



BUSINESS COMMITTEE AGENDA

Date	Time	Location
Thursday , 1 December 2016	4.00pm – 5.30pm	ASX offices – Level 1, 20 Bridge Street, Sydney

Agenda Item		Indicative Time
1.	Introduction	4.00pm – 4.05pm
2.	Service Performance Operating Performance Report The Business Committee will be provided with a report on the operational performance of cash market clearing and settlement services.	4.05pm – 4.30pm
3.	Business Matters a) Roadmap for post-trade service infrastructure To provide the Business Committee with an update on ASX’s CHES replacement project.	4.30pm – 5.00pm
4.	Regulatory Updates a) Minimum Core Capital requirement, Collateral Haircuts and ETO Initial Margins The Business Committee will be provided updates on the minimum core capital consultation, changes being introduced to collateral haircuts and ETO margin enhancements. b) Updated Code of Practice The Business Committee will be updated on the Council of Financial Regulators’ policy statements on cash equity clearing and settlement released on 12 October 2016, and ASX’s updated Code of Practice.	5.00pm – 5.10pm 5.10pm – 5.25pm
5.	Administration a) Forward work program updated b) Minutes from the 31 August 2016 meeting c) Proposed 2017 Business Committee meeting dates d) Other matters	5.25pm – 5.30pm
6.	Next Meeting The next meeting of the Business Committee is scheduled for Thursday 2 March 2017, commencing at 12:00pm.	5.30pm



Agenda Item	Indicative Time
<p>End of Year Drinks</p> <p>Business Committee Members are invited to stay for end-of-year drinks to thank members for participating throughout 2016.</p> <p>Including an informal presentation from Adrian Lovney - CEO of NPP (National Payments Platform)</p>	5.30pm – 6:30pm

NEXT MEETING: Thursday 2 March 2017, commencing at 12:00pm.



Members			Apologies
Company	Name	Job Title	
ABN AMRO Clearing	Mr Sean Lawrence	Managing Director	
ANZ	Mr Peter Mullin	Managing Director, Pensions & Investments	
ASX	Mr Peter Hiom	Business Committee Chair Deputy CEO, ASX	
Bank of America Merrill Lynch	Mr Rhys Cahill	Global Markets COO	
Bell Potter Securities	Mr Dean Surkitt	Managing Director Retail	
BNP Paribas	Mr Luc Renard	Head of Clearing & Custody	
Chi-X Australia	Mr Mike Aikins	Chief Operating Officer	
Citi	Mr Miles O'Connor	Director, Direct Custody & Clearing Securities & Funds Services	
Commonwealth Bank of Australia	Mr Sheridan Thompson	Head of Strategic Development, CommSec	
Credit Suisse	Mr Andrew Farran	Chief Operating Officer	
Deutsche Bank AG	Mr Russell Deal	Chief Operating Officer	
Goldman Sachs	Mr Jeremy Follett	Executive Director Operations	
HSBC	Mr Peter Snodgrass	Head of Direct Custody and Clearing	
J.P. Morgan	Mr Suneet Jain	Sales Business Manager, Markets & Investor Services	
Macquarie Group	Mr James Indge	Cash Equities Business Manager	
Morgans	Mr Peter Chisholm	Chief Operating Officer	
Morgan Stanley	Mr Craig McGuire	Head of Operations	
National Australia Bank	Mr Nathan Walsh	General Manager, Self Directed Wealth Products & Markets	
NSX	Mr Tom Price	Director	
Pershing Securities	Mr Rob Forbes	Chief Executive Officer	
Stockbrokers Association of Australia	Mr Andrew Green	Chief Executive Officer	



Sydney Stock Exchange Limited	Mr David Lawrence	Chief Operating Officer & Company Secretary	
UBS	Mr Conor Foley	Chief Operating Officer	

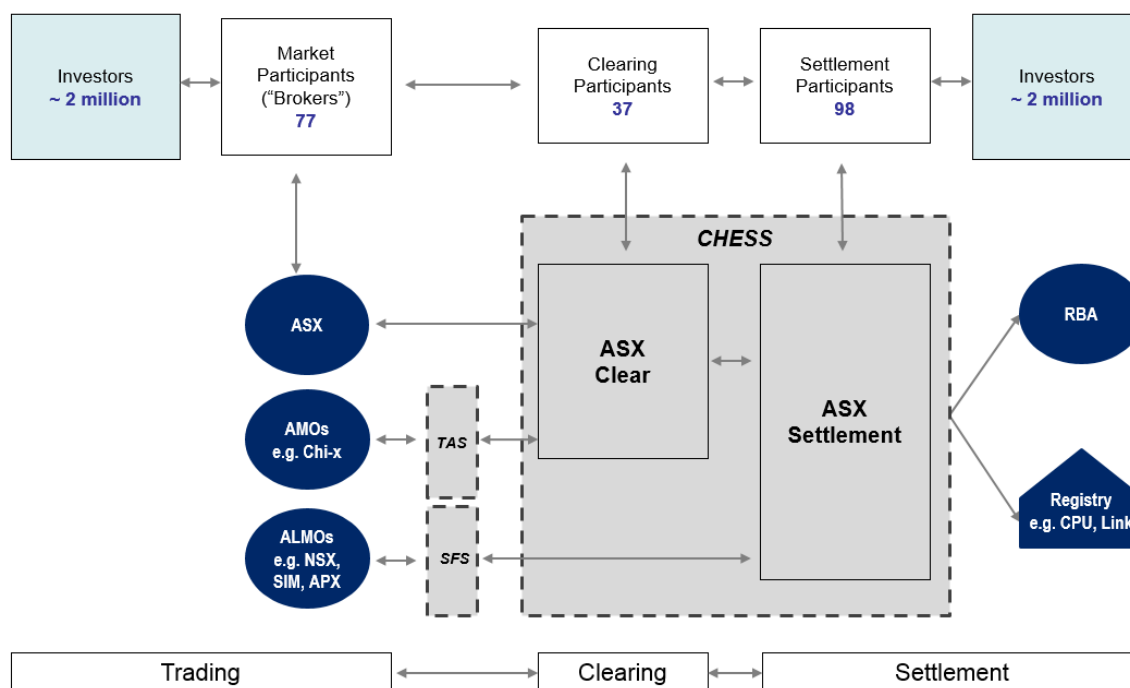
ASX Management		Apologies
Name	Job Title	
Ms Amanda Harkness	Group General Counsel & Company Secretary	
Mr Tim Hogben	Group Executive, Operations	
Mr Alan Bardwell	Chief Risk Officer	
Ms Eloise Wett	Executive General Manager, Customer Experience	
Mr Cliff Richards	General Manager, Equity Post Trade Services	
Ms Diane Lewis	Senior Manager, Regulatory and Public Policy	
Mr Gary Hobourn	Senior Economic Analyst, Regulatory and Public Policy	
Mr Rodd Kingham	Senior Manager, Equity Post Trade Services	
Mr Michael Bradwell	Senior Legal Counsel	

BUSINESS COMMITTEE MEETING PAPER AGENDA ITEM 2

Topic	Report on the operational performance of cash market clearing and settlement services
Date of the Meeting	1 December 2016
Purpose of this paper	To report on key performance metrics for ASX's clearing and settlement services.
Action required	To note the agenda paper.

BACKGROUND

Market Structure Overview



The clearing and settlement of equities performs a critical role in the operation of Australia's financial markets, helping to reduce counterparty and systemic risk, and provide transaction efficiency and certainty for end investors.

Core processes that provide these benefits include novation, netting and settlement.

Novation

Through a contractual process known as novation, ASX Clear becomes the seller to every buyer and the buyer to every seller, making it liable for completing all cleared transactions on the relevant market. Novation is deemed to occur at the point of trade and performs two important functions:

- it replaces the clearing participants' credit exposures to other clearing participants by substituting the clearing house as the central counterparty; and
- it enables the netting of settlement obligations.

Through novation, ASX Clear provides protection to non-defaulting clearing participants (and, indirectly, their clients) from the inability of a defaulting clearing participant to meet its obligations.

A key metric for monitoring novation is the percentage of on and off market trading that is novated.

Prior to novation, CORE (for ASX) and the Trade Acceptance Service (for AMOs – other trade execution venues) perform verification functions for trades submitted to ASX Clear. Following verification trades are registered for clearing. If the verification conditions are not satisfied then trades are rejected and not submitted to CHES. Once a trade is registered it is novated. Novation is deemed to have occurred at the point of trade for all trade execution venues.

Netting

ASX Clear is approved as a 'netting market' for the purposes of the Payment Systems and Netting Act. This enables the netting of settlement obligations in each individual equity, providing greater market efficiency at the time of settlement and reducing participant transaction and funding costs.

A key metric for monitoring netting is the percentage by which novated value is netted down for settlement. This metric is termed "netting efficiency".

Settlement

ASX's model for settlement maximises efficiency, while minimising the risk of settlement failure. It does this by simultaneously transferring the legal ownership of shares and facilitating the transfer of money for those shares. This is done through a Model 3 multilateral net batch settlement mechanism with irrevocable settlement finality at the end of the processing cycle. The transfer of money occurs across the Exchange Settlement Accounts of payment providers in the RBA's Information and Transfer System (RITS).

A key metric for monitoring settlement is the percentage of scheduled settlement that successfully settles (i.e. the opposite of the "fail rate"). This metric is termed "settlement efficiency".

Service availability

ASX's critical processes of novation, netting and settlement and are supported in ASX's core system CHES. It is critical for market operations, that CHES remains stable and available for processing. A key metric for monitoring systems availability is the percentage of systems uptime as measured against target availability times. The service availability target for CHES is 99.80%.

For the December 2016 quarter¹, the average monthly system availability was 100% for CHES. The average monthly availability of CHES has been 99.99% between November 2011 and October 2016.

Trade Acceptance Service

ASX Clear's Trade Acceptance Service (TAS) provides a mechanism for Chi-X to submit trades into the clearing house. The CHES system performs the clearing and settlement functions.

The Trade Acceptance Service availability target for TAS is 99.80% (the same as CHES).

For the December 2016 quarter², the average monthly system availability was 100% for the TAS. The average monthly availability of the TAS has been 99.99% between November 2011 and October 2016 (which is the same as CHES).

REPORTING ON CLEARING AND SETTLEMENT SERVICE PERFORMANCE

The key metrics noted above on novation, netting efficiency and settlement efficiency for December 2016 quarter are reported in Attachment A. They are also supported by charts demonstrating a longer reporting period in Attachment B.

