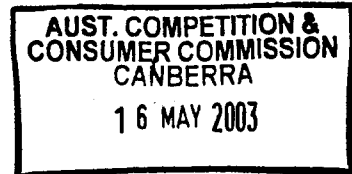


Freehills

15 May 2003

Our ref DBR:MMS:34F
 Phone 9225 5523
 Email donald.robertson@freehills.com
 Matter no 80499574
 Doc no SYDNEY\004395859

Mr Tim Grimwade
 General Manager
 Adjudication
 Australian Competition and Consumer Commission
 470 Northbourne Avenue
 DIXON ACT 2602



Dear Mr Grimwade

Australian Stock Exchange – Section 2 of the ASX Business Rules Authorisation Application

We act for Australian Stock Exchange Limited (ASX).

Please find enclosed an application submitted by ASX for authorisation under section 88(1) of the *Trade Practices Act 1974* pertaining to arrangements which, by reference to Section 2 of the ASX Business Rules, govern the operation of the Stock Exchange Automated Trading System (SEATS) for the trading of securities in the stock market conducted by ASX.

As explained below, we ask that an interim authorisation be granted for a period of six months as the ASX is currently reviewing section 2 of the Business Rules which may impact upon any final decision as to authorisation.

Background to application

The Australian Competition and Consumer Commission (**Commission**) last granted authorisation in respect of section 2 of the Business Rules on 1 April 1998. Authorisation was sought following certain amendments to section 2 of the Business Rules which had previously been authorised in 1992. Authorisation was granted for a period of 5 years to remain in force until 23 April 2003.

No substantive amendments have been made to Section 2 of the Business Rules since the 1998 authorisation.

Review of Section 2 of the Business Rules

As outlined in our telephone conversation with Ms Joanne Palisi on 16 April 2003, and as explained in greater detail within the enclosed submission, Section 2 of the Business Rules are currently being reviewed by ASX in response to changes to the *Corporations Act*. This review process is expected to be complete

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by October 2003 and may result in amendments to the Rules. The ASX therefore wishes to reserve the right to present additional information to the Commission which may be relevant to the authorisation application as a result of this review process.

Enclosures

Please find enclosed:

- (a) completed copy of Form A, the form prescribed by regulation for authorisation of agreements affecting competition;
- (b) a cheque for \$7,500 being the relevant fee for lodging one application for authorisation under section 88(1);
- (c) a copy of ASX's submission to the Commission;
- (d) a list of the Trading Participants of ASX; and
- (e) a copy of Section 2 of the Business Rules.

Requested Authorisation

Given the current review of Section 2 of the Business Rules ASX requests, in addition to a final authorisation with respect to Section 2 of the Business Rules, that the Commission grant the ASX interim authorisation for a six month period based upon the information presented in the enclosed submission. The granting of an interim authorisation will ensure that the ASX can provide the Commission with complete information as to any amendments to Section 2 of the Business Rules and the manner in which Section 2 of the Business Rules generally applies relevant amendments to the Business Rules, which may impact upon any final decision as to authorisation.

If you have any questions with respect to the above please do not hesitate to contact me.

Yours faithfully
Freehills



Donald Robertson
Partner

cc: Joanne Palisi

FORM B

Regulation 7

[Front of Form]

COMMONWEALTH OF AUSTRALIA

Trade Practices Act 1974 ---- Sub-section 88(1)

AGREEMENTS AFFECTING COMPETITION: APPLICATION FOR AUTHORISATION

To the Australian Competition and Consumer Commission:

Application is hereby made under sub-section 88(1) of the *Trade Practices Act 1974* for an authorisation under that sub-section

* to make a contract or arrangement, or arrive at an understanding, a provision of which would have the purpose, or would have or might have the effect, of substantially lessening competition within the meaning of section 45 of that Act.

* to give effect to a provision of a contract, arrangement or understanding which provision has the purpose, or has or may have the effect, of substantially lessening competition within the meaning of section 45 of that Act.

