

Diagram 1: ASX Group Structure



ASX CHESS Replacement

Much has already been stated about the CHESS Replacement Project (CRP), including the eventual closure of the project following 6 years of development and planning. Early on during the proof-of-concept phase, the hype generated by ASXL centred on the selected distributed ledger technology (DLT) as the panacea for the market. The market itself questioned ASXL's motive from the outset, noting that the CRP was primarily driven by ASXL's own business case and pursuit of commercial opportunities to extend further into ancillary and new products and services. Examples include data products, share registry functions and portfolio related services across issuers, investors and new customer groups.

A variety of market stakeholders have stated that the CRP business case has resulted in significant costs to industry with unclear benefits to the wider market. This is well documented, including ballpark costs in excess of \$100 million to industry which was sunk into the now abandoned DLT based CRP solution. NSXA will not reiterate previously stated shortcomings of the CRP in great detail, rather, certain key areas have been mentioned.

Much of the failings of the project can be attributed to the policy of maintaining a monopoly infrastructure run by a commercial enterprise. ASX has significant incentive to be the only service provider to everyone. This has the effect of crowding out potential entrants and startups wishing to compete in various areas which have influenced, over time, the implementation of legislation and regulator views as to contestability¹ of clearing and settlement services. NSXA submits that these failings have revealed more deep-seated problems and that there has certainly been legislative bias toward the incumbent at the expense of others. Meaning when a major project fails and there is no Plan B or competitors that can provide an alternative service, then government and the market bear the cost.

Project Governance

ASXL created a governance framework for CRP that was a work in progress. Governance continued to be developed as questions were asked through the quarterly ASX Business Committee meetings, various working groups and the technical committee. In the end, independent reports and assurance exercises were carried out by a number of professional firms to resemble a well thought out governance framework.

Consultation

ASXL set the tone early on in the CRP kick-off stage by creating a number of separate 'working groups' and restricted access to the technical committee. This allowed ASXL to control the content and discussions within each Working Group and segregate attendees, forcing representatives to circle back with others to obtain a fuller picture of what was being designed. Further, documentation to support important discussions was frequently provided with insufficient time for pre-reading and draft minutes and action items were often circulated well after the meetings took place.

This created an environment where confirmation bias could prevail to garner support for certain requirements driven by ASXL to be embedded into the design i.e. the new rails could continue to be laid along a preconceived track without, necessarily, turning back.

The consultation lacked meaningful collaboration expected for the replacement of a critical central market infrastructure.

Transparency

The project governance framework and consultation approach outlined above resulted in an inconsistent level of transparency across a number of key aspects of the project. Communication on the sequence of project delays is a prime example.

Pricing

Market stakeholders posed questions about pricing during the course of CRP. NSXA understands that the Australian Competition and Consumer Commission (ACCC) was involved in carrying out a review of proposed pricing.

¹ https://cdn.treasury.gov.au/uploads/sites/1/2017/06/C2015-007_CFR-ConclusionsPaper.pdf



ASXL countered by introducing a new pricing framework for CHESS 'Issuer Services' which introduced a monthly CHESS access charge for all issuers to protect its current revenue from issuers and positioned outside of clearing and settlement. At the same time, ASXL was able to protect its CHESS Holding Statement revenue by excluding these transactions from the monthly subscription fees. NSXA's current understanding is that ACCC is no longer reviewing the pricing due to the failure of CRP to be implemented.

NSXA is of the view that the current monopoly-based pricing for clearing, settlement and subregister access is considered and reviewed sooner rather than later as there is a need for the legislation to encompass fair pricing.

For example, there is no concept of a wholesale versus retail service or white labelling of the services by ASXC and ASXS. ASXS charges issuers full retail price on a monthly subscription basis. To improve this aspect, the Committee could explore other monopoly schemes for fair access such as the NBN Co pricing structure. NBN Co has no competitors but it offers a monopolistic wholesale service to telecoms providers at a wholesale price and market operators can then compete amongst themselves, on an efficiency basis, as to what price is charged to the end user. Further ASXC and ASXS also charges the market operator for access to the services. This means that the market operator has to recoup this cost from its issuers making it more expensive for NSXA companies to access the same services that ASX issuers do. Pricing should always be on a fair and equitable basis, especially when there is only one provider of that service in Australia.

