



# **Australian Dollar Debt Instrument**

# **Confirmation and Settlement Standards**



## AFMA Code of Conduct

AFMA promotes efficiency, integrity and professionalism in Australia's financial markets. The AFMA Code of Conduct (the Code) clearly articulates the ethical principles for minimum acceptable standards of behaviour and supports responsible decision making by firms and individuals engaged in financial markets activities.

All AFMA Financial Markets Members and Partner Members<sup>1</sup> are expected to observe the Code and operate with integrity, professionalism and competence. The Code is designed to support behaviours that put the interests of clients, the firm and the wider community ahead of personal or individual interests, and promotes confident participation by users in Australia's OTC markets.

The Code is presented in two parts – the [Ethical Principles](#) and the [Guidelines](#).

Market participants are reminded that they are generally expected to observe and adhere to the market standards and conventions as set out below when engaging in any form of market dealing.



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### **Disclaimer**

*It is necessary for the users of these recommendations to determine in each case the suitability or otherwise of the recommendations, proposed provisions and other documents referred to in these recommendations to their particular circumstances. These recommendations are not intended to constitute legal or other advice on which users may rely in implementing actual transactions. Nor are they intended as a substitute for legal or other advice when documenting proposed transactions. In this regard, it is strongly recommended that intending users seek prior independent professional advice in respect of the legal, taxation, stamp duty, regulatory, financial and other implications arising from the recommendations, proposed provisions and other documents referred to in these recommendations.*

*AFMA and the member organisations of the AFMA Debt Markets Operations Committee (including their individual representatives) do not accept responsibility for any losses suffered by relying on these recommendations or arising from any error or omission in them.*

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## 1. Types of Deals Covered

This document covers the following types of deals (the descriptor indicated for each deal type is used throughout this document).

### 1.1. Fixed Income Securities (FIS/longer dated securities)

Onshore/onshore Australian dollar fixed interest security for outright sale or purchase in the Australian market.

The long dated securities market in Australia involves issuing and trading in Commonwealth Government securities (CGS), State and Territory Government securities (Semi's), other public authority securities (including Australian dollar securities issued by some supranational organisations), and corporate bonds.

The long dated securities market plays a key role in the financial system.

- It provides a fund raising medium for governments and for companies.
- It provides investments for banks, life offices and pension funds, other financial intermediaries and companies.
- The Reserve Bank of Australia (RBA) also has a portfolio of CGS and trades in these as part of its monetary and liquidity management.
- The yields on CGS serve as a benchmark for other interest rates in the financial community.

A fixed interest security is a financial instrument that creates the obligation for the issuer to pay:

- a fixed sum called the face value at a specified date, known as the maturity date; and
- a series of equal periodic interest payments called coupon payments.

The basic features of a fixed interest security include:

- Denomination or face value
- Maturity date
- Coupon rate
- Frequency of coupon payments



- Identification of the issuer

Long dated securities have terms to maturity ranging from greater than 6 months to 25 years.

Instruments in this market raise funds when they are first issued. The purchaser of the new securities is the lender, and the issuer is the borrower. Securities can be traded until they mature and their redemption extinguishes the debt. Major security types are:

- *Commonwealth Government Securities (CGS)*
- *Semi Government Securities (Semi)*
- *Floating Rate Notes (FRN)* do not have fixed coupon payments, but have a fixed coupon margin set off a floating rate index. The payments are reset at specific intervals, typically on a quarterly basis. The coupon is expressed as a margin either above or below a specific short term reference rate, eg Libor for those issued in a foreign currency or BBSW if issued in Australian dollars. Some mortgage backed securities (MBS) can be considered FRN and are generally reset every month.
- *Asset Backed Securities* are supported by defined assets such as credit receivables which are usually held by way of a trust arrangement. Obligations to investors are met solely by the defined assets and resultant cash flow. An example of an asset backed security is a MBS or collateralised debt obligations (CDO). They may also be backed by credit cards, car loans, commercial loans and consumer loans or a portfolio of debt obligators in the case of a CDO.
- *Residential Mortgage Backed Securities (RMBS)* is a generic name for any bond or other style security issued by a mortgage provider and credit-supported by pools of residential mortgages or specified mortgages.
- *Capital-Indexed Bonds (CIB)* feature quarterly indexation of the outstanding capital or principal value, which is repaid in full at maturity. The indexation factor is usually based on the rate of consumer price inflation represented by the Australian Bureau of Statistics' CPI, although other price and wage indices are used. A coupon interest rate on the bond is set at issue. Interest payments will vary over time in line with the indexed capital or principal value.
- *Inflation Indexed Annuities* is a stream of regular payments that are adjusted with reference to the inflation rate to protect the real value of the payments from being eroded over time. The relevant inflation index is almost always the one quarter lagging CPI.

## **1.2. Repurchase Agreements (Repos)**

This market relates to the onshore/onshore Australian dollar fixed interest security reciprocal repurchase agreements in the Australian market. The Australian repo market is characterised by trades between institutions purely for liquidity reasons (general collateral) and those dealt to cover



short trading positions (specific collateral). Repo transactions are also undertaken with the RBA as part of its daily open market operations.

In undertaking repos the RBA accepts a range of securities that includes those issued by the Commonwealth Government, State and Territory central borrowing authorities, certain supranational organisations, bank bills (BABs) and certificates of deposit (CDs) issued by select banks licensed in Australia, and certain Australian dollar denominated securities issued by foreign governments and government agencies.

The RBA considers approaches for repos in BABs and CDs separately from those in other eligible securities and classifies them separately (bank bill collateral) from general collateral repos. BABs and CDs must be issued by eligible banks that have acceptable short term rating of P-1 or equivalent and a long term rating equivalent of A3 or above.

All other securities accepted by the RBA as collateral in their daily domestic liquidity dealings, from all market participants, qualifies as general collateral and should be accepted as such by market participants.

#### *US dollar term repo with RBA*

From 24 September 2008 the RBA is now providing ADI's with a US dollar term repo facility. In these, the RBA will provide US dollar liquidity to eligible counterparties for term against the provision by counterparties to the RBA of eligible Australian dollar securities as collateral.

Any member of the RBA's Information and Transfer System (RITS) is eligible to participate in the US dollar term repo operations, provided that entity:

- has treasury operations in Australia;
- is able to execute and settle both Australian dollar and US dollar transactions with the RBA in an efficient and timely manner; and
- satisfies the RBA's legal requirements.

The first US dollar operation was conducted on 26 September 2008 and the RBA will conduct subsequent operations subject to market conditions and demand for US dollar liquidity in this time zone.

### **1.3. Cash**

This market relates to the borrowing and lending of cash on either a secured or unsecured basis. AFMA conventions apply to deals settled in exchange settlement cash via the RBA real time gross settlement feeder systems, that is: Austraclear, RITS or SWIFT.



Conditions relating to settlements via bank cheque or other deferred settlement methods are subject to negotiation between individual participants. Loans are usually either 'at call' or for a fixed term.

Four distinct RBA ESA trading sessions occur each day. These are:

- *The morning settlement session (7:30am - 8:45pm)*, which is open to banks holding an exchange settlement account (ESA) with the RBA. It is used by these participants to fund their previous day's deferred cash flows. Only RITS settlements are permitted in this session. Once these flows are settled the Daily Settlement Session commences.
- *The daily settlement session (9:15am - 4:30pm)*, which is open to all RITS clients for settlement of transactions via the RTGS feeder systems. Session times may vary between feeder systems, however, in general, session close is within 5 minutes of RITS close. New transactions between non-ESA holders must be matched/input into the appropriate feeder system prior to session close, even though actual settlements may not occur until the Settlement Close Session.
- *The settlement close session (4:30pm - 5:15pm)*, which is used by banks to clear payments queued in the RTGS system both on behalf of the ESA holder and their clients. Only transactions between banks are permitted in this session. An interim session is conducted between 5:15pm - 5:21pm.
- *The evening session (5:30pm - 8:30pm in summer and 6:30pm in winter)* which is mainly used by banks to clear payments associated with foreign exchange transactions cleared through the CLS system, as well as reversing intra-day repo transactions with the RBA.

