

## ***ASIC Consultation Paper 152: Adopting Pre-Existing ASX and SFE Guidance on General Operational Obligations***

### **Submission**

Upon the transfer to ASIC of Market Supervision on 1 August 2010, as well as the existing ASIC Policy on management and supervision – namely:

- ASIC RG104 Licensing: meeting the general obligations, and
- ASIC RG105 Licensing: organisational competency,

At the same time, ASIC also advised that it would 'seek to follow', as an interim measure, the relevant ASX Policy on management, supervision, client relations, automated order processing, trading records, orderly markets and other matters including:

- ASX Guidance Note 6 Management requirements
- ASX Guidance Note 7 Management requirements – Responsible Executives - good fame and character
- ASX Guidance Note 8 Insurance requirements
- ASX Guidance Note 27 Ongoing compliance and supervision- Responsible Executives Responsibilities, and
- ASX Guidance Note 33 Trading Records.<sup>1</sup>

ASIC also flagged that it would be reissuing its own policy in areas the subject of ASX Guidance: see RG214.60. ASIC Consultation Paper 152 (CP152) marks the first stage of this process, and further areas for transition from ASX to ASIC policy are planned<sup>2</sup>.

We would like to comment in on the Commission's review of ASX policy on general obligations of market participants in the following areas:

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<sup>1</sup> ASIC Regulatory Guide 214 *Guidance on ASIC market integrity rules for ASX and ASX 24 markets* July 2010 at RG214.59-214.61; ASIC CP152.14-152.18

<sup>2</sup> The planned stages for the review are set out in Table 2 of the Appendix to CP152

Changes in policy are proposed in the following areas:

1. **B1 Management requirements** (ASX GN6): update for current regulatory environment and business models - no substantive change to ASX GN6
2. **B2 RE appointments & notifications** (GN7&27): remove a. good fame and character requirement, b. notification guidance and c. form for RE notifications
3. **B3 Insurance** (GN8): remove director's attestation on sufficiency of alternative insurance arrangements
4. **Trading records:**
  - a) **B4 Retention Periods - clarifying retention period (7 years)**
  - b) **B5 Provision of records to ASIC**

We would also like to conclude by commenting generally about the ongoing review of ASX policy and the rules.

### **Proposals B1-B3**

Generally the proposals regarding management & RE requirements and insurance are unobjectionable, and are of benefit for members. In particular, the proposals B2 and B3 appear to be sensible moves which will simplify processes and make them more efficient.

### **Proposal B4 – Retention period for trading records**

We note that the only change proposed is to set out ASIC's preference for compliance with the *Market Integrity Rule* retention period for trading record documentation (7 years<sup>3</sup>), rather than the *Corporations Act* and *Regulations* provision (5 years<sup>4</sup>). While this is the approach most brokers take in any case, there are brokers who follow the *Corporations Act*, so clearly this is an area that needs to be clarified. We would submit that the better course would be to fix the ambiguity and seek Government approval to change the *Regulation* to be consistent with the *Rule*, otherwise legally the *Act* may prevail.

### **Proposal B5 – Provision of trading records to ASIC**

In CP152, ASIC requests that trading record details be provided to ASIC in a standard electronic format and set out in standard 'files'. This is to assist ASIC's analysis. The Trading Record Rule requirements (Rule 4.1) will not otherwise change. Proposal B5 is set out as follows:

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<sup>3</sup> Rule 4.1.4

<sup>4</sup> Regulation 7.8.19(5)

**B5** We propose to request in our guidance that market participants standardise formatting when sending us transaction-related trading records electronically. We will encourage participants to:

- (a) send the requested electronic trading records in either .csv or Excel format, where practicable; and
- (b) include the following columns of information in the order listed below in two separate files, as indicated.

**A file for the following account information when requested**

- market participant name
- account number
- account name
- representatives authorised to trade on the account
- address of the account holder
- telephone number of the account holder

**A file for the following trading information when requested**

- account number
- buy/sell code
- quantity
- security code
- unit price
- value
- trade date
- trade time
- original order
- amended orders
- name of person who gave the instruction
- name of person who received the instruction
- name of any person who passed the instruction on between the person who initially received the instruction and the trading platform, and the date and time they passed it
- name of the DTR (designated trading representative) who entered a trading message into a trading platform
- time the DTR entered a trading message into a trading platform
- whether the trading messages was the result of AOP (automated order processing)
- the open interface device and the computer or other device of the trading participant connected to an open interface device of the trading participant through which the trading message was submitted
- name of the DTR with responsibility for that open interface device or other device connected to the open interface device (unless the trading message was the result of AOP)
- whether the trading message was submitted on the trading participant's own account or for a client

