



**ASIC**

Australian Securities & Investments Commission

## REGULATORY GUIDE 172

# Australian market licences: Australian operators

### Chapter 7 — Financial services and markets

*Issued 6/3/2002*

*From 5 July 2007, this document may be referred to as Regulatory Guide 172 (RG 172) or Policy Statement 172 (PS 172). Paragraphs in this document may be referred to by their regulatory guide number (e.g. RG 172.1) or their policy statement number (e.g. PS 172.1).*

#### ***Editor's note, September 2013:***

*This regulatory guide has not been updated since March 2002, except for the addition of an addendum on market licensee systems and controls in November 2012: see page A-1.*

*Since the release of RG 172 we have published the following related regulatory guides:*

- *RG 177 Australian market licences: Overseas operators; and*
- *RG 211 Clearing and settlement facilities: Australian and overseas operators.*

*Note that RG 172 has not been updated to take into account legislative changes to the:*

- *Corporations Amendment (Financial Market Supervision) Act 2010, which transferred market supervision to ASIC and enabled ASIC to make market integrity rules; and*
- *Corporations and Financial Sector Legislation Amendment Act 2013, which amended ASIC's obligation to conduct annual assessments of market licence holders.*

*RG 172 as a whole will be reviewed and updated in due course. For further information, please contact the Senior Executive Leader, Financial Market Infrastructure, ASIC, tel: (02) 9911 2000.*

## What this guide is about

---

RG 172.1 This guide outlines our role in and approach to financial market regulation under the *Corporations Act 2001*. It deals with financial markets operating in Australia, with particular focus on Australian operators. A separate policy will deal with issues specific to overseas operators.

RG 172.2 This guide sets out:

- A our role in market regulation  
*see RG 172.4–RG 172.14*
- B what “operate a financial market” means  
*see RG 172.15–RG 172.36*
- C what “operate a financial market in Australia” means  
*see RG 172.37–RG 172.48*
- D our approach to exemptions from market regulation  
*see RG 172.49–RG 172.67*
- E our approach to and guidance on the obligations of Australian market licensees  
*see RG 172.68–RG 172.124*
- F how to get an Australian market licence  
*see RG 172.125–RG 172.172*

The Schedule gives examples of types of activities that will require an Australian market licence.

RG 172.3 This guide replaces Superseded Policy Statement 100 *Stock markets* [SPS 100] and Superseded Policy Statement 70 *Exempt futures markets* [SPS 70].

**Important note:** The contents of this guide are based on the FSR Act at the date of this publication, Wednesday 6 March 2002, and the regulations made on 8 October 2001 and 14 and 28 February 2002 for the purposes of the FSR Act. We do not expect the substance of this policy to be materially affected by proposed further regulations. However, we will review these regulations and, if necessary, amend any details of this policy.

---

## Contents

<b>What this guide is about .....</b>	<b>1</b>
<b>A Our role in financial market regulation .....</b>	<b>4</b>
Our policy.....	4
Table A: Regulatory outcomes and mechanisms in financial markets.....	6
Underlying principles .....	8
Explanation .....	8
<b>B Do you operate a financial market?.....</b>	<b>9</b>
Our policy.....	9
Underlying principles .....	11
Explanation .....	12
Further examples.....	13
<b>C Do you operate a financial market in Australia? .....</b>	<b>14</b>
Our policy.....	14
Underlying principles .....	15
Explanation .....	16
Further examples.....	16
<b>D What is our approach to exemptions? .....</b>	<b>17</b>
Our policy.....	17
Underlying principles .....	20
Explanation .....	20
Further examples.....	21
<b>E Obligations of market licensees .....</b>	<b>22</b>
Our policy.....	22
Explanation .....	33
<b>F How do you get an Australian market licence?.....</b>	<b>36</b>
Our policy.....	36
Underlying principles .....	42
Explanation .....	42
<b>Schedule: What types of activities will require an Australian market licence? .....</b>	<b>45</b>
A Order routing systems.....	46
B internet portals.....	47
C Electronic trading services .....	49
D Cross-border trading screens.....	52
<b>Key terms.....</b>	<b>53</b>
<b>Related information .....</b>	<b>55</b>
<b>Addendum: Supplementary guidance on market licensee systems and controls .....</b>	<b>A-1</b>

## **A Our role in financial market regulation**

---

### **Our policy**

#### ***What is our role?***

RG 172.4 The Minister has the main responsibility for regulating financial markets operating in Australia. ASIC plays an important but secondary role in financial market regulation: see Explanatory Memorandum, paragraph 7.4.

RG 172.5 Our main functions in the regulation of financial markets are to:

- (a) advise the Minister about applications for a market licence, changes to operating rules, other matters in respect of which the Minister has a discretion under Part 7.2 of the Corporations Act, and other matters concerning financial markets;
- (b) assess and report to the Minister on market licensees' compliance with their obligations;
- (c) enforce market licensees' compliance with their obligations; and
- (d) enforce the prohibition on a person operating, or holding out that the person operates, a financial market in Australia, if the person does not hold a licence or an exemption.

#### ***How will we approach our role?***

RG 172.6 Whenever we perform these functions, we will have regard to:

- (a) the purposes of market regulation; and
- (b) the need to apply the regulatory regime flexibly according to the features of the market in question.

#### **Purposes of market regulation**

RG 172.7 The purposes of market regulation are to:

- (a) protect market users; and
- (b) enhance market integrity and financial system stability.

RG 172.8 Market regulation achieves these purposes primarily by requiring market operators to be licensed and to comply with the licensee obligations. By doing this, market regulation ensures that the regulatory outcomes relevant to each market are achieved.

RG 172.9 Table A sets out the regulatory outcomes for each regulatory area and the main regulatory mechanisms used to achieve these outcomes.

RG 172.10 Other regulatory mechanisms are also used to achieve these outcomes. They include our supervision of market licensees' compliance with their obligations, Ministerial disallowance of changes to the operating rules of licensed markets, and obligations imposed directly on financial services licensees.

### Flexible regulation

RG 172.11 The regulatory regime is flexible. This is because the relevance of the regulatory outcomes, and how market licensees comply with the regulatory mechanisms in order to achieve these outcomes, may vary according to the features of the market. These features include:

- (a) the structure of the market;
- (b) the nature of the activities conducted on the market;
- (c) the size of the market;
- (d) the nature of the financial products dealt with on the market;
- (e) the market users;
- (f) the participants in the market; and
- (g) the technology used in the operation of the market.

Note: See s798A(2).

**Table A: Regulatory outcomes and mechanisms in financial markets**

RG 172.12

<b>Regulatory area</b>	<b>Regulatory outcomes</b>	<b>Market regulatory mechanisms</b>
Market information	<p>Market users use the market on an informed basis. For example:</p> <ul style="list-style-type: none"> <li>• information about the market operator, market processes, listed entities, product issuers and products traded is adequate and accurate</li> <li>• pre-trade and post-trade information is made available in a timely way</li> <li>• relevant information is available to users and potential users</li> <li>• listed entities comply with the market's operating rules about disclosure</li> </ul>	<p>The market operator must:</p> <ul style="list-style-type: none"> <li>• ensure that the market is fair, orderly and transparent</li> <li>• monitor the conduct of listed entities and participants on or in relation to the market and enforce compliance with the market's operating rules</li> <li>• notify ASIC of suspected significant breaches of the law or the market's operating rules</li> </ul>
Trading	<p>Market users are confident that the market as a whole operates fairly and that they will be treated fairly. For example:</p> <ul style="list-style-type: none"> <li>• the manner in which access to bids and offers is determined is fair</li> <li>• the methods by which bids and offers are matched are fair</li> <li>• most trading takes place through the main market facility</li> <li>• the market's rules and processes minimise the risk of price manipulation or other abusive trading conduct</li> </ul>	<p>The market operator must:</p> <ul style="list-style-type: none"> <li>• ensure that the market is fair, orderly and transparent</li> <li>• monitor the conduct of participants on or in relation to the market and enforce compliance with the market's operating rules</li> <li>• notify ASIC of suspected significant breaches of the law or the market's operating rules</li> </ul>
Participant supervision	<p>Market users are confident about the participants they deal with. For example, participants:</p> <ul style="list-style-type: none"> <li>• comply properly with instructions, and properly complete transactions</li> <li>• protect their clients' interests adequately and do not act in their own interests to the detriment of their clients</li> <li>• do not misappropriate client money or other property in connection with trading on the market</li> <li>• comply with the law and the market's operating rules</li> <li>• are financially sound</li> </ul>	<p>The market operator must:</p> <ul style="list-style-type: none"> <li>• ensure that the market is fair, orderly and transparent</li> <li>• monitor the conduct of participants on or in relation to the market and enforce compliance with the market's operating rules</li> <li>• notify ASIC of disciplinary action against a participant, suspected significant breaches of the law or the market's operating rules by a participant, or the inability of a participant to meet obligations as a financial services licensee</li> <li>• have appropriate compensation arrangements protecting retail client money and other property held by participants</li> </ul>

Regulatory area	Regulatory outcomes	Market regulatory mechanisms
Market supervision	<p>Listed entities, participants and market users that breach the law or the market's operating rules are likely to be detected and disciplined, and as a result:</p> <ul style="list-style-type: none"> <li>• participants and existing and potential market users have confidence in the market</li> <li>• participants and market users are not disadvantaged by breaches of the market's operating rules</li> <li>• the market has a good reputation</li> </ul> <p>Market supervision is not compromised by:</p> <ul style="list-style-type: none"> <li>• conflicts between the market operator's duties and commercial interests</li> <li>• the influence of a major shareholder</li> <li>• the involvement of unfit individuals in the management of the market operator</li> <li>• the market operator's lack of resources</li> </ul>	<p>The market operator must:</p> <ul style="list-style-type: none"> <li>• ensure that the market is fair, orderly and transparent</li> <li>• have adequate arrangements for supervising the market</li> <li>• have adequate resources to supervise the market</li> <li>• provide information to ASIC to enable ASIC to monitor the market operator's compliance with its obligations</li> <li>• have adequate arrangements for handling conflicts of interest</li> <li>• take reasonable steps to ensure an unacceptable control situation does not exist</li> <li>• take reasonable steps to ensure that no disqualified individual becomes or is involved in the market operator</li> </ul>
Market stability	<p>The market operates reliably, and is not at risk of failing, so that:</p> <ul style="list-style-type: none"> <li>• existing and potential market users can be confident it will be available in the future</li> <li>• operators of other markets or clearing and settlement facilities will not be adversely affected by any failure of the market</li> </ul> <p>The price formation process operates reliably.</p>	<p>The market operator must:</p> <ul style="list-style-type: none"> <li>• ensure that the market is fair, orderly and transparent</li> <li>• have sufficient financial, technological, human and other resources to operate the market properly</li> </ul>
Clearing and settlement	<p>Transactions entered into on the market are cleared and settled promptly, fairly and effectively</p>	<p>The market operator must:</p> <ul style="list-style-type: none"> <li>• ensure that the market is fair, orderly and transparent</li> <li>• have adequate clearing and settlement arrangements, or disclose to participants the absence of clearing and settlement arrangements, or that the clearing and settlement arrangements are not with the operator of a clearing and settlement facility</li> <li>• monitor the conduct of participants on or in relation to the market and enforce compliance with the market's operating rules</li> </ul>

## **Underlying principles**

RG 172.13 When performing our role in financial market regulation, we will focus on the regulatory outcomes that financial market regulation seeks to achieve.

## **Explanation**

RG 172.14 Unlike the markets provisions of the old Corporations Act, Part 7.2 deals with all types of financial markets. Nevertheless, we think much of the underlying policy of Part 7.2 is similar to that of the market provisions of the old Corporations Act.