#### *RBA term deposit facility*

To further enhance the flexibility of its domestic liquidity management operations the RBA, from 24 September 2008, will offer a short term deposit facility (to be known as RBA Term Deposits). The facility will be available to those institutions holding an exchange settlement account (ESA) and to authorised deposit taking institutions (ADIs) that are members of RITS. The bank will conduct auctions at which eligible institutions will be able to bid for deposits. Auctions will be conducted periodically as required for liquidity management purposes. Tender announcements will be made via the electronic news services (Reuters – RBA35 and/or Bloomberg – RBA15) at 4:00pm the previous business day.

### **1.4. Negotiable Transferable Instruments (shorter dated securities)**

A bill of exchange is defined in the Bills of Exchange Act 1909 as 'an unconditional order in writing, addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand or at a fixed or determinable future time, a sum certain in money or to the order of a specific person, or to bearer'.



At a more practical level, a bill of exchange is generally described as a negotiable transferable instrument usually maturing within 6 months, but certainly within less than 12 months (at which time it will be redeemed for its face value). It is sold at a discount to face value, which the market believes to be the obligation (ie. debt) of a first class credit. The short dated securities market is conducted by participants who buy and sell discounted instruments with a maturity of less than 365 days.

Instruments in this market raise funds when they are first issued. The purchaser of the new securities is the lender and the issuer is the borrower. Securities can be traded until they mature when their redemption extinguishes the debt.

- Bank Accepted Bills (BAB)
- Negotiable Certificates of Deposit (NCD)
- Promissory Notes (P/N) also known as commercial paper
- Treasury Notes (T/N)

ASX Austraclear and wholesale debt market participants have been encouraging dematerialisation of securities over recent years and now a significant share of short dated securities issued are in electronic form. The market will accept electronic paper - E/Bills, E/CD, E/PN. The buyer has the right to accept or decline trades where e-paper is offered, but if so declined the deal stands with physical paper being substituted.

These product standards relate only to onshore/onshore deals. However, the market expects that participants would ensure the prompt and accurate processing of transactions with all counterparties, regardless of domicile.

## 2. Methods of Dealing

Dealers may use the following methods for dealing onshore/onshore.

Type of deal	Method of Dealing		
	<i>Broker</i>	<i>Phone</i>	<i>Electronic</i>
<i>Debt Market Instruments</i>			
FIS	✓	✓	✓
Repos	✓	✓	✓
<i>Negotiable Transferable Instruments</i>			
BAB, NCD, P/N, T/N, etc.	✓	✓	-



### 3. Know Your Client

Most deals in the OTC financial markets are made orally by telephone. Knowing precisely which legal entity you are dealing with is important both when the deal is initiated and when completing confirmations. Particular care is required when the deal is being done with or on behalf of an offshore banking unit (OBU).

The trend for banks to centralise their operations underlines the need for care in recording the correct booking entity. As an example, you may deal with Deutsche Bank Auckland, but the deal requires booking and settlement with Deutsche Bank Sydney (operations for which could be further centralised in London).

Robust know-your-client procedures are now also a key prerequisite for transactions with corporate counterparties as a result of anti money laundering, anti terrorist financing and financial services licence requirements.

### 4. Confirmations

#### 4.1. What is a Confirmation?

The word confirmation describes one of the primary functions carried out by a treasury operations department to minimise risk.

Many financial market deals are the result of oral negotiations. Parties are bound from the moment they agree orally to the terms. However, because of the possibility of misunderstanding or of disputes about the exact terms, market practice is to confirm the details of all deals either electronically or in writing.

This section sets out the standards and procedures to be adopted for confirmations. They represent accepted market practice and all participants in the market are expected to follow them.

The exchange of a complete and accurate bilateral, or two way, confirmation signifies that both parties agree on the details of a deal.

A bilateral confirmation ensures that both parties are bound by the terms of the transaction and that settlement instructions are exchanged. Confirmation should take place as soon as possible after a transaction is executed so that errors can be detected and corrected promptly, ensuring minimal risk to the counterparties.

There are two main types of confirmation — primary and secondary. A primary confirmation is the initial information exchanged by the counterparties after they execute the transaction. This can be by electronic, verbal or written communication. A secondary confirmation follows as a formal verification of the details. This is usually by letter or some other written form.



## 4.2. Matching of Confirmations

Good market practice requires not only confirming each deal, but matching confirmations to ensure that the terms of the deal are identical from both counterparties' perspectives.

Errors may occur at two stages in the dealing process: either the deal is agreed orally but booked incorrectly, or there is a fault in the confirmation even though the deal is booked correctly. In either case it is necessary to correct the error and reconfirm the deal. If you are using SWIFT to confirm deals (the relevant SWIFT standards are explained in the SWIFT user handbook), you may send an amended confirmation or issue a cancellation and replacement.

Matching confirmations will avoid errors, prevent costly payment mistakes and greatly increase back-office processing efficiency. Deals should be matched (and if necessary corrected) promptly. Preferably, this should be done within 24 hours of the exchange of confirmations. Some deal types may require faster matching and this implies the use of an automated matching system.

Where possible, and particularly where volumes/exposures indicate this, market participants should use an electronic matching and settling system such as ASX Austraclear's EXIGO system to match and settle all qualified deals.

## 4.3. Acceptable Forms of Confirmation

Deals can be confirmed by the methods indicated but it should be noted that letter, fax, telex, internet and phone are the least preferred and it is intended that they should be replaced by an electronic method.

Type of deal	Method of Dealing					
	ASX Austraclear	SWIFT <sup>2</sup>	Phone <sup>3</sup>	Letter	Fax <sup>1</sup>	Electronic <sup>1</sup>
<i>Debt Market Instruments</i>						
FIS <sup>4</sup>	✓	✓	✓	✓	✓	✓
Repos <sup>5</sup>	✓	✓	✓	✓	✓	✓
<i>Negotiable Transferable Instruments</i>						
BAB, NCD, P/N, T/N, etc.	✓	✓	✓	-	✓	✓

<sup>1</sup> Parties can confirm by fax or the internet only if they have previously expressly agreed on this method and, preferably, have exchanged a Letter of Indemnity.

<sup>2</sup> Must use appropriate SWIFT message format.

<sup>3</sup> If a SWIFT confirmation has been received within one hour of a trade, a telephone confirmation is no longer required.

<sup>4</sup> See Section 4.9 for further rules on FIS confirmations.

<sup>5</sup> See Section 4.10 for further rules on Repo confirmations.

Other:



- *Internet* - this form of confirmation is not encouraged and should be covered by a bilateral indemnity or user agreement.
- *Facsimile* - once a bilateral "fax indemnity" is in place, a facsimile is an acceptable form of confirmation.
- *Letter* - can be used as a secondary form of confirmation of transactions.
- *SWIFT* - Standard-format SWIFT messages are used for confirmation of a range of transaction types. (Brief details on SWIFT are contained in *Section 5.3.5. Services and facilities offered by SWIFT to the international financial industry include:*
  - financial telecommunications; and
  - message format standardization.

Financial telecommunications is the transmission of standardised financial transactions from one user to another user in the form of structured messages.

The formatting of SWIFT messages for the processing of money market trades is demonstrated in the SWIFT User Handbook, Standards Category 5. The confirmation messages in this category are confirmations of information already known to both parties. They apply only to the contract part of the business and are not used for the transfer of funds.

These messages provide details on:

- confirmation;
- settlement; and
- advice/instruction.

In each type of message, the details of the contract are usually agreed between the dealers of the two financial institutions by telephone or electronic means. An exchange of confirmations then takes place.

The exchange of confirmations, and their careful verification, should take place as soon as possible after the deal is made. The standard messages should be used correctly to maximise straight-through processing.

Correct use of standards includes these procedures:

- A BIC code with option A should be used in the "party" fields whenever an institution has one, even if it is not yet "live" on SWIFT.
  - Field 72 should be avoided unless important information is to be conveyed for which no specific field exists.
- *Telephone* - Recorded conversations preserve the step-by-step details of a deal. They are used only for primary confirmation of onshore/onshore transactions.



