

ASIC CLASS RULE WAIVER [CW 15/932]

EXPLANATORY STATEMENT

Prepared by the Australian Securities and Investments Commission

ASIC Market Integrity Rules (ASX Market) 2010

The Australian Securities and Investments Commission (**ASIC**) makes this instrument under Rule 1.2.1(1) of the *ASIC Market Integrity Rules (ASX Market) 2010* (the **ASX Rules**).

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

Capitalised terms in this Explanatory Statement refer to defined terms in the ASX Rules.

1. Background

Rule 3.5.8(1) and Rule 3.5.10 of the ASX Rules

Under Rule 3.5.2 of the ASX Rules, Market Participants must hold money relating to Futures Market Transactions in an account designated as a clients' trust account or a clients' segregated account (CSA).

Rule 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 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 ASX 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 requires a Market Participant to notify ASIC, in writing, within two Business Days if:

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

Waiver Application

A Market Participant applied to ASIC for a waiver of Rule 3.5.8(1), on the condition that the time for completion of the daily reconciliation is extended to 12.00 pm on the second Trading Day after the Trading Day to which the reconciliation relates. The applicant sought additional time to perform the daily reconciliations on the basis that the applicant 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 Rule 3.5.8(1).

For the reasons set out in section 2 below, ASIC decided to grant the waiver. However, in making that decision in respect of this individual application, ASIC concluded that other Market Participants with similar business models (for example, Market Participants with clients located overseas) are likely to be similarly affected by the short time frame stipulated in Rule 3.5.8(1).

Following targeted consultation, we considered it appropriate to provide a waiver to all affected Market Participants by way of a class waiver rather than individual waiver to the applicant alone.

2. Purpose of the Class Rule Waiver

The purpose of this Class Rule Waiver is to relieve certain Market Participants from the obligation under Rule 3.5.8(1) 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 Class Rule Waiver 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 Market Participants to which the relief applies are Market Participants who are 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.

This Class Rule Waiver also relieves the same Market Participants from the obligation under Rule 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.

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

The Class Rule Waiver 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 Class Rule Waiver 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 Rule 3.5.8(1).

In order to complete the CSA reconciliation within the time frame stipulated in Rule 3.5.8(1), 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 Rule 3.5.8(1) imposes on Market Participants who are reliant on information from overseas parties.

The relief from Rule 3.5.8(1) is subject to two conditions. The first condition is that the Market Participant must perform the reconciliation by 12.00 pm on the second Trading Day after the Trading Day to which the reconciliation relates. This provides the Market Participant with additional time to complete their daily CSA reconciliation.

The second condition is that the Market Participant must notify ASIC, in writing, within one Business Day if:

1. the reconciliation has not been performed in accordance with Rule 3.5.8 (other than the requirement to perform the reconciliation by 7.00 pm on the next Trading Day);
2. the reconciliation indicates that there is a deficiency in the CSA.

The relief from Rule 3.5.10(a) is subject to a condition that the Market Participant must notify ASIC in writing within one Business Day if the reconciliation has not been performed by 12.00 pm on the second Trading Day.

These notification conditions are generally consistent with the current requirements under the ASX Rules to notify ASIC in these circumstances where the reconciliation is not performed or is completed late or where the reconciliation reveals a deficiency in the CSA. However, we have reduced the notification period from two Business Days (as required under the ASX Rules) to one Business Day (under the Class Rule Waiver). This is to ensure that reporting times are consistent under the ASX Rules and under the Class Rule Waiver.

3. Operation of the class rule waiver

Enabling provision - Paragraph 1

Paragraph 1 of the Class Rule Waiver provides that the enabling provision for the instrument is Rule 1.2.1(1) of the ASX Rules.

Title – Paragraph 2

Paragraph 2 of the Class Rule Waiver provides that the title of the instrument is ASIC Class Rule Waiver [CW 15/932].

Commencement - Paragraph 3

Paragraph 3 of the Class Rule Waiver provides that the instrument commences on the day on which the instrument is registered under the *Legislative Instruments Act 2003*.

Relief from Rule 3.5.8(1) - Paragraph 4

Paragraph 4 of the Class Rule Waiver relieves a Market Participant from the obligation to comply with Rule 3.5.8(1), only to the extent that rule requires the Market Participant to perform the daily CSA reconciliation by 7.00 pm on the Trading Day after the Trading Day to which the reconciliation relates.

The relief is subject to the condition that the Market Participant performs the daily CSA reconciliation by 12.00 pm on the second Trading Day after the Trading Day to which the reconciliation relates.

Case where the relief applies – Paragraph 5

Paragraph 5 of the Class Rule Waiver provides that the relief applies in the case where the Market Participant is ordinarily unable to perform the daily CSA reconciliation by 7.00 pm on the next Trading Day because the Market Participant relies on information obtained from a person located outside Australia to perform that reconciliation.

The use of the term 'ordinarily' means that the relief would continue to apply even if the information happened to be obtained earlier on a particular day and therefore the Market Participant was able to perform the reconciliation by 7:00 on next Trading Day, for that particular day. Given that the Market Participant would in most cases not be able to perform the reconciliation at that earlier time because they rely on overseas information, the Market Participant can continue to rely on the relief on this particular day notwithstanding that they could comply with Rule 3.5.8(1).

