



ASIC

Australian Securities & Investments Commission

REPORT 323

Market assessment report: IMB Ltd

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About this report

This assessment covers the period 26 February 2011 to 24 February 2012 (the 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 IMB Ltd (IMB)

IMB was granted an Australian market licence on 8 July 2005. It was also granted an Australian clearing and settlement facility (CS facility) licence on that date too. This report covers our assessment of how well IMB has complied with its obligations as a market and CS facility licensee.

Report number	Report date
REP 249	August 2011
REP 208	June 2010
REP 171	August 2009
REP 148	January 2009
REP 100	September 2007
REP 86	October 2006

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Key findings and recommendations

Key findings

- 1 ASIC is satisfied that during the assessment period IMB had:
 - adequate arrangements for the operation of its market in accordance with its obligations under s792A(c) of the *Corporations Act 2001* (Corporations Act);
 - adequate arrangements for the supervision of its CS facility in accordance with its obligations under s821A(c) of the Corporations Act; and
 - sufficient resources to comply with its obligations under s792A(d) and 821A(d) of the Corporations Act.

Recommendations

- 2 We do not have any recommendations to make about:
 - IMB's arrangements for the operation of its market and for the supervision of its CS facility; and
 - IMB's resources for operating the market and CS facility.

A The assessment

Key points

ASIC conducts annual assessments of market licensees, such as IMB, because it is required to do so under s794C of the Corporations Act. We are also required to conduct annual assessments of CS facility licensees under s823C.

The scope of our assessment must always include the obligations found in s792A(c) and 821A(c), but we can include other Ch 7 and 8 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 and supervised its CS facility.

Scope

- 3 Under s792A(c), a market licensee must have adequate arrangements for operating the market, including arrangements for:
 - handling conflicts between the commercial interest of the licensee and the need for the licensee to ensure that the market operates in a fair, orderly and transparent way; and
 - monitoring and enforcing compliance with the market's operating rules.
- 4 ASIC is required to assess how well a market licensee complies with its obligations under s792A(c) at least once a year: s794C(2).
- 5 Under s821A(c), a CS facility licensee must have adequate arrangements for supervising the facility, including arrangements for:
 - handling conflicts between the commercial interests of the licensee and the need for the licensee to ensure that the facility's services are provided in a fair and effective way; and
 - enforcing compliance with the facility's operating rules.
- 6 ASIC must assess how well a CS facility licensee complies with its obligations under s821A(c) at least once a year: s823C(2).
- 7 In addition, in accordance with s794C(1) and 823C(1), 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 and Ch 8 respectively. In this instance, we extended the scope of the assessment to include a review of whether IMB had sufficient financial, technological and human resources to comply with its obligations under s792A(d) and 821A(d).

Approach to assessment

- 8 ASIC's current strategic framework focuses on three key priorities or outcomes. These are:
- confident and informed investors and financial consumers;
 - fair and efficient financial markets; and
 - efficient registration and licensing.
- 9 The first two priorities are particularly important for licensed markets. In the context of IMB's market, it is important to note that it is a small domestic market, where comparatively little trading occurs when compared with the larger domestic markets. IMB's market is further differentiated from the other larger domestic markets by certain unique features such as having only one security traded (being ordinary shares in IMB) and trading being restricted to members of IMB. In these circumstances, for investors and financial consumers to be confident and informed and for IMB's market to be fair and efficient, our primary focus is on the reliability of the market's operation and the extent to which it meets the legitimate expectations of its members who are market users.
- 10 In the context of IMB's CS facility it is important to note that it is operated only for IMB shares. IMB's clearing and settlement function is of limited nature when compared to the larger and more systemically important domestic facilities operated by the ASX Group, as it only involves the debiting and crediting of IMB members' transaction accounts following a share trade. What further differentiates IMB's CS facility from the other larger domestic facilities is that it is not required to comply with the financial stability standards as determined by the Reserve Bank of Australia (RBA) under s827D of the Corporations Act. This is because IMB does not settle more than \$100 million annually.
- 11 For these reasons, our assessment of IMB's market and related CS facility focuses on a narrower sub-set of the key measures than we might otherwise use if the market was a large domestic market and if the CS facility was a larger, more systemically important facility. To determine whether IMB has complied with its obligations to have adequate arrangements and resources for its market and CS facility, we focused on:
- whether there have been any changes during the assessment period to the way IMB operates its market and supervises its CS facility;
 - the nature of any complaints made by market users to IMB or ASIC about IMB's market and/or CS facility;
 - the occurrence of any technological outages in IMB's market or concerns about IMB's technological resources;
 - any material changes to the resources (including human, financial and technological) dedicated to the operation of the market and supervision of the CS facility;

- the occurrences of any conflict of interest situations, and how IMB dealt with these; and
- whether there have been any market incidents during the assessment period.