¹ Up to 31 October 2016

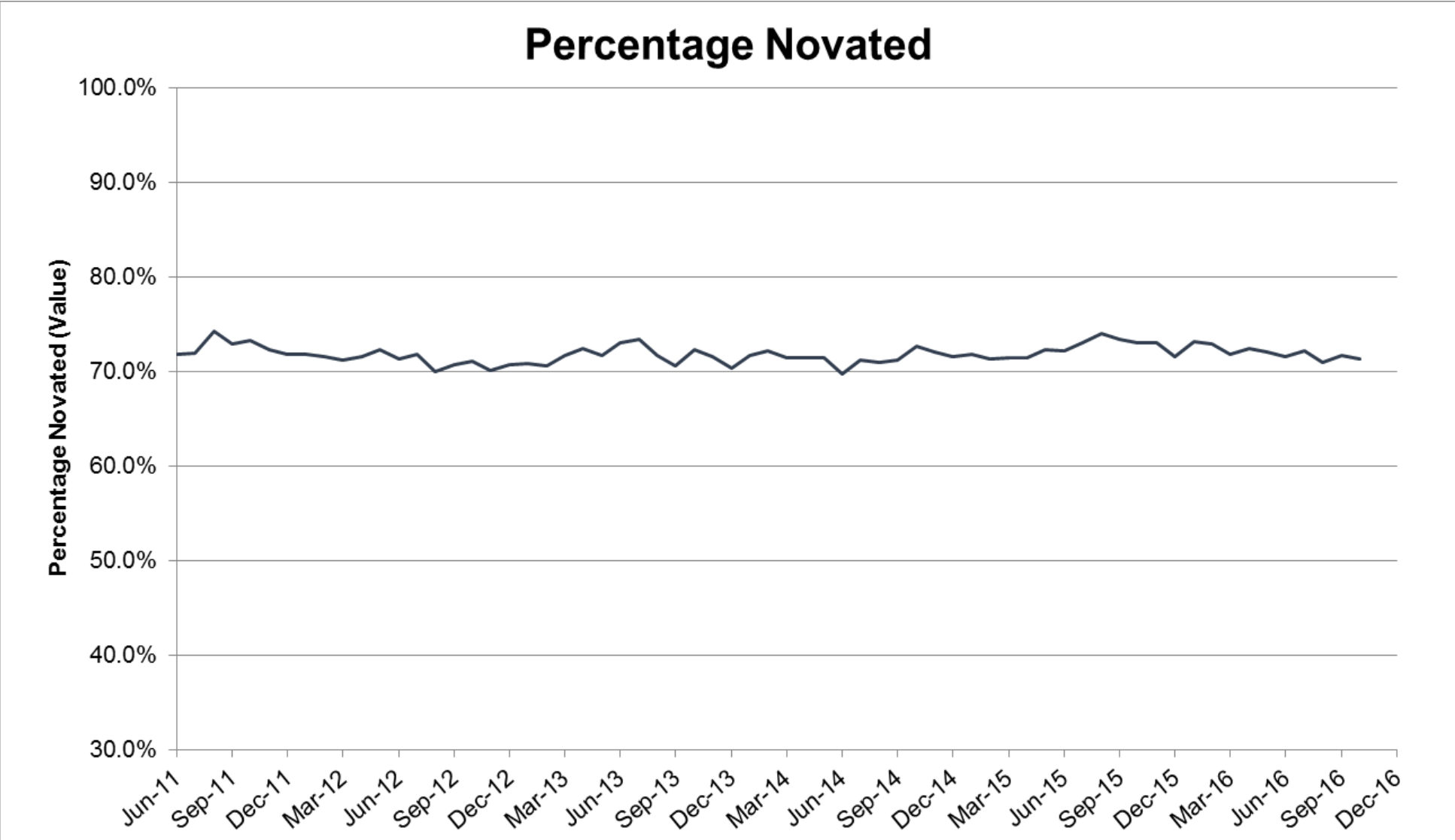
² Up to 31 October 2016

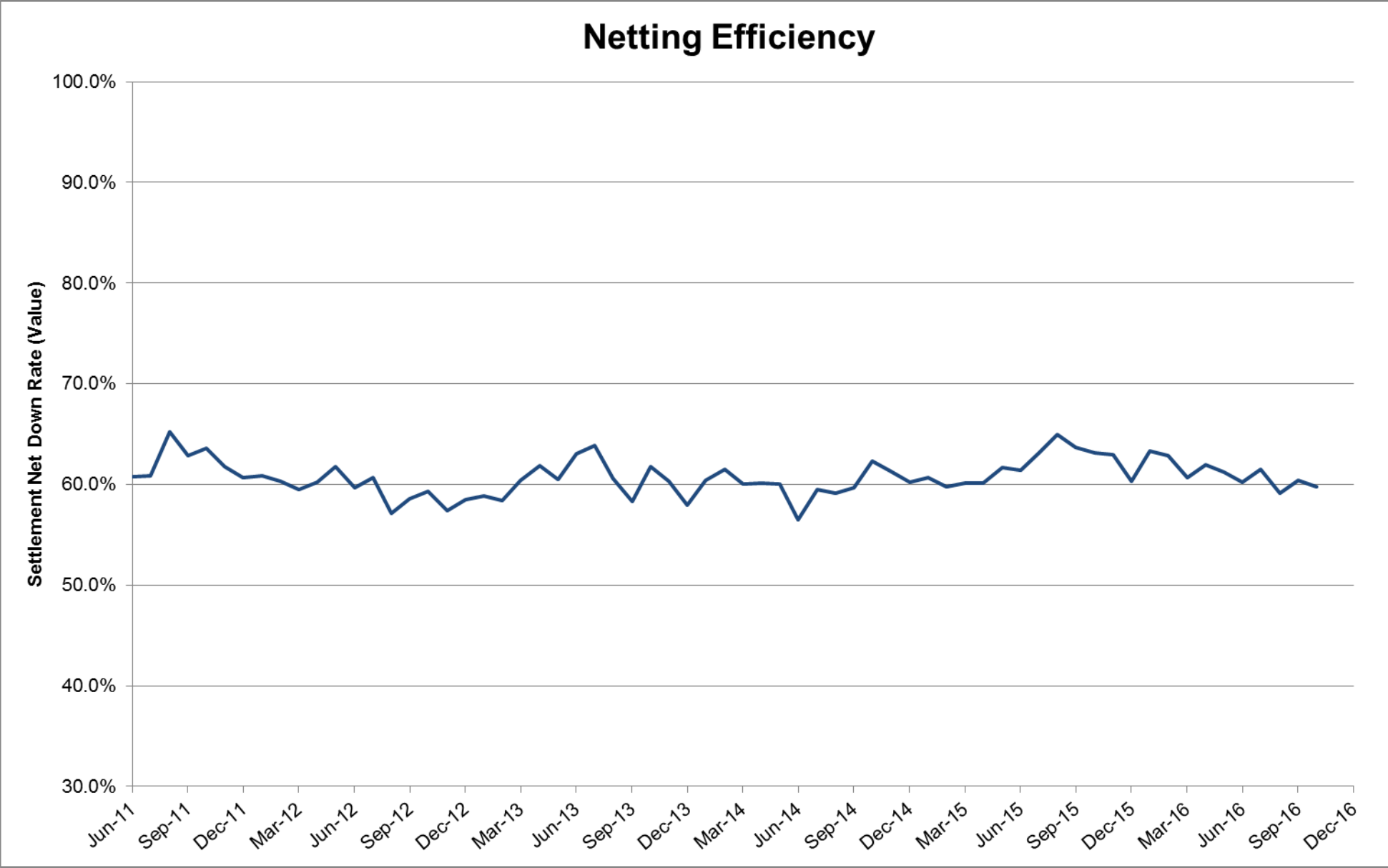
ATTACHMENT A – SUMMARY METRICS RELATING TO THE PERFORMANCE OF ASX'S CLEARING AND SETTLEMENT SERVICES

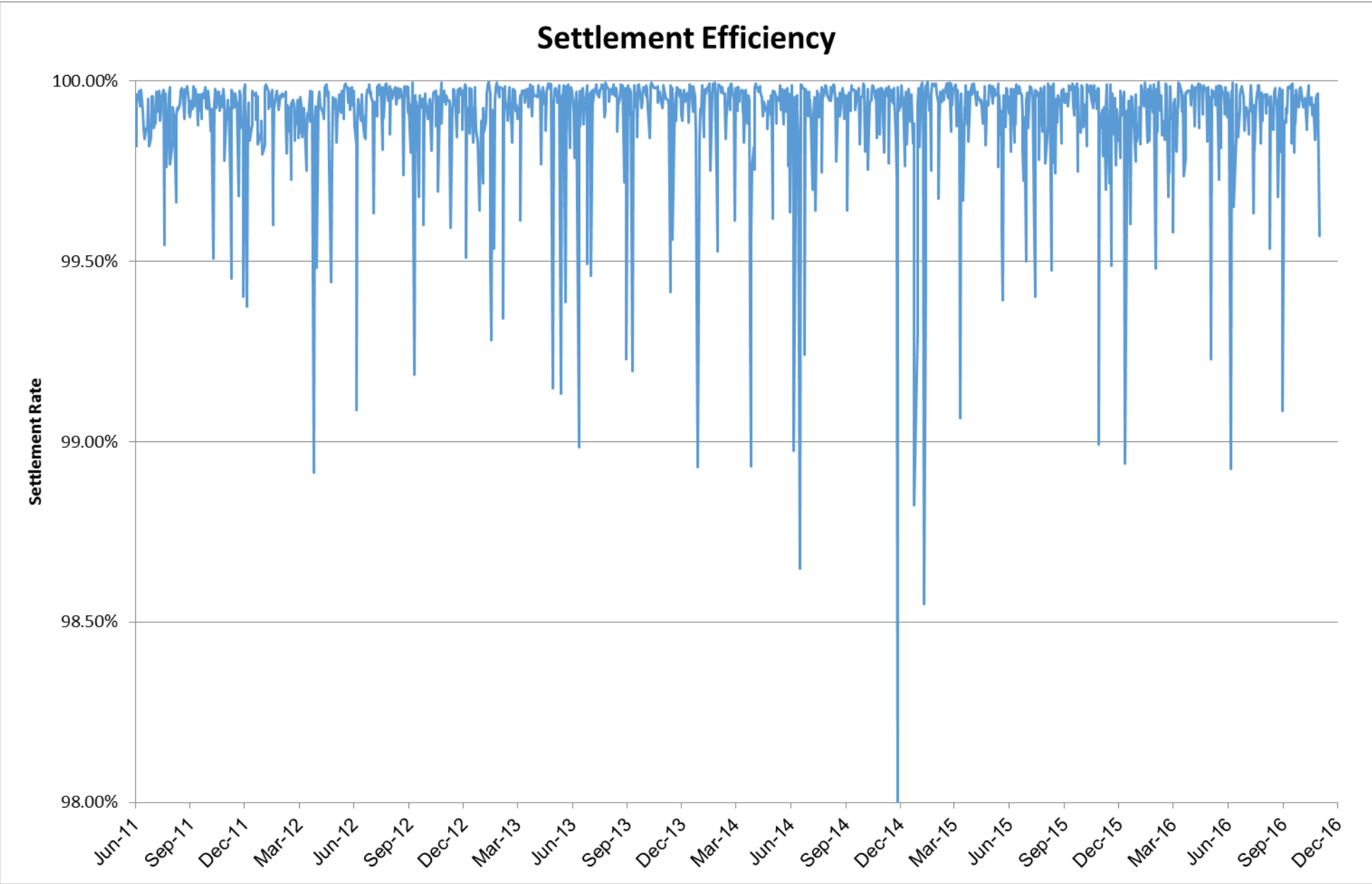
	December 2016 Quarter ³	September 2016 Quarter	June 2016 Quarter
System Availability (CHESS)	100%	100%	100%
System Availability (TAS)	100%	100%	100%
Total Trades Accepted (ASX)	20,711,710	66,861,781	64,811,380
Total Trades Rejected (ASX)	0	4	16
Total Trades Accepted (Chi-X)	6,953,659	20,458,781	18,265,912
Total Trades Rejected (Chi-X)	2	0	1
Total Settlements (SSX)	2	1	5
Total Value of Settlements (SSX)	\$0	\$0	\$6,744
Total Settlements (NSX)	98	389	342
Total Value of Settlements (NSX)	\$490,914	\$1,728,613	\$2,822,402
Daily Average Traded Value (On and Off Market)	\$6.2 billion	\$6.3 billion	\$6.3 billion
Daily Average Cleared Value	\$4.4 billion	\$4.5 billion	\$4.5 billion
Percentage Novated	71.3%	71.6%	72.0%
Daily Average Cleared Value Post-Netting	\$1.79 billion	\$1.78 billion	\$1.77 billion
Netting Efficiency	59.7%	60.3%	61.1%
Daily Average Settled Value (Including Non-Novated)	\$9.1 billion	\$9.3 billion	\$9.1 billion
Settlement Efficiency	99.91%	99.89%	99.91%

³ Up to 31 October 2016

ATTACHMENT B – PERFORMANCE OF ASX’S CLEARING AND SETTLEMENT SERVICES FROM JUNE 2011 TO OCTOBER 2016







BUSINESS COMMITTEE MEETING PAPER AGENDA ITEM 3A

Topic	Roadmap for Post-Trade Service Infrastructure
Date of the Meeting	1 December 2016
Purpose of this paper	To provide the Business Committee with an update on ASX's CHES replacement project.
Action required	The Business Committee is invited to provide feedback.

OVERVIEW

The evolving needs of customers, changes to the structure of the market, and the age of the CHES system has prompted ASX to commence a comprehensive process with the ultimate aim of replacing the current 24 year old CHES system with contemporary technology. This process is expected to take some time with a key decision being made at the end of 2017 on how best to proceed. In the meantime, the CHES system will continue to service the market well as it remains highly stable with orders of magnitude more capacity than currently required.

Over the next 12 months, ASX will be undertaking the work necessary to inform the decision in December 2017. Key activities in this process include but are not limited to:

A comprehensive stakeholder engagement process to inform, collaborate on requirements and share the evolving plan. The start of this process involved the release of a public consultation paper titled "*ASX's Replacement of CHES for Equity Post-Trade Services: Business Requirements*". Over 35 stakeholder consultation paper submissions have been received and are being reviewed by ASX. This stakeholder process has only just started and the engagement will continue over the next 12 months.

Business requirements definition for the initial build of the DLT platform that may (or may not) be ultimately used to replace CHES covers the core functions performed by CHES today. These functions include, trade registration and the core activities of clearing and settlement. Over the next 12 months, the business requirements for both clearing and settlement and other post trade services will be developed in consultation with stakeholders through an ongoing process of engagement. Consistent with best practice, all business requirements are being defined in a solution agnostic manner – meaning they are reusable and applicable to any technology solution. This work is 'no regrets' activity.

International standard messaging in the form of the widely accepted international standards organisation - ISO 20022 messaging is being analysed against existing CHES proprietary messages. Among the drivers supporting the adoption of ISO 20022 are lowering barriers to entry for new service providers and therefore providing greater choice to participants and improving the Australian cash equities market's ability to interact with other jurisdictions where these opportunities may arise.

The remainder of this paper provides detail on the planned activities to manage the required changes to ensure a successful CHES replacement.

STAKEHOLDER ENGAGEMENT

Stakeholder Consultation Process

The purpose of ongoing stakeholder engagement for CHES replacement is to inform and discuss with users and stakeholders possible changes to CHES's existing functionality and to discuss and validate business requirements for a replacement system.

These users include issuers, regulators, members of the Business Committee, other participants, solution providers and other market intermediaries.

ASX's planned stakeholder engagement and consultation process is an ongoing exercise and includes the following activities and forums:

- A public consultation paper titled "*ASX's Replacement of CHES for Equity Post-Trade Services: Business Requirements*"
- ASX's response to the consultation paper responses, respecting those submitted under confidential statuses
- Software demonstrations of the DLT prototype and an explanation of the conceptual software architecture
- Participant and industry association workshops to discuss requirements and to provide Q&A clarification
- Code of Practice Business Committee meetings
- Technical Committee meetings (as time progresses)
- Ongoing market communications to provide broadcast information updates

PLUS

- A convening of the Technical Committee to discuss ISO 20022 messaging. These workshops will commence in December 2016.
- Workshops for Business Committee members and other unrelated stakeholders to discuss stakeholders' consultation paper feedback (while respecting the confidential responses). These workshops will commence in December 2016.

A roadmap diagram on page 4 of this paper shows the high level scheduling of planned key activities.

ASX will provide regular updates to the market and continue to keep customers informed of key decisions and engagement activities to allow sufficient lead time for planning, resourcing and budgeting.

STAKEHOLDER FEEDBACK

Software Demonstrations and Workshops

As at 22nd November 2016 ASX has conducted software prototype demonstrations and participant and industry association workshops to over 35 stakeholder organisations. These sessions comprised well over 250 people – most of whom hold positions in operations, risk, compliance, regulatory, technology and senior and executive management functions. The overwhelming response to these demonstrations and workshops has been positive with workshop attendees appreciating and understanding that replacing CHES is a non-trivial task and will require measured consideration of the issues and a balance of addressing current and future needs.

Consultation Paper Responses

Due to the breadth, depth and diversity of consultation feedback, ASX will provide a detailed response in the first quarter of 2017. Nevertheless as outlined earlier, ASX will be conducting workshops from December onwards to discuss stakeholders' consultation paper feedback.

