



ASIC

Australian Securities & Investments Commission

REPORT 204

Response to submissions on CP 131 Proposed ASIC Market Integrity Rules: ASX and SFE markets

July 2010

About this report

This report highlights the issues that arose out of submissions received on Consultation Paper 131 *Proposed ASIC Market Integrity Rules: ASX and SFE markets* (CP 131) and details our response to those issues.

It also outlines the key differences between the draft and final market integrity rules for the ASX Limited (ASX) and ASX 24 (formerly Sydney Futures Exchange (SFE)) markets.

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.

Disclaimer

This report does not contain ASIC policy. Please see Regulatory Guide 214 *Guidance on ASIC market integrity rules for ASX and ASX 24 markets* (RG 214).

This report is based on ASIC market integrity rules as approved in principle by the Minister on 8 July 2010. We anticipate that the Minister will approve these rules on commencement of the transfer of market supervision legislation (i.e. on 1 August 2010). These rules would be made by ASIC on that same day.

On 1 April 2010, the ASX Group announced that it intends that the SFE market be renamed the ASX 24 market in the future. In this document the SFE market is referred to as the ASX 24 market. We also note that the ASX Group proposes to make a number of changes to the names of companies within its group. To the extent necessary, this document reflects the proposed new names of companies within the ASX Group. We note that the name changes proposed by the ASX Group have not yet been formally adopted and are subject to a number of regulatory applications. If the proposed names are not formally adopted, we will amend this document to reflect the current names at the time of publication.

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A Overview/consultation process

- 1 On 16 February 2010, ASIC released Consultation Paper 131 *Proposed ASIC Market Integrity Rules: ASX and SFE markets* (CP 131), which set out ASIC's proposals for new market integrity rules for the Australian Securities Exchange (ASX) and Sydney Futures Exchange (SFE) (now ASX 24) based on existing rules for these markets.
- 2 The consultation paper attached as appendices:
 - (a) the draft market integrity rules for the ASX and SFE markets;
 - (b) a table for each market showing the proposed division of supervisory responsibility between ASIC and ASX Limited (ASXL) and Sydney Futures Exchange Limited (SFEL) respectively; and

Note: ASXL is the market licensee that operates ASX. SFEL is the market licensee that operates that operates SFE (now ASX 24).
 - (c) a table for each market showing the extent of proposed redrafting with marked-up changes indicating where we proposed to deviate from the existing ASX Market Rules and SFE Operating Rules.
- 3 It explained our approach in developing the proposed rules and how we proposed they would apply following the transfer of market supervision to ASIC. Consultation on our proposed market integrity rules for the ASX and SFE markets closed on 26 March 2010.
- 4 This report highlights the issues that arose out of the submissions received on CP 131 and our responses to those issues. It also explains the key differences between the draft market integrity rules attached to the consultation paper and the final market integrity rules.
- 5 This report is not meant to be a comprehensive summary of all responses received. It is also not meant to be a detailed report on the market integrity rules.
- 6 This report should be read in conjunction with Regulatory Guide 214 *Guidance on ASIC market integrity rules for ASX and ASX 24 markets* (RG 214). The regulatory guide gives guidance on how ASX and ASX 24 market participants can comply with their obligations under ASIC market integrity rules for these markets.
- 7 The final market integrity rules can be downloaded from ASIC's website at www.asic.gov.au/markets: see Market Integrity Rules 1 *ASIC/ASX Market Integrity Rules* (MIR 1) and Market Integrity Rules 2 *ASIC/ASX 24 Market Integrity Rules* (MIR 2).
- 8 Tables linking the pre-existing ASX Market Rules and SFE Operating Rules to the ASIC market integrity rules are included as appendices. Explanatory statements to the made rules will also be available on the website.

