Review of online trading providers

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About this report

In 2022–23, we conducted a review of online trading providers. This report summarises our key observations on the practices we observed and sets out the results of our actions.

Contents

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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

Background

During the COVID-19 pandemic, there was a significant increase in retail investor participation in financial markets, with one in five Australian investors starting to invest in exchange traded products during the pandemic (*ASX Australian Investor Study 2023*). In response to this growth, the range of online trading providers offering trading in regulated investment products expanded. They included entities authorised to deal in securities or complex products such as contracts for difference.

Collectively, these online trading providers have over one million retail clients and hold billions of dollars in client money and assets.

In February 2021, the average daily turnover of the retail securities market peaked at $3.5 billion (or 20.15% of total turnover)—in September 2023, this declined to $1.6 billion (or 11.61% of total turnover). To broaden their revenue base, some online trading providers now offer, or are seeking to offer, high-risk products or services to retail investors. These products may be inappropriate for retail investors and result in poor investor outcomes.

Our supervision of online trading providers

With the growth in retail trading in recent years, we took a combination of risk-based proactive, thematic and reactive approaches to the supervision of online trading providers. We proactively examined the practices, business structures and product offerings of a range of online trading providers to examine potential risks and test their compliance with the financial services laws. We also responded quickly to concerning offers and practices identified in reports of misconduct and through our continuous monitoring of domestic and overseas markets. Our surveillance activities included providers ranging from emerging fintech companies who operate as an authorised representative of an Australian financial services (AFS) licensee, to CFD issuers, large stockbrokers and other AFS licensees.

We considered guidance in Regulatory Guide 104 AFS *licensing: Meeting the general obligations* (RG 104) and Regulatory Guide 234 *Advertising financial products and services (including credit): Good practice guidance* (RG 234) when reviewing:

› whether licensees were providing services efficiently, honestly and fairly, and effectively supervising their representatives, and

› whether promoters were complying with prohibitions against false or misleading statements and misleading or deceptive conduct.

Summary of key findings

This report highlights our observations from this review and identifies the range of actions we have taken in relation to:

› **High-risk offers**—Some of the products being offered or planned to be offered may be inappropriate for retail investors and expose them to new or additional risks.

› **Supervision of representatives**—Some online trading providers operate as authorised representatives of AFS licensees. We are concerned that some licensees may not have taken reasonable steps, or assigned sufficient resources, to adequately monitor and supervise their representatives.

- **Misleading or deceptive statements**—Some providers promoted their business through potentially misleading claims relating to low or zero brokerage fees, the safety and security of client assets, and how they are regulated.
- **Use of digital engagement practices**—Some providers designed their platforms to incorporate behavioural levers and choice architecture that can unfairly influence consumer decision making and lead to trading that may result in losses or consumer harm.
- **Holding client assets**—Some providers did not clearly explain how they hold client assets on trust or in pooled arrangements, making it difficult for clients to assess potential benefits and risks and make an informed choice of trading provider.
- **Holding client money**—Some providers had inadequate arrangements for handling client money which may be in breach of the client money provisions and expose clients to increased risks.

Our actions

We have used a combination of court actions, stop orders, infringement notices and other interventions to disrupt potentially harmful offers of financial products and services, improve retail investor outcomes and clarify our regulatory expectations with online trading providers.

Our actions have resulted in the following outcomes since the onset of the COVID-19 pandemic in March 2020:

- Disrupting proposals to offer retail securities lending products that carry significant risks, and are inappropriate, for retail clients.
- Disrupting proposals to offer trading in unregulated crypto-assets alongside trading in regulated securities, that may have led retail clients to underestimate risk or believe that investor protections apply where they do not.
- Improving licensee oversight of authorised representatives to ensure that trading providers have the expertise and supervision required to protect retail client assets and prevent misconduct.
- Engaging with online trading providers to rectify misleading or deceptive statements that may result in retail clients choosing to use a product or service based on inaccurate depictions of fees, safety or security.
- Promoting informed decision making by retail investors, by encouraging trading providers to enhance disclosure of product features and risks, including custody of client assets.
- Engaging with online trading providers to rectify their arrangements for holding client money, reducing the risks to investor funds by correctly segregating client funds from operational funds.

