

Australian Securities and Investments Commission answers to questions on notice

ASIC Oversight Hearing 29 April 2010

Q 1 (Proof Hansard p. 18) – False rumours

Senator MASON—Could you suggest to the committee a way that the legislature could reform the law to make it easier for you to look at false rumours?

Mr D’Aloisio—We could take that on notice. We think—

Senator MASON—I think the committee would be interested in whether there is a better way to do it.

Answer:

ASIC is a participant on CAMAC and in that role ASIC has supported the recommendation of the Corporations and Markets Advisory Committee (CAMAC) in its June 2009 Report Aspects of Market Integrity for reform to Sections 1041E, 1041F and 101G of the Corporations Act.

ASIC believes that the integrity of financial markets would be strengthened by making ss1041E (making false or misleading statements) and 1041F (inducing persons to deal) civil penalty provisions. Such a reform would involve these sections of the Act being amended to remove the fault elements in line with ss1041A-1041C which are also civil penalty provisions.

ASIC also supports CAMAC's view that making s1041G (engaging in dishonest conduct) a civil penalty provision if it were possible to cast it in suitable terms, given that the criminal concept of dishonesty is a central element of the offence as it stands.

Q 2 (Proof Hansard pp. 19–20) – Project Mint outcomes

CHAIR—I would be interested to have some sort of report from ASIC—

Mr D’Aloisio—Yes. We can take that on notice.

CHAIR—as to its successes, learnings and otherwise in terms of Project Mint. I certainly think it is important and something that needs to be ongoing, so I think it would be very helpful for us. Have there been any specific changes in terms of guidelines or anything in relation to company reporting or any particular outcomes that you can identify at this stage?

Answer:

In March 2008 ASIC started the market integrity (MINT) project to review and pursue allegations of rumourtrage and market misconduct offences.

During the initial phase of the MINT project, we investigated a number of specific rumour allegations relating to the period January to April and involving several listed entities. We served a large number of notices on brokers and hedge funds relating to these entities and their trading in other stocks we identified as having been under pressure during the same period.

Rumour activity picked up in August and September 2008, and we opened a number of new enquiries into alleged spreading of false rumours.

ASIC has liaised with the both the US Securities and Exchange Commission, and the Hong Kong Futures and Securities Commission in these inquiries.

The first broker banning proceedings were initiated in October 2008. Richard Macphillamy of Linwar Securities was banned from providing financial services for a period of 18 months.

ASIC has engaged in a wide range of activities to raise awareness of market integrity issues and improve how brokers handle market rumours.

In September 2009, ASIC published a consultation paper "Responsible handling of rumours" outlining some proposed principles and guidelines designed to assist market participants in their dealing with market rumours.

ASIC also published a consultation paper "Handling Confidential Information: best practice guidelines" in December 2009 which sets out guidelines for companies and their advisers on how to protect confidential, price-sensitive information prior to the announcement of a transaction.

ASIC announced on 12 May 2010 that it will work closely with the market over the next six to nine months to address the responsible handling of rumours and corporations' management of confidential information through industry standards rather than through regulatory guidance.

ASIC continues to monitor, and if warranted investigate, rumours that come to our attention, when we are concerned about their effect on market integrity. This is now part of our business as usual.

The principal benefits of project Mint (which has now become business as usual for ASIC) have been:

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- (a) heightening of awareness within the broker community and the markets of the legal consequences of irresponsible handling of rumours and mishandling of confidential information.
 - (b) improvements in rumour handling and handling of confidential information by brokers and companies.
 - (c) broker banning with its deterrent impact.

These outcomes have been important in maintaining confidence in the integrity of our markets. An example of that confidence is the way our market functioned for the raising of new capital during the crisis – one of the best markets in the world.

Q 3 (Proof Hansard p. 20) – Project Mint resources

Mr HARTSUYKER—I would just like to hark back to my other question about what you have spent on the project [Project Mint] so far.

Mr D’Aloisio—I would have to take that on notice. It is part of our normal business, so we would not segment and cost. It is important work, so we would not have a separate cost on it.

