

MANAGING LIQUIDITY REQUIREMENTS

<p>The purpose of this Guidance Note</p>	<ul style="list-style-type: none"> To provide guidance to participants on the minimum liquidity management arrangements they should have in place to meet their obligations under the ASX Clear Operating Rules
<p>The main points it covers</p>	<ul style="list-style-type: none"> The requirement for participants generally to have a formal liquidity risk framework in place that is appropriate to the nature, scale and complexity of their activities The requirement for a participant to have a nominated officer responsible for liquidity management The requirements for a board-approved annual liquidity plan which considers both “normal” and “stress” conditions and robust liquidity-related operational processes and management reporting The different expectations of ADIs and related bodies corporate of ADIs
<p>Related materials you should read</p>	<ul style="list-style-type: none"> Guidance Note 1 <i>Admission as a Participant</i> Guidance Note 8 <i>Notification Obligations</i>

History: Guidance Note 13 amended 09/05/22. Previous versions of this Guidance Note were issued in 08/16 and 02/22.

Important notice: ASX has published this Guidance Note to assist participants to understand and comply with their obligations under the ASX Clear Operating Rules. It sets out ASX’s interpretation of the ASX Clear Operating Rules and how ASX is likely to enforce those rules. Nothing in this Guidance Note necessarily binds ASX in the application of the ASX Clear Operating Rules in a particular case. In issuing this Guidance Note, ASX is not providing legal advice and participants should obtain their own advice from a qualified professional person in respect of their obligations. ASX may withdraw or replace this Guidance Note at any time without further notice to any person.

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1. Introduction

This Guidance Note is published by ASX Clear Pty Limited (ASX) to provide guidance to participants on the minimum liquidity management arrangements they should have in place to meet their obligations under the ASX Clear Operating Rules.

Under those rules, a participant is required to have adequate resources and processes, including financial resources and management supervision processes, to comply with its obligations as a participant under the ASX Clear Operating Rules.¹

Notwithstanding the guidance provided in this note, it should be noted that the ultimate responsibility for a clearing participant's liquidity management lies with its board, as part of its general law obligations to exercise due care and skill and not to engage in insolvent trading.

A participant should ensure that the liquidity management arrangements it has in place to meet its obligations under the ASX Clear Operating Rules are implemented in a way that would not result in a failure by the participant to meet any other legal or regulatory obligations.

2. General requirements for participants that are not ADIs or a related body corporate of an ADI

A participant that is not an authorised deposit-taking institution (ADI²) or a related body corporate³ of an ADI that is covered by the ADI's liquidity risk management framework should have a formal liquidity risk management framework in place which:

- is appropriate for the nature, scale and complexity of the participant's activities (including, where the participant carries on other activities in addition to its activities as a participant, those other activities);
- documents all key systems, processes and procedures for liquidity management⁴ and ensures that the documentation is kept up-to-date;

¹ ASX Clear Operating Rules 3.2.1(e), 3.5.1 and 4.1.1(a). For these purposes, "resources" include financial, technological and human resources and "processes" include management supervision, training, compliance, risk management, business continuity and disaster recovery processes.

² "ADI" is defined in ASX Clear Operating Rule 2.10.1 to mean an Authorised Deposit-Taking Institution that has been granted an authority to carry on banking business in Australia under the Banking Act 1959.

³ "Related body corporate" has the same meaning as in ASX Clear Operating Rule 2.10.1.

⁴ This includes, but is not limited to, the controls the participant has instituted to control its liquidity exposures such as trading limits for clients and principal trading and exposure limits for underwriting and sub-underwriting commitments.

- identifies the governance arrangements, and in particular the respective roles of the board, CEO, CFO and treasurer, in relation to liquidity management; and
- at a minimum, satisfies the expectations set out in section 5 of this Guidance Note.

3. General requirements for ADIs

Participants that are ADIs are subject to prudential regulation by the Australian Prudential Regulation Authority (APRA) and, as such, are required by APRA to have adequate liquidity arrangements in place to meet all of their obligations, whether in their capacity as an ADI or otherwise.

ASX recognises the regulatory framework administered by APRA and does not expect an ADI (including, for the avoidance of doubt, Australian branches of foreign banks that are ADIs) to have any additional liquidity arrangements in place, over and above those required by APRA to manage the liquidity risk of its activities generally.

4. General requirements for a related body corporate of an ADI

A participant that is a related body corporate of, but not itself, an ADI is not subject to the full rigours of APRA's prudential regulation. It is not uncommon, however, for a related body corporate of an ADI to have its liquidity requirements provided and managed by the ADI.