We will continue to monitor the practices, business structures and product offerings of online trading providers. Where we identify significant harm, we will consider the full range of regulatory actions available including, where appropriate, civil or criminal enforcement action.

> Online trading providers should carefully consider how the observations and areas of improvement apply to their business.

High-risk offers

Online trading providers must ensure the financial services covered by their licence are provided efficiently, honestly and fairly: section 912A(1)(a) of the *Corporations Act 2001* (Corporations Act).

With changing market conditions and a decline in retail investor trading activity from the peaks experienced during the pandemic, we have observed some online trading providers offering, or proposing to offer, high-risk products or services to retail investors. In August 2022, we warned that high-risk offers may be unfair, inappropriate and result in poor outcomes for retail investors: see Media Release (22-239MR) *ASIC warns brokers considering high-risk offers to retail investors*.

Issues at a glance

Securities lending

In Australia, securities lending has generally been limited to institutional investors who have the size, scale and experience to understand and manage the inherent risks.

'Securities lending' involves one party (the lender) transferring title of their securities to another party (the borrower). This gives the borrower unencumbered title to the securities.

The borrower is obliged to return the securities or equivalent securities to the lender either on demand or at the end of the loan term. The borrower also pays a fee and provides collateral in the form of shares, bonds or cash to secure the performance of their obligations.

Securities lending is complex and the benefits (including financial returns) are typically small. Yet the lender takes on significant risks which may be difficult for retail investors to value and understand. In our review of retail securities lending proposals these risks included:

› **Market risks**—One common reason for borrowing securities is to support short selling activities. Short selling can put downward pressure on the loaned securities and, as a result, affect the value of the lender's position.

› **Loss of voting rights**—Voting rights associated with the loaned securities are passed from the lender to the borrower in a securities lending transaction. As such, the lender must exercise their right to recall the securities if they wish to vote.

› **Tax implications**—It is important for lenders to know that there may be different tax implications from any corporate actions or substitute dividends (i.e. an amount equivalent to a dividend that occurs when a security is on loan).

› **Failure of the borrower**—The lender may suffer a loss of capital if the borrower fails or otherwise defaults on its obligations and the value of any collateral is less than the cost of replacing the loaned securities.

We also observed providers proposing to give retail clients complex and lengthy securities lending documentation normally used by financial institutions. We were concerned that these agreements were not prepared for and may not be readily understood by most retail clients.

In addition, in our review of retail securities lending proposals, we were concerned that many of the design features may not be fair or appropriate for retail investors.

Crypto-asset trading alongside regulated financial services

Crypto-assets and trading of crypto-assets are currently largely unregulated by ASIC unless the crypto-asset is a financial product. Crypto is high-risk, volatile and complex.

Note: In October 2023, the Government published a consultation paper, *Regulating digital asset platforms*, proposing a regulatory framework for digital asset platforms, including those that offer trading in digital assets.

We have seen some providers planning to offer trading in non-financial product crypto-assets alongside other regulated products and services. We were concerned that some providers **did not**:

- clearly differentiate between unregulated crypto-asset offerings and regulated offerings on their trading platforms—this may confuse retail investors, leading them to underestimate the risks of crypto-assets or believe that offers of unregulated crypto-assets have the same consumer protections as offers of regulated financial products and services
- clearly disclose how crypto-assets would be held for clients and how this may differ from their arrangements for holding regulated financial products, such as securities. For example, some of these providers:
  - presented unregulated crypto-asset offerings alongside regulated financial product offerings in the same section of their website
  - used terminology that could imply the product was regulated as a financial product, such as 'invest', 'trusted' and 'secure', and
- explicitly state that retail investor protections would not apply to unregulated crypto-assets and would not apply to crypto-asset trading on their trading platforms.