Answer:

ASIC did not allocate a specific or separate cost centre or budget to Project MINT as we saw it as a significant part of our ongoing regulatory responsibilities with a particular focus on market conduct. There was no CAPEX component.

As far as operating expenses are concerned, these were subsumed within ASIC's general operating budget and were not separately allocated or accounted for.

Q 4 (Proof Hansard p. 20) – Project Mint resources

CHAIR—Could you look at that anyway in terms of cost outcomes? It is obviously a project, so it is a defined task and undertaking that ASIC does. Certainly I think it is a very important one. It is something that needs to be ongoing. But I am very interested as well in terms of the resources that ASIC devotes to it and how it deals with that and whether the organisation has a view to continue those as a project other than ongoing work. Does it warrant at some future time to undertake another special exercise like Project Mint? I would certainly be very interested in that.

Answer:

ASIC did not allocate a specific or separate cost centre or budget to Project MINT as we saw it as a significant part of our ongoing regulatory responsibilities with a particular focus on market conduct. There was no CAPEX component.

As far as operating expenses are concerned, these were subsumed within ASIC's general operating budget and were not separately allocated or accounted for.

ASIC did, however, prioritise this project given its importance and the impact of rumours on our markets. The benefits of Project Mint were outlined in our response to Question on Notice 2.

Q 5 (Proof Hansard pp. 27–28) – Contested cases

CHAIR—Earlier you gave us a figure that I think you have quoted a number of times. It is a 90 per cent success rate with cases. Is that contested or uncontested cases? Is there a difference?

Mr D'Aloisio—They range—

CHAIR—Is that the totality of all cases?

Mr D'Aloisio—I think the definition is in the annual report. From memory, it covers the positive outcomes that are achieved. Some are achieved through court. Most are achieved through court. Some are achieved through enforceable undertakings. Some are achieved through negotiated settlement. So there is a range of what we call positive outcomes in relation to the process.

CHAIR—Is there a figure of contested cases in the annual report?

Mr D'Aloisio—I will take that on notice and get that for you. Yes, I will get that for you. I just do not have it.

Answer:

The figure of 90% successful litigation rate for the 2008-2009 financial year noted in the Annual Report represents civil and criminal results which were achieved through court. Results are also achieved in other ways such as through exercise of administrative powers and enforceable undertakings and the settlement of claims.

The 90% figure does not draw a distinction between contested and uncontested court cases.

Q 6 (Proof Hansard p. 33) – Market competition consultation

Ms Gibson— ... I will briefly touch on some of the things that we will be consulting on. We have a list of 25 things that we think are important.

...

Senator BOYCE—Could you give us on notice the list of 25, just from interest?

Ms Gibson—I could. I could write that and get that done for you, yes. It is some 25. It is in an order of priority. It is those six that are the main ones, yes, certainly. And there is the change process that obviously is going to have to be managed for everyone as you move to quite a different market.

Answer:

Note – this is the current proposed scope in May 2010. The list is by way of guide. Some issues will require more extensive consultation than others.

Subject matter of possible common rules:

1. Best execution – mechanism for ensuring brokers deliver the best possible outcome when executing client orders. Sufficient information should be available to evidence execution quality.
2. Pre-trade transparency – the circumstances where public disclosure of orders and quotes may or may not be required.
3. Post-trade transparency – the circumstances where public disclosure of details about executed trades is required immediately and where delayed publication should be permitted.
4. Data consolidation – possible mechanisms for ensuring pre- and post-trade information is made available to investors in an accurate, timely and consolidated way and at reasonable cost.
5. Direct market access/ sponsored access – intended minimum standards for market operators and participants when allowing clients to directly access a market using a participant's infrastructure or identity.
6. Algorithmic trading – intended minimum controls for participants facilitating algorithmic trading (including “high frequency trading”).
7. Tick sizes – whether minimum price increments for quotes and orders should be set to prevent stepping ahead by an economically insignificant amount and what such increments might be.
8. Access to markets – whether common rules are required to ensure there is non-discriminatory access to markets.