There were diverse and differing views with regard to support for some of the proposed changes however there were also a number of consistent themes in the consultation paper responses. Expressed by a majority of stakeholders, consistent themes from submissions included:

- No significant concerns with ASX's investigation to apply DLT to a CHES replacement system.
- A desire for a greater suite of 'Day 1' functional changes to improve cost and efficiency issues in participants back office processes. These included requests to improve the often paper based and manual processes associated with corporate actions, transfers and conversions.
- An understanding of and/or support for international standard messaging (ISO 20022) and what this means for Australia's financial market albeit many respondents naturally require the detail that will come from the work ASX has commenced in this area.
- A near universal view that all paper forms and associated paper based processes should be eliminated to the extent possible.

ASX thanks those participants who provided valuable detail, suggestions and ideas for addressing current inefficiencies while retaining the ability to see the strategic and future opportunities to improve the way our market operates.

Next Steps

Before ASX's public written response to the consultation paper feedback, due in 1st quarter 2017, the next steps in the stakeholder engagement process will include:

- The convening of the Technical Committee to discuss ISO 20022 Messaging in December 2016; and,
- Invitations to workshops for business committee members (and other unrelated stakeholders) commencing in December 2016 to discuss the stakeholder feedback received to date inclusive of consultation paper responses, bi-lateral workshop discussions and software demonstration feedback.

INTERNATIONAL STANDARD MESSAGING – ISO 20022

CHESS messaging is proprietary in format and therefore not compatible with other international systems and standards.

ASX will replace the current proprietary format with the International Standards Organisation – ISO 20022 standard and has contracted SWIFT to work on this exercise.

This work will 'feed' requirements for the CHESS replacement solution but is re-usable to any system ASX may replace CHESS with – that is the requirements and specifications in this work stream are technology solution agnostic.

The ISO 20022 work has commenced with SWIFT and will be managed in 5 workstreams, namely:

1. Gap analysis of the functions of CHESS vis-à-vis available ISO20022 messages.
2. Message mapping CHESS external interface specification - EIS to ISO 20022 messages.
3. Guidelines and maintenance of existing and new ISO messages.
4. New message process for the application to SWIFT for changes to existing or creation of new ISO 20022 messages.
5. Corporate actions phase 2 is the continuation of the work to automate and STP the processing of corporate actions.

The objectives of the Technical Committee meetings in relation to ISO2022 will be to discuss, analyse and validate ISO 20022 message types and their associated process workflows needed to achieve CHESS message and/or transaction equivalence or better. Many participants have a desire to adopt ISO 20022 messaging and also have ISO expertise within their firms and have indicated they would like to input into this stream of work. ASX welcomes this input.

SYSTEMS DEVELOPMENT

Technology Choice

In the same manner that ASX assesses the appropriateness of technology options for its other core platforms, it is assessing the application of distributed ledger technology (DLT) to post trade processing.

The assessment of DLT, an enhanced database architecture, is being undertaken with a technology vendor called Digital Asset who specialise in distributed ledger technology.

ASX currently expects to be in a position to make a decision on the technology and vendor to provide a system to replace CHESS towards the end of 2017. This means the current focus for the Business Committee and other stakeholders is being directed to the business requirements for the system, irrespective of the underlying technology.

Solution Scope

It is important to note that the solution to be delivered by Digital Asset towards the end of 2017 will not be 100% complete in terms of having all the required CHES replacement functionality. Should ASX decide to proceed to licence a version of Digital Asset’s system, another final phase of software development will be required to complete the post trade functions to ultimately allow for the decommissioning of CHES.

In the event that ASX does not decide to proceed with Digital Asset’s system towards the end of 2017, ASX would activate its CHES Replacement alternate plan – which involves adjusting the project to architect existing, known, traditional clearing and settlement solutions in a manner that allows for current CHES requirements to be met.

Innovation Potential

It should be noted that an activation of ASX’s CHES Replacement alternate plan may limit the ability to deliver future innovation and associated benefits that appear to be possible with the application of DLT. This would also forego the opportunity to ‘start with a clean sheet of paper’ with regard to a new system build.

CHES REPLACEMENT ROADMAP

This high level roadmap shows the activities completed, 2017 planned activities and the likely activities to occur in 2018 should ASX decide to progress with the DLT based system being built by its chosen technology vendor.