In the US, these central clearing, settlement and depository (akin to subregister) functions are performed by The Depository Trust and Clearing Corporation (DTCC). DTCC although a monopoly, is a not-for-profit organisation which services all market operator exchanges in the US for the betterment of the entire market.

There should be regulatory oversight of the current incumbent and the current structure of pricing for clearing, settlement and subregister access. This should happen now under the current monopoly services provided by ASXC and ASXS across clearing, settlement and subregister services.

If a competitor is to emerge, pricing should be considered again in the context of the holistic requirements from an incumbent and the services which are provided, that is, regulation should not be softened if what is presented is not alike.

CHESS Replacement Project Mark 2 (CRP2)

NSXA believes it is too soon to comment on ASXL's second attempt at the project. Initial observations on a lack of a concerted effort to learn from CRP was evident when ASXL's starting position on the business requirements was the 'Day 1' scope for CRP. Given 6 years has passed, arguably it would make sense to validate these requirements. As an example, market operators are seeking a clear commitment to interoperability where more than one clearing house and/or a settlement facility was allowed to co-exist with CRP2. It is difficult to conceive that ASXL had not considered this as a core requirement prior to being prompted by representatives of the CRP2 Technical Committee.

ASXL's Market Power: Case studies

From NSXA's own experience, the ultimate failure of the CRP represents the monopolistic mindset and position of market power ASXL exerts which NSXA has experienced in trying to compete for corporate listings. In this context, NSXA has drawn on a number of case studies to demonstrate how ASXL wields its market power to preserve its dominant position and keep competition at bay. Ultimately, had the CRP succeeded in the first instance NSXA believes that ASXL would have significantly increased its market power and cemented its central position by providing new and ancillary services at the expense of any advancement in competition and ongoing innovation by the market as a whole.

Many of these new 'initiatives' by ASXL would be driven through the CHESS subregister which incorporates the creation of issuer records and its issued securities and their shareholders through their Holder Identification Numbers (HINs). The notion of the subregister is a vital aspect and must be collectively incorporated under the banner of "clearing and settlement" when legislation on competition and controls on related pricing is pursued by Government. It should be highlighted that CHESS subregister access and services are provided through ASXS (ASX Settlement Pty Limited). ASXL has successfully masked the subregister aspect under "Issuer Services". This stifles competition and has allowed ASXL to leverage its market power. Hence, NSXA believes that the narrative moving forward needs to be expanded and become *clearing, settlement & subregister access and/or services*.

Trade Acceptance Service (TAS)



ASXL has not provided transparent and non-discriminatory pricing and access to the clearing and settlement services and ASXL has used many delaying techniques over the years to either slow or prevent access and/or entry. NSXA's experience in gaining access to TAS is one example.. The process for NSXA to gain access to the TAS took a total of *three and a half years*; for a service that was put in place for orderly access to market operators following its deployment for Chi-X (now CBOE). Throughout the process, ASXL delayed NSXA through a series of blocks:

- reviewing annual fees;
- the introduction of a 'clearability assessment' and an 'operations assessment' to ensure that NSXA stock could be cleared, although the same types of stock were already being cleared for CBOE and ASXL;
- requesting a supplementary application from NSXA incorporating the previously mentioned new assessments although NSXA listed securities were the same classification of securities as ASX listed stocks; and
- the proposed introduction of bifurcation, which required ASIC and the RBA's involvement and led to ASIC's *Open Access Principles for licensed listing markets seeking access to ASX Clear*² – this was the catalyst to obtaining the final approval for TAS access by NSXA.

Diagram 2 below provide a summary of NSXA's journey to obtain access to TAS.

