until regulatory conditions are in place for safe and effective competition (which is expected to take at least 18 months), the Code remains effective for the current year.

2. Purpose of our report

Section 5 of the Code requires that, on an annual basis, the ASX conducts both an internal review of the operation of the Code, as well as engaging an independent external auditor to perform its own review.

PwC has been engaged by the ASX as the independent external auditor to review and report on the operation of certain sections of the Code for the period 1 July 2015 to 30 June 2016, as outlined in section 5(b) and detailed below. This report outlines the procedures performed by PwC in relation to our review of the operation of those sections of the Code and the results of those procedures.

3. Scope of work

The scope of our procedures in relation to our review of the operation of the Code is in accordance with the requirements of section 5 of the Code, as reproduced in the extract below:



“(b) Additionally, ASX will engage an independent external auditor to conduct an annual review and prepare a written report regarding the operation of the Code, including with respect to:

- (1) ASX’s compliance with the cost allocation principles described in clause 3.2;*
- (2) ASX’s compliance with the access request protocols described in clause 4.3(c) relating to requests for access to clearing and settlement services;*
- (3) ASX’s compliance with the operational standards described in clause 6(c) relating to the protection of competitively sensitive information acquired by ASX Clear and ASX Settlement in the course of providing the TAS and the settlement facilitation service; and*
- (4) ASX’s pricing to verify that there is no discrimination between ASX-affiliated entities and other users of clearing and settlement services.*

The external review will be completed and the external auditor’s report will be published within 3 months following the end of each financial year. The external auditor’s report will be provided to the Boards of ASX Clear and ASX Settlement and the Forum promptly after the report’s completion. ASX will publish the report on the ASX website.”

4. Use of the work of ASX Limited Internal Audit department (Internal Audit)

As noted above, the ASX is required to conduct an annual internal review regarding the operation of the Code. This review has been assigned to Internal Audit. Given the concurrent timing and consistent nature of the procedures to be performed in relation to the operation of the Code, PwC and Internal Audit have worked collaboratively to meet their respective obligations under section 5 of the Code.

Specifically, in performing our procedures, we have relied, in part, on the procedures performed by Internal Audit in relation to assessing the ASX’s compliance with certain obligations outlined in the Code. Such reliance has been used to supplement our own procedures, and in certain cases, in place of performing separate procedures.

In determining whether reliance can be placed on the procedures performed by Internal Audit, we have given due consideration to the guidance in Auditing Standard ASA 610 – *Using the Work of Internal Auditors*. ASA 610 requires that, in determining whether the work of an internal audit function can be used, the external auditor shall evaluate:

- (a) The extent to which the internal audit function’s organisational status and relevant policies and procedures support the objectivity of the internal auditors;
- (b) The level of competence of the internal audit function; and
- (c) Whether the internal audit function applies a systematic and disciplined approach, including quality control.

Having performed the evaluation required under (a) to (c) above, we determined it was appropriate and reasonable to use the work performed by Internal Audit.



To determine the extent to which reliance could be placed, we:

- 1) Performed an assessment to determine the inherent complexity of each Code obligation. For those Code obligations we deemed to be less complex and subjective in nature, we have used the work performed by Internal Audit. For the more complex and subjective Code obligations we performed our own independent procedures.
- 2) For those Code obligations where we have used the work of Internal Audit, we have re-performed a sample of Internal Audit's procedures to evaluate the adequacy of their work.

Those obligations where Internal Audit's procedures have been utilised to supplement or replace our procedures have been detailed in Appendix A.

5. Procedures & Results

To meet our obligations under section 5 of the Code, we designed procedures in relation to each obligation under the code to assess the extent to which the obligations were being met. The procedures were determined based on our professional judgement.

The specific procedures, together with the results from performing those procedures, are detailed in Appendix A of this report.

In performing our procedures we noted no exceptions or instances of non-compliance with the obligations of the sections of the Code within the scope of our review.

6. Disclaimer

This report is intended solely for the use of ASX Settlement Pty Limited and ASX Clear Pty Limited for purposes set out above. As the specified user of our report, it is for you to assess both the procedures and our factual findings to determine whether they provide, in combination with any other information you have obtained, a reasonable basis for any conclusions which you wish to draw on the subject matter. Accordingly, we expressly disclaim and do not accept any responsibility or liability to any party other than the specified users for any consequences of reliance on this report for any purpose.

Yours faithfully

A handwritten signature in blue ink, appearing to read 'Matthew Lunn', is written over a light blue horizontal line.

