

ASIC MARKET INTEGRITY RULES (ASX MARKET-CAPITAL) 2014 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 (ASX Market-Capital) 2014* (the **ASIC Market Integrity Rules (ASX-Capital)**) under subsection 798G(1) of the *Corporations Act 2001* (the **Corporations Act**). Capitalised terms used in this Explanatory Statement (e.g. “Market Participant”) are defined in the ASIC Market Integrity Rules (ASX-Capital).

1. Enabling legislation

Subsection 798G(1) of the Corporations Act provides that ASIC may, by legislative instrument, make rules that deal with the activities or conduct of licensed markets and of persons in relation to licensed markets and financial products traded on licensed markets.

The ASIC Market Integrity Rules (ASX-Capital), along with the *ASIC Market Integrity Rules (ASX Market) 2010* (the **ASIC Market Integrity Rules (ASX)**), deal with the activities and conduct of the licensed market (the **ASX Market**) operated by ASX Limited (ACN 008 624 691) (**ASX**). From 26 May 2014, Market Participants of the ASX Market are required to comply with both the ASIC Market Integrity Rules (ASX) and the ASIC Market Integrity Rules (ASX-Capital).

2. Background

The ASIC Market Integrity Rules (ASX) were made by ASIC in August 2010. ASIC has amended the ASIC Market Integrity Rules (ASX) on a number of occasions, including in August 2011 to transfer responsibility for supervision of Market Participant capital requirements from ASX to ASIC.

All market integrity rules made by ASIC under subsection 798G(1) of the Corporations Act are legislative instruments and must be lodged for registration on the Federal Register of Legislative Instruments (**FRLI**), the Commonwealth database of legislative instruments maintained by the Office of Parliamentary Counsel (**OPC**). Each time ASIC amends the market integrity rules, ASIC is required to prepare and lodge for registration a FRLI a 'compilation' showing the rules as in force as at the date of the amendments.

In July 2013, the FRLI fee structure changed to recognise the whole-of-life cost of making material available to agencies and the public. Under the revised fee structure, ASIC is now required to pay a lodgement fee and a fee per page for each compilation of the market integrity rules it lodges for registration with FRLI. ASIC's costs for lodging compilations of the ASIC Market Integrity Rules (ASX) have increased significantly under this new fee structure.

ASIC has reviewed the ASIC Market Integrity Rules (ASX) to identify ways in which it can manage its FRLI lodgement costs in respect of compilations of those rules and has concluded that the most effective way to manage these costs is to transfer the market participant capital requirements in the ASIC Market Integrity Rules (ASX) into a separate rulebook for that market.

The market integrity rules setting out market participant capital requirements and associated capital forms comprise the bulk of the ASIC Market Integrity Rules (ASX) and accordingly will be a

significant contributing factor in the overall increase in ASIC's FRLI lodgement costs in respect of compilations of those rules. The market integrity rules setting out the capital requirements and capital forms have not been amended since they were introduced, and ASIC does not propose to amend the substance of the capital requirements at this time. ASIC therefore considers that the costs of continuing to lodge compilations of the ASIC Market Integrity Rules (ASX) that include the market participant capital requirements and associated capital forms, significantly outweigh the benefits of maintaining all of those rules within the same rulebook.

ASIC has also concluded that further cost efficiencies could be gained by reducing the number of separate capital forms in the schedules to the market integrity rules, as part of the same process.

ASIC has aligned the commencement date for these changes, with the commencement date for existing changes to Part 5.6 of the rules made by the *ASIC Market Integrity Rules (ASX Market) Amendment 2012 (No. 3)* that take effect on 26 May 2014. As a result ASIC will only be required to create a single compilation of the ASIC Market Integrity Rules (ASX Market) for the transfer of the capital requirements and the changes to Part 5.6. This approach is in accordance with guidance provided by OPC that agencies may make savings on their FRLI lodgement fees by aligning the commencement dates of amendments, to reduce the number of compilations needed. A reduction in the number of compilations also has the potential to reduce compliance costs for users of the market integrity rules.

3. Purpose of the legislative instrument

The ASIC Market Integrity Rules (ASX-Capital) repeal the capital requirements in Chapters 8 and 9 and Schedules 1A (including Annexures), 1B and 1C of the ASIC Market Integrity Rules (ASX) and 're-make' the capital requirements as Chapters 8 and 9 and Schedules 1A (including Annexures), 1B and 1C of the ASIC Market Integrity Rules (ASX-Capital). The purpose of this change is to enable ASIC to manage its FRLI lodgement costs in respect of compilations of the ASIC Market Integrity Rules (ASX). Details of the ASIC Market Integrity Rules (ASX-Capital) are contained in **Attachment A**.