We observed one provider seeking to use its regulatory status as a promotional tool for its unregulated crypto-asset offering. We were concerned this could convey the false impression that crypto-asset trading with the provider (and the underlying crypto-assets) was regulated or approved by ASIC in the same way as other financial products and services.

We are also concerned that some providers proposed to offer trading in unregulated crypto-assets without sufficient consideration of the adequacy of their risk management systems and resources. An important consideration is the holding of client money. Licensees should ensure their systems and resources will be capable of providing the financial services covered by the AFS licence and trading in unregulated crypto-assets where the risks associated with the crypto-asset services could impact the provision of regulated products and services.

Our actions

We have taken swift action to disrupt certain high-risk offers, or proposed offers, to retail investors where we were concerned the offers may be unfair, inappropriate or result in poor investor outcomes, including:

Disrupting securities lending offers to retail investors

- **Design feature concerns**—We identified one provider planning to launch a retail securities lending program which would have automatically opted-in clients, bundled the program together with other services, contained no pre-qualification or vetting of investors, and proposed a fee split heavily skewed in favour of the provider. We raised concerns that the securities lending offer may not be fair for retail investors, considering the relatively small benefit the retail investor would receive for bearing the significant risks associated with lending their securities. After we intervened, the provider decided not to proceed with this offer.
- **Inappropriate target market and defective disclosure**—We issued two interim stop orders preventing Interactive Brokers Australia Pty Ltd (Interactive Brokers)—who offered its retail securities lending

program as a derivative—from issuing the product to retail investors because of deficiencies in the product's target market determination (TMD) and product disclosure statement (PDS). We were concerned that Interactive Brokers had inappropriately included in the target market investors whose investment objectives were likely inconsistent with the features and risks of the product. We were also concerned that the PDS was defective because, among other things, it omitted important information about the benefits, fees and commissions of the product. We revoked the TMD stop order after Interactive Brokers, among other things, more narrowly defined the class of consumers which comprised the target market for the product. A final stop order was issued in respect of the PDS. Interactive Brokers has not made any further offers of the product to retail investors in Australia.

Note: See Media Release (23-056MR) *ASIC places interim stop orders on TMD and PDS for a securities lending product* (9 March 2023).

Reviewing offers of crypto-asset trading alongside securities trading

We observed several providers proposing to offer crypto-asset trading alongside regulated products and services (such as securities trading).

After we engaged with these providers, they decided not to offer non-financial product crypto-asset trading alongside regulated products and services.

Other high-risk offers

We have commenced proceedings in the Federal Court against eToro Aus Capital Limited (eToro). We are alleging breaches of:

- the design and distribution obligations—relevantly, that eToro's target market for the CFD product was far too broad for such a high-risk and volatile trading product where most clients lose money, and that the screening test was inadequate to assess whether a retail client was likely to be within the target market, and
- eToro's licence obligation to provide financial services efficiently, honestly and fairly.

Note: See Media Release (23-204MR) *ASIC sues eToro in its first design and distribution action to protect consumers from high-risk CFD products* (3 August 2023).

Case study 1: Crypto-asset trading alongside securities trading

We met with an online trading provider who was planning to offer non-financial product crypto-asset trading to its existing share trading clients. The entity's crypto-asset trading experience was designed to mimic its share trading experience, and it proposed to fully integrate the unregulated crypto-asset trading functionality into its existing share trading platform.

The provider planned to embed a 'buy/sell crypto' button in the middle of the clients' securities trading dashboard, with little or no separation between regulated financial products and unregulated products and services.

We were concerned that integrating trading in unregulated crypto-assets with share trading in this way, and using the same platform design and trading functionality for both regulated financial products and unregulated offerings, may have conveyed the false impression that crypto-asset trading with the provider and the underlying crypto-assets were regulated by ASIC and benefited from the same consumer protections as securities trading if something went wrong.

Following our engagement, the provider decided not to proceed with offering unregulated crypto-asset trading to its clients.