## B Do you operate a financial market?

---

RG 172.15 A person requires an Australian market licence if they operate a financial market in Australia that has not been exempted from the operation of Part 7.2: see s791A.

RG 172.16 This section examines when a person operates a financial market by outlining our approach to the following key terms in the definition of “financial market” in s767A:

- (a) “facility” (see RG 172.17–RG 172.19);
- (b) “through” (see RG 172.20–RG 172.21);
- (c) “offers” or “invitations” (see RG 172.22–RG 172.23);
- (d) “made” or “accepted” (see RG 172.24–RG 172.26); and
- (e) “regularly” (see RG 172.27–RG 172.28).

Note: Section 767A(1) provides:

“For the purposes of this Chapter, a *financial market* is a facility through which:

- (a) offers to acquire or dispose of financial products are regularly made or accepted; or
- (b) offers or invitations are regularly made to acquire or dispose of financial products that are intended to result or may reasonably be expected to result, directly or indirectly, in:
  - (i) the making of offers to acquire or dispose of financial products; or
  - (ii) the acceptance of such offers.”

Section 767A(2) sets out conduct that does not constitute operating a financial market.

### Our policy

#### ***What is a “facility”?***

RG 172.17 A facility is any form of infrastructure. However, this does not mean that a person operates a financial market merely because they operate an electronic means of communication or are an internet service provider: see Explanatory Memorandum, paragraph 7.14.

RG 172.18 An integrated infrastructure constitutes a single facility and may be a financial market even if any or all of its component parts, when considered in isolation, do not constitute a financial market.

RG 172.19 The following factors indicate that a number of component parts constitute an integrated infrastructure and a single facility:

- (a) the component parts are owned or controlled by the same entity or are part of the same corporate group; or
- (b) together the component parts enable the making and/or acceptance of offers or invitations and no component part is a regulated market.

These factors are not exhaustive.

### ***What does “through” mean?***

RG 172.20 A facility will not constitute a financial market merely because it is a step in a process that results in the eventual making or acceptance of offers or invitations. We read “through” in s767A(1) narrowly so that a facility only amounts to a financial market if the offers or invitations are made or accepted *by means of*, that is, *on* the facility.

RG 172.21 This means that the various forms of infrastructure that are instrumental in the eventual making or acceptance of offers or invitations are not financial markets, if they are mere channels to the facility on which the offer or invitation is made or accepted.

### ***What are “offers” or “invitations”?***

RG 172.22 We read the terms “offer” and “invitation” broadly to include:

- (a) formal contractual offers;
- (b) requests for others to make a formal contractual offer; and
- (c) requests to enter a course of negotiations with a view to entering into a binding contract.

RG 172.23 An offer or an invitation will generally identify:

- (a) a person who is likely to acquire or dispose of a financial product or their agent; and
- (b) the price at which that person is likely to acquire or dispose of a financial product.

### ***When and where are offers or invitations “made” or “accepted”?***

RG 172.24 An offer or invitation is:

- (a) *made* when and where it is received by the person to whom the offer or invitation is made or their agent; and
- (b) *accepted* when and where the acceptance is received by the person who makes the offer or invitation or their agent.

RG 172.25 A consequence of this approach, and our approach to “through” (see RG 172.20), is that only a facility by means of which or on which offers, invitations or acceptances are received constitutes a financial market. An order routing facility that merely routes offers to another person, who then enters them on a market operator’s platform, is not a financial market because there is no receipt of the offer on such a facility.

RG 172.26 We note that a facility may constitute a financial market even if binding contracts are not entered into on the facility. Invitations may be made, that is, received on a facility even if binding contracts are not entered into on the facility.

### ***What does “regularly” mean?***

RG 172.27 “Regularly” means systematically, in the sense that there are recurring opportunities to acquire or dispose of financial products through the facility. “Regularly” does not mean continuously or at specified intervals.

RG 172.28 The requirement of regularity may be satisfied even if the facility only operates for a short period of time.

## **Underlying principles**

RG 172.29 “Financial market” is defined in s767A in broad and flexible terms. When determining whether an activity falls within the scope of this definition, we must have regard to the object and purpose of the market regulation provisions: see s15AA of the *Acts Interpretation Act 1901*. Accordingly, to the extent possible, we will interpret the definition of a financial market in s767A as applying only when it is necessary to impose the licensee obligations on the market operator in order to achieve the regulatory outcomes in Table A.

## Explanation

### **What is a “facility”?**

RG 172.30 Our approach to the definition of a facility is consistent with *Carragreen Currency Corporations Pty Ltd v Corporate Affairs Commission (NSW)* (1986) 11 ACLR 298, 312-3.

### **What does “through” mean?**

RG 172.31 “Through” could be interpreted in a number of ways. In the context of s767A(1), it could mean “in consequence of”, “by reason of” or “by means of”. We have concluded that it should be construed narrowly and that a facility is only a financial market if the offers or invitations are made or accepted *by means of* the facility. That is, the offers or invitations must actually be made *on* the facility if the facility is to constitute a financial market. We have reached this conclusion because the alternative constructions lead to a definition of a financial market whose breadth is inconsistent with the policy and object of financial market regulation.

### **What are “offers” or “invitations”?**

RG 172.32 Section 767A(1)(b) indicates that the terms “offer” and “invitation” encompass formal contractual offers, requests to others to make a formal contractual offer, and requests to enter a course of negotiations with a view to entering into a binding contract. The essential feature of both an offer and an invitation for the purposes of s767A is that the offer or invitation is intended by the offeror or inviter to result in a binding contract or may reasonably be expected to result in a binding contract. A binding contract for sale identifies both parties and price. Accordingly, we say that an offer or invitation will generally identify the person making the offer or invitation or their agent, and the price.

RG 172.33 Our approach to the meaning of offer is consistent with *AG for NSW v The Mutual Home Loans Fund of Australia Ltd* [1971] 2 NSWLR 162, 165 and *AG for NSW v Australian Fixed Trusts Ltd* [1974] 1 NSWLR 110, 117.

### **When and where are offers or invitations “made” or “accepted”?**

RG 172.34 Our approach to when an offer or invitation is “made” or “accepted” is consistent with both the common meaning of those terms and case law. Cases on the interpretation of the rules about jurisdiction over contractual disputes with a foreign element provide that a contractual acceptance made by instantaneous means (essentially, any means of communication other than post or telegram) is completed or made when and where it is received: see *Entores Ltd v Miles Far East*

*Corporations* [1955] 2 QB 327; *Hampstead Meats Pty Ltd v Emerson and Yates Pty Ltd* [1967] SASR 109; *Express Airways v Port Augusta Air Services* [1980] Qd 543; *Mendelson-Zeller Co Inc v T & C Provedores Pty Ltd* [1981] 1 NSWLR 366. Additionally, the High Court has accepted that, generally, a statement “directed from one place to another where it is known or even anticipated that it will be received” is “made at the place to which it was directed”: *see Voth v Manildra Flour Mills Pty Ltd* (1990) 171 CLR 538, 568.

### **What does “regularly” mean?**

RG 172.35 Section 767A(1) provides that a facility will only constitute a financial market if offers or invitations are regularly made or accepted through the facility. That is, it is the making or acceptance of offers or invitations that must be regular, not the operation of the market. Therefore, a short-term market may still satisfy the requirement of regularity.

### **Further examples**

RG 172.36 The Schedule gives examples of some types of activities that fall both within and outside the definition of a financial market.

## C Do you operate a financial market in Australia?

---

RG 172.37 An operator of a financial market only requires an Australian market licence if they operate the financial market in Australia. This section sets out our approach to determining when a financial market operates in Australia.

### Our policy

RG 172.38 A financial market operates in Australia if it meets one or more of the following descriptions:

- (a) the financial market is operated by a body corporate that is registered under Chapter 2A of the Corporations Act;
- (b) the financial market is located in Australia; or
- (c) the financial market:
  - (i) has one or more participants in Australia (see the definition of “participant” in RG 172.95); and
  - (ii) is targeted at Australian investors.

Note: A market may operate simultaneously in Australia and other jurisdictions. This is implicit in s795B(2) and the scheme for the licensing of overseas markets in Part 7.2.

### ***When is a financial market located in Australia?***

RG 172.39 A financial market is located in Australia if:

- (a) the market has a trading floor in Australia; or
- (b) all or a significant part of the market infrastructure is located in Australia.

### ***When is a financial market targeted at Australian investors?***

RG 172.40 The following factors indicate that a financial market is targeted at Australian investors:

- (a) one or more participants in Australia have direct secure access to the market platform through a market screen;
- (b) the operator, or a person acting with the endorsement of the operator, promotes the market in Australia by, for example:
  - (i) advertising the market in Australian publications;

- (ii) sending direct mail publicity about the market to Australian addresses; or
- (iii) sending email publicity about the market to Australian addresses;
- (c) the prices on the market are denominated in Australian dollars; or
- (d) the market is regularly used by Australian investors.

RG 172.41 The following factors indicate that a financial market is *not* targeted at Australian investors:

- (a) when an Australian participant accesses the market, they are presented with information that clearly and prominently states that the market is targeted at residents of some other jurisdiction;
- (b) when an Australian participant accesses the market, they are presented with information that clearly and prominently lists the jurisdictions (other than Australia) in which the market is authorised to operate, and that information is true; or
- (c) the operator takes precautions designed to prevent use of the market by Australian investors.

Note: Such precautions include the screening of invitations, offers and acceptances from Australian addresses. Precautions that merely require market users to identify whether they are Australian are insufficient.

RG 172.42 The above factors are indicative only. They are neither exhaustive nor determinative. Determining whether the market targets Australian investors will require an assessment of all the facts and circumstances pertaining to the market.

RG 172.43 In most circumstances, an operator that wants to establish that a market does not target Australian investors will need to point to a number of relevant factors. A jurisdictional disclaimer by itself is unlikely to be sufficient.

## **Underlying principles**

RG 172.44 In determining when a financial market that falls outside s791D(1) operates in Australia, we have taken into account:

- (a) the globalisation of financial markets and the use of communications networks, such as the internet, that operate across international boundaries. We accept that it is neither feasible nor appropriate for Australian law to attempt to regulate all markets on which Australians may directly participate;
- (b) Parliament's intention to protect Australia's reputation as a global financial centre: see Explanatory Memorandum, paragraph 7.19.

This reputation would be undermined if unscrupulous and unregulated operators of financial markets were located in Australia; and

- (c) the need to protect Australian investors and the integrity of Australian markets.

### **Explanation**

RG 172.45 Section 791D(1) provides that a financial market is taken to be operated in Australia if it is operated by a body corporate that is registered under Chapter 2A of the Corporations Act.

RG 172.46 Section 791D(2) makes it clear that there are other circumstances in which a market operates in this jurisdiction.

RG 172.47 Our policy on these circumstances is consistent with our approach in Regulatory Guide 141 *Offers of securities on the internet* (RG 141) and the approach of other regulators and international organisations to regulatory authority over activities on the internet.

### **Further examples**

RG 172.48 The Schedule gives examples of financial markets that operate in Australia and financial markets that do not operate in Australia.



## D What is our approach to exemptions?

---

RG 172.49 An operator of a financial market in Australia does not require an Australian market licence if the Minister has exempted the financial market from the operation of Part 7.2.

RG 172.50 This section sets out:

- (a) when we will advise the Minister that a financial market should be exempted from the operation of Part 7.2 (see RG 172.51–RG 172.56);
- (b) the types of conditions that we will recommend on such an exemption (see RG 172.57–RG 172.58);
- (c) how to apply for an exemption (see RG 172.59); and
- (d) how we will deal with your application for an exemption (see RG 172.60–RG 172.61).