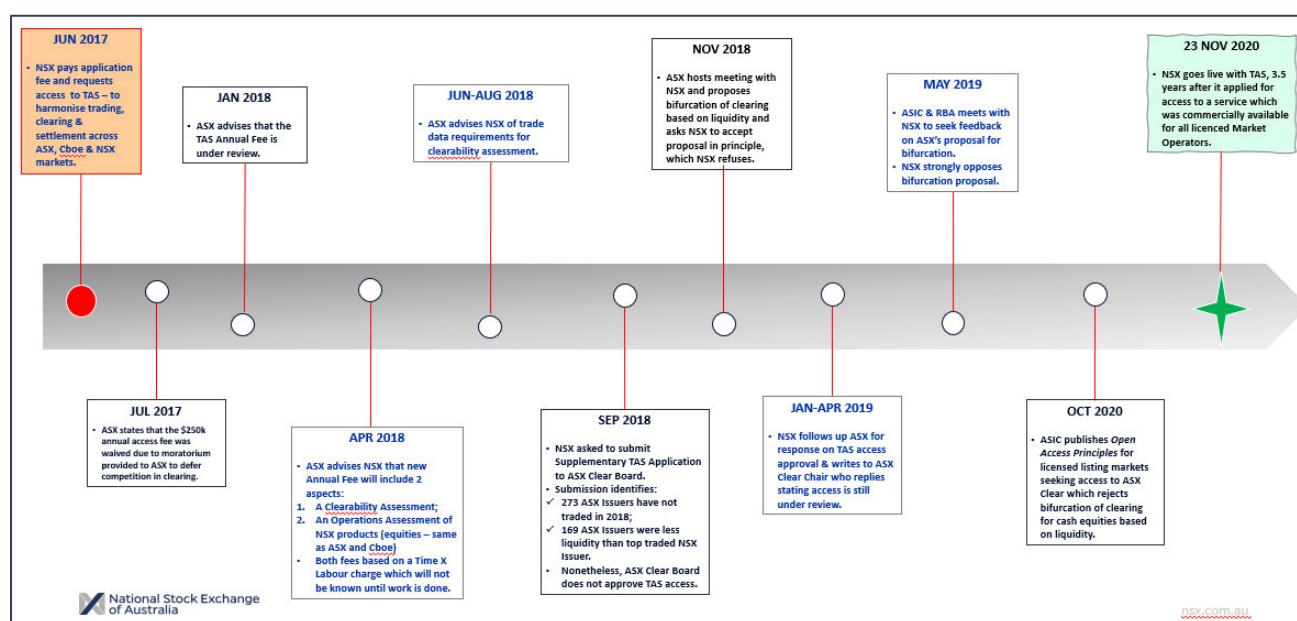


Diagram 2: Timeline of access to TAS to harmonise clearing and settlement across ASXL, CBOE and NSXA markets

On 23 November 2020, NSXA joined Chi-X (now CBOE) as a user of TAS. This resulted in harmonised clearing and settlement processes for participants across all three markets. This is shown in *Diagram 3* below.

² <https://www.cfr.gov.au/publications/policy-statements-and-other-reports/2020/application-of-the-regulatory-expectations/>