Your feedback

*B5Q1 What changes would be necessary for you to implement this request? Please provide an indication of the additional time and cost that this would involve.*

*B5Q2 Do you consider that adopting this best practice would impose an unreasonable burden?*

**Rationale**

*GN 33 does not specify the format in which market participants ought to provide trading records requested by ASIC under s912E (surveillance checks by ASIC). As a result, we receive requested trading records in a number of formats. These formats include documents sent as images and as Excel, .pdf and .csv files. This inhibits our ability to effectively and efficiently perform our regulatory functions, given the large quantities of data that cannot be analysed consistently.*

Our Members have expressed serious concerns about the proposal. Compliance with ASIC's wishes in the provision to it of trading records would be **unreasonably burdensome and expensive**.

Our Members must maintain trading records in accordance with Market Integrity Rule 4.1, which sets out the matters which must be recorded. Our Members take the obligation to maintain trading records very seriously. As ASX stated in Guidance Note 33 *Trading Records* -

*Trading Record rules have a significant part to play in the integrity of the markets conducted by ASX. They are a critical record of the causal link between the instructions of a client or a decision to trade on a Market Participant's own account ("Principal Trading") and the entry of an order into a Trading Platform (whether SEATS or the DTP). Trading Records are a primary evidentiary record of a transaction and ASX places strong reliance upon the evidentiary value of accurate Trading Records.<sup>5</sup>*

The importance of the maintenance of accurate trading records has been emphasised by a long history of ASX disciplinary matters. It is a key area of compliance for brokers.

It is true that ASX GN33 did not provide the format in which trading records must be provided to the ASX. However, there is no obligation as to such a format. The primary obligation is to maintain records in the format provided in *Market Integrity Rule 4.3.1*, and the *Corporations Act*:

**4.3.1 Records to be in writing and in English**

- (1) A Market Participant must keep all of the records it is required to maintain under this Chapter 4, in writing and in the English language or in a manner which will enable them to be readily accessible by ASIC and readily converted into writing in the English language.

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<sup>5</sup> ASX Guidance Note 33 *Trading Records* January 2006 p.1

(2) A Market Participant must, if directed by ASIC in writing to do so, convert records maintained under this Chapter 4 into writing and into English.

In addition, the *Corporations Act* allows 'books' (which includes trading records) to be maintained in writing or electronically provided they may be 'reproduced in a written form'<sup>6</sup>.

ASX GN33 also provided useful guidance on areas upon which brokers could rely on records maintained by ASX, which now form part of the *Market Integrity Rules*<sup>7</sup>.

As to the specific proposals for guidance on formatting and information to be provided in response to ASIC requests in Proposal B5 above, our Members have consistently made the following comments:

- it would be excessively time consuming;
- it would require the creation of documents not the production of documents;
- ASIC may not always require *all* the information in the two 'Files' listed in Proposal B5. Surveillance requests should be limited to trading and clients upon which ASIC is focused and not otherwise;
- time for development of such a system would be from 3 – 12 months;
- cost of IT development to achieve ASIC's request are estimated at between \$25,000 and \$300,000 per firm;
- it would be a big challenge to design the optimal framework to integrate and consolidate the capture, retention and output interface for the required data, and, to promote automation of the retrieval process as best as possible, based on and feeding into existing systems & processes;
- while most brokers record orders electronically, it would be more onerous for businesses - or a unit within a business - that maintains hardcopy order records only, as permitted under the law. The proposed requirements would mean that the data would have to be manually reconstructed in electronic form for each ASIC request, or alternatively, a new electronic system would need to be introduced to accommodate the requirements;
- many brokers use a third party IT system for order entry. Some use a different system for cash equities and derivatives. Fulfilling the Commission's preferences would mean engaging the IT provider to produce new reports and features, which is always an

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<sup>6</sup> *Corporations Act* section 1306

<sup>7</sup> Rule 4.1.5 and 4.1.6

expensive and time-consuming exercise. Moreover, experience shows that Brokers do not always benefit from economies of scale in this regard;

- additional complexity is added where brokers execute for non-market participants, custodians or overseas brokers, where certain of the client information may follow on allocation, or be retained. These situations would add complexity to the task of producing trading records in the format requested by ASIC.