* (Strike out whichever is not applicable)

(PLEASE READ DIRECTIONS AND NOTICES ON BACK OF FORM)

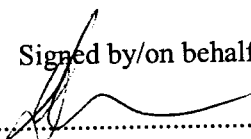
1. (a) Name of Applicant
Australian Stock Exchange Limited ACN 008 624 691
(See Direction 2 on the back of this Form)
- (b) Short description of business carried on by applicant
Stock Exchange
- (c) Address in Australia for service of documents on the applicant
C/- Mr Donald Robertson, Freehills, MLC Centre, Martin Place, Sydney NSW 2000
2. (a) Brief description of contract, arrangement or understanding and, where already made, its date
Agreement incorporating Section 2 of the ASX Business Rules used to govern participation in and the operation of the Stock Exchange Automated Trading System (SEATS) for the trading of securities in the stock market conducted by ASX.
- (b) Names and addresses of other parties or proposed parties to contract, arrangement or understanding
All Trading Participants of ASX as may change from time to time. The names and addresses of current Trading Participants are enclosed.
(See Direction 4 on the back of this Form)
3. Names and addresses (where known) of parties and other persons on whose behalf application is made
See 2 (b)
4. (a) Grounds for grant of authorisation
Please refer to the attached submission
- (b) Facts and contentions relied upon in support of those grounds
Please refer to the attached submission
(See Notice 1 on the back of this Form)
5. This application for authorisation may be expressed to be made also in relation to other contracts, arrangements or understandings or proposed contracts, arrangements or understandings, that are or will be in similar terms to the above-mentioned contract, arrangement or understanding.
 - (a) Is this application to be so expressed?
No
 - (b) If so, the following information is to be furnished
 - (i) the names of the parties to each other contract, arrangement or understanding:
N/A
 - (ii) the names of the parties to each other proposed contract, arrangement or understanding which names are known at the date of this application
N/A

(See Direction 5 and Notice 2 on the back of this Form)

6. (a) Does this application deal with a matter relating to a joint venture (See section 4J of the *Trade Practices Act 1974*)?
No
- (b) If so, are any other applications being made simultaneously with this application in relation to that joint venture?
N/A
- (c) If so, by whom or on whose behalf are those other applications being made?
N/A
7. Name and address of person authorised by the applicant to provide additional information in relation to this application:
C/- Mr Donald Robertson, Freehills, MLC Centre, Martin Place, Sydney NSW 2000

Dated 15 May....., 2003.....

Signed by/on behalf of the applicant


.....
(Signature)

DONALD BRUCE ROBERTSON
.....
(Full Name)

Solicitor ASX Limited
.....
(Description) Freehills,

Australian Stock Exchange Limited SEATS

Submission to the

**Australian Competition and
Consumer Commission**

15 May 2003

Freehills

MLC Centre Martin Place Sydney New South Wales 2000 Australia
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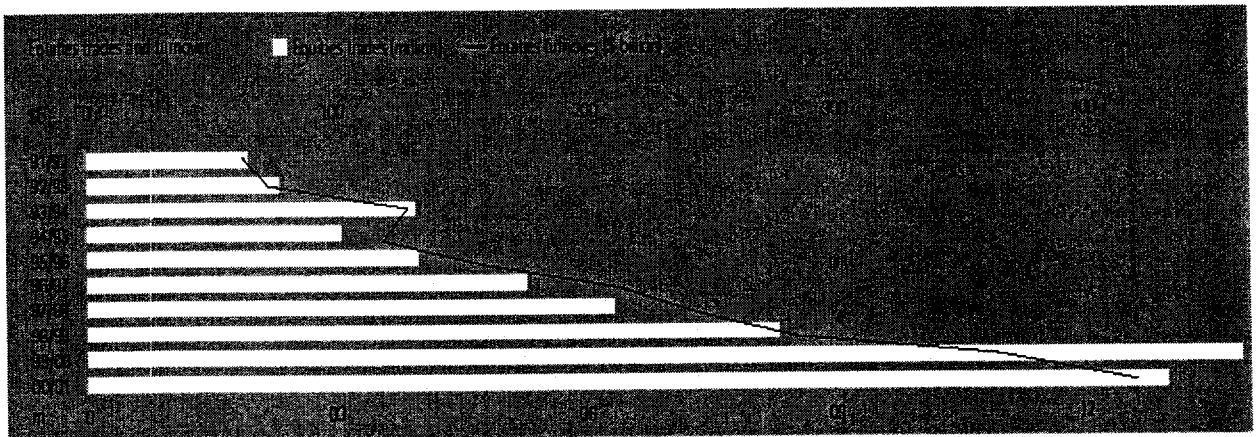
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1 ASX: An overview

- 1.1 Australian Stock Exchange Limited (**ASX**) operates Australia's primary national stock exchange for equities, derivatives and fixed interest securities. Originally a mutual organisation of stockbrokers, demutualisation took place on 13 October 1998 with ASX shares being traded on ASX's own exchange the following day.
- 1.2 As at the end of June 2002, the Australian equity market was ranked ninth in the Morgan Stanley Capital International Global Index with a relative weighting of 1.8%. During the 2001/2002 fiscal year, ASX recorded daily averages of 56,144 equity trades, the making of 58,759 options contracts and an average of 1,889 warrant trades. Equity trades are made with respect to shares of the approximately 1,500 companies listed on ASX.
- 1.3 As shown in the chart below, trading volume on ASX has increased substantially since 1991.



