



**ASIC**

Australian Securities & Investments Commission

CONSULTATION PAPER 152

# **ASIC's conversion of ASX and SFE guidance: General operational obligations**

March 2011

## **About this paper**

This consultation paper seeks feedback on ASIC's proposed minor modifications, and limited additions, to pre-existing ASX and SFE guidance that we are converting into ASIC regulatory guides, where this guidance continues to be relevant to the ASIC Market Integrity Rules (ASX Market) 2010 and the ASIC Market Integrity Rules (ASX 24 Market) 2010.

This paper focuses on the general operational obligations of ASX and ASX 24 (formerly SFE) market participants. It does not propose changes to the existing obligations under the market integrity rules.

### 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 and ASIC market integrity rules
- 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.

### Document history

This paper was issued on 28 March 2011 and is based on the Corporations Act as at 28 March 2011.

### Disclaimer

The proposals, explanations and examples in this paper do not constitute legal advice. They are also at a preliminary stage only. Our conclusions and views may change as a result of the comments we receive or as other circumstances change.

# Contents

<b>The consultation process</b> .....	<b>4</b>
<b>A Background to the proposals</b> .....	<b>6</b>
Transfer of market supervision to ASIC.....	6
Context of this paper in relation to future reviews of market integrity rules .....	7
Conversion of pre-existing ASX and SFE guidance into ASIC regulatory guides .....	8
Our approach in converting relevant guidance.....	11
Relationship to proposed Chi-X market.....	12
<b>B ASX market participants: General operational obligations</b> .....	<b>13</b>
Management requirements: Structures, policies and procedures .....	13
Management requirements: Good fame and character and notification.....	14
Responsible executive requirements.....	15
PI insurance requirements .....	16
Trading records requirements.....	17
<b>C ASX 24 market participants: Operational obligations in relation to clients</b> .....	<b>20</b>
Clients' segregated account obligations .....	20
<b>D Regulatory and financial impact</b> .....	<b>25</b>
<b>Appendix: Tracking the status of relevant ASX and SFE guidance</b> .....	<b>26</b>
<b>Key terms</b> .....	<b>29</b>

## The consultation process

You are invited to comment on the proposals in this paper, which are only an indication of the approach we may take and are not our final policy.

We are keen to fully understand and assess the financial and other impacts of this guidance. In providing your feedback, we ask you to comment on:

- the likely compliance costs;
- the likely effect on competition; and
- other impacts, costs and benefits.

Where possible, we are seeking both quantitative and qualitative information.

We are also keen to hear from you on any other issues you consider important.

Your comments will help us develop our guidance on the market integrity rules for participants of the ASX and ASX 24 markets. In particular, any information about compliance costs, impacts on competition and other impacts, costs and benefits will be taken into account if we prepare a Regulation Impact Statement: see [Section D Regulatory and financial impact](#), p. 25.

### Making a submission

We will not treat your submission as confidential unless you specifically request that we treat the whole or part of it (such as any financial information) as confidential.

Comments should be sent by 13 May 2011 to:

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## What will happen next?

<b>Step 1</b>	28 March	ASIC consultation paper released
<b>Step 2</b>	13 May	Comments due on the consultation paper
	May/June	Drafting of regulatory guides
	July	Further informal consultation on draft regulatory guides as needed
<b>Step 3</b>	August	Regulatory guides released

Note: This schedule only sets out the steps for the Stage 1 conversion of ASX guidance notes and SFE procedures. Other stages may occur concurrently.

## A Background to the proposals

### Key points

This consultation paper begins our first stage of converting pre-existing ASX and SFE guidance into ASIC regulatory guides, where this guidance continues to be relevant in helping ASX and ASX 24 (formerly SFE) market participants to comply with the market integrity rules.

We are not changing the substance of the pre-existing guidance. We will, however, make changes to reflect ASIC style and language, as well as the current regulatory environment and terminology. We have also taken the opportunity to propose some additional clarification, or minor modifications, where we consider this will be useful to market participants.

Table 1 summarises the proposals contained in this paper, while Table 2 and Table 3 in the appendix show the current status of relevant pre-existing ASX and SFE guidance.

We do not propose to modify the market integrity rules. Any proposed future changes or additions to these rules will be the subject of separate consultation. Further, this paper does not relate to the market integrity rules proposed in Consultation Paper 145 *Australian equity market structure: Proposals* (CP 145) or in Consultation Paper 148 *Proposed market integrity rules: Chi-X market* (CP 148).

### Transfer of market supervision to ASIC

- 1 On 24 August 2009, the Australian Government announced its decision to transfer the responsibility for supervising Australia's domestic licensed financial markets from market operators to the Australian Securities and Investments Commission (ASIC). Subsequently, the *Corporations Amendment (Financial Market Supervision) Act 2010* (Financial Market Supervision Act) was enacted in March 2010 to provide that responsibility for supervising trading on Australian domestic licensed financial markets be transferred from the operators of those markets to ASIC.

Note: This is in addition to ASIC's existing supervision of Australian financial services (AFS) licensees under the *Corporations Act 2001* (Corporations Act).

- 2 The Financial Market Supervision Act, which commenced on 1 August 2010, inserts a new Pt 7.2A into the Corporations Act. From this date, ASIC assumed responsibility for supervising the trading activities and conduct of business by market participants in relation to domestic licensed markets (i.e. those operated by persons licensed under s795B(1) of the Corporations Act).
- 3 Australian market licensees continue to be responsible for the operation of their markets, for monitoring and enforcing compliance with their market's

operating rules, which include their listing rules, and for providing guidance as appropriate.

- 4 This consultation paper deals only with the Australian Securities Exchange (ASX) and ASX 24 (formerly Sydney Futures Exchange (SFE)) markets.

