



ASIC
Australian Securities &
Investments Commission

PJC Corporations and Financial Services Inquiry into the CHESSE Replacement Project

Further submission by the Australian Securities and Investments Commission

22 September 2023

Contents

Overview	3
A Recent developments	5
Introduction	5
Establishment of the Cash Equities Clearing and Settlement Advisory Group	5
Overview of the Competition in Clearing and Settlement Reforms ...	6
B Responses to Cboe’s Recommendations Paper	9
Introduction	9
Review of the National Guarantee Fund and extension of this to benefit all CCPs	9
Structural separation of ASX Clear and ASX Settlement	10
Consideration of the impact of the failed CHESSE Replacement Project on industry stakeholders	11
Establishment of rules to encourage effective competition	12
Charging for routing trade executions for clearing and settlement..	14
Operational standards	14
Key terms	16

Overview

1 The PJC has asked ASIC to respond to the recommendations in the *Cboe Australia Recommendations paper for the identification of barriers to, and opportunities for the support of, competition within Australia's post-trade environment* (Recommendations Paper), dated 28 July 2023 and submitted to the PJC by Cboe Australia Pty Ltd (Cboe). In this submission, ASIC provides early views on the recommendations put forward by Cboe and explains how the Competition in Clearing and Settlement Reforms included in Schedule 3 of the *Treasury Laws Amendment (2023 Measures No. 3) Act 2023* (the Act) could potentially be used to address many of the underlying concerns raised in the Recommendations Paper.

Note: The Treasury Laws Amendment (2023 Measures No. 3) Bill 2023 passed both Houses of Parliament on 6 September 2023 and received royal assent on 20 September 2023.

2 ASIC notes the Recommendations Paper discusses complex technical matters and proposals that would require careful consideration by ASIC and the RBA (the regulators), and broad stakeholder consultation to appropriately consider the perspectives and views of other relevant stakeholders, including whether the recommendations are in the best interests of the market.

3 ASIC is committed to using its new powers on a timely basis to facilitate outcomes that are consistent with those expected in a competitive market for clearing and settlement (CS) services. This includes ensuring that competition, should it emerge, occurs in a safe and effective manner. The policy objective of facilitating competition does not, however, take precedence over the need to ensure that financial stability and effective market functioning are not adversely affected.

4 Any consideration by ASIC of the technical matters raised by Cboe (and other matters which could arise if a competing central counterparty (CCP) emerged) would be done in consultation with the RBA. ASIC, in consultation with the RBA and ACCC, would be informed by lessons learned internationally on competition in clearing, the requirements of the Australian market, and the proposed business model of an entrant CCP.

5 ASIC will seek to ensure that the rules strike an appropriate balance between regulatory benefits and costs. Setting detailed requirements in relation to safe and effective competition ahead of the emergence of an entrant CCP may result in unnecessary costs being incurred by industry should a competing CCP not emerge. However, the technological design of ASX's CS infrastructure should not raise barriers to interoperability or access to

settlement arrangements by a competing CCP. Whether competition does emerge should ultimately be a matter for the market to determine.

- 6 ASIC will continue to use all currently available and future regulatory measures to ensure ASX complies with its licence obligations and meets regulatory expectations.

A Recent developments

Key points

At ASIC's request, ASX established a Cash Equities Clearing and Settlement Advisory Group. The regulators have issued a joint letter of regulatory expectations requiring ASX Clear and ASX Settlement to resource, consult and engage with the CS Advisory Group.

The Act provides ASIC with powers to implement requirements to promote competitive outcomes, and to ensure that competition, if it emerges, is safe and effective.

Introduction

- 7 On 27 June 2023, ASIC provided testimony to the PJC on its supervision of ASX and the CHESS Replacement Project. Other stakeholders, including Cboe, also gave testimony and made written submissions on ASX's implementation of the CHESS Replacement Project.
- 8 ASIC has considered the submissions and answers to Questions on Notice made by stakeholders to the PJC, especially those commenting on the Recommendations Paper and the current co-regulatory model. ASIC notes that stakeholders showed broad support for granting new powers to ASIC and the ACCC to deal with competition in the clearing and settlement of cash equities in Australia. The following section provides an update on the recent developments and an overview of the recent Competition in Clearing and Settlement Reforms, including the types of matters that can be covered by the rules.