- *ASX-Austraclear* - This confirmation method is only available to ASX Austraclear Participants. Transactions are entered by both counterparties into the relevant ASX Austraclear EXIGO component (the Discount Securities System for Debt Market Instruments or the Fixed Interest System for FIS and Repos). Details are then matched by the system and any discrepancies highlighted. No further confirmation is required where trades have been matched in EXIGO.

#### 4.4. When Deals are to be Confirmed

Market participants have agreed the timing conventions by which confirmation should take place for onshore/onshore transactions. These conventions are as follows:

Type of deal	Timing of Confirmation	
	<i>Within one hour of deal</i>	<i>On day of deal</i>
<i>Debt Market Instruments</i>		
FIS	-	✓
Repos	✓ <sup>1</sup>	-
<i>Negotiable Transferable Instruments</i>		
BAB, P/N, T/N, etc.	- <sup>2</sup>	- <sup>2</sup>

<sup>1</sup> With repo transactions, the confirmation of the first leg is only required when the settlement date of the first leg is later than the trade date of the first leg (i.e. not a 'same day' transaction or in some cases a 'next day' transaction).

<sup>2</sup> Currently there are no formal market standards that have been agreed by market participants for the length of time taken for confirmation of BAB, P/N, N/C/D and 'At Call Cash' because of, in the main, the 'same day/next day' settlement nature of these transaction types.

#### 4.5. Procedures for Confirmation

- *SWIFT* - Hard copy printout of the SWIFT message (or receipt into a matching system) is accepted as firm evidence of the details of the deal.
- *Electronic* - The various electronic dealing systems used in the Australian debt & FX markets usually have an in built confirmation generation capacity which are an acceptable form of confirmation for most organisations. These systems currently are:
  - Reuters
  - Bloomberg
  - Yieldbroker
  - EBS
- *Telephone*

##### When the counterparty is a financial institution

Operations personnel of either party to a deal may initiate a telephone confirmation if no confirmation has been received one hour after the transaction. Both back offices must have the dealing ticket at the time. If the back office receiving the call does not have the dealing ticket, it must obtain it and inform the other back office of the status of the deal within 30 minutes of the original call.



Format to be used over telephone when the caller is Organisation A (it is imperative that the full legal name of each organisation is used, eg Westpac Banking Corporation Limited, Sydney Office, not just "Westpac"):

- A's name
- broker's name if deal is executed through a broker, e.g., "dealt by Tullett & Tokyo Liberty"
- details of confirmation, which may include:
  - client/counterparty
  - issuer
  - coupon
  - maturity
  - face value
  - yield/price
  - settlement date
  - consideration
  - settlement method
- other relevant details
- brokers name (if applicable)

When the counterparty is a corporate

If the financial institution has not received confirmation of the deal after one hour by facsimile or Internet, its operations staff should initiate a telephone confirmation.

Failure to receive corporate confirmation could result in the following:

- Incorrect counterparty name
- Incorrect SSIs
- Failed Settlement

The financial institution has a responsibility to ensure confirmation is completed.

## **4.6. Amending Deals**

If any details of a deal are amended after the initial confirmation, the deal must be reconfirmed using the same medium as originally used.

Confirmation procedure is the same as the original confirmation except that the parties are to make it clear that they are confirming an amendment to an existing deal.

It is also recommended that a full audit trail of amendments be appropriately approved and records kept.

## **4.7. Cancelling Deals**



If a deal is cancelled after confirmation, the cancellation must be confirmed within one hour.

Confirmation procedure is the same as the original confirmation except that the parties are to make it clear that they are confirming a cancellation of an existing deal.

It is also recommended that a full audit trail supporting the cancellation be appropriately approved and records kept.

#### **4.8. Late Trading**

Deals that cannot be confirmed on the deal day because of late trading must be confirmed as soon as possible and no later than 10:00am on the following business day.

If you cannot confirm full details of a trade, try to at least confirm its existence.

#### **4.9. Additional Rules for FIS Confirmations**

When confirming a FIS transaction through ASX Austraclear, the following information is to be entered:

- Stock Issuer:
- Series:
- Seller/Buyer:
- Other Participants:
- Deal Date:
- Settlement Date:
- Face Value:
- Yield Rate:
- Deal Price:
- Consideration:
- Auto Settle: Yes/No



Market practice is to confirm outright FIS trades on trade date — i.e., all trades dealt before 5:00pm are confirmed by 6:00pm. Late trades that cannot be confirmed on the same day must be confirmed by 10:00am on the following business day.

Best practice is to achieve FIS confirmations within one hour of trading. Transactions covered by this target are all securities registered in the ASX Austraclear system: Commonwealth Government securities, Semi Government securities and corporate debt instruments.

The target is to be observed by all AFMA members, regardless of their legal status and role in the market. Trades involving non members of AFMA may have to be considered separately; confirmation times for FIS trades may have to be agreed bilaterally between these counterparties.

ASX Austraclear is the preferred confirmation system for domestic FIS trades. ASX Austraclear has reporting mechanisms indicating trades not matched/confirmed. Confirmation will be satisfied if both parties have entered the relevant trade into the system. Mismatched transactions will be considered part-confirmed and unmatched transactions will be unconfirmed.

Host-to-host and SWIFT are available on ASX Austraclear to assist in meeting the target of FIS trades being confirmed within one hour. The reporting mechanism for unconfirmed transactions encourages compliance with confirmation guidelines.

#### **4.10. Additional Rules for Repo Confirmations**

These rules assume that repos will be governed by either:

- an ISDA Master Agreement which incorporates September 1992 Australian Addendum No. 9 — Reciprocal Purchase agreements; or
- the Global Master Repurchase Agreement (GMRA). The GMRA has been produced by the International Securities Markets Association (ISMA) and The Bond Market Association (previously Public Securities Association or PSA) as a master agreement for repos. Further guidance on the use of the GMRA is to be found in AFMA's Guide to OTC Documents (Part 26).

AFMA expects that the internationally recognised GMRA will become accepted by the market because it also allows for the use of margining, making the arrangements more flexible than the AFMA/ISDA documentation.

Exhibit C to the RITS Regulations references the PSA/ISMA GRMA (as amended), setting out various elections and amendments to the standard GMRA to reflect either Australian law or the way in which The RBA mandates that participants who wish to be eligible counterparties to RBA market operations transactions be members of RITS. Nothing further is required to evidence the agreement as by becoming a member of RITS they are bound by the RITS Regulations and Conditions of Operation. The



MARKET function in ASX Austraclear's EXIGO system enables participants to initiate repo trade settlements electronically by keying matching entries.

If two parties are members of RITS but want to trade other than on the terms of Exhibit C, then they can sign a GMRA attaching AFMA Annex I, which has been developed in association with market participants for use with the GMRA in Australian domestic transactions. For further details see AFMA's Guide to OTC Documents [Part 26].

Further, parties can agree outside ASX Austraclear the terms of the master agreement to govern their transactions but still use the above-mentioned MARKET function to confirm the transactions.

Following are suggested forms of repo confirmation by letter. Version 1 is used when only the second transaction is to be confirmed (this is generally acceptable unless the first transaction does not settle on the trade date). Version 2 is for use when both the first and second transactions are to be confirmed.



*Repo Confirmation Version 1 - confirming only second leg of transaction*

[Letterhead of Party A/B]

[Date]

Name and Address of Party B/A

Dear

Reciprocal Purchase Agreement Confirmation

The purpose of this letter is to confirm the terms and conditions of a reciprocal purchase agreement entered into between us on the Trade Date specified below.

This Confirmation supplements, forms part of, and is subject to, the Master Agreement dated as of [date], as amended and supplemented from time to time.

Our reference:

Trade Date:

Reciprocal Seller:

Reciprocal Buyer:

Agreed Features of securities:

Issuer:

Coupon Rate:

Maturity:

Face Value:

First Purchase Price:

Contract Rate:

[Reciprocal Purchase Date:]

[Other provisions:]

Yours sincerely

[name of party preparing Confirmation]

By:

Name:

Title:



*Repo Confirmation Version 2 - for confirming first and second legs of transaction*

[Letterhead of Party A/B]

[Date]

Name and Address of Party B/A

Dear

**Reciprocal Purchase Agreement Confirmation**

The purpose of this letter is to confirm the terms and conditions of a reciprocal purchase agreement entered into between us on the Trade Date specified below.