Supervisory Role of ASX

- 1.4 Pursuant to the *Corporations Act* ASX acts as a co-regulator of market activity through productive collaboration with the government regulator the Australian Securities & Investment Commission (**ASIC**). As a market licensee ASX is required to undertake a number of regulatory and reporting functions.
- 1.5 Under section 792(A) ASX is obliged, *inter alia*, to:
 - ensure an orderly, fair and transparent market (paragraph a);
 - comply with conditions of its licence (paragraph b);
 - have adequate arrangements for supervising the market including monitoring the conduct of participants and enforcing compliance (paragraph c); and
 - have sufficient resources to operate the market properly and with required supervisory arrangements (paragraph d).

1.6 The following table summarises ASX's supervisory activities:

Area of supervision	Market integrity activities
Markets	<ul style="list-style-type: none"> • Surveillance of market activity. • Identifying unusual trading. • Preliminary investigation of unusual trading and where necessary, referral to ASIC or relevant ASX areas.
Listed Entities	<ul style="list-style-type: none"> • Setting standards for listed entities through the ASX Listing Rules. • Supervising compliance with the ASX Listing Rules.
Market Participants	<ul style="list-style-type: none"> • Setting standards for participants, including prudential and systemic risk management through the ASX Business Rules. • Supervising compliance with the ASX Business Rules and relevant provisions of the Corporations Act. • Supervising compliance with the SCH Business Rules (the business rules governing the operation of CHES). • Investigation of breaches and presentation of appropriate cases for disciplinary action.
Systems	<ul style="list-style-type: none"> • Establishing standards for the testing and authorisation of designated trading representatives. • Maintaining trading parameter settings and the access passwords. • Monitoring compliance with trading rules and procedures. • Reporting of "incidents" to relevant ASX areas.

1.7 The development of ASX's Business Rules and other aspects of its supervisory structure are in response to both legislative requirements and the understanding that adequate supervision of ASX's markets creates confidence in Australian capital markets to the benefit of Australian companies, Australian investors, the Australian economy as a whole, as well as to ASX itself.

1.8 ASX's success in ensuring well ordered and supervised markets helps to draw international capital to such markets, thereby improving access to cheaper capital for listed companies. The retention and accumulation of domestic listings in Australia also feeds broader economic prosperity through jobs, taxation revenue and domestic reinvestment of business earnings. Investors are drawn to markets which are conducted with fairness and integrity, whose services are provided efficiently and markets which have adequate degrees of liquidity. The supervisory functions promulgated by ASX are in support of these goals.

2 Background to Current Application

Business Rules Authorised in 1998 and 1992

- 2.1 On 1 April 1998 the Australian Competition and Consumer Commission (**Commission**) granted authorisation to ASX with respect to Section 2 of the ASX Business Rules insofar as the Rules could constitute an arrangement which may have the purpose or effect of substantially lessening competition within the meaning of section 45 of the Trade Practices Act 1974 (**Act**) (**1998 Determination**).¹
- 2.2 The 1998 authorisation was sought due to amendments to Section 2 of the Business Rules. The Commission had previously granted authorisation with respect to Section 2 of the Business Rules in 1992.
- 2.3 Section 2 of the Business Rules govern the operation of the Stock Exchange Automated Trading System (**SEATS**) for the trading of securities in the stock market operated by ASX.
- 2.4 Authorisation was granted for a period of five years to remain in force until 23 April 2003.

1998 Authorisation due to introduction of open interface

- 2.5 The amendments to Section 2 of the Business Rules accommodated the SEATS 97 Open Interface project (**SEATS 97**). Open Interface refers to the published electronic protocol and method structure which facilitates communication between computer systems. It provides the mechanisms for Trading Participants to enter into and report dealings in securities by sending trading messages to SEATS. The introduction of an Open Interface environment allowed Trading Participants to customise dealing systems or trading terminals to suit their particular business needs.

