



Integrity Division

Why and How ASX Supervises the Market

Why does ASX Supervise?

Underlying Philosophy

ASX Group (ASX) supervises the market activity of participants, listed entities and other users to ensure a market of high integrity. That is, a market that is fair, orderly and transparent.

A market of high integrity creates a level-playing field for all market users, inspiring confidence among investors, brokers, companies, regulators and the broader community. Market confidence depends on the constant and vigilant supervision of all users.

Underpinning ASX's supervisory approach and the spirit of its rules and guidance notes, is a commitment by its participants and listed entities to behaviour that is ethical, honest, cooperative and transparent.

This approach relies on education and relationship building, and seeks to develop a culture beyond mere compliance that emphasises fair dealing and clear and timely disclosure.

Bolstering this approach is ASX's continuous monitoring of the market to detect behaviour that does not meet appropriate standards. ASX can employ methods of enforcement that prevent, manage or sanction inappropriate behaviour according to its severity. It also has a statutory obligation to refer certain matters to the Australian Securities and Investments Commission (ASIC).

Ensuring a market of high integrity that supports investor confidence and provides for public protection is fundamental to ASX's commercial objectives and to maintaining its international reputation. Integrity is the business not of any one division alone but of the entire organisation.

Rule Setting

ASX applies its listing, market, and clearing and settlement (CS) facility rules consistently to all participants and listed entities to ensure a fair, orderly and transparent market in which users can have confidence. ASX favours behaviour-based rules for participants and disclosure-based rules for listed entities to enable the market to determine the quality of a party's operations and market activity.

Statutory Obligations – Monitoring and Enforcement

Under the *Corporations Act*, ASX has obligations to monitor participants' and listed entities' conduct in relation to the market and the CS facility, and to enforce compliance with the operating rules.

Understanding Monitoring and Enforcement

ASX views 'monitoring and enforcement' as all supervisory activity that supports a fair, orderly and transparent market, and fair and effective CS facilities.

It encompasses both prospective supervisory activity:

- promoting compliant behaviour;
- influencing compliant behaviour;
- preventing/deterring non-compliant behaviour; and
- responding to a problem and negotiating future compliance;

and retrospective supervisory activity:

- removing the opportunity to repeat inappropriate behaviour;
- investigating a potential rule contravention or misconduct;
- determining if a rule contravention or misconduct has occurred;
- applying a sanction;
- referring a matter to ASIC.

Transparency of Enforcement Activity

Enforcement activity that is timely and transparent is likely to have the greatest corrective impact on unacceptable market behaviour. Visible enforcement also supports investor confidence in ASX's ability to monitor and enforce its rules, thus serving an important public protective purpose.

ASX's investigation and enforcement process is confidential during the investigation and Disciplinary Tribunal hearing stages. The Disciplinary Tribunal publishes the determination of its findings by way of disciplinary circulars which are also posted on the ASX website. In some cases, Tribunal outcomes will also be issued as a media release.

Multi-Level Approach

ASX has a variety of enforcement methods at its disposal to ensure the preservation of the market's integrity.

It will apply an enforcement response commensurate with the circumstances and seriousness of each inappropriate activity. For example, certain matters will be sufficiently serious to warrant sanction without any prior attempt by ASX to influence or negotiate a change of behaviour.

ASX may also implement various enforcement activities, such as educative and disciplinary, simultaneously, ensuring that it manages any conflicts that may arise between these various activities. For example, ASX may pursue a sanction against a participant for a particular type of conduct at the same time as seeking to influence systemic change within that organisation to prevent the conduct from being repeated.

How does ASX Focus Supervisory Effort?

ASX regularly assesses its utilisation of resources necessary to provide a market of the highest possible integrity. It must also ensure that it strikes the right balance between supervisory frameworks and activity that supports investor protection, and the objective of market efficiency.

Risk Assessment

ASX's understanding of market activity and continuous monitoring of market trends enable it to anticipate areas of integrity-related risk for itself and for its users.

Assessment of Adequacy of Regulatory Response

ASX is one of several entities charged with supervising market activity and the behaviour of its users. ASIC has responsibility for supervising adherence to the *Corporations Act* and parties such as professional associations and industry groups have influence over the behaviour of their stakeholders.

ASX pays close regard to the contribution of these other parties in deploying its supervisory resources. In seeking to ensure efficient and consistent regulatory oversight, ASX will work with its supervisory partners to avoid the unnecessary duplication of supervisory activity.

Regulatory Impact

The scale of impact of a supervisory activity is also relevant in assessing the most effective deployment of supervisory resources. Such impact may be measured against the market as a whole or against a particular participant.

Supervisory activity that can be publicised often has a valuable deterrent or educative effect on the broader market. ASX will always consider how such activity can be drawn to the attention of the broader market without compromising confidentiality or any ongoing investigation.

Balancing Investor Protection and Market Efficiency

Providing a fair, orderly and transparent market, and fair and effective CS facilities requires ASX to balance the needs of investor protection and market efficiency. This means establishing an infrastructure to support appropriate participant and entity behaviour, thus promoting investor confidence, while ensuring that such infrastructure provides for a deep and liquid market, and efficient methods of capital-raising.

Monitoring

The range of monitoring activity undertaken by ASX is described below.

Monitoring for Compliance

ASX applies both technology and human resources to the continual monitoring of compliance with its regulatory framework and to market-related law. Monitoring activity may be:

- Transaction-based:

- prospective, ie to verify that the proposed future activity will comply with the rules; or
 - retrospective, ie to verify that the activity has complied with the rules.
 - Participant-based:
 - general review of sector/activity; or
 - targeting of particular participant activity.
- In either case, prospective or retrospective;
- Co-regulatory, ie sharing information with other regulatory bodies.