Matthew Lunn
Authorised Representative

Code Obligation	Scope	Procedure	Findings
<p>3. Pricing</p>			
<p>3-2 Published Management Accounts for Cash Equities</p>			
<p>(a) ASX will publish management accounts in respect of the clearing and settlement of cash equities in Australia. ASX will publish these accounts on an annual basis, together with ASX's full year financial results, and make them available on the ASX website.</p>	<p>Performed by PwC</p>	<p>Ensure the annual clearing and settlement cash equities management accounts are published on the ASX website, together with the ASX's full year financial results.</p>	<p>The FY16 management accounts were: (1) published together with ASX's full year financial results, and (2) made available on the ASX website on 18 August 2016.</p>
<p>(b) In the management accounts, ASX will allocate directly attributable and common shared costs for cash equity clearing and settlement as between ASX Clear and ASX Settlement. ASX will allocate costs for the clearing and settlement functions on the following basis:</p>	<p>Performed by PwC</p>	<p>Obtain the management accounts for clearing and settlement of cash equities and ensure the accounting policies for cost allocation are consistent with the Code.</p>	<p>We note that we are separately engaged by the ASX to provide an audit opinion over the management accounts prepared for clearing and settlement of cash equities. The management accounts include an accounting policy note which outlines the cost allocation methodology used for the allocation of both directly attributable and indirect expenses. As required by the Code, indirect costs are allocated to the activities of clearing and settlement for cash equities based on appropriate drivers for each major expense category. This methodology has remained unchanged from the prior year. We have assessed the cost allocations performed by ASX in relation to the allocation of expenses to the clearing and settlement entities. From the work performed, we have noted that ASX has appropriately allocated costs to the ASX clear and ASX settlement business units. Furthermore, the methodology of allocating expenses has remained consistent with prior year, with expenditure being allocated on the basis of relevant drivers and assumptions.</p>
<p>(c) ASX will establish a policy which describes the methodology used for apportioning directly attributable and indirect or common shared costs. This policy will be reflected in the published management accounts.</p>	<p>Performed by PwC</p>	<p>Refer to section 3.2(b) above.</p>	<p>Refer to section 3.2(b) above.</p>

Code Obligation	Scope	Procedure	Findings
(d) The published management accounts will be subject to review by an external auditor.	Performed by PwC	Ensure an external auditor has been engaged to perform a review over the management accounts.	We confirm that PwC has been engaged by ASX to complete an audit over the management accounts for the (i) cash equities clearing, and (ii) cash equities settlement operations in Australia for the year ended 30 June 2016.
3-3 Non-discriminatory and Transfer Pricing			
(a) Non-discriminatory pricing: ASX is committed to providing non-discriminatory pricing to all customers and potential users. The prices for clearing and settlement services provided by ASX Clear and ASX Settlement, including rebates, revenue-sharing arrangements and discounts applicable to the use of these services, will not discriminate between ASX-affiliated and other customers or potential users of clearing and settlement services.	Used the work of Internal Audit	<ul style="list-style-type: none"> i. Identify the current clearing and settlement customers, including ASX-affiliated customers. ii. Obtain a list of all cash market clearing and settlement billing for two months and ensure that all users have been billed consistently and/or differences can be justified. iii. Obtain a list of all annual cash market clearing and settlement billing for the period under review and ensure that all users have been billed consistently and/or differences can be justified. 	<ul style="list-style-type: none"> i. The list of ASXCL and ASXS participants was obtained from the Participant Transitions team. There are 36 entities that are participants of both ASXCL and ASXS, 29 participants who are participants solely of ASXS, and one participant of ASXS which is also an Approved Listing Market Operator. ASX currently has one Approved Market Operator (AMO) and three Approved Listing Market Operators (ALMOs). There is one ASX-affiliated user of cash market clearing and settlement – ASX Limited as the holder of the market licence to operate the cash market. A sample of two months billing data was selected from the review period. For the sampled months, for each product code applicable to cash market clearing and settlement fees, the billing rate per unit was reviewed against the corresponding rates in the Clearing, Settlement and Issuer Administration Services Schedule of Fees to ensure all participants were charged the same rate per unit. No exceptions were noted. ii. In addition, for the two months selected, the billing data for five participants were reconciled to the invoices issued. No exceptions were noted. The Trade Acceptance Service (TAS) agreement for AMOs and the Settlement Facilitation Service (SFS) agreement for ALMOs only includes annual and one off / ad hoc fees. No monthly or ad hoc fees were identified for the AMO, ALMOs or ASX Limited for the period under review.



Code Obligation	Scope	Procedure	Findings
<p>(b) Transfer pricing: ASX Clear and ASX Settlement will charge all users, including ASX-affiliated entities, non-discriminatory prices for materially equivalent services.</p>	<p>Used the work of Internal Audit</p>	<p>Refer to section 3.3(a) above.</p>	<p>iii. There are no annual fees relevant for the AMO and ASX Limited. Annual fees for the ALMOs were all billed consistently with the fee schedule in the SFS agreement.</p> <p>There are no annual fees relevant for ASXCL and ASXS cash market participants as confirmed by our review of the Clearing, Settlement and Issuer Administration Services Schedule of Fees.</p> <p>There is a revenue-sharing scheme for ASXCL and ASXS. Allocation of the revenue share pools has been calculated in accordance with the details of the schemes as disclosed in the original Scheme Notices.</p>