Note: ASX Limited is the market licensee that operates ASX. Australian Securities Exchange Limited (known as Sydney Futures Exchange Limited before 1 August 2010) is the market licensee that operates ASX 24 (known as SFE before 1 August 2010).

- 5 We have made ASIC Market Integrity Rules (ASX Market) 2010 and ASIC Market Integrity Rules (ASX 24 Market) 2010, under Pt 7.2A, which deal with the activities and conduct of participants of the ASX and ASX 24 markets.

Note: Throughout this paper we will use the shortened forms 'ASIC Market Integrity Rules (ASX)' to refer to the ASIC Market Integrity Rules (ASX Market) 2010 and 'ASIC Market Integrity Rules (ASX 24)' to refer to the ASIC Market Integrity Rules (ASX 24 Market) 2010.

- 6 Our approach in making market integrity rules has been to retain the substance of most of the pre-existing obligations that apply to these market participants.

- 7 We are responsible for supervising compliance with these rules and for making and revising them as needed.

## Context of this paper in relation to future reviews of market integrity rules

- 8 The proposals contained in this consultation paper are limited to guidance on a select range of topics. The proposals do not suggest changes to the market integrity rules, nor do they propose new market integrity rules. As noted in Regulatory Guide 214 *Guidance on ASIC market integrity rules for ASX and ASX 24 markets* (RG 214), we intend to review existing market integrity rules to make any adjustments required as a result of our experience in administering the rules, the developments in the market, and the international regulatory environment. This review will be a separate exercise, likely to commence in 2012. As part of this separate exercise, we will consider overlaps between existing market integrity rules and the Corporations Act. These include, but are not limited to:

- (a) the management and supervision requirements for market participants (i.e. through responsible executives) and AFS licensees (i.e. through responsible managers);
- (b) trust account requirements; and
- (c) professional indemnity (PI) insurance requirements.

- 9 We will consult on any proposed amendments or additions to the market integrity rules at the time of this review.
- 10 Recently, in CP 145, we consulted on proposals to enhance the regulation of the Australian market, including the introduction of competition between exchange markets. CP 145 proposed market integrity rules to address some of the regulatory issues resulting from market structure developments, including the introduction of competing exchange markets.
- 11 In CP 148, we consulted on proposed market integrity rules to apply in relation to the Chi-X Australia Pty Ltd (Chi-X) market, subject to final approval of Chi-X's Australian market licence application.
- 12 This current consultation paper does not propose guidance that covers the subject matters considered by CP 145 or CP 148.
- 13 Where we develop guidance to inform new market integrity rules, we will endeavour to develop a consistent approach that applies across markets on similar subject areas, while also reducing the need for duplication of notification obligations for participants operating across markets.

## **Conversion of pre-existing ASX and SFE guidance into ASIC regulatory guides**

- 14 In RG 214, we provide guidance on a range of topics, which we note will be expanded on with the benefit of experience. RG 214 explains our expectations of market participants regarding their compliance with a number of requirements in the market integrity rules.
- 15 In RG 214, at RG 214.57–RG 214.58, we note that, in assessing a market participant's compliance with the market integrity rules, we will seek to follow the relevant published interpretation contained in pre-existing ASX guidance notes and SFE procedures, determinations and practice notes (SFE procedures). In some instances, we have already incorporated content from this guidance into the market integrity rules.
- 16 We also note in RG 214 that we will review this guidance over time and publish ASIC regulatory guides following consultation on these issues.
- 17 This consultation paper begins our process of converting the substance of pre-existing ASX and SFE guidance, as appropriate, into ASIC regulatory guides. The 20 ASX guidance notes and 23 SFE procedures involved in this process are listed in Table 2 and Table 3 of the appendix. We will build on the guidance already provided in RG 214 and have proposed some additional clarification where there has been an operational need to do so.



- 18 Given the number of ASX guidance notes and SFE procedures involved (43 in total), we will consult over a number of stages, starting with this consultation paper on some of the general obligations of ASX and ASX 24 market participants. These include:
- (a) the management requirements of market participants, including the appointment of responsible executives;
  - (b) the ongoing responsibilities of responsible executives;
  - (c) PI insurance requirements;
  - (d) trading records requirements; and
  - (e) clients' segregated account obligations for ASX 24 market participants.

Note 1: We consider the guidance contained in five ASX guidance notes and one SFE procedure in this consultation paper. These guidance notes can be sourced from the ASX Group's website, or directly at [www.asxgroup.com.au/asx-operating-rules-guidance-notes-and-waivers.htm](http://www.asxgroup.com.au/asx-operating-rules-guidance-notes-and-waivers.htm). SFE guidance contained in the procedures, determinations and practice notes may be sourced from the ASX Group's website, or directly at [www.asxgroup.com.au/old-sfe-operating-rules.htm](http://www.asxgroup.com.au/old-sfe-operating-rules.htm).

Note 2: The ASX Group continues to maintain ASX guidance notes and ASX 24 procedures that are relevant to their operating rules—these are separate to those referred to in Table 2 and Table 3.

- 19 Table 1 summarises the key proposals of this consultation paper. We will publish further omnibus or individual consultation papers on our proposed guidance for ASX and ASX 24 market participants about their obligations in relation to clients, trading and automated order processing (AOP).