AFS licensee oversight of authorised representatives

Some online trading providers operate as authorised representatives of AFS licensees. Where an AFS licensee appoints an authorised representative to provide financial services on its behalf, it must (among other things):

- take reasonable steps to ensure that its representatives comply with the financial services laws (section 912A(1)(ca) of the Corporations Act), and
- have adequate resources (including financial, technological and human resources) to provide the financial services covered by the licence and carry out supervisory arrangements (section 912A(1)(d) of the Corporations Act).

Issues at a glance

We have observed a number of online trading providers operating as authorised representatives of a licensee, including:

- **Operating independently of the licensee**—We identified several providers operating businesses independent of the licensee on whose behalf they were authorised to provide the financial services. We were concerned the licensee did not have adequate day-to-day visibility or control over the activities of these providers, with one provider even announcing the launch of new services without the licensee's express approval.
- **Operating without adequate supervision**—We identified several providers operating as authorised representatives of a licensee that lacked sufficient expertise and understanding of the representatives' business and operations. Some of these providers offered, or sought to offer, complex or novel products such as retail securities lending, which were outside the scope of the licensee's day-to-day financial services business. We also observed that the compliance function of this licensee was underdeveloped relative to the nature and scale of their representatives' business and operations, and we were concerned that these representatives were operating without adequate supervision.
- **Receiving and holding client money in their own name**—We found several corporate authorised representatives were receiving and holding client money in bank accounts in their own names, and not in the name of the licensee for whom they were providing financial services: see also 'Holding client money' below.

Our actions

We will continue to undertake targeted reviews of the supervisory arrangements of licensees and, where appropriate, take action where a licensee fails to meet its supervisory obligations, including under section 912A(1) of the Corporations Act.

We have commenced civil penalty proceedings in the Federal Court against Lanterne Fund Services Pty Ltd for failing to comply with various obligations imposed on AFS licensees, including failing to implement and maintain robust risk and compliance procedures to manage its authorised representatives.

Note: See Media Release (22-174MR) *ASIC issues civil penalty proceedings against wholesale licensee Lanterne Fund Services for risk and compliance failures* (7 July 2022).

Misleading or deceptive statements

The marketing and promotion of financial products and services can strongly influence retail investors when they are making investment decisions, including which trading providers to use.

The law prohibits conduct that is misleading or deceptive, or likely to mislead or deceive, in relation to financial products or services. This applies to online trading providers who must ensure that any statements made in their promotion of financial products and services are true, accurate and able to be substantiated.

Issues at a glance

In our review, we identified online trading providers making potentially misleading or deceptive statements on their websites and other promotional materials relating to:

- **Fees disclosure**—We identified several providers marketing 'zero' or 'low-cost' brokerage to attract clients. However, to use their services, clients often had to incur a range of other material fees and charges (such as foreign currency conversion costs) which generated significant revenue for these providers. We were concerned that some of these claims of 'zero' or 'low-cost' brokerage were not true to label, particularly where other fees and charges were payable by the client or where the service was 'bundled' with other products or services that effectively subsidised the brokerage and caused retail investors to take on additional risk.
- **Claims about safety and security**—We identified several providers using the terms 'safe' and 'secure' to describe their arrangements for holding client money and assets, without qualification. We were concerned that these representations may have created a misleading impression that these arrangements were without risk.
- **Use of ASIC's name and logo**—We identified several providers using ASIC's name and logo to promote their products or services. We were concerned this may lead consumers to believe that the provider, and their products or services, had been approved or endorsed by ASIC. You must *never* reproduce the ASIC logo or other ASIC graphics without express approval from ASIC.

Our actions

We have engaged directly with online trading providers to rectify their websites and other disclosures. Specifically, our actions have resulted in the following outcomes:

- four providers have either ceased making claims of 'zero' or 'low' cost brokerage or have qualified these claims by providing a more detailed and prominent summary of all applicable trading fees or costs payable by a client
- one provider removed the outdated fee comparisons between itself and its competitors
- six providers ceased using the terms 'safe' and 'secure', without any further qualification, to describe their arrangements for holding client money and assets, and
- two providers removed ASIC's name and/or logo from their promotional materials.