Where an ADI has a liquidity management framework that is implemented on an aggregate group or country level, then a participant that is a related body corporate of the ADI and included within that framework may rely on that framework as meeting the requirements of this guidance note, provided:

- the ADI is responsible for managing the participant's liquidity requirements;
- substantially all of the participant's liquidity requirements are provided by the ADI;
- senior management or the board of the participant have sufficient information available to them to be satisfied that the participant's ongoing liquidity requirements will be met by the ADI, including receiving appropriate reports about the participant's liquidity position as considered necessary; and
- if at any stage the senior management or board of the participant have concerns about whether the ADI's liquidity management arrangements are adequate to meet the liquidity requirements of the participant, they are able to escalate that issue within the ADI.

Otherwise, a participant that is a related body corporate of, but not itself, an ADI must meet the minimum liquidity management requirements set out in sections 2 and 5 of this Guidance Note.

5. Minimum liquidity management requirements

5.1 Nominated officer responsible for liquidity management

The overall responsibility for liquidity management within a participant must be allocated to a nominated officer (effectively the "treasurer" of the participant) who:

- is responsible for overseeing:
 - the initial preparation and updating of the participant's twelve month liquidity plan (see section 5.2 below); and
 - the day-to-day operational management of the participant's liquidity (although not for settlement, reporting or bank reconciliations – see section 5.3 below);
- has the requisite experience and qualifications to manage liquidity risk; and
- will act as ASX's first point of contact for discussions related to the participant's liquidity risk management.

These responsibilities should be reflected in the formal job description of the nominated officer.

ASX must be advised of the appointment or any subsequent departure of the nominated officer within 10 business days of the change taking effect. Such advice is to be provided via email to CRAteam@asx.com.au.

5.2 Twelve month liquidity plan

A participant must have in place a liquidity plan that covers at least the following 12 months and that:

- identifies the liquidity requirements⁵ likely to arise over the next 12 months under both “normal” and “stress” conditions (including, where the participant carries on other activities in addition to its activities as a participant, in relation to those other activities);
- identifies the funds available to the participant to meet its liquidity requirements, addressing in particular:
 - any requirements that need to be met to have access to those funds⁶ or any restrictions on the use of those funds;
 - the certainty and timeliness of access to those funds (in both normal and stress conditions); and
 - how client and non-client monies are segregated and the extent to which client monies are able to be used to meet the liquidity requirements of the participant;
- explains how the participant has defined “normal” and “stress” conditions (in the latter case, ASX’s expectation is that liquidity plan should address participant-specific, customer-specific, crypto asset-specific and general market conditions);
- includes the specific stress scenarios set out in section 5.6 below in the calculation of the liquidity requirement under “stress conditions”;
- sets out the key assumptions made in the plan; and
- sets out the key risks to achieving the plan and how these risks are to be managed or mitigated.

The nominated officer responsible for liquidity management must review the plan at the end of each quarter and extend it for an additional quarter.

The liquidity plan should be based on, and consistent with, the participant’s current business strategy and business plan and its current financial circumstances. If there is a change to the participant’s business strategy, business plan or financial circumstances, the nominated officer responsible for liquidity management should review the plan to ensure that it remains current and effective.

The plan must be reviewed and approved by the participant’s board at least annually and whenever there is a material change in the participant’s business strategy, business plan or financial circumstances.

5.3 Segregation of duties

There must be an appropriate segregation of duties between those managing liquidity and those:

- settling transactions and moving funds (typically an operations/settlements function);
- recording and extracting the data used for management reporting on liquidity requirements and the funds available to meet those requirements (typically a finance function); or

⁵ The sources of the liquidity requirement should be specified within the liquidity plan at an appropriately detailed level – e.g. where a participant uses a service company, expenses that are recharged to the participant should be disclosed according to their nature and not combined as a single cash outflow line of management/service fees paid to associated entities.

⁶ For example where the participant is relying on a subordinated debt facility, the use of that facility will require approval from ASX.

- performing bank reconciliations.

5.4 Management reporting

The participant must have management information systems and reporting arrangements that provide the board and senior management with current and forward-looking information on the liquidity position of the participant that is accurate, appropriate and timely.

At a minimum this should include:

- a quarterly “Sources and Uses of Funds” report to senior management and the board of the participant, with an analysis of any material variances to the liquidity plan;
- a quarterly report to senior management and the board of the participant on the participant’s current and forecast liquidity positions over the next 12 months, again with an analysis of any material variances to the liquidity plan; and
- a set of early warning indicators to alert senior management and the board of potential issues in meeting operational liquidity requirements.

