

2 September 2016

PRODUCTIVITY COMMISSION DRAFT REPORT  
SUPERANNUATION COMPETITIVENESS AND EFFICIENCY  
- RESPONSE SUBMISSION -

The Depository Trust and Clearing Corporation (DTCC) commends the Productivity Commission on its thorough draft report, *How to Assess the Competitiveness and Efficiency of the Superannuation System*. We welcome the opportunity to provide general comments and feedback in addition to our earlier submission, [sub. 15] which outlined our support for operational efficiency as a key consideration.

As an industry-owned global data, technology and infrastructure provider to financial markets, DTCC has a distinct view of post trade best practice as well as economies of scale that can be achieved within and across markets. We suggest the Commission's review include some of the following underlying operational processes and factors that will influence the overall efficiency and effectiveness of Australia's superannuation system now and into the future.

#### *Summary*

In the spirit of completeness reflected in the current draft report we believe the Commission should strive to include in its assessment of 'operational efficiency' investment functions and processes described typically within the industry as 'middle and back office'.

We believe this is a key part of the ecosystem in which inefficient practices can create unnecessary costs and downside risk, at the expense of end investors' returns. Furthermore, while the middle and back office is often defined in terms of processes occurring *within* each institution, we emphasise that many critical processes happen 'between' organisations as part of the investment 'supply chain'. Also, while the superannuation process in Australia is currently very domestically oriented in terms of focus and the end investor segment it services, it will need to be more globally oriented in future.

As part of the Commission's review, we suggest operational functions and processes be assessed as they occur today in the Australian market as well as firms' readiness to evolve and embrace global best practice and operational interconnectivity with overseas markets.

Specifically, we recommend the Productivity Commission include within its 'operational efficiency' focus:

#### *1. Adoption of Shared Global Infrastructure*

The growing scale of Australia's superannuation system combined with advances in technology, cost pressures, increasing regulatory and compliance requirements, greater globally interconnectedness between markets, and evolving needs and expectations of investors requires a step change in how market participants transmit, receive, verify, reconcile, store, apply and protect post-trade data. In some cases these activities are still performed by manual methods, proprietary systems and fragmented platforms (e.g. post trade systems that cannot handle both cross-border and domestic trade processing, and/or equity and fixed income trade processing) in the Australian market.

Globally, particularly in mature markets including the US and Europe, firms are increasingly embracing utility structures and centralised network platforms for critical but generic post trade activities such as institutional trade matching, data management (including for know-your-client, or KYC, and Standing Settlement Instructions, or SSI, management and general reference data). This step-change is seeing

participants move from legacy processes and siloed systems to single source-of-truth management models and centralized processing platforms to reduce risk and cost, including eliminating duplicated processing infrastructure. Increasingly, overseas, institutions are leveraging global operational platforms that enable cross-border trading capability alongside domestic.

**Suggestion:** Review how and to what extent fund management firms and counterparties are utilising shared global infrastructures to optimise process efficiency and risk management. Review the extent to which middle and back office friction, systems fragmentation and manual processing is resulting in cost and risk as well as hampering institutions' ability to offer offshore investment exposure.

## 2. Adoption of Automation and STP

Automating securities processing amongst brokers, custodian banks, outsourcers and asset managers can bring improved scalability and efficiency to the broader market. This is particularly the case where labour costs and manual processes are relatively high. Straight-through processing (STP) lowers operational and counterparty risk and enables higher returns to the end investor.

In 2014, DTCC commissioned research comparing trade-matching practices by country, asset class and segment across Asia Pacific, culminating in a whitepaper titled *'The Asia Pacific Post Trade 100: Post-trade Practices in Asia'* which highlighted Same Day Affirmation (SDA) rates as a quantitative indicator of automation and STP efficiency. SDA refers to the complete verification of essential trade details between the investment manager and the broker/dealer on the same day the transaction is executed (T+0), and a higher rate implies both a greater level of automation as well as more efficient related workflows.

In the Australian market, levels of middle office automation vary between asset classes. For example, middle office processing of fixed income and listed derivatives trading is generally less automated than it is for equities, suggesting unrealised efficiency gains. Other parts of the market, such as back office handling of short-term money market instruments can feature operational complexities and challenges not seen in other markets.

**Suggestion:** Your review should include how and to what extent firms are utilising automation and international best practice to maximise efficiency, allowing greater preservation of member capital.

## 3. Interconnectedness

We acknowledge the commission's view that the superannuation system is more contained and predictable than the banking and finance sectors, however in today's market we recommend that applying an 'interconnectedness lens' of risk management activities can meaningfully enhance systemic resilience, at a firm and industry level.

As an officially designated Systemically Important Financial Market Utility (SIFMU) in the US, DTCC has undertaken considerable work to better understand the role of interconnectedness in the transmission of risk. In October 2015, DTCC published a paper *'Understanding Interconnectedness Risks, To Build A More Resilient Financial System'*, which offered practical guidelines for risk management professionals.

DTCC is happy to make this work, research and insights available to the Commission.

## 4. Innovation

As a global provider of market infrastructure, DTCC has exposure to many market developments that are evolving today and will drive future operational efficiencies in financial services. We reinforce our view that a thorough review of Australia's superannuation system needs to include an assessment of whether Australia's policy and regulatory settings encourage or inhibit take-up of these developments, as well as the local industry's capacity to adopt newer practices and technologies.

Developments that may have significant benefit to the super industry in future:

- the digitisation, standardization and centralization of reference data to support operational, compliance and risk management activities;
- emerging solutions to enable firms to meet increased regulatory requirements (e.g. automated collateral management processes); and
- advances in cybersecurity.

Distributed ledger technology (DLT)/'blockchain' has the potential to further streamline and simplify financial industry infrastructure, particularly if standards are adopted to enable interoperability between platforms is encouraged. In 2016, DTCC wrote a whitepaper '*Embracing Disruption: Tapping the Potential of Distributed Ledgers to Improve the Post-trade Landscape*' which lays out key building blocks for leveraging DLT in financial services which we are also happy to make available to the Commission.

### *Conclusion*

DTCC wholly supports the need for a sound and resilient Australian superannuation system, with underlying structures and processes that enable it to effectively and efficiently fulfil its objective 'to provide income in retirement to substitute or supplement the Age Pension'.

Given effectiveness and efficiency is so greatly determined on the supply side, including underlying market structures, we suggest the Productivity Commission incorporate a thorough review of operational inputs and processes in its assessment.

I welcome the opportunity to discuss any aspect of this submission further and can be contacted on the number provided with this submission.

Sincerely,



Matthew Chan  
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### **About the DTCC**

With over 40 years of experience, the Depository Trust & Clearing Corporation ([www.dtcc.com](http://www.dtcc.com)) provides post-trade market infrastructure for the global financial services industry. Through its subsidiaries, DTCC automates, centralizes, and standardizes the post-trade processing of financial transactions, mitigating risk, increasing transparency and driving efficiency for thousands of broker/dealers, custodian banks and asset managers worldwide. User owned and industry governed, we seek to simplify the complexities of clearing, settlement, asset servicing, data management and information services across asset classes, bringing increased security and soundness to financial markets. DTCC's subsidiary Omgeo Pty Ltd has been active in the Australian market since 2001, supporting the automation of cash equities, fixed income, exchange-traded derivatives, repos and equity swaps post-trade processing. By streamlining post-trade operations such as confirmation, allocation, Standing Settlement Instructions (SSI) enrichment and settlement notification, firms are able to accelerate the clearing and settlement of trades – increasing operational efficiency within Australia's superannuation system and, for the end-investor, serving to increase after-fee returns.