Fintech firm Bobbob Pty Ltd has also paid $53,280 to comply with infringement notices issued by ASIC for representations it made about a crypto-asset linked investment product.

Note: See Media Release (23-261MR) *Fintech company pays penalties for crypto product representations* (27 September 2023).

Digital engagement practices

The law prohibits conduct that is misleading or deceptive, or likely to mislead or deceive, in relation to financial products or services. Online trading providers must also ensure the financial services covered by their licence are provided efficiently, honestly and fairly: section 912A(1)(a) of the Corporations Act.

Retail investors who use online trading platforms are exposed to a variety of digital engagement practices which influence the choice architecture within which their decisions are made. These may include:

- **gamified incentives** (e.g. prizes and giveaways)
- **social trading** (e.g. influencer marketing, education communities and copy trading), and
- **the design** of trading apps, websites and marketing materials.

Digital engagement practices increase the speed, reach and frequency of marketing and distribution channels and are used by providers to drive revenue growth by attracting and retaining retail clients.

While a given digital engagement practice may not be inherently harmful, their use individually and in combination may be harmful and should be assessed across the product or service lifecycle.

Digital engagement practices have the potential to create a complex and potentially harmful ecosystem of stimulant experiences for investors. This ecosystem may obscure the true cost to trade, or encourage excessive trading or trading products which are inappropriate for retail investors where the risks may not be understood and result in investor loss.

Online trading providers have an incentive to encourage investors to maximise the value and frequency of their trading. This may not be in the best financial interests of investors.

Issues at a glance

- **Inducements to trade**—Digital engagement practices were used by some providers with the express intention to increase client transaction activity to generate fees from frequent trading. Some of these digital engagement practices included:
  - promoting simple, low cost, easy access to trading, combined with seamless website and trading app experiences to reduce the steps and frictions for new clients to sign up and trade
  - inducements of cash giveaways, free shares and trades to sign up and place a trade by a deadline, prize draws providing clients with more entries the more they traded, and simulated trading competitions on social media for prizes, and
  - charity donations by providers based on client trade volumes.
- **Influencing consumers through behavioural levers**—Digital engagement practices were designed using behavioural levers to maximise consumer engagement with their platform. Commonly, providers outsourced behavioural science and analytics (including artificial intelligence (AI) and machine learning) to inform their use of behavioural levers. Examples included:
  - gamified features incorporated into marketing, websites and trading apps which replicated the intermittent reinforcement from video and arcade games, sports, betting and social media

- social trading features such as the ability to 'watch' and 'follow' other traders or financial influencers sharing their investing stories as part of a trading 'club' or 'community'.

- **Design features used to cross-sell high-risk products**—Some providers used digital engagement practices to influence the 'choice architecture' of their products and services, 'nudging' consumers to trade high-risk, speculative products such as contracts for difference (CFDs) or crypto. Examples included:
  - funnelling techniques using paid search engine results combined with website navigation design to redirect consumers who may be looking to invest in shares to webpages promoting CFD trading instead
  - website design which placed high-risk products alongside shares or gave high-risk products greater prominence than shares on a landing page which could imply similar risk characteristics, and
  - presentation and framing techniques designed to make high-risk products appear to have more benefits and a lower risk profile than shares.