This Confirmation supplements, forms part of, and is subject to, the Master Agreement dated as of [date], as amended and supplemented from time to time.

Our reference:

FIRST TRANSACTION

Trade Date:

Buyer:

Seller:

Agreed Features of securities:

Issuer:

Coupon Rate:

Maturity:

Face Value:

First Purchase Date:

First Purchase Price:

**SECOND TRANSACTION**

Reciprocal Seller:

Reciprocal Buyer:

Contract Rate:

[Reciprocal Purchase Date:]

[Other provisions:]

Yours sincerely

[name of party preparing Confirmation]

By:

Name:

Title:



Rules for amending repos:

- If the repo was originally entered in ASX Austraclear, then the amendment must be made by using the Repo function within the Market Repo Facility in ASX Austraclear.
- If the repo was originally confirmed by fax, amendments must be reconfirmed by fax.
- Variations to repos can also be confirmed with a supplementary letter confirmation.

Following is a suggested format for confirming as a letter. It should be appropriately amended if other forms of confirmation are used.

[Letterhead of Party A/B]

[Date]

Name and Address of Party B/A

Dear

Reciprocal Purchase Agreement Supplementary Confirmation

The purpose of this letter is to confirm a variation to apply from the Variation Date specified below for the specified REPO.

This Confirmation supplements, forms part of, and is subject to, the Master Agreement dated as of [date], as amended and supplemented from time to time.

REPO Reference Number: Reciprocal Seller:

Reciprocal Buyer:

Reciprocal Seller:

Reciprocal Buyer:

Variation Date:

Variations:

[New Contract Rate:]

[New Reciprocal Purchase Date:]

[Other]

Yours sincerely

[name of party preparing Confirmation]

By:

Name:

Title:



## 5. Settlement

### 5.1. What is Settlement?

Settlement (of securities) is the process whereby securities or interests in securities are delivered, usually against payment, to fulfil contractual obligations, such as those arising under securities trades. Settlement involves the delivery of securities from one party to another. Delivery usually takes place against payment, but some deliveries are made without a corresponding payment.

Settlement is the exchange of an agreed currency amount or exchange of security on a specified value date. Settlement can take a number of different forms, including:

- a one-way cash payment, made electronically or physically;
- a payment of one currency for the receipt of another currency;
- delivery v payment — the simultaneous exchange of cash for a security; or
- delivery free of payment – the movement of a security between parties without any cash payment.

### 5.2. Standard Settlement Instructions

Standard Settlement Instructions (“SSI”) are a list of standard bank account and security settlement account details exchanged between market participants. These represent the accounts through which a financial markets participant pays and receives cash or securities in settlement of financial markets transactions. The details of each bank account must be listed, including the name and location of the bank, the account number and usually the SWIFT addresses. The security settlement account details can either be those of the trading principal or that of their external settlement agent.

If SSI are in place, it is possible to take advantage of straight-through processing.

If SSI are not in place, full payment instructions and security settlement details must be exchanged at the time of the deal or no later than the time of the confirmation.

Where one counterparty wishes to deviate from the SSI, it is the responsibility of the deviating party to advise the other party of the amended or changed instruction before settlement.

### 5.3. Settlement Methods and Payment Systems



### 5.3.1. Australian Payments Clearing Association

[www.apca.com.au](http://www.apca.com.au)



APCA is a public company owned by the Australian banks, building societies and credit unions. It has been in existence since February 1992 and has specific accountability for key parts of the Australian payments system, particularly payments clearing operations.

APCA co-ordinates, manages and ensures the implementation and operation of effective payments clearing and settlement systems, policies and procedures. It is currently responsible for establishing and managing five payments clearing systems. Clearing systems provide a single, clear body of rules and decision-making structures governing the conduct of clearing and settling. These are described below.

APCA does not process payments. Individual institutions participating in each clearing system are responsible for their own clearing operations which they must conduct according to APCA's rules.

Clearing system management involves a participatory approach. The members of each clearing system appoint a committee of management with delegated powers and responsibilities. System members participate in annual meetings which provide a forum for discussion on all matters relating to the operations and management of the relevant system.

The company's reporting and decision-making structure ensures a high degree of co-ordination in managing and developing Australia's payments clearing arrangements. Membership criteria, and conditions of access and participation, are open to scrutiny and can be changed as circumstances change. Trade practices authorisation has been granted for the activities of APCA and its existing clearing systems on public benefits grounds.

APCA's charter allows it be responsive to developments in payments services. It is not restricted to regulating clearing and settlement of prevailing payments services and can adapt to the development of new payments systems by altering the classification and structure of its existing clearing systems or creating new clearing systems as the need arises.

### 5.3.2. Reserve Bank Information & Transfer System (RITS)

[www.rba.gov.au](http://www.rba.gov.au)



RITS is the platform for Australia's Real Time Gross Settlement System (RTGS), described in the previous section. It was originally developed as a securities settlement system in 1991 but this functionality ceased in February 2002.

All banks and other Exchange Settlement Account Holders are required to be members of RITS so that they can participate in RTGS. Organisations who wish to deal with the Reserve Bank in market operations transactions are also required to be RITS members.



Banks and financial institutions must manage their intra-day liquidity requirements in real time to ensure all payment obligations are met. Banks must therefore have sufficient cash in their accounts with the RBA throughout the processing day. If a bank has a shortfall of available cash during the day it must have the limits and ability to be able to borrow exchange settlement cash from the market or enter into a repurchase agreement (repo) with the RBA.

### 5.3.3. Real-Time Gross Settlement (RTGS)

[www.rba.gov.au](http://www.rba.gov.au)



The introduction by the Reserve Bank of Australia (RBA) in June 1998 of Real Time Gross Settlement (RTGS) has contributed to a reduction in credit, settlement and systemic risks.

In an RTGS system, processing and final settlement of funds transfer instructions take place continuously and immediately. As it is a gross settlement system, transfers are settled individually, without netting debits against credits. Moreover, the settlement process is based on the real-time transfer of central bank (exchange settlement account) money. An RTGS system can thus be characterised as a funds transfer system that is able to provide continuous intra-day finality for individual transfers.

RTGS systems limit payment system risk. Payments are settled irrevocably at the time of receipt through the payments system. This contrasts with the previous net-deferred method which allowed banks to make payments on an unrestricted basis during the day. Final settlement did not occur until the successful completion of the 9.00 am exchange settlement interbank process on the following business day.

Banks and financial institutions must manage their intra-day liquidity requirements in real time to ensure all payment obligations are met. Banks must therefore have sufficient cash in their accounts with the RBA throughout the processing day. If a bank has a shortfall of available cash during the day it must have the limits and ability to be able to borrow exchange settlement cash from the market or enter into a repurchase agreement (repo) with the RBA.

SWIFT PDS (Payment Delivery System) carries large-value payments on an RTGS basis. SWIFT's FIN-Copy function passes the settlement details through to the RBA using a central computer interface with the counterparties' financial institutions. SWIFT PDS is controlled by the Australian Payments and Clearing Association (APCA). Membership of SWIFT PDS is open to the RBA and all exchange settlement account-holders.

New RTGS session times were put in place with the introduction of Continuous Linked Settlement for foreign exchange transactions (see Foreign Exchange Product Standards and Procedures).



#### 5.3.4. ASX Austraclear

[www.asx.com.au](http://www.asx.com.au)



ASX Austraclear's main function is as a Central Securities Depository. It facilitates exchanges in certificates of deposit, commercial paper, semi-government bonds and notes, bills of exchange, fixed and floating rate securities and securitised assets by removing the need for a physical transfer of paper. It electronically records book-entry changes in ownership of entitlement as securities are traded or pledged as collateral. The transfer of securities occurs on what is known as a delivery versus payment (DVP) basis, i.e. ownership of securities does not change until the system receives advice that funds are cleared or free of payment (DFP) i.e. ownership of securities changes with no cash component. This means that the risk of trade failures is eliminated. Participants have the reassurance that transactions are settled in real-time funds and are confirmed by a bank.

