Synergy Financial Markets Pty Ltd
ABN 80 150 565 781
AFSL No. 403863

Level 27, 25 Bligh Street
Sydney, NSW. 2000. Australia

8 August 2017

Ms Katie Ryder
Senior Lawyer, Market Integrity Group
Australian Securities and Investments Commission
Level 5, 100 Market Street
SYDNEY NSW 2000
By Email to: policy.submissions@asic.gov.au

Dear Ms Ryder

Synergy Financial Markets Pty Ltd – Submissions in Response to CP 291

Synergy Financial Markets Pty Ltd (**Synergy**) appreciates the opportunity to provide feedback on ASIC's proposals to make Client Money Reporting Rules 2017 under s981J of the *Corporations Act 2001*. Those proposals are set out in Consultation Paper 291 *Reporting rules: Derivative retail client money* (CP 291) (**Draft Rules**) and impose record-keeping, reconciliation and reporting requirements on Australian financial services (**AFS**) licensees that hold derivative retail client money that is 'reportable client money'.

Synergy considers that the intent of the record keeping, reconciliation and reporting requirements in the Draft Rules are necessary and appropriate in light of the introduction of the client money reforms to take effect in 2018. In this regard, Synergy considers that the Draft Rules:

1. Will improve the transparency of a Licensee's receipt and use of derivative retail client money;

2. Will not significantly impact our business or create overly burdensome compliance obligations, or impose significant additional costs.

3. Are an appropriate tool to assist ASIC regulate the over-the-counter (**OTC**) retail derivatives sector and assist with the identification of client money anomalies in appropriate cases; and

4. Will provide adequate protection for retail clients.

That being said there are specific issues in respect of the Draft Rules which Synergy would like to bring to ASIC's attention, and if possible, engage further with ASIC on.

These are:

1. The time "as at" which the daily and monthly reconciliation should occur (Draft Rules 2.1.1 and 2.2.2) should correlate with the New York close of trade, being 4.59.59pm New York time (**New York Close**), rather than 7pm as currently required under the Draft Rules.

2. The next business day requirement in which to perform accurate reconciliations under Draft Rule 2.2.1(3) should be extended to within 3 business days. Next business day reporting is too short a window to resolve anomalies in figures arising from factors outside the control of Licensee. A 3 business day window in which to undertake the daily reconciliation requirement would resolve this issue.

3. The $1,000,000 non-compliance civil penalty provisions are extreme and inconsistent with other similar ASIC-regulated reporting regimes.

We note that Synergy is also a member of the Australian CFD & FX Association Limited (ACN 608 241 274) (**Association**) and has reviewed the submissions prepared on behalf of the Association. To the extent that issues raised in submissions of the Association are not dealt with here, Synergy requests that ASIC treat those issues as having been raised in this letter as well.

7pm Reporting Time

Synergy submits that ASIC should not adopt 7pm as the time at which "a financial services licensee must perform an accurate reconciliation (refer to Draft Rule 2.2.1 and 2.2.2) (we assume "7pm" means 7pm Australian Eastern Time). Rather, it is submitted, a more appropriate time "as at" which the accurate reconciliation should occur should correlate with the New York close of trade, being 4.59.59pm New York time (**New York Close**) (this is usually around 7am Australian Eastern Standard Time). This is because:

1. OTC derivatives brokers, including Synergy are international businesses, with clients in many jurisdictions throughout the world. A significant portion of Synergy's business is generated from the Asian and European markets which are mostly open at 7pm (AEST) (the European markets getting into full swing at this time). It is during this period that performing a daily reconciliation would prove to be onerous.

2. The New York Close is the global standard time for international financial transactions and is the benchmark by which industry participants open and close their trading days, including balancing our books and calculating profit and loss and client liabilities.

3. In the FX market, the international community (including Australia) agreed, approximately 20 years ago, to define the trading day to finish at the New York Close as part of CLS (Continuous Linked Settlements).

