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Senate Standing Committees on Economics  
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## **Inquiry into the performance of the Australian Securities and Investments Commission (ASIC)**

ASX is pleased to be invited to make a submission to the Committee's inquiry into the performance of ASIC. ASX's submission is focussed on the terms of reference that relate to matters that ASX has direct engagement with, namely: ASIC's enabling legislation and ability to fulfil its responsibilities; the accountability framework to which ASIC is subject; and ASIC's collaboration with other regulators.

There is a small group of financial regulators (ASIC, RBA, APRA and Treasury) that play a critical role in establishing and enforcing a regulatory framework that has a high impact on critical economic outcomes. These include: financial stability; investor/consumer protection; and facilitating efficient markets that will foster the growth and international competitiveness of Australia's capital markets and support Australian economic growth.

ASX believes that Australia's financial services regulation has, by and large, been working well and that the regulators, including ASIC, have been performing their role well. The ability of Australia to avoid some of the excesses that led to the Global Financial Crisis (GFC) can be attributed, in part, to Australia's regulatory framework and policy settings.

As a leading financial services provider ASX has strong working relationships with its two primary regulators ASIC and the RBA.

ASX has extensive contact with ASIC across all aspects of our business. As the holder of a market operator's licence and licences to run clearing and settlement facilities ASX Group entities are required to be assessed annually against its licence obligations. There are also requirements for its clearing and settlement facilities to be in compliance with the RBA's Financial Stability Standards and its facilities are subject to annual assessment against those obligations.

ASX and ASIC also work closely together on matters relating to ASIC's administration of their market surveillance and participant oversight obligations and in the context of our shared role in the enforcement of the continuous disclosure requirements. These processes work well with regular meetings and exchanges of information.

ASX is also required to go through a Ministerial disallowance process for all listing and operating rule changes. As a result of this we work closely with ASIC throughout the rulemaking process. Over recent times there have been improvements in that process and ASIC has shown a willingness to actively engage with ASX on the business case and risks of product and service innovations, as well as acknowledge critical timing issues. We believe this has improved the timeliness of ASIC's responses to ASX business initiatives.

While assessing past performance is important it is even more important to look to the future and the challenges that will confront Australian businesses, which are relatively small players in an increasingly global marketplace. Just as many Australian businesses (such as ASX) are striving to be globally connected and internationally competitive – our regulators also need to understand the impact domestic regulatory settings have on Australian businesses and Australia's ability to continue to attract capital and to efficiently allocate it to its most productive uses.

Recent changes to regulatory arrangements in Australia and overseas, some of which are still working their way through the system, have naturally focussed on enhancing financial system stability following the experience of the GFC. It is timely now for industry and regulators to turn our focus to growing our markets and ensuring they continue to underpin Australia's relative strong economic performance.

Achieving optimal policy outcomes requires that all regulations/market structure changes should be subject to a robust 'top down' cost-benefit analysis by regulatory and policy agencies. Such an analysis should satisfy a number of criteria:

- Does the reform benefit end users – corporations, fund managers, investors?
- Can regulators continue to secure the stability of financial markets?
- Does the change support Australia's competitive position and its ambition to be a regional financial centre?

Going forward regulators, including ASIC, will need to be assessed against their ability to promote policy changes that meet all three of these criteria.

ASX also has a productive working relationship with the Treasury as the organisation responsible for advising the Commonwealth Government on public policy issues relating to capital markets and financial services.

The following sections briefly outline ASX's views on particular elements of the Committee's terms of reference as they apply to ASIC's responsibilities for regulation of Australia's securities markets.

### **ASIC's enabling legislation and whether any barriers prevent ASIC from fulfilling its legislative responsibilities and obligations**

There do not appear to be any particular barriers to ASIC fulfilling its regulatory responsibilities and obligations. In recent times, ASIC has been given increased powers with regards to responsibility for front-line market surveillance to identify and police market misconduct and to supervise market participant activities.