It is important to note that ASX Austraclear is not a dealing-room trading system. It is not an exchange clearing house and it does not become party to the transaction.

Although its primary focus is as a depository for securities, the ASX Austraclear system (EXIGO) also facilitates exchange of irrevocable AUD payments (cash) between participants. ASX Austraclear allows members to coordinate their cash transactions with their banks.

ASX Austraclear delivers a range of service options designed to streamline operational processes and enhance market participants' straight through processing capabilities. Some of these options relevant to debt market transactions include:

- Deal instruments trade entry and confirmation: refer section 4.3.
- Automatic or manual (depending on the option selected at the deal entry stage) electronic deal settlement.
- AUD cash payments: ASX Austraclear offers the capability to settle electronic cash transfers via the RBA Real Time Gross Settlement (RTGS) system (see previous section). The Electronic Cash Transfers (ECTs) are two-sided and can be bank-to-corporate (B2C), corporate-to-corporate (C2C) or bank-to-bank (B2B). ASX Austraclear also accommodates fall-back End of Day settlement in the event that RTGS becomes unavailable.
- Please refer to the Austraclear System Participant User Guide for detailed information on the above functions.
- Connection via SWIFT: ASX Austraclear provides SWIFT members with the ability to interface directly with EXIGO via the SWIFT system.
- Connection via Host-to-Host Link: Host-to-Host Link provides an alternative method of delivering FIS trades or payment instructions to the ASX Austraclear system. Participants



input transactions on their own computers and transfer/ download a file of these transactions directly to the system.

ASX Austraclear participants include all licensed banks, merchant and international banks, major life insurance, superannuation and trust companies, Federal and State Government bodies, security dealers and brokers. Each member is bound by the regulations contained in the "Regulations and Operations Manual". These regulations detail the rights and obligations of all parties involved with the EXIGO system. Those wishing to join ASX Austraclear must satisfy the Board of ASX Austraclear that they are able to conform with its regulations and nominate a banker and bank account to enable ASX Austraclear to secure a bank guarantee for cash transactions.

### **5.3.5. Society for Worldwide Interbank Financial Telecommunications (SWIFT)**

[www.swift.com](http://www.swift.com)



SWIFT is the Society for Worldwide Interbank Financial Telecommunication, a member owned cooperative through which the financial world conducts its business operations with speed, certainty and confidence. Over 8,300 banking organisations, securities institutions and corporate customers in more than 208 countries trust us every day to exchange millions of standardised financial messages.

Our role is two-fold. We provide the proprietary communications platform, products and services that allow our customers to connect and exchange financial information securely and reliably. We also act as the catalyst that brings the financial community together to work collaboratively to shape market practice, define standards and consider solutions to issues of mutual interest.

SWIFT enables its customers to automate and standardise financial transactions, thereby lowering costs, reducing operational risk and eliminating inefficiencies from their operations. By using SWIFT customers can also create new business opportunities and revenue streams.

SWIFT has its headquarters in Belgium and has offices in the world's major financial centres and developing markets.

#### *Physical Security Delivery*

ASX Austraclear, through its EXIGO system, provides a service to enable the removal of the electronic record of the physical security to allow physical delivery of securities between counterparties. This service is separate to the electronic settlement system operated by ASX Austraclear.

In order for counterparties who are also members of ASX Austraclear to settle their transactions physically they must use the 'Withdrawal' functions in EXIGO in accordance with the ASX Austraclear System Regulations and Operating Manual. It should be noted that the Reserve Bank of Australia is the Registry for Commonwealth Government Securities (and some other small issuers) and as such is able to confirm uplifts of these stock types from ASX Austraclear.



Fixed Interest Securities can then be transferred via the use of Transfer & Acceptance forms and payment made by arrangement between the parties using an alternate payment means.

Discount Securities can then be physically delivered and payment made by an alternate payment means by arrangement between the parties.

Please refer to the EXIGO User Guide for further details.

It should be noted that in conjunction with the introduction of the EXIGO system, ASX Austraclear are encouraging de-materialisation of securities and advocating that new securities only be issued in electronic form.

### **5.3.6. Clearstream International**

[www.clearstream.com](http://www.clearstream.com)



The world's entire financial system is built on trust. When assets are traded, both parties must be sure they will receive their part of the transaction. Given the complexity, speed and quantity of assets involved, a fast, secure and trusted third-party is absolutely essential for settling transactions.

Clearstream is a leading European supplier of post-trading services. The wholly owned subsidiary of Deutsche Börse ensures that cash and securities are promptly and effectively delivered between trading parties. It also manages safe keeps and administers the securities that it holds on behalf of its customers. Over 300,000 domestic and internationally traded bonds, equities and investment funds are currently deposited with Clearstream.

Clearstream maintains relationships with around 2,500 customers in over 100 countries. Its global network extends across 45 markets. Backed by flexible securities lending and collateral management services, Clearstream offers one of the most comprehensive international securities services available, settling more than 250,000 transactions daily.

Clearstream International was formed in January 2000 through the merger of Cedel International and Deutsche Börse Clearing. The full integration of Clearstream was completed in July 2002.

A core part of Clearstream's service offering is the settlement of transactions in global and international securities and domestic securities traded across borders.

Additionally, for selected stock exchanges and instruments, transactions are routed to Clearstream automatically for further processing after trading on the exchange.

Secure and high-performance straight-through transaction processing enables efficient and virtually risk-free settlement.



As a custodian Clearstream is responsible for the management, safekeeping and administration of securities on deposit. We can also offer a range of custody services to reduce your custody administration costs

### 5.3.7. Euroclear

[www.euroclear.com](http://www.euroclear.com)

The Euroclear logo is the word 'Euroclear' in a bold, italicized, black sans-serif font.

The Euroclear group is the world's largest provider of domestic and cross-border settlement and related services for bond, equity, fund and derivatives transactions.

User owned and user governed, the Euroclear group includes Euroclear Bank, based in Brussels, as well as the national central securities depositories Euroclear Belgium, Euroclear France, Euroclear Nederland and Euroclear UK & Ireland.

Euroclear also owns EMXCo, the UK's leading provider of investment-fund order routing.

Euroclear's clients comprise over 2,000 professional financial institutions, located in over 80 countries worldwide:

- leading banks
- broker/dealers
- custodians
- other institutions professionally engaged in securities markets

### 5.3.8. Depository Trust & Clearing Corporation (DTCC)

[www.dtcc.com](http://www.dtcc.com)



DTCC, through its subsidiaries, provides clearing, settlement and information services for equities, corporate and municipal bonds, government and mortgage-backed securities, money market instruments and over-the-counter derivatives. In addition, DTCC is a leading processor of mutual funds and insurance transactions, linking funds and carriers with their distribution networks.

DTCC's depository provides custody and asset servicing for 3.5 million securities issues from the United States and 110 other countries and territories, valued at \$40 trillion. In 2007, DTCC settled more than \$1.86 quadrillion in securities transactions.

DTCC's joint venture company, Omgeo, has over 6,000 customers in 45 countries and plays a critical role in institutional post-trade processing, acting as a central information management and processing hub for brokers, investment managers and custodian banks.



## **5.4. Reconciliation**

### **5.4.1. What is reconciliation**

The reconciliation function in treasury operations is the final verification that the settlement process has taken place correctly for each transaction and that the appropriate account has been debited or credited. Reconciliation can take a number of forms.

### **5.4.2. Reconciliation of all Outstanding Transactions**

This reconciliation can take place in one of two formats. On a regular basis financial market participants confirm either all outstanding transactions or select a sample. They may issue an audit confirmation letter to counterparties requesting them to confirm all outstanding transaction details. Recipients of such a letter reply to the issuer noting any transaction detail differences, which are then investigated.

### **5.4.3. Dealer Position Reconciliation**

Either progressively during the day, or at close of business, the dealer's currency or product position is reconciled to internal blotter or system records. This procedure is of vital importance as it is imperative that the dealer is trading from correct internal records. Costs (losses) can be incurred where a position is incorrect and the true position is therefore not being managed.