While the proposal may make surveillance inquiries more convenient for ASIC, such convenience to ASIC would be outweighed by the inconvenience, cost and unreasonable burden to the industry. It is not for our Members to ensure that ASIC has appropriate systems. Brokers will continue to use their best efforts to comply with the rules as they stand.

Moreover, the matters addressed in Proposal B5 are substantive, and should not be introduced via ASIC policy. If ASIC wishes to proceed with their introduction, they should be only introduced through a formal Rule change process, which must be approved by the Minister<sup>8</sup>, rather than updating a Regulatory Guide which may de facto become a requirement.

## OTHER MATTERS

We would also like to take the opportunity to mention two matters not specifically covered in CP152, but relevant to the further review of ASX policy and the rules. Both of these matters have been raised previously by us.

### 1. Removal of Duplication

For a number of years the Association has noted and sought the removal of substantive requirements that were previously duplicated in the *ASX Market Rules* and the *Corporations Act*. Since 1 August 2010 these same duplications exist in the *ASIC Market Integrity Rules* and the *Corporations Act*. It is therefore pleasing to see that ASIC proposes a staged process to address these duplicated provisions. While the Working Paper only addresses one of them - the time for retention of trading records (7 years in the MIR compared to 5 years in the Act/Regs) - we note that ASIC intends to address a number of other areas of duplication or inconsistency.

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<sup>8</sup> *Corporations Act* section 798G(3)

We have been advised that CP152, while it is the first step in the conversion of ASX policy (via Guidance Notes) to ASIC Policy (via Regulatory Guides), is not the start of a review of the policy and market integrity rules flagged in RG214.

As noted in our submission to Treasury on the Draft Market Supervision Bill in December 2009, duplication and/or inconsistency has existed between the *Corporations Act* and ASX Rules for a number of years, which the Association has been active in lobbying for resolution.

We set out below for completeness our full list of duplication areas, noting that ASIC plans to address certain of them (the relevant *Market Integrity Rule* and *Corporations Act* provision shown in parenthesis):

- Confirmations (Rule 3.4/s.1017F)
- Managed Discretionary Accounts (Rule 3.3 etc/CO04/194)
- Staff Trading (Rule 5.4/s.991F)
- Trading Records (Rule 4.1/s.991D)
- Trust Accounts (Rule 3.5/Pt 7.8 Div 2)
- Client order priority (Rule 5.1/s.991C)
- Principal trading (Rule 3.2/s.991E)
- Complaints (Rule 4.2.2/s.912A(1)(g), etc<sup>9</sup>)
- Insurance/compensation (Rule 2.2 – s.912B)
- Financial Records & Audit (Rule 4.2.1 etc/Pt 7.8 Div 6)
- Breach Reporting (s.912D - we note that this is considered in CP145), and
- Responsible Manager v. Responsible Executive requirements.

Together with the transition of ASX policy to ASIC, we very much look forward to the forthcoming review of the rules. This is the ideal opportunity to streamline and rationalise these various requirements, which will be of benefit to market participants, market operators and clients alike. We commend ASIC for flagging the commencement of the process and look forward to assisting in it.

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<sup>9</sup> The complaints provisions of the current Market Integrity Rules and the *Act* are not exactly the same. For example, the *Corporations Act* requirements (s912A(1)(g); s912B) only apply to complaints by retail clients, while the Market Integrity Rule on complaints registration and handling applies to all complaints. Under licence conditions, ASIC also expects that licensees have sufficient resources to handle complaints. Accordingly, the Complaints handling and registration requirements under the *Market Integrity Rules* may be superfluous, in view of the other obligations on complaint handling.

## **2. General Operational obligations**

*Management structures/plans flexibility:* As you would be aware from our past discussions and submissions our Members are very concerned about the overly prescriptive approach that ASX took to Management Plans. In most cases ASX effectively demanded to 'sign-off' or positively approve Management Plans. We do not see this as the role of a regulator. It is up to the licensee/participant to ensure compliance with the various management and supervision requirements. There is no argument with that. It should however be left up to the licensee/participant to make the arrangements to ensure compliance, in a manner that is appropriate to each firm. We trust that this approach will be reflected in ASIC policy.

Thank-you for the opportunity to comment on this policy. We are particularly grateful for the opportunity to comment on an earlier Working Draft of the Consultation Paper. Should you have any further inquiries, please contact Doug Clark, Policy Executive ([dclark@stockbrokers.org.au](mailto:dclark@stockbrokers.org.au)).

**Stockbrokers Association of Australia**

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