Current status of Section 2 of the Business Rules

- 2.6 No material amendments have been made to Section 2 of the Business Rules since the 1998 Determination. However, as explained below, an anticipated review of the Business Rules by ASX due to changes to the market licensing provisions of the *Corporations Act* may result in future amendments.
- 2.7 ASX holds an Australian market licence under section 792(A) of the *Corporations Act* which was introduced in March 2002. ASX is in the process of reviewing, and where necessary re-drafting, its operating rules (including Section 2 of the Business Rules) to comply with the terms of its licence and the March 2002 amendments to the *Corporations Act*. ASX expects to lodge any new rules for approval with ASIC no later than October 2003.

¹ The Business Rules themselves do not constitute an agreement. Rather, as a condition of participation in the ASX trading system Trading Participants (formerly known as Member Organisations prior to demutualisation) agree to comply with the ASX Business Rules.

2.8 ASX must ensure that it complies with current legislative requirements regarding operating rules and written procedures by March 2004.

3 Purpose of Business Rules

- 3.1 By establishing the structure of the ASX trading platform and trading system, the Business Rules promote market transparency and discourage market manipulation. The Business Rules thereby create confidence in the ASX system to the benefit of participants and, consequently, ASX's competitive position with respect to competing exchanges worldwide. In addition, the Business Rules promote market efficiencies thereby maximising liquidity to the benefit of Trading Participants, listed entities and, ultimately, the investing public. Specific objectives of the Business Rules include the following:
- to provide a framework for Trading Participants to comply with the operational rules;
 - to maintain an orderly, fair and informed market;
 - to ensure that market participants do not interfere with the efficiency and integrity of ASX's markets or the proper functioning of SEATS;
 - to promote transparency;
 - to maximise liquidity in the market for securities;
 - to maintain and improve ASX's competitive position in the global context; and
 - to maintain public confidence in its markets.
- 3.2 Not only is there *significant* public benefit in having rules and procedures guiding the efficient operation of the ASX markets, such rules are required by the *Corporations Act*. In addition, the Business Rules can be considered as pro-competitive in creating conditions whereby ASX can compete for listings with other exchanges worldwide and that in providing a secure and efficient environment for market participants and investors, competition for the provision of services within the ASX system is promoted.
- 3.3 It is noted that the Commission did not identify any detriments to competition flowing from Section 2 of the Business Rules within the 1998 Determination.

4 The 1998 Determination

Objectives of SEATS 97

- 4.1 SEATS 97 (the advent of which gave rise to the amendments noted in the 1998 Determination) introduced an open interface environment allowing Member Organisations (now, following demutualisation, referred to as Trading Participants) greater flexibility in their utilisation of the SEATS System by removing the requirement to use a standardised ASX terminal thereby increasing operational efficiency.
- 4.2 Paragraph 9 of the 1997 Submission states:

"In essence, the SEATS Open Interface facility supports the order placement sector of the cycle of equities transaction; that is, the series of processes flowing from an investment decision including choosing a market, deciding on and engaging intermediaries and giving instructions."

1997 amendments and findings by the Commission

- 4.3 The 1997 amendments, which were authorised by the 1998 Determination, addressed issues that arose specifically from the open interface environment such as market integrity, financial risk, security, audit trail and dealing related issues. The authorised amendments were in respect of the subject categories described below.²

(a) Automated Order Processing (AOP)

AOP is the process by which orders are registered in a Trading Participant's system and, if accepted for submission into SEATS by the Trading Participant submitted as corresponding trading messages without being keyed or re-keyed.³

ASX's primary objective in moving to AOP was to keep pace with competitor stock exchanges.⁴

The rules regarding the operation of AOP and Automated Client Order Processing (which is included as part of AOP), place certain obligations on Trading Participants. ASX noted in its 1997 Submission that these rules and procedures are necessary for reasons of efficiency and integrity of ASX's market or the proper functioning of SEATS. This was accepted by the Commission in the 1998 Determination.⁵

² Please see the 1997 Submission or the 1998 Determination for more detailed information. Please note that although the currently used term 'Trading Participant' is used to refer to entities with trading access to SEATS the 1998 Determination, as it was prior to the demutualisation of ASX, referred to Member Organisations.

³ 1997 Submission at paragraph 19.

⁴ 1997 Submission at paragraph 25.

⁵ 1998 Determination at paragraph 7.39.