4. Consultation

On 30 April 2014 ASIC wrote to Market Operators of the APX, ASX, ASX 24, Chi-X and FEX Markets, the Australian Bankers' Association (ABA), Australian Financial Markets Association (AFMA), the Financial Services Council (FSC) and the Stockbrokers Association of Australia (SAA), seeking feedback on the proposed changes to the market integrity rules to transfer market participant capital requirements into a separate rulebook for each market, and streamline the capital forms. Generally respondents were supportive of the proposal, with a number suggesting that ASIC take additional steps to 'consolidate' the capital rulebooks of the APX, ASX, ASX 24, Chi-X and FEX Markets into a single rulebook. No other significant issues were raised.

5. Penalties

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 ASIC Market Integrity Rules (ASX-Capital) maintains the same penalties that were payable in relation to breaches of the capital requirements under the ASIC Market Integrity Rules (ASX).

6. Commencement of the Instrument

The ASIC Market Integrity Rules (ASX-Capital) will commence on the later of 26 May 2014 and the day on which the ASIC Market Integrity Rules (ASX-Capital) instrument are 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

A Regulation Impact Statement was not required for the ASIC Market Integrity Rules (ASX-Capital) as it is minor or machinery in nature and does not substantially alter the existing requirements for Market Participants.

ATTACHMENT A

Chapter 1: Introduction

Part 1.1: Preliminary

Part 1.1 of the ASIC Market Integrity Rules (ASX-Capital) reflects Part 1.1 of the ASIC Market Integrity Rules (ASX). ASIC makes the rules under subsection 798G(1) of the Corporations Act (Rule 1.1.1). The title of the rules is the *ASIC Market Integrity Rules (ASX Market-Capital) 2014* (Rule 1.1.2). The rules will commence on the later of 26 May 2014 and the day on which the instrument is registered under the *Legislative Instruments Act 2003* (Rule 1.1.3).

The ASIC Market Integrity Rules (ASX-Capital) apply to the activities and conduct of the ASX Market, and of persons in relation to the ASX Market and in relation to Financial Products traded on the ASX Market (Rule 1.1.4). The Market Operator, Market Participants, and any other entities prescribed by regulations made under section 798H of the Corporations Act as being required to comply with the market integrity rules, must comply with the rules as specified in the rules (Rule 1.1.5).

In the ASIC Market Integrity Rules (ASX-Capital), conduct engaged in by on behalf of a person by officers, Employees or other agents of the person, or by any other person at the direction or with the consent or agreement (whether express or implied) of an officer, Employee or agent of the person, is deemed to have been engaged in by the person (Rule 1.1.6). Where is necessary to establish the state of mind of a person for the purposes of the rules in respect of conduct engaged in by the person, it is sufficient to show that an officer, Employee or other agent of the person by whom the conduct was engaged in, had that state of mind (Rule 1.1.7).

Part 1.2: Waiver

Part 1.2 of the ASIC Market Integrity Rules (ASX-Capital) reflects Part 1.2 of the ASIC Market Integrity Rules (ASX). ASIC may relieve a person or any class of persons from the obligation to comply with provisions of the rules, either generally or in a particular case or category, and either unconditionally or subject to such conditions as ASIC thinks fit (Rule 1.2.1), and may specify the period or specific event during which the relief will apply (Rule 1.2.3). If any conditions on a waiver are imposed, all of the conditions must be complied with for the waiver to be effective (Rule 1.2.1(2)) and failure to comply with a condition is a breach of Rule 1.2.2. ASIC may withdraw a waiver in writing at any time (Rule 1.2.1(3)).

A waiver, conditions on a waiver and a request by a person for a waiver must be in writing, and ASIC may publish notice of a waiver (subrules 1.2.1(4), (5) and (6)). ASIC may also establish, maintain and publish a register for recording details of relief, in accordance with Rule 1.2.4.

Part 1.3: Notice, notification and service of documents

Part 1.3 of the ASIC Market Integrity Rules (ASX-Capital) reflects Part 1.3 of the ASIC Market Integrity Rules (ASX). A Market Participant must have email for the purpose of receiving notices under the rules (Rule 1.3.1). ASIC may give notice to a Market Participant under the Rules by a number of methods set out in Rule 1.3.2.

Part 1.4: Interpretation

Part 1.4 of the ASIC Market Integrity Rules (ASX-Capital) sets out provisions for interpreting the rules and reflects Part 1.4 of the ASIC Market Integrity Rules (ASX). In the rules, references to time are to the time in Sydney, Australia (Rule 1.4.1). Words and expressions defined in the Corporations Act will unless otherwise defined or specified in the rules or the contrary intention appears, have the same meaning in the rules (Rule 1.4.2).