**Table 1: Summary of proposals**

ASX/SFE guidance considered		Overview of proposed action	Cross-references
ASX guidance notes (GNs)			
GN 6	Management requirements	We propose to update this guidance to reflect the current regulatory environment and the developments in business models since 2005.  We do not propose to otherwise change the substance of this guidance.	See B1
GN 7	Management requirement— Good fame and character— Reliance on APRA requirements	We propose <i>not</i> to retain: <ul style="list-style-type: none"> <li>• the 'good fame and character' definition; nor</li> <li>• the guidance on the notification of responsible executive appointments.</li> </ul>	See B2

ASX/SFE guidance considered		Overview of proposed action	Cross-references
GN 27	Ongoing compliance and supervision—Responsibilities of responsible executives	<p>We propose <i>not</i> to retain the guidance on the notification of responsible executive appointments using the notification form.</p> <p>We do not propose to otherwise change the substance of this guidance.</p>	See B2(b)
GN 8	Insurance requirements	<p>We propose to no longer request a director to submit an attestation of how they have formed the opinion that alternative insurance arrangements are reasonable and that a related body corporate can pay an insurance claim.</p> <p>We do not propose to otherwise change the substance of this guidance.</p>	See B3
GN 33	Trading records	<p>We propose to:</p> <ul style="list-style-type: none"> <li>acknowledge the different requirements for AFS licensee market participants under reg 7.8.19(5) and under Rule 4.1.4 of the ASIC Market Integrity Rules (ASX) in relation to the duration of time trading records are to be retained, and provide additional guidance that participants retain records for the longer period of seven years prescribed in the market integrity rules;</li> </ul> <p>Note: Throughout this paper we will use the shortened form 'Rule 4.1.4 (ASX)' (for example) to refer to a particular rule of the ASIC Market Integrity Rules (ASX).</p> <ul style="list-style-type: none"> <li>request market participants to submit electronic trading information requested by ASIC in a standardised .csv or Excel format, and to include the information listed at B5(b).</li> </ul> <p>We do not propose to otherwise change the substance of this guidance.</p>	See B4–B5
SFE procedures, determinations and practice notes (PDPs)			
PDP 2.2.26	Clients' segregated account obligations	<p>We propose <i>not</i> to retain aspects of the guidance that have already been incorporated into the market integrity rules.</p> <p>We also propose to:</p> <ul style="list-style-type: none"> <li>request that ASX 24 market participants maintain additional supporting documentation to supplement their accounting records;</li> <li>provide additional guidance that participants should maximise the term 'clients' segregated account' in an account name to ensure that a person would reasonably identify the account as a clients' segregated account;</li> <li>request that participants perform daily reconciliations of the clients' segregated account as a matter of good practice; and</li> <li>continue to encourage participants to educate their clients on the inherent risks associated with co-mingling client money within the clients' segregated account, although we do not propose to retain SFE Notice 50/06.</li> </ul> <p>We do not propose to otherwise change the substance of this guidance.</p>	<p>See C1</p> <p>See C2–C5</p>

Note: In converting ASX and SFE guidance we expect to also make the changes referred to in paragraph 25.

- 20 We will amend our ASX and ASX 24 guidance to incorporate these proposals in light of the feedback we receive. We will informally consult with industry in preparing the final form of ASIC regulatory guidance to reflect the substance of pre-existing guidance and the proposals in this consultation paper.
- 21 Table 2 and Table 3 in the appendix show the current status of all relevant ASX guidance notes and SFE procedures as at the date of issue of this consultation paper. These tables will be continuously updated in future publications as we continue our conversion of pre-existing guidance into ASIC regulatory guides for ASX and ASX 24 market participants.

## Our approach in converting relevant guidance

- 22 We will convert into ASIC regulatory guides the substance of pre-existing ASX and SFE guidance that continues to be relevant in interpreting ASIC market integrity rules for these markets. We consider that this process will assist ASX and ASX 24 market participants by providing up-to-date guidance on a select number of topics. We will adapt our final guidance in response to the industry feedback we receive on our limited proposals to modify or clarify pre-existing guidance, such as those contained in this consultation paper.
- 23 Given the number of guidance documents involved, we will complete this conversion in a number of stages. In this first stage, we will convert into ASIC guidance the substance of five ASX guidance notes and one SFE procedure that continues to be relevant in interpreting the market integrity rules (i.e. where the rules have come over in a similar form and are compatible with the Corporations Act and ASIC's regulatory remit).
- 24 We will consult separately on some guidance documents, while others may be grouped together by subject matter where possible. For ease of reference, these thematic groupings will be retained, wherever possible, in our final regulatory guides. For example, the consolidated guidance on general operational obligations and the consolidated guidance on trading obligations will be published in separate regulatory guides.
- 25 In the conversion process, we expect to make changes to:
- (a) reflect ASIC style and language;
  - (b) incorporate updates in current law and practice;
  - (c) remove guidance already adopted into the relevant market integrity rules; and
  - (d) update superseded regulatory references, such as 'ASX Market Rules and Procedures'.

- 26 Some further minor modifications may also be required to:
- (a) ensure that the guidance fits in with our regulatory remit (where there are inconsistencies);
  - (b) update guidance that is out of date;
  - (c) meet operational needs;
  - (d) fill any gaps identified;
  - (e) delete areas that are no longer relevant; and
  - (f) provide additional clarification as appropriate.
- 27 As noted in RG 214, we recognise that there are a small number of market integrity rules that deal with the same or similar subject areas as the Corporations Act. Where we have identified divergent approaches taken in the market integrity rules, the Corporations Act and pre-existing ASIC, ASX and ASX 24 guidance, we have noted any overlap and propose additional guidance where appropriate.
- 28 As noted above, in due course we intend to review the market integrity rules to further minimise duplication with the Corporations Act. It is important to recognise that the proposals described in this consultation paper are separate to any future reviews of, or additions to, the market integrity rules.

## Relationship to proposed Chi-X market

- 29 As noted above, we have recently consulted on specific market integrity rules for the Chi-X market: see CP 148. These proposed rules build on relevant ASX Market Rules. When settling the conversion of existing ASX and SFE guidance, we will also have regard to the application of the proposed ASIC regulatory guides to markets other than ASX and ASX 24—for example, the proposed Chi-X market.

