



**ASIC**  
Australian Securities &  
Investments Commission

# Managing conflicts of interest in wholesale financial markets

**Report 742 | October 2022**

## **About this report**

This report:

- › summarises the findings of our thematic review of arrangements used by participants in wholesale financial markets for managing conflicts of interest
- › highlights our observations of better and poorer practices when managing conflicts of interest.

# Contents

Executive summary	2
ASIC's market supervision focus	4
Approach to conflicts management	5
Operation of the control room function	6
Effectiveness of policies and procedures	7
Robustness of information barriers	8
Effectiveness of staff training and awareness	9
Approach to governance and supervision	10
Appendix 1: Our review methodology	11
Appendix 2: Related information	12

## About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents: consultation papers, regulatory guides, information sheets and reports.

## 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. Examples in this report are purely for illustration; they are not exhaustive and are not intended to impose or imply particular rules or requirements.

# Executive summary

Following a thematic 'deep dive' review of five large Australian financial services (AFS) licensees (licensees) from 2019–22 (inclusive), we identified what we consider to be better and poorer practices when managing conflicts of interest in wholesale financial markets.

## Important role of wholesale markets

Australian businesses and governments use debt capital markets to fund operations and fixed income, currencies and commodities (FICC) markets to manage risk. These wholesale financial markets (referred to as 'wholesale markets') underpin growth in Australia's real economy.

We have increased our focus on the conduct of participants in wholesale markets due to the significant conduct risks that may arise in these markets, such as the misuse of confidential information, which can harm:

- › the integrity of and confidence in wholesale markets
- › Australian investors, such as superannuation fund members, and
- › consumers, such as home borrowers.

'Adequate arrangements to identify and effectively manage conflicts are crucial to prevent poor client outcomes and to maintain confidence in market integrity.'

**Danielle Press** | ASIC Commissioner

## Our key findings

We reviewed the practices relating to conflicts management of participants that operate in wholesale markets. We identified better and poorer practices in six key areas. These are not attributable to each participant reviewed: see Appendix 1 for our review methodology.

All participants in wholesale markets should consider whether these better and poorer practices apply to their businesses. This report complements ASIC's existing regulatory guidance on conflicts management arrangements set out in Appendix 2. We note that the better practices may exceed the minimum standards required by law.

- › **Approach to conflicts management: Poorer practices** included approaches that were reactive to incidents and regulatory inquiries, where controls were ad hoc and not mapped to specific risks. **Better practices** embedded a proactive approach for identifying, assessing and managing specific conflicts arising within each business, and across the group.
- › **Operation of the control room function: Poorer practices** included poorly resourced control rooms that were reliant on manual processes, where staff spent more time on data entry and record-keeping than assessing and responding to commercial and transactional conflicts. **Better practices** included proactive monitoring and challenging of front-office business activities by control room staff.
- › **Effectiveness of policies and procedures: Poorer practices** included broadly drafted policies and procedures, which led to confusion when applied to specific business activities and mismanagement of conflicts. **Better practices** provided sufficient detail for staff to

understand how to identify and appropriately manage conflicts that may arise in ordinary business and employee behaviours.

- › **Robustness of information barriers: Poorer practices** failed to appropriately restrict access to confidential information. **Better practices** designed and implemented robust information barriers which were continuously aligned to current business models and activities.
- › **Effectiveness of staff training and awareness: Poorer practices** included low levels of awareness of conflicts likely to arise across both public- and private-side businesses. Training was generic and not sufficiently tailored to the specific needs of the business. **Better practices** conducted learning needs assessments and bespoke training on specific business activities using practical scenarios.
- › **Approach to governance and supervision: Poorer practices** included a lack of governance committees that regularly convened to consider conflicts and immature control functions that lacked resourcing, competency and clear roles and responsibilities in relation to conflicts management. **Better practices** had clear channels to escalate conflicts to committees, with clear ownership and accountability in their terms of reference.

# ASIC's market supervision focus

We have been expanding our oversight of wholesale markets to detect potential misconduct, drive behavioural change, and raise standards.

## Our work

Wholesale markets are systemically important to the Australian economy. Through our work we have found significant conduct risks arising in these markets due to conflicts of interests. This is consistent with findings from other regulators globally.

### Bank bill swap rate (BBSW) case study

BBSW is a key credit-based benchmark used to measure the rates at which Australian banks can borrow funds in wholesale markets. Much of the banks' wholesale debt and deposits are linked to BBSW either directly or as part of their interest rate hedging practices. This means that movements in BBSW can influence lending rates on household and business loans. It is also widely referenced in Australian financial contracts including the derivatives market, where approximately \$20 trillion in notional value is referenced.

