

EXPLANATORY STATEMENT for

ASIC Market Integrity Rules (Securities Markets) Class Waiver 2018/298

Prepared by the Australian Securities and Investments Commission

ASIC Market Integrity Rules (Securities Markets) 2017

The Australian Securities and Investments Commission (**ASIC**) makes ASIC Market Integrity Rules (Securities Markets) Class Waiver 2018/298 (the **instrument**) under subrule 1.2.1(1) of the *ASIC Market Integrity Rules (Securities Markets) 2017* (the **Rules**).

Under subrule 1.2.1(1) of the Rules, ASIC may relieve any person or class of persons from the obligation to comply with a provision of the Rules.

Unless indicated to the contrary, capitalised terms in this Explanatory Statement have the same meaning as in the Rules.

1. Background

Consolidation of the market integrity rules

As part of its supervisory responsibilities, ASIC reviewed the 14 market integrity rule books in force in late 2016 and identified the need to consolidate certain market integrity rule books which covered substantively similar existing obligations across like domestic licensed markets.

In Consultation Paper 277 *Proposals to consolidate the ASIC market integrity rules (CP 277)*, ASIC proposed to consolidate the Pre-Commencement Market Integrity Rules to create a single set of market integrity rules for the ASX, Chi-X, IR Plus, NSX and SSX Markets.

Following public consultation, ASIC made the Rules in November 2017. Generally, the Rules maintain the substance of the regulatory regime embodied in market integrity rules (the **Pre-Commencement Market Integrity Rules**) applicable prior to the commencement of the Rules, including the *ASIC Market Integrity Rules (ASX Market) 2010*. The Rules will repeal the Pre-Commencement Market Integrity Rules on 7 May 2018.

Upon the repeal of the Pre-Commencement Market Integrity Rules, ASIC Waivers made under the Pre-Commencement Market Integrity Rules will also be repealed, including ASIC Class Waiver [CW 15/932].

[CW 15/932] provides conditional relief from subrule 3.5.8(1) and paragraph 3.5.10(a) of the ASX Rules. Subrule 3.5.8(1) and paragraph 3.5.10(a) of the ASX Rules correspond to subrule 3.5.8(1) and paragraph 3.5.10(a) of the Rules respectively.

In Report 547 *Response to submissions on CP 277 Proposals to consolidate the ASIC market integrity rules (REP 457)* ASIC announced that as part of its project to consolidate the market integrity rules it would remake existing individual and class waivers under the Rules before 7 May 2018.

Subrule 3.5.8(1) and Rule 3.5.10

Subrule 3.5.8(1) requires a Market Participant to perform a daily reconciliation of the aggregate balance held by the Market Participant at the close of business on each Business Day in its clients' segregated account (*CSA*), and the corresponding balance as recorded in the Market Participant's accounting records. This daily reconciliation must be performed by 7.00 pm on the Trading Day after the Trading Day to which the reconciliation relates.

The purpose of the daily reconciliation is to ensure that all client money related to Futures Market Transactions is properly segregated and accounted for in the *CSA*. The Rules require this reconciliation to be completed on a daily basis and in a timely fashion to ensure that any deficiencies in the *CSA* are quickly identified and corrected.

Rule 3.5.10 of the Rules requires a Market Participant to notify ASIC, in writing, within two Business Days if:

- (a) a reconciliation has not been performed in accordance with Rule 3.5.8 (paragraph 3.5.10(a)); or
- (b) according to a reconciliation performed pursuant to Rule 3.5.8, Total Deposits is less than Total Third Party Client Monies (paragraph 3.5.10(c)).

[CW 15/932]

ASIC granted [CW 15/932] after considering an application from a Market Participant who sought additional time to perform the required daily reconciliations on the basis that it relies on information obtained from various overseas parties in order to complete the reconciliation accurately. The receipt of this information from overseas parties is affected by, among other factors, differences in time zones. The applicant submitted that, due to the need to obtain this information from overseas parties, it was not always practicable for it to complete the reconciliation accurately in the time mandated by subrule 3.5.8(1) of the ASX Rules.

Following targeted consultation, ASIC considered it appropriate to provide relief by way of class waiver to all Market Participants where similar circumstances apply, rather than individual waiver to the applicant alone.

2. Purpose of the instrument

The purpose of the instrument is to relieve Market Participants in certain circumstances from the obligation under subrule 3.5.8(1) of the Rules to perform daily reconciliations by 7.00 pm on the next Trading Day of the aggregate balance held in the *CSA* at the close of business on each Business Day. The instrument has the effect

of extending this deadline to 12.00 pm on the second Trading Day after the Trading Day to which the reconciliation relates.

The relief from subrule 3.5.8(1) of the Rules applies where a Market Participant is ordinarily unable to perform the reconciliation by 7.00 pm on the next Trading Day because they rely on information obtained from a person outside Australia in order to perform the reconciliation.