## B ASX market participants: General operational obligations

### Key points

We propose to retain the substance of ASX guidance on management requirements, with the following changes to:

- update the guidance to reflect recent developments in market participants' business models;
- no longer refer to APRA's criteria for meeting the 'good fame and character' requirement (because Rule 2.1.4 (ASX) now sets out the criteria to be applied); and
- no longer retain the guidance on the notification requirements for responsible executive appointments (because these are now imposed by Rule 2.3.1 (ASX)).

We also propose to:

- no longer request a director to submit an attestation about their alternative insurance arrangements where PI insurance is provided by a related body corporate;
- clarify the duration of time that trading records are to be retained; and
- include guidance on the preferred format for the delivery of trading records to ASIC (see Chapter 4 (Records) of the ASIC Market Integrity Rules (ASX)).

## Management requirements: Structures, policies and procedures

### ASX guidance

- 30 ASX Market Rules Guidance Note 6 *Management requirements* (GN 6) outlines the minimum requirements for an appropriate management structure and effective supervisory procedures. In particular, GN 6 addresses the need for market participants to have documented supervisory procedures and sufficient resources both in terms of systems and personnel. Responsible executives and directors are the key personnel held accountable for ensuring that a market participant remains compliant with its regulatory obligations.
- 31 Other than our proposal at B1, we do not propose to change the substance of this guidance.

## Proposal

**B1** We propose to update the guidance in GN 6 to reflect the current regulatory environment and the developments in business models since the guidance was first published in 2005. These changes will relate to specialised procedures that cover complex products, outsourcing, automated systems and the review of supervisory systems.

### Your feedback

**B1Q1** Should we include any further guidance on other management requirements, in addition to the proposals contained in this consultation paper? If so, please give details of the areas requiring our guidance, and your suggestions about the information needed.

**B1Q2** Should we define what a 'management structure' is for a market participant—for example, by referring to supervisory procedures for compliance with the law and market integrity rules?

## Management requirements: Good fame and character and notification

### ASX guidance

- 32 ASX Market Rules Guidance Note 7 *Management requirement—Good fame and character—Reliance on APRA requirements* (GN 7) sets out guidance on:
- (a) how directors and responsible executives may be deemed to be 'of good fame and character and of high business integrity'; and
  - (b) the expectation for market participants to lodge a notification of appointment of directors and responsible executives with ASX.
- 33 For the purposes of paragraph 32(a), ASX recognises the use of the Australian Prudential Regulation Authority's (APRA) criteria, as contained in APRA's *ADI authorisation guidelines*, on condition that the market participant immediately notifies ASX if they receive notice from APRA that APRA may consider the person not to be of good fame and character. While originally drafted to apply only to APRA-regulated market participants (e.g. authorised deposit-taking institutions (ADIs)), the guidance is in practice applied by many market participants.
- 34 GN 7 and ASX Market Rules Guidance Note 27 *Ongoing compliance and supervision—Responsibilities of responsible executives* (GN 27) provides guidance on the obligation to notify ASX about the appointment of directors and responsible executives under ASX Market Rule 4.3.2, and the desirable period within which the supervisory responsibilities of a former responsible

executive are to be reassigned (i.e. within six weeks of departure of the incumbent responsible executive).

- 35 ASX guidance in GN 27 recognises that the responsible executive regime is similar in many respects to the responsible manager requirements for AFS licensees, and seeks to minimise competing obligations. We propose to adopt a similar approach and will look at these competing obligations, as they apply to the current regulatory environment, when reviewing the market integrity rules with the Corporations Act requirements: see paragraphs 8–9.

### Proposal

**B2** We propose *not* to retain:

- (a) the definition of 'good fame and character', as it is specified in GN 7; nor
- (b) the guidance in GN 7 and GN 27 that specifies how notifications should be made about responsible executive appointments and supervisory arrangements.

*Your feedback*

B2Q1 Do you agree with our approach? If not, why not?

### Rationale

- 36 Rule 2.1.4 (ASX) now sets out the criteria for assessing 'good fame and character for persons involved in business', which largely reflect the criteria in s913B(4). As such, it is no longer necessary to refer to APRA's criteria.
- 37 The guidance on notification requirements in GN 7 and GN 27 is no longer relevant because Rule 2.3.1 (ASX) imposes a new obligation on market participants to notify ASIC within 10 business days about the appointment of a new responsible executive, or if a person ceases to be a responsible executive of the market participant.

## Responsible executive requirements

### ASX guidance

- 38 GN 27 outlines the responsible executive's regulatory objectives, as contained in the ASX Market Rules, and assists a market participant to manage its ongoing compliance and supervision requirements by describing the supervisory controls, processes, systems and culture within its business that the responsible executive is accountable for.
- 39 Other than our proposal at B2(b), we do not propose to change the substance of this guidance.

## PI insurance requirements

### ASX guidance

- 40 ASX Market Rules Guidance Note 8 *Insurance requirements* (GN 8) provides guidance on the interpretation of ASX Market Rules that related to a market participant's requirement to hold PI insurance. GN 8 provides guidance on the following issues:
- (a) the requirement for market participants to hold PI insurance;
  - (b) when to notify ASX in relation to PI insurance;
  - (c) market participants' obligations if the PI insurance is provided by a related body corporate; and
  - (d) the action ASX would take if a market participant failed to obtain PI insurance.
- 41 With the exception of ASX Market Rule 4.6.5, which required market participants to inform ASX of any other matters in relation to their insurance maintained under ASX Market Rule 4.6, ASIC has adopted ASX Market Rule 4.6 in its entirety—that is, only drafting amendments were made to reflect the transfer of supervision from ASX to ASIC. The market integrity rules to which GN 8 specifically relates are:
- (a) Rule 2.2.1 (ASX) Obligation to have insurance;
  - (b) Rule 2.2.2 (ASX) Insurance with a related body corporate; and
  - (c) Rule 2.2.4 (ASX) Notification of claims.
- 42 We do not propose to change the substance of the guidance provided in GN 8 (other than our proposal at B3).
- 43 We recognise that there is a difference between the AFS licensing regime, which requires licensees who provide services to retail clients to hold PI insurance, and the market integrity rules, which require all market participants to hold PI insurance, irrespective of whether they provide financial services to wholesale or retail clients. We will consider the differences in approach when reviewing the market integrity rules with the Corporations Act requirements: see paragraphs 8–9.