Major banks were found to have attempted to engage in unconscionable conduct in relation to the setting of BBSW in a way that may have benefited their own interests over the interests of counterparties and clients. This misconduct may have undermined market integrity and confidence in the BBSW rate set. Fundamental to mitigating this risk is establishing and embedding effective controls to manage conflicts.

## Legislation

Participants who are licensees are required under section 912A(1)(aa) of the *Corporations Act 2001* to have in place adequate arrangements for managing conflicts of interest. This includes identifying conflicts of interest (actual, apparent or potential) that must be avoided, such as in cases where disclosing them and/or imposing internal controls will be inadequate.

The misuse of inside information is also an offence under section 1043A.

It is important to note that a conflict of interest can arise due to the receipt of confidential information, and not just what may be considered to be material non-public information ('inside information'). For example, confidential client information obtained in the ordinary course of business could be misused in a way that is detrimental to another client, a counterparty or the integrity of the market generally.

# Approach to conflicts management

Participants should have a strategic approach for identifying and assessing specific conflicts arising within and across business units.

## Our focus

The approach to conflicts management is fundamental in directing how a participant seeks to manage, disclose or avoid conflicts of interest.

## Our observations

### Poorer practice observations

- › The risk appetite for 'conflicts of interest' risk was not articulated in sufficient detail so that it was difficult for the participant to assess whether certain activities were within their risk tolerance.
- › 'Conflicts of interest' was only captured under general risk categories in the risk taxonomy so that associated conduct risks within business units were not identified. Management of these risks were ad hoc and reactive.
- › Senior management were unable to explain how conflicts management applied to their day-to-day businesses or the specific controls that have been embedded.
- › Reporting of commercial and transactional conflicts to the control room was heavily dependent on the judgement of front office staff, with the basis of such decisions to report not documented or independently reviewed.



### Better practice observations

- › Regularly benchmarked arrangements against any ASIC and industry guidance—for example, Australian Financial Markets Association (AFMA) guidelines and Financial Markets Standards Board (FMSB) standards.
- › Comprehensive risk assessments to identify likely conflict scenarios and associated conduct risks within and across business units. Controls were then mapped to the identified conflicts to assess whether the associated risks were being effectively managed and to identify any residual risks. This was documented in a 'conflicts catalogue' and regularly updated subject to an ongoing quality assurance process.
- › Conflicts management frameworks that set out clearly the key elements of the participant's approach to conflicts management, including policies and procedures, information barriers, training, monitoring and surveillance and consequence management.
- › Staff promoted effective disclosure by walking through complex order execution strategies with their clients and providing all relevant information including the participant's role and relationship (e.g. where a dealer trades as principal and does not act as agent).
- › Declined commercial transactions to avoid a potential conflict of interest where competing interests of one client may be favoured over another client.

# Operation of the control room function

Control rooms should be equipped and resourced to carry out their duties in an accurate, timely and comprehensive manner.

## Our focus

The control room plays an important role in maintaining the integrity of information barriers and managing conflicts of interest, particularly as the financial institution takes on multiple roles and activities through its private-side and public-side businesses servicing clients and counterparties with competing interests.

## Our observations

### Poorer practice observations

- › Heavy reliance on manual data entries into the control room workflow systems, which was time-consuming and error-prone.
- › Lack of a quality assurance review process for information recorded in control room registers (e.g. private-side 'watch lists' and public-side 'restricted lists') so inaccuracies were not detected, compromising conflicts checks and monitoring.
- › Resourcing of control rooms failed to keep pace with key changes in risk profiles and business models across the group.
- › Disproportionate high turnover in control room staff, with roles remaining vacant for an extended period. These resourcing issues impacted continuity and operational effectiveness.

- › Lack of investment in technology systems and reliance on legacy systems to support the control room, limiting the ability to automate repetitive processes.
- › Irregular communication with the monitoring and surveillance team so that conflict issues identified from surveillance systems were not being promptly addressed.



### Better practice observations

- › Regular lookback reviews to assess the timeliness and accuracy of transactional information recorded on business systems and reported to the control room.
- › Regular monitoring of deal pipelines to ensure that the control room was notified of reportable deals in a timely manner.
- › Ongoing two-way engagement with business teams regarding conflict issues including challenging materiality assessments and improving practices.
- › Control room staff had dedicated coverage over different aspects of conflicts management, such as conflicts clearance and monitoring, which allowed staff to build specialist skills in their coverage areas.
- › Data in control room registers used in trading and electronic communication surveillance to detect misuse of confidential information or other potential misconduct.