Establishment of the Cash Equities Clearing and Settlement Advisory Group

- 9 In early August, the ASIC Chair hosted an industry roundtable comprising a small group of recognised industry leaders, and including ASIC Commissioner Danielle Press and the then Deputy Governor of the Reserve Bank of Australia, Michele Bullock. The roundtable was convened to address longstanding industry concerns over the CHESS Replacement Project and the adequacy of ASX's stakeholder engagement and governance, including ASX's management of intragroup conflicts of interest.
- 10 At ASIC's request, ASX has established a Cash Equities Clearing and Settlement Advisory Group (CS Advisory Group): see also [ASIC's submission to the PJC](#) (PDF 632 KB), dated 10 May 2023. The CS Advisory

- Group, led by independent Chair Alan Cameron AO, was designed to increase industry contribution to key strategic cash equity CS issues.
- 11 Given that ASX expects to announce the CHESS replacement solution design in the December quarter of 2023, the initial focus of the new advisory group will be on the CHESS Replacement Project. However, it is intended in the longer term that the CS Advisory Group will provide advice on key strategic CS matters, such as T+1, to provide input into the governance of ASX Clear Pty Ltd (ASX Clear) and ASX Settlement Pty Ltd (ASX Settlement).
- 12 The regulators have issued a [joint letter of regulatory expectations](#) to ASX Clear and ASX Settlement, requiring them to resource, consult and engage with the CS Advisory Group in good faith and in the public interest. The regulators will actively monitor ASX Clear's and ASX Settlement's engagement with the CS Advisory Group and the ASX CS Board's response to advice provided by the group.

Overview of the Competition in Clearing and Settlement Reforms

- 13 The Competition in Clearing and Settlement Reforms have a long history, with the Council of Financial Regulators' (CFR) work with the ACCC commencing in 2011: see [Review of Financial Market Infrastructure Regulation](#) (PDF 627 KB) (treasury.gov.au). They are the culmination of extensive review and industry consultation by the CFR on competition in the clearing and settlement of cash equities in Australia.
- 14 The [2015 review of competition in clearing cash equities](#) by the CFR recommended reforms that would allow competition in clearing and settlement (CiCS). In March 2016, the Government endorsed the conclusions of that review. The Treasurer released the [CFR's advice to Government](#), accepted the CFR's recommendations and endorsed a policy stance of openness to competition in clearing and settlement for cash equities. This included implementing legislative changes to:
- (a) allow ASIC to impose requirements on ASX's cash equity CS facilities, including rule-making powers for ASIC in respect of CS facilities; and
 - (b) grant the ACCC an arbitration power to provide for recourse in disputes about the terms of access to ASX's cash equity CS services.
- 15 Following further stakeholder consultation in 2017, the CFR produced several policy statements outlining [the regulatory expectations for ASX's conduct in operating cash equity CS services in Australia](#) (PDF 210 KB) (the Regulatory Expectations) and the minimum conditions for the safe and effective competition in clearing and settlement of cash equities in Australia (respectively the [Minimum Conditions \(Clearing\)](#) (PDF 254 KB) and the [Minimum Conditions \(Settlement\)](#)).

- 16 On 6 September 2023, the Act passed both Houses of Parliament. The Explanatory Memorandum to the Bill explains that Schedule 3 includes amendments to the *Corporations Act 2001* (Cth), the *Competition and Consumer Act 2010* (Cth) and the *Australian Securities and Investments Commission Act 2001* (Cth) to facilitate competitive outcomes in the provision of CS services for Australia's financial markets. The amendments provide ASIC with powers to:
- (a) implement and enforce requirements for a provider of CS services to operate in a way that achieves competitive outcomes; and
 - (b) ensure that competition in clearing and/or settlement, should a competitor emerge, is safe and effective.
- 17 The Act also provides the ACCC with the power to conduct binding arbitration to resolve disputes regarding access to CS services where the CS service and the CS facility it is connected to are part of the same corporate group and are covered by a declaration made by the Minister.
- 18 The overarching objective of these amendments is to facilitate outcomes for the monopoly provision of CS services which are similar to those which might be expected in a competitive environment, and to ensure that competition, if it emerges, is safe and effective. ASIC will, following an initial determination by the Minister, be able to make rules that deal with the activities, conduct and governance of CS facility licensees, their associated entities and other persons specified by regulations, in relation to the provision of CS services (the CS Service Rules). It is intended that the CS Service Rules may deal with matters including, but not limited to:
- (a) the dealings of a CS facility licensee with users of the facility, including participants, end users, potential or actual competing CS facilities (such as CCPs and/or securities settlement facilities, and/or central securities depositories), technology service providers and other relevant stakeholders;
 - (b) the CS facility licensee's governance arrangements (including its board composition and participation of users in the CS facility's governance arrangements);
 - (c) the CS facility licensee's arrangements for handling conflicts of interest (including how the CS facility handles confidential information of its competitors);
 - (d) the CS facility licensee's accountability (including public reporting);
 - (e) the CS facility licensee's provision of services to users (including competitors) including:
 - (i) investment in core infrastructure;
 - (ii) service levels;

