



**ASIC**

Australian Securities & Investments Commission

**REPORT 189**

# **Market assessment report: Yieldbroker Pty Limited**

**ACN 092 250 345**

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## **About this report**

This report summarises ASIC's sixth annual assessment of Yieldbroker Pty Limited (Yieldbroker) under s794C of the *Corporations Act 2001* (Corporations Act).

This assessment covers the period 1 July 2008 to 30 September 2009 (assessment period).

### About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents.

**Consultation papers:** seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance.

**Regulatory guides:** give guidance to regulated entities by:

- explaining when and how ASIC will exercise specific powers under legislation (primarily the Corporations Act)
- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
- giving practical guidance (e.g. describing the steps of a process such as applying for a licence or giving practical examples of how regulated entities may decide to meet their obligations).

**Information sheets:** provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

**Reports:** describe ASIC compliance or relief activity or the results of a research project.

### Previous reports on Yieldbroker

Yieldbroker was granted an Australian market licence on 3 February 2004.

Report number	Date released
REP 45	June 2005
REP 60	October 2005
REP 87	November 2006
REP 114	February 2008
REP 163	July 2009

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## Key findings and recommendations

### Key findings

- 1 ASIC is satisfied that Yieldbroker has:
  - adequate arrangements for the supervision of its markets in accordance with its obligations under s792A(c) of the Corporations Act; and
  - sufficient resources to operate its markets properly and for the required supervisory arrangements to be provided under s792A(d) of the Corporations Act.

### Recommendations

- 2 We do not have any recommendations to make in relation to Yieldbroker's current supervisory arrangements.

## A The assessment

### Key points

ASIC conducts annual assessments of market licensees, such as Yieldbroker, because it is required to do so under s794C of the Corporations Act.

The scope of our assessment must include the obligations found in s792A(c), but we can include other Ch 7 obligations too.

We use the licensee's self-assessment reports, information from our previous assessments, our observation of the licensee's performance, market intelligence and other things to form a view of how well the licensee has operated its market.

### Purpose and scope

- 3 Under s792A(c), a market licensee is required to have adequate arrangements for supervising the market, including for:
- handling conflicts between the commercial interests of the licensee and the need for the licensee to ensure that the market is fair, orderly and transparent;
  - monitoring the conduct of participants on or in relation to the market; and
  - enforcing compliance with the market's operating rules.
- 4 We are required to assess how well a market licensee complies with its obligations in s792A(c) at least once a year: s794C(2).
- 5 In addition, we are permitted to extend the scope of our assessment to review how well a licensee complies with any or all of its obligations under Ch 7: s794C(1). In this instance, we extended the scope of the assessment to include a review of whether Yieldbroker has sufficient financial, technological and human resources to comply with its obligations under s792A(d).

### Background

- 6 Yieldbroker was granted an Australian market licence (market licence) on 3 February 2004. A copy of Yieldbroker's market licence is available on ASIC's website at [www.asic.gov.au/markets](http://www.asic.gov.au/markets).

- 7 Yieldbroker’s market licence permits it to operate two markets—the Dealer-to-Client market and Interdealer market. Both markets are electronic platforms which facilitate trading in bonds and debentures. Current products traded on the markets include Australian government and semi-government bonds, CPI-linked bonds, treasury notes, corporate bonds, Floating Rate Notes and New Zealand government bonds. In May 2009, Yieldbroker made changes to its operating rules, including changes to clarify that the Yieldbroker platform can facilitate primary market issuance.
- 8 In the over-the-counter financial markets, the total turnover of Australian government debt securities and non-government debt securities for the 2008–2009 period was \$792 billion and \$494 billion, respectively.<sup>1</sup>
- 9 The Dealer-to-Client market allows participants known as clients to request quotes from participants known as dealers. The Interdealer market allows dealer participants to trade directly with each other on a principal-to-principal basis.
- 10 The participants in Yieldbroker’s markets either hold an Australian financial services (AFS) licence or are professional investors. Yieldbroker has applied for a variation to its market licence which, if granted, will remove the AFS licence requirement if an AFS licence is not required by law or if participants hold a relevant exemption.
- 11 There are 12 dealers participating in Yieldbroker’s Dealer-to-Client market. Of these, 11 are shareholders of Yieldbroker.

## Our methodology

### Our assessment process

- 12 A market licensee’s obligations are ongoing. Whether it is likely to comply with its obligations in the future cannot be judged merely by reference to its past compliance.
- 13 We therefore use the assessment process to:
- reach conclusions about the adequacy of the arrangements a market licensee has in place for supervising its market in accordance with its obligations under the Corporations Act at the time of the assessment; and
  - identify issues that in our view need, or may need, to be addressed to ensure ongoing compliance.