### Our policy

#### ***When will we advise the Minister to exempt a financial market?***

RG 172.51 We will only advise the Minister that an exemption should be granted in rare and exceptional circumstances.

RG 172.52 We will normally only advise the Minister to exempt a particular financial market or type of financial market if we think there is no public benefit in regulating the market under Part 7.2 because:

- (a) the regulatory outcomes in Table A are not relevant to the market;
- (b) the regulatory outcomes in Table A are achieved without regulation under Part 7.2; or
- (c) the cost of regulation required to achieve the regulatory outcomes in Table A significantly outweighs the benefits of those outcomes.

These categories may overlap.

#### Regulatory outcomes achieved without Part 7.2

RG 172.53 We may advise the Minister to exempt a financial market from the operation of Part 7.2 because it is subject to other forms of regulation (such as the financial services licensing regime) that ensure that the regulatory outcomes in Table A are achieved without regulation under Part 7.2.

Note: For example, an electronic trading service (ETS) would generally not require regulation as a financial market in order to achieve the regulatory outcomes in Table A, *if*:

- (a) the operator of the ETS has an Australian financial services licence; and
- (b) the operation of the ETS is governed by the operating rules of a licensed market and supervised by the operator of the licensed market.

In these circumstances, regulation of the ETS under Part 7.2 would involve unnecessary regulatory duplication.

However, regulation as a financial market may be necessary if the volume of trading on the ETS is such that:

- (a) the ETS plays a central role in price formation for a particular financial product; or
- (b) execution, settlement or other system failures or market malpractice on the ETS would have major ramifications for the market for that financial product as a whole.

In these circumstances, the regulatory outcomes in Table A may not be achieved unless the ETS is regulated under Part 7.2.

See RG 172.176 of the Schedule for more examples on electronic trading services.

### Regulatory cost significantly outweighs benefits

RG 172.54 In deciding whether to advise the Minister to exempt a market because the cost of regulation significantly outweighs the benefits, we will take into account factors such as:

- (a) the volume of trading on the market;
- (b) the characteristics of the market operator, including whether it operates any other markets;
- (c) the nature of products traded on the market, including the purposes for which they are acquired; and
- (d) the number of products traded on the market. (If the financial products of more than one issuer<sup>1</sup> are traded on a market, we are unlikely to advise the Minister to exempt the market.)

Note: For example, we may advise the Minister to exempt a market operated by an incorporated club, on which shares in the club can be traded. There is usually an insignificant volume of trading on such a market because there are a limited number of shares that can be traded on the market and because the shareholders tend to retain their shareholdings. Moreover, the shares are not acquired or disposed of primarily for the purpose of making a financial investment. Shareholders acquire shares primarily for the purpose of obtaining club membership. In these circumstances, the cost of regulation as a financial market would be unduly onerous.

---

<sup>1</sup>In this instance, contrary to s761E(6), we do not define the operator of a derivatives market as an “issuer”.

### Other circumstances

RG 172.55 We will not advise the Minister to exempt an overseas market solely because the market is subject to regulation in the foreign country where its principal place of business is located. The operator of such a market should seek a licence under s795B(1) or (2).

RG 172.56 We will not advise the Minister to exempt a market solely because there is doubt about whether the products traded on the market are, or should be, within the definition of financial product. In these circumstances, the operator should seek a declaration under s765A(2).

### ***What is our approach to conditions on an exemption?***

RG 172.57 We will not advise the Minister to exempt a particular financial market or type of financial market where we consider that numerous substantive conditions would need to be imposed on the exemption.

RG 172.58 However, we may advise the Minister to impose the following or similar conditions (among others) on an exemption where relevant:

- (a) the operator must hold the appropriate Australian financial services licence;
- (b) the key features of the market must remain as they were when the exemption was granted;
- (c) the operator must report to us periodically so that we can satisfy ourselves that the operator is complying with the conditions on the exemption;
- (d) the operator must alert users of the market to the fact that the market is exempted from the operation of Part 7.2.

### ***How to apply for an exemption***

RG 172.59 If you want the Minister to exempt a particular financial market or type of financial market, you should apply to us by letter. Your application should fully describe:

- (a) the operation of the particular financial market or type of financial market; and
- (b) why it should be exempted from the operation of Part 7.2.

### ***How will we deal with your application for an exemption?***

RG 172.60 We will aim to advise the Minister about your application for exemption within 4 weeks of receiving an application that contains *all* documents and information needed by us to assess your application. The 4-week period does not include time during which we are waiting for you

to respond to a request for further information, nor the time the Minister takes to consider your application.

RG 172.61 Occasionally, we may need to consult with the public about an application for exemption. In such cases, it will take us longer than 4 weeks to provide advice to the Minister. In deciding whether to consult with the public, we will consider:

- (a) whether the exemption is for a type of financial market or a particular financial market;
- (b) the features of the market, including:
  - (i) the size of the financial market; and
  - (ii) the market users; and
- (c) the likely impact of the market on Australian investors and the integrity of Australian markets.

## **Underlying principles**

RG 172.62 We will give effect to the Parliamentary intention that the exemption power in s791C is not to be used to provide an alternative regulatory regime for financial markets.

## **Explanation**

### ***When will we advise the Minister to exempt a financial market?***

RG 172.63 Our approach to exemptions is consistent with Parliament's intention as expressed in the Explanatory Memorandum: see, generally, paragraphs 7.26 and 7.27.

### **Other circumstances**

RG 172.64 Exempting a financial market solely because it is subject to regulation in the foreign country where its principal place of business is located would undermine the licensing regime for overseas markets in Part 7.2.

### ***What is our approach to conditions on an exemption?***

RG 172.65 The Minister's exemption power is not intended to create an alternative regulatory regime: see Explanatory Memorandum, paragraph 7.26. Where an exemption would be subject to conditions that constitute a substitute regulatory regime, we will not advise that the exemption be granted.

### ***How will we deal with your application for an exemption?***

RG 172.66 We think that, in most cases, public consultation about exemptions will be unnecessary because markets seeking exemption will generally have a limited impact on Australian investors or the public generally. We also note that the Minister is not required to take into account the public interest or our advice before making an exemption.

### **Further examples**

RG 172.67 The Schedule gives examples of circumstances in which we would recommend that a financial market be exempted from the operation of Part 7.2, and circumstances in which we would not make such a recommendation.

## **E Obligations of market licensees**

---

RG 172.68 The main obligations that a market licensee must comply with on a continuing basis are set out in s792A. Additional specific obligations are set out in s792B–792I.

RG 172.69 This section sets out:

- (a) what market licensees should do to ensure compliance with their licensee obligations (see RG 172.71–RG 172.75);
- (b) our general approach to assessing compliance with the licensee obligations (see RG 172.76–RG 172.80);
- (c) guidance on how we interpret and assess compliance with the following specific obligations:
  - (i) the obligation to do all things necessary to ensure that the market is fair, orderly and transparent (see RG 172.81–RG 172.85);
  - (ii) the obligation to have adequate arrangements for supervising the market (see RG 172.86–RG 172.101);
  - (iii) the obligation to have sufficient resources (see RG 172.102–RG 172.106);
  - (iv) the obligation to have compensation arrangements (see RG 172.107–RG 172.113); and
  - (v) the obligation to provide us with an annual report (see RG 172.114–RG 172.115).

RG 172.70 We do not discuss every licensee obligation. We will review our guidance from time to time to ensure that it deals with areas where we think guidance is needed.

### **Our policy**

#### ***What should market licensees do to ensure compliance with the licensee obligations?***

##### Planning

RG 172.71 Generally, a market licensee will best be able to ensure continuous compliance — and report on the extent of its past compliance

for the annual report (see reg 7.2.06(c) and RG 172.114–RG 172.115) — if it actively plans:

- (a) what it will do to ensure compliance; and
- (b) how it will monitor and assess its compliance.

We think that such planning is especially important to ensure compliance with the supervisory obligation.

RG 172.72 We expect that a market licensee's planning will address:

- (a) the mechanisms for performing each obligation;
- (b) the outcomes and/or standards against which compliance with each obligation will be measured and why these have been selected;
- (c) the procedures, resources and timetables for monitoring and assessing performance of each obligation; and
- (d) the procedures and structures for internal and external reporting of the outcomes of the self-monitoring and assessment.

### Monitoring and assessing

RG 172.73 A market licensee will only be able to ensure continuous compliance — and analyse the extent of its past compliance for the annual report (see reg 7.2.06(c) and RG 172.114–RG 172.115) — if it actively monitors and assesses its own compliance.

RG 172.74 A market licensee's processes for monitoring and assessing compliance should:

- (a) reliably and efficiently identify actual or potential breaches of the licensee obligations;
- (b) deal adequately with any breaches detected; and
- (c) enable the market licensee to fairly and reasonably conclude whether and how well it has complied with each of its obligations.

RG 172.75 A market licensee's processes for monitoring and assessing compliance are unlikely to meet these criteria unless they:

- (a) are sufficiently independent of the market licensee's other activities to ensure they are not improperly influenced by commercial considerations;
- (b) are comprehensive and frequent;

- (c) require the market licensee to reassess its compliance with its obligations if there are significant changes in:
  - (i) market operations;
  - (ii) market users;
  - (iii) operating rules; or
  - (iv) the market licensee's resources; and
- (d) include adequate processes for monitoring and assessing the performance of any outsourced licensee obligations.

***What is our general approach to assessing compliance with the licensee obligations?***

How will we assess compliance?

RG 172.76 In assessing how well a market licensee is complying with its licensee obligations for the purposes of s794C, we will examine:

- (a) the market's operating rules, documented procedures, plans and other written processes;
- (b) the market's operational processes, practices, systems and structures;
- (c) any planning the market licensee has done towards ensuring ongoing compliance with its obligations (see RG 172.71–RG 172.72);
- (d) the market licensee's processes for monitoring and assessing compliance and the results of that monitoring or assessment (see RG 172.73–RG 172.75);
- (e) the market licensee's annual report for the previous year (see RG 172.114–RG 172.115);
- (f) the results of our own assessment program; and
- (g) any other relevant material.

RG 172.77 We will take into account all the features of the market because the processes and conduct required to comply with the licensee obligations vary significantly depending on the features of the market.

RG 172.78 We will consider a market licensee's likely future compliance with its obligations as well as its past and current compliance. Our assessment must take into account the fact that the licensee obligations are ongoing and continuous and therefore cannot be assessed by reference to a single moment in time. We will not determine whether a market licensee is likely to comply in the future merely by reference to its past compliance.



### When will we assess compliance?

RG 172.79 We must assess and report to the Minister at least once a year on a market licensee's compliance with its supervisory obligation under s792A(c): see s794C(2). We will usually do this mandatory assessment after we receive the annual report required under s792F.

RG 172.80 We may also do an assessment of a market licensee's compliance with its supervisory and other licensee obligations at any other time. We will generally do such an additional assessment if:

- (a) matters come to our attention that give us cause for concern about a market licensee's compliance with any of its obligations; or
- (b) there are significant changes in the features of the market.

We may consult with licensees about doing additional assessments on a more regular basis.

### ***Fair, orderly and transparent: s792A(a)***

RG 172.81 Under s792A(a), a market licensee must do all things necessary to ensure that the market is fair, orderly and transparent, to the extent that it is reasonably practicable to do so. This obligation applies both as:

- (a) a broad description of all the licensee obligations; and
- (b) a separate obligation that the market licensee must comply with.

