

**ASIC MARKET INTEGRITY RULES (COMPETITION IN EXCHANGE MARKETS)
AMENDMENT 2014 (NO. 1)
EXPLANATORY STATEMENT**

Prepared by the Australian Securities and Investments Commission

Corporations Act 2001

The Australian Securities and Investments Commission (*ASIC*) makes the *ASIC Market Integrity Rules (Competition in Exchange Markets) Amendment 2014 (No. 1)* (the *Instrument*) under subsection 798G(1) of the *Corporations Act 2001* (the *Corporations Act*). Capitalised terms used in this Explanatory Statement (e.g. “Participant”) are defined in the *ASIC Market Integrity Rules (Competition in Exchange Markets) 2011* (the *ASIC Market Integrity Rules (Competition)*).

1. Enabling legislation

Subsection 798G(1) of the *Corporations Act* provides that ASIC may, by legislative instrument, make rules that deal with the following:

- (a) the activities or conduct of licensed markets;
- (b) the activities or conduct of persons in relation to licensed markets;
- (c) the activities or conduct of persons in relation to financial products traded on licensed markets.

The ASIC Market Integrity Rules (Competition) deal with the activities and conduct of licensed markets on which certain Financial Products (Equity Market Products, CGS Depository Interests and ASX SPI 200 Futures) are traded. Those Financial Products are currently traded on the licensed markets operated by ASX Limited (*ASX*), Chi-X Australia Pty Ltd (*Chi-X*) and Australian Securities Exchange Limited (*ASX 24*). The ASIC Market Integrity Rules (Competition) apply as specified in the Rules to Participants and Market Operators of those markets.

2. Background

Crossing Systems

On 5 August 2013, ASIC made the *ASIC Market Integrity Rules (Competition in Exchange Markets) Amendment 2013 (No. 2)*. That instrument amended the disclosure requirements under the ASIC Market Integrity Rules (Competition) for a Participant that operates one or more Crossing Systems.

‘Crossing Systems’ are automated services provided by a Participant that match or execute Orders of the Participant’s clients with Orders of:

- (a) the Participant;
- (b) other clients of the Participant; or
- (c) any other person whose Orders access the automated service,

otherwise than on an Order Book.

The purpose of the amendments, which took effect in November 2013, was to improve transparency about Crossing Systems and to ensure there is publicly available information about, among other things, where client Orders may be matched or executed (i.e. in the Crossing System operated by the Participant, or in other Crossing Systems operated by third parties).

Under the ASIC Market Integrity Rules (Competition) as amended, a Participant is required to make disclosures about each of its Crossing Systems by providing certain information to ASIC in a 'Crossing System Initial Report' (Rule 4A.2.1) and also by making certain information available free of charge on a publicly accessible website (Rule 4A.3.1).

The information to be disclosed under Rules 4A.2.1 and 4A.3.1 includes information about Order flows between Crossing Systems. Participants sought clarification from ASIC about whether those Rules also required disclosure of information about Order flows between Participants that operate Crossing Systems, and about Order flows that occur via another person ('Aggregator') (e.g. another Participant that operates an aggregation algorithm and transmits Orders between Crossing Systems and Participants that operate Crossing Systems). In November 2013, ASIC released FAQ A1¹ clarifying that all such Orders flows should be disclosed under the Rules.

Regulatory Data

On 20 November 2012, ASIC made the *ASIC Market Integrity Rules (Competition in Exchange Markets) Amendment 2012 (No. 1)*. That instrument amended the ASIC Market Integrity Rules (Competition) by inserting Chapter 5A. Under Chapter 5A, a Participant is required to provide the following data (***Regulatory Data***) on Orders and Trade Reports from 10 March 2014 (the ***Compliance Start Date***):

- (a) the execution venue;
- (b) the capacity in which the Participant is acting (agent, principal, or both);
- (c) the origin of the Order or Transaction (e.g. client account identifier);
- (d) the intermediary ID (i.e. AFS licence number); and
- (e) flagging of directed wholesale Orders or Transactions.

Since the time Chapter 5A was introduced, Participants have requested additional time to implement, and facilitate an orderly roll-out of system changes for, the Regulatory Data obligations.

3. Purpose of the legislative instrument

Crossing Systems

The purpose of items [1] to [5] of Schedule 1 of the Instrument is to amend Rules 4A.2.1 and 4A.3.1 to clarify that those Rules require disclosure of Order flows between Participants that operate Crossing Systems, and Order flows that occur via an Aggregator, in addition to Order flows between Crossing Systems. The purpose of this change is to reflect in the Rules the clarification previously made in FAQ A1.

