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Committee Secretary
Senate Economics Committee
Department of the Senate
PO Box 6100
Parliament House
CANBERRA ACT 2600

Dear Sir

Corporations (National Guarantee Fund Levies) Amendment Bill 2007

I am writing to indicate that the Australian Securities Exchange Ltd (ASX) strongly supports the proposed Corporations (National Guarantee Fund Levies) Amendment Bill 2007.

ASX believes that the imposition of a cap on the levies payable by exchanges and their participants in any one year offers the potential to allow the National Guarantee Fund (NGF) to attract a wider range of, well-capitalised, institutions to consider direct participation in ASX markets and associated clearing facilities. This can be achieved while ensuring that Australia's investor protection scheme remains by far the most generous in the world. We are not aware of any compensation fund of this type anywhere in the world where the administrator of the fund has an unlimited capacity to levy market participants in order to replenish the fund. (It is also becoming increasingly unusual, following the demutualisation of exchanges, for national laws to vest responsibility in exchanges for the maintenance of compensation funds).

The NGF was established at the time of the formation of the then Australian Stock Exchange in 1987 when the fidelity funds of the six state exchanges were merged. The NGF is a statutory compensation fund established by the Corporations Act with its assets managed by the Board of the Securities Exchanges Guarantee Corporation (SEGC), a wholly-owned subsidiary of ASX Limited. (The legislation does not require that any organisation seeking to establish a new market in securities be obliged to offer the same high standard of compensation, the appropriate standard being a matter for Ministerial discretion in the case of a domestic operator and a matter where there is no explicit obligation to establish compensation arrangements in the case of an offshore-domiciled operator).

The types of investor protection claims that can be made on the NGF[1] are for:

- completion of sales and purchases of quoted securities entered into by a dealer on ASX's equities and debt markets where the transaction is required to be reported to ASX. The dealer may have failed to provide to the client, after settlement, the securities purchased or the proceeds of the sale, or may have been suspended by ASX or the Australian Clearing House (ACH);

- loss that results if a dealer transfers marketable securities without authority;

[1] Source: SEGC Annual Report 2006. Note, as a result of the split of the NGF on 31 March 2005, the Australian Clearing House assumed liability for clearing support claims.

- loss that results if a dealer cancels or fails to cancel a certificate of title to quoted securities contrary to the provisions of the operating rules of the Australian Settlement and Transfer Corporation;

- loss that results if a dealer becomes insolvent and fails to meet its obligations in respect of property (usually money or securities) that had been entrusted to it in the course of, or in connection with, its business of dealing in securities, up to a statutory maximum per dealer of 15% of the 'minimum amount' of the NGF.

Since its establishment in 1987, the NGF has paid out just under $22 million in respect of claims (a net $13.4 million after recoveries). However most of this was paid during the early years of the scheme. Since 1998-99 a total of only $644,000 has been paid out of the NGF[2], and no payments have been made after 2002-03.

Most of the early, larger, payments were in response to broker insolvency, but in more recent years the most common claim relates to the unauthorised transfer of securities.

Since around 1993, a number of improvements have occurred in ASX's settlement and transfer systems as well as in the practices of individual market participants. Improved monitoring by ASIC/ASX and reporting by participants of their capital adequacy, and more sophisticated risk management techniques have been adopted by participants and ASX clearing houses. This has had the effect of reducing the potential risks facing the NGF in the area of broker insolvency.

The Corporations Act provides the SEGC Board, with approval of the appropriate Minister, with the power to determine the 'minimum amount' needed for the Fund in order for it to meet claims and the administration costs of SEGC and the NGF. The minimum amount has been set at $76 million since 2005.

The 'minimum amount' is determined on the basis of actuarial advice to make the Fund capable of withstanding extreme but reasonably feasible events at a prudential level of strength.

If the monies in the NGF falls below the "minimum amount" the SEGC can raise funds by imposing a levy on ASX or on all or a class of participants of ASX[3].

Since the formation of the NGF, the amount in the NGF has not fallen below the 'minimum amount' and, as such, there has been no need to for the SEGC to introduce a levy. The Fund, at 30 June 2006 held monies totalling $96.8 million – a sizeable buffer above the minimum amount.

However, the existence of a theoretically unlimited levying power has restricted the ability of some of our larger, well-capitalised institutions, particularly deposit-taking banks from becoming direct participants in ASX markets and associated clearing facilities because of concerns expressed by the prudential regulator, the Australian Prudential Regulation Authority (APRA) about deposit-taking institutions having unlimited exposures.

A well designed cap on levies has the potential to remove these concerns, and allow banks, currently members of the NGF through separate subsidiaries to join as direct members. This would not only help make the NGF itself more robust but would also allow these participants to better manage their internal operations across a range of markets. For example, the existing arrangements can mean that banks may participate on ASX and SFE (Sydney Future Exchange) markets through separate subsidiaries, despite them now both being operated by ASX.

In summary, we believe the amendments contained in the Bill will:

- ensure Australia retains a generous investor protection regime via the NGF; and

[2] The largest payment in any one year was $300,000.
[3] The SEGC also has other options at its disposal, including: seeking the Minister's approval to reduce the 'minimum amount', taking out insurance against the liability, paying claims in installments, or borrowing (including from ASX) to meet claims due.

- allow a broader range of financial institutions (e.g. deposit-taking banks) to become direct members of the NGF – adding to the financial strength of the Fund and allowing market participants to better organise their operations.

For these reasons ASX supports the Corporations (National Guarantee Fund Levies) Amendment Bill 2007.

Yours sincerely

Malcolm Starr

Malcolm Starr
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Regulatory and Public Policy