5.5 Operational processes

The following operational processes must be maintained:

- daily forecasting of liquidity over at least the next 5 business days, with forecasting based on “normal” and “stress” conditions (as set out in the liquidity plan per section 5.2) and factoring in all of the participant’s liquidity requirements;⁷
- clear and documented escalation procedures and delegations of authority to deal with liquidity issues; and
- daily reconciliation of all bank accounts (both trust and general) to verify funding availability.

5.6 Specific stress scenarios

The calculation of liquidity requirements under stress conditions in the 12 month liquidity plan (per section 5.2 above) and the daily forecasting over the next 5 business days (per section 5.5 above) must include the separate quantification of the liquidity requirements resulting from each stress scenario set out in this section of the Guidance Note.

A participant is expected to demonstrate it has sufficient liquidity to cover the higher of the liquidity requirement resulting from (i) the participant’s self-defined stress assumptions or (ii) each specific stress scenario set out in this section.

Scenario 1 - Crypto-exchange traded product (ETP) securities “sell-down”

For the purpose of this scenario, crypto-ETPs are defined as ETPs with direct exposure to crypto-assets as the underlying asset.

Novated trades in ETPs with direct exposure to crypto-assets that are yet to settle with ASX are subject to large cash market margin (“CMM”) requirements⁸ from ASX as a result of the historic volatility of the price of the underlying crypto-assets. Such trades are also subject to very large stress tests⁹ by ASX as part of the daily calculation of ASX’s exposure to each participant – the size of the stress tests reflect the possible size of future price moves in “extreme but plausible market conditions”.

⁷ This should include, but not be limited to, normal ASX settlement and margin obligations, possible additional margin calls to meet capital-based position limits or stress test exposure limits; exposures arising from principal trading; underwriting and sub-underwriting commitments, and any other liquidity requirements arising from the participant’s non-ASX activities

⁸ As at January 2022, the CMM requirements envisaged are 40% for Bitcoin ETPs and 50% for Ether ETPs.

⁹ As at January 2022, the stress tests envisaged for both Bitcoin and Ether ETPs are price moves of -100% and +200%.

This scenario is intended to ensure that a participant which clears trades in crypto-ETPs has sufficient liquid resources to cover the CMM and additional initial margins (“AIMs”) calls that may result from the sale in a 2 day period of a significant proportion of the participant’s clients’ (and own) holdings of crypto-ETPs (and so help the participant and its clients avoid any “liquidity trap” associated with such elevated levels of sale volumes). Such elevated sale volumes could occur in response to adverse news relating to the specific underlying crypto-asset or crypto-assets in general which result in both an immediate price drop and the possibility of a much greater and imminent price drop.

Participants should use the following assumptions to calculate the CMM and AIMs driven liquidity requirements from this scenario:

1. A 40% drop in the current price of crypto-ETPs has occurred
2. In response to this price drop:
 - i. 50% of clients (and own) crypto-ETP positions in the participant’s CHES Holdings¹⁰ are sold over a 2 day period with no offsetting purchases.
 - ii. A participant may use a lower assumed sales percentage than 50% if it has robust operational processes that allows it to limit the value of client sales orders it will accept for a particular security or securities¹¹. A participant must receive explicit approval from ASX to use such a lower percentage - a participant must demonstrate the effectiveness of these processes to ASX’s satisfaction prior to such approval being granted.
 - iii. Where a participant clears trades in crypto-ETPs for clients whose positions are not held as part of the participant’s CHES Holdings, the participant must establish (and fully document) an approach to quantifying the crypto-ETP sales volumes from such clients under this scenario¹².

Participants should estimate the CMM requirement and also AIMs calls resulting from these assumed sales under the ASX price increase stress test. In doing so, participants need to make an appropriate assumption regarding STEL utilisation before the inclusion of the impact of the assumed sales - ASX would expect the STEL utilisation percentage incorporated in the 5 day forecast to be heavily weighted towards current/recent utilisation whilst that used for the 12 month liquidity plan would be largely informed by average utilisation over the previous 12 months.

The parameters of this scenario (i.e. the price decrease and percentage of crypto-ETPs sold) will be kept under review by ASX and may change over time in response to actual issuance of, and trading activity in, crypto-ETPs. A minimum notice period of at least 3 months will be provided by ASX of any increase in one or both of these parameters.

¹⁰ Participant CHES Holdings comprises those CHES Holdings belonging to Account Participants which the clearing participant controls in addition to its own Participant Sponsored Holdings and Direct Holdings. (Capitalised terms have the same meaning as in the ASX Settlement Operating Rules.)

¹¹ In accordance with section 1, a participant should ensure that the use of such processes would not result in a failure to meet its legal and regulatory obligations.

¹² ASX expects a participant to be able to demonstrate that the approach used is prudent and consistent with the treatment of the participant CHES Holdings under this scenario.