RG 172.82 Because this obligation underlies all the other licensee obligations, a market licensee that is not meeting one of its other licensee obligations is also likely not to be meeting this obligation. A market licensee that meets this obligation is likely to operate a market that achieves all the regulatory outcomes in Table A that are relevant to that market.

RG 172.83 "Fair, orderly and transparent" should be treated as a composite phrase. If there is a conflict between the elements of the phrase, we expect a market licensee to achieve an appropriate balance between the demands of each element.

RG 172.84 The obligation to "do all things necessary" is qualified by the phrase "to the extent that it is reasonably practicable to do so". In other words, a market licensee must do everything reasonably practicable to ensure that the market is fair, orderly and transparent.

RG 172.85 If a market licensee is not doing something that we think is necessary for the market to be fair, orderly and transparent, we will only assess it as complying with this obligation where the licensee can satisfy us that it is not reasonably practicable for it to do that thing. Cost by itself will not make it "not reasonably practicable" to do a particular thing,

unless the cost to the market licensee is manifestly excessive or unreasonable when compared to the market integrity, investor protection or other benefits that would result from doing the thing.

***Supervisory obligation: s792A(c)***

RG 172.86 In assessing how well a market licensee is complying with its obligation in s792A(c) to have adequate arrangements for supervising the market, we will consider how the market licensee:

- (a) handles conflicts of interest (see RG 172.87–RG 172.91);
- (b) monitors the conduct of participants (see RG 172.92–RG 172.101);
- (c) monitors trading and other market activity and (if relevant) disclosure by listed entities, to detect potential or actual non-compliance with the law or the market’s operating rules;
- (d) deals with actual or suspected breaches of the law or the market’s operating rules, including remedial, disciplinary and other deterrent measures;
- (e) deals with complaints about the market or participants;
- (f) shares supervisory responsibilities and information with:
  - (i) us; and
  - (ii) operators of other markets and clearing and settlement facilities that have the same participants as the market licensee; and
- (g) makes available and uses resources for conducting supervisory activities.

**Handling conflicts of interest**

RG 172.87 In assessing a market licensee’s arrangements for handling conflicts of interest, we will consider whether:

- (a) the arrangements comply with any regulations made under s798E;
- (b) under the arrangements, actual or potential conflicts of interest are reliably identified and appropriately responded to (see RG 172.88–RG 172.90); and
- (c) the market licensee’s organisational and reporting structures separate its commercial activities from its supervisory activities to a significant degree (see RG 172.91).

***When may conflicts of interest arise?***

RG 172.88 In order to identify and appropriately respond to actual or potential conflicts of interest, a market licensee will need to anticipate when such conflicts may arise.

RG 172.89 Conflicts between the commercial interests of the licensee and the need to ensure the market is fair orderly and transparent may arise in any area where a market licensee makes supervisory decisions. They may involve, for example, the market licensee's competitors (actual or potential), joint venturers, associates, or entities in which the market licensee has a significant shareholding. Conflict situations may also involve the market licensee's securities, or other financial products derived from these securities, that are traded on a market operated by the market licensee.

RG 172.90 Conflicts of interest may arise in connection with decisions about:

- (a) admission of a person to the market as either a participant or a listed entity;
- (b) participation in clearing and settlement facilities operated by the market licensee or a related entity;
- (c) monitoring of a listed entity or market participant;
- (d) investigative or disciplinary action; or
- (e) the exercise of discretions, such as granting waivers from the market's operating rules or charging variable fees.

*What are acceptable organisational and reporting structures?*

RG 172.91 The following are indicia of organisational and reporting structures that involve a significant separation of commercial and supervisory activities:

- (a) employees whose responsibilities involve both supervisory and commercial activities report to different people for each type of activity; and
- (b) employees who are responsible for monitoring and assessing the market licensee's compliance with its supervisory obligation report to:
  - (i) a person who is not responsible for making commercial decisions; or
  - (ii) a committee of the market licensee's board with a majority of independent, non-executive members.

### Monitoring participant conduct

RG 172.92 Under s792A(c)(ii), a market licensee must have adequate arrangements for monitoring the conduct of participants on or in relation to the market.

RG 172.93 What constitutes adequate arrangements for monitoring participant conduct will vary according to the nature of the market, its participants and the participant conduct being monitored. For example, arrangements for monitoring trading on a continuous electronic market may only be adequate if they involve constant electronic surveillance, whereas periodic physical attendance at a participant's office may constitute adequate arrangements for monitoring record keeping. In all situations, we will consider whether the arrangements ensure that the relevant regulatory outcomes in Table A are achieved.

RG 172.94 In the following paragraphs, we give guidance on:

- (a) who is a "participant"; and
- (b) what participant conduct must be monitored.

*Who is a "participant"?*

RG 172.95 A "participant" of a financial market is defined in s761A as "a person who is allowed to directly participate in the market under the market's operating rules". We consider that a person "directly participates" in a market if:

- (a) the person's access to the market's trading mechanism, for the purpose of making offers or invitations through the market, is not intermediated; or
- (b) the person has, or is taken to have, direct legal responsibility for an offer or invitation that has been made through the market (including for some or all of the obligations that arise immediately if a market contract is formed).

RG 172.96 Our interpretation of "participant" excludes a person who is able to transmit an offer or an invitation to a market's trading platform by means of an automated ("straight through") electronic order processing facility, in circumstances where:

- (a) the market's trading platform identifies the offer or invitation as having been transmitted from another person ("participant"); and
- (b) the market's operating rules make the participant (or another participant) legally responsible for the transmission.

In this situation, we consider that the person's access to the market is intermediated and the person does not "directly participate" in the market. This is the case whether the market operator or some other person makes the automated electronic order processing facility available.

*What participant conduct must be monitored?*

RG 172.97 Section 792A(c) does not require a market licensee to monitor all the diversified business activities of participants in its market. However, a market licensee must monitor conduct of participants:

- (a) “on or in relation to the market” (see s792A(c)(ii)); and
- (b) that is dealt with in the market’s operating rules (this is inherent in s792A(c)(iii) and expressly referred to in reg 7.2.07(b)).

Note: The participant conduct that must be monitored under s792A(c)(ii) and (iii) overlaps to a large extent because the operating rules must deal with conduct of participants “in relation to the market”: see reg 7.2.07(b).

RG 172.98 We interpret the words “on or in relation to the market” in s792A(c)(ii) as referring at a minimum to conduct by a participant that:

- (a) leads or may lead directly to or is part of a transaction effected through the market;
- (b) is connected with the settlement of transactions effected through the market, to the extent that participant conduct connected with settlement of those transactions is dealt with under the market’s operating rules;
- (c) relates to a participant’s ability to comply with the financial services law or the market’s operating rules and to meet all its obligations (including financial obligations) for business connected with the licensee’s market; or
- (d) where a participant deals on behalf of a client — relates to dealings between the participant and the client or prospective client connected with making or accepting of offers or invitations through the market or settling market transactions on behalf of the client.

RG 172.99 For those markets where participants deal on behalf of clients, we interpret s792A(c)(ii) and (iii) and reg 7.2.07 as requiring the operating rules to deal with (and a market licensee to monitor) the aspects of the participant–client relationship that are “in relation to the market”.

RG 172.100 We think that at a minimum this includes the following participant conduct towards clients or prospective clients:

- (a) conduct that relates to effecting transactions through the market on behalf of a client, including:
  - (i) the provision by participants to clients of information about the financial products able to be traded on the market and how they are traded; and
  - (ii) filtering of offers, invitations or acceptances received from clients; and
- (b) conduct that relates to a participant's rights against or obligations to a client, or a client's rights against or obligations to a participant, in connection with effecting or settling transactions effected or to be effected through the market, or with the holding or application of client money or client property for those purposes.

RG 172.101 If participants in a licensee's market are also participants in another market or markets, the market licensee must have appropriate supervision and information sharing arrangements with these markets. We consider that a participant's conduct does not fall outside the scope of a market licensee's supervisory obligation merely because of uncertainty about the market to which the conduct in question relates or was intended to relate, or because the participant is also a participant in another market.

### ***Sufficient resources: s792A(d)***

#### Financial resources

RG 172.102 In order to comply with the obligation in s792A(d) to have sufficient financial resources, a market licensee must assess what financial resources it will need to fund the ongoing proper operation of the market, its supervisory arrangements and all its other activities.

RG 172.103 A market licensee's assessment must be based on reasonable estimates of its revenue, expenses and liabilities. For newly established markets, it may not be appropriate to include any revenue in the assessment. For longer-established market licensees, the market's history of operation can be taken into account in determining the projected revenue, expenses and liabilities.

RG 172.104 A market licensee's financial resources must be sufficient to fund all its activities, not just the operation of a particular market. The stability and continuity of a particular market cannot be separated from the overall financial health and continuity of the market licensee.

## Technological resources

RG 172.105 If a market licensee wishes to implement a significant change to its technological resources, we will generally require an independent expert to verify at the licensee's expense the ongoing adequacy of its technological resources after the change.

RG 172.106 However, we may not require an independent expert's verification if, in light of the market licensee's record in technological development, we are satisfied that it has the internal expertise to verify to us the ongoing adequacy of its technological resources.

## ***Compensation arrangements: s792A(e)***

What are adequate Division 3 compensation arrangements?

RG 172.107 We will not adopt a final policy on compensation arrangements under Division 3 of Part 7.5 before we know the Government's final view on compensation arrangements in the financial services industry generally.

RG 172.108 In the meantime, we will assess each case individually and will be flexible in assessing whether particular arrangements are adequate. We will be concerned to ensure that retail clients have adequate redress, but we will attempt not to involve a market licensee in major "structural" change or investment. The fidelity fund provisions in the old Corporations Act may provide some guidance to market licensees about structuring Division 3 compensation arrangements.

Who is responsible for Division 3 compensation arrangements?

RG 172.109 A market licensee must be directly responsible for:

- (a) controlling and maintaining any compensation arrangements under Division 3 of Part 7.5;
- (b) ensuring their ongoing adequacy; and
- (c) determining claims and payments under these arrangements.

RG 172.110 A market licensee cannot satisfy its Division 3 compensation obligations by pointing to arrangements under someone else's control, such as:

- (a) individual insurance arrangements put in place by a participant in the licensee's market; or
- (b) an external dispute resolution scheme to which some or all of the participants in the licensee's market belong.

RG 172.111 However, it may be reasonable with appropriate safeguards for a market licensee to outsource or delegate aspects of the administration of its compensation arrangements: see s885I(2).

### Providing information about Part 7.5 compensation arrangements

RG 172.112 Under s792I, a market licensee must make publicly available up-to-date information that helps retail investors understand their rights and remedies under the compensation arrangements that are in place under Part 7.5. This includes information about:

- (a) the types of claims which can be made, by whom, how, and any relevant time limits for making claims;
- (b) what type of compensation may be provided and any monetary limits on that compensation;
- (c) who administers the compensation arrangements, the source of the funding, and the total size of the funding;
- (d) how long it takes to process claims, how claims are investigated and who makes the decisions about claims;
- (e) what review (if any) of decisions about claims is available; and
- (f) to whom information about the claim may be provided, and any other relevant confidentiality or privacy-related information.

RG 172.113 When choosing how information is to be made available to the public, a market licensee should take into account the need to periodically update the information. The Explanatory Memorandum refers to a market's internet site as a possible avenue for making the information publicly available: see paragraph 7.65. We think the information must also be available to members of the public who do not have access to the internet.

### ***Annual report: s792F***

RG 172.114 A market licensee's annual report must include an analysis of the extent to which the market licensee considers it has complied with the licensee obligations: see reg 7.2.06(c). We think that this analysis should be a form of self-assessment against previous planning for compliance: see RG 172.71–RG 172.72.