The instrument also provides relief from the obligation under paragraph 3.5.10(a) of the Rules to notify ASIC, in writing, within two Business Days, if the reconciliation has not been performed by 7.00 pm on the next Trading Day.

ASIC accepts that, in the case of Market Participants that require information from overseas parties for the completion of CSA reconciliations, the deadline in subrule 3.5.8(1) imposes an unnecessary compliance burden and carries an associated risk of inaccuracies in the reconciliation.

The instrument reduces the compliance burden for those Market Participants by providing an extension of time to perform their daily CSA reconciliation. At the same time, the instrument ensures that those reconciliations are performed more thoroughly and accurately, and without significantly increasing the risk to client money.

The availability of information from overseas parties can be affected by a range of factors including differences in time zones.

Once the Market Participants receive the requisite information from the overseas parties, they also require sufficient time to perform a robust and meaningful reconciliation and to investigate and resolve any issues in the reconciliation process. In circumstances where errors are encountered, or the Market Participant experiences delays caused by internal or external factors (for example, internal system failures or delay in the receipt of information from a third party), this can result in a failure by the Market Participant to meet the deadline stipulated in subrule 3.5.8(1) of the Rules.

In order to complete the CSA reconciliation within the time frame stipulated in subrule 3.5.8(1) of the Rules, a Market Participant may be required to rely on information that is incomplete or provisional and this may result in a reconciliation process that is less accurate or less thorough. This increases the risk that client money is not properly segregated and accounted for, resulting in inadequate protection of client money.

ASIC considers that the risk of a short, conditional extension of the deadline for completing daily CSA reconciliations is outweighed by the risk and regulatory burden that subrule 3.5.8(1) of the Rules imposes on Market Participants who are reliant on information from overseas parties.

Notifications required under the conditions of the relief are generally consistent with the current requirements under the Rules to notify ASIC in these circumstances where the reconciliation is not performed, is completed late or where the reconciliation reveals a deficiency in the CSA. However, ASIC has reduced the notification period from two Business Days (as required under the Rules) to one Business Day (under the

instrument). This is to ensure that reporting times are consistent under the Rules and under the instrument.

3. Operation of the instrument

Name of legislative instrument

Section 1 of the instrument provides that the name of the instrument is *ASIC Market Integrity Rules (Securities Markets) Class Waiver 2018/298*.

Commencement

Section 2 of the instrument provides that the instrument commences on the day after the instrument is registered on the Federal Register of Legislation.

Authority

Section 3 of the instrument provides that the instrument is made under subrule 1.2.1(1) of the Rules.

Interpretation

Subsection 4(1) of the instrument provides that in the instrument, unless the contrary intention appears, capitalised terms have the same meaning as in the Rules.

Subsection 4(2) of the instrument provides that in the instrument a reference to time is to the time in Sydney, Australia.

Time for reconciliation of clients' segregated accounts

Subsection 5(1) of the instrument provides that a Market Participant does not have to comply with subrule 3.5.8(1) of the Rules for so long as the Market Participant performs the reconciliation referred to in that subrule by 12.00 pm on the second Trading Day after the Trading Day to which the reconciliation relates.

Subsection 5(2) of the instrument provides that the relief in subsection 5(1) of the instrument applies where the Market Participant is ordinarily unable to perform the reconciliation referred to in subrule 3.5.8(1) of the Rules by 7.00 pm on the Trading Day after the Trading Day to which the reconciliation relates, because the Market Participant relies on information obtained from a person located outside Australia to perform the reconciliation referred to in that subrule.

Time for notifying ASIC in respect of reconciliation

Section 6 of the instrument provides that a Market Participant does not have to comply with paragraph 3.5.10(a) of the Rules for so long as the Market Participant notifies ASIC, in writing, within one Business Day if a reconciliation has not been performed by 12.00 pm on the second Trading Day after the Trading Day to which the reconciliation relates.

Conditions

Section 7 of the instrument provides that it is a condition of the relief in subsection 5(1) of the instrument that where the Market Participant performs the reconciliation referred to in subrule 3.5.8(1) on the second Trading Day after the Trading Day to which the reconciliation relates, the Market Participant must notify ASIC, in writing, within one Business Day if:

- (a) the reconciliation has not been performed in accordance with Rule 3.5.8 (except to the extent that Rule requires the Market Participant to perform the reconciliation by 7.00 pm on the Trading Day after the Trading Day to which the reconciliation relates); or
- (b) according to the reconciliation, Total Deposits is less than Total Third Party Client Monies.

4. Consultation

ASIC consulted with the Australian Financial Markets Association (*AFMA*) and members of the AFMA Futures Steering Committee before making [CW 15/932].