### Director's attestation

#### Proposal

- B3** When PI insurance is provided by a related body corporate, we propose *not* to retain the notification requirement in GN 8 for a director of a market participant to submit an attestation of:
- (a) how they have formed the opinion that the level of insurance cover and excess is reasonable; and
  - (b) how they have satisfied themselves that the related body corporate would be able to pay an insurance claim if necessary.



*Your feedback*

B3Q1 Do you agree with our proposed approach? If not, why not?

B3Q2 Would retaining the requirement to submit an attestation impose an unreasonable burden in practice?

**Rationale**

- 44 A market participant's directors are not required to submit a director's attestation under the market integrity rules—however, we expect directors to perform the necessary due diligence before relying on insurance cover provided by a related body corporate—for example, to ensure that the level of PI cover provided by the related body corporate is adequate, as determined (acting reasonably) by the market participant, taking into account the nature and extent of the business carried on by the market participant.
- 45 In addition, we would expect a market participant to be able to show, if requested to do so, how they have formed the opinion that the level of insurance cover is adequate, and how they have satisfied themselves, and will continue to satisfy themselves, that the related body corporate has adequately provided for the level of cover it is providing. We would expect the market participant to retain records of the due diligence process they complete and be able to provide a copy of this assessment on request.

**Trading records requirements****ASX guidance**

- 46 ASX Market Rules Guidance Note 33 *Trading records* (GN 33) provides assistance to market participants in interpreting former ASX Market Rule 4.10 (Trading records) in maintaining trading records to provide an audit trail for compliance in relation to client orders. Specifically, GN 33 provides background information on the importance of trading records, the rule requirements and interpretive guidance on:
- (a) capturing and maintaining trading records;
  - (b) specific interpretations of elements of ASX Market Rule 4.10;
  - (c) how names should be recorded;
  - (d) performing periodic internal reviews of trading records;
  - (e) relying on records maintained by ASX; and
  - (f) relying on ASX records for the purposes of the Corporations Act.
- 47 Other than our proposals at B4–B5, we do not propose to change the substance of the guidance in GN 33.

## Duration for retaining trading records

### Proposal

- B4** Until we review the market integrity rules and the Corporations Act requirements, we propose to provide guidance that AFS licensee market participants, subject to obligations under both reg 7.8.19(5) and Rule 4.1.4 (ASX), retain trading records for the longer duration—that is, the seven years required under the market integrity rules.

#### *Your feedback*

- B4Q1 Are there any practical issues with this proposed approach? Please provide details.

### Rationale

- 48 We acknowledge the different requirements for AFS licensee market participants under reg 7.8.19(5), which requires AFS licensees to retain records (including trading records) for at least five years, and under Rule 4.1.4 (ASX), which requires records (including trading records) to be kept for a period of seven years. We will consider these differences in approach when we review the market integrity rules with the Corporations Act requirements.

## Providing records to ASIC: Preferred method of delivery

### Proposal

- B5** We propose to request in our guidance that market participants standardise formatting when sending us transaction-related trading records electronically. We will encourage participants to:
- (a) send the requested electronic trading records in either .csv or Excel format, where practicable; and
  - (b) include the following columns of information in the order listed below in two separate files, as indicated.

#### **A file for the following account information when requested**

- market participant name
- account number
- account name
- representatives authorised to trade on the account
- address of the account holder
- telephone number of the account holder

**A file for the following trading information when requested**

- account number
- buy/sell code
- quantity
- security code
- unit price
- value
- trade date
- trade time
- original order
- amended orders
- name of person who gave the instruction
- name of person who received the instruction
- name of any person who passed the instruction on between the person who initially received the instruction and the trading platform, and the date and time they passed it
- name of the DTR (designated trading representative) who entered a trading message into a trading platform
- time the DTR entered a trading message into a trading platform
- whether the trading messages was the result of AOP (automated order processing)
- the open interface device and the computer or other device of the trading participant connected to an open interface device of the trading participant through which the trading message was submitted
- name of the DTR with responsibility for that open interface device or other device connected to the open interface device (unless the trading message was the result of AOP)
- whether the trading message was submitted on the trading participant's own account or for a client

*Your feedback*

B5Q1 What changes would be necessary for you to implement this request? Please provide an indication of the additional time and cost that this would involve.

B5Q2 Do you consider that adopting this best practice would impose an unreasonable burden?

**Rationale**

- 49 GN 33 does not specify the format in which market participants ought to provide trading records requested by ASIC under s912E (surveillance checks by ASIC). As a result, we receive requested trading records in a number of formats. These formats include documents sent as images and as Excel, .pdf and .csv files. This inhibits our ability to effectively and efficiently perform our regulatory functions, given the large quantities of data that cannot be analysed consistently.

## C ASX 24 market participants: Operational obligations in relation to clients

### Key points

We propose to retain the substance of the guidance in SFE Operating Rules Procedure 2.2.26 *Clients' segregated accounts* (PDP 2.2.26), including continuing to encourage ASX 24 market participants to educate their clients on the inherent risks associated with the co-mingling of client money within the clients' segregated account.