Regulatory Data

¹ <http://asic.gov.au/asic/ASIC.NSF/byHeadline/FAQs-Market-structure>

The purpose of item [6] of Schedule 1 of the Instrument is to extend the Compliance Start Date for the Regulatory Data obligation for Participants to 28 July 2014.

Details of the Instrument are contained in [Attachment A](#).

4. Consultation

Crossing Systems

ASIC consulted on its proposal to make the *ASIC Market Integrity Rules (Competition in Exchange Markets) Amendment 2013 (No. 2)* (the instrument that amended the disclosure requirements for Participants that operate Crossing Systems) through *Consultation Paper 202 Dark liquidity and high-frequency trading: Proposals* (CP 202) released on 18 March 2013. As part of that consultation process, ASIC also held meetings with industry stakeholders and information sessions for members of the Australian Financial Markets Association (*AFMA*), the Financial Services Council (*FSC*) and the Stockbrokers Association of Australia (*SAA*).

ASIC has consulted on its proposal to clarify the operation of the Crossing System obligations through direct discussions with Participants that operate Crossing Systems. Following those discussions, ASIC clarified the intended operation of Rules 4A.2.1 and 4A.3.1 in FAQ A1. The changes at items [1] to [5] of Schedule 1 of the Instrument reflect the clarifications made in FAQ A1.

Regulatory Data

ASIC consulted on its proposal to make the *ASIC Market Integrity Rules (Competition in Exchange Markets) Amendment 2012 (No. 1)* (the instrument that introduced the Regulatory Data obligations) through:

- (a) ASIC Consultation Paper 145 *Australian equity market structure: Proposals* (CP 145) released on 4 November 2010;
- (b) ASIC Consultation Paper 168 *Australian equity market structure: Further proposals* (CP 168) released on 20 October 2011;
- (c) ASIC Consultation Paper 179 *Australian market structure: Draft market integrity rules and guidance* (CP 179) released on 28 June 2012; and
- (d) meetings with stakeholders throughout the consultation process and information sessions for members of AFMA, the FSC and SAA.

ASIC consulted on the proposal to extend the Compliance Start Date for the Regulatory Data obligation to 28 July 2014, through direct discussions with ASX, Chi-X and Participants of the ASX and Chi-X Markets. There was broad support for the change, which was made in response to Participants requesting additional time to implement the Regulatory Data obligations.

5. Penalties

Subsection 798G(1) of the Corporations Act provides that market integrity rules are legislative instruments for the purposes of the *Legislative Instruments Act 2003*.

Subsection 798G(2) of the Corporations Act provides that market integrity rules may include a penalty amount for a rule. A penalty amount must not exceed \$1,000,000. The penalty amount set out

below a rule is the penalty amount for that rule. The Instrument does not affect the penalties payable in relation to any Rule.

6. Commencement of the Instrument

The Instrument will commence in accordance with the Commencement information in the Instrument, being on the day after the day on which the Instrument is registered under the *Legislative Instruments Act 2003*.

7. Statement of Compatibility with Human Rights

A Statement of Compatibility with Human Rights is included in this Explanatory Statement at **Attachment B**.

8. Regulation Impact Statement

Crossing Systems

The amendments to the disclosure requirements for Participants that operate Crossing Systems were the subject of Regulation Impact Statement: *Australian market structure: Further proposals* in June 2013. That Regulation Impact Statement was lodged on the Federal Register of Legislative Instruments (FRLI) with the *ASIC Market Integrity Rules (Competition in Exchange Markets) Amendment 2013 (No. 2)*.

Regulatory Data

The introduction of the Regulatory Data obligations was the subject of Regulation Impact Statement: *Australian equity markets: Further proposals* in October 2012. That Regulation Impact Statement was lodged on FRLI with the *ASIC Market Integrity Rules (Competition in Exchange Markets) Amendment 2012 (No. 1)*.

A further Regulation Impact Statement was not required for this Instrument as it is minor or machinery in nature and does not substantially alter the existing requirements for Participants the subject of the Regulation Impact Statements referred to above.

ATTACHMENT A

Paragraph 1 – Enabling Legislation

This paragraph provides that the Instrument is made, with the written consent of the Minister, under subsection 798G(1) of the *Corporations Act 2001*.

Paragraph 2 – Title

This paragraph provides that the title of the Instrument is the *ASIC Market Integrity Rules (Competition in Exchange Markets) Amendment 2014 (No. 1)*.

Paragraph 3 – Commencement

This paragraph provides that the Instrument commences on the day after the day on which the Instrument is registered under the *Legislative Instruments Act 2003*.

