

22 August 2019

Mr Andrew McPherson
Senior Specialist
Market Infrastructure
Australian Securities & Investments Commission
Level 5, 100 Market Street
SYDNEY NSW 2000

By email: rules.resilience@asic.gov.au

Dear Mr McPherson

**ASIC CONSULTATION PAPER CP 314 – PROPOSED MIRS FOR
TECHNOLOGICAL AND OPERATIONAL RESILIENCE
SUBMISSION FROM STOCKBROKERS AND FINANCIAL ADVISERS
ASSOCIATION**

We refer to ASIC Consultation Paper CP 314 issued on 27 June 2019 (“CP 314”) proposing amendments to Securities and Futures Market Integrity Rules (MIRs) in respect of technological and operational resilience. The Stockbrokers and Financial Advisers Association (SAFAA) appreciates the opportunity to provide the comments below in relation to CP 314.

SAFAA members understand the reason for ASIC directing attention on non-financial areas of risk, such as operational and technological risk. Market Participants appreciate that the increasing utilization of electronic systems for execution, trading and settlement present risks that require prudent management.

From the feedback SAFAA received, larger Market Participants, particularly those operating within global groups or who operate significant electronic trading businesses, have established frameworks that may better equip them to meet detailed and prescriptive rules such as those proposed in CP 314.

However, many firms operating a more traditional broking model are likely to require a substantial change to systems, processes, arrangements and resourcing, depending on how much flexibility may exist with respect to the MIRs proposed in CP 314. There were concerns generally expressed that the proposed MIRs could have a substantial impact on the costs of doing business for many firms within the small to medium sector of the market, but the benefits to the market and to investors of applying the highest level of requirements were highly questionable, as indeed was the purpose of doing so.

As you will see, Members have concerns that they cannot at this stage estimate what the cost and timing requirements of implementing the proposals in CP 314 are likely to be, in view of lack of clarity about some of the key terms used in the MIRs. However, an overarching comment made by Members was that, given the comprehensive nature of the proposals, the 6 month **implementation period** that is being proposed is **not sufficient**.

We summarise below the feedback received from Members according to the broad themes expressed.

Comments

1. Reasons for the proposals

We know of no failures by Market Participants that give rise to the need to re-cast the existing, principles based MIRs.

It appears to Members that the reason for the proposals in CP 314 was that other jurisdictions had passed rules with this level of detail, and accordingly ASIC was looking to follow them.

Members do not consider that this is a sufficient reason for replacing MIRs that are working. The new Rules will bring a whole raft of administrative cost and effort without a corresponding benefit. CP 314 fails the cost: benefit test.

Furthermore, as we set out below, there are a many issues with the wording of the proposed MIRs that will make their implementation, and ongoing compliance, a very costly exercise.

2. Uncertainty and vagueness of key terms

Members acknowledge that CP 314 uses language that incorporates some flexibility for Participants. Whilst Members are supportive of principles-based rules in general, they have highlighted that key elements of the MIRs are vague and uncertain. This, coupled with the introduction of a raft of specific MIRs, each bearing a very high financial penalty for non-compliance, has led Members to consider that the framework is highly onerous, in the absence of greater clarity being given.

One example cited by all Members was the meaning of the term “critical system”.

Note 1 to the definition states that the term:

...would generally include but are not limited to, functions, infrastructure, processes and systems that deliver or support order acceptance, routing and entry, clearing and settlement of transactions, payments and deliveries of financial products and funds, accounting for or reconciling client money, trust accounts, securities and funds, confirmations and regulatory data reporting.”

We note that elsewhere CP 314 states that the term will also include trade surveillance systems.

This is extremely broad. It is left open to much interpretation as to what is and is not included. On a conservative reading, not much is left out, but query how practical such an interpretation would be. For a smaller firm with only the most basic of electronic order routing and execution, the volume of work that an expansive view of this definition would require would be enormous.

There are other terms that are similarly vague or which are so broad that it makes it difficult to understand what is actually required, or to anticipate the time that will be required to implement the required changes. An example is the distinction between what constitutes an “incident” and what is a “major event”.

Members were strongly of the view that more clarity is required as to how ASIC would approach a situation where different Market Participants reached different conclusions as to the interpretation of some of these terms, such as one firm concluding that a system was not a “critical system” whereas another firm concluded that it was.

3. Timing and Cost

In view of the uncertainty of key terms, common feedback from Members was that they were not able to offer estimates or comments on the likely cost and timing of

implementation of the new framework, until more clarity was provided as to what was required.