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<sup>1</sup> Australian Financial Markets Association, *2009 Australian Financial Markets Report*, p. 2.

## What we focused on for this assessment

- 14 Our focus in this assessment was to review:
- any changes in Yieldbroker's operations from the previous year's assessment;
  - Yieldbroker's supervisory procedures including, in particular, its arrangements for managing conflicts of interest; and
  - whether Yieldbroker has adequate resources.

## What we considered

- 15 In conducting our assessment we reviewed:
- information we received from and about Yieldbroker in the ordinary course of our dealings with Yieldbroker, including Yieldbroker's annual regulatory report required under s792F;
  - Yieldbroker's unaudited financial statement for the year ended 30 June 2009;
  - documents produced by Yieldbroker in response to our notice under s30 of the *Australian Securities and Investments Commission Act 2001* to obtain information about how Yieldbroker is meeting certain obligations under the Corporations Act;
  - information we received during our visit to Yieldbroker's office on 13 November 2009, where we spoke to Yieldbroker's Compliance Officer;
  - Yieldbroker's policies and procedures for the conduct of Yieldbroker in general and its supervisory responsibilities in particular.

## Consultation

- 16 Our findings are set out in Section B. Yieldbroker has had the opportunity to view and comment on the factual accuracy of a draft version of this report. Where appropriate, our findings in Section B reflect Yieldbroker's clarifications.

## B Our observations for Yieldbroker

### Key points

We consider that Yieldbroker's arrangements for supervising its markets are adequate, including arrangements for:

- handling conflicts between its commercial interests and the need to ensure that the markets are fair, orderly and transparent;
- monitoring the conduct of participants on or in relation to the markets; and
- enforcing compliance with the markets' operating rules.

Yieldbroker did not make any substantial changes to its supervisory arrangements during the assessment period.

We do not have any recommendations to make in relation to Yieldbroker's current supervisory arrangements.

We also note that Yieldbroker has complied with its reporting obligations under the Corporations Act.

### Supervisory arrangements

- 17 We conclude that Yieldbroker has:
- adequate arrangements for the supervision of its markets in accordance with its obligations under s792A(c); and
  - sufficient resources to operate its markets properly and for the required supervisory arrangements to be provided under s792A(d).
- 18 This conclusion is based on the following observations:
- Yieldbroker's supervisory arrangements did not change during the assessment period. These arrangements include:
    - a Compliance Officer who is responsible for supervising the markets and participants, and has supervisory and disciplinary powers;
    - a Compliance Committee which oversees supervision and has the power to conduct disciplinary hearings; and
    - the disciplinary powers of the Board of Directors.
  - participation in the markets is restricted to professional investor participants who can only trade on their own behalf or on behalf of wholesale clients;



- no serious market failures or disruptions have occurred during the assessment period; and
- no information has come to our attention to suggest that the supervisory arrangements in place have not been operating properly.

### **Managing conflicts of interest**

- 19 Yieldbroker's arrangements for managing conflicts of interest between its supervisory and commercial interests have not changed since the previous assessment. In brief:
- the Compliance Officer is not involved in commercial decision-making and reports directly to the Board of Directors; and
  - there is a Compliance Committee with the following function and characteristics:
    - the committee deals with referrals from the Compliance Officer;
    - the committee must have a majority of members who are neither directors of Yieldbroker nor of its participants;
    - decisions of the committee are determined by a majority vote; and
    - committee members must avoid acting in connection with any matter that places them in a position of conflict between their duties as a member of the committee and any other duty or interest.
- 20 Yieldbroker maintains a conflicts of interest register to record all conflicts of interest issues and actions taken. There were no conflicts of interest identified during the assessment period.

### **Monitoring the market and conduct of participants**

- 21 Yieldbroker has developed its own monitoring software (Tibtomcat), which monitors all system activity in real time and provides static reporting. Tibtomcat is the primary tool used by the Compliance Officer to monitor the markets.
- 22 On a weekly basis the Compliance Officer reviews all price and trading information obtained via the system's reporting function. These reviews are aimed at identifying patterns of behaviour that may evidence breaches, or possible breaches, of the operating rules and/or the Corporations Act (such as market manipulation, insider trading, misleading or deceptive conduct and fraud). Due to the limited number of trades on the markets, the Compliance Officer is able to review orders and transactions in the context of the relevant products, transaction type and market conditions.
- 23 Tibtomcat also provides real-time monitoring of system stability and identification of sources of system problems. Alarm notices are generated

when the system detects conduct by participants on the market that triggers or exceeds certain parameters set by the system. Depending on the nature of the alerts, they are reviewed by either the Compliance Officer and/or the Helpdesk. For instance, the Compliance Officer may investigate situations where clients do not trade at the best prices, whereas the Helpdesk reviews or investigates alerts triggered as a result of system issues such as outages and problems with participant access.