We do not propose to retain guidance where this has been adopted as part of the ASIC Market Integrity Rules (ASX 24).

We also propose to request that participants:

- maintain additional supporting documentation to supplement the accounting records required in Rule 2.2.6(k) (ASX 24);
- maximise the term 'clients' segregated account' in an account name to ensure that a person would reasonably identify the account as a clients' segregated account; and
- perform daily reconciliations of clients' segregated accounts.

Note: Throughout this paper we will use the shortened form 'Rule 2.2.6 (ASX 24)' (for example) to refer to a particular rule of the ASIC Market Integrity Rules (ASX 24).

## Clients' segregated account obligations

### SFE guidance

- 50 PDP 2.2.26 sets out how ASX 24 market participants may meet their obligations under former SFE Operating Rule 2.2.26. The SFE procedure provides practical guidance to market participants who hold client money about:
- (a) how and where to deposit money into the clients' segregated accounts;
  - (b) what withdrawals are permitted from the clients' segregated accounts; and
  - (c) how and when money from the clients' segregated accounts may be invested.
- 51 Other than our proposals at C1–C4, we do not propose to change the substance of the guidance in PDP 2.2.26.

## Proposal

- c1** We propose *not* to retain the following guidance in PDP 2.2.26, which has been incorporated into the ASIC Market Integrity Rules (ASX 24):
- (a) PDP 2.2.26(4), which notes that there are additional restrictions on certain investments, such as the need for an investment to be readily realisable and to have 50% of the money invested on 24-hour call (see Rule 2.2.6(i)(ii));
  - (b) PDP 2.2.26(6), which provides additional guidance on how to ensure that client money is separated from the market participant's own money by ensuring that, where the market participant conducts proprietary business, a house account is maintained for the payment of margin liabilities (see Rule 2.2.6(a)(iii) and (iv) (ASX 24));
  - (c) PDP 2.2.26(7), which provides for the handling of property received from clients (see Rule 2.2.6(m) (ASX 24));
  - (d) the part of PDP 2.2.26(8) that states that the segregated account must be designated as a 'clients' segregated account' unless maintained outside Australia and the law requires it to be designated in some other way (see Rule 2.2.6(a)(i) and (ii) (ASX 24));
  - (e) the part of PDP 2.2.26(8) that states that the money received from a client must be deposited in a clients' segregated account of the market participant on or before the next day after the funds are received (see Rule 2.2.6(c) (ASX 24)); and
  - (f) PDP 2.2.26(9), which requires additional money to be deposited in a clients' segregated account where a client is still in deficit after five days (see Rule 2.2.6(f) (ASX 24)).

### Your feedback

C1Q1 Do you agree with this approach? If not, why not?

## Rationale

- 52 The guidance identified at C1(a)–C1(f) has been incorporated into the ASIC Market Integrity Rules (ASX 24) and, as such, does not need to be retained in our regulatory guidance.

## Record-keeping for withdrawal from clients' segregated accounts

### Proposal

- c2** We propose that ASX 24 market participants should maintain, as a matter of good practice, the following supporting documentation as a supplement to their accounting records under Rule 2.2.6(k) (ASX 24):
- (a) a written instruction or record of a client's request for withdrawal;
  - (b) a copy of the client statement reflecting that, before the withdrawal was executed, the market participant confirmed that the client account was in surplus by referring to a copy of the client statement; and

- (c) if the payment relates to payment of brokerage, written evidence documenting the way the brokerage was calculated before the withdrawal.

*Your feedback*

- C2Q1 Would the proposed guidance assist in complying with Rule 2.2.26(k) (ASX 24)? Please provide reasons.
- C2Q2 Are there any practical issues with following this guidance that are unreasonably burdensome? If so, please describe, where possible, the nature and amount of the costs and effort involved.

**Rationale**

- 53 Rule 2.2.6(k) (ASX 24) requires ASX 24 market participants to ‘maintain such accounting records as accurately indicate each withdrawal from a clients’ segregated account’. Historically, breaches of former SFE Operating Rule 2.2.26(k) reflected that there was a lack of understanding about the records that a market participant should maintain to comply with the rule’s requirement to provide a complete and accurate audit trail for each withdrawal. We therefore propose to provide this additional guidance.

**Designating accounts as ‘clients’ segregated accounts’**

**Proposal**

- c3 We propose to provide additional guidance, for the purposes of Rule 2.2.6(a)(i) (ASX 24), that where market participants are unable to include the full term ‘clients’ segregated account’ in the account name, due to the limited number of characters available, the participant should maximise the term used in the space available to ensure that a person would reasonably identify the account as a clients’ segregated account. The account should remain clearly identifiable as a clients’ segregated account on all views of the account that are accessible on account statements and systems.

*Your feedback*

- C3Q1 Are there any practical issues with the proposed guidance outlined in C3? Please provide details.

**Rationale**

- 54 Rule 2.2.6(a)(i) (ASX 24) requires that an account holding client money must be designated as a ‘clients’ segregated account’. This is to assist in identifying client monies. Given the limited number of characters available for electronically naming bank accounts, we propose that, at the time the account is set up, the account name should maximise the use of the term ‘clients’ segregated account’ to ensure that a person would reasonably identify the account as holding client monies. We understand that this is consistent with the approach adopted in practice by SFE.

## Reconciliation of clients' segregated accounts

### Proposal

- c4** We propose that ASX 24 market participants should perform regular reconciliations of clients' segregated accounts to confirm that client money has been correctly deposited and withdrawn in accordance with the market integrity rules. We consider that, as a matter of good practice, daily reconciliations would be appropriate.

