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27 March 2013

Manager, Capital Markets Unit
Corporations and Capital Markets Division
The Treasury
Langton Crescent, Parkes ACT 2600

Attention: Amy Little

By email: financialmarkets@treasury.gov.au

Dear Ms. Little,

Clarification of uncertainty relating to coverage of market compensation regimes under Part 7.5 of the Corporations Act

Thank-you for forwarding the Treasury Issue Paper *Clarification of Part 7.5 compensation arrangements* dated March 2013.

Until the anomaly identified in the Issue Paper was brought to our attention, we assumed that the **'default position'** applied. That is, if the client has not nominated the Exchange on which an order is to be executed, the client will be entitled to the protection of the NGF; if they nominate Chi-X, the Division 3 scheme will apply.

As discussed in the Issue Paper, it would appear that the **'Schedule version'** of the relevant provision (subsection 885D(2)) does not reflect this default position. This version was intended to apply to the situation where one market operator had both NGF and Division 3 compensation arrangements, for example, where ASX operates both an equities (NGF) and a futures (Div.3) market.

That the 'Schedule version' is now law is a concern, as it has introduced uncertainty as to the relevant compensation scheme.

The 'Schedule version' clearly did not anticipate the 'dual participant' scenario that we now have, that is, where one firm may be a participant of more than one exchange which conduct markets in the same products. Since 2011, this has been the case in Australia, where ASX-listed products are traded on both ASX and Chi-X. Most major firms are now participants of ASX and Chi-X.

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As to timing, it is crucial that this uncertainty is removed as quickly as possible. While Chi-X has operated since 2011, a recent regulatory change brings the issue into sharper focus.

On 1 March 2013, the **Best Execution Rule**¹ came into full effect after an 18-month transition period. This means that participants are required to obtain the best outcome (e.g. price) for clients trading in products traded on more than one exchange, namely ASX and Chi-X. For most brokers who are participants of both exchanges, compliance with this rule has meant the adoption of systems called '**smart order routers**'. These systems automatically send orders to the exchange which give the better outcome, for example, price. While it is possible to set parameters, this means that brokers may not know on which exchange an order will be executed, at the time of entry. Therefore, with Best Execution, any compensation scheme that depends on the client's instructions as to execution venue has just become even more problematic, since the client hardly ever gives such an instruction.

We therefore agree that it is desirable that the apparent uncertainty regarding coverage of compensation schemes be removed as a matter of urgency, and the 'default position' restored. We also agree with the drafting solution proposed.

Thank-you for the opportunity to comment on this proposal. We would be happy to discuss this matter further with you at your convenience. Should you require any further information, please contact me or Doug Clark, Policy Executive on dclark@stockbrokers.org.au.

Yours sincerely,



David W Horsfield
Managing Director/CEO

¹ ASIC Market Integrity Rules (Competition in Exchange Markets) 2011 Rule 3