Background

- 12 IMB is an authorised deposit-taking institution (ADI) under the *Banking Act 1959* and is regulated by the Australian Prudential Regulation Authority (APRA).
- 13 IMB was granted a market licence and a CS facility licence in July 2005. The licences are available for viewing at www.asic.gov.au/markets.
- 14 The only class of financial products that can be dealt with on IMB's market are ordinary shares in IMB. IMB's motivation for operating the market is to provide its members with a low-cost, simple and accessible platform for the trading of IMB shares with other IMB members. To become a member of IMB, an individual must have a deposit or loan account with IMB.
- 15 To trade on IMB's market, a member needs to have a transaction account and a share trading account. IMB shareholders and market users are predominantly retail investors.
- 16 The Share Trading team, which currently consists of 10 members from the Banking Services department, operates the market and CS facility. The team is led by the Market Manager, who is responsible for the day-to-day running of the market and CS facility. With the exception of one share trading officer, none of the other employees in the Share Trading team have exclusive responsibilities over the market, but are instead rotated in and out of the role.
- 17 At the time of the assessment, IMB had approximately 39.9 million shares on issue. The total volume traded on IMB's market during the assessment period was approximately 1.3 million shares, with a monthly average of 166,251 shares. The total value of shares transacted on IMB's market during the assessment period was approximately \$7.9 million, with a monthly average of \$662,314. The total number of share trades done on the market during the assessment period was 620.
- 18 IMB's CS facility is operated only for IMB shares. IMB's clearing and settlement function is limited to facilitating the debiting and crediting of IMB members' transaction accounts following a share transaction. Once a share transaction is completed, IMB's share trading system, known as FACTS, automatically updates the share registry and the Share Trading team generates the share certificates.

- 19 IMB is not required to comply with the financial stability standards, as determined by the RBA under s827D of the Corporations Act, because IMB does not settle more than \$100 million per year.
- 20 IMB is not a listed disclosing entity, as defined in the Corporations Act; however, a condition of IMB's market licence requires IMB to disclose price-sensitive information to ASIC and to make it available to the market. IMB provides this information on its website and at IMB's branches.
- 21 In addition to holding a market licence and a CS facility licence, IMB holds an Australian financial services (AFS) licence that permits it to carry on a financial services business in deposit and payment products, general insurance products, life risk insurance products and retirement savings account products. This assessment of IMB does not cover IMB's compliance with its AFS licence obligations.

Our methodology

Our assessment process

- 22 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. We therefore use the assessment process to:
- reach conclusions about the adequacy of the arrangements a market licensee (such as IMB) has in place in accordance with its obligations under s792A(c) and 821A(c) of the Corporations Act at the time of the assessment; and
 - identify issues, which in our view need, or may need, to be addressed to ensure ongoing compliance.

Materials we reviewed

- 23 In conducting our assessment we considered:
- IMB's annual regulatory report provided to ASIC, as required under s792F and 821E;
 - IMB's financial accounts for the half year ending 31 December 2011;
 - the previous assessment report on IMB, Report 249 *Market assessment report: IMB Limited* (REP 249);
 - information we received from and about IMB in the ordinary course of our dealing with IMB as a market and CS facility licensee;
 - publicly available information on IMB's website, including share prices, media releases, market announcements, and policies and procedures;

- information obtained from a media search on IMB; and
- IMB's response to our questionnaire.

Consultation

24 Our findings are set out in Section B of this report. IMB 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 IMB's clarifications.

B Our observations

Key points

We have considered the adequacy of IMB's arrangements and resources for the operation of its market and supervision of its CS facility, including arrangements for:

- handling conflicts between its commercial interests and its need to ensure that the market is fair, orderly and transparent and the CS facility's services are provided in a fair and effective way; and
- monitoring and enforcing compliance with the operating rules of the market and CS facility.