RG 172.115 We expect the analysis under reg 7.2.06(c) to:

- (a) state the objective outcomes and/or standards against which the market licensee has measured its compliance with each of its obligations and explain how those outcomes and/or standards evidence compliance with the particular obligation;
- (b) identify and explain any divergences during the year between the market licensee's planned and actual activities and resources for



performing its obligations and for monitoring its own performance of those obligations; and

- (c) state and explain the market licensee's conclusions about:
- (i) whether it has achieved those outcomes and/or standards and the extent to which it has fully complied with each obligation;
  - (ii) if less than full compliance is identified — how the market licensee will ensure it achieves full compliance with each obligation in the future;
  - (iii) the adequacy and effectiveness of its operating rules and procedures and of its supervisory arrangements in achieving a fair, orderly and transparent market;
  - (iv) the strengths and any weaknesses in its activities and resources for performing each of its obligations;
  - (v) the strengths and any weaknesses in its activities and resources for monitoring its own performance of each of its obligations; and
  - (vi) if any inadequacy or weaknesses have been identified — how the market licensee proposes to address or has addressed those matters.

## Explanation

### ***What should market licensees do to ensure compliance with the licensee obligations?***

#### Planning

RG 172.116 If a market licensee fails to plan how it will ensure, monitor and assess its compliance, we think it is unlikely that the licensee will be able to:

- (a) ensure compliance with its licensee obligations;
- (b) demonstrate to us that it is complying and will continue to comply with its licensee obligations;
- (c) notify us of potential or actual breaches; or
- (d) make the analysis of its compliance that we expect in its annual report.

#### Monitoring and assessing

RG 172.117 Regulation 7.2.06(c) requires a market licensee to analyse the extent to which it considers that its activities and resources have resulted in full compliance with its licensee obligations. It would be impossible for a market licensee to comply with this obligation without

monitoring and assessing the extent of its compliance. We think such monitoring and assessing will also help ensure continuous compliance with the licensee obligations.

RG 172.118 A market licensee remains responsible for compliance with each of its licensee obligations even if it outsources performance of some aspect of the obligations. Therefore, a market licensee must have adequate processes for monitoring and assessing the performance of any outsourced activities.

### ***What is our general approach to assessing compliance with the licensee obligations?***

How will we assess compliance?

RG 172.119 Section 794C(1) specifically provides that, when assessing compliance with the licensee obligations, we may take into account any information and reports that we think appropriate. The specific licensee obligations in s792B, 792C, 792D, 792E and 792F ensure that we have the information and reports necessary to assess compliance.

### ***Supervisory obligation: s792A(c)***

Monitoring the conduct of participants

*What participant conduct must be monitored?*

RG 172.120 In determining what aspects of the participant-client relationship must be monitored under s792A(c), we have taken into account the fact that a market's operating rules must include requirements about participant conduct in relation to the licensed market that:

- (a) have the objective of "promoting honesty and fair practice" (see reg 7.2.07(b)(i)); and
- (b) punish conduct "inconsistent with just and equitable principles in the transaction of business" (see reg 7.2.07(b)(iii)).

RG 172.121 The market licensee's operating rules must also facilitate the assessment and, if appropriate, the investigation of market-related disputes between participants and their clients: see reg 7.2.07(i).

### ***Compensation arrangements: s792A(e)***

Who is responsible for Division 3 compensation arrangements

RG 172.122 Under s792A(e) and 881A(1), a market licensee must ensure that it has approved Division 3 compensation arrangements in relation to its market. The licensee also has a number of ongoing obligations in relation to those arrangements. If the Minister considers at any time that the market licensee's compensation arrangements under

Division 3 of Part 7.5 are not adequate, approval of the arrangements may be revoked: see s882C.

RG 172.123 Given a market licensee's compensation obligations and the potential impact on its licence in the event of non-compliance, we think that the obligation on the market licensee under s792A(e) is to have compensation arrangements that are under its own control.

RG 172.124 We think the Corporations Act also requires a market licensee to have ultimate responsibility for determining claims made under its Division 3 arrangements and for paying compensation, as these are aspects of the market licensee's control of the arrangements. This follows from provisions such as s883C (other sources of funds), s892D (powers of relevant authorities) and the levy provisions in s883D.

## F How do you get an Australian market licence?

---

RG 172.125 The Minister may grant an applicant an Australian market licence if satisfied that the criteria in s795B(1) or (2) are met. This guide deals with the criteria in s795B(1). The criteria in s795B(2) for an application from an overseas market operator will be dealt with in a separate policy.

RG 172.126 This section sets out:

- (a) what you must include with your application (see RG 172.127–RG 172.136);
- (b) how we will deal with your application (see RG 172.137–RG 172.141); and
- (c) what we will consider when advising the Minister on your application (see RG 172.142–RG 172.155).

### Our policy

#### ***What must you include with your application?***

RG 172.127 There is no application form for an Australian market licence. An application must be made in accordance with s795A and include the information and documents referred to in reg 7.2.11 and 7.2.12. Where the regulations require “a description” or “details” of certain matters, we expect an applicant to give sufficient description or details to provide the Minister and us with a comprehensive understanding of the relevant matter.

RG 172.128 An applicant must provide documents or information that positively demonstrate that it meets the criteria in s795B(1). In particular, the applicant must demonstrate that it has the skills, expertise, procedures and capacity to satisfy each of its obligations when the market commences and on a continuing basis: see s795B(1)(b).

RG 172.129 The information and documents required will vary depending on the features of the market. Examples include:

- (a) representations by each of the applicant’s directors that, to the best of the director’s knowledge, the applicant meets the criteria in s795B(1);
- (b) descriptions of the systems, structures, processes and resources which the applicant will use to comply with its licensee obligations;

- (c) independent verification of the systems, structures, processes and resources which the applicant will use to comply with its licensee obligations; and
- (d) evidence of testing of the market's systems and processes.

RG 172.130 We expect the applicant to certify that the information and documents provided with the application are true, correct and complete.

RG 172.131 We will consider issuing further guidance on applying for a licence if needed.

### Supervisory arrangements

RG 172.132 At the application stage, it will generally be difficult for an applicant to demonstrate that it has adequate arrangements for supervising the market (see s792A(c) and 795B(1)(d)) because those arrangements may be untested.

RG 172.133 We think that the best way for an applicant to demonstrate that it has adequate arrangements is by showing that it has planned how it will comply with its supervisory obligation: see RG 172.71–RG 172.72. The planning should:

- (a) cover in detail the applicant's arrangements for supervising the market over at least the forthcoming year, including how it will monitor and assess the adequacy of these arrangements; and
- (b) deal with each of the matters referred to in s792A(c), namely:
  - (i) handling conflicts of interest;
  - (ii) monitoring the conduct of participants on or in relation to the market; and
  - (iii) enforcing compliance with the operating rules.

### Financial resources

RG 172.134 It may also be difficult for an applicant to demonstrate the adequacy of its financial resources: see s792A(d) and 795B(1)(b).

RG 172.135 We will generally be satisfied that a new applicant for a market licence has sufficient financial resources, if it has access to enough readily realisable financial resources to meet the financial requirements (including liabilities) that will arise during at least the first 12 months after the licence is granted, from:

- (a) the operation of the market;
- (b) the applicant's supervisory arrangements; and
- (c) any other activity the applicant conducts.

RG 172.136 An applicant must base its assessment of the amount required on reasonable estimates of its revenue, expenses and liabilities over the 12-month period. For most start-up markets, in particular, this will mean that it will not be appropriate to include any revenue in the assessment.

### ***How will we deal with your application?***

RG 172.137 The time it will take us to provide the Minister with advice about an application depends on the complexity of the application. We aim to deal with simpler applications within 12 weeks of receiving them. More complex applications will take up to 16 weeks. These time frames are based on receiving *all* information and documents required. If we ask you to supply more information, we do not count the time during which we are waiting for your response. If the application requires public consultation, this will normally take a further 6 weeks.

RG 172.138 We will decide whether your application requires public consultation on a case-by-case basis. The factors we will consider when making this decision include:

- (a) whether the market may have a regulatory impact on existing licensed markets;
- (b) whether the market may affect the reputation of Australia as a financial centre;
- (c) the features of the market, including:
  - (i) the size of the financial market; and
  - (ii) the market users; and
- (d) the likely impact of the market on Australian investors and the integrity of Australian markets.

RG 172.139 We will return any application that does not contain the information and documents required by the Corporations Act and the regulations.

RG 172.140 We may request clarification or explanation of the information or documents provided by an applicant.

RG 172.141 We may also request independent verification by a suitably qualified third party of a particular matter or aspect of the market's operation. In such a case, the applicant must provide the verification at its own cost. We will generally require independent verification of the adequacy of an applicant's technological and financial resources.

### ***What will we consider when advising the Minister about your application?***

RG 172.142 When framing our advice to the Minister about granting a licence, we will consider:

- (a) the law and regulations, particularly the matters in s795B and 798A;
- (b) how the regulatory outcomes in Table A will be achieved in the market's operation; and
- (c) what conditions might need to be imposed on a market licence.

#### **Licence conditions**

RG 172.143 In our advice to the Minister, we may include suggestions about the mandatory conditions on a licence: see s796A(4), 882A(4), 882B(4)(b) and RG 172.160–RG 172.161.

RG 172.144 We may also advise the Minister to impose supplementary conditions, especially where such conditions are necessary to ensure:

- (a) a regulatory outcome in Table A is achieved, for example:
  - (i) a condition requiring the market licensee to provide a risk disclosure statement to each new participant on the market about particular risks associated with the market; or
  - (ii) conditions dealing with the market licensee's other activities, so as to minimise the effect of any failure in those other activities on the market; or
- (b) compliance with the licensee obligations, for example:
  - (i) a condition requiring the appointment of a person to perform a particular role in relation to the market (such as supervisor); or
  - (ii) a condition requiring the market operator to regularly report to us on its financial resources.

RG 172.145 We will consult with the applicant about the type of conditions we may recommend before we give our advice to the Minister about the application.

#### **Clearing and settlement**

RG 172.146 A financial market may have:

- (a) no clearing and settlement arrangements;
- (b) clearing and settlement arrangements not provided by a CS facility licensee; or
- (c) clearing and settlement arrangements provided by a CS facility licensee.

RG 172.147 We will advise the Minister that the applicant should have some form of clearing and settlement arrangements if:

- (a) concluded contracts are entered into on the market; and
- (b) parties to contracts do not know in advance the identity of the person with whom they contract.

RG 172.148 We may also advise the Minister that clearing and settlement arrangements are necessary in other circumstances, particularly where there are retail market users.

RG 172.149 We will consider the following factors in deciding whether to advise the Minister that an applicant's clearing and settlement arrangements should be provided by a CS facility licensee:

- (a) whether the clearing and settlement arrangements will be provided by a person other than a participant, or an agent of a participant, in the market;
- (b) the size and sophistication of the market, including whether there are retail market users in the market;
- (c) the classes of financial products and the anticipated volume of trading;
- (d) the complexity of the clearing and settlement arrangements proposed for the market, including the resources required to conduct the arrangements;
- (e) the procedures for dealing with failure to settle;
- (f) whether the clearing and settlement arrangements may result in systemic risks; and
- (g) the extent to which the clearing and settlement arrangements are otherwise regulated, for example, whether the arrangements are set out in the market's operating rules.

RG 172.150 We will consider issuing further guidance on what we consider to be adequate clearing and settlement arrangements if our experience in the administration of this policy indicates the need for such guidance. We will also consider issuing policy or guidance on applying for a CS facility licence, if needed.