Rule 1.4.3 provides definitions for terms used in the rules. Those defined terms reflect definitions in Rule 1.4.3 of the ASIC Market Integrity Rules (ASX) that applied to Chapters 8 and 9 and Schedules 1A (including Annexures), 1B and 1C of the ASIC Market Integrity Rules (ASX).. There are additional definitions specified in Chapters 8 and 9 and Schedule 1A.

Part 1.5: Repeal

Part 1.5 of the ASIC Market Integrity Rules (ASX-Capital) provides for the repeal of the capital requirements from the ASIC Market Integrity Rules (ASX). Rule 1.5.1 provides that Chapters 8 and 9, and Schedules 1A (including Annexures), 1B and 1C of the ASIC Market Integrity Rules (ASX) are repealed. Those provisions are replaced by Chapters 8 and 9, and Schedules 1A (including Annexures), 1B and 1C of the rules.

Chapters 2 to 7

There is no Chapters 2 to 7 in the rules. To maximise consistency between the capital requirements under these rules and the ASIC Market Integrity Rules (ASX), the numbering of the capital requirements in the ASIC Market Integrity Rules (ASX) has been maintained.

Chapter 8: Capital requirements

Chapter 8 of the ASIC Market Integrity Rules (ASX-Capital) replaces, and is identical to, Chapter 8 of the ASIC Market Integrity Rules (ASX). Chapter 8 of the rules sets out the core obligation on a Market Participant of the ASX Market to comply with the Capital Requirements. A Market Participant must at all times comply with the Risk-Based Capital Requirements in Schedule 1A to the rules, unless the Market Participant:

- is only a Principal Trader; or
- has elected to comply with NTA Requirements in Schedule 1B (available to Market Participants that have Trading Permission for Futures Market Transactions only); or
- is a Clearing Participant of ASX Clear and complies with the capital requirements under the ASX Clear Operating Rules.

Chapter 9: Accounts and audit

Chapter 9 of the ASIC Market Integrity Rules (ASX-Capital) replaces, and is with minor exceptions identical to, Chapter 9 of the ASIC Market Integrity Rules (ASX). Chapter 9 of the rules sets out the core reporting requirements for a Market Participant of the ASX Market that complies with the Risk-Based Capital Requirements or the NTA Requirements.

Part 9.2 requires Market Participants complying with the Risk-Based Capital Requirements to submit to ASIC Ad Hoc, Summary, Monthly and Annual Risk-Based Returns, related Risk-Based Return Declarations (and in the case of partnerships, bi-annual statutory declarations) at the times specified.

ASIC was able to reduce three of the four different returns relating to the Risk-Based Capital Requirements in Schedule 1C to a single 'master' return from which other returns can be derived. In order to accommodate this change, new Rule 9.2.1A sets out definitions for the Ad-Hoc, Summary, Monthly and Annual Audited Risk-Based Returns and related Risk-Based Return Declarations. These definitions act as signposts to the relevant sections of the streamlined 'master' returns and declaration in Schedule 1C. References to the form numbers in Schedule 1C throughout the remainder of Chapter 9 have been replaced with the defined terms.

The forms in Form 3B (Parts 1 and 2) and Form 4B (Parts 1 and 2) were bespoke capital returns for partnerships and have been removed because they were only used by one Market Participant. ASIC may direct a Market Participant that is a partnership to continue to prepare and deliver bespoke monthly returns and declarations (see revised Rule 9.2.3(1)(c) and (d) and Rule 9.2.4(1)(f) and (g)). Partnerships remain required to submit bi-annual statutory declarations (Rule 9.2.5).

Part 9.3 requires Market Participants complying with the NTA Requirements to submit to ASIC Ad Hoc, Summary, Monthly and Annual NTA Returns and related NTA Return Declarations at the times specified.

ASIC was able to reduce three of the four different returns relating to the NTA Requirements in Schedule 1C to a single 'master' return from which other returns can be derived. In order to accommodate this change, new Rule 9.3.1A sets out definitions for the Ad-Hoc, Summary, Monthly and Annual Audited NTA Returns and related NTA Return Declarations. These definitions act as signposts to the relevant sections of the streamlined 'master' returns and declaration in Schedule 1C. References to the form numbers in Schedule 1C throughout the remainder of Chapter 9 have been replaced with the defined terms.

A Market Participant may continue to submit certain of its returns and declarations using the ASX Return Lodgement and Monitoring System as provided in Rule 9.4.2. A Market Participant must continue to assist its auditor in any audit conducted under Part 9.2 or 9.3 (see Rule 9.5.1).