IMB did not make any substantial changes to its arrangements for operating the market and supervising its CS facility.

We do not have any recommendations to make about IMB's arrangements and resources for the operation of its market and supervision of its CS facility.

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

Supervisory arrangements

- 25 We conclude that during the assessment period IMB had:
- adequate arrangements for the operation of its market in accordance with its obligations under s792A(c) of the Corporations Act;
 - adequate arrangements for the supervision of its CS facility in accordance with its obligations under s821A(c) of the Corporations Act; and
 - sufficient resources to comply with its obligations under s792A(d) and 821A(d) of the Corporations Act.
- 26 This conclusion is based on our review of the measures that typically guide our assessment of IMB and like markets, being:
- the nature of any changes made to the policies and procedures relating to the operation of the market, supervision of the CS facility and enforcement of the market's operating rules;
 - the nature of any complaints made by market users about the market and/or CS facility;
 - the occurrence of any technological outages;
 - changes in human, financial and technological resources dedicated to the operation of the market and supervision of the CS facility;

- arrangements for managing conflicts of interest;
- the occurrence of any market incidents;
- the nature or level of trading activity conducted on the market; and
- arrangements for monitoring the market.

Nature or level of trading

- 27 During the assessment period, the nature or level of trading activity conducted on IMB's market was not subject to significant change in comparison to the previous assessment period.
- 28 While there were slightly higher levels of trading activity during the course of the assessment period, the number, value and volume of trades are not considered to be materially different to what is usually observed on IMB's market.

Policies and procedures

- 29 During the assessment period, the only change made to IMB's policies and procedures for the monitoring of its market was the increase of the significant price movement threshold to 15 cents from 5 cents. The basis for this change was to better reflect the relatively illiquid nature of trading on IMB's market. IMB is of the view that a 5 cent price movement has not been sufficiently indicative of unusual trading warranting further investigation. Based on what we have seen in the past with the illiquid nature of trading on IMB's market, we tend to agree with IMB that this increase in the price threshold is a more appropriate trigger for further monitoring.

Managing conflicts of interest

- 30 Given the nature of the operation of IMB's market we agree with IMB on what it has identified as possible areas of conflicts of interest flowing from operating a market in its own shares, these are:
- conflict between IMB's interest in reducing costs to its business generally and its duty as a market licensee to run a fair, orderly and transparent market;
 - the potential for staff and their associates to trade ahead of other participants on the basis of an informational advantage by virtue of their employment or association with IMB; and
 - conflict that may arise due to staff and director ownership of IMB shares, which could potentially adversely affect the policing of disclosure obligations imposed by the market licence.

31 There were no changes made to IMB's conflict management arrangements during the assessment period.

32 Based on the information we have received from IMB, we consider that IMB's arrangements for managing conflicts of interest are adequate.

Continuous disclosure

33 IMB's market only quotes one product, being IMB ordinary shares, so it has no official list. As IMB is not listed on an 'official list', as defined in the Corporations Act, it is not a 'listed disclosing entity', as defined in the Corporations Act.

34 Accordingly, IMB is not subject to statutory obligations to immediately disclose material developments that a reasonable investor would expect should be disclosed. However, it is a condition of IMB's market licence that all price-sensitive information must be lodged with ASIC and made available on its website and at IMB's branches in a timely manner.

35 IMB has in place policies and procedures for complying with this licence condition. To assess the extent to which IMB has complied with this licence condition, we analysed all the market announcements and general media releases published on IMB's website during the assessment period. We did not find any evidence to suggest that price-sensitive information was not disclosed to the market on a timely basis.

36 Furthermore, to test IMB's compliance with its continuous disclosure obligations, we conducted a search of various media sources to see if there was any price sensitive information about IMB that was not disclosed publicly. We did not find any information of this nature.

Complaints handling

37 We did not receive any complaints from market users about IMB's operation of its market and supervision of its CS facility during the assessment period.

38 IMB has a share market dispute resolution policy to deal with market-related disputes; a copy is available on its website.

39 During the assessment period, IMB received four complaints regarding:

- a human error in loading buy/sell order;
- timing in relation to IMB's share dividend announcements;
- timing in relation to payments of final dividends; and
- partial matching of shares.

40 IMB has indicated that all of the above issues were resolved. We have not identified any information that would suggest otherwise.

