



ASIC
Australian Securities &
Investments Commission

Explanatory Statement

ASIC Corporations (Financial Requirements for Custodial or Depository Service Providers) Instrument 2023/648

This is the Explanatory Statement for *ASIC Corporations (Financial Requirements for Custodial or Depository Service Providers) Instrument 2023/648* (the **Instrument**)

The Explanatory Statement is approved by the Australian Securities and Investments Commission (**ASIC**).

Summary

1. The Instrument imposes specific financial requirements on Australian financial services (**AFS**) licensees that are custodians or depository service providers. The Instrument modifies the *Corporations Act 2001* (the **Corporations Act**) by inserting section 912AC. Section 912AC requires custodians and depository service providers to comply with additional provisions set out in the Instrument as part of satisfying the obligation to have adequate financial resources under paragraph 912A(1)(d) of the Corporations Act.
2. The Instrument preserves the effect of Class Order [CO 13/761] *Financial requirements for custodial or depository service providers* (**[CO 13/761]**), which was issued in 2013. [CO 13/761] was due to expire or ‘sunset’ on 1 October 2023. Following consultation, ASIC considered that [CO 13/761] was operating effectively and efficiently to achieve its objectives, and continued to form a necessary and useful part of the legislative framework.
3. As a result, [CO 13/761] has been remade in a legislative instrument, with only minor drafting changes to reflect ASIC’s current style and format, remove redundant provisions and update definitions, while preserving the current effect of the Instrument. In light of there being no significant changes to the financial requirements detailed in [CO 13/761], this Explanatory Statement should be read in conjunction with the [Explanatory Statement for CO 13/761](#).
4. ASIC makes the Instrument under paragraph 926A(2)(c) of the Corporations Act. That paragraph provides that ASIC may declare provisions to which section 926A applies (i.e. Part 7.6, other than Divisions 4 and 8) in relation to a person or financial product, or a class of persons or financial products, as if specified provisions were omitted, modified or varied as specified in the declaration.
5. Section 912AC contains the following requirements:

-
- (a) tailored cash needs requirements;
 - (b) net tangible assets requirements;
 - (c) cash or cash equivalents requirements;
 - (d) audit opinion requirements in relation to the licensee's financial requirements.

Purpose of the instrument

- 6. The purpose of the Instrument is to continue the financial requirements set out in [CO 13/761] in substantially the same form.
- 7. Following consultation, ASIC formed the view that [CO 13/761] is operating effectively and efficiently and continues to form a necessary and useful part of the legislative framework. Therefore, the legislative instrument was remade using ASIC's current style and format, while preserving the current effect of the instrument.
- 8. The Instrument remade [CO 13/761] subject to the following minor changes:
 - (a) provided an expiry date of 1 October 2028;
 - (b) updated the name of the legislative instrument;
 - (c) reflected current drafting practice and updated the format of the current document;
 - (d) simplified the drafting to give greater clarity;
 - (e) updated legislative references and definitions; and
 - (f) corrected any minor drafting errors.
- 9. The financial requirements in section 912AC reflect the general objectives of the AFS licence requirements in *Regulatory Guide 166 AFS licensing: Financial requirements (RG 166)*. The requirements aim to ensure that:
 - (a) a licensee has sufficient financial resources to conduct its financial services businesses in compliance with the Corporations Act (including carrying out supervisory arrangements);
 - (b) there is a financial buffer that decreases the risk of a disorderly or non-compliant wind-up if the business fails; and
 - (c) there are incentives, through risk of financial loss, for the licensee owners to comply.

Consultation

10. In March 2023, ASIC consulted on the remake of CO 13/760 and LI 2022/449 in Consultation Paper 367: *Remaking ASIC class orders: [CO 13/760], [CO 13/761] and ASIC Instrument 2022/449 (CP 367)*. In CP 367, ASIC proposed the remake of [CO 13/760] and LI 2022/449, without significant changes, and for a period of five years.
11. ASIC received seven submissions in response to CP367. The feedback on CP 367 generally supported our proposals to remake the financial requirements legislative instruments without substantive changes. Report 769 *Response to submissions on CP 367 Remaking ASIC class orders on financial requirements* (Report 769) summarises the key issues raised in the submissions and ASIC's responses. As outlined in Report 769, ASIC has provided additional explanation in this explanatory statement and additional guidance in RG 166 in response to some of the issues raised. The Instrument also corrects the definition of 'excluded assets' and amends the definition of 'revenue'.
12. ASIC has self-certified that it is not required to prepare an Impact Analysis for the Instrument. This is because following a formal consultation process with affected stakeholders, ASIC has assessed that [CO 13/761] is operating effectively and efficiently.

Operation of the instrument

General

13. Section 5 of the Instrument inserts section 912AC of the Corporations Act which, under subsection 912AC(1), applies to AFS licensees that are custodians and depository service providers, other than a licensee that is:
 - (a) a body regulated by the Australian Prudential Regulation Authority (APRA) that is not required to comply with paragraph 912A(1)(d) of the Corporations Act; or
 - (b) a market participant; or
 - (c) a clearing participant.

This is because other requirements apply to these AFS licensees under ASIC or APRA policy.