# Effectiveness of policies and procedures

Policies and procedures should be clear and provide sufficient detail for staff to understand how to identify and appropriately manage conflicts.

## Our focus

Documented policies and procedures equip staff to better manage conflicts of interest within and across business units.

## Our observations

### Poorer practice observations

- › Broad exemptions for a range of transactions from the conflict clearance process gave front office staff wide discretion so that reportable business activities were not being reported.
- › Expedited conflicts clearance process for certain transactions that was not well defined, where formal reporting channels were minimised and greater pressure was placed on the control room to turn around the clearance requests quickly.
- › Key terms in the conflicts of interest policies were inconsistent and not sufficiently detailed so that there was uncertainty in how conflicts should be managed across the participant's wholesale markets businesses.
- › Policies and procedures for managing conflicts of interest were not stored in a centralised library, so staff were unsure where to source the relevant documents.



### Better practice observations

- › Conflicts of interest policy made clear reference to regulatory obligations, delineation of roles and responsibilities (e.g. business teams 'owning' the risk) and links to specific team policies and procedures.
- › Clear guidance setting out what types of capital markets transactions were considered 'reportable' transactions to the control room so that it would be recorded in a control room register (e.g. transactional conflicts register).
- › Clear guidance setting out circumstances when a 'reportable' transaction should be reported—for example, reporting a transaction not just prior to signing a mandate letter but at the time when a mandate (verbal or written) is likely to materialise.
- › Additional guidance material used to embed policies and procedures into business practices, providing concise information and ease of reference for key processes—for example, having detailed steps for transactional conflicts clearance and materiality assessments.
- › Mandatory requirement in deal checklist that a supporting rationale be documented if a decision is made that a transaction is not a 'reportable transaction'.

# Robustness of information barriers

Participants should ensure that information barriers are robust to manage conflicts and prevent misuse of confidential information.

## Our focus

Information barriers are important arrangements for enforcing restrictions on the use and disclosure of confidential information.

## Our observations

### Poorer practice observations

- › Information barriers and access restrictions did not appropriately manage conflicts arising from new research and syndicate functions co-located with public-side businesses.
- › Sales and trading teams were co-located side by side in the same seating rows so that private conversations could be overheard or computer screens seen.
- › Instances where public-side staff were able to use their ID cards to gain access to private-side areas.
- › Lack of electronic user access reviews to detect unauthorised access to databases storing confidential information, including changes in roles and business activities.



### Better practice observations

- › Physical and electronic controls established, monitored and regularly reviewed to keep pace with changes to the business risk profile and prevent inappropriate sharing of, or unauthorised access to, private-side information.
- › Additional restrictions in place (e.g. 'special purpose information barriers') to manage information flows arising from particularly complex or highly sensitive transactions.
- › Clear wall-crossing processes, with approvers limited to senior staff with oversight responsibilities.
- › Separate reporting lines and remuneration metrics for the public-side and the private-side businesses.
- › Physical segregation between sales and trading staff was subject to periodic review to ensure arrangements remained robust with any proposed changes to floorplans requiring approval from second-line compliance.
- › Co-location of first-line business assurance and second-line compliance with front office staff to provide additional desk supervision.
- › Second-line surveillance and control room teams were physically segregated from all public- and private-side staff, operating from a secure room. The teams were also electronically segregated, with any files stored in shared drives only accessible to that respective team.

# Effectiveness of staff training and awareness

Participants should provide ongoing training and seek to raise staff awareness of their responsibilities in managing conflicts of interest.

## Our focus

Raising staff awareness helps embed conflicts management arrangements in business practices and employee behaviours.

## Our observations

### Poorer practice observations

- › Generic training on conflicts management provided to all staff with no consideration of the specific needs of each business unit.
- › Training did not seek to emphasise the importance of conflicts management to staff so that the potential harm of unmanaged conflicts to their clients, counterparties or the market generally was not well understood.
- › Repeated instances of front office staff failing to report and reporting transactions late to the control room suggested a low level of staff awareness and failure to appropriately prioritise conflicts management in their day-to-day business activities.