Review of technology options														
Selection of DLT partner														
DLT Prototype build														
Vendor system build														
Project updates - Webinars, web & email														
ISO 20022 Analysis - ASX & SWIFT														
Stakeholder DLT prototype demonstrations														
Stakeholder consultation activities														
Stakeholder business requirements process														
Stakeholder technical workshops														
ISO 20022 Working Group - ASX & Clients														
	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	
	2015	2016				2017				2018				

~~~end~~~

# BUSINESS COMMITTEE MEETING PAPER AGENDA ITEM 4A

|                              |                                                                                                                                                                                         |
|------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Topic</b>                 | <b>Update: Minimum Core Capital requirement, Collateral Haircuts and ETO Initial Margins</b>                                                                                            |
| <b>Date of the Meeting</b>   | 1 December 2016                                                                                                                                                                         |
| <b>Purpose of this paper</b> | To update the Committee on the Minimum Core Capital consultation, implementation of collateral haircuts and ETO margin enhancements to cover spread, liquidity and concentration risks. |
| <b>Action required</b>       | For noting                                                                                                                                                                              |

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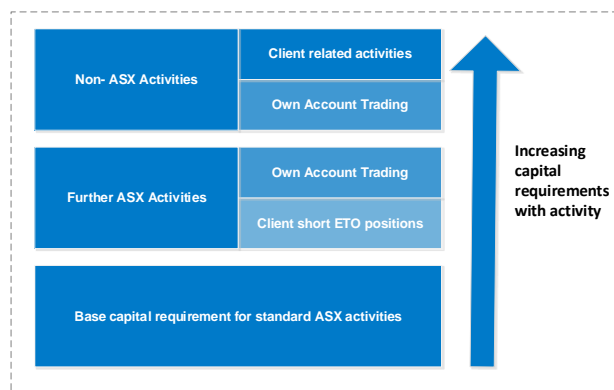
## EXECUTIVE SUMMARY

The Committee will recall that ASX proposed a number of enhancements to its risk control framework including a more risk responsive approach to setting Clearing Participant (CP) minimum core capital requirements, a less stringent approach to the setting of collateral haircuts including tiering of equity haircuts and finally, the introduction of spread, liquidity and concentration multipliers.

The paper provides an update in respect of the implementation of these proposed enhancements.

## MINIMUM CORE CAPITAL REQUIREMENT (MCCR)

The Committee will recall that under proposed changes to the minimum core capital requirements (MCCR), ASX is looking to introduce a risk responsive MCCR approach whereby requirements for Clearing Participants will be based on the level and complexity of Participant activity, where such activity is defined as (a) non-ASX business, (b) client short option activity and (c) own account business activity. Each activity attracts an additional capital requirement of \$2.5m unless deemed to be de-minimis and if material, a higher requirement of \$5m applies.



The intention to issue the Consultation Paper was flagged at the April 2016 ASX Clear Risk Consultative Committee and its release announced to the market on 30 June 2016. ASX engaged in bi-lateral discussions with a number of Clearing Participants, including those expected to be materially impacted by the proposed changes. Through these discussions and direct submissions, ASX has collated responses from 14 Clearing Participants and two industry associations (AFMA and the Stockbrokers Association). The industry representative bodies and larger well-capitalised CPs are neutral to broadly supportive (13 entities), while feedback from lower capitalised brokers (4) is less favourable.

Following a high level preliminary assessment of the responses, the key takeaways are:

- The majority of CPs were supportive of the risk reflective nature of the methodology, and as such ASX does not intend to make any fundamental changes to the approach.

- ASX will however (a) provide more detail in respect of definitions of each risk factor including relevant examples where appropriate (b) introduce de-minimis thresholds for short ETO activity and, (c) provide more clarity in respect of what constitutes “material activity” in respect of each of the three risk factors.

ASX intends to release the draft new MCCR rules (together with procedures and other rulebook related documentation), reflecting relevant feedback from Participants, for market consultation in Q1 2017. Participants will be required to provide their comments within a period of approximately 6 weeks from release of these draft rules.

### **CHANGES TO COLLATERAL HAIRCUT SETTING APPROACH**

ASX flagged at the April and August Business Committee meetings, the intention to introduce two methodology changes to its collateral haircut setting approach:

- a) Use of a less stringent definition of stress events for collateral haircut setting (agreed with the RBA), from the worst move to the 5th worst move, in the last 20 years (i.e. 99.9% confidence interval); and
- b) Better alignment of the haircut rates of eligible equity collateral securities with their inherent volatility characteristics by introducing several haircut tiers within which securities with similar volatility profiles are grouped together.

The new methodology resulted in collateral haircuts ranging from 15% to 30% for eligible ASX 200 securities compared to a flat 30% for all these securities and 10% for the S&P/ASX 200 SPDR ETF (previously 14%), and came into effect on 19 September 2016. On implementation, the calculated value of collateral held for margin purposes increased by \$350m (15%). Collateral haircuts, eligibility criteria and requests for new types of eligible collateral, are due to be reviewed again in May 2017 as part of the annual cycle.

### **SPREAD, LIQUIDITY AND CONCENTRATION RISKS**

The Committee will recall that ASX outlined at the August meeting, a more granular approach to dealing with spread, liquidity and concentration risks which will enable better management and tailoring of both initial margins (IM) and capital stress tests (CST) to such risks at a CP level. These risks are to be addressed through the introduction of liquidity and concentration multipliers and spread charges, where add-ons/multipliers will be subject to overall additional initial margin threshold floors per Clearing Participant for both the ETO and Cash Markets.

Spread charges are anticipated to be implemented in December and will be reflected in greater Volatility Scanning Ranges for exchange traded options (spread charges are not being applied to cash equities).

The final implementation of liquidity and concentration multipliers is still to be finalised, and estimated to be in Q2/Q3 2017.

ASX will keep the Committee updated in respect of this implementation schedule.



## BUSINESS COMMITTEE MEETING PAPER AGENDA ITEM 4B

|                              |                                                                                                                                                                             |
|------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Topic</b>                 | <b>Updated Code of Practice</b>                                                                                                                                             |
| <b>Date of the Meeting</b>   | 1 December 2016                                                                                                                                                             |
| <b>Purpose of this paper</b> | The Business Committee will be updated on the Council of Financial Regulators' policy statements on cash equity clearing and settlement and ASX's updated Code of Practice. |
| <b>Action required</b>       | To note the agenda paper.                                                                                                                                                   |

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On 12 October 2016, the Treasurer announced the release of two policy statements by the Council of Financial Regulators on clearing and settlement for the cash equity market:

- [Regulatory Expectations for Conduct in Operating Cash Equity Clearing and Settlement Services in Australia](#) (Regulatory Expectations)
- [Minimum Conditions for Safe and Effective Competition in Cash Equity Clearing in Australia](#) (Minimum Conditions)

The development of the two policy statements by CFR was endorsed by the Government as part of its announcement on cash equities clearing competition on 30 March 2016.

ASX has updated its cash equities clearing and settlement Code of Practice to align it with the Regulatory Expectations. The Business Committee was advised of the updated Code of Practice on 12 October 2016.

### Regulatory Expectations

The Regulatory Expectations apply to ASX's engagement with, and provision of services to, users of its cash equities clearing and settlement services while it remains the sole provider of such services. The Regulatory Expectations relate to key governance, pricing and access matters.

Legislative changes will be implemented to grant the appropriate regulatory agencies rule-making powers to enforce the Regulatory Expectations and provide the ACCC with the power to arbitrate access disputes.

The Regulatory Expectations will be periodically reviewed by the regulatory agencies and subject to change in the event that a committed competitor emerges with respect to the provision of any of ASX's cash equities clearing and settlement services. They will also be reviewed and subject to change if there is a material change in the operating environment for these services, for example, the implementation of new post-trade infrastructure.

The Regulatory Expectations are provided in Attachment A.

### Updated Code of Practice

The updated Code of Practice sets out ASX's commitment to comply with the Regulatory Expectations, and its commitments to customers and other stakeholders in managing cash equities clearing and settlement infrastructure and services for the Australian market.

The updated Code of Practice retains all of the core commitments from the original Code (which was introduced in August 2013) relating to transparent and non-discriminatory pricing and access, and the protection of confidential information received from other market operators in the course of providing the Trade Acceptance Service and the Settlement Facilitation Service. ASX has made a number of additional commitments, including to retain at least 50% non-executive directors on its Boards of ASX Clear and ASX Settlement who are independent of ASX Limited.

The Business Committee has also replaced the Forum as the primary forum for providing input to Management and the Boards of ASX Clear and ASX Settlement on the operation and development of cash equities clearing and settlement infrastructure and services. Over the period ahead, this will include a focus on the replacement of CHES.

ASX will commission an annual independent audit of its governance, pricing and access arrangements benchmarked against the Regulatory Expectations. The results of the first audit will be released at the same time as ASX's FY17 financial results are released in August 2017.

ASX is in the process of developing a framework and terms of reference for the annual audit process. The terms of reference for the annual audit will be provided to the Business Committee at its next meeting, which is currently scheduled for 2 March 2017.

The updated Code of Practice is provided in Attachment B.

### **Minimum Conditions**

The Minimum Conditions outline the measures that the regulators would require be taken to support a licence application from a second clearing house seeking entry to the market to clear cash equities listed on ASX's market. Before a second clearing house could be granted a licence, legislative framework and rule-making and arbitration powers (for the ACCC) will need to be put in place.

The Minimum Conditions recognise that the regulatory framework needed to support another clearing house would be costly to implement. In view of this, the Minimum Conditions state that while the regulators would offer a prospective competitor guidance on potential specific requirements through bilateral discussions prior to the submission of a licence application, the detailed specific requirements would not be articulated or implemented until such time as a committed competitor emerged or was likely to emerge. The Minimum Conditions also clarify that ASX would not be required to make up-front operational changes to accommodate competition until such time as a competing CCP committed to entry.

The Minimum Conditions relate to the following:

1. Adequate regulatory arrangements. These should include:
  - (a) rigorous supervision against the CCP Standards and other requirements under the Corporations Act
  - (b) application of the CFR's framework for regulatory influence over cross-border CS facilities
  - (c) ex ante wind-down plans
  - (d) appropriate arrangements for regulatory oversight in a multi-CCP environment.
2. Appropriate safeguards in the settlement process. The cash equity settlement model applied in a multi-CCP environment should seek as far as possible to preserve the efficiencies of the prevailing model at the time a competitor emerged, while:
  - (a) affording materially equivalent priority to trades novated to a competing CCP
  - (b) minimising financial interdependencies between competing CCPs in the settlement process
  - (c) facilitating appropriate default management actions.
3. Access to the securities settlement infrastructure on non-discriminatory, transparent, fair and reasonable terms.
4. Appropriate interoperability arrangements between competing cash equity CCPs.

The Minimum Conditions are provided in Attachment C.

### **ATTACHMENTS**

Attachment A – Regulatory Expectations for Conduct in Operating Cash Equity Clearing and Settlement Services in Australia (Regulatory Expectations)

Attachment B – ASX Cash Equities Clearing and Settlement Code of Practice

Attachment C – Minimum Conditions for Safe and Effective Competition in Cash Equity Clearing in Australia (Minimum Conditions)

# Regulatory Expectations for Conduct in Operating Cash Equity Clearing and Settlement Services in Australia

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A Policy Statement by the  
Council of Financial Regulators

October 2016

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## Background

On 30 March 2016, the Government endorsed the conclusions of a review of competition in clearing Australian cash equities carried out by the Council of Financial Regulators (CFR) and the Australian Competition and Consumer Commission (ACCC) – together, the Agencies – in the first half of 2015. These conclusions are set out in the Agencies' report, *Review of Competition in Clearing Australian Cash Equities: Conclusions* (the Conclusions), published at the time of the Government's announcement.<sup>1</sup>

Among the conclusions arising from the review, the Agencies undertook to publicly set out regulatory expectations for ASX's conduct in operating its cash equity clearing and settlement (CS) services until such time as a committed competitor emerged. The Conclusions presented the core elements that the Agencies expected to be included in the set of regulatory expectations. The core elements aim to address key governance, pricing and access matters that are dealt with under ASX's pre-existing *Code of Practice for the Clearing and Settlement of Cash Equities in Australia* (the Code), as well as some of the additional commitments proposed by ASX in its submission to the review and some gaps in the Code identified by stakeholders.

Consistent with the Agencies' commitment and drawing primarily on the core elements proposed in the Conclusions, this policy statement establishes a set of *Regulatory Expectations for the Conduct of Cash Equity Clearing and Settlement Services in Australia* (Regulatory Expectations). The Regulatory Expectations apply to ASX's engagement with, and provision of services to, users of its monopoly cash equity CS services for both ASX-listed and non-ASX-listed securities. Users are broadly defined to include participants of the ASX CS facilities; end users; unaffiliated market operators, central counterparties and settlement facilities; technology service providers; and other relevant stakeholders.

ASX will be expected immediately to commit to acting in accordance with the Regulatory Expectations established in this policy statement. The Agencies acknowledge that the Regulatory Expectations are not legally enforceable under the existing legislative framework. Accordingly, the Conclusions recommended that legislative changes be implemented to grant the relevant regulators rule-making powers that would enable them to impose enforceable requirements on ASX consistent with the Regulatory Expectations if these expectations were either not being met or were not delivering the intended outcomes. These powers would be held in reserve and would be expected to be used only in the event of a material deviation from the Regulatory Expectations or where ASX's conduct was generating undesirable outcomes for the market. In addition, the Conclusions recommended that the ACCC be granted an arbitration power that would provide for binding resolution of material disputes, arising where a user was seeking access to any aspect of ASX's monopoly cash equity CS services, consistent with the Regulatory Expectations. The ACCC may therefore have regard to the Regulatory Expectations when making a binding determination under the proposed arbitration power. The Government has committed to pursue legislative changes in accordance with these recommendations.

Should a committed competitor emerge for any aspect of ASX's cash equity CS services, the Agencies will review and make any necessary changes to the scope of the Regulatory Expectations to exclude that particular aspect. The Agencies also expect to review the Regulatory Expectations periodically, including in the event of material changes to the operating environment for these services. Such reviews may assess the ongoing appropriateness of the Regulatory Expectations and their effectiveness in delivering the intended outcomes, with consideration given to stakeholder feedback.

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<sup>1</sup> The Conclusions and the Government's response are available at <<http://www.treasury.gov.au/ConsultationsandReviews/Consultations/2015/Review-of-competition-in-clearing-Australian-cash-equities>>.

The Agencies will also establish structured arrangements for engaging with stakeholders in relation to ASX's adherence to the Regulatory Expectations.

## Regulatory Expectations

The Regulatory Expectations for the conduct of ASX's monopoly cash equity CS services are intended to support the long-term interests of the Australian market by delivering outcomes that are consistent with those that might be expected in a competitive environment. In particular, the Regulatory Expectations seek to ensure that ASX remains responsive to users' evolving needs and maintains transparent and non-discriminatory pricing of, and terms of access to, its monopoly cash equity CS services.

