15 August 2018

TO:
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Senior Analyst
Market Supervision
Australian Securities and Investments Commission
Level 5, 100 Market Street
SYDNEY NSW 2000

email: Capital.Review@asic.gov.au

FROM:

Director
Pritchard and Partners Pty Ltd
10 Murray Street
Hamilton, NSW, 2303

RE: Response to Consultation Paper 302.

Pritchard and Partners Pty Ltd ("Pritchards") wishes to provide a response to the ASIC Consultation Paper 302: Proposed changes to ASIC's capital requirements for market participants.

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About Pritchards

Pritchard & Partners Pty Limited was established in 1996 and is a licensed firm of stockbrokers and financial advisers.

Pritchard & Partners Pty Limited has been licenced by the Australian Securities and Investments Commission since 1996, and in the same year became the first corporate member, and the first new broking member firm in 26 years of the then Stock Exchange of Newcastle Limited (now the National Stock Exchange of Australia Limited).

The directors of Pritchard & Partners Pty Limited have been principally responsible for the renaissance of the Exchange and sponsored the first new listings on the Exchange in 2000. Starting a process in 1995, Pritchard & Partners Pty Limited was instrumental in obtaining the Australian Market licence ("AML") from the Australian Government and creating the initial infrastructure so that the NSX could open for business in February 2000.

Today, the firm remains the longest standing member of the NSX.

Pritchard & Partners Pty Limited provides its clients with a range of financial services including the following:

- Public Listing Services
- Corporate Finance Services
- Nominated Adviser Services
- Sponsoring Broker Services
- Stockbroking Services
- Private Wealth Management

Executive Summary to the response

1. Pritchards have provided detailed comments on areas that relate to its AFSL. The executive summary provides a precise of those comments;
2. General comments have been provided on the section related to Futures;
3. Pritchards submits that the Chart and data provided by ASIC on international core capital levels does not support the conclusion made by ASIC to raise the core capital requirement for NSX participants to $500,000. The chart and the data provided by ASIC in fact demonstrates that the current core capital requirements are in line with Australia's major trading partners. Therefore, the conclusion does not support the increase to the core capital value;
4. Comparing the risk of Australia with that of New Zealand, Hong Kong and Singapore is wrong given the highly speculative nature of the companies listed on those markets compared to Australia and its other major trading partners listed in the study. Therefore, the conclusion does not warrant that the core capital value should be increased;
5. ASIC appears to have only considered the capital frameworks of New Zealand and Singapore, and does not explain why these are better than that of Australia, Canada or the United Kingdom.
6. Authorised deposit taking institutions that act as participants should not be exempt from the Capital Rules and should be placed under the same requirements as other participants;
7. A transitionary time for any impacts on the balance sheet should be a minimum of 24 months and recognise the concept of the cost of capital;
8. It is submitted that the present underwriting regime works well and there should not be an increase in capital requirements;
9. **Pritchards submits that the current level of core capital is sufficient and is in line with international standards and comparative risk levels.**

General Comments about CP 302

1. ASIC has not presented a compelling argument for change (see point 9 above). Just because a measure has been in place for a long time does not mean that the measure is inadequate. Of course, the measure should be reviewed from time to time but in this case there is no compelling case presented for change.
2. The statistical data presented does not have academic rigour. That is, the data is open to another interpretation which better fits the hypothesis of no change than for change.
3. The sample of 35 participants seems to exclude 30 additional participants on ASX and 11 non-ASX participants. Including these additional participants would provide a fuller statistical picture of the conditions and risks facing all participants.
4. ASIC appears to have made no attempt to calculate the actual level of risk applicable to each type of participant or of the market as a whole.
5. CP 302 provides a narrow focus in its analysis. For instance, it ignores analysis of investor protection regimes such as Participant Professional Indemnity Insurance, the ASX National

Guarantee Fund and the NSX Compensation arrangements. There are more efficient mechanisms available to protect investors than mandating a blanket increase in core capital.

6. The original introduction of ASX's Rule 1A risk ratio provided a risk weighted approach to the various exposures a participant faced rather than relying on core capital increases. It is safe to say that the larger the participant and the greater the market share of a participant and the range of services offered is more accurate measure of the risk that an individual participant faces.
7. If investor assets are sufficiently quarantined and protected from a participant's operations there should not be a need for core capital or risk weighted measures. That is even if a participant becomes insolvent but investor client assets are adequately protected then investors should not suffer loss simply because a participant has become insolvent.