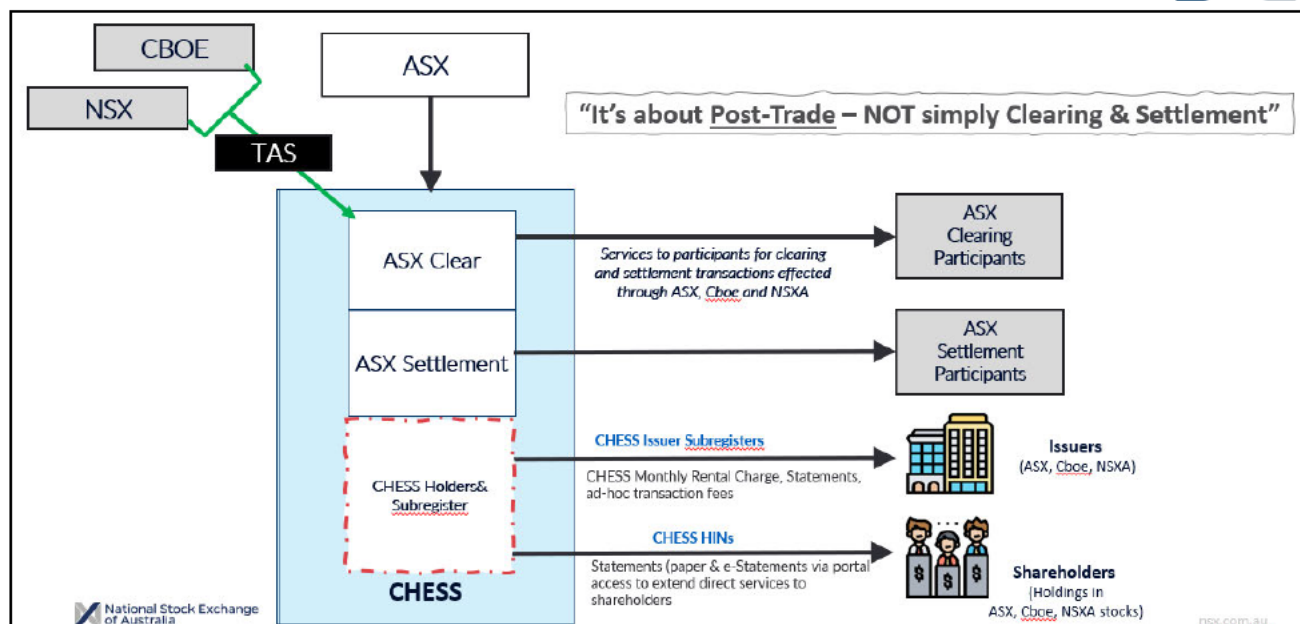


Diagram 3: Market Operator Access to CHESS through Trade Acceptance Service (TAS)

Issuer Reference Data and Issuer Subregister Services

ASXL is currently the sole 'agent' designated by the International Association of National Numbering Agencies to issue ISIN (International Securities Identification Numbering) codes for Australia. The ISIN is linked to the ticker (stock) code of the company (e.g. BHP). This is an important and sticky function as the ISIN and ticker are the key system and business identifiers of the issuer record and another monopoly role performed by ASXL. NSXA believes that the issuance of ISINs and ticker codes should be decentralised as is commonly the case overseas.

Diagram 4 below demonstrates the extent of the commercial relationship that ASXL imposes on NSXA issuers and their shareholders through the control of Holder Identification Numbers (HINs).

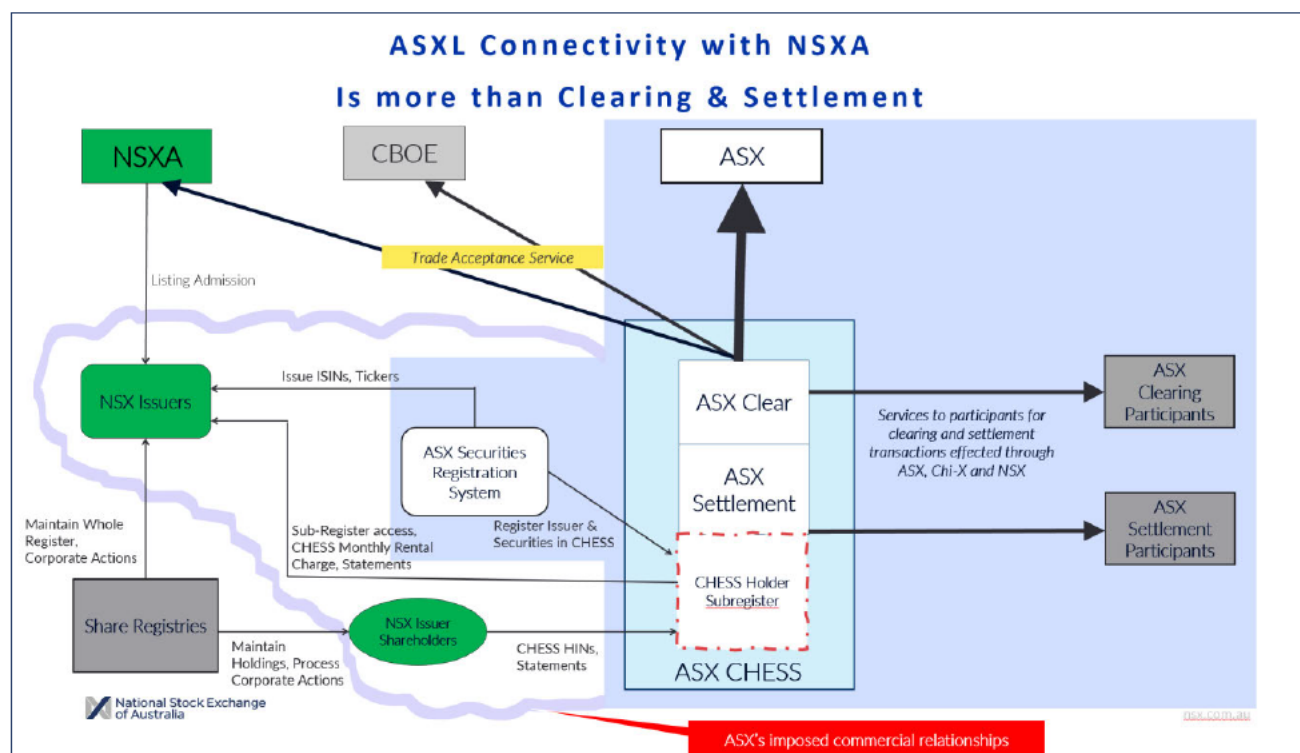


Diagram 4: ASXL Footprint is far more than Clearing and Settlement



Fees for clearing, settlement and subregister access under the guise of Issuer Services