To give effect to the Regulatory Expectations, ASX should publicly commit to a revised Code that incorporates the Regulatory Expectations or adopt another equivalent mechanism. ASX is also expected to commit to submitting an annual external audit of its governance, pricing and access arrangements to the Agencies and members of relevant user governance arrangements, benchmarked against the Regulatory Expectations. This audit generally would not be required to form a judgement on the more subjective matters contained in the Regulatory Expectations, such as the promptness and efficiency of investments or the efficiency of prices. Rather, such an audit should develop an evidence base of relevant actions taken by ASX, and in particular provide assurance that it has policies and procedures in place aligned with the Regulatory Expectations and that it has conducted its operations in accordance with these policies and procedures. The outcomes of such audits are expected to be discussed with the ASX Boards, the Agencies and members of relevant user governance arrangements. The findings of such audits may be one input to any decision by the relevant regulators to employ the rule-making or arbitration powers once the supporting legislative framework is in place. The Agencies may additionally periodically request that ASX commission more detailed reviews of how particular aspects of its governance, pricing and access arrangements meet the Regulatory Expectations, or indeed carry out such reviews themselves.

Consistent with its existing arrangements to comply with its broader obligations under the *Corporations Act 2001*, ASX should continue to capture any complaints submitted by users, as well as its corresponding responses, within its complaints-handling system.

The Regulatory Expectations comprise the elements set out below.

### 1. User input to governance

To ensure responsiveness to users' evolving needs, transparent formal mechanisms should be maintained within ASX's governance framework to give users a strong voice in strategy setting, operational arrangements and system design, and to make ASX's monopoly cash equity CS services directly accountable to users. As part of this:

- (a) ASX should make an explicit public commitment to investing promptly and efficiently in the design, operation and development of the core CS infrastructure for the Australian cash equity market, including the Clearing House Electronic Sub-register System (CHES) and any future replacement system. This commitment should be supported by governance processes that enable users to provide input on the setting of the investment strategy. Investments should ensure that, to the extent reasonably practicable, the performance, resilience, security and functionality of the core CS infrastructure meet the needs of users, recognising the diversity and differing needs of users. At a minimum, the core CS infrastructure should accommodate internationally accepted communication procedures and standards.

- (b) ASX should ensure that the membership of its user governance arrangements is representative of the user base of its CS services, and that members are able to have a strong input into the agenda and format of meetings or other user governance mechanisms and the setting of priorities.
- (c) ASX should demonstrate that it has had regard to the views of members in setting the terms of reference for the external audits of its governance, pricing and access arrangements carried out in accordance with the Regulatory Expectations. This may take the form of members' non-objection of the proposed terms of reference. These terms of reference may change following any review of the Regulatory Expectations.
- (d) ASX should maintain accountability arrangements that provide for regular public attestations as to the effectiveness of its interactions with users. For example, the following arrangements would be appropriate:
  - (i) ASX's user governance mechanisms operate on a 'comply or explain' basis; that is, the relevant Board would take actions in accordance with recommendations from the user governance mechanisms, or else explain why such actions had not been taken.
  - (ii) ASX report, on at least an annual basis, the service developments and investment projects that it has progressed and how it has taken into consideration the views of users.
- (e) ASX should formally commit to retaining a Board structure for ASX Clear and ASX Settlement that comprises a minimum of 50 per cent of non-executive directors that are also independent of ASX Limited, and where a subset of these independent directors can form a quorum.
- (f) ASX should establish governance structures and reporting lines at the management and operational levels that promote access to its CS services on commercial, transparent and non-discriminatory terms. These arrangements should ensure that the interests of users are upheld in accordance with Regulatory Expectation 3. This may be demonstrated, for example, through the key performance indicators set for relevant management.

## 2. Fair, transparent and non-discriminatory pricing of CS services

ASX should publicly commit to an appropriate minimum level of transparency of pricing across its range of monopoly cash equity CS services. The pricing of these services should not discriminate in favour of ASX-affiliated entities (except to the extent that the efficient cost of providing the same service to another party was higher). Other than where pricing is anti-competitive or gives rise to financial stability or market functioning issues, the fees charged by ASX are a commercial matter for ASX and its customers. Nevertheless, to ensure that the fees charged by ASX for its cash equity CS services are fair, transparent and non-discriminatory:

- (a) ASX should ensure that all prices of individually unbundled CS services, including rebates, revenue-sharing arrangements and discounts applicable to the use of these services:
  - (i) are transparent to all users of the services
  - (ii) do not discriminate in favour of ASX-affiliated entities, except to the extent that the efficient cost of providing the same service to another party was higher
  - (iii) are made available to stakeholders in a form such that the impact of pricing changes can be readily understood.

- (b) ASX should maintain an appropriate method for determining the prices of its CS services so as to generate expected revenue that reflects the efficient costs of providing those services, including a return on investment commensurate with the commercial risks involved.
- (c) ASX should make an explicit public commitment that any changes in the prices of its CS services will not be implemented in a way that would materially shift revenue streams between aspects of its trading, clearing and settlement services.
- (d) ASX should publish any increases in its CS fee schedules along with an attestation justifying their reasonableness. For the most material such increases, this attestation would be expected to refer to relevant metrics and other evidence, such as the calculated return on equity, benchmarked price lists, or an independent review of how ASX's cash equity CS fees compare with those of CS facilities in other markets.
- (e) ASX should maintain an appropriate model for the internal allocation of costs, including the cost of allocated capital, as well as policies to govern the transfer of prices between the relevant ASX Group entities. Compliance with the model and policies would be expected to be subject to internal audit review. The model and policies should be based on reasonable cost allocation principles. For example:
  - (i) where possible, costs should be directly allocated to the service(s) which give rise to those costs
  - (ii) shared costs should be allocated based on appropriate and transparent metrics.
- (f) ASX should negotiate commercially and in good faith with unaffiliated market operators and CS facilities regarding fees and other financial contributions charged for any extensions to its monopoly CS services, and in particular those provided under the existing Trade Acceptance Service and the Settlement Facilitation Service.

### 3. Commercial, transparent and non-discriminatory access to CS services – service levels, information handling and confidentiality

ASX should facilitate access to its cash equity CS services on commercial, transparent and non-discriminatory terms. Non-discriminatory terms in this context are terms that do not discriminate in favour of ASX-affiliated entities (except to the extent that the cost of providing the same service to another party is higher). As part of this:

- (a) ASX should have objectives for its CS services that include an explicit public overarching commitment to supporting access to its CS services on commercial, transparent and non-discriminatory terms. ASX should maintain standard user terms and conditions that are consistent with these objectives, taking into account the legitimate business interests of ASX and any parties seeking access to its CS services.
- (b) Service level agreements should commit ASX to providing access to its CS services for unaffiliated market operators and CS facilities on operational and commercial terms and service levels that are materially equivalent to those that apply to ASX as a market operator or CS facility.
- (c) ASX should publish and adhere to protocols for dealing fairly and in a timely manner with requests for access. These protocols should include reasonable timeframes for responding to enquiries and arrangements for dealing with disputes. Nothing in the protocols should affect either party's right to refer a dispute to arbitration by the ACCC once the arbitration regime is implemented.



- (d) ASX should make an explicit commitment to ensuring that any investments in the systems and technology that support its cash equity CS services do not raise barriers to access from unaffiliated market operators or CS facilities. Announcements of any material investments in the systems and technology that support ASX's cash equity CS services should be accompanied by a public attestation that those investments will be designed in a way that does not raise such barriers.
- (e) ASX should retain, and periodically review, its standards for the handling of sensitive or confidential information. Consistent with governance arrangements that promote access on commercial, transparent and non-discriminatory terms (see Regulatory Expectation 1(e)), these arrangements should ensure that conflict sensitive information pertaining to the strategic plans of unaffiliated market operators or CS facilities is handled sensitively and confidentially, and cannot be used to advance the interests of ASX as a market operator or CS facility.

# ASX Cash Equities Clearing and Settlement Code of Practice

## ASX CLEAR AND ASX SETTLEMENT

### Customer and stakeholder commitments

In October 2016, the 'Regulatory Expectations for the Conduct of Cash Equity Clearing and Settlement Services in Australia' (Regulatory Expectations) were released by the Council of Financial Regulators. This Code of Practice sets out ASX's commitment to comply with the Regulatory Expectations, and its commitments to customers and other stakeholders in managing cash equities clearing and settlement infrastructure and services for the Australian market.

ASX is committed to ensuring Australia's clearing and settlement infrastructure is efficient, well capitalised, and well regulated. ASX recognises the importance of working collaboratively with customers and other stakeholders to deliver world class financial infrastructure and clearing and settlement services that meet the needs of a diverse range of users in the Australian cash equities market.





## Customer and stakeholder engagement

ASX is committed to meaningful engagement with customers and other stakeholders about the ongoing development of cash equity clearing and settlement infrastructure. ASX recognises the importance of engagement on the design and functionality of the infrastructure to ensure it continues to meet the needs of the market, and is consistent with relevant international best practice



## Transparent and non-discriminatory pricing

ASX's group structure supports the efficient delivery of services to all of its customers. ASX is committed to the principles of transparency and non-discrimination in pricing its cash equities clearing and settlement services



## Transparent and non-discriminatory access

ASX is committed to providing access to clearing and settlement services on transparent and non-discriminatory terms, and will respond to requests for access in a fair and timely manner



## Protection of confidential information

ASX Clear and ASX Settlement will not misuse any confidential information acquired in the course of providing clearing and settlement services





# 1. Customer and stakeholder

ASX is committed to meaningful engagement with customers and other stakeholders about the ongoing development of cash equity clearing and settlement infrastructure. ASX recognises the importance of engagement on the design and functionality of the infrastructure to ensure it continues to meet the needs of the market, and is consistent with relevant international best practice

## Commitments

- ASX will invest in the ongoing operation and development of the core cash equities clearing and settlement infrastructure promptly and efficiently. Such investments will seek to meet the needs of users, recognising the diversity and differing needs of users
- ASX will maintain an advisory Business Committee consisting of representatives of key users of cash equities clearing and settlement services
- ASX will hold quarterly Business Committee meetings for the purpose of providing input to Management and the Boards of ASX Clear and ASX Settlement on the ongoing operation and development of cash equities clearing and settlement infrastructure and services
- The Boards of ASX Clear and ASX Settlement will give due consideration to any material matters raised by, or recommendations of, the Business Committee. The Boards of ASX Clear and ASX Settlement will jointly provide a written response to Business Committee reports, including an explanation of why any recommendations had not been followed
- ASX will consult the Business Committee on its investment decisions in relation to the design, operation and development of new cash equities clearing and settlement infrastructure and services, including the development of a transition and implementation plan for new infrastructure
- ASX will report annually to the Business Committee on the cash equities clearing and settlement service developments and investment projects progressed, and how it has taken into consideration the views of users
- ASX will commission an annual independent review of its governance, pricing and access arrangements benchmarked against the Regulatory Expectations. A report prepared by the reviewer will be provided to the Business Committee and the Agencies (ACCC, ASIC, RBA and Treasury)
- Any interested party may provide information to ASX Clear and ASX Settlement in respect of the operation and development of cash equities clearing and settlement infrastructure and services by sending a written submission to the Chair of the Business Committee or the ASX Group General Counsel
- ASX will respond to any complaints relating to the provision of cash equities clearing and settlement services or this Code of Practice by users in a timely manner in accordance with its Complaints Handling Procedures.





## 2. Transparent and non-discriminatory pricing

ASX's group structure supports the efficient delivery of services to all of its customers. ASX is committed to the principles of transparency and non-discrimination in pricing its cash equities clearing and settlement services

### Commitments

- ASX will publish on its website fee schedules for all clearing and settlement services, including a brief description of each service
- The published fee schedules will set out the details, including eligibility criteria, of any rebates, revenue-sharing arrangements and discounts applicable to each service
- ASX Clear and ASX Settlement will not implement price changes with the purpose of materially shifting revenue streams between other trading, clearing and settlement services
- ASX will publish any increases in its fee schedules for clearing and settlement services, and attest to their reasonableness
- ASX will provide customers with information to assist them to assess the expected cost impacts of pricing changes and the expected cost impacts associated with new products and initiatives
- ASX will annually publish management accounts in respect of the clearing and settlement of cash equities in Australia. The management accounts will be subject to review by an external auditor
- ASX will publish a cost allocation and transfer pricing policy that describes the methodology used for allocating revenue, directly attributable costs, indirect and common shared costs and capital that relates to the clearing and settlement of cash equities in Australia. This policy will be reflected in the published management accounts
- ASX will maintain an appropriate method for determining the prices of its cash equities clearing and settlement services so as to generate expected revenue that reflects the efficient costs of providing those services, including a return on investment commensurate with the commercial risks involved
- ASX Clear and ASX Settlement will provide non-discriminatory pricing to all customers, including ASX-affiliated entities, and potential users of clearing and settlement services
- ASX Clear and ASX Settlement will charge all users, including ASX-affiliated entities, non-discriminatory prices for materially equivalent services
- ASX will negotiate on commercial grounds and in good faith with other market operators regarding fees and other financial contributions charged for any extensions to the Trade Acceptance Service and the Settlement Facilitation Service.





### 3. Transparent and non-discriminatory access

ASX is committed to providing access to clearing and settlement services on transparent and non-discriminatory terms, and will respond to requests for access in a fair and timely manner

#### Commitments

- ASX is committed to ensuring its investments in the systems and technology that support its cash equities clearing and settlement infrastructure are not designed in such a way as to raise barriers to access to other market operators or clearing facilities
- ASX Clear and ASX Settlement will publish transparent standard terms and conditions for access to cash equities clearing and settlement services by participants, and access to clearing and/or settlement arrangements for cash equities to other market operators through either the Trade Acceptance Service or the Settlement Facilitation Service
- ASX Clear and ASX Settlement will provide access to clearing and settlement services on a non-discriminatory basis
- ASX Clear and ASX Settlement will not unreasonably prohibit, condition or limit (directly or indirectly) access by a person or company to clearing and settlement services
- ASX Clear and ASX Settlement will consider requests for access to clearing and settlement services by other market operators, including requests for changes to clearing and settlement services, in a timely manner
- ASX Clear and ASX Settlement will provide access to clearing and settlement services to other market operators on operational and commercial terms and service levels that are materially equivalent to those that apply to ASX's market
- Where a request for a change in the clearing and/or settlement services provided under the Trade Acceptance Service or Settlement Facilitation Service has been agreed, ASX Clear and/or ASX Settlement will provide in writing to the customer the scope of any technical development and any changes to the ASX operating rules and procedures required. An indicative cost and timeline for implementing the change and the internal project priority will also be provided in writing
- ASX Clear and ASX Settlement will consult other market operators on the service levels under the Trade Acceptance Service and the Settlement Facilitation Service from time to time
- ASX Clear and ASX Settlement will publish protocols which set out target timeframes for responding to requests for access to cash equities clearing and settlement services