Investigation

Where circumstances arise that may indicate a potential breach of its rules or the law, ASX may pursue an investigation via a number of means, including interviews, discussions, requests for information from the participant or entity involved, or by the collation and analysis of information from other sources.

Range of Supervisory Responses

The broad range of supervisory enforcement measures open to ASX are described below.

Education and Guidance

ASX commits extensive resources to the education, guidance and training of its participants and listed entities to ensure that they operate within the spirit and intention of the supervisory framework and the law. In particular, the following activities are undertaken:

- Seminars and workshops to educate in relation to new rules or areas of law which have significant market impact;
- Demonstrations of ASX monitoring and supervisory capability to discourage inappropriate behaviour;
- Guidance material to assist in understanding the intention of the regulatory framework;
- Discussion to assist in understanding or interpreting the regulatory framework; and
- Establishment of base levels of competence.

Persuasion

Where it appears that a participant or entity has breached or may potentially breach a rule, ASX may pursue corrective action through discussion and persuasion. Such action may be to ensure that disclosure is provided in a timely way or that a potentially manipulative market activity ceases. The persuasive approach may also be coupled with retrospective review and the sanctioning of the behaviour. If, following an investigation, ASX considers it has sufficient evidence to demonstrate that a participant has contravened ASX rules it will commence disciplinary proceedings.

Escalation within an Organisation

ASX understands that the reputations of participants and entities may be damaged if investigatory or sanctioning activity becomes public. Where disciplinary proceedings are not appropriate, ASX may seek to achieve a supervisory outcome in other ways such as via Management Letters. In such cases, ASX will bring to the attention of a participant's

or entity's senior management, Board or relevant parent the inappropriate behaviour of operational staff requiring corrective measures or structural reform to ensure future compliance.

Warning

Where a potential rule breach or inappropriate behaviour arises, ASX may decide that a warning is an adequate enforcement response in order to encourage corrective action and to deter future misconduct. In some cases, such warnings may be made public in order to act as a further sanction and/or to more broadly influence the market in relation to appropriate conduct.

Publicly Identifying a Potential Breach

It may be effective to use market pressure to ensure regulatory compliance by publicly identifying potential breaches. For example, if ASX believes that there has been a failure to comply with a company's disclosure obligations under the Listing Rules and this has not been adequately explained, it may publicly query the company and release the company's response.

Agreed Remedial Action

Where it appears that a participant or entity may have breached or may potentially breach a rule, ASX may pursue corrective action to promote an improvement in compliance standards and processes through mutually agreed, formal and documented strategies.

Enforced Remedial Action

Where it appears that a participant or entity may have breached or may potentially breach a rule, enforced corrective action may be pursued via the Disciplinary Tribunal imposing a program to embed improved compliance standards and processes within that organisation. For example, an ongoing program of external audit and reporting on compliance standards and internal controls may be imposed.

Suspending or Removing the Capacity to Operate on Market

ASX has powers to suspend or remove a participant's or entity's market status in response to a serious breach of the rules or in order to manage an informed and orderly market. These powers will only be used in exceptional cases as they impinge significantly upon the ability of a participant to do business and the ability of investors to trade in the securities of a particular entity.

ASX Penalty

ASX has the power to sanction inappropriate participant conduct by disciplinary action before a disciplinary tribunal. This may result in the application of a financial or administrative penalty. An independent tribunal of the participant's peers (the Disciplinary Tribunal) determines the type and scale of penalty. ASX's fining power extends only to participants not listed entities.

Publication of penalty:

Such a penalty may be published as a means of educating and influencing the broader market in relation to appropriate behaviour. Publication of a penalty is also an important element of market transparency and public protection.

Escalation of penalty for repeated behaviour:

The Disciplinary Tribunal will take into account the repeated involvement of a participant in several incidents of similarly inappropriate behaviour in determining the level of penalty.

Referral to ASIC

ASX has statutory obligations to refer suspected significant breaches of its operating rules and of the *Corporations Act* to ASIC. ASX also has obligations to refer prescribed breaches to ASIC. ASIC has the power to prosecute breaches of the *Corporations Act*

Exercise of Discretion

The application of enforcement activity in the face of potentially aberrant behaviour requires the exercise of discretion. ASX recognises that it is important to treat participants fairly and equally, and that it must be consistent in its approach. It is equally important to differentiate between behaviours of different participants and entities, and to consider all circumstances. This requires ASX to have documented policies in relation to the interpretation and implementation of its rules, to effectively communicate these policies and to record the exercise of any discretion so as to monitor the consistency of its application.

Policy and parameters:

Parameters for the exercise of discretion in accordance with ASX policy are established in the written procedures of each discretion-exercising department.

Waivers:

ASX does not wish to inhibit legitimate transactions and business processes that do not undermine the core principles on which its rules are based. ASX will balance the commercial need of its participants and entities with the need to maintain the integrity of the market. Accordingly, ASX may grant waivers after considering the circumstances of a particular case where there would be no adverse impact on the integrity of the market.

Communication:

These parameters and policy guidelines are communicated to participants and listed entities through formal publications, such as Guidance Notes and circulars, and through regular discussion and education sessions.

Recording:

Each ASX department has established mechanisms for recording its supervisory activity. This is monitored by management to ensure a consistency of approach and to identify and respond to emerging trends in market activity that may indicate the need for policy change.