- (iii) transparent, non-discriminatory, and fair and reasonable pricing of the CS services; and
 - (iv) the provision of access to the CS services (including data) on transparent, non-discriminatory, and fair and reasonable terms;
 - (f) coordination, cooperation and links between CS facilities, including in respect of interoperability, settlement, default management, risk management, recovery and resolution;
 - (g) coordination and cooperation between CS facilities, registries and issuers in respect of the transfer and administration of holdings of financial products; and
 - (h) the cessation of the provision of services by a CS facility (including a structured wind-down supported by financial commitments).
- 19 Once a Ministerial determination is made, ASIC may make rules that address the intended objectives behind the recommendations made by Cboe. However, the final form of the rules, including any rules stipulating specific requirements, such as interoperability obligations and access requirements between competing CS facilities will need to undergo substantial public consultation to ensure that ASIC has given the appropriate consideration to different stakeholders' views, business models and operating requirements. The CS Service Rules will also be subject to Ministerial consent.
- 20 It may also be the case that an emerging competitor or other relevant stakeholders have a differing view to those expressed by Cboe. In the absence of a committed competitor, it is not possible to identify with the required degree of certainty what those detailed specific requirements might be. However, what is known is that 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 or otherwise seek to frustrate access to data or services that are necessary for the provision of settlement services by a competing service provider. Whether competition does emerge is ultimately a matter for the market to determine.

B Responses to Cboe's Recommendations Paper

Key points

The Recommendations Paper raises complex technical questions and matters that would require further regulatory consideration with the RBA and ACCC and broader public consultation.

ASIC's new CS Services rule-making powers may address some of the recommendations, and would be subject to consultation, Ministerial consent, and parliamentary disallowance.

Introduction

- 21 The Recommendations Paper raises complex technical questions and matters that require further regulatory consideration working closely with the RBA and the ACCC, and broader public consultation.
- 22 Following a Ministerial determination, ASIC will be able to make CS Services Rules that may address some of the underlying concerns highlighted in the Recommendations Paper. The development of CS Services Rules will be subject to industry consultation to ensure ASIC considers a broad range of stakeholders' views, different business models and interests. Cboe and other industry stakeholders will have the opportunity to engage with ASIC and inform the drafting of these rules.

Review of the National Guarantee Fund and extension of this to benefit all CCPs

Cboe Recommendation 1

The regulators and Treasury review the allocation and role of the National Guarantee Fund contribution of \$71.5 million, allocated to ASX Clear as 'restricted capital reserve', having regard to the benefit of supporting resilience and competition across Australia's financial market. Given their origin, Cboe considers there is a strong argument these funds should be available for the benefit of all CCPs.