### Better practice observations

- › Detailed case studies were a substantive part of the training material. These case studies illustrated in detail how conflicts can arise. They were tailored to staff business activities in order to provide staff with practical knowledge on how to identify, escalate and appropriately manage conflicts likely to arise in their day-to-day activities.
- › Business teams provided specific input on key learning needs or staff knowledge gaps to assist with the development of conflicts-related training material.
- › Systemic issues or emerging risks detected from monitoring activities helped inform particular focus areas for training, the content of policies and procedures, and the design of the risk and control framework.
- › Staff demonstrated awareness of their role in conflicts management by proactively communicating to the control room about changes during the lifecycle of the transaction (e.g. size, timing) and the type of information being received.
- › Business workflow system prompted staff to consider whether there were potential conflict issues or inside information each time a new deal was entered and reminded them to log the deal to the transactional conflicts register.
- › Senior management regularly communicated the importance of managing conduct risks including conflicts, setting 'the tone from the top' to raise staff awareness of their responsibilities.

# Approach to governance and supervision

Participants should ensure that their governance structure for conflicts management provides clear escalation channels for remediating operational conflict issues.

## Our focus

Governance structures provide oversight of conflict issues within and across business units, formal escalation channels and accountability.

## Our observations

### Poorer practice observations

- › A conflicts committee with responsibility for control room issues had not convened for several years reflecting a lack of senior management engagement.
- › Failure to remediate significant conflict issues identified and escalated by internal compliance functions, with some issues repeatedly identified and escalated over a number of years.
- › Some independent control functions lacked clarity regarding respective roles and responsibilities for management of conduct risk between first and second line of defence which created tension and produced gaps in coverage.
- › No centralised incident register for recording conflict issues, leading to inconsistent and incomplete reporting and escalation.



### Better practice observations

- › A specific governance committee covered escalated conflict issues as a standing item on the agenda. This committee was comprised of senior staff across business, compliance and control room with sufficient levels of authority and capacity to make business decisions to manage conflicts effectively.
- › Clear channels for staff to escalate conflicts to committees, with clear ownership and accountability in their terms of reference.
- › Key conflict issues, developments (e.g. implementation of technology solutions) and business trends were reported on a regular basis to governance committees with accountability to ensure conflicts arrangements remain effective.
- › Front office supervisors required to monitor transactions in which their deal team members were involved to ensure that existing transactions with potential conflict issues or inside information had been recorded in the transactional conflicts register and were up to date.
- › Internal audit carried out independent periodic reviews relating to the control room function and conflicts management by specific businesses/enterprise-wide, with senior management being accountable for remediating findings from the reviews.

## Appendix 1: Our review methodology

Between 2019 and 2022 (inclusive), we engaged with five licensees as part of a thematic 'deep dive' review, and a 'high level' benchmarking review of another licensee, of arrangements used by these participants for managing conflicts of interest in wholesale financial markets. Our review was informed by industry standards, including the FMSB's publications.

We focused on reviewing the arrangements in place across the participants' public-side business and private-side business (including sales and trading, capital markets and corporate advisory teams) relevant to wholesale market activities. We note that not all aspects of conflicts management arrangements were reviewed.

We reviewed:

- › the policies, processes and procedures for identifying and managing conflicts of interest
- › the systems and controls over business practices and employee behaviours that relate to managing conflicts of interest
- › the governance and supervisory arrangements that relate to managing conflicts of interest.

The transactional conflicts clearance process (identifying, assessing and addressing actual, apparent and potential conflicts of interest) and the management of confidential information arising from these transactions (particularly for debt capital market transactions) was a key focus area.

Our review involved face-to-face and/or virtual meetings. We also reviewed policies and procedures and sample sets of transaction information. Intelligence from ASIC's wider work, including observations from court enforceable undertakings, was considered as part of the review.

### Participants reviewed

**Australia and New Zealand Banking Group Limited**

**Commonwealth Bank of Australia**

**JPMorgan Chase Bank, National Association**

**Macquarie Group Limited**

**National Australia Bank Limited**

**Westpac Banking Corporation**

## Appendix 2: Related information

In addition to the information and observations set out in this report, ASIC publishes the following regulatory guides and reports that consider conflicts management arrangements:

- › [Regulatory Guide 79](#) *Research report providers: Improving the quality of investment research*
- › [Regulatory Guide 181](#) *Licensing: Managing conflicts of interest*
- › [Regulatory Guide 264](#) *Sell-side research*
- › [Report 393](#) *Handling of confidential information: Briefings and unannounced corporate transactions*
- › [Report 605](#) *Allocations in equity raising transactions*
- › [Report 652](#) *Wholesale FX practices in Australia*
- › [Report 668](#) *Allocations in debt capital market transactions*
- › [Report 741](#) *Conduct risk in wholesale fixed income markets.*