### Operating rules

RG 172.151 Operating rules are all rules determined or established by the market operator that:

- (a) deal with the activities or conduct of the market or the activities or conduct of persons in relation to the market;



- (b) impose substantive obligations on, or grant rights to, the market operator, any market user, any participant or any listed entity; and
- (c) are not written procedures as required by the regulations or compensation rules within the meaning of Part 7.5.

Note: For example, a form prescribed by an operating rule would generally not be an operating rule because it does not impose substantive obligations.

RG 172.152 Operating rules may include rules relating to matters other than those specified in reg 7.2.07.

RG 172.153 When reviewing a market's operating rules as part of a licence application (or when reviewing amendments to the rules), we will consider whether, in light of the features of the market, the rules:

- (a) meet the requirements of the Corporations Act and regulations and, in particular, whether the rules ensure that the market is fair, orderly and transparent;
- (b) are legally effective;
- (c) are consistent with the licensee obligations and existing or proposed licence conditions;
- (d) may mean the regulatory outcomes in Table A are not achieved;
- (e) may undermine the policy of the law that the Minister should be able to disallow rules that are objectionable from a regulatory perspective;

Note: For example, a rule that gives a market licensee a general power to waive other rules may undermine the policy because it may effectively allow the market licensee to amend the rules without requiring the amendment to be considered by the Minister in accordance with s793E.

- (f) can be effectively implemented, including whether the market operator has systems, structures, processes and resources to administer the rules and supervise compliance with the rules; and
- (g) are consistent with international standards in comparable regulatory regimes.

### Written procedures

RG 172.154 If written procedures deal with matters relating to operating rules, they should only deal with administrative matters and not impose substantive obligations.

RG 172.155 Written procedures should be clearly identifiable as such so that there is no confusion about what constitutes the market's operating rules.

## Underlying principles

RG 172.156 In order to advise the Minister about a licence application, we need to understand the way in which the proposed market will operate. In dealing with applications, we seek to be flexible. However, there are certain minimum requirements that we think are necessary for us to adequately advise the Minister about an application.

## Explanation

### ***What must you include with your application?***

#### Financial resources

RG 172.157 In deciding that generally an applicant should have access to sufficient readily realisable resources to meet its financial requirements for 12 months, we were guided by the reference to 12 months in reg 7.2.12(h), and by our own experience in dealing with market applications.

### ***What will we consider when advising the Minister about your application?***

RG 172.158 The Minister must have regard to any relevant advice we give him about an application: see s798A(2)(h). The Minister must also consider specific matters in s798A(2) that relate to the features of the market.

#### Licence conditions

RG 172.159 A significant change from the old Corporations Act is the power of the Minister to impose conditions when issuing a licence. The Minister's ability to impose conditions on a licence is a key component to providing flexibility in the administration of the market provisions. We may give advice to the Minister about the conditions that we think should apply to a market licensee.

RG 172.160 Section 796A(3) stipulates when licence conditions can be imposed. All licences are subject to mandatory conditions, set out in s796A(4), which specify:

- (a) the particular market that is licensed;
- (b) the class or classes of financial product that can be dealt with on the market; and
- (c) the type of clearing and settlement arrangements, where the Minister considers that the market licensee should have clearing and settlement arrangements.

RG 172.161 If compensation arrangements under Division 3 of Part 7.5 are required, a licence will also include mandatory conditions under s882A(4) or 882B(4)(b) setting out the minimum amount of cover and the source of the funds.

### Clearing and settlement

RG 172.162 “Clearing and settlement arrangements” is defined in s790A as arrangements for the clearing and settlement of transactions. They may or may not be provided by a CS facility licensee. A CS facility licensee is licensed to operate a clearing and settlement facility. “Clearing and settlement facility” is defined in s768A and reg 7.1.09 and 7.1.10.

RG 172.163 We think that clearing and settlement arrangements (whether provided by a CS facility licensee or not) are necessary for anonymous markets. Without clearing and settlement arrangements, people trading on an anonymous market may not be able to achieve efficient settlement of transactions. Without some assurance of efficient settlement processes, a market will not be orderly.

RG 172.164 It is difficult to determine when clearing and settlement arrangements should or should not be provided by a CS facility licensee. Our approach identifies circumstances and factors that we think are relevant in determining when the more regulated clearing and settlement arrangements provided by a CS facility licensee must be in place. These factors revolve around the complexity of the clearing and settlement arrangements and the likely size of the market.

### Operating rules

RG 172.165 Effective operating rules are essential for a fair, orderly and transparent market, and we will consider them in detail when reviewing a licence application.

RG 172.166 “Operating rules” is defined in s761A and the minimum content of the operating rules is specified in reg 7.2.07: see Explanatory Memorandum, paragraph 7.77.

RG 172.167 The Corporations Act emphasises the importance of operating rules by requiring them to be considered when a market application is made and by providing that a change to a rule be subject to the power of the Minister to disallow the amendment: see s793D, 793E and 795B(1)(c).

RG 172.168 The Corporations Act also provides that the operating rules have effect as a contract under seal: see s793B. A range of persons, including a person aggrieved by a failure to comply with the rules, may take action to enforce the operating rules: see s793C.

RG 172.169 Most markets also have a range of procedures and guidance notes. It is important that there be a clear understanding of which procedures and guidance notes, if any, are in fact operating rules. Failure to lodge a change to an operating rule has a significant consequence, in that the change ceases to have effect at the end of the 21-day period allowed for lodging the rule with us.

RG 172.170 We recognise that not all requirements imposed by a market licensee are operating rules, so we think it is important to indicate the matters that we do not consider to be operating rules. Our proposed test focuses on whether a substantive obligation is imposed by the rule, in which case it should be regarded as an operating rule.

### Written procedures

RG 172.171 The Corporations Act distinguishes between operating rules and written procedures. Regulation 7.2.08 prescribes the content of written procedures. The Explanatory Memorandum recognises that written procedures may include matters in addition to those prescribed by the regulation: see paragraph 7.77.

RG 172.172 Generally, written procedures will not impose substantive obligations on participants or market users. Substantive obligations should be contained in the operating rules so as to ensure that they are legally binding and subject to Ministerial disallowance. We would expect written procedures to operate as explanation, detailing processes and arrangements, and amplifying the operating rules.

## **Schedule: What types of activities will require an Australian market licence?**

---

RG 172.173 The examples in the Schedule illustrate how to use this guide to work out whether a person must hold an Australian market licence in order to operate various kinds of facilities.

The examples relate to:

- A** Order routing systems: see RG 172.174
- B** internet portals: see RG 172.175
- C** Electronic trading services: see RG 172.176
- D** Cross-border trading screens: see RG 172.177

**Important note: This Schedule contains examples of the application of our policy in Sections B, C and D. The examples illustrate our policy; they do not constitute our policy. The examples are not comprehensive; they do not describe all possible forms of financial market.**

## A Order routing systems

RG 172.174

### Does the company require an Australian market licence?

<p>What are the facts?</p>	<p>(a) A company operates an electronic service that allows persons to enter offers or invitations for acquisition or disposal of financial products.</p> <p>(b) The electronic service transmits or routes those offers or invitations to another person who forwards them to a financial market, not operated by the company, for quotation or execution.</p> <p>(c) The electronic service does not perform any function other than transmitting or routing the offers or invitations. In particular, offers or invitations are not altered in any way before they are transmitted to the financial market. (However, the offers or invitations may be aggregated and/or filtered. If the filters detect any problems, the offer or invitation is either returned to the person who placed it or otherwise diverted from the service.)</p>
<p>Does the company operate a financial market?</p>	<p>The company is not operating a financial market: the facility operated by the company is not one through which offers or invitations are made.</p> <p>The offers and invitations are <i>made</i> when they are received by the person to whom the offer or invitation is made or by their agent. The offers or invitations are received on the financial market to which the order routing system routes them, not on the order routing system.</p> <p><b>See RG 172.24.</b></p> <p>Offers or invitations are not made <i>through</i> a facility merely because that facility is a step in the process that results in the eventual making of the offer or invitation. <b>See RG 172.20.</b></p>

**On these facts, the company does not require an Australian market licence.**

**The company should consider whether it needs an Australian financial services licence.**

## B internet portals

RG 172.175

### EXAMPLE 1: Does the company require an Australian market licence?

<p>What are the facts?</p>	<ul style="list-style-type: none"> <li>(a) A company, registered under Chapter 2A of the Corporations Act, operates a financial services website.</li> <li>(b) Various licensed advisers, brokers, fund managers and market operators advertise their services on the company's site.</li> <li>(c) On entering the site, viewers see a prominent disclaimer stating that the company does not in any way endorse any services or markets that may be accessed through the site.</li> <li>(d) Viewers can click on links that take them from the company's site to other websites, some of which are operated by Australian market licensees and provide access to licensed markets and some of which are operated by foreign companies and provide access to markets which are not licensed under Australian law.</li> <li>(e) The company receives remuneration from linked sites based on the number of viewers who use the relevant link.</li> <li>(f) When viewers activate a link to another website, they immediately see a pop-up box telling them they are leaving the company's site. Similarly, when returning to the company's site, viewers see a pop-up box telling them they are entering the company's site.</li> <li>(g) The company does not endorse, select, modify or exercise control over the content of material on its website, except that it retains the right to remove, or refuse to transmit, material it considers may be illegal or defamatory.</li> </ul>
<p>Does the company operate a financial market?</p>	<p>The company is not operating a financial market: the facility operated by the company is not one through which offers or invitations are made.</p> <p>The offers and invitations are <i>made</i> when they are received by the person to whom the offer or invitation is made or by their agent. The offers or invitations are received on the financial markets which are accessed through the internet portal operated by the company. <b>See RG 172.24.</b></p> <p>Offers or invitations are not made <i>through</i> a facility, such as an internet portal, merely because that facility is a step in the process that results in the eventual making of the offer or invitation. <b>See RG 172.20.</b></p>

**On these facts, the company does not require an Australian market licence.**

***B internet portals (continued)*****EXAMPLE 2: Does the company require an Australian market licence?**

What are the facts?	<p>(a) A company, registered under Chapter 2A of the Corporations Act, operates a financial services facility, including a website.</p> <p>(b) On the website various licensed dealers indicate their willingness to deal in certain financial products and/or provide firm prices for financial products.</p> <p>(c) Using the facility, investors viewing the site may submit a price enquiry on a financial product listed on the site. The investor's price enquiry and contact details are then forwarded to all dealers in the facility who have indicated their willingness to deal in the relevant financial product. Any dealer may then contact the investor, and negotiations take place between the dealer and investor.</p> <p>(d) Alternatively, investors viewing the site can click on a dealer's firm price posted on the site. The dealer is then notified of the investor's interest and can contact the investor to negotiate a contract.</p> <p>(e) In both the situations described in paragraphs (c) and (d), contracts are negotiated directly between the investor and the dealer, and the dealer is entitled to withdraw offers or invitations made through the website if not satisfied about the ability of the investor to settle the transaction.</p>
Does the company operate a financial market?	<p>The company is operating a financial market: the facility operated by the company is one through which offers or invitations are made.</p> <p>At a minimum, the communications made on the facility are requests to enter into a course of negotiations with a view to entering into a binding contract. They identify persons who are likely to acquire or dispose of financial products and the prices at which those persons are likely to acquire or dispose of a financial product. <b>See RG 172.22–RG 172.23.</b></p>
Does the company operate that market in Australia?	<p>The market is operated in Australia because the company is registered under Chapter 2A of the Corporations Act. <b>See s791D(1).</b></p>
Will the market be exempted from the operation of Part 7.2?	<p>We will not advise that the market be exempted from the operation of Part 7.2. There is public benefit in regulating the market under Part 7.2. <b>See RG 172.52.</b></p>

