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# GOVERNMENT RELEASES PROPOSALS TO REGULATE FINANCIAL BENCHMARKS

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Legal Briefings – By **Steven Rice**

The Government has released proposals to reform the regulation of financial benchmarks in Australia. Firms which rely on benchmarks to provide financial services or which provide services against benchmarks should be aware of these proposals and consider making a submission in respect of the proposed law reform.

## THE PROPOSALS AND THEIR BACKGROUND

The proposals will:

- introduce a new regime for licensing of providers of 'significant financial benchmarks', known as 'benchmark administrator licensees';
- give ASIC the power to impose rules on benchmark administrator licensees and the service providers to such licensees (and potentially other persons); and
- create offences and civil penalty provisions in respect of various forms of market misconduct relating to financial benchmarks.

The proposals are based on the International Organization of Securities Commissions Principles for Financial Benchmarks, that were developed in light of investigations and enforcement actions regarding attempted manipulation of major interest rate benchmarks, as well as recommendations of the Financial Stability Board.

## WHAT IS A ‘FINANCIAL BENCHMARK'?

The term ‘financial benchmark’ will cover prices, estimates, rates, indices and values which are:

- made available to users (whether for a fee or not);
- calculated periodically based on transactions, currencies or financial instruments (amongst other things); and
- used as a reference for calculating the interest payable, price or value of a financial product (amongst other things).

## WHAT IS A ‘SIGNIFICANT FINANCIAL BENCHMARK’?

As will be seen below, the licensing requirement only applies to ‘significant financial benchmarks’. These are financial benchmarks which have been declared by ASIC to be significant after ASIC has been satisfied that they are ‘systemically important’, would give rise to a ‘material risk of financial contagion’ if they were disrupted, or if disrupted would result in a ‘material impact on retail or wholesale investors in Australia’. None of these critical terms is defined in the draft proposals, and no indication of their scope is given in the draft Explanatory Memorandum. For example, how a ‘material impact’ would be assessed by ASIC is not discussed in the proposals, including by which reference point materiality would be assessed.

## WHAT ARE ‘BENCHMARK ADMINISTRATOR LICENCES’ AND WHAT POWERS ARE AVAILABLE TO ASIC IN RESPECT OF THEM?

A criminal offence is proposed to be created which would be committed by a person who (in general terms) administers or holds out that they administer a significant financial benchmark but who does not hold a ‘benchmark administrator licence’.

The proposals contain a mechanism for applying for and granting benchmark administrator licences, and imposing conditions on such licences. ASIC will be able to vary, cancel or suspend a licence using powers which are similar to those which are currently in place for an Australian financial services licence (**AFSL**). The circumstances when ASIC may seek suspension or cancellation of the licence are circumscribed as compared to the AFSL regime. ASIC will need to have regard to factors including whether it is in the public interest to take actions such as granting, suspending or cancelling a benchmark administrator licence.

Benchmark administrator licences would be subject to a number of obligations. These include to:

- comply with conditions ASIC imposes on the licence;
- notify ASIC that it has failed to comply with conditions on its licence;
- assist ASIC, APRA and the Reserve Bank; and
- give ASIC access to the licensee's facilities.

ASIC also has a range of powers in respect of benchmark administrator licensees. ASIC may give a licensee directions if the licensee is not complying with its obligations, require a report of the licensee (including an audit statement in respect of the report), and undertake a compliance assessment of the licensee.

## WHAT RULES COULD ASIC MAKE IN RESPECT OF FINANCIAL BENCHMARKS AND HOW ARE THOSE RULES TO BE ENFORCED?

ASIC would be able to make 'financial benchmark rules'. These rules could deal with the 'role of internal and external parties' involved in the administration of benchmarks, the design of benchmarks, business continuity planning, governance, conflicts of interest, and reporting of data to ASIC. The rules would generally apply to benchmark administrator licensees, although would also apply to certain service providers to benchmark administrators. The proposals contain an ability for regulations to be made which establish the persons to whom the rules would apply.

ASIC would also be able to make 'compelled financial benchmark rules'. These rules could, for example, require the holder of a benchmark administrator licence to continue to generate or administer the significant financial benchmark. They could also require a benchmark participant to continue to provide information to a benchmark administrator.

Compliance with these rules is enforceable by civil penalty provisions, infringement notices, and enforceable undertakings, in a similar way to the current ASIC market integrity rules. The civil penalty for contravening the rules will be that set out in the rules, when made. ASIC must generally consult before making the rules.

## WHAT OFFENCES AND CIVIL PENALTIES ARE PROPOSED?

The proposals create new offences and civil penalty provisions in respect of conduct relating to financial benchmarks. The following conduct will be prohibited:

- manipulating a benchmark (conduct which results in a benchmark which is generated or administered at an artificial level);
- false or misleading statements in respect of the generation or administration of a benchmark; and
- dishonest conduct in respect of the generation or administration of a benchmark.

Separate offences are created where the benchmark is a significant financial benchmark and the conduct results in an Australian entity suffering a disadvantage from the use of the benchmark.

The criminal penalties are significant – in the case of a body corporate, the greater of 45,000 penalty units (currently $8.1 million), 3 times the benefit of the offence, or 10% of its annual turnover in the past 12 month period. The maximum civil pecuniary penalty proposed for a body corporate is $1 million.

## EXTRA-TERRITORIAL SCOPE

The offence provisions have an extended geographical scope. Foreign nationals and foreign bodies corporate will be subject to the offence provisions if the conduct giving rise to the offences occurs at least partly in Australia. The offence provisions also apply to conduct which occurs outside Australia if the conduct is in respect of a significant financial benchmark.

## NEXT STEPS

Submissions on the proposals are due by 24 July 2017.

# KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.

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