- 23 Following a Ministerial determination in 2005, responsibility and liability for the management of a clearing participant default was transferred from the National Guarantee Fund (NGF) to ASX Clear. The payment of \$71.5 million to ASX Clear was made on 31 March 2005 as part of this transfer of responsibility: see [Securities Exchanges Guarantee Corporation](#)—

- [What is the National Guarantee Fund?](#) Since that time the funds have been legally held by ASX Clear.
- 24 The changes to the NGF and the *Corporations Regulations 2001* were aligned to ASX Clear's obligations as a CS facility licensee under Pt 7.3 of the Corporations Act, including the obligation to comply with the RBA's Financial Stability Standards for CCPs (FSS for CCPs) under s821A(1)(aa)(i) and s827D(2)(a). In addition to these standards, all licensed CS facilities have a direct obligation under s821A(1)(d) of the Corporations Act to have sufficient resources (including financial, technological and human resources) to operate a CS facility properly. Any potential new entrant CCP seeking to obtain a CS facility licence would need to demonstrate that it could comply with the obligations that would apply if the licence were to be granted, which includes the licensee obligations under s821A of the Corporations Act.
- 25 CCPs are required to maintain a pool of financial resources to cover potential losses due to the default of one or more clearing participants. One of the typical components of a CCP's financial resources is a default fund. These default funds must be held by the CCP, be unencumbered and immediately available to a CCP on the default of a participant to minimise market disruption and to ensure that the CCP can continue to meet its obligations to non-defaulting participants. A CCP's default fund is typically made up of contributions from the CCP and its participants.
- 26 ASX Clear's default fund is currently sized at \$250 million, including the \$71.5 million that is held in a 'restricted capital reserve': see [ASX Annual Report 2022](#). It appears that there is no legal mechanism for the recovery by Government of this payment from ASX, and any legal requirement for repayment of funds would be a matter for Government.

Structural separation of ASX Clear and ASX Settlement

Cboe Recommendation 2

The regulators require ASX Clear and ASX Settlement to be structured in such a way that, at an operations, governance and technology level, they are incentivised to, and rewarded for, servicing all their customers equally. ASX Group must not be able to continue to use its dominant position through its CS functions to diminish competition in areas in which it competes with non-ASX businesses.

- 27 Any decisions relating to the structural separation of ASX Clear and ASX Settlement are matters for ASX and/or Government to consider and go beyond the intended policy objectives of the Competition in Clearing and Settlement Reforms and ASIC's new CS Service rule-making powers.

- 28 As set out in paragraph 18, ASIC's new powers will include the ability to develop CS Service Rules relating to governance arrangements and arrangements for handling conflicts of interest, including a CS facility's management of intragroup conflicts of interest.
- 29 We expect ASX Clear and ASX Settlement to focus on identifying and managing intragroup conflicts of interest and gaining the trust and confidence of its customers, including non-affiliated market operators that have competing interests with ASX Limited. Customer and stakeholder trust and confidence is critical to the CHESSE Replacement and ASX Clear and ASX Settlement's operation of national infrastructure for the benefit of the entire Australian financial market, listed companies and investors.
- 30 As set out in paragraphs 9–12, the recently established CS Advisory Group will advise the boards of ASX Clear and ASX Settlement on key strategic CS issues and contribute to the successful replacement of CHESSE. ASIC views the establishment of the CS Advisory Group as critical to restoring confidence in the CHESSE Replacement, effective stakeholder engagement by ASX and as an input to the governance of ASX Clear and ASX Settlement. We will carefully monitor ASX's response to the advice of the group.
- 31 ASIC will continue to monitor ASX Clear and ASX Settlement's compliance with their existing obligations under the Corporations Act and, if necessary, use our new powers under the proposed Pt 7.3A of the Corporations Act to achieve compliance with future ASIC CS Services Rules by ASX Clear and ASX Settlement.

Consideration of the impact of the failed CHESSE Replacement Project on industry stakeholders

Cboe Recommendation 3

The regulators consider the effects that the failed CHESSE Replacement Project and the requirement for a complete restart of this project have on competition when exercising their supervision functions and any rule-making powers, noting that these failures have resulted in industry stakeholders needing to commit resources to ASX up until 2032.

- 32 We acknowledge the impact on the broader industry of ASX's decision to pause and redesign the CHESSE Replacement Project. In implementing a CHESSE replacement, we expect ASX to actively engage and consult with industry on whether a phased or single cutover approach is taken to migrate to a CHESSE Replacement.
- 33 Consistent with the policy objectives of the Act, we will be able to make CS Service Rules that facilitate outcomes that would be expected in a

- competitive market for CS services, and ensure that competition, should it emerge, is safe and effective.
- 34 For example, CS Service Rules could include requirements in relation to interoperability arrangements and the use of global technology standards, as well as requirements around transparent, non-discriminatory, fair and reasonable pricing of and access to CS services.
- 35 As explained in paragraphs 3.36 and 3.37 of the [Explanatory Memorandum](#) to the Bill, ASIC's role is to make rules relating to the broad conduct of pricing—for example, by requiring a CS facility licensee to provide certain pricing information to a user. The consideration of pricing for specific CS Services and access to these services are matters for the ACCC to consider.
- 36 Under the Act, the ACCC will have the power to conduct binding arbitration to resolve disputes about the terms of access to ASX's CS services.

