



10 September 2024

Ms Dodie Green, Senior Manager
Market Infrastructure
Australian Securities and Investments Commission

By email.

Dear Ms Green

Consultation Paper 379: ASIC CS Services Rules

AFMA appreciates the opportunity to comment on the proposed ASIC CS Services Rules.

AFMA supports sensible proportionate practices around the provision of clearing and settlement services while it remains a single provider service market.

While many of the proposals are continuations of the measures put in place under the Statement of Expectations and are generally supported, we suggest rebalancing the proposals that go beyond existing arrangements as we are concerned these could create significant barriers to innovation, and ongoing costs and difficulties for the industry.

As ASIC is aware, a careful balance needs to be struck between the benefits and costs of regulatory interventions. While we can see the logic, and in the present circumstances, the drivers of all the 2.4.6 proposals, we suggest that ASIC rebalances these proposals for as drafted they are expected to be a significant drag on upgrades and innovation.

Please find our more detailed responses below. Please note that AFMA makes this submission on behalf of its market participant members.

We thank you again for ASIC's engagement with the industry both through the paper and the broader dialogue.

Yours sincerely

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A1Q1 We would welcome stakeholder views on whether the prospect of competition emerging in cash equity CS services has changed since 2015. Do you believe the proposed obligations on CS service providers will achieve the intended policy objective of facilitating competition, or competitive outcomes in the absence of competition?

AFMA is not aware of any significant changes to the prospect of competition in cash equity CS services emerging but notes increased participation of well-capitalised global players in the local market.

The regulatory settings broadly (with on balance exceptions as noted below) support the facilitation of competition should commercial factors drive that outcome.

While we support many of the proposed obligations, and some of the new obligations, we believe some may not be a net benefit given their significant costs to innovation and agility. There is a risk of regulation unduly hampering ongoing industry upgrades and evolution and creating costs that must be borne by participants and investors.

B1 We propose to implement the Regulatory Expectations as enforceable obligations through the ASIC CS Services Rules 2024. See the draft ASIC CS Services Rules 2024 in the attachment to this paper.

B1Q1 Do you consider that the proposed rules cover the Regulatory Expectations and, more broadly, are sufficient to facilitate competitive outcomes in the monopoly provision of CS services? If not, what (if any) are the other obligations the CS services rules should impose?

AFMA holds that the proposed rules are more than those necessary to facilitate competitive outcomes. The rules that continue the current practices are welcomed, and some of the additional proposals that increase transparency are supported, but some rules given their associated regulatory burden appear not to be justified on a cost benefit basis.

B1Q2 Do you have any feedback in relation to how the Regulatory Expectations have been implemented in the draft CS services rules (set out in the attachment to this paper)?

We do not have any drafting feedback. Our concerns are related to the policy intent of some proposals. The entities most affected are more likely to have comment on drafting matters.

B1Q3 Do you expect to incur any costs as a result of our proposal? If so, please provide an estimate of the time and costs that you will expend. In providing this estimate, please compare your costs with the situation where we do not introduce the proposed rule. Please provide feedback on whether these costs are likely to be one-off or ongoing.

We do not note any additional costs for the implementation of the Expectations as Rules, but note those directly affected would be better placed to advise.

B2 We propose to introduce rules that require a CS service provider to engage an independent expert to conduct an audit and prepare a written report about the CS service provider's compliance with the proposed rules (annual review).

B2Q1 Do you agree with the scope of the annual review? If not, please provide detailed reasons for your answer.

While there is validity in episodic or periodic independent audit of compliance with the Rules, this cadence may be too frequent for BAU circumstances. Generally Clearing and Settlement is a relatively stable business area that does not see changes that might impact compliance. Consideration might be given to setting any periodic cadence relative to the amount of change in a period. For the present period for example every 2 years may be appropriate, whereas during steady state a period of 3 or 4 years may be appropriate.

B2Q2 Should the proposed scope of the annual review be extended to include technology and governance issues in relation to the CHES replacement program, noting that these matters are also a consideration under Part 7.3 of the Corporations Act?

AFMA is an active participant on the CHES Replacement programs Business Committee, Technical Committee, and numerous working groups. In our view that is informed by these participations, the existing review load on the replacement program has passed the point where value is being added and a reduction rather than an increase in reviews is the direction most likely to support project success.

B2Q3 Do you expect to incur any costs as a result of our proposal? If so, please provide an estimate of the time and costs that you will expend. In providing this estimate, please compare your costs with the situation where we do not introduce the proposed amendment. Please provide feedback on whether these costs are likely to be one-off or ongoing.

Annual review costs will increase costs for investors and market participants. As such they should be used in a targeted and judicious manner.