Shortly after the responsibility for market surveillance and participant supervision were transferred from ASX, ASIC was given new rulemaking powers, the boundaries of which are prescribed within overarching legislation and are targeted at enhancing market integrity. These regulatory powers require a public consultation process to be conducted with stakeholders and are subject to final Ministerial approval. ASX supported the conferral of these rulemaking powers to provide ASIC with the ability to respond quickly to any emerging policy challenges without the delays that normally accompany legislative change.

These arrangements appear to have worked relatively well to date.

The success of such regulatory arrangements, however, are highly dependent on ASIC (or other financial regulators) undertaking rigorous cost-benefit analysis prior to proposing regulatory change.

It is important that in making these assessments ASIC (and other regulators) reach out to end customers to ensure their views are captured and reflected in any cost-benefit analysis rather than just the impact on intermediaries in the financing chain. These key customer groups include both investors (retail and institutional) as well as borrowers (eg listed companies).

For example, ASX supported the rigorous approach ASIC has taken in reviewing issues such as the impact of the changing nature of dark liquidity and the growth of high frequency trading (HFT) may have on market quality and market integrity. By carefully studying the issues and publishing reports that provide independent, fact-based analysis ASIC has enabled a more informed and broader public debate on perceived problems and the available policy responses.

The policy development process and ultimate policy settings ASIC has established have attracted significant positive attention from other jurisdictions. Australia is seen as being proactive in managing these issues before they begin to significantly affect market quality and undermine public confidence, as they have in other countries.

ASX is a member of the Business Council of Australia (BCA) and supports the principles the BCA identified as the key to promoting a well-functioning regulatory system (see box below). These principles are as relevant to all financial regulators as to other Government regulatory bodies.

#### BCA Principles of a High Performing Regulatory System<sup>1</sup>

- **The problem to be solved is well understood:** before government seeks to regulate, it must understand the problem or policy priority in depth and test the case for regulation, along with the risks and consequences of not regulating a particular activity.
- **New regulation is subject to cost-benefit analysis:** the costs of new regulation are thoroughly assessed and tested with the community through cost-benefit analysis, which includes an explicit understanding of the costs to the community including business.
- **Regulation achieves its objectives at least cost:** regulation is carefully targeted to achieve its stated objectives and minimise the cost impacts on the community including business.
- **Regulators perform efficiently:** regulation is administered by regulators in the most efficient manner possible to facilitate economic progress.
- **Regulation is constantly reviewed:** existing regulation is constantly reviewed from first principles through new Regulation Impact Statements, with regulations amended or removed if it cannot be established that they are appropriately targeted to an ongoing risk or problem.

It is clear that the approach to regulation and to policy making processes must be designed to deliver regulatory settings that make our markets work better and which produce net benefits to the community.

There already are practical examples where ASIC has applied such principles in considering and, where necessary, rejecting policy solutions. For example, in its review of dark liquidity and HFT, ASIC identified policy options (eg minimum resting times for small orders and a narrowing in tick sizes for some securities) that did not receive wide-spread industry support or seem to pass a rigorous cost-benefit analysis. Feedback indicated that the implementation and ongoing compliance costs would have been significant while the measures would be unlikely to achieve the desired policy objectives. Based on that industry feedback and their own policy analysis ASIC decided not to proceed with those measures and instead focussed on policies where the benefits would be likely to exceed the costs.

The success of such an approach depends critically on the skill sets within the regulators. ASX notes that ASIC has been active in hiring people with a diverse range of backgrounds, particularly those with a commercial/business background to broaden the organisation's skill sets. This has been reflected in the degree of practical expertise and market insights they have been able to bring to a range of complex policy issues. In an area like financial services it is imperative that ASIC keeps up to date with emerging market trends. The steps ASIC has taken to broaden its skills base shows a clear intent to achieve this.

#### The accountability framework to which ASIC is subject and whether it needs to be strengthened

As noted above, ASX believes that the regulatory framework for financial services operates relatively well in Australia. That said, it is important that processes are in place to ensure that regulation is provided in the most efficient and effective manner possible.

Parliament and its relevant committees have a critical role in providing external oversight of Australia's regulatory agencies. High degrees of transparency into both the policy development and the policy enforcement processes are also vital to enable scrutiny of the regulator's activities and to enhance public confidence that they are fulfilling their regulatory mandates.