Notification Condition – Paragraph 6

Paragraph 6 of Class Rule Waiver provides that it is a condition of the relief in Paragraph 4, that 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 (other than the requirement to perform the reconciliation by 7.00 pm on the next Trading Day); or
- b) according to the reconciliation, Total Deposits is less than Total Third Party Client Monies.

Relief from Rule 3.5.10(a) and Notification Condition – Paragraph 7

Paragraph 7 of the Class Rule Waiver relieves a Market Participant from the obligation to comply with Rule 3.5.10(a), only to the extent that rule requires the Market Participant to notify ASIC that a reconciliation has not been performed by 7.00 pm on the Trading Day after the Trading Day to which the reconciliation relates.

The relief is subject to the condition that 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.

Interpretation – Paragraph 8

Paragraph 8 of the Class Rule Waiver provides that capitalised terms used in the Class Rule Waiver have the meaning given to them in the ASX Rules.

4. Consultation

ASIC consulted with the Australian Financial Markets Association (AFMA) and members of the AFMA Futures Steering Committee on the Class Rule Waiver, and in particular the additional time required to perform the daily CSA reconciliation.

AFMA and its members supported ASIC's proposal for an extension, 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.

ASIC concluded that an extension of time to 12.00 pm on the second Trading Day strikes 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, the Class Rule Waiver ensures that any investigation of a potential deficiency can still commence during business hours on the second Trading Day.

We also consulted with AFMA and its members on the likely effect of the Class Rule Waiver on compliance costs. AFMA (on behalf of its members) confirmed that the Class Rule Waiver did not result in any cost savings. Rather, the effect of the Class Rule Waiver is that reconciliations can be performed accurately and without breaching the existing requirements under the ASX Rules.

5. Statement of Compatibility with Human Rights

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

ATTACHMENT A

Statement of Compatibility with Human Rights

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

ASIC CLASS RULE WAIVER [CW 15/932]

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*.

1. Overview of the legislative instrument

The Australian Securities and Investments Commission (*ASIC*) makes this instrument under Rule 1.2.1(1) of the *ASIC Market Integrity Rules (ASX Market) 2010* (the *ASX Rules*).

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

Under Rule 3.5.2 of the ASX Rules, market participants must hold money relating to futures market transactions in an account designated as a clients' trust account or a clients' segregated account (CSA).

Rule 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 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:

1. a reconciliation has not been performed in accordance with Rule 3.5.8 (Rule 3.5.10(a)); or
2. according to a reconciliation performed pursuant to Rule 3.5.8, total deposits is less than total third party client monies (Rule 3.5.10(c)).

The Legislative Instrument applies in the case where a market participant is ordinarily unable to perform the reconciliation referred to in Rule 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 Legislative Instrument relieves those market participants from the obligation under Rule 3.5.8(1) to perform daily CSA reconciliations by 7.00 pm on the next trading day. It also relieves market participants from the obligation under Rule 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.

The relief from Rule 3.5.8(1) is subject to two conditions. The first condition is that the market participant must perform the reconciliation by 12.00 pm on the second trading day after the trading day to which the reconciliation relates. This provides the market participant with additional time to complete their daily CSA reconciliation.

The second condition is that the market participant must notify ASIC, in writing, within one business day if:

1. the reconciliation has not been performed in accordance with Rule 3.5.8 (other than the requirement to perform the reconciliation by 7.00 pm on the next trading day);
2. the reconciliation indicates that there is a deficiency in the CSA.

The relief from Rule 3.5.10(a) is subject to a condition that the market participant must notify ASIC in writing within one business day if the reconciliation has not been performed by 12.00 pm on the second trading day.

These notification conditions are generally consistent with the current requirements under the ASX Rules to notify ASIC in these circumstances where the reconciliation is not performed or is completed late or where the reconciliation reveals a deficiency in the CSA. However, we have reduced the notification period from two business days (as required under the ASX Rules) to one business day (under the Legislative Instrument). This is to ensure that reporting times are consistent under the ASX Rules and under the Legislative Instrument.

ASIC makes this Legislative Instrument because it accepts that, in the case of market participants that require information from overseas parties for the completion of CSA reconciliations, the deadline in Rule 3.5.8(1) imposes an unnecessary compliance burden and carries an associated risk of inaccuracies in the reconciliation.

The Legislative 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 Legislative Instrument ensures that those reconciliations are performed more thoroughly and accurately, and without significantly increasing the risk to client money.

2. Human rights implications

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.

3. Consultation

ASIC consulted with the Australian Financial Markets Association (AFMA) and members of the AFMA Futures Steering Committee on the Legislative Instrument, and in particular the additional time required to perform the CSA reconciliation.

AFMA and its members supported ASIC's proposal for an extension, 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.

ASIC concluded that an extension of time to 12.00 pm on the second trading day strikes 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, the rule ensures that any investigation of a potential deficiency can still commence during business hours on the second trading day.

We also consulted with AFMA and its members on the likely effect of the Legislative Instrument on compliance costs. AFMA (on behalf of its members) confirmed that the Legislative Instrument did not result in any cost savings. Rather, the effect of the Legislative Instrument is that reconciliations can be performed accurately and without breaching the existing requirements under the ASX Rules.