



**ASIC**

Australian Securities & Investments Commission

## REPORT 244

# Response to submissions on CP 161 Proposed ASIC market integrity rules for capital and related requirements: ASX, ASX 24 and Chi-X markets

August 2011

### **About this report**

This report highlights the key issues that arose out of the submissions received on Consultation Paper 161 *Proposed ASIC market integrity rules for capital and related requirements: ASX, ASX 24 and Chi-X markets* (CP 161) and details our response to those issues.

### 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 constitute legal advice. We encourage you to seek your own professional advice to find out how the Corporations Act and other applicable laws apply to you, as it is your responsibility to determine your obligations.

This report does not contain ASIC policy. Please see Regulatory Guide 226 *Guidance on ASIC market integrity rules for capital and related requirements: ASX and ASX 24 markets* (RG 226).

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## A Overview/Consultation process

1 In Consultation Paper 161 *Proposed ASIC market integrity rules for capital and related requirements: ASX, ASX 24 and Chi-X markets* (CP 161), we sought feedback on our proposals for market integrity rules for capital and related requirements for the ASX market, the ASX 24 market (formerly known as the Sydney Futures Exchange market) and the proposed new market (Chi-X market) to be operated by Chi-X Australia Pty Limited. We proposed that these rules would transfer across to ASIC, the ASX Group's current capital and related requirements, consistent with our general approach to the transfer of supervision from the ASX Group to ASIC.

Note: In this report, we use 'ASX Group' to refer collectively to ASX Limited, which operates the ASX market, and Australian Securities Exchange Limited, which operates the ASX 24 market.

2 CP 161 dealt with:

- (a) the transfer of rules for capital, reporting and margin for the ASX and ASX 24 markets;
- (b) proposed penalties for breaches of these rules;
- (c) the status of current market guidance materials for the ASX and ASX 24 markets;
- (d) the status of current waivers for the ASX and ASX 24 markets;
- (e) proposed capital and reporting rules for the Chi-X market;
- (f) a new obligation for ASX 24 market participants to reconcile client money daily (consistent with the current obligation on ASX market participants); and
- (g) a change to the deadline for non-clearing ASX market participants lodging monthly capital returns from one month after the end of the month to 10 days after the end of month (consistent with the obligation on non-clearing ASX market participants).

3 This report highlights the key issues that arose out of the submissions received to CP 161 and our response to those issues.

4 This report is not meant to be a comprehensive summary of all responses received, nor a detailed report on every question in CP 161. We have limited this report to the key issues.

5 This report should be read in conjunction with Regulatory Guide 226 *Guidance on ASIC market integrity rules for capital and related requirements: ASX and ASX 24 markets* (RG 226).

## Responses to consultation

- 6 We received a number of written submissions to CP 161 from retail and institutional brokers, industry associations and compliance firms. We are grateful to respondents for taking the time to send us their comments. Some verbal comments were also made to us to clarify and explain comments in the written submissions.
- 7 For a list of the non-confidential respondents to CP 161, see the appendix. Copies of these submissions are on the ASIC website at [www.asic.gov.au/cp](http://www.asic.gov.au/cp) under CP 161.
- 8 The majority of submissions were supportive of our proposals. However, we have refined some of our guidance and the market integrity rules to take into account the feedback in the submissions we received. Our final guidance on the ASIC market integrity rules for capital and related requirements for the ASX and ASX 24 markets is published in RG 226.

## B Summary of responses

### Key points

Respondents to CP 161 were generally supportive of all our proposals. The main concerns related to our proposed two new requirements (i.e. the requirement for all ASX 24 market participants to complete daily reconciliation of client money and the reduced monthly reporting deadline for non-clearing ASX 24 market participants).

On our proposal for daily reconciliations of client money, two participants argued that this would require additional work. However, most respondents had no concerns and were already doing daily reconciliations. We have adopted this proposal, including the proposed 1 January 2012 start date.

On our proposal for a reduced monthly reporting deadline, a few participants argued they may need time to get their IT systems ready or that they may need extra time to collate information from overseas offices. We have addressed this by postponing the start date of the reduced deadline from 1 August 2011 to 1 January 2012 and will consider granting a waiver, where a participant is able to demonstrate there are sufficient grounds.

### Transfer of rules for ASX and ASX 24 markets

- 9 In CP 161, we proposed to make market integrity rules for capital, reporting and margins for ASX and ASX 24 market participants, modelled on the current requirements in the ASX and ASX 24 Operating Rules. The main consideration underlying this approach was to retain the structure and drafting used in the current capital, reporting and margin requirements in the ASX and ASX 24 Operating Rules to ensure market certainty and to minimise the impact on participants.
- 10 The majority of respondents agreed with this approach.
- 11 One respondent questioned the suitability of retaining the existing ASX Group risk-based capital requirements for ASX market participants. It also suggested that ASIC consider requiring participants to include underwriting risk when calculating their level of required risk-based capital.
- 12 Two submissions raised concerns about the regulation of Australian financial services (AFS) licensees that are not market participants, arguing that there would be advantages in these licensees being regulated in a similar way to market participants.
- 13 One respondent raised a concern about the confidentiality of returns lodged with ASIC through the ASX Group's electronic returns lodgement portal and suggested that lodging returns directly with ASIC may be preferable.

- 14 One clearing ASX 24 market participant raised concerns about our proposed reporting deadline for annual returns and about the details required in the director's statement. However, it eventuated that, as a clearing participant, these requirements will not apply to them.

*ASIC's response*

We have adopted the approach set out in CP 161.

As stated in CP 161, we may review the suitability of the capital rules for these markets, after we have been supervising capital requirements for a period. This may also involve a review of what entities the rules should apply to.