4. Synergy's liquidity providers generate statements which show all open and closed trades of clients for the Trading Day beginning and ending at this time. Reconciling client money in accordance with the Draft Rules at this time would not be an overly difficult process.

Should ASIC insist on a 7pm Reporting time, rather than New York Close, Synergy anticipates that it will have to build new systems and effectively undertake duplicate reporting. One report which is already undertaken at New York Close, and another report for the purposes of the Draft Rules. This will increase, significantly, our compliance costs and efficiency.

Daily Reconciliation by 7pm the following business day

Draft Rule 2.2.1.(3) provides that *"the reconciliations required by [Draft Rule 2.2.1] must be completed by 7.00 pm on the business day following the business day to which the reconciliation relates"*.

In Synergy's submission, there are a number of issues with the chosen next business day time frame:

1. In most cases, this only allows a 24 hour window which is insufficient for investigating and rectifying any anomalies which may arise in information received pertaining to client money; and

2. Given any anomalies arising out of unresolved issues relating to client money (arising under 1) will need to be reported to ASIC in accordance with Draft Rule 3.1.1 – it will create an unnecessary compliance burden on us and other licensees; and

3. For ASIC, this will result in a substantially higher volume of reporting, but the information reported will be of lower quality and prove to be an unnecessary drain on ASIC's resources. That is, a greater increase in reporting will make triaging non-compliant issues far more difficult.

In order to resolve these issues, Synergy submits that the Draft Rule 2.2.1(3) be amended to read:

> *The reconciliations required by this Rule must be completed by New York Time* [defined in rules] *on the <u>third</u> business day following the business day to which the reconciliation relates.*

Penalty Regime

Synergy submits that the current penalty regime for non-compliance with the Draft Rules are:

1. Disproportionate to the seriousness of a breach of the Draft Rules. We note the following in support of this submission:

   a. ASIC should use the power given to it to set the maximum penalties for a breach of a rule as a means of communicating to the Court the perceived seriousness of the offence.

   b. Principles of fairness require that there be a degree of proportionality between the seriousness of the contravention and the quantum of the maximum penalty.[1]

   c. The penalty levels as drafted fail in achieving the above mentioned purposes. For example, Draft Rule 2.1.2(a) imposes a penalty of $1,000,000 on a financial services licensee that fails to comply with a request by any person for written records pertaining to Rule 2.1.1 within two business days. It is submitted that a $1,000,000 maximum penalty for a provision which could hypothetically be breached by a single day's delay is grossly disproportionate.

[1] Australian Law Reform Commission, *Securing Compliance: Civil and Administrative Penalties in Australian Federal Regulation,* DP 65) 2002), ALRC, Sydney, para 18.15.

d. Nearly every rule is capable of contravention in a technical, minor and accidental way, which is completely in appropriate for a $1,000,000 civil penalty. We have not been able to identify any corresponding technical compliance provisions in any other legislation that carry such extreme penalties for non-compliance. Whilst the *Market Integrity Rules* contain $1,000,000 penalties, these are reserved for intentional / dishonest and/or conflicted conduct (discussed further below)

2. Inconsistent with other similar ASIC regulated regimes, as well as other comparable provisions of the *Corporations Act*. In this regard, Synergy notes:

   a. The imposition of a $1,000,000 penalty for the failure to keep adequate records, by way of example, by Draft Rule 2.1.1 can be contrasted to the 1,000 penalty unit ($210,000) penalty for essentially the same conduct under Chapter 2 of the *ASIC Derivative Transaction Rules (Reporting)* 2013.

   b. Whilst ASIC have noted in CP 291 that "the proposed client money reporting rules (and associated penalties) are broadly consistent with the existing reconciliation and reporting requirements that apply to domestic exchange-traded derivatives under ASIC Market Integrity Rules (ASX 24 Market) 2010 ", this is not correct. The *ASIC Market Integrity Rules* for the ASX 24 Market do indeed create a similar reporting and compliance framework to the rules currently proposed for Retail Client Money. But the penalties that ASIC has chosen for breaches of the Client Money Reporting rules are out of scale with the penalties for similar breaches of the ASX 24 *Market Integrity Rules*.