Code Obligation	Scope	Procedure	Findings
<p>4. Access to clearing and settlement services</p>			
<p>4-3 Responsiveness to Requests</p>			
<p>(c) ASX Clear and ASX Settlement will publish protocols on the ASX website which set out target timeframes for responding to requests for services and dispute resolution processes for AMOs and ALMOs.</p>	<p>Used the work of Internal Audit</p>	<p>Review the ASX website for the protocols on:</p> <ul style="list-style-type: none"> i. responding to AMO and ALMO service requests ii. dispute resolution processes (including pre-access and post-access disputes). 	<ul style="list-style-type: none"> i. In the “Customer Access” section of the website (http://www.asx.com.au/cs/customer-access.htm): <ul style="list-style-type: none"> (1) The “Services for Approved Market Operators” sub-section has a link to the “Procedures for Access Requests by Approved Market Operators”. This document tables the actions and timeframes for new customer enquiries and requests for the enhancement or expansion of the TAS. (2) The “Services for Approved Listing Market Operators” sub-section has a link to the “Procedures for Access Requests by Approved Listing Market Operators”. This document tables the actions and timeframes for new customer enquiries, new service enquiries, enquiries regarding potential enhancement to the Settlement Facilitation Service and operational matters. ii. The dispute resolution processes are detailed on the asx.com website in the following sections: <ul style="list-style-type: none"> (1) The “Code of Practice for Clearing and Settlement of Cash Equities in Australia Access Protocols” document (pre-access disputes) (2) The Trade Acceptance Service, Contractual Terms of Service for the provision of a trade acceptance service to Australian financial market licensees in respect of CHES-eligible ASX-quoted financial products (in the Dispute Resolution sub-section). (3) The template “Settlement Facilitation Service Agreement” (in the “Dispute Resolution” sub-section).

Code Obligation	Scope	Procedure	Findings
<p>6. Protection of Confidential Information</p>			
<p>(c) ASX Clear and ASX Settlement will put in place operational standards for the protection of AMO and ALMO competitively sensitive information acquired by ASX Clear and ASX Settlement in the course of providing the TAS or the Settlement Facilitation Service. ASX will consult with AMOs and ALMOs on the development of Information Handling Standards to implement information barriers within ASX to safeguard AMO and ALMO competitively sensitive information.</p>	<p>Performed by PwC</p>	<p>i. Ensure that ASXCL and ASXS have put in place operational standards for the protection of AMO and ALMO competitively sensitive information acquired by ASXCL and ASXS.</p> <p>ii. Obtain correspondence to confirm that ASX has consulted with AMOs and ALMOs (as identified for 4.2(a)) on the development of Information Handling Standards to implement information barriers within ASX to safeguard AMO and ALMO competitively sensitive information obtained.</p>	<p>i. Management confirmed that there were no changes during the reporting period FY16 to the processes that were confirmed as being in place previously.</p> <p>When an AMO or ALMO contacts management with data that they wish to be treated as CSI by ASXCL and ASXS, ASX first reviews the information to assess whether or not it is competitively sensitive. If it is, ASXCL and ASXS request permission to share the data with the relevant management contacts. Once permission is granted, the information is forwarded to the “permitted” staff for their review. They are required to advise whether they see any issues with the request and/or if they require any further information. For each member of staff receiving CSI, ASX Regulatory Assurance management meets with them and provides training to ensure they understand the requirements of the Information Handling Standards.</p> <p>The information obtained is ring-fenced and kept in a secure directory where access is limited, and management use hush-mail to correspond internally and externally with the affected parties.</p> <p>Management noted that it is the responsibility of the AMO and ALMO to ensure they send correspondence through to the relevant ASX counterparts and identify that the AMO/ALMO seeks to have the material characterised as conflict sensitive information.</p>
			<p>ii. A consultation paper dated 23 Jan 2014 has been included on the ASX website (http://www.asx.com.au/regulation/public-consultations.htm) and have been sent to AMO or ALMOs on - Clearing and Settlement Services for Approved Market Operators and Approved Listing Market Operators: Enhanced service levels and information handling standards.</p>



Code Obligation

Scope

Procedure

Findings

It was noted that the consultation paper includes proposals to enhance the protection of confidential information received from AMOs and ALMOs. Through inquiries with management it was noted that proposed amendments from the consultation process have been completed and came into effect on 1 July 2014.

It was noted that submissions from Chi-X and APX to the consultation paper have been included on the ASX website (refer to link listed above). ASX's responses to these submissions have also been published on the website.

Since the release of the above consultation paper, ASX has issued another consultation paper on the Code of Practice for Clearing and Settlement of Cash Equities in Australia – Proposed Operational Improvements dated 3 Dec 2014 on the ASX website.

We have confirmed with management that ASX has also:

- expanded the Trade Acceptance Service in 2015 to provide AMOs with non-discriminatory access to clearing and settlement arrangements for trades in CHES-eligible financial products that are admitted to quotation on an AMO's market but are not quoted on ASX's market. The TAS Legal Terms were amended to effect this expansion in service.
- issued AMOs with a Feb 2016 review of the TAS Legal Terms.