**On these facts, the company requires an Australian market licence.**



## C Electronic trading services

RG 172.176

### EXAMPLE 1: Does the company require an Australian market licence?

<p>What are the facts?</p>	<ul style="list-style-type: none"> <li>(a) A company, registered under Chapter 2A of the Corporations Act, operates an electronic trading service for the trading of shares in bodies corporate.</li> <li>(b) The company is a participant of a market that is licensed under Part 7.2 and is also a licensed dealer under Part 7.6.</li> <li>(c) The operation of the electronic trading service is governed by the operating rules of the licensed market and supervised by the operator of that licensed market.</li> <li>(d) The electronic trading service allows users to trade in shares of specific bodies corporate, all of which are listed on the licensed market.</li> <li>(e) The electronic trading service allows users to anonymously display bid and offer prices and order sizes.</li> <li>(f) The electronic trading service executes orders against orders received from other users of the electronic trading service.</li> <li>(g) The volume of trades executed on the electronic trading service in any particular class of shares of a particular body corporate does not exceed 10% of the total for that class.</li> </ul>
<p>Does the company operate a financial market?</p>	<p>The company operates a financial market: the electronic trading service is a facility through which offers to acquire or dispose of financial products are regularly made and accepted.</p>
<p>Does the company operate that market in Australia?</p>	<p>The market is operated in Australia because the company is registered under Chapter 2A of the Corporations Act. <b>See s791D(1).</b></p>
<p>Will the market be exempted from the operation of Part 7.2?</p>	<p>We may advise the Minister to exempt the market from the operation of Part 7.2. The market is subject to other forms of regulation that are sufficient to achieve the outcomes in Table A. <b>See RG 172.52–RG 172.53.</b></p> <p>The market is subject to regulation:</p> <ul style="list-style-type: none"> <li>(a) by the operator of the licensed market in paragraph (c); and</li> <li>(b) of the company under Part 7.6 (financial service providers).</li> </ul>

**On these facts, we may advise the Minister to exempt the market from the operation of Part 7.2.**

**C Electronic trading services (continued)****EXAMPLE 2: Does the company require an Australian market licence?**

What are the facts?	<p>(a) Paragraphs (a) to (f) of Example 1 apply.</p> <p>(b) The volume of trades executed on the electronic trading service in any particular class of shares of a particular body corporate exceeds 50% of the total for that class.</p>
Does the company operate a financial market?	The company operates a financial market: the electronic trading service is a facility through which offers to acquire or dispose of financial products are regularly made and accepted.
Does the company operate that market in Australia?	The market is operated in Australia because the company is registered under Chapter 2A of the Corporations Act. <b>See s791D(1).</b>
Will the market be exempted from the operation of Part 7.2?	We will not advise that the market be exempted from the operation of Part 7.2. In light of the volume of trading on the electronic trading service, regulation of the market under Part 7.2 is in the public interest. <b>See RG 172.52–RG 172.53.</b>

**On these facts, the company requires an Australian market licence.**

**C Electronic trading services (continued)****EXAMPLE 3: Does the company require an Australian market licence?**

What are the facts?	<p>(a) A company, incorporated under the law of a foreign jurisdiction, operates an electronic trading service through the internet.</p> <p>(b) The electronic trading service allows users to trade in specific securities, none of which is listed on an Australian licensed market.</p> <p>(c) The electronic trading service allows users to anonymously display bid and offer prices and order sizes in the relevant securities.</p> <p>(d) The electronic trading service executes orders against orders received from other users of the electronic trading service.</p> <p>(f) On entering the site, viewers see a prominent and true statement that the market is regulated by the law of the foreign jurisdiction and may only be used by residents of that jurisdiction.</p> <p>(g) Prices on the market are not denominated in Australian dollars.</p> <p>(h) The operator screens offers sent from Australian addresses, but five Australian investors have directly participated in the market and purchased securities through the market in the last year.</p>
Does the company operate a financial market?	The company operates a financial market: the electronic trading service is a facility through which offers to acquire or dispose of financial products are regularly made and accepted.
Does the company operate that market in Australia?	<p>The market is not operated in Australia:</p> <p>(a) the operator of the market is not a body corporate registered under Chapter 2A of the Corporations Act;</p> <p>(b) the market is not located in Australia; and</p> <p>(c) although the market has Australian participants, the operator of the market does not target Australian investors. <b>See RG 172.38.</b></p> <p>When taken as a whole, the facts and circumstances pertaining to the market indicate that the operator has not targeted Australian investors, even though Australian investors have used the market.</p> <p><b>See RG 172.40–RG 172.43.</b></p>

**On these facts, the company does not require an Australian market licence.**

## D Cross-border trading screens

RG 172.177

### Does the company require an Australian market licence?

<p>What are the facts?</p>	<p>(a) A company, incorporated under the law of a foreign jurisdiction, operates a securities market that is regulated in that jurisdiction.</p> <p>(b) The market has a trading system that permits participants to enter orders and effect trades on-screen, via market screens located in their offices.</p> <p>(c) The market screens are connected to the trading system of the market through secure access.</p> <p>(d) A participant located in Australia has direct secure access to the market's trading system via a market screen in its office in Australia and uses it to enter bids and offers on the market on behalf of a number of its Australian clients.</p>
<p>Does the company operate a financial market?</p>	<p>The company operates a financial market: it operates a facility on which offers to acquire or dispose of securities are regularly made and accepted.</p>
<p>Does the company operate that market in Australia?</p>	<p>The market operates in Australia because it has an Australian participant and is targeted at Australian investors. <b>See RG 172.38 and RG 172.40–RG 172.43.</b></p> <p>The fact that the market also operates in another jurisdiction does not preclude the conclusion that it operates in Australia. <b>See RG 172.38.</b></p>
<p>Will the market be exempted from the operation of Part 7.2?</p>	<p>Although the market is regulated by the laws of a foreign jurisdiction, we will not advise that the market be exempted from Part 7.2. <b>See RG 172.55.</b></p>

**On these facts, the company requires an Australian market licence.**

## Key terms

---

RG 172.178 In this guide, unless a contrary intention appears:

“ASIC” means the Australian Securities and Investments Commission

“Corporations Act” means the *Corporations Act 2001* (as amended by the FSR Act) and includes regulations made for the purposes of that Act

“CS facility licensee” means a person who holds an Australian CS facility licence

Note: This is a definition contained in s761A of the Corporations Act.

“Explanatory Memorandum” means the Explanatory Memorandum to the *Financial Services Reform Bill 2001*

“financial product” has the meaning given by Division 3 of Part 7.1 of the Corporations Act

Note: This is a definition contained in s761A of the Corporations Act.

“FSR Act” means the *Financial Services Reform Act 2001* and includes regulations made for the purposes of the FSR Act

“FSR commencement” means 11 March 2002, the date fixed by Proclamation under s2(2) of the FSR Act on which Schedule 1 of the FSR Act is to commence

Note: Schedule 1 contains the financial market licensing provisions under Part 7.2.

“licence” means an Australian market licence under s795B that authorises a person to operate a financial market

“licensee obligations” means the obligations of a market licensee as set out in Subdivision A of Division 3 of Part 7.2 of the Corporations Act

“market licensee” means a person who holds an Australian market licence

Note: This is a definition contained in s761A of the Corporations Act.

“market users” means investors who acquire or dispose of financial products in a financial market. Investors may be participants dealing for themselves or, where participants act as intermediaries, the clients of the participants

“old Corporations Act” means the Corporations Act as in force immediately before FSR commencement

“participant” means a person who is allowed to directly participate in the market under the market’s operating rules

Note: This is a definition contained in s761A of the Corporations Act.

“Part 7.2” (for example) means a Part of the Corporations Act (in this example numbered 7.2)

“RG 141” (for example) means a regulatory guide (in this example numbered 141)

“reg 7.2.10” (for example) means a regulation in the *Corporations Amendment Regulations 2001 (No 4)* (in this example numbered 7.2.10)

“retail client” has the meaning given by s761G

Note: This is a definition contained in s761A of the Corporations Act.

“supplementary condition” means a condition on an Australian market licence other than a condition referred to in s796A(4), 882A(4) or 882B(4)(b)

“s782” (for example) refers to a provision of the Corporations Act (in this example numbered 782).

## Related information

---

RG 172.179

### Headnotes

Australian market licence, financial market, financial market regulation, regulatory outcomes, exemptions, fair, orderly and transparent, supervisory obligation, supervisory arrangements, conflicts of interest, financial resources, licence conditions, clearing and settlement arrangements, operating rules, written procedures

### Policy statements

Superseded Policy Statement 70 *Exempt futures markets* [SPS 70]

Superseded Policy Statement 100 *Stock markets* [SPS 100]

### Regulatory guides

RG 141 *Offers of securities on the internet*

### Legislation

Corporations Act, Chap 2A, Part 7.2, Part 7.5, Part 7.6, s761A, 765A, 767A, 768A, 790A, 791A, 791C, 791D, 792A, 792B, 792C, 792D, 792E, 792F, 792G, 792H, 792I, 793B, 793C, 793D, 793E, 794C, 795A, 795B, 796A, 798A, 881A, 882A, 882C, 883C, 883D, 892D, Corporations Amendment Regulations 2001 (No 4), reg 7.1.09, 7.1.10, 7.2.06, 7.2.07, 7.2.08, 7.2.11, 7.2.12, Acts Interpretation Act 1901, s15AA

### Cases

*AG for NSW v Australian Fixed Trusts Ltd* [1974] 1 NSWLR 110, 117

*AG for NSW v The Mutual Home Loans Fund of Australia Ltd* [1971] 2 NSWLR 162, 165

*Carragreen Currency Corporations Pty Ltd v Corporate Affairs Commission (NSW)* (1986) 11 ACLR 298, 312-3

*Entores Ltd v Miles Far East Corporations* [1955] 2 QB 327

*Express Airways v Port Augusta Air Services* [1980] QdR 543

*Hampstead Meats Pty Ltd v Emerson and Yates Pty Ltd* [1967] SASR 109

*Mendelson-Zeller Co Inc v T & C Providores Pty Ltd* [1981] 1 NSWLR 366

*Voth v Manildra Flour Mills Pty Ltd* (1990) 171 CLR 538, 568

**Consultation papers**

CP 29 *Australian market licences: Australian operators* (November 2001)

**Media releases**

[MR 02/76] Australian market licences under Financial Services Reform Act, 6 March 2001



## Addendum: Supplementary guidance on market licensee systems and controls

### Key points

This addendum supplements our guidance in RG 172, and outlines our expectations under the Corporations Act for domestic market licensees to:

- maintain adequate systems and controls to ensure that the market they operate is fair, orderly and transparent;
- maintain sufficient resources in relation to their systems and controls that are appropriate for the nature, size and complexity of the market;
- have in place appropriate testing arrangements, adequate business continuity plans, sufficient capacity and adequate security in relation to their systems. Procedures should be in place to monitor and review these arrangements periodically; and
- notify ASIC of major system changes in sufficient time before the changes occur, and have appropriate processes to communicate information technology system management plans to stakeholders.

RG 172.180 Under s792A of the Corporations Act, holders of an Australian market licence under s795B(1) (market licensees) must, to the extent it is reasonably practicable to do so, do all things necessary to ensure that the market they operate is a fair, orderly and transparent market.

Note: In this addendum, the term ‘market licensees’ refers to domestic market licensees only—that is, holders of an Australian market licence under s795B(1).