(b) Designated Trading Representatives

Only designated trading representatives are permitted to submit trading messages and conduct trading in SEATS on behalf of a Trading Participant.⁶

Section 2 of the Business Rules limited access to the market to designated trading representatives who hold a Dealers Licence or proper authority from the Trading Participant permitting that person to deal in securities. Furthermore, in order to obtain registration as a designated trading representative, a person must pass an exam in relation to the dealing rules.⁷

The Commission considered that there is public benefit in rules that limit access to the market to suitably qualified and experienced people provided that such rules do not unduly restrict participation and provided there are adequate appeal mechanisms in place.⁸

(c) Orderly market and manipulative trading

As noted by ASX, rules concerning the maintenance of an orderly market and manipulative trading imposed (and continue to impose) an obligation on the Trading Participant to ensure the conduct of an orderly market and prohibit trading which will have the purpose or effect of creating a false or misleading appearance of active trading in securities.⁹

The amended rules clarified the nature and scope of the Trading Participant's obligations. ASX noted that there is public benefit in ASX having powers to take appropriate enforcement action to protect the interests of its markets.

The Commission accepted that the amended rules provide more guidance as to what is expected from Trading Participants than was previously the case.¹⁰ The Commission further noted that an appeal process is available (in response to an ASX determination that a Trading Participant has breached the rules) which acted to limit "the likelihood that undefined terms which are open to interpretation will be interpreted in an anti-competitive way."¹¹ Finally, the Commission noted that the manipulative trading provisions reflected prohibitions against false trading and market rigging contained within the Corporations Law.

⁶ 1997 Submission at paragraph 15. In response to changes to the Corporations Act Section 2 of the Business Rules now refer to holders of a Dealers Licence, an Australian Financial Services Licence or a Representative of a Trading Participant.

⁷ 1997 Submission at paragraph 16.

⁸ 1998 Determination at paragraph 7.53.

⁹ 1998 Determination at paragraph 7.54.

¹⁰ 1998 Determination at paragraph 7.58.

¹¹ 1998 Determination at paragraph 7.60.

(d) ASX market control powers

The Commission reviewed ASX's market control powers which enable ASX to suspend the trading permission of a Trading Participant or access to SEATS where it is necessary for the efficiency and integrity of the ASX markets or the proper functioning of SEATS.¹² The market control powers also enable ASX to restrict access to SEATS in particular circumstances, including where it is considered necessary to maintain an orderly, fair and informed market or where a Trading Participant is suffering technical difficulties.¹³

ASX noted that "it is essential in an automated market operating with an open interface that ASX has specific additional powers to ensure that the market is conducted in a fair and orderly manner".¹⁴

The Commission accepted that it is important for the protection of the integrity of the market and the investing public that ASX has access to powers to take immediate actions under the rules and in view of its obligations under the Corporations Law.¹⁵

Final Determination as to authorisation

4.4 Within the 1998 Determination the Commission did not identify any detriments flowing from Section 2 of the Business Rules. Further, and following its acceptance of ASX's rationale for promulgating the Business Rules, the Commission found that in all the circumstances the arrangements for which ASX sought authorisation:

- are likely to result in a benefit to the public; and
- that benefit would outweigh the detriment to the public constituted by any lessening of competition that would be likely to result from the arrangements.¹⁶

4.5 Consequently, the Commission granted authorisation for a period of five years until 23 April 2003.

¹² 1997 Submission at paragraph 53.

¹³ 1997 Submission at paragraph 57.

¹⁴ 1997 Submission at paragraph 60.

¹⁵ 1998 Determination at paragraphs 7.68 to 7.70.

¹⁶ 1998 Determination at paragraph 8.1.

5 Amendments since 1998 Determination

5.1 No material amendments have been made to Section 2 of the Business Rules since the 1998 Determination. Relevant non-material changes include:

- changes of the term “Membership Organisations” to the term “Trading Participants”, reflecting the demutualisation of ASX as anticipated and referred to in the 1998 Determination; and
- the inclusion of Rule 2.1A “Entitlement to Trade on SEATS”; and
- Rule 2.3.2A “Communications with SEATS”.