In relation to confidentiality, the ASX Group's role in receiving returns is simply one of automatically forwarding the returns to ASIC. Nonetheless, we intend to review these arrangements at a later date with a view to having returns lodged directly with ASIC.

## Proposed penalties for ASX and ASX 24 markets

- 15 In CP 161, we proposed to set maximum penalty amounts in line with the maximum amounts set by the existing ASIC market integrity rules for the ASX and ASX 24 markets (i.e. \$20,000, \$100,000 or \$1,000,000), noting that the *Corporations Act 2001* (Corporations Act) allows ASIC to set maximum penalty amounts of up to \$1,000,000 for market integrity rules.
- 16 We explained that in proposing each maximum penalty amount, we have taken into account the ASX Enforcement and Appeals Rulebook, along with decisions of the ASX Group's past and present review bodies.
- 17 There was support among respondents for our proposals.

*ASIC's response*

We have adopted the approach set out in CP 161.

## Status of current market guidance materials for ASX and ASX 24 markets

- 18 In CP 161, we proposed to take into account the ASX Group's guidance materials—the *Capital Liquidity Handbook* and the *Capital Requirements Guidance*—when interpreting the proposed market integrity rules for the ASX market.
- 19 We also proposed not to take into account any ASX Group guidance materials when interpreting the proposed market integrity rules for the ASX 24 market, as all relevant guidance will be reflected in the market integrity rules.

- 20 We stated that after a period, we may consider reviewing our policy position on these guidance materials in light of changes in the market or other factors and that, if so, we would consult with industry further at that stage.
- 21 There was support among respondents for our proposals.

*ASIC's response*

We have adopted the approach set out in CP 161.

## Status of current waivers for ASX and ASX 24 markets

- 22 In CP 161, we proposed to grant waivers from the proposed market integrity rules, similar to those currently granted to participants by the ASX Group from the capital, reporting and margin requirements in the ASX and ASX 24 Operating Rules.
- 23 Respondents were supportive of this proposal. One respondent also thought ASIC should work closely with the ASX Group in relation to waiver requests involving both the ASIC market integrity rules and the ASX Group's clearing rules to ensure similar outcomes.

*ASIC's response*

All ASX Group waivers in effect on 31 July 2011 have been automatically transferred to apply to the ASIC market integrity rules under reg 10.14.04 of the Corporations Regulations 2001.

## Proposed capital and reporting rules for Chi-X market

- 24 In CP 161, we proposed to make market integrity rules for capital and reporting (but not margins), modelled on our proposed market integrity rules for capital and reporting for the ASX market, with only the minimum changes necessary to tailor them for the Chi-X market, to take effect from 31 October 2011, the potential start date for the Chi-X market.
- 25 We also proposed to take a similar approach in setting maximum penalties as we proposed to take for the ASX market.
- 26 All respondents agreed with our proposed approach of having similar rules for the ASX and Chi-X markets.
- 27 One respondent argued further that the market integrity rules for capital should be the same, not only for the ASX and Chi-X markets, but also for all other markets, including the National Stock Exchange and the Asia Pacific Exchange, to reduce the potential for regulatory arbitrage.



*ASIC's response*

We have adopted the approach set out in CP 161.

At a future date, we may consider further harmonisation of capital requirements.

## **Obligation for ASX 24 participants to reconcile client money daily**

- 28 In CP 161, we proposed to insert a new rule into the market integrity rules for the ASX 24 market requiring all ASX 24 market participants to complete daily reconciliations of client money, to take effect from 1 January 2012.
- 29 We also stated our belief that daily reconciliations should normally form part of a market participant's compliance process for protecting client money, given that, in an insolvency situation, client money can be at risk if it is not properly segregated.
- 30 We also referred to Consultation Paper 152 *ASIC's conversion of ASX and SFE guidance: General operational obligations* (CP 152), in which we proposed daily client money reconciliations as a matter of good practice for ASX 24 participants: see proposal C4. An express requirement would further harmonise the obligations of the participants of the ASX and ASX 24 markets.
- 31 Respondents generally agreed with our approach, with most respondents stating that they already completed daily reconciliations of client money as a matter of good practice. Some respondents also stated that they believe the proposed rule for daily reconciliation of client money was a positive development due to greater harmonisation between ASX and ASX 24 markets.
- 32 Concerns were raised by two participants about the additional time it would take them to complete daily client reconciliations.

*ASIC's response*

We have adopted the approach set out in CP 161.

We view such daily reconciliations as an essential part of a participant's compliance process for protecting client money. We also view harmonisation of the ASX and ASX 24 market rules as important.

Further, most participants already complete daily reconciliations as part of their standard compliance process. We acknowledge that a few participants may need additional resources to complete daily reconciliations. We believe the 1 January 2012 start date will allow these participants adequate time to prepare.

## Change to deadline for lodging ASX 24 capital returns

- 33 In CP 161, we proposed to reduce the lodging time for ASX 24 market monthly capital returns from one month after the end of each month to 10 business days after the end of each month, to take effect from 1 August 2011. This is so that monthly reports are more up-to-date and to harmonise this deadline with the ASX market's current 10-business day deadline.
- 34 Some participants argued that their IT systems would not be ready by 1 August 2011 for the reduced reporting deadline. Some international participants also argued that it may be difficult for them to meet this deadline, as they may not be able to obtain necessary information from their overseas offices in time.

### *ASIC's response*

We have adopted the approach set out in CP 161, but with effect from 1 January 2012, rather than 1 August 2011.

We have postponed the start date to give participants time to ensure their IT systems are ready. Where a participant has difficulty meeting this deadline, we may consider granting them a waiver to extend the reporting period.

## Appendix: List of non-confidential respondents

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- Australian Financial Markets Association
  - Stockbrokers Association of Australia
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