### **5.4.4. Timeliness**

The timely reconciliation, prompt investigation and resolution of any discrepancies is essential in treasury operations. Failure to follow up items immediately increases the risk of nostro overdraft costs or late settlement costs. Non-reconciled items can also lead to market and credit risks.

### **5.4.5. Settlement Failure**

Early detection of a counterparty's failure to settle is crucial. The failure to settle could be simply an error or oversight by the counterparty, but in some cases it could be something far more serious, such as a lack of funds. In this situation, the early detection of the problem could minimise potential losses.

### **5.4.6. Cash Account Reconciliations**

A participant in the financial markets holds different currency accounts, including AUD and non-AUD for payment and receipt of funds in settlement transactions. A foreign currency account with an offshore bank (correspondent) is called a nostro (our) account.

Reconciliation of all accounts must be performed for all currencies.



The main purpose of the cash/ nostro account reconciliation is to ensure that expected cash movements agree with the actual cash movements of each currency in the cash/nostro account. If differences exist, a financial institution must follow up with either the correspondent or the counterparty to resolve the difference. The cause of the difference may be that incorrect trade information was captured or that the correspondent made an error with a payment. Accuracy and efficiency in the confirmation process avoids most errors relating to incorrect settlement.

If the cash/nostro account reconciliation is not performed, or is performed incorrectly, the actual account balances will be different from internal records. This will result in the financial institution paying overdraft costs on short balances or receiving less than market rates on any long balances. In some circumstances market risk can be incurred where an incorrect payment or receipt is a result of a transaction recorded incorrectly and this has remained undetected.

Several types of bank statements are available for reconciliation. These range from SWIFT or other electronically derived means to paper-based statements. Bank statements should be reconciled at the earliest possible time after close of business.

#### **5.4.7. Security Account Reconciliations**

Financial Markets Participants should perform daily reconciliations of Securities settled in Exigo. To perform this task effectively the reconciliations area is required to retrieve a portfolio report from the ASX Exigo system. It is recommended the participant reconcile this report to its settlement system the below fields:

- Face Value
- ISIN (on long term securities)
- Issuer
- Current Principle (Principle reducing securities)
- Maturity Date
- Beneficial holder (Stock held in Sub-Account in clients name – Safe Custody)
- Account held in Exigo (if applicable)

Any reconciliation breaks should be investigated immediately and escalated to the appropriate management level as required by organisational policy & procedures. It may identify problems within the previous day's settlement where booking or settlement discrepancies have occurred.

Security Reconciliations should be performed as soon as practicable after end of day.



## 5.5. Investigation

The investigation process determines the cause of a discrepancy and prompt follow-up action results in minimisation of any compensation claims or overdraft charges. This process is normally a result of the reconciliation process that has uncovered a discrepancy or anomaly.

Good value is defined as "giving value to a payment that the payment should have originally had if it had been affected on the original date". If the discrepancy was caused by an error at the bank then the bank must arrange to pay the counterparty the principal sum with the good value or to pay the counterparty compensation. Where one organisation has been "unduly enriched" through another organisation's error then the enriched party will be asked to return this benefit. Compensation rules for the calculation of claims apply in various jurisdictions.

## 5.6. Compensation Rules

[www.apca.com.au](http://www.apca.com.au)



The Australian Payments Clearing Association ('APCA') has developed a single set of rules for calculating compensation when a payment is made on a day other than the day agreed, or is made in error to an account or person other than agreed. These rules, known as the Standard Inter-Organisation Compensation Rules, are capable of being applied in any clearing and settlement system whose participants settle with each other by adjusting their Exchange Settlement Account balances held with the Reserve Bank of Australia.

A range of different rules has applied within the financial industry for calculating compensation when errors were made between clearing participants. Which rules apply depended largely on the nature of the underlying transaction or the method of payment used for the underlying transaction. This range of compensation rules led to confusion about which rules should be applied to a given situation.

Participants in clearing systems may also use these rules in relation to claims by their customers.

The APCA Standard Inter-Organisation Compensation Rules came into force on 13 June 2001. For further information contact APCA or see their web site.

## 6. Guideline Procedures in the case of Early Redemption of FI Securities in Austraclear

When an issuer chooses to early redeem a line of FIS securities that have been electronically lodged and traded in the Austraclear system, the following conventions should be followed to avoid ongoing administrative charges for issuer and holders, reconciliation issues for holders:



- The Issuer or its representative should contact all beneficial owners to advise of the early redemption of the said securities. This communication should be in writing and confirmed receipt at least 5 business days before the redemption settlement date.
- Upon Redemption settlement date, the Issuer or its representative should place trades in the EXIGO system to “buy” each line of stock back from each beneficial owner or its representative. Noting this is settled free of payment. The maturing funds will be credited directly to your EXIGO account via corporate actions.
- The Issuer or its representative should then request a withdrawal of the redeemed securities removing them from the EXIGO settlement system.

## **7. Guideline Procedures in the case of Lost or Stolen Physical Securities**

### **7.1. Introduction**

Even though only about 1% of AUD securities are now in the form of ‘physical’ securities, as opposed to de-materalised securities in electronic form lodged in the ASX Austraclear system, AFMA continues to published these procedure as a guide to market participants as to the action they may take to place other participants on notice when ‘physical’ negotiable securities are believed to be lost or stolen.

AFMA believes that prompt notification to all participants will greatly assist in reducing the possibility of fraudulent negotiation, thereby reducing the risk of loss to all parties to the lost or stolen negotiable securities. Accordingly, this guide primarily addresses the methods of giving such notification.

Also enclosed is an example contact list on which telephone, telex, fax numbers etc. may be recorded so as to save time when in need. These numbers should be regularly updated.

It is stressed that this procedure is a guide only and is not intended to be a complete or definitive statement of the law on the subject matter. AFMA recommends that each participant should seek legal advice as to its rights and liabilities in respect of lost or stolen negotiable securities to which it is a party.

### **7.2. Contact List**

*ASX Austraclear*

Telephone: 1300 362 257

Facsimile: +612 9256 0426

E-mail: [exigo@asx.com.au](mailto:exigo@asx.com.au)



*RBA Registry Services*

Telephone: (02) 9551 9938

Facsimile: (02) 9551 8020

E-mail: registry@rba.gov.au

*Advertising Agent*

Name:

Telephone:

OR

*Newspapers*

- Australian Financial Review
- The Australian
- The Sydney Morning Herald
- The Melbourne Age
- The West Australian
- The Courier Mail (Brisbane)
- The Advertiser (Adelaide)

(Telephone numbers can be found on the front/back page of the particular newspaper)

*Broadcasts*

- By facsimile: requires a multi number programmable (or similar) machine.
- By Reuters/Telerate: broadcast on your dealing page.
- By S.W.I.F.T.: by S.W.I.F.T. with an urgent priority

## **7.3. Checklist**

### **7.3.1. Types of Securities Covered**

- BAB/ BEB
- NCD
- P/N



### **7.3.2. Who to Advise?**

- ASX Austraclear and RBA Registry Services
- Other Participants
- The Drawer, Acceptor, Maker, Issuer (endorsers if known)
- Newspapers
- Your Security Officer(s), your Legal Advisers, the Police, your Insurers (as applicable)

### **7.3.3. What Details to Advise?**

- Type of Security
- Date of Issue
- Maturity Date
- Drawer, Payee, Acceptor and the Maker or Issuer
- Place accepted/payable (if appropriate)
- Details of prior endorsements (if known)
- Any identifying marks, numbers etc.
- Circumstances of loss/theft (if considered appropriate)

### **7.3.4. How to Advise?**

Use the electronic methods of advice for the initial notification. If it is going to take a significant period of time to put together the details listed in point 7.3.3, then a brief preliminary notification should be considered. The points listed below are not in order of importance and many of these points may be handled simultaneously.

- *Your security officer/adviser and your Legal Adviser should probably be the first advised.*

Advising police authorities should be considered especially if theft is a possibility.

Your Legal Advisers should be consulted so as to clarify your rights, duties and liabilities in respect of the lost or stolen securities.



- *Advise ASX Austraclear - Initially by telephone and facsimile.*

Have the original advice, signed in accordance with your ASX Austraclear signing authority, delivered promptly. ASX Austraclear should be requested to effect a broadcast over the EXIGO System.