#### *Your feedback*

- C4Q1 Do you agree with our approach? If not, why not?
- C4Q2 What do you consider to be a suitable frequency for reconciling accounts?

### Rationale

- 55 We consider that regular reconciliations of clients' segregated accounts are pivotal for enabling expeditious and effective detection of discrepancies that may lead to client loss and settlement risk.

## Notice to clients about clients' segregated accounts

### SFE guidance

- 56 PDP 2.2.26(11) recommends that ASX 24 market participants pass on to their clients a notification (in the form of an SFE Notice) relating to funds placed in the clients' segregated account. This is a practical step to highlight to clients that funds in the clients' segregated account are co-mingled and, therefore, individual client funds may be at risk if another client defaults—that is, even if it is not their own default. PDP 2.2.26 recommends that market participants distribute SFE Notice 50/06 to their clients.

### Proposal

- c5** We propose to continue to encourage market participants to educate their clients on the inherent risks associated with the co-mingling of client money within the clients' segregated account, although we do not propose to retain SFE Notice 50/06.

#### *Your feedback*

- C5Q1 Do you agree with our approach? How best do you think this can be achieved with minimal operational burden?
- C5Q2 Should we provide a standard information sheet for distribution to clients?

### **Rationale**

- 57 SFE Notice 50/06 sets out important information about how clients' segregated accounts operate and the potential contingent liabilities that may arise for clients out of the operation of these accounts.
- 58 The notification explains that the purpose of clients' segregated accounts is to separate client money from house money so that client money is insulated in the event of a market participant default—that is, a market participant may not apply clients' segregated accounts money to meet house liabilities.
- 59 However, if one client defaults, the market participant has the right to apply all client funds to meet the default. There has been evidence to suggest that the implications of this are not well understood, particularly in the retail trader community. As such, we consider it is important to encourage market participants to continue to notify their retail clients about these risks.



## D Regulatory and financial impact

60 In developing the proposals in this paper, we have carefully considered their regulatory and financial impact. On the information currently available to us we think they will strike an appropriate balance between:

- (a) providing industry with sufficient clarity to comply with the ASIC Market Integrity Rules (ASX Market) 2010 and the ASIC Market Integrity Rules (ASX 24 Market) 2010; and
- (b) protecting the integrity of the market and retail clients.

61 Before settling on a final policy, we will comply with the Australian Government's regulatory impact analysis (RIA) requirements by:

- (a) considering all feasible options, including examining the likely impacts of the range of alternative options which could meet our policy objectives;
- (b) if regulatory options are under consideration, notifying the Office of Best Practice Regulation (OBPR);
- (c) if our proposed option has more than minor or machinery impact on business or the not-for-profit sector, preparing a Regulation Impact Statement (RIS).

62 All RISs are submitted to the OBPR for approval before we make any final decision. Without an approved RIS, ASIC is unable to give relief or make any other form of regulation, including issuing a regulatory guide that contains regulation.

63 To ensure that we are in a position to properly complete any required RIS, we ask you to provide us with as much information as you can about:

- (a) the likely compliance costs;
- (b) the likely effect on competition;
- (c) other impacts, costs and benefits; and
- (d) the necessary lead time to implement the changes.

of our proposals or any alternative approaches: see 'The consultation process' p. 4.

## Appendix: Tracking the status of relevant ASX and SFE guidance

Table 2 and Table 3 show the current status of all relevant ASX guidance notes and SFE procedures, determinations and practice notes as at the date of issue of this consultation paper. These tables will be continuously updated in future publications as we continue our conversion of pre-existing guidance into ASIC regulatory guides for ASX and ASX 24 market participants.

Note: The stages of conversion indicated below may run concurrently.

**Table 2: Status of pre-existing ASX guidance relevant to ASIC Market Integrity Rules (ASX Market) 2010**

Relevant pre-existing ASX guidance notes (GNs)		Current status and comments
GN 1	Prevention of manipulative trading	To be reviewed in 2011, together with the AOP guidance notes (GN 19, GN 21 and GN 22)
GN 3	Reporting to clients—Confirmations	Stage 3 conversion
GN 4	New clients	Stage 2 conversion
GN 5	New clients—Electronic client agreements for derivatives market transactions	Stage 2 conversion
GN 6	Management requirements	Stage 1 conversion: see CP 152 (issued March 2011)
GN 7	Management requirements—Good fame and character—Reliance on APRA requirements	Stage 1 conversion: see CP 152 (issued March 2011)
GN 8	Insurance requirements	Stage 1 conversion: see CP 152 (issued March 2011)
GN 11	Client order priority	Stage 3 conversion
GN 12	Client money and property—Client funds deposited with third parties	Stage 2 conversion
GN 13	Prohibition of advice to clients	Stage 2 conversion
GN 19	Automated order processing: Certification	To be converted in light of responses to CP 145
GN 21	Automated order processing: Authorised persons	To be converted in light of responses to CP 145
GN 22	Automated order processing: Operational requirements	To be converted in light of responses to CP 145
GN 23	New clients or clients trading in new products for the first time—Dispatch of ASX explanatory booklets	Stage 2 conversion

Relevant pre-existing ASX guidance notes (GNs)		Current status and comments
GN 27	Ongoing compliance and supervision—Responsibilities of responsible executives	Stage 1 conversion: see CP 152 (issued March 2011)
GN 29	Managed discretionary accounts	To be reviewed separately
GN 31	Client agreements—Requirements: The requirement for participants to enter into client agreements with clients	Stage 2 conversion
GN 32	Bulk authorisation of index arbitrage orders in ITS	Stage 3 conversion
GN 33	Trading records	Stage 1 conversion: see CP 152 (issued March 2011)
GN 37	Maintenance of an orderly market when closing out settlement failures	Stage 3 conversion

