

ASX Disciplinary Matter – Pershing Securities Australia Pty Ltd

The ASX Chief Compliance Officer (“**CCO**”) has determined that Pershing Securities Australia Pty Ltd (“**Pershing**”) did not comply with ASX Clear Operating Rule (“**ASX CR**”) 5.1.1, due to a failure by Pershing to comply with the Risk Based Capital Requirements set out in Schedule 1 to the ASX CR (the “**Contravention**”). The CCO imposed a fine of \$50,000 (plus GST) for the Contravention.

Defined terms have the meaning provided in the ASX CR, unless provided.

The circumstances of this matter are as follows:

On 27 October 2016, an ASX trading participant that was a client of Pershing’s clearing services reported four Exchange Traded Option market transactions in two batches. Pershing sought to use the price average function in the ASX Derivative Clearing System with respect to each batch, however system limitations required Pershing to bypass this function and allocate each market transaction individually to the counterparty.

On 28 October 2016 Pershing became aware that two market transactions had not been successfully allocated and had remained in the client’s suspense account overnight, causing Pershing to owe a margin payment to ASX Clear by 10:30am on 28 October 2016, which it settled on time.

The margin obligation triggered further obligations under ASX CR Schedule 1, Annexure 1, clause 5, under which a Participant must calculate its Counterparty Risk Requirement in respect of client trades in margined financial instruments. This requirement applies from the time that amounts due to the clearing house are normally scheduled for payment (in this case, 10.30am).

ASX CR Schedule 1.2.3(1)(a) also requires a Participant to calculate its Operational Risk Requirement in the manner described.

As a result of these requirements, Pershing’s Capital Ratio fell below 1.2 on 28 October 2016 between 10:30am (when the margin payment was due) and 4.05pm (when the outstanding transactions were allocated and Pershing’s counterparty exposure thereby ceased).

Between 28 October 2016 and 31 October 2016, Pershing made a number of reports to ASX as to its Liquid Capital, Total Risk Requirement and Capital Ratio (being the ratio of its Liquid Capital to its Total Risk Requirement), which indicated that it had erroneously taken into account the counterparty risk arising from the unallocated market transactions on either 27 October 2016 or at close of business on 28 October 2016. This was in error, for (as explained above) the counterparty risk arising from those transactions applied during the period the margin was required to be paid to ASX, i.e. between 10:30am and 4:05pm on 28 October 2016.

As such, during this period, Pershing ought to have reported that its Liquid Capital was less than its Total Risk Requirement on 28 October 2016 between 10:30am and 4:05pm, which it later acknowledged to be correct. Accordingly, Pershing did not notify ASX Clear immediately that its Capital Ratio had fallen below 1.2, in contravention of Rule S1.2.2(1)(b).

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

- a) The Risk Based Capital Requirements are fundamental to ASX Clear’s prudential regulation of participants. Failure to comply with those requirements has the potential to adversely affect the financial stability of participants, the financial security of clients, and

the integrity of the market. ASX therefore views any breach of the requirements to be a material breach.

- b) ASX's view is that the Contravention was brought about by deficiencies in Pershing's systems and processes for responding to the constraints of ASX's system, managing messages received from ASX, allocations, and monitoring its suspense account.
- c) Issues with Pershing's systems and processes can lead to errors in responding to changing circumstances which, given the number of clients for Pershing's third party clearing services, could have wide reaching effects on the ASX market.
- d) Pershing promptly took comprehensive remedial action to correct the systems issues that led to the Contravention.
- e) Pershing cooperated with ASX's investigation and did not contest the proceeding.
- f) No party suffered any loss as a result of Pershing's conduct.
- g) The breach lasted for only a brief period.
- h) Pershing did not act unconscionably towards its clients.
- i) Pershing did not attain any financial benefit from the Contravention.
- j) Pershing's history of compliance with the ASX CR and other operating rules.
- k) Previous disciplinary decisions.

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.