



ASIC

Australian Securities & Investments Commission

REPORT 546

Response to submissions on CP 291 Reporting rules: Derivative retail client money

October 2017

About this report

This report highlights the key issues that arose out of the submissions received on Consultation Paper 291 *Reporting rules: Derivative retail client money* (CP 291) and details our responses 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 Information Sheet 226 *Complying with the ASIC Client Money Reporting Rules 2017* (INFO 226).

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A Overview/Consultation process

- 1 In [Consultation Paper 291](#) *Reporting rules: Derivative retail client money* (CP 291), we consulted on proposals to make the ASIC Client Money Reporting Rules 2017 (client money reporting rules). The client money reporting rules impose requirements on Australian financial services licensees to ensure greater transparency in the use of derivative retail client money and enhance ASIC's surveillance of the retail derivatives sector.
- 2 The client money reporting rules require a licensee that holds 'reportable client money' to:
 - (a) keep accurate records of the amount of reportable client money it receives on both an individual client basis and a total basis;
 - (b) perform daily and monthly reconciliations of the amount of reportable client money it has recorded in its records against the amount actually held in the client money account;
 - (c) notify ASIC if it fails to perform a reconciliation in accordance with the client money reporting rules;
 - (d) prepare and give to ASIC an annual directors' declaration and an external auditor's report on its compliance with the client money reporting rules; and
 - (e) establish, implement and maintain policies and procedures designed to ensure compliance with the client money reporting rules.
- 3 This report highlights the key issues that arose out of the submissions received on CP 291 and our responses to those issues.
- 4 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 every question from CP 291. We have limited this report to the key issues.
- 5 We received four confidential and eight non-confidential responses to CP 291. We are grateful to respondents for taking the time to send us their comments.
- 6 For a list of the non-confidential respondents to CP 291, see the appendix. Copies of these submissions are currently on the ASIC website under [CP 291](#).

Responses to consultation

- 7 The main issues raised by respondents related to those proposals which require licensees to:
- (a) comply with requests for records from clients and ASIC within two business days;
 - (b) perform reconciliations of the amount of reportable client money held 'as at' 7 pm Sydney time;
 - (c) perform daily reconciliations within one business day of the day to which the reconciliation relates;
 - (d) perform daily and monthly reconciliations of both the aggregate and individual client money balances of reportable client money;
 - (e) retain records of reconciliations performed under the client money reporting rules;
 - (f) give ASIC a written report if a reconciliation performed under the client money reporting rules identifies a surplus or deficit in the client money account;
 - (g) prepare and give ASIC an external auditor's report and directors' declaration within three months of the end of each financial year ending after 1 July 2018;
 - (h) be liable for maximum penalties of \$1,000,000 for breaches of the client money reporting rules; and
 - (i) comply with the client money reporting rules in relation to overseas exchange traded futures contracts.

B Record-keeping and reconciliation submissions

Key points

This section outlines the feedback received on our proposed record-keeping and reconciliation requirements in the client money reporting rules.

Specifically, the feedback relates to our proposals to require licensees to:

- comply with requests for records from clients and ASIC within two business days;
- perform reconciliations of the amount of reportable client money held 'as at' 7 pm Sydney time;
- perform daily reconciliations within one business day of the day to which the reconciliation relates;
- perform daily and monthly reconciliations of both the aggregate and individual client money balances of reportable client money; and
- retain records of reconciliations performed under the client money reporting rules.

Complying with requests for records by ASIC or clients

- 8 We proposed that a licensee should be required to comply within two business days with written requests from ASIC or its clients for certain records which are required to be kept under the client money reporting rules.

Stakeholder feedback

- 9 We received three submissions which provided that it may be difficult or impossible to comply with every request within two business days, particularly in unforeseen or extenuating circumstances. Two of these submissions recommended that the period be extended to five business days. The other submission recommended that the period be extended to 30 days for consistency with the timeframe under the *Privacy Act 1988* to comply with requests for access to a person's own personal information.

ASIC's response

To address this feedback, we have amended the requirements in rule 2.1.2 of the client money reporting rules to require licensees to comply with requests for records within five business days (or such longer period as agreed between the licensee and the requesting party).

We accept that complying with requests for records within two business days may be onerous and, in certain circumstances,

impossible. As such, we have amended rule 2.1.2 to extend the timeframe within which the requests must be complied with to five days and to also give licensees the flexibility to negotiate a longer timeframe with the agreement of the requesting party.

We note that this is a shorter timeframe than that required for requests for a person's own personal information under the *Privacy Act 1988*. However, we consider that it is less onerous to provide a client with a specific record (which the licensee is required to keep under the client money reporting rules) than it is to comply with requests for personal information. As such, we consider five business days should be sufficient time to comply with such requests.

Reconciliations of money held 'as at' a particular time

- 10 We proposed that licensees should be required to perform daily and monthly reconciliations of the amount of reportable client money held 'as at' 7 pm Sydney time on the relevant business day.