- *Advise other Market Participants*

Besides advertisements in the appropriate financial press referred to below, market participants can be advised electronically.

The methods available are:

- Broadcast by Reuters and/or similar information vendor system
- Broadcast by Facsimile
- Broadcast by SWIFT

In considering the method or methods to be used, attention should be paid to the type of instrument and the likely recipients of the broadcast.

A combination could be used in an effort to cover all participants. To assist, lists of the different types of participants can be obtained from sources such as the RBA, ABA, IBSA, AFMA if not already held.

- *Advise the Drawer, Acceptor or Maker/Issuer*

Initially by telephone and follow it up in writing. Endeavour to get a name for future contact.

- *Contact newspapers to arrange advertisements.*

You should consider using The Australian Financial Review and/or The Australian along with a major paper in each capital city.

To assist you in arranging space quickly the services of an advertising agency could be considered.

## **7.4. Legal Background**

Reference should be made to your legal advisers to determine your rights and liabilities in respect of lost or stolen securities to which you may be a party or holder. These will vary depending on whether you are the maker, drawer, acceptor, payee, issuer, endorser or holder in due course.



Some points of interest are:

- The Bills of Exchange Act 1909 refers only to lost bills. It appears the Act is not concerned with the manner by which the bills have become lost. Therefore, stolen bills could be considered to be included with lost bills.
- Replacement Bills - Before arranging replacement Bills of Exchange, it would be appropriate to consider the time left until maturity. The Bills of Exchange Act 1909 Section 74 covers replacement Bills of Exchange. Points 3. to 6. following refer to replacement bills of the same tenor as the original bills and the rights/duties of the parties thereto.
- The drawer may be approached to draw a replacement bill and the drawer may require an Indemnity and adequate security for the Indemnity before signing such replacement bills: see Bills of Exchange Act 1909, Section 74 (1), (2) and (3).
- The acceptor may be approached to accept replacement bills and may require an Indemnity and adequate security for the Indemnity before signing such replacement bills: see Bills of Exchange Act 1909, Section 74 (5), (6) and (7).
- The endorser(s) may be approached to endorse replaced bills and may require an Indemnity and adequate security for the Indemnity before signing such replacement bills: see Bills of Exchange Act 1909, Section 74 (8), (9) and (10).
- Should the drawer, acceptor and/or endorser refuse to draw, accept or endorse, as the case may be the replacement bills an application can be made to the court for an order so directing them to draw, accept or endorse, as the case may be: see Bills of Exchange Act 1909, Section 74 (11) and (12).
- The Bills of Exchange Act 1909 stipulates rules for presentation for payment and it should be noted that non-presentation shall discharge the drawer and endorsers: see Section 50 (1). Rules for presentation for payment are listed in Section 50 (2), whilst legally acceptable excuses for delay or non-presentation for payment are listed in Section 51.
- Providing the loss or theft of the bill was beyond the control of the holder and not due to his default, misconduct or negligence, the acceptor would normally find it difficult to avoid his liability on the bill by reason of its loss or theft. This view must be considered in terms of the type of acceptance, i.e. whether general or qualified: see Section 57 (1) and (2).

It is usual market practice for acceptances to be in general rather than specific form and therefore, in cases of a general acceptance the acceptor would not be discharged from his liability by way of the holder being unable to present a lost or stolen bill.

## **7.5. Other Issues**



#### *Promissory Notes*

Promissory Notes are specifically covered by part {IV} of the Bills of Exchange Act and Section 95 (1) provides for the application to Promissory Notes of Part {II} or the Act.

#### *Negotiable Certificates of Deposit (NCD)*

Most NCDs are drafted as promissory notes but need not take that form. The provisions of the Act as they relate to Promissory Notes would also apply to NCDs where they take the form of Promissory Notes.

#### *Insurance*

Each market participant should ensure that its insurance coverage is adequate to cover the possible risks associated with lost securities.

#### *ASX Austraclear*

The risk of loss or theft of negotiable instruments is increased with the increase in physical 'handling'. AFMA strongly recommends that all participants in the market consider utilising the services of ASX Austraclear for lodgment, trading and safe-keeping of securities.

#### *Reference Material*

AFMA recommends that each participant for their reference, should have available an up to date copy of the Bills of Exchange Act 1909. Also a copy of an authoritative reference book for example 'Riley's Bills or Exchange', Third Edition by Chappenden and Bilinsky.

## **7.6. Sample Communications and Documentation**



Example Advertisement

**WARNING OF LOST/STOLEN NEGOTIABLE INSTRUMENTS**

Notice is given that a number of Bills of Exchange, Promissory Notes and Negotiable Certificates of Deposit were lost/stolen from the offices of ..... on .....

Some of the stolen instruments are negotiable to bearer. Others are negotiable to order of specified payees. The instruments mature between ..... and ..... Full Particulars are set out below.

[SET OUT FULL PARTICULARS HERE]

Should any of the stolen instruments come to your attention they should not be negotiated or paid, or taken in satisfaction of any payment or other obligation.

You are requested to contact ..... immediately. Telephone No: .....

.....  
MANAGING DIRECTOR

Example Indemnity in relation to lost Bills Payable on specified date (to Accepting Bank by last Holder).

THIS REQUEST AND INDEMNITY is made the ..... day of ..... 20.....

BETWEEN:

..... {name of acceptor}("the bank")

AND

..... {last known holder of bill} of  
..... ("the Holder")

RECITALS:

A. On the ..... day of ....., 20..... {name of drawer} drew a Bill of Exchange Serial Number ..... on the Bank having a face value of \$..... and due on the ..... day of ....., 20..... ("the Bill").

B. The Bill was purchased by the Holder.



C. The Bill was lost by the Holder and the Holder did not negotiate, lodge or dispose of it to a third party.

D. The Holder had made a diligent search for the Bill but it has not been found.

E. The Holder has requested the Bank to pay the face value of the Bill without production of the Bill upon the following terms and conditions:

1. The Holder represents and warrants:

- a) That the Holder has lost the Bill and that the Holder has caused diligent searches
- b) That the Holder has not negotiated, lodged or disposed of the Bill in any way to any third party.

2. The Holder HEREBY REQUESTS the Bank to pay the Holder the sum of \$..... (insert face value of Bill) without production of the Bill.

3. The Bank agrees to pay the Holder the sum referred to in clause 2 after the due date without production of the Bill provided that the Bill has not been presented by any person to the Bank for payment on the date of maturity of the Bill.

4. In consideration of the Bank agreeing to make the payment pursuant to the Holder's request the Holder hereby unconditionally and irrevocably undertakes to indemnify the Bank and keep the Bank indemnified against all claims, demands, actions, losses, expenses (including reasonable legal expenses) however arising or incurred by the Bank on the Bill, or in consequence of, or in connection with, the presentation of the Bill to the Bank for payment.

5. If in the opinion of the Bank, the Bank is obliged to pay any person (other than the Holder pursuant to this agreement) on or in respect of the Bill, the Holder HEREBY AGREES that, upon written demands, it will immediately pay to the Bank the sum equivalent to the face value of the Bill together with any other sum to which the Bank is entitled pursuant to clause 4 hereof.

6. Should the Holder fail to pay the Bank immediately the total amount demanded pursuant to clause 5 above, the Bank is hereby authorised to debit any account or accounts in the name of the Holder with the amount so demanded (and to open an account in the name of the Holder if the Bank deems necessary for such purpose). Any overdrawn balance shall bear interest at the current rate charged by the Bank for overdrafts.

7. Upon payment to the Holder by the Bank pursuant to the Holder's request in Clause 2 hereof, the Bank shall be entitled to the property in and possession of the Bill. The Holder HEREBY AGREES not to make any claims against the Bank in respect of the Bill (other than pursuant to the request contained herein) and should the Bill be subsequently found, or come into the Holder's possession or control, the Holder shall



return the Bill to the Bank.