**Table 3: Status of pre-existing SFE guidance relevant to ASIC Market Integrity Rules (ASX 24 Market) 2010**

Relevant pre-existing SFE procedures, determinations and practice notes		Current status and comments
1.13, 2.2.23	Order records and accounting records	Stage 2 conversion
2.2.25	Client documentation	Stage 2 conversion
2.2.26	Clients' segregated account obligations	Stage 1 conversion: see CP 152 (issued March 2011)
2.2.28	Mandatory recording of information by the exchange and its participants	Stage 2 conversion
3.1.1	Expressions of interest	Stage 3 conversion
3.1.4, 3.1.5	Market manipulation and misleading acts or practices regarding price	Stage 4 conversion
3.1.6	Entering orders without an intent to trade	Stage 4 conversion
3.1.7	Orders to be transmitted as soon as received	Stage 4 conversion
3.1.8	Orders to be transmitted and executed in the sequence received	Stage 4 conversion
3.1.9	Aggregation of orders	Stage 3 conversion
3.1.10	Disclosure	Stage 4 conversion
3.1.11	Withholding orders	Stage 3 conversion
3.1.12	Withdrawing orders	Stage 3 conversion
3.1.13	Pre-arrangement	Stage 4 conversion

<b>Relevant pre-existing SFE procedures, determinations and practice notes</b>		<b>Current status and comments</b>
3.1.14	Trading to the exclusion of others	Stage 3 conversion
3.1.15	Wash trades	Stage 4 conversion
3.1.17	Personal account trading	Stage 4 conversion
3.1.18	Dual trading prohibition	Stage 4 conversion
3.1.19	Trades to be allocated in sequence of order receipt	Stage 4 conversion
3.2	Strategy trades	Stage 4 conversion
3.3	Pre-negotiated business	Stage 4 conversion
3.4	Block trades	Stage 3 conversion
3.5	Exchange for physical transactions	Stage 3 conversion

## Key terms

Term	Meaning in this document
ADI	authorised deposit-taking institution
AFS licence	An Australian financial services licence under s913B of the Corporations Act that authorises a person who carries out a financial services business to provide financial services Note: This is a definition contained in s761A of the Corporations Act.
AFS licensee	A person who holds an Australian financial services licence under s913B of the Corporations Act Note: This is a definition contained in s761A of the Corporations Act.
AOP	automated order processing
APRA	Australia Prudential Regulation Authority
ASIC	Australian Securities and Investments Commission
ASIC Market Integrity Rules (ASX)	ASIC Market Integrity Rules (ASX Market) 2010—rules made by ASIC under s798G of the Corporations Act for trading on ASX
ASIC Market Integrity Rules (ASX 24)	ASIC Market Integrity Rules (ASX 24 Market) 2010—rules made by ASIC under s798G of the Corporations Act for trading on ASX 24
ASX	The market known as the Australian Securities Exchange, operated by ASX Limited
ASX 24	The market formerly known as the Sydney Futures Exchange (SFE), operated by ASX Limited
ASX 24 Operating Rules	ASX Limited's new operating rules, which replace the pre-existing SFE Operating Rules
ASX guidance notes	Guidance notes providing assistance to ASX market participants on ASX's interpretation of the former ASX Market Rules
ASX Market Rules	Previous operating rules made by ASX Limited dealing with activities or conduct of its market and of persons in relation to the market
ASX Operating Rules	ASX Limited's new operating rules, which replace the pre-existing ASX Market Rules
Australian domestic licensed financial market	A financial market licensed under s795B(1) of the Corporations Act
Australian market licence	Australian market licence under s795B of the Corporations Act that authorises a person to operate a financial market

Term	Meaning in this document
automated order processing	As defined in Rule 1.4.3 (ASX)
Corporations Act	<i>Corporations Act 2001</i> , including regulations made for the purposes of that Act
Corporations Regulations	Corporations Regulations 2001
designated trading representative	As defined in Rule 1.4.3 (ASX)
DTR	designated trading representative
Financial Market Supervision Act	<i>Corporations Amendment (Financial Market Supervision) Act 2010</i>
GN 6 (for example)	An ASX guidance note (in this example, numbered 6)
market integrity rules	Rules made by ASIC, under s798G of the Corporations Act, for trading on domestic licensed markets
market licensee	Holder of an Australian market licence
market participant	As defined in s761A of the Corporations Act
PI insurance	professional indemnity insurance
PDP 2.2.26 (for example)	An SFE procedure (in this example, numbered 2.2.26)
Pt 9.4B (for example)	A part of the Corporations Act (in this example, numbered 9.4B), unless otherwise specified
reg 7.2A.01 (for example)	A regulation under the Corporations Regulations (in this example, numbered 7.2A.01), unless otherwise specified
RG 214 (for example)	An ASIC regulatory guide (in this example, numbered 214)
Rule 4.1.4 (ASX) (for example)	A rule of the ASIC Market Integrity Rules (ASX) (in this example, numbered 4.1.4)
Rule 2.2.1 (ASX 24) (for example)	A rule of the ASIC Market Integrity Rules (ASX 24) (in this example, numbered 2.2.1)
s913B(4) (for example)	A section of the Corporations Act (in this example, numbered 913B(4)), unless otherwise specified
SFE	The market formerly known as Sydney Futures Exchange (now ASX 24)
SFE Operating Rules	Previous operating rules made by Sydney Futures Exchange Limited dealing with activities or conduct of its market and of persons in relation to the market
SFE procedures	Procedures, determinations and practice notes providing assistance to ASX 24 market participants on SFE's interpretation of the former SFE Operating Rules
Sydney Futures Exchange Limited	Former name of the market licensee that operates ASX 24, formerly the Sydney Futures Exchange. This entity is now known as Australian Securities Exchange Limited