ASX Disciplinary Matters

The ASX Chief Compliance Officer ("**CCO**") has recently made determinations with respect to two separate matters, the first of which involves Credit Suisse AG, Sydney Branch, and the second Credit Suisse Equities (Australia) Limited. Details of these matters are set out below.

Matter 1

The CCO has determined that Credit Suisse AG, Sydney Branch ("**CS-AG**") did not comply with ASX Clear (Futures) Operating Rule ("**ASX CFR**") 46.5 and Rule 46.5 of the ASX Clear (Futures) Procedures, Determinations and Practice Notes (the "**Direction**"), by failing to Close Out back-to-back Open Positions in accordance with the Direction, resulting in its reported Daily Beneficial Ownership Report ("**DBOR**") Day 1 positions being inaccurate in contravention of ASX 24 Operating Rule 6704 (each a "**Contravention**").

The CCO imposed a fine of $50,000 (plus GST) for the Contraventions.

Defined terms have the same meaning as in the ASX CFR, unless otherwise provided.

<u>The circumstances of this matter are:</u>

The Direction contains detailed instruction as to the implementation of ASX CFR 46.5 and, by extension, ASX CFR 46.1. Importantly, it provides that:

- A participant must Close Out back-to-back Open Positions within each individual account by a particular time.
- Back to Back Open Positions are not to be Closed Out across individual accounts that are grouped in an omnibus account.

CS-AG is the recipient of a waiver from ASX Clear (Futures) which allows it to report futures positions held in the accounts of nominated offshore related bodies corporate at the omnibus level on the day following the relevant trade (known as a "**DBOR Day 1**"), followed by a separate report by 8:00am on the second day ("**DBOR Day 2**") containing a breakdown of the positions reported in the DBOR Day 1, detailing all clients holding an Open Position that comprise the omnibus account reported on the previous day.

CS-AG performs daily Close Outs of Open Interest in a system which submits information about the number of futures contracts to be netted down to ASX Clear (Futures)' clearing system ("**Genium**"). In doing this, CS-AG collects data from its affiliates via an upload from the system operated by the affiliates.

Contravention 1:

On 10 June 2015, CS-AG identified a higher number of back to back Open Positions than it expected. This was the result of CS-AG having failed to perform the daily Close Out of a particular omnibus account in accordance with the Direction since 28 April 2015. This omnibus account concerned a related body corporate of CS-AG. On 11 June 2015 CS-AG self-reported this discovery to ASX.

CS-AG's internal investigation found that a member of the IT team determined that an email address used to provide information between the system associated with the omnibus account and the system which calculates and executes the Close Out was incorrect, and had accidentally changed it to an invalid address. This error subsisted between 28 April 2015 and 12 June 2015, so that CS-AG's available Open Interest as reported to ASX was overstated in that period. Further, CS-AG's DBOR Day 2 was sourced directly from the omnibus' system, and so did not correlate with its DBOR Day 1. CS-AG acknowledged that its reported Open Interest for a number of contracts was significantly inflated.

Contravention 2:

On 30 January 2017, CS-AG conducted a review of the pre-submission reconciliation check for DBOR reporting. The review identified that the same omnibus account system showed a position of 1 long and 1 short in a particular contract for a related entity, while in CS-AG's system these two positions were netted to zero. CS-AG went on to identify four affected affiliated entities.

CS-AG later advised ASX that its operations team and all book owners of the affected entities understood that each legal entity's positions were to be netted down in Genium on a per entity basis and in the omnibus account on the Exchange.

In determining penalty, the CCO, among other things, took into account the following matters:

a) CS-AG implemented a comprehensive and effective remediation plan.

b) The Contraventions were inadvertent and unintentional.

c) CS-AG did not derive a financial benefit from the Contraventions.

d) The Contraventions were self-reported by CS-AG. In each case, CS-AG promptly undertook an internal review to provide an assessment and intended remediation.

e) The Contraventions potentially had a materially adverse impact on the fairness or effectiveness of the clearing facility operated by ASX Clear (Futures). Futures participants have a legitimate interest in the integrity of reported open interest figures. Reported open interest is used by traders, together with price and traded volume, to predict market trends and to gauge liquidity. Accordingly, any errors in the reporting of it negatively impacts the market and ASX 24's reputation.

f) The events comprising each Contravention are not isolated and occurred over an extended period of time, CS-AG have on three previous occasions reported similar breaches. Also:

    i) Contravention 1 subsisted from 28 April 2015 to 10 June 2015, representing 31 trading days, which ASX regards as an extended period for a breach of this nature.

    ii) Contravention 2 subsisted from the commencement of the Direction 1 July 2010.

    Therefore, while CS-AG has a good history of complying with ASX operating rules generally, its compliance with ASX CFR 46.5 has not been satisfactory.

g) The occurrence of each Contravention, and the extent of remediation now required, indicates that CS-AG's compliance program was not effective at the relevant time. For related reasons, the Contraventions also indicate a weakness in CS-AG's risk management framework at the relevant time.

h) Despite the absence of a deliberate intention to mislead ASX Clear (Futures) or other Participants, the Contraventions unfairly impacted other stakeholders.

i) Contravention 1 was discovered during the expiry period for a number of ASX 24 contracts, being a time of increased volatility.

j) Previous disciplinary decisions, including comparable decisions of other exchanges.

Sanction Guidelines

The CCO determined that, given the circumstances in this matter, a fine of $50,000 (plus GST) was an appropriate sanction. The CCO is of the opinion that this sanction will act as a deterrent and appropriately serves the interests of ASX and its participants.