- 24 In addition to the monitoring process identified above, participants are required to confirm their ongoing compliance with the operating rules via an annual requirement to notify Yieldbroker of any breaches. No such notifications were received during the assessment period.
- 25 The Compliance Officer reports to the Board monthly about the results of the weekly review, the investigation and assessment of any issues and/or disputes, and the steps taken to resolve those issues and/or disputes. The monthly reports to the Board indicate that during the assessment period:
- there were no identified breaches of the operating rules or market conduct that may have contravened the operating rules or Corporations Act; and
  - there were no investigations or disputes.
- 26 The bulk of trading activity takes place on the Dealer-to-Client market, which is conducted via the Request for Quote function. The nature of this one-way market in itself limits the potential for unlawful trading activity.
- 27 In addition to reviewing system alarm notices, Yieldbroker's Helpdesk is responsible for processing and auditing participant access, user credentials and trading authorities, and preparing routine reports reviewed by the Compliance Officer.

### **Enforcing compliance with the operating rules**

- 28 Yieldbroker did not make any substantial changes, during the assessment period, to the way in which it enforces compliance with its operating rules.
- 29 Participants in the markets undertake to comply with the Participation Deed, operating rules, the Corporations Act, Australian Financial Markets Association (AFMA) and other market conventions, and any directions issued by ASIC to Yieldbroker. Participants also undertake to access and use the system in a manner that is honest, fair and efficient so as to promote the ongoing protection of the market.
- 30 Where a participant has breached an operating rule, the Compliance Officer is required to issue a warning to the responsible participant. The Compliance Officer may make a recommendation to the Compliance Committee, which may recommend that the Board take disciplinary action. The Board has the

power to make a final determination (which may or may not be in accordance with the Compliance Committee's recommendations) by issuing a warning or fine, suspending or terminating a participant's right to access the system, removing the participant's current pricing references from the system and/or directing the Compliance Officer to notify ASIC.

31 The Compliance Committee only convenes when the Compliance Officer makes a referral to it for disciplinary action to be taken. As the Compliance Officer made no referrals, the committee did not convene during the assessment period.

32 As stated at paragraph 25 above, during the assessment period there were no identified breaches of the operating rules or market conduct that may have contravened the operating rules or Corporations Act, and there were no investigations or disputes.

## Resources

33 We are satisfied that Yieldbroker has sufficient financial, technological and human resources for the required supervisory arrangements to be provided.

### Financial

34 We have reviewed Yieldbroker's financial position and are satisfied that it has access to sufficient financial resources to operate its market and to provide adequate supervisory arrangements.

35 Yieldbroker's financial resources are derived from:

- participation fees on dealers in the Dealer-to-Client market;
- trade fees levied in the Interdealer market; and
- income from the distribution of indicative price data.

36 During the assessment period five additional shareholders purchased shares in Yieldbroker. Yieldbroker is currently owned in equal shares by eleven large financial institutions.

### Technological

37 Yieldbroker's technological resources have dealt adequately with existing volumes on the markets and no serious market disruptions have occurred.

38 These resources comprise various leased and owned hardware assets, software applications and processes for trading and system auditing, monitoring and reporting. These processes include the periodical review of system security to identify and resolve any significant risks, and to ensure

that activity on the system is always secured in line with industry expectations.

### **Human**

- 39 During the assessment period, Yieldbroker relied on its General Manager, Compliance Officer and Helpdesk staff to perform the required supervisory functions for the markets. In our view, this resourcing is sufficient.

## **Conclusion**

- 40 Based on our assessment, we do not have any recommendations to make in relation to Yieldbroker's current supervisory arrangements.

## Key terms

Term	Meaning in this document
AFMA	Australian Financial Markets Association
AFS licence	An Australian financial services licence under s913B that authorises a person who carries out a financial services business to provide financial services
ASIC	Australian Securities and Investments Commission
Ch 7 (for example)	A chapter in the Corporations Act (in this example numbered 7)
Corporations Act	<i>Corporations Act 2001</i> (Cth)
Australian market licence	Australian market licence under s791A
market licensee	Holder of an Australian market licence
Yieldbroker	Yieldbroker Pty Limited
s794C (for example)	A section of the Corporations Act (in this example, numbered 794C), unless otherwise specified