Detailed Comments to ASIC questions

ASIC Proposal	Feedback
B1Q1 Do you agree that market participants of futures markets should be subject to a risk-based capital framework? If not, please provide detailed reasons.	B1Q1: Yes
B1Q2 Do you consider a minimum core capital requirement of $1,000,000 to be an appropriate threshold? If not, please provide details.	B1Q2: No comment
B1Q3 What impact would this proposal have on your business? Please include any benefits or costs (in dollar terms) associated with the proposal (as a one-off benefit or cost, and on an annual basis).	B1Q3: None, Pritchards do not trade in futures.
B1Q4 Would you prefer ASIC to retain the existing NTA requirement or move to a risk-based approach? Please give detailed reasons for your answer.	B1Q4: No
B1Q5 Do you foresee any practical issues with imposing a risk-based capital framework on participants of futures markets?	B1Q5: No
B1Q6 Do you consider six months to be an appropriate length of time to allow futures market participants to transition from the NTA requirement to the risk-based capital framework?	B1Q6: No. A minimum of 24 months should be set. This is because the NTA requirement is measured by the balance sheet and it takes time for organisations to restructure their balance sheets.
B2Q1 Do you agree that market participants should be required to hold additional capital if they hold commodity positions? If not, please provide detailed reasons.	B2Q1: Yes.
B2Q2 Do you consider the proposed commodity position risk amount adequately addresses the position risk of holding commodity positions? If not, please provide details.	B2Q2: No comment.
B2Q3 What impact would this proposal have on	

ASIC Proposal	Feedback
your business? Please include any benefits or costs (in dollar terms) associated with the proposal (as a one-off benefit or cost, and on an annual basis).	B1Q3: None.
B2Q4 Do you foresee any practical issues with imposing a commodity position risk amount?	B2Q4: No.
B2Q5 Do you agree with the proposed commodity position risk factors? If not, please provide details.	B2Q5: No comment.
C1Q1 Do you agree that the core capital requirement should be increased?	C1Q1: No.
C1Q2 Do you consider that this proposal provides greater protection for retail clients?	C1Q2: No. The change is predicated on an invalid comparison to the markets of New Zealand, Hong Kong and Singapore. These markets have greater comparative risk than Australia.
C1Q3 What impact would this proposal have on your business? Please include any benefits or costs (in dollar terms) associated with the proposal (as a one-off benefit or cost, and on an annual basis).	C1Q3: More capital would be required to be placed into the business. We currently satisfy all capital requirements at the current levels. Introducing more capital would have both a one-off cost and an ongoing cost. The opportunity cost of capital concept would apply and the return on capital concept would also apply. Both would introduce increase cost in lost opportunities for the use of the capital.
C1Q4 Do you consider the proposed core capital requirement too onerous? If so, why?	C1Q4: We consider the proposal ill-conceived based on an invalid comparison. The figures stated for participants (para 23), do not provide an analysis of those participants that are only on the NSX market.
C1Q5 What do you consider an appropriate length of time for market participants of securities markets to meet the minimum core capital requirement of $500,000?	C1Q5: As a general concept it takes time for changes to be implemented where a reconstruction or expansion of a balance sheet is required. For instance, when Banks are required to increase their Tier 1 capital by APRA they need to seek funding from the market. This funding can typically require up to a two year or longer lead time before they can comply with new capital requirements.
C1Q6 Should ASIC instead introduce a two-tier core capital requirement that distinguishes between market participants based on the type of business being conducted (e.g. a $500,000 core capital requirement for market participants that hold client money, and a $250,000 core capital requirement for market participants that do not hold client money)?	C1Q6: No. Any tiered structure should be commensurate with the risks faced by that participant in the market(s) that they operate in.
C2Q1 Do you agree that a market participant should hold additional capital if it engages in	C2Q1: No. The participant would be able to gauge the level of risk to their business of either