Paragraph 4 – Amendments

This paragraph provides that Schedule 1 of the Instrument amends the *ASIC Market Integrity Rules (Competition in Exchange Markets) 2011*.

Schedule 1 – Amendments

Item [1] Paragraph 4A.2.1(1)(b)

Item [1] of Schedule 1 to the Instrument omits the words “and whether the Crossing System transmits Orders to other Crossing Systems, or receives Orders from other Crossing Systems” from Rule 4A.2.1(1)(b). This change has been made because the requirement in Rule 4A.2.1(1)(b) to provide information about whether the Crossing System transmits Orders to other Crossing Systems, or receives Orders from other Crossing Systems, has been replaced by the requirement in new Rule 4A.2.1(1)(ba) (see item [2] below).

Item [2] After paragraph 4A.2.1(1)(b)

Item [2] of Schedule 1 to the Instrument inserts a new paragraph (ba) in Rule 4A.2.1(1). New paragraph (ba) provides that a Participant that operates, or proposes to operate, a Crossing System must lodge with ASIC a report which describes, if applicable, the information required by item 5, column 3 of the Table in subrule 4A.3.1(2). This change will ensure that ASIC receives in a Crossing System Initial Report the same information that a Participant is required to disclose in its Publicly Available Crossing System Information under item 5 of the Table in Rule 4A.3.1(2), as revised by item [3].

Item [3] Subrule 4A.3.1(2), Table item 5

Item [3] of Schedule 1 to the Instrument omits item 5 of the Table in Rule 4A.3.1(2) and substitutes a revised item 5.

Revised item 5 requires that if Orders may be executed or matched in another Crossing System because they are transmitted by the Participant or by the Participant's Crossing System:

- (a) to one or more other Crossing Systems or to a Participant that operates a Crossing System; or

- (b) to another person (an *Aggregator*) who further transmits the Orders to one or more other Crossing Systems or to a Participant that operates a Crossing System,

or if Orders may be executed or matched in the Participant's Crossing System with Orders received (whether directly, or via an Aggregator) from a Crossing System operated by another Participant, or from a Participant that operates a Crossing System, then the Participant must include the following information in its Publicly Available Crossing System Information:

- (c) the code identifying the other Crossing System;
- (d) the legal name of the Participant that operates the other Crossing System; and
- (e) for each Crossing System and Participant identified under paragraphs (c) and (d), whether Orders are transmitted to, or received from the other Crossing System or Participant (whether directly, or via an Aggregator), or both.

Revised item 5 clarifies the matters that a Participant must disclose in its Publicly Available Crossing System Information, in accordance with the clarification provided in ASIC FAQ A1.

Item [4] After the Table in subrule 4A.3.1(2)

Item [4] of Schedule 1 to the Instrument inserts a note. The note provides an example of person that may be an 'Aggregator' for the purposes of item 5 of the Table in Rule 4A.3.1(2), such as another Participant that receives Orders and operates an aggregation algorithm that transmits received Orders to one or more other execution venues (licensed markets, or other Crossing Systems).

Item [5] Paragraph 5A.1.1(1)(b)

Item [5] of Schedule 1 to the Instrument replaces the date "10 March" in Rule 5A.1.1(1)(b) with "28 July". This change means that Participants will now have until 28 July 2014 to start complying with the requirements in Chapter 5A of the Rules to provide Regulatory Data on Orders and Trade Reports.

ATTACHMENT B

Statement of Compatibility with Human Rights

Prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011

ASIC Market Integrity Rules (Competition in Exchange Markets) Amendment 2014 (No. 1)

This Legislative Instrument is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

A. Overview of the legislative instrument

1. The Legislative Instrument is made under subsection 798G(1) of the *Corporations Act 2001 (Corporations Act)* and amends the ASIC Market Integrity Rules (Competition in Exchange Markets) 2011 (*ASIC Market Integrity Rules (Competition)*). The ASIC Market Integrity Rules (Competition) apply to the activities and conduct of licensed markets on which certain Financial Products (Equity Market Products, CGS Depository Interests and ASX SPI 200 Futures) are traded. Those Financial Products are currently traded on the licensed markets operated by ASX Limited (*ASX*), Chi-X Australia Pty Ltd (*Chi-X*) and Australian Securities Exchange Limited (*ASX 24*). The ASIC Market Integrity Rules (Competition) apply as specified in the Rules to Participants and Market Operators of those markets.