Responses to consultation

- 9 We received six responses to CP 131 from the following entities:
- (a) Australian Banker's Association (ABA);
 - (b) Australian Financial Markets Association (AFMA);
 - (c) ASX Limited;
 - (d) Chi-X;
 - (e) QBE Insurance Group; and
 - (f) Stockbrokers Association of Australia.
- 10 We are grateful to respondents for taking the time to send us their comments.
- 11 Generally, respondents expressed support for ASIC's approach of maintaining the status quo by retaining the substance of existing rules. Industry was comfortable with the proposed split of rules between ASX/SFE and ASIC as set out in the consultation paper. Most of the issues raised in the submissions were of a technical nature and have been addressed in the drafting of the final market integrity rules to the extent possible.
- 12 In addition to technical issues, interested parties raised concerns about a relatively small number of more substantial issues. These are addressed in Section B of this feedback report.

Key differences between draft and final market integrity rules

- 13 Some technical changes have been made to the market integrity rules to take into account feedback from interested parties.
- 14 In addition to these changes, we have made amendments to the market integrity rules to take into account:
- (a) additional detail and obligations from existing requirements and information currently in guidance notes, procedures, appendices to procedures, determinations and practice notes of the ASX Market Rules and SFE Operating Rules;
 - (b) additional market integrity rules about providing information to ASIC that apply to ASXL and SFEL only; and
 - (c) discussions with the ASXL and SFEL where it was agreed that some topics would move from ASX Market Rules to market integrity rules and that one topic was no longer necessary.

B Summary of responses

Key points

Generally, respondents expressed support for ASIC's approach to creating market integrity rules and our objective of maintaining the status quo by retaining the substance of existing operating rules in our market integrity.

Most of the issues raised by interested parties were of a technical nature and have been addressed in the drafting of the final market integrity rules to the extent possible.

In addition to technical issues, interested parties raised concerns about:

- duplication with the Corporations Act;
- overlap with the operating rules of the market operator;
- topics that are likely to be contained in common rules for competition;
- the disciplinary process; and
- the need for substantive changes in some areas.

Duplication with the Corporations Act

- 15 There are a small number of market integrity rules that deal with the same or similar subject matters as dealt with by other provisions of the *Corporations Act 2001* (Corporations Act). Accordingly, those rules may overlap with or supplement obligations arising from Australian financial services (AFS) licence conditions and other Corporations Act provisions.
- 16 We intend in the future to review the market integrity rules to create one set of market integrity rules for like markets. We intend to use that opportunity to review and address duplication with the Corporations Act.

Overlap with operating rules

- 17 A small number of market integrity rules overlap with obligations contained in the operating rules of the market operator. The overlap is not extensive and it lies in areas where the market operator has an operational interest; while ASIC has an interest from a market integrity perspective.
- 18 We are developing cooperation processes (including protocols in some circumstances) with market operators outlining our complementary approach to supervision and enforcement so that at a working level we are minimising practical consequences of the overlap in the two sets of rules.

Common rules for competition

- 19 Interested parties expressed views that some additional topic areas should form part of ASIC's regulatory framework (e.g. best execution, pre- and post-trade transparency, direct market access filters and trade cancellations).
- 20 Rather than create additional market integrity rules or transfer existing market operating rules dealing with these subjects now, we propose that rules of this kind may form part of the common rules for competition which will be consulted upon separately later this year.

The disciplinary process

- 21 Issues raised by interested parties about the disciplinary process will be addressed in our regulatory guide on the Markets Disciplinary Panel (MDP).
- Note: See Consultation Paper 136 *Markets Disciplinary Panel* (CP 136) at www.asic.gov.au/cp. CP 136 was released on 26 May 2010 and comment closed on 21 June 2010. We intend to issue our final guidance on this topic before 1 August 2010.
- 22 We have taken into account comments from interested parties about the allocation of penalty tiers to specific rules and made amendments we considered appropriate.
- 23 The penalties for breaches of the market integrity rules are based on the current ASX Disciplinary Tribunal Sanction Guidelines. We have relied on those guidelines to determine which penalty level applies to each rule. The penalty amount set out in a market integrity rule must not exceed AUD1 million and is similar to the maximum fine the ASX Disciplinary Tribunal may currently impose.
- 24 In addition to preserving a maximum penalty, each penalty tier has a minimum of zero. The factors which the MDP will take into account in deciding outcomes for breaches of market integrity rules, including what remedies are appropriate, will be contained in the final regulatory guide on the MDP.

