



**ASIC**

Australian Securities & Investments Commission

**REPORT 239**

# **Market assessment report: Asia Pacific Exchange Limited**

**ACN 080 399 220**

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## **About this report**

This report summarises ASIC's seventh annual assessment of Asia Pacific Exchange Limited (APX) under s794C of the *Corporations Act 2001* (Cth) (Corporations Act).

This assessment covers the period 1 March 2010 to 31 December 2010 (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 APX

Australia Pacific Exchange was granted an Australian market licence on 11 August 2004. Since then, the following variations to the market licence have been granted:

- from 8 April 2009, to reflect the change to APX's current name, Asia Pacific Exchange Limited (APX); and
- from 29 June 2010, to reflect the inclusion of an unconditional bank guarantee as an additional source of funds for APX's Division 3 compensation arrangements and to remove certain obsolete licence conditions.

Report number	Report date
REP 199	June 2010
REP 166	August 2009
REP 154	April 2009
REP 116	January 2008
REP 90	February 2007
REP 61	November 2005

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# Key findings and recommendations

## Key findings

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

## Recommendations

- 2 We do not have any recommendations to make about APX's current supervisory arrangements and resources.

## A The assessment

### Key points

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

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

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

### Purpose and scope

- 3 Under s792A(c) a market licensee is required to have adequate arrangements for supervising the market, including arrangements for:
  - handling conflicts between the commercial interests of the licensee and the need for the licensee to ensure that the market is fair, orderly and transparent;
  - monitoring the conduct of participants on or in relation to the market; and
  - enforcing compliance with the market's operating rules.
- 4 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 In addition, we are permitted to extend the scope of our assessment to review how well a licensee complies with any or all of its obligations under Ch 7: s794C(1). In this instance, we extended the scope of the assessment to include a review of whether APX has sufficient financial, technological and human resources to comply with its obligations under s792A(d).
- 6 This report covers the period 1 March 2010 to 31 December 2010, although we have had regard to subsequent developments.

## Background

- 7 For the history of APX’s Australian market licence and the structure and nature of APX’s market, see *Market assessment report: Asia Pacific Exchange Limited* (REP 199), paragraphs 6–14.
- 8 A further variation to APX’s market licence was granted with effect from 29 June 2010. This variation formed part of changes made to APX’s Division 3 compensation arrangements, to include an unconditional bank guarantee as an additional source of compensation funds. Certain obsolete conditions were also deleted from APX’s market licence. Copies of APX’s market licence and variations to it are available on ASIC’s website at [www.asic.gov.au/markets](http://www.asic.gov.au/markets).
- 9 Throughout this assessment period there was no trading activity on APX’s market, as was the case during the preceding assessment period.
- 10 Until November 2010, Everbrite Corporation Limited (Everbrite) was the only entity approved to list (listee) on the APX market. Everbrite’s securities were suspended from quotation for an extended period, as a consequence of the company’s failure to comply with certain listing rule requirements. APX then removed Everbrite from its official list in November 2010 and for the remainder of the assessment period, there were no entities approved as APX listees.
- 11 During the assessment period, APX admitted four new market participants in the category of ‘sponsor’, whose role it is to advise listees throughout the listing process and for the first few years of listing. APX now has seven entities approved as sponsors. There is also one approved ‘broker’ participant with permission to trade on APX’s market.

## Our methodology

### Our assessment process

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

- identify issues, which in our view need, or may need, to be addressed to ensure ongoing compliance.

### **What we focused on for this assessment**

- 14 Our focus in this assessment was to review APX's progress with developing business plans for reactivating the market. This included examining APX's plans for its new market structure and participation framework, as well as how it will ensure the adequacy of its human, financial and technological resources when trading recommences on the market.
- 15 We also examined APX's handling of Everbrite's delisting.

### **What we considered**

- 16 In conducting our assessment we considered:
- material received under a notice served under s30 of the *Australian Securities and Investment Commission Act 2001* (Cth), including financial statements;
  - APX's annual regulatory report required under s792F of the Corporations Act;
  - information received from and about APX in the ordinary course of our dealings with APX;
  - policies and procedures for the conduct of APX in general and its supervisory responsibilities in particular;
  - publicly available information on APX's website; and
  - discussions held with APX personnel, including the APX Managing Director, Company Secretary and staff from APX's compliance and operations departments.

### **Consultation**

- 17 Our findings are set out in Section B of this report. APX 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 APX's clarifications.

## B Our observations

### Key points

We have considered the adequacy of APX's arrangements and resources for supervising its market, including arrangements for:

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

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

We do not have any recommendations to make about either APX's current supervisory arrangements or resources.

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

### Supervisory arrangements

- 18 We conclude that APX has:
- adequate arrangements for the supervision of its market in accordance with its obligations under s792A(c) of the Corporations Act; and
  - sufficient resources to operate its market properly and for the required supervisory arrangements to be provided under s792A(d) of the Corporations Act.
- 19 This conclusion is based on the following observations:
- the nature of the market as described in paragraphs 7–11;
  - APX's confirmation that the arrangements for supervising its market have not changed from the previous reporting period;
  - no serious market failures or disruptions have come to our attention; and
  - during the assessment period, no information came to our attention to suggest that the supervisory arrangements in place were not operating adequately.