ASIC Proposal	Feedback
underwriting or sub underwriting activity? If not, please provide reasons. C2Q2 Do you consider our proposed underwriting and sub underwriting risk requirement adequately addresses underwriting risk? Does your business have alternative approaches to manage underwriting risk? C2Q3 Do you agree that a market participant need not hold additional capital if the underwriting or sub underwriting is fully sub underwritten or fully subscribed? If not, please provide reasons. C2Q4 Are you satisfied that our proposed underwriting and sub underwriting risk requirement adequately addresses the risk of regulatory arbitrage among entities that engage in underwriting/sub underwriting? C2Q5 What impact would this proposal have on your business? Please include any benefits or costs (in dollar terms) associated with the proposal (as a one-off benefit or cost, and on an annual basis). C2Q6 Is it sufficiently clear how the underwriting and sub underwriting risk requirement must be calculated?	being able to fully underwrite, partially under-write or sub-underwrite before they enter into the arrangements. This would normally include an analysis of a worst case scenario. C2Q2: No comment C2Q3: Yes. C2Q4: No comment. C2Q5: If the proposals are implemented there could be a lessening of the number of new underwritten capital raisings. This would increase additional uncertainty into the market, of a Company's ability to raise capital and may as a result create further risks. C2Q6: No.
C3Q1 Do you agree that a market participant should hold additional capital if it engages a sub underwriter? If not, please provide reasons. C3Q2 Do you consider our proposed sub underwritten positions method adequately addresses the counterparty risk associated with sub underwriting? Does your business have alternative approaches for managing this risk? C3Q3 Do you agree that the counterparty risk amount for a sub underwriting should commence at the time the sub underwriting commitment is entered into, and cease 31 days after the commitment becomes unconditional? If not, please provide reasons. C3Q4 What impact would this proposal have on your business? Please include any benefits or costs (in dollar terms) associated with the proposal (as a one-off benefit or cost, and on an annual basis). C3Q5 Is it sufficiently clear how the counterparty risk requirement using the sub underwritten positions method must be	C3Q1: No. This is because the sub-underwriter assumes a portion of the risk to underwrite. Any agreement on sub-underwriting usually recognises such risk and so would have in place mechanisms to address adverse events. C3Q2: No comment C3Q3: No comment C3Q4: No comment C3C5: No

ASIC Proposal	Feedback
calculated?	
C4Q1 Do you agree that a market participant should be required to calculate a credit derivative-specific non-standard risk amount? If not, please provide details. C4Q2 Do you consider that this proposal adequately addresses the counterparty risk of credit derivatives? C4Q3 What impact would this proposal have on your business? Please include any benefits or costs (in dollar terms) associated with the proposal (as a one-off benefit or cost, and on an annual basis).	C4Q1: No Comment. C4Q2: No comment. C4:Q3: None.
C5Q1 Do you agree that reducing the number of risk calculation methods will make it easier to comply with the Securities Capital Rules? If not, please provide reasons. C5Q2 What impact would this proposal have on your business? Please include any benefits or costs (in dollar terms) associated with the proposal (as a one-off benefit or cost, and on an annual basis). C5Q3 Would you prefer ASIC to retain the existing risk calculation methods, or make further changes to simplify risk requirement calculations? Please give detailed reasons for your answer, and include in your response what risk calculation methods (if any) you consider can either be removed from the rules or simplified.	C5Q1: Pritchards agrees with reforms aimed at reducing the complexity of the calculation methods, however some participants may find it easier to comply if there are a range of methods open to them which better fit their business model and risk exposure. C5Q2: None C5Q3: The simplification of all rules is always worthwhile.
C6Q1 Do you agree that margined equities, debt instruments and warrants should be subject to the non-margined financial instruments method? If not, please provide details. C6Q2 Do you agree that where an initial margin isn't charged (or where the initial margin is low) that the counterparty risk amount should be the potential credit exposure factor in Table A5.2.2? C6Q3 Do you consider that this proposal adequately addresses counterparty risk? C6Q4 Is it sufficiently clear how the counterparty risk requirement must be calculated? C6Q5 What impact would this proposal have on your business? Please include any benefits or costs (in dollar terms) associated with the	C6Q1: No comment. C6Q2: No comment. C6Q3: No comment. C6Q4: No comment. C6Q5: No comment.

