

10 September 2024

Dodie Green
Senior Manager, Clearing and Settlement Facilities
Australian Securities and Investments Commission
Level 5, 100 Market Street
Sydney NSW 2000

By email: CSfacilities@asic.gov.au

Dear Dodie,

Cboe Clear Europe N.V. (**Cboe Clear**) welcomes the opportunity to make a submission on the Australian Securities and Investments Commission's (**ASIC**) draft CS Services Rules (**Rules**).

Cboe Clear is a leading pan-European central counterparty (**CCP**). Connected to 46 trading venues across Europe, it is the most connected and largest open-access CCP by market share.¹ Cboe Clear is part of the Cboe group, which operates the largest pan-European stock exchange by market share. We promote open, competitive and integrated European markets, bringing significant benefits to all market participants, particularly end investors.

Cboe Clear's experiences in a competitive market for clearing services (**CS**) makes it a strong proponent of regulatory settings that promote competition. In Cboe Clear's view, competition should be the default policy for financial services regulatory policymakers. It provides the best outcomes for participants in financial markets and, because of the important role financial markets play in facilitating capital formation, the economy more generally.

Cboe Clear would like to take the opportunity presented by this consultation to outline its views on the appropriate regulatory settings for competition in CS services for cash equities in Australia, if and when a committed competitor emerges. In particular, we take this opportunity to express our strong support for regulatory settings in a competitive environment which:

¹ Based on internal estimates.

1. avoid a 'preferred clearing' model; and
2. ensure that vertically integrated groups take a proactive approach to avoiding the creation of new barriers to access and the removal of historical or legacy barriers.

We have engaged closely with our colleagues at Cboe Global Markets Australia in preparing this submission. We hope our experiences assist ASIC in developing rules to achieve the best outcomes for users and investors in a competitive environment for CS services. While we will refer to the issues facing CCPs, many of these comments will be applicable to competition in the provision of settlement services by competing securities settlement facilities (**SSF**).

Models of interoperability

We understand that the CFR considered issues relating to interoperability in its 2012 *Competition in Clearing Australian Cash Equities: Conclusions* paper (**2012 Report**):

“The Agencies have also considered the implications of interoperability between CCPs... giving participants of multiple trading venues a choice of clearing through a single interoperable CCP could be a means of mitigating some costs associated with a multi-CCP environment including the need to establish duplicate clearing connections. Implementing interoperability would, however, introduce costs and risks and take considerable time. As seen in European markets in which interoperability has emerged, the interests of the parties negotiating an interoperability agreement are unlikely to be aligned; it can therefore be difficult to reach mutually acceptable commercial terms without regulatory intervention. Given the associated complexities and risks, the case for any regulatory intervention to facilitate interoperability would need to be considered carefully and the implications fully understood by the Agencies.”²

Cboe Clear understands that the CFR's current policy is a general commitment to implementing requirements for interoperability between competing CCPs and/or SSFs if and when a committed competitor emerges. The CFR's Minimum Conditions for Cash Equity Clearing in Australia (**Minimum Conditions Clearing**) and Minimum Conditions for Cash Equity Settlement in Australia (**Minimum Conditions Settlement**); together, the **Minimum Conditions**) note that, once a committed competitor emerges, rules will be made to implement these policy statements, including in relation to interoperability.

² Pages 3-4.

The 2012 Report also included an outline of some of the issues posed by potential interoperability arrangements in Europe.³ Currently, some European markets provide for ‘preferred clearing’ arrangements. Under this model of competition in CS services, a trade is cleared by either the incumbent (typically vertically integrated) clearer or the ‘preferred CCP’ where *both* parties to a trade nominate the ‘preferred CCP’. In other words, both parties must agree to use a preferred clearer before the trade can clear with a competing clearer, otherwise it is cleared by the incumbent clearer.

In Cboe Clear’s view, this is not an effective model for competition. This model relies on participants maintaining connections to different CCPs, which significantly increases the costs facing participants, not just in terms of connectivity but also in relation to the bifurcation of clearing exposures and the capital costs that this creates. These costs, in turn, must be passed on to clients. It also reduces the ability of emerging CCPs to compete on the basis of their products, because it creates powerful incentives for participants to remain with those CCPs which have large participant bases and the gravitational pull of inertia, even if the quality or price of their services is worse. The model, due to both parties to a trade being required to match on the order book to clear away from the incumbent CCP, is heavily weighted to clearing remaining with the incumbent and does not realize the potential of open access and true user choice, thereby constraining the benefits of clearing choice.

In contrast, a competition model that supports a fully interoperable clearing environment would mandate competing CCPs to interact with each other to clear trades regardless of which CCP the parties to a trade select. Under this model, clients and participants who have connections to one CCP could continue to trade with clients/participants with connections to another CCP. The competing CCPs would maintain links between each other to facilitate the necessary risk management arrangements, such as inter-CCP margining, which are operationally similar to those the CCP already provides for its clearing members. These would be conducted on an aggregate portfolio exposure basis, allowing for significant economies of scale which are not possible under the preferred clearing model.

As the 2012 Report outlines, this model is not without potential new costs and risks, particularly in relation to managing the risks posed by the exposures between competing CCPs, although it does not change the overall market risk portfolio composition. Nevertheless, Cboe Clear considers that these potential costs and risks can be managed effectively with appropriate regulatory settings, as they are in those European markets which provide for full interoperability, and are outweighed by the efficiencies which will

³ Page 28.

accrue to the industry from a fully interoperable clearing model. These efficiencies will accrue from both increased competitive pressure which will generate better market outcomes, and by avoiding the need for participants to setup costly duplicate links with the necessary operations to manage multiple non-interoperable CCPs, or maintain multiple initial margin exposures due to bifurcated clearing portfolios.

Open access

Cboe Clear's experience in the European market for post-trade services has illustrated the importance of open, fair access to post-trade infrastructure, including to those facilities operated by vertically integrated groups. This is supported by market participants, who receive the benefits of full interoperability including lower clearing fees, settlement netting and compressed margin through netted portfolios.

Given the prevalence of vertically-integrated market infrastructures, a competitive environment for post-trade services is likely to include at least one vertically-integrated competitor. As a result, regulators must consider the risks posed by this structure.

Most importantly, vertically integrated post-trade service providers cannot be allowed to raise barriers to access to upstream competitors. These barriers may take the form of differential connection or other technology requirements which impose different forms of access on unaffiliated market operators, and the participants who trade on these markets.

Moreover, while Cboe Clear understands that these Rules are only intended to apply to the monopoly provision of certain CS services, ASIC should ensure that those rules addressing access issues are retained in rules made for a competitive environment if and when it materializes.

Certainty in open and fair access to incumbent CS facility infrastructure will, in Cboe Clear's view, support the potential emergence of a committed competitor. This would be a positive development for users of Australia's equity market infrastructure. As a result, Cboe Clear supports those rules which prohibit the incumbent provider from raising barriers to access in new technology builds, particularly the CHES replacement system. If a competitor emerges it is likely they will need to interact with this system if full interoperability is to be achieved, so it is important that rules relating to core system design and non-discriminatory access are closely enforced over the design and development of this system, as well as the existing system.

Next steps

Once again, Cboe Clear thanks ASIC for taking the time to consider this submission. While we understand that the matters we have raised may not be directly relevant to the current monopoly environment for CS services in Australia, we are keen to ensure that a competitive environment, if and when it emerges, facilitates the best outcomes for users of Australia's equity markets.

If you have any questions about this submission, please do not hesitate to contact me on

[REDACTED].

Kind regards,

[REDACTED]

Vikesh Patel

Global Head of Clearing, President Cboe Clear Europe