C1 We propose to introduce rules that: (a) define 'international open communication procedures and standards' to mean procedures and standards for messaging and reference data: (i) ISO 20022; and (ii) FIX 5.0; and (b) require a CS service provider to take all reasonable steps to ensure that any changes to its core systems accommodate international open communication procedures and standards.

C1Q1 Do you agree with this proposal? In your response, please give detailed reasons for your answer.

AFMA recognises the central and important roles played by both ISO 20022 and FIX 5.0. These are well respected and mature standards that would be a logical choice should a 'hard coding' of the meaning of 'international open communication procedures and standards' be necessary at this time.

However, we expect that with the passage of time these standards will be replaced by future standards, and as such suggest that a softer regulatory approach is appropriate.

For example, guidance rather than rules might be used to state that 'international open communication procedures and standards' should be understood as referring to standards such as ISO 20022 and Fix 5.0, their successors and other standards of similar quality.

C1Q2 Do you agree with the definition of 'international open communication procedures and standards' and do you consider that the definition covers the relevant procedures and standards, noting that these will be fixed as at the date the rules are made? In your response, please give detailed reasons for your answer.

See our response to C1Q1.

C1Q3 Do you expect to incur any costs as a result of our proposal? If so, please provide an estimate of the time and costs that you will expend. In providing this estimate, please compare your costs with the situation where we do not introduce the proposed amendment. Please provide feedback on whether these costs are likely to be one-off or ongoing.

See our response to C1Q1.

C1Q4 The proposed rules are intended to ensure that CS service providers' core systems accommodate technical interoperability with users' systems. More broadly, what do you understand by 'interoperability' and the scope of interoperability in the Australian market?

This is a technical question we are not best placed to answer.

C2 We propose to introduce a rule to require the CS service providers to undertake an independent review of the pricing of their CS services against the price of similar services in other comparable international markets within a year after the proposed rules are made, and thereafter at least every five years, and to publish the results of the review.

C2Q1 Do you agree with this proposal, including the scope and frequency at which the review needs to be conducted? In your response, please give detailed reasons for your answer.

For such a review to be effective it would need to be done at arm's length. There are complexities in the different operating models that can make direct comparisons difficult.

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C2Q2 Do you expect to incur any costs as a result of our proposal? If so, please provide an estimate of the time and costs that you will expend. In providing this estimate, please compare your costs with the situation where we do not introduce the proposed amendment. Please provide feedback on whether these costs are likely to be one-off or ongoing.

The costs of these reviews will ultimately be borne at least in part by investors and market participants. To balance these costs any reviews must be well-balanced.

C3 We propose that the CS services rules will apply to CS service providers, defined as: (a) ASX Clear and ASX Settlement (the covered licensees); (b) a direct or ultimate holding company of a covered licensee that makes, or participates in making, decisions that relate to the provision of CS services; or (c) an associated entity of the covered licensee that provides a CS service, in its capacity as such a provider.

C3Q1 Do you agree with the definition and scope of 'CS service provider'? In your response, please give detailed reasons for your answer.

We do not raise any objections to this proposal.

C3Q2 Do you expect to incur any costs as a result of our proposal? If so, please provide an estimate of the time and costs that you will expend. In providing this estimate, please compare your costs with the situation where we do not introduce the proposed amendment. Please provide feedback on whether these costs are likely to be one-off or ongoing.

See above.

C4 We propose to introduce rules that will require the covered licensees to have appropriately documented policies and procedures in place to identify and mitigate any actual or perceived conflicts between the interests of: (a) the covered licensee or an associated entity; and (b) an unaffiliated entity.

C4Q1 Do you agree with this proposal? In your response, please give detailed reasons for your answer.

We agree with this proposal. Managing conflicts of interest should be done in a structured and predictable manner.

C4Q2 Does this proposal adequately address the management of the conflicts of interest between the covered licensees and other entities within ASX Group in relation to the provision of CS services? If not, please elaborate on further or alternative options.

AFMA holds this is an appropriate approach at this time.

C4Q3 Do you expect to incur any costs as a result of our proposal? If so, please provide an estimate of the time and costs that you will expend. In providing this estimate, please compare your costs with the situation where we do not introduce the proposed amendment. Please provide feedback on whether these costs are likely to be one-off or ongoing.

Participants do not expect to incur any significant costs in relation to this proposal.

C5 We propose to introduce rules that require:

- (a) a CS service provider to take all reasonable steps to ensure that its core systems are designed and developed in a way that does not raise barriers to access by unaffiliated entities;
- (b) a CS service provider to maintain and publish policies and procedures designed to ensure that investment, design and development of its core systems, including changes to its core systems, do not raise barriers to access for unaffiliated entities;
- (c) a CS service provider to include in any public statements about material investments in core systems, a statement whether the policies and procedures referred to in (b) have been complied with;
- (d) a covered licensee to engage an independent expert to conduct a review and prepare a written report (external assurance report) about compliance with (a) before the board makes a final decision on the matters covered by the policies;
- (e) a covered licensee to provide the external assurance report to the representative body for feedback before it is provided to the board;
- (f) a covered licensee to make the report publicly available as soon as practicable or no later than one month after it has been provided to the board.