Establishment of rules to encourage effective competition

Cboe Recommendation 4

- After the CiCS legislation is passed, ASIC establishes firm rules in key areas that are needed for competition to emerge and be effective. Potential emerging competitors must be assured that:
- (i) competition will be on a fully interoperable basis;
 - (ii) competing CCPs will be linked on a peer-to-peer basis;
 - (iii) access to the CHES settlement batch and the Central Securities Depository (CSD) will rank equally between CCPs; and
 - (iv) access to key competitor systems will be on an equal access basis.
- 37 ASIC is committed to using its new powers in a timely manner, while ensuring any proposed new rules carefully balance the policy objective of facilitating competition while not compromising financial stability or effective market functioning. ASIC, in consultation with the RBA and ACCC, will be informed by lessons learned internationally on competition in clearing, the requirements of the Australian market and the proposed business model of an entrant CCP.
- 38 The Council of Financial Regulators (CFR) Minimum Conditions for Safe and Effective Competition in Clearing (Minimum Conditions (Clearing)) aim to give potential entrants sufficient clarity as to the measures that would need to be in place before the regulators could advise in favour of a competing CCP's licence application.

- 39 We have been clear in the CFR's Minimum Conditions policy statement that the technological design of ASX Clear and ASX Settlement infrastructure should not raise barriers to the interoperability or access to settlement arrangements by a competing CCP. Under ASIC's new rule-making powers, this expectation could be codified as an obligation, ahead of the emergence of competition.
- 40 Interoperability between competing CCPs could facilitate competition by reducing the entry costs for a future competitor both in terms of lower development costs (i.e. building to industry standards rather than bespoke ASX standards) and the time taken to launch. However, the Minimum Conditions (Clearing) set out 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—and to avoid incurring unnecessary costs by industry should a competing CCP not emerge. We note that CCP interoperability has been successfully implemented in other markets.
- 41 Should a competing CCP emerge, ASIC will work closely with the RBA to consider the technical and complex policy considerations flagged in the Minimum Conditions (Clearing). In doing so, we will carefully consider stakeholder views, including Cboe's, on key matters including the interoperability operating model and the mechanics of CCP linkages.
- 42 In addition, as set out in the Minimum Conditions (Clearing), the RBA would need to consider additional guidance to the FSS for CCPs (CCP Standards) that deals with the management of risks arising from interoperable links. At the same time, the regulators would clarify arrangements for the regulatory oversight of matters such as default management and CCP recovery in a multi-CCP environment.
- Note: See [Minimum Conditions for Safe and Effective Competition in Cash Equity Clearing in Australia](#).
- 43 If a competing CCP were to emerge, as an ongoing monopoly provider, ASX Settlement's services would remain under the CFR's Regulatory Expectations and therefore fall under ASIC's rule-making powers for the purpose of facilitating competitive outcomes in the absence of competition in settlement. This would include the provision by ASX Settlement of access to its cash equity CS services on commercial, transparent and non-discriminatory terms to users, including an entrant CCP. The Act also grants the ACCC powers to arbitrate disputes regarding access, including pricing, to services licensed under Pt 7.3 of the Corporations Act.

Charging for routing trade executions for clearing and settlement

Cboe Recommendation 5

No Australian market operator, or its aligned CS service, should be able to charge market or clearing participants, investors or competing CS infrastructures for routing trade executions for clearing and settlement.