Crossing Systems

2. On 5 August 2013, ASIC made the *ASIC Market Integrity Rules (Competition in Exchange Markets) Amendment 2013 (No. 2)*. That instrument amended the disclosure requirements under the ASIC Market Integrity Rules (Competition) for a Participant that operates one or more Crossing Systems². The purpose of the amendments, which took effect in November 2013, was to improve transparency about Crossing Systems and to ensure there is publicly available information about, among other things, where client Orders may be matched or executed (i.e. in the Crossing System operated by the Participant, or in other Crossing Systems operated by third parties).
3. In November 2013, ASIC released FAQ A1³ clarifying that the information to be disclosed under Rules 4A.2.1 and 4A.3.1 includes information about Order flows between Participants that operate Crossing Systems, and about Order flows that occur via another person (an 'Aggregator')⁴, in addition to Order flows between Crossing Systems. This Legislative Instrument amends Rules 4A.2.1 and 4A.3.1 to clarify the operation of those Rules in accordance with ASIC's FAQ A1.

Regulatory Data

² 'Crossing Systems' are automated services provided by a Participant that match or execute Orders of the Participant's clients with Orders of the Participant, other clients of the Participant, or any other person whose Orders may access the service, otherwise than on an Order Book.

³ <http://asic.gov.au/asic/ASIC.NSF/byHeadline/FAQs-Market-structure>

⁴ An 'Aggregator' may be, for example, another Participant that operates an aggregation algorithm and transmits Orders between Crossing Systems and Participants that operate Crossing Systems.

4. On 20 November 2012, ASIC made the *ASIC Market Integrity Rules (Competition in Exchange Markets) Amendment 2012 (No.1)*. That instrument amended the ASIC Market Integrity Rules (Competition) by inserting Chapter 5A. Under Chapter 5A, a Participant is required to provide the following data (**Regulatory Data**) on Orders and Trade Reports from 10 March 2014 (the **Compliance Start Date**):
 - (a) the execution venue;
 - (b) the capacity in which the Participant is acting (agent, principal, or both);
 - (c) the origin of the Order or Transaction (e.g. client account identifier);
 - (d) the intermediary ID (i.e. AFS licence number); and
 - (e) flagging of directed wholesale Orders or Transactions.
5. This Legislative Instrument amends paragraph 5A.1.1(1)(b) of the ASIC Market Integrity Rules (Competition) to extend the Compliance Start Date for the Regulatory Data obligation for Participants to 28 July 2014. This change was made in response to requests by Participants for additional time to implement, and facilitate an orderly roll-out of system changes for, the Regulatory Data obligations.

B. Human rights implications

6. This Legislative Instrument does not have any effect on human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011* because it does not engage any of the applicable rights or freedoms.

C. Conclusion

7. The Legislative Instrument is compatible with human rights as it does not raise any human rights issues.

D. Consultation

Crossing Systems

8. ASIC consulted on its proposal to make the *ASIC Market Integrity Rules (Competition in Exchange Markets) Amendment 2013 (No. 2)* (the instrument that amended the disclosure requirements for Participants that operate Crossing Systems) through *Consultation Paper 202 Dark liquidity and high-frequency trading: Proposals* (CP 202) released on 18 March 2013. As part of that consultation process, ASIC also held meetings with industry stakeholders and information sessions for members of the Australian Financial Markets Association (*AFMA*), the Financial Services Council (*FSC*) and the Stockbrokers Association of Australia (*SAA*).
9. ASIC has consulted on its proposal to clarify the operation of the Crossing System obligations through direct discussions with Participants that operate Crossing Systems. Following those discussions, ASIC clarified the intended operation of Rules 4A.2.1 and 4A.3.1 in FAQ A1.

Regulatory Data

10. ASIC consulted on its proposal to make the *ASIC Market Integrity Rules (Competition in Exchange Markets) Amendment 2012 (No. 1)* (the instrument that introduced the Regulatory Data obligations) through:

- (a) ASIC Consultation Paper 145 *Australian equity market structure: Proposals* (CP 145) released on 4 November 2010;
- (b) ASIC Consultation Paper 168 *Australian equity market structure: Further proposals* (CP 168) released on 20 October 2011;
- (c) ASIC Consultation Paper 179 *Australian market structure: Draft market integrity rules and guidance* (CP 179) released on 28 June 2012; and
- (d) meetings with stakeholders throughout the consultation process and information sessions for members of AFMA, the FSC and SAA.

11. ASIC consulted on the proposal to extend the Compliance Start Date for the Regulatory Data obligation to 28 July 2014, through direct discussions with ASX, Chi-X and Participants of the ASX and Chi-X Markets. There was broad support for the change, which was made in response to Participants requesting additional time to implement the Regulatory Data obligations.

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