Schedule 1A (including Annexures) – Capital liquidity requirements

Schedule 1A of the ASIC Market Integrity Rules (ASX-Capital) replaces, and with the exception of a small number of references to the streamlined capital return forms, is identical to, Schedule 1A of the ASIC Market Integrity Rules (ASX). Schedule 1A sets out the Risk-Based Capital Requirements, which require a Market Participant to maintain at all times 'Liquid Capital' greater than the Market Participant's 'Total Risk Requirement' and 'Core Capital' of \$100,000 or more (subject to use of Approved Subordinated Debt).

Annexures 1 to 5 of Schedule 1A of the ASIC Market Integrity Rules (ASX-Capital) replace, and are identical to, Annexures 1 to 5 of Schedule 1A to the ASIC Market Integrity Rules (ASX). Annexures 1 to 5 provide for methods by which Market Participants must calculate the counterparty risk amount, counterparty large exposure risk amount, issuer large exposure risk amount and position risk amounts for the purposes of determining their 'Total Risk Requirement'.

Schedule 1B – NTA requirements

Schedule 1B replaces, and is identical to, Schedule 1B of the ASIC Market Integrity Rules (ASX). Schedule 1B sets out the NTA Requirements, which require a Market Participant to have at all times NTA (calculated as the sum of the values of the assets (both non-current and current) owned by the Market

Participant less the sum of any liabilities (secured and unsecured) attaching to those assets or to the Market Participant) of at least \$1,000,000.

Schedule 1C

Schedule 1C of the ASIC Market Integrity Rules (ASX-Capital) sets out the following forms in relation to the Risk-Based Capital Requirements:

- Form 1 (Part 1) – the Ad-Hoc Risk Based Return;
- Form 2 (Part 2) – the "Risk-Based Return Declaration", which can be adapted for use in respect of Annual Audited, Monthly, and Summary Risk-Based Returns;
- Form 3A (Part 1) – from which the Annual Audited, Monthly and Summary Risk-Based Returns are now derived;
- Form 5 – the Auditors' report on the Annual Audited Return;
- Form 6 – the Key Risks and Internal Systems Statement; and
- Form 7 – the Partnership Statutory Declaration.

Schedule 1C of the ASIC Market Integrity Rules (ASX-Capital) sets out the following forms in relation to the NTA Requirements:

- Form 8 (Part 1) –from which the Ad-Hoc, Annual Audited and Monthly NTA Returns are now derived;
- Form 8 (Part 2) – the "NTA Return Declaration", which can be adapted for use in respect of Ad-Hoc, Annual Audited, Monthly, and Summary NTA Returns; and
- Form 9 (Part 1) – the "Summary NTA Return".

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 (ASX Market-Capital) 2014

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 Instrument

The *ASIC Market Integrity Rules (ASX Market-Capital) 2014* (the **Legislative Instrument**), along with the *ASIC Market Integrity Rules (ASX Market) 2010* (the **ASIC Market Integrity Rules (ASX)**), deal with the activities and conduct of the licensed market (the **ASX Market**) operated by ASX Limited (ACN 008 624 691) (**ASX**).

The Legislative Instrument repeals the capital requirements Chapters 8 and 9, and Schedules 1A (including Annexures), 1B and 1C of the ASIC Market Integrity Rules (ASX), and 're-makes' those capital requirements as Chapters 8 and 9, and Schedules 1A (including Annexures), 1B and 1C of the Legislative Instrument. The capital requirements in the Legislative Instrument are substantially identical to the capital requirements in the ASIC Market Integrity Rules (ASX).

The purpose of the Legislative Instrument is to reduce ASIC's costs for lodging compilations of the ASIC Market Integrity Rules (ASX). Those costs have increased significantly under the new fee structure for lodgements on the Federal Register of Legislative Instruments (FRLI) introduced in July 2013.

Following the introduction of the new fee structure, ASIC conducted a review of the rules to identify ways in which ASIC could manage its FRLI lodgement costs in respect of compilations of the ASIC Market Integrity Rules (ASX). ASIC concluded the most straightforward and efficient way to manage those costs was to separate the capital requirements into a separate set of rules. The Legislative Instrument achieves this outcome.

B. Human rights implications

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

C. Conclusion

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

D. Consultation

On 30 April 2014 ASIC wrote to Market Operators of the APX, ASX, ASX 24, Chi-X and FEX Markets, the Australian Bankers' Association (ABA), Australian Financial Markets Association (AFMA), the Financial Services Council (FSC) and the Stockbrokers Association of Australia (SAA), seeking feedback on the proposed changes to the market integrity rules to transfer market participant capital requirements into a separate rulebook for each market, and streamline the capital

forms. Generally respondents were supportive of the proposal, with a number suggesting that ASIC take additional steps to 'consolidate' the capital rulebooks of the APX, ASX, ASX 24, Chi-X and FEX Markets into a single rulebook. No other significant issues were raised.

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