

## ASX CLEAR - NOVATION

This document seeks to explain how and when novation occurs (including the requirement for notification of the transaction to be received by ASX Clear), as well as when a novated transaction may cease being novated.<sup>1</sup>

### Novation

A trading participant to a Cash Market Transaction or Derivatives Market Contract has exposure to the counterparty trading participant until novation occurs in respect of that transaction or contract.

Novation represents the replacement of a Cash Market Transaction or Derivatives Market Contract between trading participants with two separate Cash CCP Transactions or Derivatives CCP Contracts between ASX Clear and each clearing participant for that transaction or contract.

As a result, ASX Clear becomes the seller to every buying clearing participant and the buyer to every selling clearing participant under each Cash Market CCP Transaction or Derivatives CCP Contract, and in that capacity is responsible to that counterparty for completion.<sup>2</sup>

### Requirements for Novation

For a Cash Market Transaction or Derivatives Market Contract<sup>3</sup> to be novated:

- it must be eligible for both registration<sup>4</sup> and novation<sup>5</sup>; and
- notification of the transaction must be received by ASX Clear;<sup>6</sup>

in accordance with the ASX Clear Operating Rules.

ASX Clear also has the right to decline to register and novate a Derivatives Market Contract or impose conditions on such registration and novation (including the provision of Cover) in certain circumstances.<sup>7</sup>

If transactions due for novation are not identified in the clearing information received from ASX Clear,<sup>8</sup> clearing participants are strongly encouraged to notify ASX Clear. This could help facilitate early awareness of issues which meant that ASX Clear was not receiving notification of transactions.<sup>9</sup>

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<sup>1</sup> This summary information is provided for guidance only and should be read in conjunction with the ASX Clear Operating Rules. It does not replace or vary those Operating Rules. Capitalised terms used in this document have the meaning given to them in the ASX Clear Operating Rules.

<sup>2</sup> ASX Clear Operating Rule 12.2.3.

<sup>3</sup> For Derivatives Market Contracts, the notification and registration steps referred to below relate to the Derivatives Market Transaction under which the Derivatives Market Contract was entered into.

<sup>4</sup> Refer to ASX Clear Operating Rules 12.1.1 and 12.1.1A for eligibility for registration.

<sup>5</sup> Refer to ASX Clear Operating Rule 12.2.1 for eligibility for novation.

<sup>6</sup> ASX Clear Operating Rules 12.1.1(b) and 12.1.1A. For Market Transactions other than OTC Options Market Transactions, AMOs must cause a valid message (notifying the trade being submitted for registration and novation) to be made available for collection in the message collection facility provided in CHES (for Cash Market Transactions) or the Derivatives Clearing System (for Derivatives Market Transactions). In the event of a technical outage, trades may however be notified to ASX Clear and ASX Settlement by alternative means on a temporary basis where the AMO, ASX Clear and ASX Settlement agree that this is likely to lessen the impact of the technical outage on users.

<sup>7</sup> ASX Clear Operating Rules 12.13 and 12.14.

<sup>8</sup> For example, Cash Market Transactions notified via 164 (Notified Broker Broker Trade) messages or Derivatives Market Contracts notified for designation or give-up in the trade allocation screen available via the GUI.

<sup>9</sup> For example, due to a transmission fault between the systems of an Approved Market Operator and ASX Clear.

## When Novation Occurs

### Cash Market Transactions

For Cash Market Transactions which meet the above requirements for novation, the ASX Clear Operating Rules deem the novation of such transactions as having taken effect from immediately after:

- for transactions entered into on the market - the matching of bids and offers on the market of the Approved Market Operator; or
- for transactions reported to the market - the recording of the transaction by the Approved Market Operator.<sup>10</sup>

### Derivatives Market Contracts

Derivatives Market Contracts which meet the above requirements for novation are novated at the time the Derivatives Market Contract has been properly designated to Accounts of both clearing participants in whose names the novated Derivatives Market Contracts will be registered.<sup>11</sup>

## When Novation May Cease

In certain circumstances, ASX Clear can be relieved of its obligations in respect of Cash CCP Transactions or Derivatives CCP Contracts. This includes in the case of:

- Cash CCP Transactions, where ASX Clear:
  - reasonably considers it appropriate to maintain the orderly operation and integrity of the clearing facility;
  - is requested to do so by an AMO or ASX Settlement to ensure the efficiency, orderly operation, integrity or proper functioning of the market or settlement facility;
  - is notified by an AMO that the underlying transaction has been cancelled; or
  - is requested by the buying participant and selling participant to the underlying transaction to do so;<sup>12</sup>
- Derivatives CCP Contracts, where ASX Clear:
  - is notified by the relevant AMO or clearing participants that there was an error in the particulars of the underlying Derivatives Market Contract reported to ASX Clear; or

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<sup>10</sup> ASX Clear Operating Rule 12.2.1 (with ASX Clear Operating Rules Procedure 12.1.5 dealing with when registration occurs). Accordingly the time taken by ASX Clear to receive and process a transaction notified by an Approved Market Operator (including to validate the transaction as eligible for registration and novation, as referred to in the Note to ASX Clear Operating Rule 12.2.1) does not affect the effective time of novation of the transaction.

<sup>11</sup> ASX Clear Operating Rule 12.2.1 (with ASX Clear Operating Rules Procedure 12.1.5 dealing with when registration occurs). Under ASX Clear Operating Rule 11.3, designations must be notified to ASX Clear by 7pm (Sydney time) on the day of the trade. If a clearing participant fails to do so, ASX Clear will designate that Derivatives Market Contract for registration in the clearing participant's Suspense Account. A trading participant to a Derivatives Market Contract continues to have exposure to the counterparty trading participant to that contract until such designation has occurred in respect of both buying and selling clearing participants in respect of that contract.

<sup>12</sup> ASX Clear Operating Rules 12.7.1, 12.7.2 and 12.7.6. This occurs through ASX Clear removing the relevant Cash CCP Transactions from transactions to be notified for settlement, prior to netting for settlement taking place i.e. by end of day (generally 7pm) on the trade date. If this occurs ASX Clear has no obligation in relation to those transactions, with the trading participants to the original Cash Market Transaction being again in a direct contractual relationship on the terms of that original transaction (unless that transaction has also been cancelled).

- is notified by the relevant AMO (or in the case of an OTC Options Market Transaction, by the relevant clearing participants) that the underlying Derivatives Market Contract has been cancelled or amended;<sup>13</sup> and
- both Cash CCP Transactions and Derivatives CCP Contracts, where the buying trading participant or selling trading participant entered into the underlying market transaction fraudulently.<sup>14</sup>

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<sup>13</sup> ASX Clear Operating Rules 12.21 and 12.22. This occurs through ASX Clear cancelling registration of the Derivatives CCP Contracts that arose from novation of the Derivatives Market Contract. In the case of an error or amendment, corrected Derivatives CCP Contracts may be registered in their place if ASX Clear considers appropriate.

<sup>14</sup> ASX Clear Operating Rule 12.2.5. This does not apply to the counterparty Cash CCP Transaction or Derivatives CCP Contract arising from the same market transaction unless ASX Clear is also entitled to be discharged from performing its obligations as counterparty to that transaction or contract.