Stakeholder feedback

- 11 We received a significant number of submissions which provided that it would be difficult for various licensees to perform reconciliations of the money held as at 7 pm Sydney time as their close of trading is 5 pm New York Time. It was also submitted that 5 pm New York Time is commonly used for purposes such as performing balance snapshots and finance charge calculations. Consequently, it was submitted that entities should instead be required to perform reconciliations of reportable client money held as at 5 pm New York time.

ASIC's response

We accept that a licensee's close of trading time will depend on the particular circumstances of that business. Consequently, we have amended the daily and monthly reconciliation requirements in subrule 2.2.1(1) and 2.2.2(1) to require licensees to reconcile the amount of reportable client money held as at a time determined by the licensee (provided it is the same time each business day).

This amendment will give a licensee the flexibility to ensure that the reconciliation is performed on the amount of reportable client money held at its own nominated reconciliation time. In addition, the usefulness and integrity of the reconciliation will not be affected by the change as the reconciliation will be required to be performed on amounts held as at the same time each day.

Performing daily reconciliations by a particular time

- 12 We proposed that licensees should be required under the client money reporting rules to perform daily reconciliations by 7 pm on the business day following the day to which the reconciliation relates (i.e. within one business day).

Stakeholder feedback

- 13 We received five submissions which provided that licensees generally require additional time to identify anomalies in their accounts arising from factors outside their control (for example, bank book errors or unidentified client deposits). It was submitted that, without an extension to the timeframe within which the reconciliations must be performed, many licensees would be required to submit reports to ASIC on an almost daily basis because of these anomalies. The submissions recommended extending the period to 72 hours to give entities sufficient time to consider these anomalies and consequently perform a more accurate reconciliation.

ASIC's response

We accept that requiring licensees to perform daily reconciliations within 24 hours may result in ASIC receiving a high volume of reports which contain minor discrepancies. To address this feedback, we have amended the requirement in subrule 2.2.1(3) to require the daily reconciliations to be completed within three business days of the end of the business day to which the reconciliation relates.

Information to be included in the written records of reconciliations

- 14 We proposed that a licensee should be required to perform reconciliations on both the aggregate balance and individual client balances of the reportable client money it holds. In addition, a licensee is required to retain a written record of a reconciliation it performs under the client money reporting rules for a period of at least seven years from the date the record is made.

Stakeholder feedback

- 15 We received submissions suggesting it was not clear what information should be included in the records of these reconciliations. As such, a number of submissions requested that ASIC should either prescribe the form of the reconciliation records in the client money reporting rules or provide guidance on the information that should be included in those records.

- 16 One submission also requested clarification on whether a total reconciliation that is supported by system records which identify individual client balances would meet the requirements to perform both aggregate and individual client balance reconciliations under the client money reporting rules.

ASIC's response

We have addressed these submissions by providing additional guidance on complying with the client money reporting rules in INFO 226. INFO 226 provides an example of the information ASIC expects to be included in a licensee's reconciliation records. In addition, INFO 226 clarifies that a licensee may comply with its obligations under the client money reporting rules by performing a total reconciliation which is supported by the individual client balances comprising the licensee's 'reportable client money'.

C Reporting submissions

Key points

This section outlines the feedback received on our proposed reporting requirements in the client money reporting rules.

Specifically, the feedback relates to our proposals to require licensees to:

- give ASIC a written report if a reconciliation performed under the client money reporting rules identifies a surplus or deficit in the client money account; and
- prepare and give ASIC an external auditor's report and directors' declaration within three months of the end of each financial year ending after 1 July 2018.

Reporting a discrepancy to ASIC

- 17 We proposed that a licensee should be required to give ASIC a written report if a reconciliation performed under the client money reporting rules identifies a difference (i.e. either a surplus or a deficit) between the amount held in a client money account and the amount recorded in the licensee's records maintained under the client money reporting rules.

Stakeholder feedback

- 18 We received feedback which provided that if this requirement was not changed, licensees would be required to report differences to ASIC almost every day. One submission suggested that ASIC should only require client money deficits to be reported. It was also submitted that ASIC should consider amending the reporting requirement to only require 'significant' or 'material' differences identified by the reconciliation to be reported to ASIC.

ASIC's response

We consider it is important for both surpluses and deficits in the client money account to be reported, as they can both be indicators that a licensee is having issues complying with the client money regulatory regime. Surpluses of client money can reduce the transparency of a licensee's use of client money and may even mask a licensee using client money for impermissible purposes. In addition, we consider it is not appropriate to impose a significance threshold on the reporting requirement as multiple breaches which a licensee may consider to be 'insignificant' may similarly raise compliance concerns.

Our proposal to extend the timeframe within which the daily reconciliations should be performed to three business days should give licensees sufficient time to reconcile reportable client money balances (including identifying the source of any unidentified deposits and working through any other anomalies) and should consequently reduce the frequency with which licensees will be required to report discrepancies to ASIC.

Annual auditor's report—Timing and details

- 19 We proposed that a licensee should be required to prepare and give ASIC, within three months of the end of the licensee's financial year, an external auditor's report that states whether the licensee has systems that have enabled it to comply with the client money reporting rules.