AFMA and its members supported ASIC's proposal for the extension of time, but they indicated that the consensus view of the members was that a full day extension to 7.00 pm on the second Trading Day was preferred. No arguments were provided in support of the full day extension.

When making [CW 15/932] ASIC concluded that an extension of time to 12.00 pm on the second Trading Day struck an appropriate balance between the compliance burden on Market Participants and the importance of protecting client money through a requirement to produce timely reconciliations. Timely reconciliations are an important client money protection because they provide an early alert to potential deficiencies. By requiring the reconciliation to be completed by 12.00 pm on the second Trading Day, [CW 15/932] ensured that any investigation of a potential deficiency could commence during business hours on the second Trading Day.

ASIC also consulted with AFMA and its members on the likely effect of [CW 15/932] on compliance costs. AFMA (on behalf of its members) confirmed that [CW 15/932] would not result in any cost savings. Rather, the effect of [CW 15/932] is that reconciliations can be performed accurately and without breaching the existing requirements under the market integrity rules.

The instrument is part of a wider project to consolidate the market integrity rules. ASIC consulted extensively with market operators, market participants and industry bodies before making the Rules and the instrument.

The consultation period for Consultation Paper 277 *Proposals to consolidate the ASIC market integrity rules (CP 277)* occurred between 24 January 2017 and 7 March 2017. ASIC held over 25 meetings with stakeholders during and following that period. In addition, ASIC consulted ASIC's Market Advisory Panel on the proposals. ASIC received five non-confidential submissions and six confidential submissions to CP

277 from a broad range of stakeholders including from market participants, market operators and industry associations.

The Office of Best Practice Regulation has assessed the proposals implemented by the Rules and the instrument as having a minor impact on business, community organisations or individuals and confirmed that no further analysis, in the form of a Regulatory Impact Statement is required (OBPR ID 22449).

Statement of Compatibility with Human Rights

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

ASIC Market Integrity Rules (Securities Markets) Class Waiver 2018/298

ASIC Market Integrity Rules (Securities Markets) Class Waiver 2018/298 (the *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*.

Overview

The Australian Securities and Investments Commission (*ASIC*) makes this instrument under subrule 1.2.1(1) of the *ASIC Market Integrity Rules (Securities Markets) 2017* (the *Rules*). Under subrule 1.2.1(1), ASIC may relieve any person or class of persons from the obligation to comply with a provision of the Rules.

Subrule 3.5.8(1) requires a market participant to perform a daily reconciliation of the aggregate balance held by the market participant at the close of business on each business day in its clients' segregated account (*CSA*), and the corresponding balance as recorded in the market participant's accounting records. This daily reconciliation must be performed by 7.00 pm on the trading day after the trading day to which the reconciliation relates.

The purpose of the daily reconciliation is to ensure that all client money related to futures market transactions is properly segregated and accounted for in the CSA. The reconciliation is required to be performed in a timely fashion to ensure that any deficiencies in the CSA are quickly identified and corrected.

Rule 3.5.10 requires a market participant to notify ASIC, in writing, within two business days if:

- (a) a reconciliation has not been performed in accordance with Rule 3.5.8 (paragraph 3.5.10(a) of the Rules); or
- (b) according to a reconciliation performed pursuant to Rule 3.5.8, total deposits is less than total third party client monies (paragraph 3.5.10(c) of the Rules).

The instrument relieves market participants, in certain circumstances, from the obligation under subrule 3.5.8(1) to perform daily CSA reconciliations by 7.00 pm on the next trading day. The relief from subrule 3.5.8(1) applies in the case where a market participant is ordinarily unable to perform the reconciliation referred to in subrule 3.5.8(1) by 7.00 pm on the next trading day, because the market participant relies on information from a person outside Australia to perform this reconciliation.

The instrument also relieves market participants from the obligation under paragraph 3.5.10(a) to notify ASIC, in writing, within two business days, if the reconciliation has not been performed by 7.00 pm on the next trading day.

Notifications required under the conditions of the relief from subrule 3.5.8(1) are generally consistent with the current requirements under the Rules to notify ASIC in these circumstances where the reconciliation is not performed, is completed late or where the reconciliation reveals a deficiency in the CSA. However, ASIC has reduced the notification period from two Business Days (as required under the Rules) to one Business Day (under the instrument). This is to ensure that reporting times are consistent under the Rules and under the instrument.

The instrument reduces the compliance burden for those market participants by providing an extension of time to perform their daily CSA reconciliation. At the same time, the instrument ensures that those reconciliations are performed more thoroughly and accurately, and without significantly increasing the risk to client money.

Human rights implications

This legislative instrument does not engage any of the applicable rights or freedoms.

Conclusion

This legislative instrument is compatible with human rights as it does not raise any human rights issues.

Australian Securities and Investments Commission