Matter 2

The CCO has determined that Credit Suisse Equities (Australia) Limited ("**CSEAL**") did not comply with its obligations under:

- ASX Settlement Operating Rule ("**ASX SR**") 4.18.1, to have adequate resources and processes to comply with its obligations as a participant; and
- ASX SR 4.7.1(b), to meet the technical and performance requirements applicable to participants by failing to have such settlement and recording systems as are necessary for its operations,

(each a "**Contravention**").

The CCO imposed a penalty of $30,000 plus GST for the Contraventions.

Defined terms have the same meaning as in the ASX SR, unless otherwise provided.

The circumstances of this matter are as follows:

On 23 November 2015, CSEAL completed the final steps in the migration of its core equity confirmation and settlement system from one third party product to another. Certain settlement services were also outsourced using an Account Operator model to a related entity of the vendor. The migration was a joint project with the vendor that ran for over 18 months.

Between 23 November and 27 November 2015, the vendor had recurring technical issues associated with the migration, causing a series of failed settlements by CSEAL. In response to this situation, ASX Settlement authorised a number of delayed settlements, and levied fees on CSEAL for failing to meet its net sale settlement obligations under ASX SR 10.11.11 over this period.

CSEAL conducted a post-implementation review of the migration concluding that factors contributing to the serious inadequacy of the migration process which lead to the series of settlement failures included inadequate project governance, testing and audit trail. CSEAL implemented a significant remediation plan to address the findings of the review.

Contravention 1

ASX SR 4.18.1 and ASX SR 6.1.1 require participants to have adequate resources and processes to comply with their obligations as a participant. "**Resources**" is defined to include "technological resources" and "**processes**" to include "risk management, business continuity and disaster recovery processes" (ASX SR 4.18.1). ASX SR Procedure 4.18 requires an applicant to certify that it has sufficient resources and processes to be eligible to be admitted as a participant. In conducting that certification, the procedure directs participants to have regard to the content of Guidance Note 10 "Business Continuity and Disaster Recovery" and Guidance Note 9 "Offshoring and Outsourcing". Accordingly, the ASX SR intend for the factors set out in these guidance notes to inform the scope of a participant's obligations to have sufficient resources and processes under ASX SR 4.18.1.

Therefore, the above facts represent breaches of the key requirements of:

- section 3.9 "**Change Management**" of Guidance Note 10, that dictates that "all participants should have and comply with change management policies and procedures that are designed and function to ensure that changes to its ASX Clear and ASX Settlement operations are thoroughly assessed, tested, and authorised, and that appropriate disaster recovery and roll-back arrangement are in place, before changes are implemented."
- section 7 "**Due diligence enquiries**" of Guidance Note 9, requiring a participant to undertake appropriate due diligence before entering into an outsourcing arrangement with another party to establish that the provider has:
    - the human, financial and technological resources;
    - the knowledge and expertise;
    - the internal processes and procedures; and
    - any authorisations,

  needed to perform the activities being outsourced.

Contravention 2

These events also represent a breach of CSEAL's obligation under ASX SR 4.7.1(b) to have the settlement and recording systems necessary for its existing and anticipated obligations.

In determining penalty, the CCO, among other things, took into account the following matters:

a) ASX regards compliance with the organisational requirements in ASX SR 4.18.1 to be of utmost importance. A participant must be able to demonstrate at all times that it has the necessary resources and processes required for it to operate to an appropriate standard as expected of a participant admitted to ASX's settlement facility.

   While ASX acknowledges that the migration was a complex process undertaken over many months, the risk which accompanies such complexity makes it incumbent upon a participant to ensure that all reasonable steps are taken to ensure that its business and the efficient operation of ASX's clearing and settlement facilities is not interrupted. This is the reason for the requirements of due diligence before entering into an outsourcing arrangement (Guidance Note 9) and for effective change management procedures (Guidance Note 10).

b) In the course of ASX's investigation, CSEAL pointed to a number of matters indicating that it had complied with ASX SR 4.18.1, including:

   - It had established governance for the migration project, which was considered to have appropriate management representation and resources to manage and govern the project.
   - It had selected an experienced outsourcing provider with proven human, financial and technological resource, and executed a service-level agreement with change management processes in line with obligations under the ASX operating rules.
   - It maintained experienced management and resources throughout the project and following implementation.

   While ASX acknowledges that CSEAL took steps to ensure the success of the migration project, the ensuing issues mean that it cannot be said that CSEAL had and complied with a change management policy that functioned to ensure that changes were thoroughly tested and that appropriate recovery and roll-back arrangements were in place.

c) ASX appreciates the frankness of the post-incident report in identifying the shortcomings in CSEAL's change management and due-diligence processes ahead of the migration. ASX also notes CSEAL's assurances regarding the remediation it has conducted in response to the issues highlighted. Accordingly, if a contravention attributable to similar failures were to occur in the future it would likely attract a stronger penalty.

d) CSEAL chose not to contest the Contraventions.

e) CSEAL did not intentionally cause the Contraventions.

f) CSEAL did not act unconscionably towards its clients.

g) CSEAL did not gain any business advantage from the Contraventions.

h) CSEAL's history of compliance with the relevant rules and their antecedents, and its compliance history more generally.

Sanction Guidelines

The CCO determined that, given the circumstances in this matter, a fine of $30,000 (plus GST) was an appropriate sanction. The CCO is of the opinion that this sanction will act as a deterrent and appropriately serves the interests of ASX and its participants.