<sup>1</sup> Business Council of Australia, *Standards for Rule Making*, p7

The case for having effective external review arrangements that can drive greater regulatory efficiency are strengthened when industry are also directly funding those activities. The introduction of the ASIC cost recovery arrangements in January 2012 will see around \$20 million per annum being funded by market users over coming years. Such an arrangement demands transparent accountability processes that can provide industry with confidence that the money is being well spent.

From ASX's perspective such accountability arrangements should raise few concerns for regulatory authorities such as ASIC, as they are able to fulfil their regulatory obligations in a relatively efficient manner. Such processes should, however, lead to ongoing and incremental efficiencies that will provide benefits to both the regulators and their regulated parties.

For example, regulatory agencies must have specific targets and resources that balance the critical importance of a well regulated financial market with the need to grow the economy and advance Australia's competitive position and with the need to minimise the cost of regulation on businesses and consumers

### **The workings of ASIC's collaboration, and working relationships, with other regulators and law enforcement bodies**

As noted above ASX has two primary regulators to which it subject (ASIC and the RBA), as well as having direct contacts with Treasury (in its role as a policy adviser to the Government) and to a lesser extent APRA (as the regulator of some of ASX's largest participants/customers).

There is an intersection of responsibilities across regulators particularly with regards to ASX's clearing and settlement facilities where ASIC has responsibilities for ASX's licence to operate the facilities while the RBA is responsible for financial stability matters.

ASX has observed that the coordination between financial regulators (including ASIC) has deepened over recent years, particularly in the post-GFC period. The Council of Financial Regulators (CFR) has become a key body for ensuring regulatory authorities work together to deliver efficient and effective policy frameworks. This is a positive development that contrasts very favourably to some other jurisdictions, where competition between regulators can lead to regulatory overlap or differences of approach in similar areas that only deliver sub-optimal regulatory outcomes, higher compliance costs for industry and less efficient economic outcomes.

The major challenge facing local financial regulators, including ASIC, going forward is ensuring that Australia plays a proactive role in international policy forums such as the International Organization of Securities Commissions (IOSCO) and the Committee on Payment and Settlement Systems (CPSS). These bodies are clearly influencing global standards and principles that are applied in local jurisdictions.

It is important that Australia has seat at the table(s) where the key regulatory decisions are made. It is also important that Australia plays a constructive role in key international regulatory bodies, such as Greg Medcraft's role as Chair of IOSCO.

Following the GFC there has been a significant focus by G20 regulators and finance ministers on reforms designed to strengthen financial system stability through a range of measures to promote greater/earlier identification of risks; ensure systemically significant financial institutions employ robust risk management processes; and provide regulators with the appropriate tools to deal effectively with crisis situations.

While many of the global problems were not ones that originated in Australia (or the Asian region) it remains the case that rule design by international bodies is largely driven by European and US regulators and the impacts on other important markets, particularly those in the Asian region are not well considered. In fact, such outcomes can have the effect of favouring European or US markets competitively.

This will present challenges to all Australian regulators, not just ASIC, to work closely with regional bodies to help promote the interests of Asian markets in the policy debates. This will also require regulators to work closely with business to achieve mutual recognition and to make Australia's capital markets internationally competitive.

In adopting global regulatory principles and applying them to Australia we should make sure that while we remain in broad step with the rest of the world, we don't impose a competitive disadvantage on our own financial players by applying these principles ahead of other jurisdictions or by being too prescriptive and not giving due weight to local conditions when applying them to our markets. When we seek to benchmark our market structure arrangements we should also place greater emphasis on those of our Asian region competitors rather than seeking line by line alignment with the US and European models that are directed at the failures in their home markets which have very different characteristics to our own.

We are encouraged that there is a good understanding of the importance of this and good engagement by regulatory agencies such as ASIC and RBA with local stakeholders in advancing Australian national interests.

Yours sincerely

A handwritten signature in black ink, appearing to read "Amanda Harkness". The signature is written in a cursive, flowing style.

**Amanda J. Harkness**  
Group General Counsel & Company Secretary