Once an NSXA issuer is listed, ASXS is involved with the sub-register access, charges a CHES Monthly rental fee to NSXA issuers directly and separately charges issuers for the issuance of CHES Holding Statements to shareholders. (Refer to *Diagram 4* above).

CHES Holding Statements are prominently ASX-branded often leading to confusion for shareholders of NSXA issuers. *Diagram 5* below shows the proposed branding for CHES Statements which NSXA disputed on the basis that the branding on the statement was confusing for investors and it was unclear as to which exchange the security is listed on. *Diagram 6* below shows the final version of the CHES Statements following a few iterations proposed by ASXL. Although improved, NSXA notes that the ASX branding remains dominant by being placed on the left drawing attention initially to ASX. The use of the generic ASX Group logo adds to the confusion.



Diagram 5: Proposed branding on CHES Statements to NSXA issuers

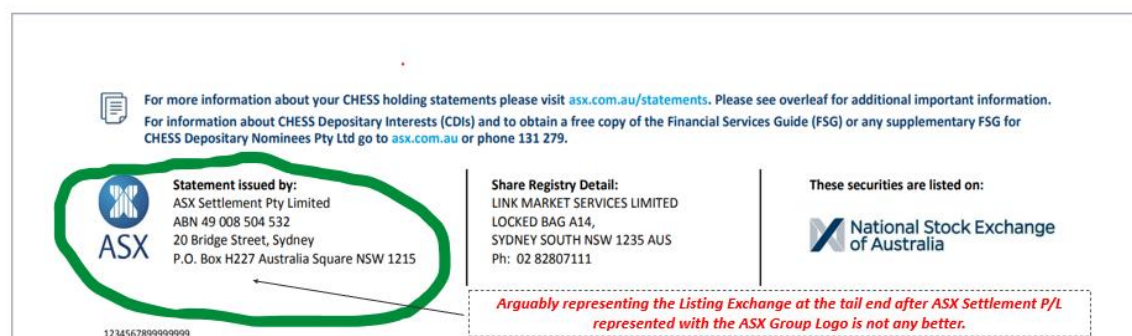




Diagram 6: Final version of CHES Statements

The monthly ASX-branded invoices prominently positions ASXL to extend its commercial relationship with NSXA issuers. NSXA issuers are charged a monthly subscription fee by ASX Settlement Pty Limited. Previously, NSXA was charged a total access fee on behalf of all NSXA issuers with a single invoice to NSXA. This allowed NSXA to maintain a better and more visible relationship with its issuers. With the new arrangement, ASXL now has a direct, regular and visible relationship with the NSXA issuers.

In addition, should an issuer be in dispute, for example over invoicing, ASXL has the power to suspend services, which impedes on NSXA's power and obligation to administer its Listing Rules. Again, there should be some form of separation here to ensure competition is enabled and achieved.



 ASX Settlement Pty Ltd ABN 49 008 504 532 PO Box H224 Australia Square Sydney NSW 1215 Enquiries: Accounts Receivable Phone: 612 9227 0703 Fax: 612 9227 0553 Email: ar@asx.com.au		TAX INVOICE	
 Sydney NSW 2000 Australia		Invoice Number Invoice Date Customer Number Customer ABN Due Date 31/08/2022	


Product Code	Description	Quantity	Unit Price	Unit	Line Amount (Excl GST)	GST	Amount Due (Incl GST)
04900256	Chess Charges for UIC:  Subscription fee - Corporate Issuers <i>For issuer Code: A2A</i>	1.00	125.290	EA	125.29	12.53	137.82
Special Notes: Details on fees and charges – refer to fee schedules: https://www.asxonline.com/public/documents/asx-schedule-of-fees.html Issuer Services fee changes effective 1 July 22: https://www2.asx.com.au/issuers/issuer-services/our-services?#new							

Diagram 7: ASXS's Monthly invoices to NSXA issuers

Further, the whole market questions the need for the duplication of CHESS Holding Statements which is a function that the share registry also fulfils. This could possibly have been solved by making the issuance of CHESS Holding Statements optional based on the consent of CHESS HIN shareholders supported with a change to the ASX settlement rules. This demonstrates the ASX Group's reluctance to place the betterment of the market ahead of its commercial interests driven by the revenue derived from CHESS Holding Statements and related transactions (CHESS messages).