Members indicated that there should be a follow-on round of consultation after additional clarification is provided, at which they will in a better position to provide this information.

4. Key Third parties not subject to the framework

A number of Members highlighted that a major issue with the effectiveness of the proposals in CP 314, and the ability of Market Participants to meet the obligations set out in it, is the fact that key third parties, in particular, system vendors, whose cooperation is required in order to make the arrangements work, are not subject to the framework (or any regulatory framework, for that matter). Without the ability to bring those parties into the framework, it may prove difficult for Market Participants to comply with what is expected of them under the MIRs.

For example, a number of the requirements as to outsourcing and other such matters are likely to necessitate Market Participants re-negotiating contractual arrangements with those parties.

Some parties may have no interest in renegotiating anything. Some may be global entities, which may want a single form of agreement with all customers, and may have no appetite for separate terms applying in various jurisdictions.

Some may be prepared to make changes, but may seek to extract higher charges for doing so, which will mean higher costs for the end-client. Members stressed that this could have a considerable impact on the question of cost (see our comments under section 3 above).

Some system providers will deal with multiple firms, or in some cases, the vast majority of Market Participants. It is sub-optimal for the majority of the Market Participants to be seeking to engage in the same negotiations with the one entity, not only from the point of view of duplication of this process, but certainly also from the point of view of the vendor.

Ideally, consideration needs to be given to some mechanism that would bring these to within the framework so that Market Participants can be in a better position to deliver the outcomes that ASIC is looking for more efficiently and cost effectively.

In relation to system testing and certification, there has always been an issue of requiring every Market Participant, who has bought the same system, to undertake the same duplicate process for the same system. A more efficient approach is called for.

5. Conflict with other regulatory frameworks

Members have expressed concern as to how the ASIC framework will sit with the growing number of regulatory frameworks that are being applied to the areas of data management and cyber risk.

In particular, the potential for conflict with APRA requirements has been raised by Market Participants who are part of an APRA-regulated group, as well as conflict with the operation of the Notifiable Data Breach reporting regime that has recently come into force.

6. Notification of major events

Members questioned what use ASIC will make of all of the “immediate” notification by a Market Participant of a “major event”, and whether the later report after seven days should not serve as sufficient notification by itself. Given the high level of detail that is inherent in the proposals, removing any step that does not serve any useful purpose will assist in managing the additional cost and resourcing that the framework will involve.

7. Impact on small and medium Market Participants

As mentioned earlier, whilst some of the Larger Market Participants, and those which have a significant AOP business model, may have adopted many or a number of the processes relating to technology that are set out in CP 314, firms with a more traditional business model, particularly at the small and medium end, may not have.

Members questions the extent to which some of the measures, particularly those relating to change management and Business Continuity Planning, are needed, or are justified in view of the cost versus such benefit as may be delivered.

As regards back-up, will every firm be required to have a back-up site, with all of the significant costs that maintaining such a site will entail? To require this for all firms is highly questionable.

Without wishing to diminish the significance of continuity of service to clients, an outage in the execution system employed by a small broker may not represent nor have the same market impact as that of a top 10 broker. The difference between executing a trade now, as opposed to later in the day when a system outage has been rectified, may not impact a retail client to the same extent as it would a large fund manager or institutional client, for whom any delay could be critical.

At the smaller to medium end, minimization of cost is highly important to a firm's business model and their service offering to their clients. For this reason, Members expressed concern about mandating an operational and technical framework on this sector of the market that equated to a top tier broker, that could seriously impact on their cost structure. This would inevitably impact on the cost of the services they provide for clients, and can potentially make their business non-viable.

It would not be a good outcome if the regulatory framework were to have the anti-competitive effect of imposing a cost structure that forced middle to lower tier of broking firms out of the market. This would hardly be ensuring the resilience of services to the client.

8. Implementation Period

Noting our comments above regarding the difficulties that members expressed in making estimates about the likely timeframe and resources needed to implement the proposals, in the absence of more clarity, there was nevertheless a widespread view that 6 months would not be sufficient time in which to undertake the necessary reviews of existing arrangements and implement the types of changes that CP 314 was indicating. There was widespread agreement that a longer implementation period would be needed.

CONCLUSION

SAFAA appreciates the opportunity to comment on the Proposals in CP314. We would be happy to discuss any issues arising these comments, or to provide any further material that may assist. Should you require any further information, please contact Peter Stepek, Policy Executive, on (02) 8080 3200 or email pstepek@stockbrokers.org.au.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Andrew Green', with a stylized flourish at the end.

Andrew Green
Chief Executive