Areas for improvement

We identified the following areas for improvement among the online trading providers we reviewed:

- **Marketing and distribution practices**—We are concerned that inducements designed to entice consumers to frequently trade, including digital engagement practices which use AI and gamification, may result in excessive trading ('churning') which leads to poor client outcomes. Frequent trading exposes retail investors to short-term losses as opposed to longer term investing, which can allow investors to ride out short-term volatility.
- **Disclosure of trading fees and alignment with marketing materials**—Providers who actively promote low-cost trading and zero brokerage should consider whether their claims are likely to mislead or deceive consumers by masking the true cost to trade, potentially in breach of the law. We observed providers promoting 'zero' brokerage for trading overseas equities. However, these trades were subject to foreign exchange (FX) conversion fees that were not prominently displayed on the provider's website or marketing materials: see also 'Misleading or deceptive statements' above.
- **Sign-off processes**—Inadequate oversight of digital engagement practices used in marketing and distribution practices may, among other things, indicate a failure to take reasonable steps to distribute a financial product consistent with the TMD.
- **Use of global marketing strategies**—The failure to properly consider and tailor marketing content designed by the provider's overseas head office may result in marketing which is inappropriate for Australian retail investors.
- **Supervision of representatives and affiliates**—The failure to have adequate supervisory arrangements and other controls in place, including for reviewing representations about expertise, strategies, products traded and returns which are referenced (including the use of financial influencers, copy traders, leader boards and rankings) may result in misleading statements or unlicensed conduct.

We will continue to monitor the use of digital engagement practices by online trading providers. Where we identify significant harm, we will consider the full range of regulatory actions available including, where appropriate, civil or criminal enforcement action.

Case study 2: Presenting high-risk financial products as share trading

An online trading provider who does not offer share trading in Australia promoted in search engine results and on a webpage that 'shares from all popular markets' could be traded on its trading platform.

The search engine results directed consumers to a webpage headed 'Trade Share CFDs' which carried several prominent headings, buttons and links about trading shares, such as: 'Trade popular Australian and global shares', 'View Our Shares', 'Check out our Cannabis Shares', 'Trade shares with leverage', 'List of shares – click here' and a table of 'Shares' listing example company names and share prices.

When consumers clicked on these links, they were taken to webpages which promoted CFDs.

These practices may confuse or mislead retail investors, even where qualified by other statements on the webpage. Shares and CFDs are different financial products with significantly different risk profiles. If investors who want to trade shares are 'nudged' by a provider to trade derivatives instead, this could result in unexpected losses for consumers on more complex and high-risk products.

As a result of our intervention, the online trading provider agreed to take corrective action to clarify its offer of share CFDs on its website.

Holding client assets

When an investor purchases shares on a licensed market in Australia, they can either have their shares registered on:

- the CHESS subregister maintained by ASX—these are known as CHESS sponsored holdings, or
- the issuer subregister maintained by the issuing company—these are known as issuer sponsored holdings.

CHESS sponsored holdings are given a holder identification number (HIN), which connects shareholders to their CHESS sponsored shares.

To reduce their operating costs, some online trading providers are using an omnibus HIN structure to hold client assets. Under these arrangements, the shares of clients are co-mingled under one HIN and held by a custodian.

While the use of omnibus HINs is common among operators of wrap accounts and overseas trading firms, they are traditionally less common when individuals purchase shares directly in Australia.

The following table provides a comparison of individual and omnibus HIN arrangements:

Item	Individual HIN	Omnibus HIN
Registration and ownership	Assets are registered in the name of the investor. Investor retains legal and beneficial ownership of their assets	Assets are registered in the name of the custodian and held on trust for the investor. The custodian is the legal owner of the assets, while the investor has a beneficial interest
Account structure	Assets are held on the investor's individual HIN	Assets of multiple investors are pooled and held on an omnibus HIN
Voting rights	Investor has direct access through the issuer	Depends on investor's agreement with their custodian
Corporate actions	Investor has direct access through the issuer	Depends on investor's agreement with their custodian
Issuer communications	Investor has direct access through the issuer	Depends on investor's agreement with their custodian

Issues at a glance

In our review, we observed some online trading providers using an omnibus HIN structure to hold client assets. We were concerned that these arrangements were not clearly disclosed to clients and impeded their ability to make an informed choice about which service provider to use. In particular, we were concerned that some online trading providers presented an unbalanced and one-sided view of potential cost savings and other benefits derived from the use of omnibus HIN holding arrangements, without providing adequate information about other important features and potential risks of this structure (including the risk of loss arising from the relevant holding structure and the different legal interest of clients).