9. Market operator systems and controls – whether additional standards regarding market operator systems and controls should be imposed on market operators to contribute to market integrity.

10. Off-market trading – whether market participants should be permitted to trade outside the rules of a market operator and the implications of such trading.

11. Crossing networks – options for the regulatory treatment for broker internal client crossing systems that currently operate under the franchise of the ASX.

12. Cancelled, failed, varied trades – intended default arrangements for cancelled, failed and varied trades. Whether market operators should be obliged to have an error trade policy and whether it should be a whole-of-market approach.

13. Clock synchronisation – whether market operators and/or participants should synchronise their clocks to facilitate chronological time-stamping.

14. Transaction reporting – whether participant transaction reporting to ASIC (of non-public information) would aid in whole-of-market surveillance including providing adequate audit trails.

15. Suspicious activity reporting – whether reporting of suspicious activity to ASIC would aid in surveillance.

16. Trading during a takeover – intended common standards for trading during a takeover.

17. Short-selling – whether any supplemental rules are required dealing with short selling in a multi-market environment.

18. Clearing and settlement – whether it is necessary to set a maximum settlement timeframe (i.e. T+3).

Other issues we expect to consult on:

19. Market operator cooperation – expectations for market operators to share information between themselves and with ASIC to facilitate investigations and a common approach between market operators to manage and coordinate trading halts and suspensions.

20. ASIC's supervisory approach – our intended approach to supervising market operators and participants in a whole-of-market way.

21 Fees for supervision – whether revisions are required to cost recovery for ASIC supervision (in consultation with Treasury).

22. Compensation arrangements – whether there are any issues with the existing compensation arrangements in a multi-market environment (in consultation with Treasury).

Q 7 (Proof Hansard p. 43) – FIDO website and superannuation fees

Mr HARTSUYKER—On the FIDO website in relation to super fees, there is a disclaimer on the site that says they do not represent all of the additional fees and costs being incurred by a particular fund. Some of them go to that FIDO website.

Mr D’Aloisio—Is this on the calculator?

Mr HARTSUYKER—Yes.

Mr D’Aloisio—And the assumptions around the calculator?

Mr HARTSUYKER—Yes. Really, the question is: what are these fees and costs that are not disclosed? If so, why not? What is the rationale of all of that? How effective is it if you have a range of costs that are not disclosed?

Mr D’Aloisio—I will take that on notice. I suspect that the disclaimer or the comment is really to say that the calculators are there to give you a guide and that we do not necessarily have all of the fees that could apply but this gives you a way of testing and looking at things. But I am happy to take that on notice and give you a more specific answer.

...

Mr HARTSUYKER—When you have looked at that, I would be really interested in any comments on the quantum—perhaps take a couple of examples—of the different fees disclosed and undisclosed.

Answer:

What fees are not disclosed and why?

Fees that are excluded from the calculator are listed in the calculator guide that is available on the website. Fees are excluded because:

- they do not apply to all fund members, only if the member requests a particular additional service;
- they add to the complexity of the calculator but do not have a significant impact on results for the average user (eg \$50 impact on an end payout of \$100,000 plus), or
- there is not a consistent method to apply them.

The specific fees that were excluded and the reasons are:

- Termination fees: When the user is transferring from one fund to another these fees have been included, because for legacy funds the early exit fees can

be quite significant. When the user retires, any termination fees that apply have been excluded because they are not significant (eg \$50 one-off fee).. .

- Buy and sell spreads: We have left out these buy and sell fees, because they would add to the complexity of the calculator but do not have a large impact on the average user..
- Fees for switching between investment options: These fees would not apply to most people, as they only apply if members changes investment options. In addition, the fees will not have much impact on the result (eg \$50). The calculator assumes that once you have made an investment choice you will stay in the same investment option for significant period. This assumption would be valid for the majority of people.

How effective is it if you have a range of costs that are not disclosed?

The calculator is an effective educational tool. Extending the calculator to include minor fees would not make the calculator a more effective tool as the majority of users would not be affected by them and the calculator would be more difficult to use. The calculator does not purport to be accurate to the exact dollar. It gives a reasonably accurate estimate.