- ASX Clear and ASX Settlement will publish protocols for dispute resolution processes for other market operators regarding pre-access disputes. Post-access dispute processes will be provided in the legal terms for the Trade Acceptance Service and the Settlement Facilitation Service.





## 4. Protection of confidential information

ASX Clear and ASX Settlement will not misuse any confidential information acquired in the course of providing clearing and settlement services

### Commitments

- ASX Clear and ASX Settlement will comply with ASX's published Conflict Handling Arrangements policy
- ASX Clear and ASX Settlement will comply with the published Information Handling Standards for the protection of confidential and competitively sensitive information acquired by ASX Clear and ASX Settlement in the course of providing the Trade Acceptance Service and the Settlement Facilitation Service
- ASX Clear and ASX Settlement will periodically review the Information Handling Standards to ensure that they remain effective
- ASX Clear and ASX Settlement will not use any confidential or competitively sensitive information acquired in the course of providing clearing and settlement services for any other purpose than that for which it was provided
- ASX Clear and ASX Settlement will not use any confidential or competitively sensitive information acquired in the course of providing clearing and settlement services to provide an advantage to an affiliated entity of ASX Clear or ASX Settlement
- ASX Clear and ASX Settlement will be comprised of at least 50 per cent of non-executive directors that are not also directors of ASX Limited
- ASX will ensure that a quorum for the Boards of ASX Clear and ASX Settlement can be constituted by directors that are not also directors of ASX Limited to consider competitively sensitive information provided by another market operator.



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As the sole licensed operator of clearing and settlement facilities for the Australian cash equities market, ASX Clear and ASX Settlement are committed to providing clearing and settlement services in accordance with the principles of meaningful customer and stakeholder engagement, transparent and non-discriminatory pricing, transparent and non-discriminatory access and the protection of commercially sensitive information. The commitments set out in this document builds on the principles contained in the Customer Charter of ASX in which ASX commits to:

1. Work with customers to deliver products and services that meet their needs and that provide them with choice
2. Support Australia's aspiration to be globally competitive and become one of the leading financial centres in the Asia Pacific region
3. Make its products and services available on a non-discriminatory basis and on reasonable commercial terms
4. Manage its businesses and operations on a commercial basis to benefit its customers and provide appropriate returns to ASX shareholders
5. Recognise its role as a provider of critical financial infrastructure to the Australian financial markets, and make the necessary investments to ensure it can fulfil this role and provide confidence to market participants, investors and regulators
6. Run its operations in compliance with all legal and regulatory obligations
7. Maintain conflict handling arrangements that provide assurance and transparency about the way ASX conducts its business.

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**Visit [asx.com.au/cs/](http://asx.com.au/cs/)**

ASX has a section of its website dedicated to providing customers and other stakeholder's information on its cash equities clearing and settlement infrastructure and services. This information can be obtained by visiting.



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# Minimum Conditions for Safe and Effective Competition in Cash Equity Clearing in Australia

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A Policy Statement by the  
Council of Financial Regulators

October 2016

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## Background

On 30 March 2016, the Government endorsed the recommendations of a review of competition in clearing Australian cash equities carried out by the Council of Financial Regulators (CFR) and the Australian Competition and Consumer Commission (ACCC) – together, the Agencies – in the first half of 2015. These recommendations are set out in the Agencies' report, *Review of Competition in Clearing Australian Cash Equities: Conclusions* (the Conclusions), published at the time of the Government's announcement.<sup>1</sup>

With the Government's endorsement of the Agencies' recommendations, a policy stance of openness to competition has been confirmed. This stance recognises prevailing legislative settings that are accommodative of competition, as well as the potential benefits of competitive discipline. At the same time, the Conclusions acknowledge that competition in clearing could have cost, risk and efficiency implications for the functioning of markets, financial stability and access for unaffiliated market operators and clearing and settlement (CS) facilities. Accordingly, the Conclusions recommend legislative changes to facilitate a set of minimum conditions for safe and effective competition in cash equity clearing (Minimum Conditions (Clearing)).

As a first step, the Agencies have undertaken to set out the Minimum Conditions (Clearing) in a publicly stated policy. This document fulfils this commitment. The Conclusions recommend that the Minimum Conditions (Clearing) cover the following: (i) adequate regulatory arrangements; (ii) appropriate safeguards in the settlement process; (iii) access to settlement infrastructure on non-discriminatory, transparent, fair and reasonable terms; and (iv) appropriate interoperability arrangements between competing cash equity central counterparties (CCPs). The Minimum Conditions (Clearing) have been developed with reference to the prevailing market structure in settlement – in which there is a sole provider of settlement services. Nevertheless, the statutory framework (Part 7.3 of the *Corporations Act 2001*) applies to both clearing and settlement and recent rapid advances in technological developments may increase the prospect of competition emerging. The Agencies will consider the need for specific policy guidance to be issued in respect of settlement facilities.

The Minimum Conditions (Clearing) aim to give potential entrants sufficient clarity as to the measures that the Australian Securities and Investments Commission (ASIC) and the Reserve Bank of Australia (the Bank) would require be taken before they could advise in favour of a licence application. This should assist in establishing the business case for any competing provider. In addition to meeting existing licensing requirements under the Corporations Act, any licence applicant would be expected to demonstrate that it could viably provide services in this market in a manner consistent with the Minimum Conditions (Clearing).

Some aspects of the Minimum Conditions (Clearing) are not enforceable under the existing regulatory framework (such as requirements for materially equivalent settlement arrangements and the establishment of interoperability). The Agencies will therefore work with Government to implement legislative changes that would:

- allow the relevant regulators to implement and enforce the Minimum Conditions (Clearing) through the use of a rule-making power if and when a competitor emerged
- grant the ACCC power to arbitrate disputes regarding access to services licensed under Part 7.3 of the Corporations Act. In the context of the current settlement market structure, this would ensure that any competing CCP was able to access ASX's settlement infrastructure on fair,

<sup>1</sup> The Conclusions and the Government's response are available at <<http://www.treasury.gov.au/ConsultationsandReviews/Consultations/2015/Review-of-competition-in-clearing-Australian-cash-equities>>.

transparent and non-discriminatory basis with terms and conditions, including price, which are fair and reasonable.

Given the importance of the Minimum Conditions (Clearing) in ensuring that competition did not adversely affect financial stability or effective market functioning, ASIC and the Bank would be unable to advise in favour of a licence application until these measures had been implemented. The Agencies accept that this process could take some time. Consistent with the position of openness to competition, however, ASIC and the Bank would be prepared to engage with any potential entrant in the interim and commence consideration of a licence application, should one be submitted.

The proposed legislative framework to implement the Minimum Conditions (Clearing) would set out the relevant high-level requirements, leaving the relevant regulators to impose any specific obligations at a later stage through the use of the rule-making powers. It is envisaged that the new legislation would set the scope of the rule-making powers and the circumstances in which these powers could be used. The accompanying Explanatory Memorandum could provide further guidance on the nature of specific requirements that might be imposed through the use of these powers. In the case of interoperability, for instance, the rules would be likely to include such details as the criteria against which a CCP would be obliged to consider an access request from a competitor (and the acceptable grounds for rejecting such a request), the required scope and operational functionality of a link, and the timeframe on which a request that met the criteria should be granted.

Certain of the Minimum Conditions (Clearing) would need to be further supported by operational changes and, once implemented, would rely on other aspects of the regulatory framework. In the case of interoperability, for example, the rule-making power would establish and enforce the access requirement; once in place, the relevant regulators would monitor the operation of the link and the management of risks arising from the link under existing powers. The Bank would need to elaborate additional guidance to the *Financial Stability Standard for Central Counterparties* (CCP Standards) that deals with the management of risks arising from interoperable links.<sup>2</sup> At the same time, the Agencies would clarify arrangements for the regulatory oversight of matters such as default management and CCP recovery in a multi-CCP environment.

To the extent possible, the relevant regulators would offer a prospective competitor guidance on potential specific requirements through bilateral discussions prior to submission of a licence application, but detailed specific requirements would not be articulated or implemented until such time as a committed competitor emerged or was likely to emerge. The Agencies recognise that the rule-making process and the need to make operational arrangements to support a multi-CCP environment would defer the commencement of operations by a competitor. However, to implement the rules and require that operational changes be made in advance would lead to redundant industry investment and regulatory cost should a competitor fail to emerge. This is particularly important given that the rules will deal with matters such as interoperability and materially equivalent settlement arrangements between the emerging competitor and incumbent CCP, which could be costly to establish.

Accordingly, ASX would not be required to make up-front operational changes to accommodate competition until such time as a competing CCP committed to entry. However, at the same time, the technological design of ASX's CS infrastructure should not raise barriers to the potential future implementation of interoperability or access to settlement arrangements by a competing CCP.

2 The Bank's CCP Standards are available at <<http://www.rba.gov.au/payments-and-infrastructure/financial-market-infrastructure/clearing-and-settlement-facilities/standards/central-counterparties/2012/>>.

This statement should be read alongside the analysis on the costs and benefits of competition detailed in the Conclusions. Since the Minimum Conditions (Clearing) have been developed in the context of a market structure in which the settlement of cash equities is monopolistic, the statement also refers to the *Regulatory Expectations for Conduct in Operating Cash Equity Clearing and Settlement Services in Australia* (Regulatory Expectations).<sup>3</sup> The Regulatory Expectations would, for instance, govern the terms of access to ASX Settlement, ASX's securities settlement facility for cash equities.

The Agencies also expect to review the Minimum Conditions (Clearing) periodically, including in the event of material changes to the operating environment or market structure for these services, such as the emergence of a competing settlement facility.

## Minimum Conditions for Safe and Effective Competition

The Minimum Conditions (Clearing) relate to the following.

1. Adequate regulatory arrangements. These should include:
  - (a) rigorous supervision against the CCP Standards and other requirements under the Corporations Act
  - (b) application of the CFR's framework for regulatory influence over cross-border CS facilities
  - (c) *ex ante* wind-down plans
  - (d) appropriate arrangements for regulatory oversight in a multi-CCP environment.
2. Appropriate safeguards in the settlement process. The cash equity settlement model applied in a multi-CCP environment should seek as far as possible to preserve the efficiencies of the prevailing settlement model at the time a competitor emerged, while:
  - (a) affording materially equivalent priority to trades novated to a competing CCP
  - (b) minimising financial interdependencies between competing CCPs in the settlement process
  - (c) facilitating appropriate default management actions.
3. Access to the securities settlement infrastructure on non-discriminatory, transparent, fair and reasonable terms.
4. Appropriate interoperability arrangements between competing cash equity CCPs.

Each of the Minimum Conditions (Clearing) identified above is considered in greater detail in the remainder of this policy statement.

### 1. Adequate regulatory arrangements

#### **(a) Rigorous oversight against the Financial Stability Standards and other requirements under the Corporations Act**

The Corporations Act gives ASIC and the Bank joint regulatory responsibility for supervising CS facility licensees. The Bank is responsible for ensuring that CS facilities comply with the CCP Standards and take any other steps necessary to reduce systemic risk. The CCP Standards are aligned with the financial stability-related requirements of the CPMI-IOSCO *Principles for Financial Market*

<sup>3</sup> The Regulatory Expectations are available at <http://www.cfr.gov.au/publications/cfr-publications/2016/regulatory-expectations-policy-statement/>.

*Infrastructure* (PFMI), which establish an international benchmark for the risk management and operational standards of CS facilities.<sup>4</sup> ASIC is responsible for ensuring CS facilities comply with other obligations under the Corporations Act, as elaborated in ASIC's Regulatory Guide 211: *Clearing and Settlement Facilities: Australian and Overseas Operators* (RG211).<sup>5</sup>

Equivalent application of these oversight standards across competing CCPs should be sufficient to limit any scope for competition on the basis of less onerous risk controls, and thereby ensure that the market continues to function in a safe and effective manner. The Agencies nevertheless acknowledge the need for close vigilance at the margins of the standards, including cost-cutting measures and product development processes.

***(b) Application of the CFR's framework for regulatory influence over cross-border CS facilities***

If a new entrant CCP was seeking to leverage existing capabilities in overseas cash equity markets ASIC and the Bank's supervisory approach would be guided by the CFR's Regulatory Influence Framework.<sup>6</sup> This is a framework for ensuring that Australian regulators have sufficient influence over overseas providers of clearing and settlement services in the Australian market to support domestic policy objectives.

One measure under the Regulatory Influence Framework, which would apply primarily where a CS facility was both systemically important in Australia and had a strong domestic connection, is the requirement to incorporate locally and seek a domestic CS facility licence. As articulated in the additional guidance on the Regulatory Influence Framework, the threshold for application of this requirement would be likely to be set at a relatively low level for any CCP seeking to clear ASX securities. The Agencies consider this to be an integral part of the Minimum Conditions (Clearing), at least until ASIC and the Bank are comfortable with the arrangements for cross-border coordination and management of FMI recovery and resolution.<sup>7</sup> The precise threshold for the requirement would be discussed and agreed with a prospective competitor in order to provide the entrant with sufficient certainty to support business plans and investment decisions. The threshold would also be made transparent to market participants, market operators and ASX, to ensure that all stakeholders had the necessary information to formulate business plans with certainty.

***(c) Ex ante wind-down plans and associated commitments***

Since a commercially driven exit of a CCP in a competitive environment could disrupt activity in the segment of market activity that it cleared, the Agencies see a case to include measures aimed at mitigating such market disruption within the Minimum Conditions (Clearing).

4 The PFMI, published by the Committee on Payment and Settlement Systems (now known as the Committee on Payments and Market Infrastructures (CPMI) and the International Organization of Securities Commissions is available at <[http://www.bis.org/cpmi/info\\_pfmi.htm](http://www.bis.org/cpmi/info_pfmi.htm)>

5 ASIC's Regulatory Guide 211 is available at <<http://asic.gov.au/regulatory-resources/find-a-document/regulatory-guides/rg-211-clearing-and-settlement-facilities-australian-and-overseas-operators/>>

6 The CFR's framework for ensuring appropriate influence over cross-border clearing and settlement facilities (the Regulatory Influence Framework) is available at <<http://www.treasury.gov.au/ConsultationsandReviews/Consultations/2012/cross-border-clearing>>. Guidance on the application of this framework in the case of CCPs is available at <<http://www.cfr.gov.au/publications/cfr-publications/2014/pdf/app-reg-influence-framework-cross-border-central-counterparties.pdf>>

7 The international work on recovery and resolution of FMIs is currently ongoing. Domestically, in February 2015, the government released a consultation paper on legislative proposals to establish a special resolution regime for FMIs in Australia, available at <<http://www.treasury.gov.au/ConsultationsandReviews/Consultations/2015/Resolution-regime-for-financial-market-infrastructures>>. The CFR's response to this consultation was published in November 2015. This is available at <<http://www.cfr.gov.au/publications/cfr-publications/2015/resolution-regime-financial-market/>>.

In particular, all competing CCPs – including the incumbent and any new entrants – would be required to commit *ex ante* to a notice period of at least one year prior to any planned exit from the market. This should be supported by ring-fenced capital sufficient to cover operating expenses for the duration of the notice period, calculated on a rolling basis, as well as clearly articulated wind-down plans which would be discussed with ASIC and the Bank.

The Agencies acknowledge that the conditions stated here are more stringent than the requirements for orderly wind-down envisaged in the CCP Standards; Standard 14 on general business risk requires that ‘at a minimum, a CCP should hold, or have legally certain access to, liquid net assets funded by equity equal to at least six months of current operating expenses’. The Agencies consider this difference to be appropriate, as this condition is intended to provide for a planned exit for commercial reasons, while the Standard 14 seeks to protect against exit due to the crystallisation of business risk.