We also identified several online trading providers using the terms 'safe' and 'secure' in their marketing materials, apps and websites, without any other qualification, to describe their arrangements for holding assets. We were concerned this created the impression that these arrangements were without risk: see also 'Misleading or deceptive statements' above.

Our actions

We have engaged directly with online trading providers about their arrangements for holding client assets, resulting in the following outcomes:

- **Enhanced disclosure**—We raised concerns with a provider that it did not clearly disclose to clients that it was using an omnibus HIN holding arrangement and what this means for clients. Following our engagement, the provider amended its website to include new and prominently positioned FAQs addressing its use of an omnibus HIN holding structure. This provided clients with information about the benefits and risks associated with the online trading provider's arrangements for holding client assets.
- **Removal of potentially misleading claims**—Following our direct engagement, six providers ceased using the terms 'safe' and 'secure', without appropriate qualification, to describe their arrangements for holding client assets.
- **Changes to custody arrangements**—After we raised concerns, a licensee took control of, and transferred into its own name, the client custody accounts previously held in the name of the provider operating as the licensee's authorised representative.

Holding client money

Strong client money handling protections are essential for maintaining investor confidence in the Australian financial system.

Client money is money paid to a financial services licensee in connection with a financial service that has been provided, or will or may be provided, or in connection with a financial product (subject to certain exceptions).

The law contains important requirements designed to protect client money and the interests of clients, including:

- requiring a licensee to hold client money in a designated account on trust and separate from its own funds, and
- limiting the circumstances in which a licensee can use client money.

Issues at a glance

In our review, we observed some online trading providers:

- **Using alternative arrangements for holding client funds**—We identified several providers using virtual or digital wallets, typically structured as a non-cash payment (NCP) facility, to accept and hold client funds. We were concerned that, in some instances, this resulted in:
  - client funds not being held on trust in a designated client money account as required by section 981B of the Corporations Act, and
  - client funds being co-mingled with persons who were not clients of the provider (e.g. with other clients of the NCP facility issuer).

  This can expose client funds to greater risk in the event of the licensee's (or other relevant party's) insolvency. We were also concerned that some licensees did not clearly explain to clients how their money was being held (e.g. it was difficult to ascertain from the online trading provider's website and other information provided to clients) and there was insufficient information about the risks. This impeded clients' ability to make informed choices about whether to trade with a provider using these alternative arrangements.
- **Receiving and holding client money in their own name**—We found several corporate authorised representatives were receiving and holding client money in bank accounts in their own names, and not in the name of the licensee for whom they were providing financial services. We were concerned that the licensee who had appointed these providers to provide financial services on its behalf did not hold client money directly on trust for the benefit of these clients. This can increase the risk of losses associated with non-permitted withdrawals, fraud and other operational breaches by these online trading providers.
- **Using client money for non-permitted purposes**—We identified one provider withdrawing client money to 'pre-fund' its expected daily trading activities with an external trading partner. We were concerned that client money was being used for a non-permitted purpose contrary to section 981C of the Corporations Act and regulation 7.8.02(1) of the *Corporations Regulations 2001* (Corporations Regulations). We immediately engaged with this online trading provider to ensure it established a new funding arrangement with its external trading partner.

- **Not properly designating client money accounts**—We identified several providers that had failed to designate their client money accounts as a trust account, as required by section 981B of the Corporations Act and regulation 7.8.01(2) and (5) of the Corporations Regulations. For example, some of the bank accounts we observed only contained the name of the licensee, and no reference to it being a client trust account (or client segregated account where permitted).