14. Subsection 912AC(2) specifies that a licensee to which section 912AC applies is taken to have complied with the conditions (if any) of its AFS license that relate to cash needs, net tangible assets and audit opinion requirements.

Tailored cash needs requirements

15. Subsection 912AC(3) requires a licensee to prepare a cash flow projection covering at least the next 12 months based on what is reasonably likely to happen over this period. The cash flow projection must be approved by directors

of the licensee at least once a quarter as satisfying the cash needs requirement. The licensee must document the calculations and assumptions used in preparing the projection and describe why those assumptions are appropriate. The cash flow projection must be updated in certain circumstances.

Net Tangible Asset requirement

16. The NTA requirement applies to all licensees that hold a licence authorisation to provide custodial or depository services, whether or not the licensee actually provides custody or depository service, is an incidental provider only or provides no custodial or depository services at all.
17. Subsection 912AC(4) requires licensees that provide custodial and depository services to hold net tangible assets (NTA) requirements as follows:
 - (a) for a licensee that is not an incidental provider, at least the greater of \$10 million or 10% of the licensee's average revenue; and
 - (b) for a licensee that is an incidental provider, at least the greater of \$150,000 or 10% of average revenue.
18. A licensee which is an incidental provider (first licensee) does not have to meet the NTA requirements in subsection 912AC(4) if subsection 912AC(5) applies. Subsection 912AC(5) applies to the first licensee if all the financial products to which the custodial or depository services relate, are held by another licensee (second licensee). The second licensee must be authorised to provide a custodial or depository service, must not be an incidental provider and must comply with the NTA requirements.
19. Subsection 912AC(5) may also apply to a licensee that provides no financial services at all. In order to rely on s912AC(5), the licensee must appoint a second licensee under paragraph s912AC(5)(a).

Revenue

20. The NTA requirement requires a calculation of the licensee's average revenue. *Revenue* is defined in s912AC(12) to include the licensee's revenue (within the meaning given by the accounting standards) and, to the extent it is not the licensee's revenue, any amount paid or payable for the performance of the obligations imposed on the licensee to provide custodial or depository services, even if those obligations are performed by another entity.
21. The calculation of a licensee's *revenue*, therefore, includes any payments made for the performance of custodial or depository services, as well as any other payments made to an agent or authorised representative of the licensee that provides custodial or depository services on the licensee's behalf.

Liquidity requirement

22. Subsection 912AC(7) requires licensees that have to meet NTA requirements under subsection 912AC(4) to hold at least 50% of its required NTA in cash or cash equivalents and 100% of its required NTA in liquid assets.

Audit opinion

23. Subsection 912AC(10) sets out the requirements for the content of an opinion of a registered company auditor (**audit opinion**) covering the period during which the licensee was authorised to provide custodial or depository services. The auditor is required to provide an audit opinion on the matters specified in subparagraphs 912AC(10)(a) and 912AC(10)(b).

Excluded assets

24. The Instrument expressly includes ‘deferred tax assets’ in the definition of ‘excluded assets’ in order to bring the requirements in line with the financial requirements for issuers of retail OTC derivatives under [*ASIC Corporations \(Financial Requirements for Issuers of Retail OTC Derivatives\) 2022/705*](#). The effect is that ‘deferred tax assets’, like other intangible assets, are excluded assets for the purposes of calculating the licensee’s ‘adjusted assets’ when calculating a licensee’s NTA.
25. This instrument also makes a correction in paragraph (c) of the definition of ‘excluded assets’ so that all categories of assets in paragraph (c) will be excluded where the licensee may exercise any form of power or control over them.

Legislative instrument and primary legislation

26. The subject matter and policy implemented by the Instrument are more appropriate for a legislative instrument rather than primary legislation because:
- (a) the modifications made by the Instrument are highly specific amendments designed to ensure the application of primary legislation is consistent with the intended policy and the enabling provisions in the primary legislation;
 - (b) the Instrument preserves the effect of [CO 13/761] which was due to sunset on 1 October 2023; and
 - (c) following consultation, ASIC considered that [CO 13/761] was operating effectively and efficiently to achieve its objectives and continued to form necessary and useful parts of the legislative framework; and

Duration of the instrument

27. ASIC considers that five years is the appropriate duration for the Instrument.

Legislative authority

28. The source of power to make the instrument is paragraph 926A(2)(c) of the Corporations Act.
29. The instrument is a disallowable legislative instrument.

Statement of Compatibility with Human Rights

30. The Explanatory Statement for a disallowable legislative instrument must contain a Statement of Compatibility with Human Rights under subsection 9(1) of the *Human Rights (Parliamentary Scrutiny) Act 2011*. A Statement of Compatibility with Human Rights is in the Attachment.

Statement of Compatibility with Human Rights

This Statement of Compatibility with Human Rights is prepared in accordance with Part 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

ASIC Corporations (Financial Requirements for Custodial or Depository Service Providers) Instrument 2023/648

Overview

1. The Instrument imposes financial requirements on Australian financial services licensees that provide custodial or depository services. The Instrument continues the financial requirements under its predecessor instrument, ASIC Class Order [CO 13/761] *Financial requirements for custodial and depository service providers (CO 13/761)* with minor and technical changes only.

Assessment of human rights implications

2. This instrument does not engage any of the applicable rights or freedoms.

Conclusion

3. This instrument is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.