Substantive changes

- 25 Interested parties sought some changes to the substance of the market integrity rules in areas such as trust account requirements, management requirements and responsible executive requirements, as part of a harmonised supervisory regime.
- 26 Amending the substance of existing market integrity rules and obligations at this stage would change the status quo and be likely to require a lengthier lead-in time for market participants to make changes to systems and operating models to comply with the amended market integrity rules.
- 27 Making such changes would be inconsistent with our policy objective for this stage of the process of maintaining the status quo and minimising change. We will review these rules as part of a wider review of the market integrity rules in the next 12 to 18 months.

C Key differences between draft and final market integrity rules

Key points

Some technical changes have been made to the market integrity rules to take into account feedback from interested parties.

In addition to these changes, we have made amendments to the market integrity rules to take into account:

- additional detail and obligations from existing requirements and information in guidance notes, procedures, appendices to procedures, determinations and practice notes of the ASX Market Rules and SFE Operating Rules;
- additional market integrity rules about providing information to ASIC that apply to ASXL and SFEL only; and
- discussions with ASXL and SFEL where it was agreed that some topics would move from ASX Market Rules to market integrity rules and that one topic was no longer necessary.

Note: The final market integrity rules can be downloaded from the ASIC website at www.asic.gov.au/markets: see MIR 1 and MIR 2.

Additional detail and obligations from associated material

- 28 We have amended the draft market integrity rules to include information from guidance notes, procedures, appendices to procedures, determinations and practice notes currently in the ASX Market Rules and SFE Operating Rules.
- 29 Examples include:
- (a) the accreditation process for ASX derivatives retail client advisers;
 - (b) the minimum information which must be contained in client agreements for clients dealing for the first time in futures, options, warrants and party-paid securities through the ASX market; and
 - (c) requirements surrounding the certification of automated order processing systems.

New rules applicable only to the market operator

- 30 We have created new market integrity rules for providing information to ASIC by market operators. These new rules only apply to ASX and ASX 24 market operators at this stage and impose no additional obligations on market participants.
- 31 For the ASX 24 market, these rules supersede the proposed draft rules which required the market operator to give notice of a decision to cancel an order of a trade to ASIC and to provide daily beneficial ownership reports and exceptional reports.

New or removed topic areas

- 32 In discussions with ASXL and SFEL, it was agreed that some topics would move from ASX Market Rules to market integrity rules.
- 33 We have also removed one proposed ASIC market integrity rule for the ASX market because it is no longer necessary.

Market integrity rules for the ASX market

- 34 The final market integrity rules for the ASX market now include rules that were in the operating rules on the following topics:
- (a) professional indemnity insurance requirements;
 - (b) cash market products subject to takeover bids, schemes and on-market buy-backs;
 - (c) steps ASIC can take in instances of a cornered market;
 - (d) designated trading representatives (DTRs); and
 - (e) educational requirements and accreditation for ASX derivatives retail client advisers, including renewal of accreditation, voluntary withdrawal of accreditation, suspension or withdrawal of accreditation and re-accreditation after withdrawal or expiry, and continuing professional education requirements.
- 35 We have also removed one proposed rule relating to monthly reporting requirements for derivatives market transactions (ASX Market Rule 7.17). This topic is covered by the Australian Clearing House Pty Limited (ACH) Clearing Rules and is no longer necessary.
- 36 There are no other substantial changes to the topics contained in the market integrity rules for the ASX market.

Market integrity rules for the ASX 24 market

- 37 A new rule relating to concentration of risk that a participant may have has been added to the final ASIC market integrity rules for the ASX 24 market. This rule provides that participants shall not permit any one client to represent such a percentage of the trading by the participant as may prejudice or diminish the ability of the participant to meet its obligations.
- 38 There are no other substantial changes to the topics contained in the market integrity rules for the ASX 24 market.

Appendix: List of non-confidential respondents

- Australian Banker's Association (ABA)
 - Australian Financial Markets Association (AFMA)
 - ASX Limited
 - Chi-X
 - QBE Insurance Group
 - Stockbrokers Association of Australia
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