RG 172.181 Market licensees should have sufficient resources, including appropriate technological resources. RG 172 provides general guidance for market licensees—at RG 172.12 and RG 172.105–RG 172.106—on the requirements and verification of technological resources.

RG 172.182 As markets have become more automated and high-speed in nature, we believe that it is appropriate to supplement our guidance in RG 172 on market licensee systems and controls. This addendum outlines our expectations under the Corporations Act for domestic market licensees to maintain adequate systems and controls and ensure that their technology releases are well managed.

### How this guidance applies

RG 172.183 This guidance applies to all domestic market licensees—that is, holders of an Australian market licence under s795B(1) of the Corporations Act. In an

increasingly technology-driven and competitive market environment, it is important that our expectations are clear and consistently applied to these market licensees, even though the markets may differ in their nature, size and complexity. The high-level principles in this addendum constitute a broad framework for systems and controls relevant to all these market licensees. We expect market licensees' systems and controls to be proportionate to the scale and scope of their business.

- RG 172.184 In general, we expect these market licensees' systems to be robust enough to perform reliably through stressed market conditions and ensure continuity of the trading that takes place through the market, including having sufficient capacity to cater for spikes in the volume of messaging traffic. We also expect that all market participants seeking access to the market licensee's systems or services (including co-location services) should have access on fair, non-discriminatory terms.
- RG 172.185 The guidance provided in this addendum about our expectations for systems and controls is relevant to each market to different degrees. How the guidance applies will depend on the size of the market, the complexity of trading and the number and type of market participants and connections in the market. Examples used in this addendum are not intended to be exhaustive.
- RG 172.186 We will assess a market licensee's compliance with the principles in this addendum as part of our periodic assessment of the licensee and in our assessment of any changes the licensee may propose to make to its systems. We will also take into account the licensee's self-assessment of the extent to which it has complied with these principles.

## Appropriate testing arrangements for trading systems

- RG 172.187 Market licensees should have appropriate testing arrangements to ensure that their systems are functional and reliable, and do not pose a threat to fair and orderly trading. Testing is a crucial part of ensuring that trading and other key systems function as intended.
- RG 172.188 The testing methodologies should be designed to ensure that:
- (a) the operation of the system complies with relevant regulatory obligations;
  - (b) controls embedded in the systems work as intended; and
  - (c) electronic trading systems can continue to work effectively in stressed market conditions.
- RG 172.189 When introducing or modifying an electronic trading system, relevant testing should be performed before going live, including but not limited to the types of testing listed below. The results of trading systems testing should be documented and made available to ASIC on request.

## Connectivity testing

- RG 172.190 A market licensee should perform connectivity testing to validate the continuity of network communications by verifying that the network is properly connected, with message traffic taking the desired route. For example, if a market licensee plans to introduce a new electronic trading system, it could use a 'simulated trading environment' to make sure that the system and market participants are properly connected to enable interactions to take place.
- RG 172.191 Connectivity testing could also involve testing data feeds to the market licensee, such as from market data providers, relevant clearing and settlement facilities, as well as the connectivity between market licensees.
- RG 172.192 Market licensees subject to regulation under the ASIC Market Integrity Rules (Competition in Exchange Markets) 2011 should test their connectivity with each other to ensure they comply with their cooperation requirements for the coordination of trading suspensions and information sharing under Section I of Regulatory Guide 223 *Guidance on ASIC market integrity rules for competition in exchange markets* (RG 223).

## Conformance testing

- RG 172.193 A market licensee should perform conformance testing designed to determine whether a system meets predefined standards—for example, whether the system complies with Financial Information eXchange (FIX) protocols and specifications, and that quality assurance standards are being met. It should include interoperability testing and confirmation of associated internal procedures.
- RG 172.194 Conformance testing should also include testing for compliance with the market licensee's operating rules and procedures, obligations under the Corporations Act or ASIC market integrity rules (to the extent that they apply to systems and controls).

## Regression testing

- RG 172.195 A market licensee should perform regression testing to detect potential problems in existing functional and non-functional areas of a system after changes and/or enhancements have been made. For example, when undertaking system enhancements, the market licensee should review relevant legacy code and infrastructure to evaluate the compatibility of the system changes with existing software and hardware.

## Functional testing

- RG 172.196 A market licensee should perform functional testing to ensure that a system works as intended by verifying its features against its functional

requirements. For example, the market licensee should test the functionality of orders in the trading system (i.e. entry, amendment, cancellation and execution of an order). Testing can also involve the functionality of the interrelation of one order to another, such as iceberg orders or pegged orders.

### **Testing environment for stakeholders**

- RG 172.197 For changes affecting market participants, market data providers or the ASIC Australian market regulation feed, a market licensee should provide a testing environment where affected stakeholders can test their systems against the market licensee's modifications.
- RG 172.198 In addition to the testing for trading systems, the market licensee should have testing environments with sufficient capacity to enable market participants to adequately stress test algorithmic programs and order flow (e.g. in a low-latency, high-message volume, volatile environment). This is especially relevant for large, fully automated markets with high levels of message traffic.

### **Adequate business continuity planning**

- RG 172.199 Market licensees should have adequate business continuity, backup and disaster recovery plans for each of their systems that support order entry, order routing, execution, market data, trade reporting and trade comparison.
- RG 172.200 We expect market licensees to have arrangements in place to ensure that critical business functions will be available to stakeholders that require access, and the impact of a disruption or outage of services on stakeholders is minimised.
- RG 172.201 Market licensees should:
- (a) consider an adequate range of possible scenarios related to their systems and controls;
  - (b) have the supporting policies, guidelines and procedures needed to address disruptive incidents (including but not limited to system failures), and ensure a timely resumption of services; and
  - (c) back up business and compliance critical data that flows through their electronic trading systems.
- RG 172.202 Depending on the nature, size and complexity of their business, market licensees should consider having procedures in place for moving to, and operating the electronic trading system from, a backup site.
- RG 172.203 We expect market licensees to have adequate arrangements to ensure timely access to appropriately skilled and knowledgeable internal and vendor technical support for their specific system configurations, particularly while implementing system changes.

- RG 172.204 International standard-setting organisations offer additional information and guidance that market licensees may consider when developing their business continuity arrangements. Examples include the following:
- (a) The emerging International Standards Organization (ISO) standard, ISO 22301 *Societal security: Preparedness and continuity management systems—Requirements*, specifies requirements for setting up and managing an effective business continuity management system.
  - (b) In Australia, Standards Australia has published HB 292-2006 *A practitioner's guide to business continuity management*.
  - (c) Specifically in relation to the financial industry, in August 2006, a joint forum of the International Organization of Securities Commissions (IOSCO), the Basel Committee on Banking Supervision (BCBS) of the Bank for International Settlement (BIS), and the International Association of Insurance Supervisors (IAIS) issued a paper, *High-level principles for business continuity*, which set out principles-based guidelines on effective business continuity management.

## Capacity management and stress testing

- RG 172.205 Market licensees should have sufficient system capacity to accommodate reasonably foreseeable volumes of trading activity. We expect market licensees to have arrangements in place to prevent capacity limits on messaging from being breached.
- RG 172.206 Market licensees should keep capacity requirements under review and conduct capacity stress tests regularly. These systems should be adaptable to manage trading behaviours (such as quote-stuffing) and scalable to allow for changes in response to elevated message levels and/or stressed market conditions that might breach their capacity. Stress testing of infrastructure, computers and applications should also be conducted regularly.

## Adequate systems security

- RG 172.207 Market licensees should have adequate physical and electronic security arrangements to protect their systems, and the premises where systems are housed. The security arrangements should be designed to prevent misuse or unauthorised access to systems, and to ensure the integrity of the data and information in the systems.
- RG 172.208 There should be procedures in place to restrict access to servers and systems to internal or external personnel with appropriate security clearance. For example, systems should be protected by operating system and application security to limit internal access to authorised personnel, and by firewalls to prevent unauthorised external access. A proactive strategy should be in place

to prevent cyber attacks. Server rooms, co-location facilities and data centres should be secure from unauthorised physical access.

## Periodic monitoring and review

- RG 172.209 We expect market licensees to monitor and review the above arrangements. To ensure that systems and controls remain continually effective, market licensees should periodically monitor and review their arrangements for systems testing, business continuity, capacity management and security. They should remedy deficiencies and deal with identified problems in an appropriate and systematic way, as soon as reasonably possible.
- RG 172.210 The monitoring and review arrangements should be proportionate to the nature, size and complexity of the market. A market licensee may conduct these periodic reviews as part of a self-assessment, or may consider engaging an independent third party (such as an independent expert in exchange markets or an information system auditor) to perform the necessary reviews.
- RG 172.211 The frequency of reviews will also vary according to the nature, size and complexity of the market (e.g. annual, semi-annual, quarterly, or monthly). Review results may be communicated to ASIC as part of the market licensee's annual report under s792F of the Corporations Act.

## Stakeholder communications

- RG 172.212 Market licensees should have appropriate processes in place to release information technology system management plans to stakeholders (i.e. issuers, investors, market participants, vendors, other market licensees and ASIC). The plans should clearly identify mandatory versus optional changes and allow sufficient time for stakeholders to adapt to the changes.
- RG 172.213 The plans should be maintained for at least a 12-month period and should be routinely updated so that industry has a rolling schedule of upcoming changes. Market licensees should take into account the commercial, technological, supervisory and regulatory impact of changes to their systems and controls on stakeholders, and assess stakeholder readiness to deal with the impact of the changes.
- RG 172.214 We consider it critical that market licensees promote the orderly implementation of market changes where there are systems implications for market users, including timely distribution of sufficiently detailed notifications, and that best endeavours are used to ensure project schedules are adhered to

once established. Every effort should be made to ensure that market licensees, vendors and market participants maintain appropriate quality standards.

Note: In this addendum, 'market users' means investors who acquire or dispose of financial products in a financial market. Investors may be market participants dealing for themselves or, where participants act as intermediaries, the clients of the participants.

RG 172.215 For example, for material system changes, market licensees should obtain stakeholder readiness attestations on the changes before their final implementation. Where attestations cannot be obtained or it is impractical, appropriate alternative arrangements should be in place between the licensee and stakeholders.

Note: For examples of what is likely to be considered a material system change, see RG 172.220.

RG 172.216 In this context, on the basis that sufficient notice has been given of a material system change, market users should also use best endeavours to ensure that they are ready to comply with all reasonable change initiatives.

## Notification to ASIC of material system changes

RG 172.217 Market licensees should notify ASIC of material system changes in sufficient time before they occur so that we can consider the market integrity issues associated with these changes, both for our own surveillance function and for the wider market. The notification should outline the approach to managing the change, key project milestones and their preferred dates, including risk management, communication to the market, and the anticipated impact on market participants and the wider market.

RG 172.218 When assessing these changes, we expect market licensees to take into account the impact of their initiatives on market integrity. We may discuss with a market licensee the implications of its system changes for stakeholders. We may request that an independent third party verify the changes to ensure that these are managed appropriately and in an orderly manner. The third party may be an independent expert in exchange markets, an information system auditor or another person that we consider is suitably qualified and experienced.

RG 172.219 When classifying material system changes, a market licensee should consider the likely impact on market participants, and the fair, orderly and transparent operation of the wider market. A material change is likely to involve a high degree of effort or complexity in implementation and/or have significant stakeholder impact.

RG 172.220 Examples of what is likely to be considered a material change, subject to discussion with ASIC, include:

- (a) a change of trading system by a market licensee;

- (b) the introduction of new infrastructure allowing the physical proximity of processing servers to minimise latency;
- (c) a change to order matching and execution algorithms; and
- (d) the change or removal of a financial threshold for an order type.