Furthermore, as discussed above, a commercially driven exit of a CCP could disrupt activity in the segment of market activity that it cleared. Such disruption could also arise if an existing provider scaled back its activities due to increased costs (e.g. if its exposures became concentrated in less liquid products). The Agencies would therefore work with the CCPs and relevant market operators to establish *ex ante* contingency arrangements to ensure the continued provision of clearing services for less liquid securities in the event that the incumbent CCP for those securities exited the market or reappraised its provision of those services.

***(d) Appropriate arrangements for regulatory oversight in a multi-CCP environment***

The Agencies do not see a strong case for a material change in ASIC and the Bank’s supervisory responsibilities in a multi-CCP environment. This view is consistent with the idea that participant oversight is central to a CCP’s risk management activities, given the proprietary risk exposure that a CCP assumes to its participants.

However, a more fragmented view of participants in a multi-CCP environment could disrupt arrangements for monitoring and managing clearing risk, including perhaps most notably in default management. As part of the Minimum Conditions (Clearing), the Agencies would clarify arrangements for regulatory oversight, particularly in relation to default management and CCP recovery, at such time as a committed competitor emerged.

Competition in clearing could also give rise to adverse selection in both products and participants. For instance, a competing CCP may be motivated to only offer clearing services in the most liquid securities or to structure their business so as to favour larger participants over smaller participants. This could lead to the fragmentation of the market along the lines of liquidity, with potential implications for the profile of exposures to be managed by each CCP. If a competing CCP were to emerge, the Agencies might consider steps to mitigate these effects, such as through closer oversight of product and participant scope; it is acknowledged, however, that there could be practical challenges in implementing such steps.

## 2. Appropriate safeguards in the settlement process

The entry of a competing cash equity CCP would have implications for the design, operation and organisation of the settlement model. Any changes to the existing settlement arrangements could potentially give rise to additional costs, as well as financial and operational risks. In light of this, the Agencies see a case to set minimum conditions around the design of the settlement model for a multi-CCP environment. As far as possible, the new model would need to preserve the efficiencies of the prevailing settlement model in a single-CCP environment, while affording materially equivalent

priority to a competing CCP. It should also minimise financial interdependencies between CCPs in the settlement process and facilitate appropriate default management actions.

### 3. Access to ASX Settlement on fair, transparent and non-discriminatory terms

In the absence of an alternative provider of cash equity settlement services emerging, any new cash equity CCP would require access to the vertically integrated incumbent settlement facility, ASX Settlement. To the extent that it remains the sole provider of cash equity settlement services, ASX Settlement would be required to facilitate the provision of access to its cash equity settlement infrastructure on a fair, transparent and non-discriminatory basis with terms and conditions, including price, that are fair and reasonable.

The Regulatory Expectations, outlined by the Agencies in a separate policy statement, deal with access to monopoly clearing and settlement services. The relevant provisions in the Regulatory Expectations explicitly address access on fair, transparent and non-discriminatory terms; these provisions would also apply to ASX Settlement's provision of clearing and settlement services to a competing CCP for cash equities under the Minimum Conditions (Clearing). Additionally, the ACCC will have the power to arbitrate disputes in relation to price and/or non-price terms and conditions of access where negotiations guided by the Regulatory Expectations fail.

### 4. Appropriate interoperability arrangements between competing CCPs

Interoperability has been identified as a potentially effective mechanism for ensuring that the benefits of competition are realised while mitigating some of the adverse implications, including market fragmentation and increased operational costs for participants. Based on analysis summarised in the Conclusions, the Agencies consider that a requirement to establish appropriate interoperability arrangements between cash equity CCPs, prior to a competing CCP commencing operations, would be a necessary condition to support competition.

Given commercial and operational considerations, the incumbent CCP may have little incentive to voluntarily develop interoperability arrangements with a new entrant. 'Open access' obligations or other regulatory measures may therefore need to be imposed to facilitate the establishment of fair and effective interoperability between the incumbent CCP and any new CCP seeking to enter the Australian cash equity market.

The Agencies also acknowledge that interoperability may give rise to additional complexities and risks. Should a competing CCP emerge, an effective risk management framework for interoperability arrangements would need to be put in place in order to mitigate these incremental risks. Specifically, the Bank would need to issue additional guidance to clarify how the requirements under CCP Standard 19 (FMI Links) should be met for the purpose of establishing safe and effective interoperable links.



# BUSINESS COMMITTEE MEETING PAPER AGENDA ITEM 5A

|                              |                                                                                                                                              |
|------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Topic</b>                 | <b>Forward Work Program Update</b>                                                                                                           |
| <b>Date of the Meeting</b>   | 1 December 2016                                                                                                                              |
| <b>Purpose of this paper</b> | To update the Business Committee on the forward work program extending to March 2017.                                                        |
| <b>Action Required</b>       | The Business Committee is invited to review completed items and provide feedback on the future topics for discussion and the prioritisation. |

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## OVERVIEW

The forward work program included in Attachment A covers the period of meetings of the Business Committee from February 2016 to March 2017. The Business Committee provided input into the forward work program at the 17 February, 15 June and 31 August 2016 meetings and members have had further opportunity to add topics via e-mail.

The forward work programme has been amended to reflect requests to continue updates on - the developments on COFR review of clearing competition, capital and risk impacts, and infrastructure roadmap developments for Post-Trade services (in particular new technology opportunities and the eventual replacement of CHES).

The program is consistent with previous forward work program in that it has been developed around the following four major themes:

1. Capital efficiency and industry economics;
2. Participant structure flexibility and efficiency;
3. Service Innovation; and
4. Technology and Infrastructure enhancements.

## QUESTIONS FOR THE BUSINESS COMMITTEE

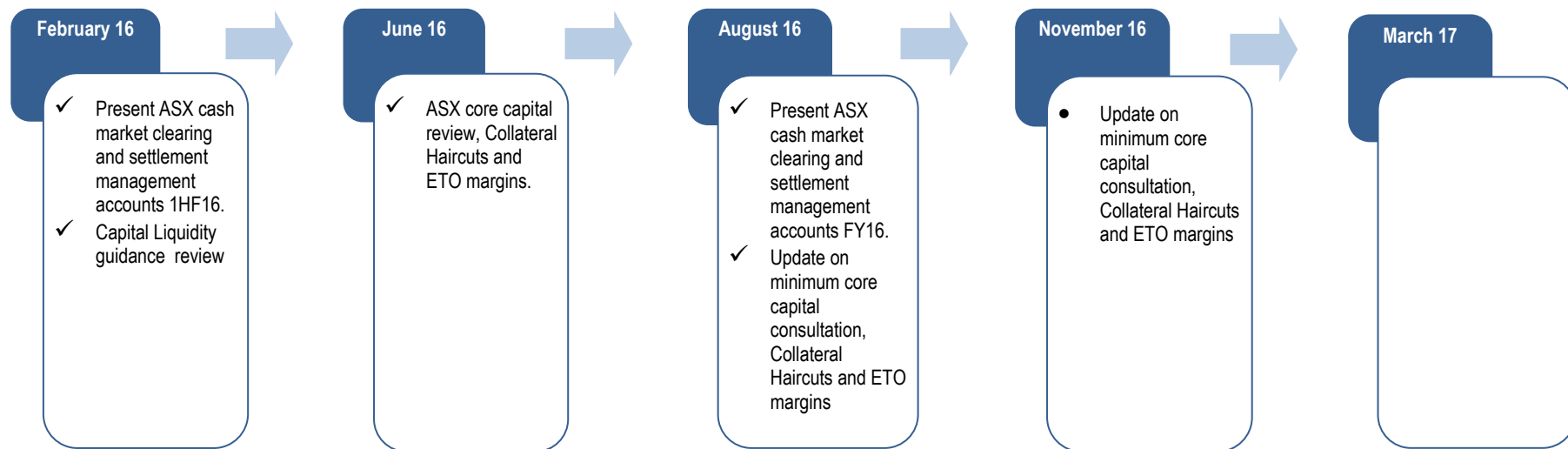
- Does the draft forward work program extending to March 2017 reflect industry priorities?
- Are there additional topics that could be considered for inclusion?

## ATTACHMENTS

Attachment A – Forward work program draft – February 2016 to March 2017.

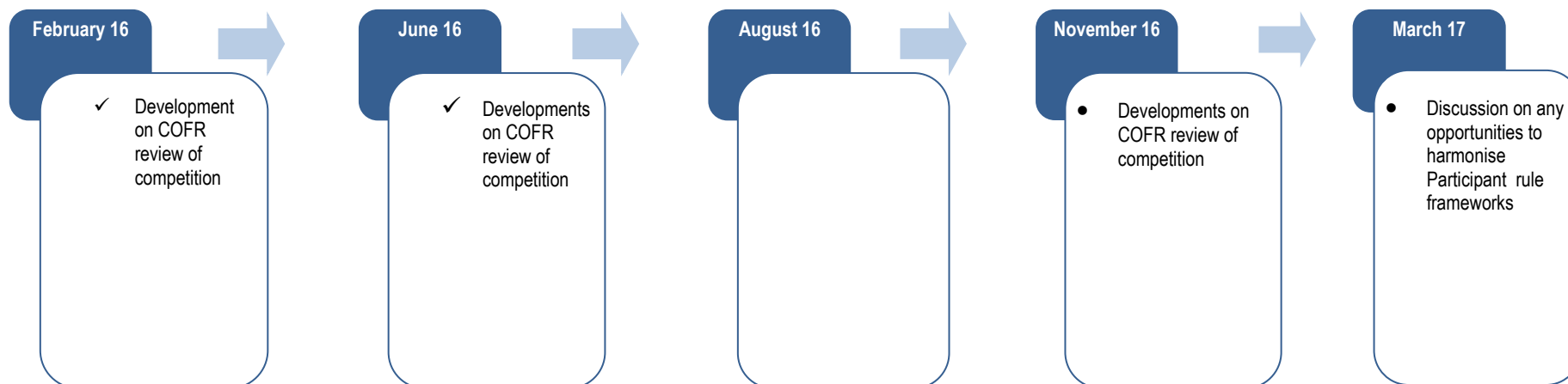
| Theme                                        | Objectives                                                                                      | Possible topics for discussion / agenda items                                      | Description of topic                                                                                                                                                                                                                                                                  |
|----------------------------------------------|-------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1. Capital Efficiency and industry economics | To minimise the capital costs for ASX's customers whilst maintaining robust CCP capital support | a. ASX cash market clearing and settlement economics                               | ASX to publish management accounts in respect of the clearing and settlement of cash equities in Australia at the same time that ASX reports its half and full-year results. ASX will provide a detailed briefing at the Business Committee meeting following publication of results. |
|                                              |                                                                                                 | b. Minimum core capital requirements, Collateral Haircuts and ETO Initial Margins. | ASX will provide an overview and update on the minimum core capital consultation paper, changes being introduced to collateral haircuts and ETO margin enhancements to cover spread, liquidity and concentration risk.                                                                |
|                                              |                                                                                                 |                                                                                    |                                                                                                                                                                                                                                                                                       |
|                                              |                                                                                                 |                                                                                    |                                                                                                                                                                                                                                                                                       |

Timing for Business Committee Consideration of Topics



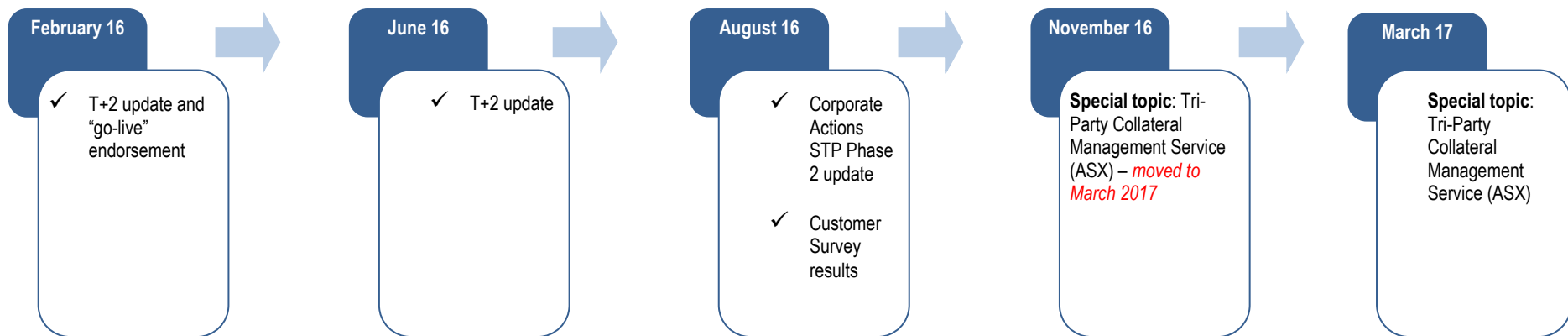
| Theme                                                         | Objectives                                                                            | Possible topics for discussion / agenda items          | Description of topic                                                                                                                                                                                    |
|---------------------------------------------------------------|---------------------------------------------------------------------------------------|--------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>2. Participant Structure, Flexibility &amp; Efficiency</b> | To align ASX's participant access regime with its customers' evolving business models | a. Participant rule framework                          | ASX will continue to explore opportunities to harmonise and standardise the Operating Rules across markets and facilities as appropriate. ASX will continue to liaise with industry on key focus areas. |
|                                                               |                                                                                       | b. Developments on COFR review of Clearing competition | ASX will update the Committee on any developments on the Council of Financial Regulators Review of Competition in Clearing Australian Cash Equities.                                                    |
|                                                               |                                                                                       |                                                        |                                                                                                                                                                                                         |
|                                                               |                                                                                       |                                                        |                                                                                                                                                                                                         |

**Timing for Business Committee Consideration of Topics**



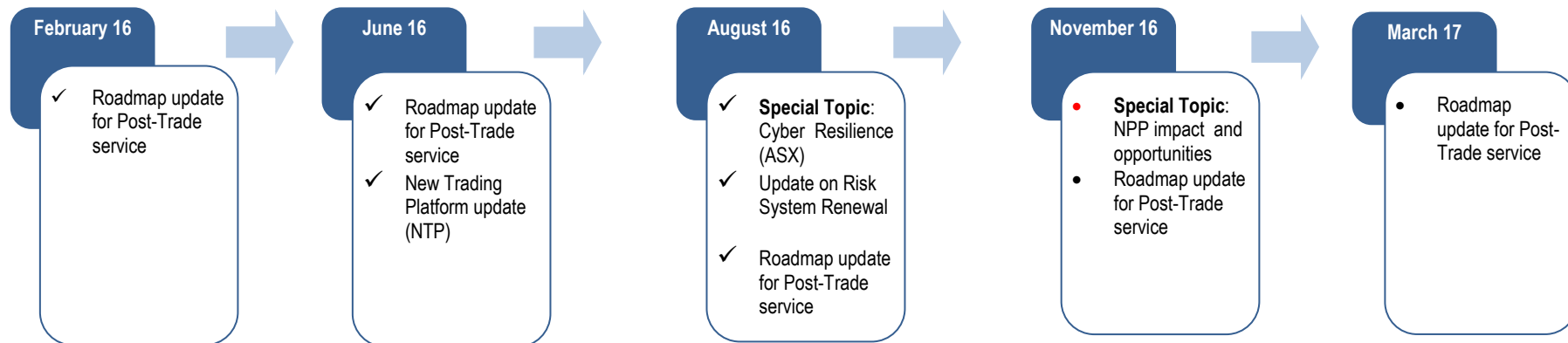
| Theme                 | Objectives                                                                   | Possible topics for discussion / agenda items             | Description of topic                                                                                                                                                                                                                                                                                               |
|-----------------------|------------------------------------------------------------------------------|-----------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 3. Service Innovation | To deliver global best practice cash market clearing and settlement services | a. Updates on the implementation of T+2 settlement cycle  | ASX will provide regular updates on the industry’s readiness to meet T+2 settlement by 1Q2016. The Committee will be provided with opportunities to provide feedback and endorsement where required.                                                                                                               |
|                       |                                                                              | b. Corporate Action straight through processing – Phase 2 | The ASX will present plans for future and continued enhancements in streamlined processes for corporate actions in context of CHES replacement plans. Principles which will deliver further streamlined process for the announcement, data capture and delivery (using ISO 20022) of corporate action information. |
|                       |                                                                              | c. Customer Service Survey Results <i>(New)</i>           | The ASX will provide results from the recent customer service survey and discuss the key areas of focus going forward.                                                                                                                                                                                             |
|                       |                                                                              |                                                           |                                                                                                                                                                                                                                                                                                                    |

Timing for Business Committee Consideration of Topics



| Theme                                                 | Objectives                                                                             | Possible topics for discussion / agenda items    | Description of topic                                                                                                                                                          |
|-------------------------------------------------------|----------------------------------------------------------------------------------------|--------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>4. Technology &amp; Infrastructure Enhancement</b> | To maintain and upgrade technology and infrastructure consistent with global standards | a. Roadmap for Post-Trade service infrastructure | ASX will provide an update on next steps following the recent announcement of ASX’s intention to explore the use of distributed ledger technology (DLT) for CHES replacement. |
|                                                       |                                                                                        | b. ASX Risk Systems Development                  | ASX will provide updates as required on the current Risk Systems development program.                                                                                         |
|                                                       |                                                                                        | c. New Trading Platform (NTP) update             | ASX will provide updates as required on the New Trading Platform replacement program.                                                                                         |
|                                                       |                                                                                        |                                                  |                                                                                                                                                                               |

**Timing for Business Committee Consideration of Topics**



## **BUSINESS COMMITTEE MEETING PAPER AGENDA ITEM 5B**

|                              |                                                                                                                                              |
|------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Topic</b>                 | <b>Minutes from 31 August 2016 meeting</b>                                                                                                   |
| <b>Date of the Meeting</b>   | 1 December 2016                                                                                                                              |
| <b>Purpose of this paper</b> | To provide Business Committee members with a copy of the minutes and Business Committee report to the Forum from the 31 August 2016 meeting. |
| <b>Action required</b>       | To approve the minutes and report to the Forum from the 31 August 2016 meeting.                                                              |

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Draft minutes and the draft report to the Forum from the 31 August 2016 Business Committee meeting were emailed to all members of the Business Committee on 12 September 2016 for comments by 19 September 2016.

There were no changes to the draft minutes or report suggested by Business Committee members.

The Business Committee minutes were signed by the Chair on 21 September 2016.

A copy of the minutes and report to the Forum from the 31 August 2016 meeting are provided in Attachments A and B.

### **ATTACHMENTS**

Attachment A – Minutes from the 31 August 2016 Meeting

Attachment B – Business Committee Report to the Forum from the 31 August 2016 Meeting