20 A description of APX's supervisory framework is set out at paragraph 23 of *Market assessment report: Asia Pacific Limited* (REP 166).

### **Managing conflicts of interest**

21 As far as is practicable, APX effectively manages its conflicts of interest.

22 APX continues to operate out of a secure area within the office of its parent company, AIMS Financial Group (AIMS). APX is currently training two AIMS staff members as APX Action Officers, so that they will be able to perform operational functions in APX's Listing and Market Administration & Supervision divisions. Depending on the level of activity in APX's market when it recommences, the Action Officers may be initially be shared with AIMS; that is, they will work part-time for APX and part-time for AIMS. APX will review these arrangements in line with market activity levels and one or more of the part-time Action Officers may commence full-time with APX, when activity levels warrant it.

23 APX's Department Manager, in charge of APX's operational divisions, is also shared with AIMS. She is expected to become a full-time APX employee when the market becomes active and trading levels warrant it.

24 The employees that APX shares with AIMS are subject to stringent confidentiality and conflict management requirements for the work they do for the two entities. APX's electronic files are saved in a separate electronic directory to AIMS's. Access to APX's directory is not available to AIMS employees and shared employees may only access APX's directory when working within the secure APX area.

25 APX's employee code of conduct and conflict management plan specify requirements regarding employees' disclosures of material interests and the separation of supervisory decisions from commercial ones. These are described in paragraph 31 of REP 166.

26 As APX implements its business plans and reactivates its market, it will need to be mindful of any new conflicts of interest that may arise. We will monitor the ongoing adequacy of APX's conflict handling arrangements and review them in its next assessment of APX.

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

27 APX's arrangements for monitoring participants are described in paragraphs 28–32 of REP 166.

28 When it reactivates its market, APX plans to put in place a different market framework from that which applied when the market was last active. Consistent with this, APX will require new policies, procedures, processes and rules to monitor its market and conduct of market participants. APX is

working with us to prepare its rules and supervisory arrangements in line with the proposed new market structure. In next year's assessment we will review how APX has implemented the new arrangements.

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

29 APX did not make any changes during the assessment period to the way in which it enforces compliance with its operating rules.

30 APX had no cause to take any enforcement action against any of its participants during the assessment period.

31 In respect of listees, as set out in paragraph 10, in November 2010 APX ended quotation of the securities of Everbrite and removed that entity from the official list. Throughout the delisting process, APX followed the requirements of the APX Listees' Listing Standards, including affording Everbrite the right to request a hearing and/or make submissions to APX prior to being delisted.

## **Resources**

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

### **Financial resources**

33 APX's financial resources have been a focus of our last four assessments.

34 Since October 2008, AIMS has provided APX with a non-recourse financing facility to fund APX's ongoing activities. On 30 April 2010, the total available via the facility was increased to \$1.85 million, with these funds being available to APX up to and including 31 December 2011. APX will draw down funds via the facility as and when required. We have reviewed both the original executed loan agreement and the amending document increasing the loan facility.

35 As set out in APX's business plan and cash flow forecasts, APX will invest in new market infrastructure and resources as part of its preparations to reactivate the market during 2011.

36 We are satisfied that AIMS is committed to funding APX's preparations to reactivate its market and then the operation and supervision of the market.

### **Technological resources**

37 APX's technological resources were adequate over the assessment period.

38 During the assessment period, APX held discussions with potential providers of electronic trading and settlement services for the market. APX has structured its new operating rules around these arrangements being in place when active trading recommences. APX anticipates that agreements with service providers will be finalised during the first half of 2011. We will work with APX to ensure that the arrangements and rules framework relating to APX's new electronic trading and settlement are adequate.

### **Human resources**

39 As indicated in paragraphs 22–23 above, APX utilises some AIMS staff on a part-time basis. APX has indicated that when its market is reactivated, it will review its resourcing arrangements and it is expected that:

- the APX Department Manager will work on a full-time basis for APX; and
- one or both of the AIMS employees being trained as APX Action Officers will be also appointed as full-time APX employees.

40 APX's Assistant Department Manager is, and will remain, a full-time APX employee.

41 In our view, APX's human resources are sufficient for APX's current activities. In next year's assessment, we will review how APX adapts its human resourcing to meet market activity levels.

## **Conclusion**

42 There have been no significant changes in the way in which APX's market operates since our last assessment. Based on this year's assessment, we do not have any recommendations to make about APX's current supervisory arrangements and resources.

## Key terms

Term	Meaning in this document
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 <p>Note: This is a definition contained in s761A of the Corporations Act.</p>
AIMS	AIMS Financial Group
APX	Asia Pacific Exchange Limited
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
Everbrite	Everbrite Corporation Limited
market licensee	Holder of an Australian market licence
s794C (for example)	A section of the Corporations Act (in this example, numbered 794C), unless otherwise specified