NSXA suggests a separation of these items from the Clearing and Settlement Facility:

- ISIN and ticker codes – decentralisation of this ancillary reference data function that feeds CSFs and the subregister, and;
- Holder Identification Numbers (HINs) – decentralisation of data ownership and access driven by HIN owners' consent (consumer data rights).

Holistic Approach to Competition

NSXA is of the opinion that there are more aspects to competition than just the CSF licence. NSXA contends that the components that make up the licence are all subject to the past view of what ASXL had in place when the licence regime came into being. That means other operators have been locked out or dissuaded from competing in these areas. Regulators (as The Agencies in the 2015 CFR report) have expressed doubt that committed competitors would emerge due to a notion of weak contestability.³ NSXA submits that Clearing and Settlement is contestable and there are overseas jurisdictions inclusive of multiple facilities that interoperate, for example Target2-Securities in Europe.

³ https://cdn.treasury.gov.au/uploads/sites/1/2017/06/C2015-007_CFR-ConclusionsPaper.pdf

(page 4 – bullet point 2 and page 49)



For example, NSXA may wish to pursue a clearing and settlement solution to service its own issuers and have no desire to offer services to ASXL or CBOE issuers. This offering may even bypass a CCP clearing function but rely on access to HIN records to facilitate a streamlined settlement and subregister service for its issuers and their shareholders. Therefore, NSXA proposes that a holistic view of competition needs to be considered to promote and enable innovation to prosper. A possible solution is to consider the issuance of tiered CSF licences and/or the inclusion of licence conditions. This may include certain thresholds incorporating aspects such as scale, complexity, transaction volumes and values.

NSXA proposes that *Principles of Competition* are introduced which holds ASX Clear and ASX Settlement accountable to the spirit of open access and the intent of the legislation to follow. This may build upon ASIC's *Open Access Principles for licensed listing markets seeking access to ASX Clear*. Although such principles may not have regulatory powers of enforcement they can act as a severe deterrent and promote adherence through visibility of any breaches.

Conclusion

NSXA has made this submission from a unique position as a competing market operator of ASX and as a customer of ASXC and ASXS. The CHES Replacement Project raised many questions around project governance, consultation, transparency and pricing.. The market questioned ASXL's motive from the outset, noting that the CRP was primarily driven by ASXL's own business case and pursuit of commercial opportunities to extend further into ancillary and new products and services.

From NSXA's own experience, the ultimate failure of the CRP represents the monopolistic mindset and position of market power that the ASXL exerts and which NSXA has experienced in trying to compete for corporate listings. In this context, NSXA outlined a number of case studies to demonstrate how ASXL wields its market power to preserve its dominant position and keep competition at bay. Ultimately, had the CRP succeeded NSXA believes that ASXL would have significantly increased its market power and cemented its central position by providing new and ancillary services at the expense of any advancement in open access, competition and ongoing innovation by the market as a whole.

Although it is too soon to comment on the ASXL's second attempt at the CHES replacement project, the initial failure has raised a number of well documented issues. It has also provided regulators and Government with an opportunity to deal with the key issue arguably arising from ASXL's non provision of transparent and non-discriminatory pricing of and access to clearing and settlement services – showcased by NSXA's 3.5 year timeline to access TAS. Other related examples include pricing, issuer reference data, billing and access to CHES as outlined in this submission. NSXA believes that Government should act now to remove anomalies and reduce ASXL's current market power. This may be assisted by developing *Principles of Competition* which can introduce such concepts as consent driven access to HINs (a conceptual extension of consumer data rights), separation of issuer reference data (ISINs and tickers) as examples.

It is important that ASXL is not given a free rein to technically design a replacement system that protects or even enhances these current monopoly 'functions and features' ahead of legislative change.

On behalf of the Board of National Stock Exchange of Australia

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