# MINUTES

## BUSINESS COMMITTEE MEETING

| Date                      | Time             | Location                                        |
|---------------------------|------------------|-------------------------------------------------|
| Wednesday, 31 August 2016 | 12.00pm – 1.48pm | ASX Offices – Level 1, 20 Bridge Street, Sydney |

| Agenda Item |                                                                                                                          |
|-------------|--------------------------------------------------------------------------------------------------------------------------|
| 1.          | <b>Lunch</b>                                                                                                             |
| 2.          | <b>Service Performance</b><br>a) Operating Performance Report                                                            |
| 3.          | <b>Customer Service Survey Results</b>                                                                                   |
| 4.          | <b>Management Accounts for Cash Market Clearing &amp; Settlement</b>                                                     |
| 5.          | <b>Business Matters</b><br>a) Roadmap for post-trade service infrastructure<br>b) Cyber Resilience                       |
| 6.          | <b>Regulatory Updates</b><br>a) Minimum Core Capital requirement, Collateral Haircuts and ETO Initial Margins            |
| 7.          | <b>Administration</b><br>a) Forward work program updated<br>b) Minutes from the 15 June 2016 meeting<br>c) Other matters |
| 8.          | <b>Next Meeting</b><br>The next meeting of the Business Committee is scheduled for Wednesday, 30 November 2016.          |

**NEXT MEETING:** Wednesday, 30 November 2016



| <b>Members</b>                 |                                                         |                                                                 |
|--------------------------------|---------------------------------------------------------|-----------------------------------------------------------------|
| <b>Company</b>                 | <b>Name</b>                                             | <b>Job Title</b>                                                |
| ABN AMRO Clearing              | Mr Sean Lawrence                                        | Managing Director                                               |
| ANZ                            | Mr Andrew Kourdin<br>(as delegate for Peter Mullin)     | Head of Execution Assurance and Middle Office                   |
| ASX                            | Mr Peter Hiom                                           | Business Committee Chair<br>Deputy CEO, ASX                     |
| Bank of America Merrill Lynch  | Mr Rhys Cahill                                          | Global Markets COO                                              |
| BNP Paribas                    | Mr Luc Renard<br>(as delegate for David Braga)          | Head of Security Services                                       |
| Chi-X Australia                | Mr Mike Aikins                                          | Chief Operating Officer                                         |
| Citi                           | Mr Miles O'Connor                                       | Director, Direct Custody & Clearing Securities & Funds Services |
| Commonwealth Bank of Australia | Mr Sheridan Thompson                                    | Head of Strategic Development, CommSec                          |
| Credit Suisse                  | Mr Matthew Gallagher<br>(as delegate for Andrew Farran) | Head of Operations                                              |
| Deutsche Bank AG               | Mr Russell Deal                                         | Chief Operating Officer                                         |
| Goldman Sachs                  | Mr Jeremy Follett                                       | Executive Director Operations                                   |
| HSBC                           | Mr Peter Snodgrass<br>(as delegate for Andrew Bastow)   | Head of Direct Custody & Clearing, HSBC Securities Services     |
| J.P. Morgan                    | Mr Suneet Jain                                          | Sales Business Manager, Markets & Investor Services             |
| Macquarie Group                | Mr James Indge                                          | Cash Equities Business Manager                                  |
| Morgans                        | Mr Peter Chisholm                                       | Chief Operating Officer                                         |
| Morgan Stanley                 | Mr Craig McGuire                                        | Head of Operations                                              |
| National Australia Bank        | Mr Greg Bowrey<br>(as delegate for Nathan Walsh)        | General Manager, Self-Directed Wealth Products & Markets        |
| Pershing Securities            | Mr Rob Forbes                                           | Chief Executive Officer                                         |





|                                       |                   |                                             |
|---------------------------------------|-------------------|---------------------------------------------|
| Stockbrokers Association of Australia | Mr Andrew Green   | Chief Executive Officer                     |
| Sydney Stock Exchange Limited         | Mr David Lawrence | Chief Operating Officer & Company Secretary |
| UBS                                   | Mr Conor Foley    | Chief Operating Officer                     |

| Apologies              |                 |                          |
|------------------------|-----------------|--------------------------|
| Company                | Name            | Job Title                |
| NSX                    | Mr Tom Price    | Director                 |
| Bell Potter Securities | Mr Dean Surkitt | Managing Director Retail |

| ASX Management      |                                                                 |
|---------------------|-----------------------------------------------------------------|
| Name                | Job Title                                                       |
| Ms Amanda Harkness  | Group General Counsel & Company Secretary                       |
| Mr Tim Hogben       | Group Executive, Operations                                     |
| Mr Alan Bardwell    | Chief Risk Officer (Item 6(a))                                  |
| Ms Eloise Wett      | Executive General Manager, Customer Experience                  |
| Mr Cliff Richards   | General Manager, Equity Post Trade Services                     |
| Mr Stephen Hammon   | General Manager, Finance (Item 4)                               |
| Mr Rodd Kingham     | Senior Manager, Equity Post Trade Services                      |
| Mr Michael Bradwell | Senior Legal Counsel                                            |
| Mr Daryn Wedd       | General Manager, Technology Security and Governance (Item 5(b)) |
| Mr Tristan Geering  | Chief Information Security Officer (Item 5(b))                  |



## **AGENDA ITEM 1: LUNCH**

The Chair formally opened the meeting at 12.15pm.

The Chair noted two apologies and welcomed Members and delegates.

## **AGENDA ITEM 2: SERVICE PERFORMANCE**

### **a. Operating Performance Report**

The ASX Group Executive, Operations spoke to the agenda paper noting that the metrics for the September quarter are only for the period up to 29 July 2016 and flagged certain metrics including:

- Trading on ASX and Chi-X is in line with the previous quarter and trading on NSX and SSX was slightly down on the previous quarter
- CHES and TAS availability was 100%
- Percentage novated was around 72% (balance trade reports)
- Netting 99.93% on volume; 62% on value

The Group Executive, Operations also reported that since the change to the batch settlement cut-off time to 11.30am there have been no requests for extension to settlement cut-off.

There were no questions from Members on the metrics.

The Group Executive, Operations also reported on the following matters:

- Brexit decision – there were a record number of equity trades on the day (1.55m) of the Brexit announcement and despite the increase, all systems and processes functioned as normal. Additional margin was called intra-day and all was paid on time. A record number of settlements (158,008) settled two business days later and the systems all worked well. The efficiency of netting was highlighted with the 1.55m trades resulting in 18,630 scheduled net settlements. Fail rates were very low.
- Annual assurance reports – these reports which are prepared by PwC were issued in August reporting on ASX's systems. PwC's opinion was that there were no material issues.
- CHES Release 9 – was released on 13 August 2016. That Release included 20 new messages for mFund. No issues have been identified with that Release.

No questions or issues were raised by Members.

## **AGENDA ITEM 3: CUSTOMER SERVICE SURVEY RESULTS**

The ASX Executive General Manager of Customer Experience spoke to the agenda paper noting that this was the second ASX customer service survey and that it had be conducted in two parts: an interview with customers and an online survey.



The EGM Customer Experience noted that the results of the survey included an acknowledgement by customers that ASX has made improvements but that there is areas where more work is needed. The EGM Customer Experience noted the areas where the feedback was that more work is needed and discussed the steps that ASX was taking to improve customer service.

In response to a question from a Member regarding what ASX's model for customer service is it was noted that this is determined by the type of customer. The Chair noted that a particular focus for ASX management is 1:1 engagement with customers to find out what customers want in terms of service and to identify current issues and future issues.

#### **AGENDA ITEM 4: MANAGEMENT ACCOUNTS FOR CASH MARKET CLEARING & SETTLEMENT**

The ASX General Manager Finance reported to the meeting in relation to the Cash Market Clearing Management Income Statement and the Cash Market Settlement Management Income Statement for the year ended 30 June 2016 noting that the statements have been audited by PwC and that the statements had been prepared using the same methodology as the previous year.

The General Manager Finance noted that the effect of the cut in clearing fees charged by ASX will be seen in the next Cash Market Clearing Management Income Statement.

There were no questions from Members on this item.

#### **AGENDA ITEM 5: BUSINESS MATTERS**

##### **a. Roadmap for post-trade service infrastructure**

The ASX General Manager, Equity Post Trade Services spoke to the agenda item noting the updates in relation to ASX's investigation of distributed ledger technology (DLT) that had been provided at the earlier Business Committee meetings.

The General Manager, Equity Post Trade Services reported on the interactions by ASX with stakeholders that are to occur over the next 5-6 months including:

- software demonstrations by ASX of DLT at ASX's premises commencing in the week following the Business Committee meeting. The demonstration will be a different demonstration to the one that followed the previous Business Committee meeting and will be based on 4-5 core things that CHES does including performance of clearing and settlement. Learnings from participant failures have been factored in to enhance the system. In response to a question from a Member it was confirmed that Members would be invited to the demonstration. The intention being to invite 2-3 firms at a time with about 5 people from each firm attending with ideally a cross section of representatives from within a firm. In response to a question from a Member it was reported that ASX would not be presenting the demonstrations on the internet as this had not proved to be feasible.
- the release of a consultation paper in the fortnight after the meeting inviting responses from stakeholders. The consultation paper will explain the current processes in CHES and the design philosophy of the proposed DLT based solution.
- technical workshops in about 5-6 months' time seeking input from stakeholders.



The General Manager, Equity Post Trade Services also reported that ASX was investigating the possible use of international standards messaging in the proposed DLT solution. It was also reported that the ASX Senior Manager, Equity Post Trade Services would lead the stakeholder engagement which would include the use of webinars, immersions and workshops.

The General Manager, Equity Post Trade Services reported that by the end of 2017 ASX expected to have the software developed to a stage to be able to determine whether it could replace CHES. It was also reported that there was no firm time-frame for implementation however stakeholders will be engaged on the most appropriate timing for a transition to implementation. It was noted that if DLT was determined not to be an appropriate replacement for CHES, the learnings from exploration of DLT could be used for an alternative replacement of CHES.

A Member noted that for some participants, budgeting starts in August each year and asked whether participants could have a preliminary view from ASX in August 2017 to enable budgeting. The Chair reported that ASX would be able to provide an update on progress in August 2017.

#### **b. Cyber Resilience**

The ASX General Manager, Technology Security and Governance and the ASX Chief Information Security Officer spoke to the agenda paper including noting the types of information that ASX is holding, strategies that ASX employs to protect data and recent trends in cyber threats including malware, phishing, denial of service attacks, social engineering and ransomware.

It was also reported that ASX uses a variety of controls in a defence in depth strategy to mitigate the cyber risk, including the use of the private ASX Net network for much of the key trading, clearing and settlement transactional traffic. It was also noted that the ASX is assisting the Federal Government in undertaking a cyber security 'health check' of the top ASX 100 entities which will go to the audit committee chairs of those organisations with the aim of raising awareness of cyber risk at the Board level.

The Chief Information Security Officer reported that a key element of cyber resilience is having a good relationship and methodology with business partners which enables continued working together if there is a cyber-attack. It was also reported that it is better to understand across the industry what types of attacks are happening. The meeting then discussed the benefit of sharing information regarding cyber-attacks between organisations as cyber-attacks are often repeated at other organisation and in different regions. A Member reiterated the benefit of sharing information between organisations and another Member recommended that a regular forum be established for the chief security executives of member organisations to share information regarding recent incidents and trends in cyber-security [**AGREED ACTION 1**].

### **AGENDA ITEM 6: REGULATORY UPDATES**

#### **Minimum Core Capital requirement, Collateral Haircuts and ETO Initial Margins**

The ASX Chief Risk Officer provided an update in relation to the minimum core capital consultation, collateral haircut changes and ETO margin enhancements including noting that:



- ASX will consolidate the feedback received from the minimum core capital consultation and then go back to the market.
- The liquidity management guidance note had been issued on the date of the meeting with an effective date of the end of February 2017.
- Collateral haircut changes have been approved by the Board including a move to tiered levels. There is a notice coming out in the week after the meeting with implementation in mid-September 2016.
- Will come back to the Committee later in the year on the ETOs initial margins liquidity and concentration add ons methodology.
- Sentinel risk management system – the current focus is on ASX Clear Futures. Won't include ASX Clear until 2018.

There were no questions on this item.

**AGENDA ITEM 7: ADMINISTRATION**

**a. Forward work program updated**

The Chair invited Members to contact the Senior Manager, Equity Post Trade Services if they had suggested items for the forward work program.

**b. Minutes from the 15 June 2016 meeting**

The Chair noted the minutes from the 15 June 2016 meeting and invited comments. As there were no comments, the Chair noted that the minutes were approved.

**c. Other matters**

There were no other matters.

**NEXT MEETING**

The next meeting will be held on Wednesday, 30 November 2016. The Chair proposed that the meeting be held later in the afternoon on that date.

As there was no further business discussed, the meeting closed at 1.48pm.

Signed as a correct record of the meeting.

Chairman

21/9/16

Date



# BUSINESS COMMITTEE REPORT TO THE FORUM

## BUSINESS COMMITTEE MEETING

At its 31 August 2016 meeting, the Business Committee was updated on:

- Record level of equities trading activity that occurred on the day of the Brexit announcement. Those trades resulted in a record level of settlement activity – ASX's systems and processes functioned as normal
- Results of the second ASX customer service survey
- Cash Market Clearing and Cash Market Settlement Management Income Statements for the year ended 30 June 2016
- Roadmap and upcoming interactions with stakeholders on ASX's exploration of the potential use of distributed ledger technology to replace CHES to include software demonstrations, release of a consultation paper and workshops.
- ASX's cyber security controls and recent trends in cyber attacks
- the minimum core capital consultation, collateral haircut changes and ETO margin enhancements

## KEY RECOMMENDATIONS

There were no recommendations arising from the meeting.

## KEY ISSUES DISCUSSED

- ASX's ongoing exploration of the potential use of distributed ledger technology for CHES replacement.
- Cyber resilience and the importance of information sharing between organisations regarding cyber-attacks as a means of building cyber resilience.

## AGREED ACTIONS

1. An information sharing forum be established for the chief security executives of Business Committee member organisations and other market participants to share information regarding recent incidents and trends in cyber-security.

## BUSINESS COMMITTEE MEETING PAPER AGENDA ITEM 5C

|                              |                                                                             |
|------------------------------|-----------------------------------------------------------------------------|
| <b>Topic</b>                 | <b>2017 Proposed Business Committee Dates</b>                               |
| <b>Date of the Meeting</b>   | 1 December 2016                                                             |
| <b>Purpose of this paper</b> | To provide Business Committee members with the proposed 2017 meeting dates. |
| <b>Action required</b>       | To note proposed dates.                                                     |

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The proposed 2017 Business Committee meeting dates are set out below.

| <b>Business Committee Meeting Dates</b>              |
|------------------------------------------------------|
| Thursday, 2 March 2017<br>Commencing at 12.00pm      |
| Thursday, 13 June 2017<br>Commencing at 12.00pm      |
| Wednesday, 6 September 2017<br>Commencing at 12.00pm |
| Thursday, 30 November 2017<br>Commencing at 4.00pm   |

Additional meetings may be called if there is a change in the market structure or policy.

Members are asked to contact the Business Committee Chair by email at [bc.chair@asx.com.au](mailto:bc.chair@asx.com.au) if there are any issues with the proposed dates.