Trading system outages

41 There were no outages to the FACTS system during the assessment period.

Monitoring the market

42 IMB's main monitoring tool for the market is the Share Market Monitoring Log, which the Share Trading team uses to record actions taken or observations made about:

- suspicious activity;
- market manipulation by a participant or IMB;
- withdrawn orders;
- director trades;
- procedural errors and complains; and
- fluctuations in the share price of 15 cents or more.

43 During the assessment period, there were 27 observations of notable share price movements involving a movement in price of more than 15 cents. IMB made inquiries and confirmed that the share trades occurred as a result of matters such as:

- shareholders seeking quick access to funds or requiring the shares to be sold by a certain date, and thus placing an order at a price that would ensure a match;
- large disposals of shares due to sales by deceased estates; or
- less demand from purchasers of shares, leading to an adjustment in price.

44 On the basis of the information we received from IMB during the assessment process, we are satisfied that IMB's market monitoring tool is adequate.

Resources

45 We are satisfied that during the assessment period IMB had sufficient financial, technological and human resources to comply with its obligations under s792A(d) and 821A(d) of the Corporations Act.

46 IMB advised that during the assessment period there were no significant changes to the financial, technological or human resources used to operate the market and supervise the CS facility. The only notable changes to human resources are detailed further below.

Financial resources

- 47 The operation of the market and CS facility forms only a small fraction of IMB's general business activities and is low cost. IMB generates income from the market by levying an administration fee for each completed transaction. The expenses associated with the market and CS facility are generally limited to the employment costs for one dedicated full-time employee and stationery expenses associated with the production of trade records and share certificates. Any shortfall between income and expenses directly associated with its market and CS facility is not considered material by IMB and can be easily absorbed by profits generated from IMB's general banking and lending activities.
- 48 We reviewed the latest audited financial statements available from IMB at the time of our assessment and consider that IMB has sufficient revenues to cover the costs of operating its market and CS facility for the next 12-month period.

Technological resources

- 49 There were no changes made to FACTS during the assessment period. IMB advised that, given the nature of trading on the market, there are no planned changes to FACTS in the near future.

Human resources

- 50 The Share Trading team, responsible for operating the market and supervising the CS facility, is made up of 10 members. Only one share trading officer has exclusive responsibilities over the market, with the remaining nine being rotated in and out of the role. IMB advised ASIC that it manages any potential or actual conflicts in relation to the Share Trading team by not remunerating these staff according to a commission structure.
- 51 During the assessment period, two new employees were appointed to the Shares Trading team, replacing two staff members who had left.

Clearing and settlement

- 52 We are satisfied that during the assessment period, IMB had adequate arrangements and sufficient resources for the supervision of its CS facility in accordance with its obligations under s821A(c) and (d) of the Corporations Act.
- 53 The CS facility operated by IMB is limited to the debiting and crediting of a buyer's and seller's transaction account.

- 54 In May 2005, the RBA amended its financial stability standards for securities settlement facilities under s827D of the Corporations Act, so that the standards now only apply to facilities settling more than \$100 million a year. This was done so that small CS facilities such as IMB's, which are unlikely to affect the overall stability of the Australian financial system, are not subject to unnecessary regulation. Accordingly, IMB's CS facility does not need to comply with the RBA's financial stability standards.
- 55 IMB has indicated that during the assessment period there were no changes to the way it operates the CS facility. We are not aware of any changes to this facility and it continues to operate according to statutory requirements.

Conclusion

- 56 Based on this assessment, we do not have any recommendations to make about:
- IMB's arrangements for the operation of its market and for the supervision of its CS facility; and
 - IMB's resources for operating the market and CS facility.

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.
APRA	Australian Prudential Regulation Authority
ASIC	Australian Securities and Investments Commission
Australian market licence	Australian market licence under s795B of the Corporations Act that authorises a person to operate a financial market
Ch 7 (for example)	A chapter in the Corporations Act (in this example numbered 7)
Corporations Act	<i>Corporations Act 2001</i> , including regulations made for the purposes of that Act
CS facility	Clearing and settlement facility
FACTS	IMB's share trading system
IMB	IMB Ltd
market licensee	Holder of an Australian market licence
RBA	Reserve Bank of Australia
s794C (for example)	A section of the Corporations Act (in this example, numbered 794C), unless otherwise specified