ASIC Proposal	Feedback
proposal (as a one-off benefit or cost, and on an annual basis).	
C7Q1 Do you agree that market participants with negative net assets should be required to lodge daily returns with ASIC? If not, please provide reasons. C7Q2 Do you consider that this proposal will help ASIC to identify liquidity and solvency issues in a more timely manner?	C71: Generally, yes. C7Q2: It is unclear if this would be the result from the discussion provided by ASIC.
C8Q1 Do you consider that market participants that are partnerships should largely be required to comply with the same requirements as other market participants? If not, please provide reasons. C8Q2 What impact would this proposal have on your business? Please include any benefits or costs (in dollar terms) associated with the proposal (as a one-off benefit or cost, and on an annual basis).	C8Q1: Yes C8Q2: None.
C9Q1 Do you agree that a market participant should be required to disclose its aged debtors to ASIC? If not, please provide details.	C9Q1: No, not on a regular basis. The Aged Debtors report should be included when ASIC determines that a daily capital liquidity report is required to be lodged.
C10Q1 Do you agree that approved subordinated debt should not be used to meet the core capital requirement? If you disagree, please provide reasons. C10Q2 What impact would this proposal have on your business? Please include any benefits or costs (in dollar terms) associated with the proposal (as a one-off benefit or cost, and on an annual basis). C10Q3 Do you think a 24-month transitional period would give sufficient time to comply with an increased core capital requirement?	C10Q1: No. If it is properly sub ordinated to all liabilities it is in effect capital, and therefore there is no reason why it should not be allowed to be used to satisfy the core capital requirement. C10Q2: If we are required to raise our core capital it reduces the choices we have in what kind of capital structure we use C10Q3: Minimum transitional arrangements should be for 24 months.
C11Q1 Do you have any comments on our proposed amendments to the definition of 'Financial Asset Revaluation Reserves' or 'Future Income Tax Benefit'?	C11Q1: No Comment
C12Q1 Do you have any comments on our proposed amendment to the definition of	C12Q1: No Comment

ASIC Proposal	Feedback
'Liquid'?	
C13Q1 Do you have any comments on our proposed amendment to the definition of 'Qualifying Debt Instruments' or our proposed definition of 'Credit Rating Agency'?	C13Q1: No Comment
C14Q1 Do you agree with the inclusion of Euronext 100, NZX 50, FTSE STI and KOSPI 200 in our list of recognised market indexes? If not, please provide details. C14Q2 Are there any other market indexes that you believe should be recognised by ASIC?	C14Q1: No comment C14Q2:.
C15Q1 Do you agree with our proposal to increase the number of recognised financial regulators? If not, please provide details. C15Q2 Are there any other financial regulators that you believe should be recognised by ASIC?	C15Q1: No comment. C2Q2:
D1Q1 Do you agree with our proposal to impose liquidity requirements on market participants? If not, please provide detailed reasons explaining why not. D1Q2 Do you consider our proposals adequately address the liquidity risks likely to be faced by market participants? Does your business have alternative approaches for managing liquidity risk? D1Q3 What impact would this proposal have on your business? Please include any benefits or costs (in dollar terms) associated with the proposal (as a one-off benefit or cost, and on an annual basis). D1Q4 Are the proposed liquidity requirements sufficiently clear? Do you consider that additional guidance is required?	D1Q1: The proposal is for participants to provide ASIC with cash flow forecasts. However, the questions relate to liquidity only. D1Q2: See D1Q1 D1Q3: See D1Q1 D1Q4: See D1Q1
D2Q1 Do you agree with our proposal to exempt market participants that are also authorised deposit taking institutions from complying with the Securities Capital Rules and the Futures Capital Rules? If not, please provide detailed reasons explaining why not.	D2Q1: No. APRA as regulator of authorised deposit taking institutions primary role is to protect the interests of deposits. Where the equivalent of an authorised deposit taking institution has collapsed overseas, the regulatory authority has protected depositors interests above those of other creditors. By allowing an authorised deposit taking

ASIC Proposal	Feedback
	institution to be exempt from capital requirements, will mean additional counterparty risk for those parties dealing with the authorised deposit taking institution. It will also mean that they will have a significant cost of capital advantage compared to other institutions. • .
D3Q1 Do you agree with our proposal to require market participants to notify ASIC in relation to other capital requirements? If not, please provide detailed reasons explaining why not.	D3Q1: Yes.