Rule 2.1A

5.2 Rule 2.1A sets out the requirement that only Trading Participants are allowed to submit trading messages into SEATS and enter into ASX transactions as well as setting out basic registration and notification requirements in order to be considered a Trading Participant. It is not necessary that a Trading Participant be a Clearing Participant. Rule 2.1A therefore also sets out the general criteria to be considered a Clearing Participant and the functions and certain terms which an organisation which is not a Clearing Participant, and which intends to be a Trading Participant, must enter into with a registered Clearing Participant. Such requirements, which promote the objective of an orderly, fair and informed market include terms dealing with:

- the opening, approving and monitoring of accounts;
- procedures with respect to discretionary accounts;
- risk management provisions; and
- provisions dealing with trade confirmation and reporting.

Rule 2.3.2A

5.3 Rule 2.3.2A also promotes an orderly and well functioning market in support of ASX’s regulatory requirements. In accordance with this Rule, when ASX reasonably believes that there is a fact or matter which may impair the ability of a Trading Participants’ open interface device to communicate reliably with SEATS, it may require testing of the Open Interface device and take necessary steps to ensure the proper functioning or orderly operation of SEATS.

5.4 Delineated steps include:

- providing instructions or directions to the Trading Participant; and/or
- suspending trading permission or suspending the connection with SEATS until satisfied that communication problems have been resolved.

5.5 Rule 2.3.2A specifically requires notification of ASX activity and allows for submissions on the part of the Trading Participant with respect to proposed ASX action. The rule also contains a fair hearing and natural

justice clause. Furthermore, Rule 2.3.2A indicates that a Trading Participant, when dissatisfied with a decision of ASX, may appeal the decision to the Appeal Tribunal.

6 Public Benefit and Section 2 of the Business Rules

Statutory Test

- 6.1 An application made under sub-section 88(1) of the Act, is to be granted provided the applicant satisfies the relevant test in sub-section 90(6). In respect of a proposed contract, arrangement or understanding which may have the purpose or effect of substantially lessening competition within the meaning of section 45, authorisation is to be granted where:
- (a) the provisions of the proposed contract, arrangement or understanding would result, or be likely to result in a benefit to the public; and
 - (b) the benefit would outweigh any detriment to the public constituted by any lessening of competition that would result, or would be likely to result, from the contract, arrangement or understanding.

No substantial lessening of competition

- 6.2 The Commission did not identify any detriments to competition flowing from Section 2 of the Business Rules in the 1998 Determination.
- 6.3 The Business Rules are pro-competitive in that in promoting trading efficiency and transparency conditions are created whereby ASX can compete for listings with other exchanges worldwide. The provision of a secure and efficient trading environment also promotes competition for the provision of exchange related services. Furthermore, the creation of a transparent and efficient trading system creates confidence in the ASX exchange which promotes liquidity within Australian capital markets. This, in turn, benefits the competitive position of Australian listed companies to the overall benefit of the Australian economy.

Clear public benefit

- 6.4 Even if the Commission were to identify any lessening of competition flowing from Section 2 of the Business Rules the likely public benefits clearly outweigh any anti-competitive lessening of competition.
- 6.5 In its 1998 Determination the Commission affirmed the public benefits of the Business Rules identified in the 1992 authorisation of SEATS adding that:

“... changes introduced as a result of the open interface will provide the benefits identified in paragraph 7.25 above as well as delivering increased efficiencies particularly through allowing Member Organisations to choose and tailor their trading systems to suit the requirements and features of their businesses (rather than being tied to standard ASX technology) and as a result of Automated Order Processing (encompassing Automated Client Order Processing).”¹⁷

¹⁷ 1998 Determination at paragraph 7.29.

- 6.6 No material changes have been made to Section 2 of the Business Rules since the 1998 Determination. Accordingly, the public benefits flowing from an orderly, fair and informed market as found by the Commission in its 1998 Determination continue to exist and continue to be a basis for authorisation.

7 Requested Authorisation

- 7.1 Section 2 of the Business Rules are currently being reviewed by ASX in response to changes to the *Corporations Act*. This review process is expected to be complete by October 2003 and may result in amendments to the Business Rules. ASX, therefore, wishes to reserve the right to present additional information to the Commission which may be relevant to this authorisation application.
- 7.2 Given the current review of Section 2 of the Business Rules ASX requests, in addition to final authorisation with respect to Section 2 of the Business Rules, that the Commission grant ASX interim authorisation for a six month period based upon the submissions contained herein. The granting of an interim authorisation will ensure that ASX can provide the Commission with complete information as to any relevant amendments to Section 2 of the Business Rules and the manner in which Section 2 of the Business Rules generally applies which may impact upon any final decision as to authorisation.