Stakeholder feedback

- 20 We received submissions requesting that the time by which the auditor's report is required to be lodged should align with a licensee's existing annual auditor report requirements. It was submitted that it would be more convenient for licensees and auditors if the timeframe aligned with the lodgement period that applies to many licensees for their FS71 reports (i.e. within four months of the end of the licensee's financial year), rather than requiring all licensees to lodge the auditor's report within three months of their end of financial year.
- 21 In addition, we received submissions that it would help licensees and auditors if the client money reporting rules prescribed the form of the auditor's report.
- 22 One submission specifically requested guidance on whether the auditor's opinion is to be based on limited assurance or reasonable assurance.

ASIC's response

We have addressed these submissions by extending the time by which a licensee is required to lodge an auditor's report with ASIC from three months to four months after the end of its financial year.

We have also addressed the feedback by amending the client money reporting rules to prescribe the form of the auditor's report which is required to be lodged under paragraph 3.1.2(1)(b). The form clarifies the level of assurance the auditor's opinion is to be based on, namely reasonable assurance.

Annual auditor's report and directors' declaration—Commencement

- 23 We proposed that the requirement to prepare an external auditor's report and directors' declaration should only apply to financial years ending after 1 July 2018. This means licensees are not required to prepare a report or declaration for the financial year ending 30 June 2018. However, a licensee will be required to prepare a report and declaration for the previous six months if its financial year ends in December 2018.

Stakeholder feedback

- 24 We received feedback that the commencement of this requirement should be postponed as licensees with financial years ending in December 2018 may have difficulties ensuring they are able to comply within such a timeframe.

ASIC's response

We consider that no amendment to the commencement of the requirements in rule 3.1.2 is necessary. Licensees should be able to ensure their compliance with these requirements for financial years ending after 1 July 2018.

D Application of the rules to licensees subject to market integrity rules

Key points

This section outlines the feedback received in relation to the proposed application of the client money reporting rules to any licensee (including ASX 24 participants) which holds reportable client money.

Reconciliations of client money relating to futures contracts

- 25 We proposed that the rules should apply to any licensee which holds reportable client money. The proposed definition of reportable client money was money that:
- (a) is ‘derivative retail client money’ within the meaning of the Corporations Act; and
 - (b) is or relates to a derivative other than a derivative entered into on a market that is licensed under s795B(1) of the Corporations Act and no exemption under s791C or s798M covers the market.

Stakeholder feedback

- 26 One submission recommended that the client money reporting rules should not apply to money received by an ASX 24 participant, regardless of whether the money relates to domestic or foreign futures contracts. The basis of this submission was that Part 2.3 of the ASIC Market Integrity Rules (ASX 24 Market) 2010 (ASIC Market Integrity Rules (ASX 24)) already imposes reconciliation requirements in relation to overseas exchange traded futures contracts. Accordingly, it was submitted that it was inappropriate to require ASX 24 participants to perform two separate reconciliations of this client money.

ASIC’s response

We agree that there is limited regulatory benefit in requiring client money received in relation to overseas exchange traded futures contracts to be the subject of two different reconciliations. We have addressed this submission by exempting participants in the ASX 24 market or the FEX market from performing reconciliations of reportable client money which is already the subject of reconciliations performed in compliance with the ASIC Market Integrity Rules (ASX 24), the ASIC Market Integrity Rules (FEX Market) 2013 or the ASIC Market Integrity Rules (Futures Markets) 2017. In addition, these licensees do not need to comply with the client money reporting rules if the only reportable client money received by the licensee is reconciled in compliance with these market integrity rules.

E Penalties

Key points

This section outlines the feedback received in relation to ASIC's proposed maximum penalties for breaches of the client money reporting rules.

Excessive penalties

- 27 We proposed a maximum penalty of \$1,000,000 for breaches of any of the requirements in the client money reporting rules.

Stakeholder feedback

- 28 The submissions we received expressed concern that the maximum penalties for contravening the client money reporting rules were too harsh and excessive. Respondents considered that the penalties for breaching certain client money reporting rules were inconsistent with, and disproportionate to, penalties imposed for breaches of other similar requirements imposed by ASIC.

ASIC's response

We consider that all client money reporting rules should remain subject to a maximum penalty amount of \$1,000,000. We have been empowered by the Government's client money reforms to impose this maximum penalty for breaches of the client money reporting rules.

We do not consider that a maximum penalty amount of \$1,000,000 will result in excessive penalties. It is important to note that, in the case of minor or insignificant breaches of the client money reporting rules, it is very unlikely that the maximum penalty will be imposed. We consider that a maximum penalty amount of \$1,000,000 is an appropriate deterrent to breaching requirements in the client money reporting rules, which we consider to be very important for protecting retail investors.

Appendix: List of non-confidential respondents

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- Australian CFD & FX Association
 - Australian CFD & FX Forum
 - Gleneagle Securities (Aust) Pty Ltd
 - GO Markets Pty Ltd
 - International Capital Markets Pty Ltd
 - KPMG
 - Saxo Capital Markets (Australia) Pty Ltd
 - Synergy Financial Markets Pty Ltd
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