      A. For example, both rules set out daily and monthly reconciliation requirements (Rule 2.3.2 and 2.3.3 in the *ASIC Market Integrity (ASX 24 Market) Rules 2010,* Rules 2.2.1 and 2.2.2 in the proposed *Client Money Reporting Rules*). Should we encounter issues in the reconciliation (which is not unlikely - see above), we must then report this to ASIC. Failure to do so carries a $100,000 penalty under the ASX 24 Market Integrity Rules and a $1,000,000 penalty in the Client Money Reporting Rules. We do not see any justification for this discrepancy and would therefore suggest that ASIC revises the penalties which it proposes to implement under the proposed rules.

      B. Whilst the *ASIC Market Integrity Rules (ASX 24 Market) 2010 Market Integrity Rules* contain $1,000,000 penalties, these are reserved for intentional / dishonest, misleading and/or conflicted conduct. For example (emphasis added):

         - Under rule 3.1.2.(1)(a) a market participant must not offer to purchase or sell or deal in any contract as Principal with <u>the intent</u>, or if it has the effect, of creating a <u>false or misleading appearance</u> of active trading in any Contract or with respect to the market for, or the price of, any Contract.

         - Under rule 3.1.2.(1)(b) a market participant must not offer to purchase or sell or deal in any contract on account of any other person with: <u>the intent</u>, or awareness that the person placing the order <u>has the intent</u>, or in circumstances where the market participant ought reasonably to have suspected that the person placing the order has the <u>intent to create a false or misleading appearance</u> of active trading in any Contract or with respect to the market for, or the price of, any Contract.

- Under Rule 3.1.3(1) a market participant must not enter orders without the intent to trade

3. Given the quantum involved, ASIC may face difficulties in enforcing the penalties through "civil penalty proceedings" in light of the fact that:

    a. the standard of proof required of ASIC is heightened by the penalty level. Courts applying the *Briginshaw* standard may require more convincing and conclusive evidence in circumstances where a declaration of contravention may result in severe consequences against the contravening party.

    b. The privilege against self incrimination or penalty privilege may apply. We note that *Treasury Law Amendment (2016 Measures No. 1) Bill 2016* does not abrogate the privilege with respect to the client money rules. We respectfully submit that Rule 3.1.1 is therefore subject to the application of the privilege, with results mirroring the outcome in *Pyneboard Pty Ltd v Trade Practices Commission* (1983) 152 CLR 528.

    c. They may be punitive rather than deterrent in nature and therefor attract far higher standards of proof.

In order to ameliorate against these issues, Synergy submits that the penalty levels should be set at more reasonable amounts, which accord more closely with the seriousness of the conduct proscribed. This will allow ASIC to confidently bring cases against a larger number of contravening parties without a great deal of resistance from the Courts, or indeed from the contravening parties themselves.

This is not to say that the penalty levels should be set so low as to be insignificant. The quantum proposed: $210,000, is sufficient enough to act as a deterrent, will not cause unnecessary obstacles in its administration, and furthermore, is still a significant enough penalty in, especially in circumstances of repeated contravention.

Such a penalty (1,000 penalty units):

a) Is more proportional to the rule that the penalty is attempting to enforce, and

b) Is consistent with ASIC-regulated rule regimes such as the Derivative Transaction Rules or the ASX 24 Market *Market Integrity Rules*, and

c) Will be easier for ASIC to administer, thereby better serving the purpose of the rules than a $1,000,000 penalty.

Synergy thanks ASIC for the opportunity to make these submissions. We would appreciate the opportunity to engage further with ASIC on the terms of the Draft Rules in the near future.

Kind regards,

Christian Dove
Managing Director
Synergy Financial Markets Pty Ltd