C5Q1 Do you agree with this proposal? In your response, please give detailed reasons for your answer.

AFMA holds that taken as a whole this proposal should be rebalanced given the associated costs. We respond to each proposal as listed in C5 below:

- (a) We suggest a redrafting of the requirement that ‘all reasonable steps’ be made to ‘give due consideration to’, ‘reasonable steps’ or similar. As currently drafted this requirement introduces significant regulatory risk for design and development decisions and operations. These risks may discourage development and modification of such systems. AFMA is keen that innovation and development continue beyond the current project on a regular cycle, to achieve this outcome the CS operator should not have regulatory risk set in such a way that *any* oversight might be construed as a breach.
- (b) We do see benefit in policies and procedures being ‘designed to ensure that investment, design and development of its core systems, including changes to its core systems, do not raise barriers to access for unaffiliated entities’ and support this requirement.
- (c) To avoid acting as a barrier to innovation, agility, and creating unnecessary costs any requirements around public statements should not apply to the regular upgrades that while material in scope and cost would prima facie not be expected to have risks to barriers to access no matter their materiality in terms of cost.

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(d), (e), and (f) – proposals responded to as a group:

External assurance reports that are required to be reviewed by the Board with associated public reporting will add significantly to the risk and cost of industry upgrades. Such requirements should not be necessary for each change or innovation.

AFMA expects to be requesting such upgrades and innovations on a regular basis when the replacement system is live and does not support these regulatory requirements for such BAU upgrades and changes as they are likely to reduce the interest in upgrades and the agility with which they can be made.

Beyond this orientation away for almost all upgrades, some Participants would support such requirements for system-defining changes such as the one currently underway, while others would not support them even for these changes.

C5Q2 Do you expect to incur any costs as a result of our proposal? If so, please provide an estimate of the time and costs that you will expend. In providing this estimate, please compare your costs with the situation where we do not introduce the proposed amendment. Please provide feedback on whether these costs are likely to be one-off or ongoing.

There are likely significant costs that will manifest in multiple ways. Beyond the direct costs of the reports and regulatory burden, they will likely mainly be in a decrease in upgrades and features given regulatory risks and costs.

C6 We propose to introduce rules that: (a) require a covered licensee to publish audited management accounts on an annual basis in respect of its CS services; (b) the audited management accounts must include a cost allocation and transfer pricing policy that describes the methodology used for allocating revenue and costs.

C6Q1 Do you agree with this proposal? In your response, please give detailed reasons for your answer.

In the absence of competition AFMA supports the publication of audited management accounts on an annual basis in respect of the CS services. We support the inclusion of a cost allocation and transfer pricing policy that describes the methodology used for allocating revenue and costs.

C6Q2 Do you expect to incur any costs as a result of our proposal? If so, please provide an estimate of the time and costs that you will expend. In providing this estimate, please compare your costs with the situation where we do not introduce the proposed amendment. Please provide feedback on whether these costs are likely to be one-off or ongoing.

While there are likely minor costs in the absence of competition, audited management accounts are an important tool for the industry in ensuring fair and transparent pricing.

C7 We propose to introduce rules that require a CS service provider to engage an appropriately qualified independent expert to conduct a review, prepare a written report about the appropriateness of the CS service provider's model for the internal allocation of costs and publish the report (cost allocation model report).

C7Q1 Do you agree with this proposal? In your response, please give detailed reasons for your answer.

AFMA supports this proposal.

C7Q2 Do you expect to incur any costs as a result of our proposal? If so, please provide an estimate of the time and costs that you will expend. In providing this estimate, please compare your costs with the situation where we do not introduce the proposed amendment. Please provide feedback on whether these costs are likely to be one-off or ongoing.

As a one-off for each cost allocation model we expect this to be a proportionate cost.

D1 We propose a three-month transition period for the commencement of the ASIC CS Services Rules 2024.

D1Q1 Do you agree with the proposed three-month transition period? In your response, please provide detailed reasons for your answer.

As our participant members are not directly affected we are not best placed to advise.

D1Q2 In implementing the proposed rules, how will you need to change your business practices? In your response, please provide detailed reasons for your answer.

NA.

D1Q3 Do you foresee any new material risks being introduced to your organisation in complying with the proposed rules? If so, please provide detailed reasons for your answer.

NA.