- 44 CFR's Regulatory Expectations set out that ASX Clear and ASX Settlement should maintain an appropriate method for determining the prices of their CS services to generate expected revenue that reflects the efficient costs of providing those services, including a return on investment commensurate with the commercial risks involved.
- 45 As set out in paragraph 3.37 of the Explanatory Memorandum to the Bill, ASIC's CS Service Rules may deal with transparent, non-discriminatory, fair and reasonable pricing of CS services. However, ASIC is only expected to make rules relating to the broad conduct of pricing. Matters such as how and what level prices should be set for access to specific CS services may be dealt with using the ACCC's arbitration power.

Note: See paragraph 3.37 of the [Explanatory Memorandum](#) to the Treasury Laws Amendment (2023 Measures No. 3) Bill 2023.

Operational standards

Cboe Recommendation 6

Competing CCPs should transparently agree and maintain operational standards within core functions that deliver to the highest standards of performance and resilience within securities clearing for Australia's investors, participants and stakeholders.

- 46 We agree that it would be appropriate for a memorandum of understanding (MoU) to be established between competing CCPs to promote information sharing and cooperation. This would be consistent with the MoU established between competing markets ASX and Cboe.
- 47 Some of the matters raised by Cboe in this recommendation may, subject to further regulatory consideration, be caught by existing regulatory obligations under Pt 7.3 of the Corporations Act or through potential future enforceable regulatory obligations imposed on the competing CCPs under either ASIC CS Service Rules and existing or additional RBA guidance on its CCP Standards.

- 48 ASIC, when considering potential new obligations to be set out in the CS Service Rules, would consider whether it may be appropriate to rely on or require the development of industry protocols or codes, an MoU or other potential mechanisms.

Key terms

Term	Meaning in this document
ACCC	Australian Competition and Consumer Commission
ASX Clear	ASX Clear Pty Ltd
ASX Settlement	ASX Settlement Pty Ltd
Bill	Treasury Laws Amendment (2023 Measures No. 3) Bill 2023
Cboe	Cboe Australia Pty Ltd
CCP	Central counterparty
CCP Standards	Financial Stability Standards for Central Counterparties as set by the RBA
CFR	Council of Financial Regulators
CHESSE	Clearing House Electronic Subregister System
CHESSE replacement, or CHESSE replacement system	The new system that will replace the current CHESSE, and which is to be delivered or implemented as part of the CHESSE Replacement Project
CHESSE Replacement Project	The project established by ASX to replace CHESSE with the CHESSE replacement system
CHESSE user	A CHESSE user is defined by ASX as any organisation that connects directly to CHESSE. This includes market operators, CS participants, product issuer settlement participants, share registries and payment providers
CiCS	Competition in Clearing and Settlement
Corporations Act	<i>Corporations Act 2001</i> , including regulations made for the purposes of that Act
CS	Clearing and settlement
CSD	Central Securities Depository
CS Advisory Group	Cash Equities Clearing and Settlement Advisory Group
CS Service	A CS service is defined in the Act as a service that can only be provided if it has access to a CS facility or to data used in the operation of a CS facility. The operation of a CS facility is taken to be the provision of a CS service

Term	Meaning in this document
CS Service Rules	Rules that ASIC will be able to make, following a determination by the Minister, that deal with the activities, conduct and governance of CS facility licensees, their associated entities and other persons specified by regulations, in relation to the provision of CS services
External Review	The external review undertaken by Accenture into certain aspects of the CHESS Replacement Project application delivery between September and November 2022
FSS	Financial Stability Standards as set by the RBA
MoU	Memorandum of Understanding
NGF	National Guarantee Fund
PJC	The Parliamentary Joint Committee on Corporations and Financial Services: Oversight of ASIC, the Takeovers Panel, and the Corporations Legislation
Pt 7.3 (for example)	A part of the Corporations Act (in this example numbered 7.3), unless otherwise specified
RBA	Reserve Bank of Australia
Recommendations Paper	The <i>Cboe Australia Recommendations paper for the identification of barriers to, and opportunities for the support of, competition within Australia's post-trade environment</i> , dated 28 July 2023 and submitted to PJC
regulators	ASIC and the RBA
Regulatory Expectations	CFR's <i>Regulatory Expectations for Conduct in Operating Cash Equity Clearing and Settlement Services in Australia</i> which govern ASX pricing, access, and governance arrangements as a sole provider of cash equity clearing and settlement services
s821A (for example)	A section of the Corporations Act (in this example numbered 821A), unless otherwise specified