Our actions

We have required online trading providers to rectify their arrangements for holding client money. Our early intervention has resulted in timely and strengthened client money arrangements and protections for retail investors, including:

- one provider is moving away from the use of NCP facilities for holding client money and is establishing a client money account with an Australian deposit-taking institution
- one licensee has taken control of, and transferred into its own name, the client money account previously held in the name of the provider operating as the licensee's authorised representative
- one provider has established a new funding arrangement with its external trading partner so that it no longer involves the pre-emptive withdrawal of client money from the client money account—the provider's 'pre-funding' commitments are now satisfied by using its own funds, not client money, and
- four providers have rectified the designation of their client money accounts as trust accounts, including by adding the word 'trust' to the account name.

Case study 3: Pre-emptively withdrawing client money to fund external brokerage

We observed an online trading provider withdrawing client money ahead of orders being placed by clients to 'pre-fund' its account with its external trading partner.

- The client money was withdrawn from the trust account without a corresponding trade instruction from the client.
- The client money provisions in the Corporations Act protect the interests of clients by limiting the circumstances in which client money may be withdrawn.
- A licensee is not permitted to withdraw client money from the client money account in circumstances where a client has not yet traded securities or has not otherwise directed or authorised the licensee to do so.
- We required this provider to establish a new funding arrangement with its external trading partner—its 'pre-funding' commitments are now satisfied with its own funds and not client money.

Key terms and related information

Key terms

AFS licensee	A person who holds an Australian financial services licence under section 913B of the Corporations Act **Note:** This is a definition contained in section 9.
ASX	Australian Securities Exchange
authorised representative	A person authorised by an AFS licensee, under section 916A or 916B of the Corporations Act, to provide a financial service or services on behalf of the licensee
CFD	A contract for difference
CHESS	Clearing House Electronic Subregister System—a computer system operated by the ASX that (among other things) is used to provide an electronic subregister for shares in listed companies
CHESS sponsored holdings	Shareholdings recorded on the CHESS subregister maintained by ASX
choice architecture	Choice architecture refers to features in an environment that influence consumer decisions and actions. These features are present at every stage of product design and distribution. Examples include product bundling, default settings, sales process and website design
Corporations Act	*Corporations Act 2001*, including regulations made for the purposes of that Act
Corporations Regulations	*Corporations Regulations 2001*
crypto-assets	A digital representation of value or rights (including rights to property), the ownership of which is evidenced cryptographically and that is held and transferred electronically by: (a) a type of distributed ledger technology; or (b) another distributed cryptographically verifiable data structure
digital engagement practices	Digital engagement practices are tools including behavioural techniques, differential marketing, gamification, design elements or design features that intentionally or unintentionally engage with retail investors on digital platforms as well as the analytical and technological tools and methods
FX	Foreign exchange
HIN	Holder identification number—an identifier that connects shareholders to their CHESS sponsored shares

NCP facility	Non-cash payment facility
omnibus HIN	A HIN in which securities and other CHESS sponsored holdings for more than one beneficial owner are co-mingled under one HIN and held by a custodian or sub-custodian
online trading provider	An entity that offers online trading in regulated investment products. This includes entities authorised to deal in securities or issue complex products such as contracts for difference or other derivatives
PDS	Product disclosure statement
TMD	Target market determination

Related information

Headnotes

CFDs, client assets and money, digital engagement practices, gamification, high-risk offers, interventions, misleading or deceptive statements, online trading providers, retail investors, supervision of authorised representatives

Legislation

ASIC Act, section 12DA–12DB

Corporations Act, sections 911A, 912A, 981A–981H, 1041E, 1041H

Corporations Regulations, regulations 7.8.01–7.8.02

ASIC documents

RG 104 *AFS licensing: Meeting the general obligations*

RG 234 *Advertising financial products and services (including credit): Good practice guidance*

22-174MR *ASIC issues civil penalty proceedings against wholesale licensee Lanterne Fund Services for risk and compliance failures*

22-239MR *ASIC warns brokers considering high-risk offers to retail investors*

23-056MR *ASIC places interim stop orders on TMD and PDS for a securities lending product*

23-204MR *ASIC sues eToro in its first design and distribution action to protect consumers from high-risk CFD products*

23-261MR *Fintech company pays penalties for crypto product representations*