EXECUTED on behalf )  
of )  
{holder} by its )  
Attorney )  
) )  
under the Power of Attorney dated )  
) )  
In the presence of: )

EXECUTED on behalf )  
of )  
{bank} )  
by its Attorney )  
) )  
under the Power of Attorney dated )  
) )  
(who states that he holds the office in the )  
bank indicated under his signature) in the )  
presence of: )

Example Written Notification to Market Participants

[DATE]

Dear Sir

A number of Bills of Exchange, Promissory Notes and Negotiable Certificates of Deposit were lost/stolen from the offices of our company on ..... Particulars of the lost/stolen paper are attached to this letter.

Although none of the paper is presently payable on demand (maturity dates range between ..... and .....), some of it is payable to bearer.

There may be an attempt to negotiate the lost/stolen paper by forging further endorsements or negotiating to persons who have no knowledge of the loss/theft.

Will you please notify all relevant staff and branches of the loss/theft and circulate the attached list of the particulars of the lost/stolen paper.

Please notify the undersigned immediately should any person attempt to negotiate any of the paper to you (or present it for payment on maturity). You should not pay on or give value for any of the



lost/stolen paper. Any endorsements appearing on the paper other than the last endorsement shown on the attached particulars may be forged or of a holder with no title.

Your co-operation in assisting us in tracing the paper (and the thieves) would be appreciated.

.....  
MANAGING DIRECTOR

## 8. Australian and International Documentation

### 8.1. ISDA Master Agreements and User's Guide

[www.isda.org](http://www.isda.org)



The International Swaps and Derivatives Association (ISDA) Master Agreement is used in conjunction with ISDA Definitions (including standard formats for confirmations) to document a wide range of financial markets transactions, including derivatives transactions, between market participants both within Australia and across multiple jurisdictions. The Master Agreement is also designed to facilitate single or cross-product netting by novation and collateralisation. The most recent version is the 2002 Master Agreement, although the 1992 Master Agreement remains valid and is still widely used. The 1992 agreement also accommodated transactions that could be documented under the earlier 1987 agreements with their 1989 and 1990 addenda.

ISDA has also prepared a User's Guide. This manual is designed to assist in understanding and using the 2002 ISDA Master Agreement, definition booklets and forms of confirmation. It provides a detailed, section-by-section review of the 2002 Master Agreement and how it differs from the 1992 Master Agreement, as well as sections dealing with tax matters, set-off and HpML.

For derivatives products, the ISDA Master Agreement is the most widely accepted documentation used. The Master Agreement forms the basis for AFMA's Guide to OTC Documents.

Counterparties should attempt to have an ISDA Master Agreement in place prior to entering into derivatives transactions. Where a transaction is agreed prior to the execution of a Master Agreement, the confirmation should state that the transaction has been entered into on the basis of the standard terms contained in the ISDA Master Agreement pending negotiation and execution thereof. Refer section 4 above for recommended wording by product type.



## 8.2. International Capital Markets Association – Global Master Repurchase Agreement

[www.icma-group.org](http://www.icma-group.org)



ICMA is a unique self regulatory organisation and an influential voice for the global capital market. It represents a broad range of capital market interests including global investment banks and smaller regional banks, as well as asset managers, exchanges, central banks, law firms and other professional advisers amongst its 400 member firms. ICMA's market conventions and standards have been the pillars of the international debt market for almost 40 years, providing the self regulatory framework of rules governing market practice which have facilitated the orderly functioning and impressive growth of the market. ICMA actively promotes the efficiency and cost effectiveness of the capital markets by bringing together market participants including regulatory authorities and governments.

The expanding role of the Association in response to the growing challenges of increased regulation, lead to the formation of the International Capital Market Association in July 2005 by the merger of the International Securities Market Association (ISMA) and the International Primary Market Association (IPMA), creating an organisation with a broad franchise across the primary and secondary international capital market. This new association has the mandate and the means to represent the interests of the investment banking industry in maintaining and developing an efficient and cost effective international market for capital.

A reciprocal purchase agreement (repo) is an agreement for the sale of securities having certain features by one entity (A) to another entity (B), with another agreement entered into at the same time for the sale by (B) to (A) of securities having the same features. The second transaction is settled at a time following settlement of the first transaction.

In July 1996 the Reserve Bank of Australia incorporated then PSA/ISMA Global Master Repurchase Agreement (GMRA) Terms into the RITS Regulations. All repos entered into through ASX Austraclear (which has since taken over the settlement function for Commonwealth Government Securities) are governed by these terms. The most recent version of these terms is known as the Global Master Repurchase Agreement, published in 2000.

The GRMA Terms are internationally recognised and also allow for the use of margining, making arrangements more flexible than the AFMA/ISDA documentation. AFMA therefore expects that the GMRA Terms will be accepted by the market as standard terms and conditions.

It still acceptable, however, to use existing documentation for repo transactions that are not entered into through ASX Austraclear.

## 8.3. AFMA Guide to Australian OTC Transactions

[www.afma.com.au](http://www.afma.com.au)



The Guide to Australian OTC Transactions provides a standardised approach to the legal documentation necessary for participants transacting in Australian over-the-counter (OTC) markets. Essentially, it is the reference gateway to bilateral documentation providing a low cost alternative to seeking legal advice on ISDA® and other Master Agreements & Addenda.

### **8.3.1. Background to the Guide**

In 1987 the International Swaps and Derivatives Association, Inc. developed a standard Master Agreement for use in risk management markets. The AFMA Guide to Australian OTC Transactions ("the Guide") was first published in 1990 as a guide to members of AFMA for using that document when the parties wanted to specify the governing law as the law in force in one of the Australian states or territories.

The options available to parties wanting to participate in risk management markets has expanded significantly since 1990, with the ISDA Master Agreement being updated with new 1992 and 2002 versions, new master agreements being released by other organisations, new products being introduced to the industry and significant changes to the regulatory structure affecting risk management products.

The Guide has been prepared and updated by Mallesons Stephen Jaques, Solicitors (with the exception of 3.11 "Environmental products" and 3.12 "Gas Transactions" which have been prepared by and updated by Johnson Winter & Slattery) under instructions from the AFMA Documentation Committee ("the Committee"), member firms of which are elected every two years by AFMA Financial Markets members directly involved in documenting financial markets transactions. The Committee typically has representatives from domestic and international banks, state treasury corporations and funds managers.

### **8.3.2. What does the Guide Contain?**

The Guide is separated into six parts:

- 1) "How to use this Guide" is an introduction on the use of the Guide.
- 2) "Master Agreements" which is a commentary on the Master Agreements covered by the Guide.
- 3) "Products" contains guidance on how to document particular types of risk management products using the ISDA Master Agreement.

"Confirmations" describes the use of confirmations including the use of long form confirmations.

The products covered by the Guide are:

- Interest rate products;



- Currency products;
  - Credit derivatives;
  - Equity derivatives;
  - Securities lending;
  - Repos;
  - Electricity;
  - Optional electricity clauses;
  - Commodities;
  - Environmental products; and
  - Gas.
- 4) "Issues" is commentary on selected issues facing market participants, including regulation, tax, netting, investment managers, novations, collateral and EMU.
  - 5) "Cases on derivatives" contains summaries, and links to published judgments, of cases dealing with derivatives.
  - 6) "History and Update" contains PDFs of prior versions of the Guide.

### **8.3.3. Purpose**

The purpose of the Guide is to facilitate the use of the ISDA Master Agreement or, where appropriate, the other master agreements by having a recommended approach and to ensure that the amendments made to the master agreements for use under the law in force in one of the Australian states or territories are as uniform as possible.

It achieves this by providing legal commentary on the ISDA Master Agreement and, where appropriate, other master agreements, when the parties want to specify the governing law as the law in force in one of the Australian states or territories (other than South Australia, Tasmania and the Northern Territory).

With the AFMA Documentation Committee overseeing maintenance of the Guide, updates are incorporated in a timely manner. The latest version is available online to all subscribers' employees for a single annual access fee.



Who should subscribe?

- Institutions that transact in OTC markets
- Settlements and confirmations departments
- Risk managers
- Corporate Legal officers
- Consulting and advisory bodies
- Participants in the energy sector

Training courses on the use of the Guide to Australian OTC Transactions are available.

- Introductory OTC Documentation
- Advanced OTC Documentation