

19 October 2011

General Manager
Retail Investor Division
The Treasury
Langton Crescent
PARKES ACT 2600

BY EMAIL: futureofadvice@treasury.gov.au

Dear Sir/Madam

Exposure Draft Tranche 2 – Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011 (Bill)

The second tranche of the draft legislation released by Treasury in October 2011 contained a number of proposed securities law reforms that will impact on the derivatives industry generally as well as CMC Markets Asia Pacific Pty Ltd and its group entities (**CMC Markets**).

CMC Markets has reviewed the draft Bill and Explanatory Memorandum (**EM**) and we set out below a number of issues on which CMC Markets wishes to make submissions.

1. Background

CMC Markets is a market-maker in derivatives in the Australian retail financial services market. An over the counter (**OTC**) provider, we are one of the market leaders in providing Contracts for Difference (**CFDs**) in Australia.

CMC Markets was established in 1989 in the United Kingdom as a Foreign Exchange market maker. CMC Markets' sought to deliver a trading service to the retail market that offered institutional-style pricing and execution. In 1996, CMC Markets released the world's first online Internet Foreign Exchange trading platform. CMC Markets has subsequently extended the product base to include CFDs, Financial Spread Betting and Currency Futures. CMC Markets has offices on four continents and online access to CFDs over 17 international markets.

In Australia, CMC Markets provides CFDs over currencies, indices, commodities and equities.

CMC Markets has arrangements with a number of intermediary companies (**Partners**) who CMC Markets pays a commission or rebate for either:

- (a) the referral of the client to CMC Markets; or
- (b) a trade placed by or on behalf of the client in respect of certain CFD Products with or without the provision of financial product advice.

2. Original intention of the FOFA reforms and the Explanatory Memorandum

The EM highlights the example of financial advisers who may be "conflicted" between receiving product commissions and providing unbiased financial product advice to retail clients. Further, the FOFA FAQs note that the focus of the ban on conflicted remuneration structures is "removing conflicts of interest that may cause bias, or the potential for bias, in financial advice due to payments from product providers to those providing advice".

The payments CMC Markets makes to its Partners are not of this kind and do not impact the financial product advice which may be provided by the Partner.

Further, the EM discusses the “ineffectiveness of current disclosure of conflicts and conduct rules” however CMC Markets and its Partners are very diligent in disclosing to retail clients the fees, rebates and commissions that are applicable.

The FOFA FAQs state that “it is not the intent that a transparent and product neutral regime with a client-paid fee would be subject to the ban, unless it is an asset-based fee relating to geared products or investment amounts.”

Submission: We submit that the CFD industry was a sub-section of the Financial Services Industry which was not originally intended to be captured by the FOFA reforms. Treasury originally stated these reforms were aimed at the financial planning industry and industries which were not transparent about certain payments. This kind of conduct does not represent our business but unfortunately our business may be affected significantly by the reforms if left unchanged prior to enactment.

3. How will Tranche 2 of the FOFA reforms affect CMC Markets?

3.1 Conflicted remuneration

"Conflicted remuneration" is currently defined under the Bill as any benefit, whether monetary or non-monetary, given to a financial services licensee, or a representative of a financial services licensee, who provides financial product advice to retail clients, and which might influence the choice of financial product recommended by the licensee, or might otherwise influence the financial product advice given to retail clients.

This definition includes benefits which are dependent on the total value of financial products of a particular kind recommended by the licensee or total value of investments of a particular kind made by retail clients to whom the licensee provides financial product advice.

Since the definition of conflicted remuneration covers both the provider of general advice to a retail client and the issuer of a financial product, this amendment will impact our Partner relationships for those Partners who are providing either personal or general advice and receiving a monetary benefit.

Whilst this impacts approximately only 5 to 10% of our Partners currently, it represents over 70% of our Partner-generated revenue if the Bill is interpreted to include situations where the benefit paid could potentially influence the choice of financial products recommended but in reality does not influence the client's choice of financial products. Further, in the next 12 months this is an area of the business which we will be targeting and which we expect will experience significant growth for CMC Markets.

If the legislation was passed in its current form, it will have such a significant impact on the relationships with our Partners and our Partners business it may result in that part of the business having to be shut down.

Submission: We submit that the inclusion of both general advice and personal advice in the definition of “conflicted remuneration” is an unintended consequence of the Bill and does not reflect the original intention of the FOFA amendments.

The FOFA Information Pack dated 28 April 2011 states at Section 3 “where certain reforms also have application to the provision of general advice, this is generally for practical reasons and regulatory simplicity’. We submit that taking this approach has unintended affects such as the situation described above.

Please confirm why general advice has been included in the definition of conflicted remuneration.

We further submit that arrangements such as ours with our Partners and clients referred by Partners were not intended to be captured by the FOFA amendments. Our fees, commissions and rebates to our Partners are already transparent to the client (they are included in our Financial Services Guide and the Financial Services Guide of the Partner) and are not the kinds of payments which the legislation intends to restrict.

We further submit that general advice provided by an issuer in relation only to products issued by that issuer should be excluded from the definition of conflicted remuneration. For example, the general advice specific to CMC products and not any other financial products should not be captured by this definition. If CMC is issuing the financial product itself, and in so doing is providing product information about its own product, any monetary benefits provided in respect of such CMC financial products should not be considered conflicted remuneration.

Suggested amendments: We suggest that the definition of conflicted remuneration should be amended to exclude general advice from the definition of conflicted remuneration. We understand that this might already be achieved by the exception in s963A(1)(c) however we would require further clarification on the interpretation of this exception to understand how many of our Partners could benefit from it (see below).

We further suggest that an exemption be included to exclude monetary benefits paid to a financial services licensee (or representative of a financial services licensee) who provides financial product advice in respect of financial products which are issued by the product issuer and such financial product advice is specific only to the financial product issued.

Furthermore, a potential breach of the FOFA legislation should be triggered by the actual provision of conflicted advice as opposed to making the payment when the recipient is licensed to provide the advice or the advice may not have been provided at all i.e. where there is no advice given then it follows that there be no conflict or potential for conflict.

3.2 *Execution only exception – section 963A(1)(c)*

The exception contained in section 963A(1)(c) might apply to our Partner relationships if:

- (a) the benefit is given to the licensee in relation to the issue or sale of the financial product to a retail client; and
- (b) no financial product advice in relation to the product has been given to the client by the licensee, representative of the licensee or the representative.

Since a number of Partners are operating under an execution only model currently, we may be able to rely on this exception for execution only services however further clarity on this exception would be required.

Submission: We submit that the Execution Only exemption contained in section 963A(1)(c) may apply to the affected parts of our business however we request further clarification on the extent of this exemption.

3.3 *Non-monetary benefits - sections 963B(c) and (d)*

The exceptions contained in sections 963B(c) and (d) in relation to education and training and IT software and support respectively may also be relevant for our Partner relationships however further clarification on the extent of these exemptions would be appreciated.

Submission: We submit that the Education & Training and IT Software & Support exemptions contained in sections 963B(c) and (d) may apply to the affected parts of our business however we request further clarification on the extent of these exemptions.

3.4 *Other banned remuneration – section 964*

Section 964 states that an issuer must not give any monetary financial benefit to a licensee or a representative of a licensee who provides financial product advice to retail clients.

As above under item 2.1, this definition of “Other banned remuneration” is very broad as it covers both personal and general advice and therefore would capture payments made from CMC Markets to some of its Partners who provide financial product advice to retail clients.

Submission: For the reasons noted above under item 2.4 we submit that the inclusion of both general advice and personal advice in the definition of “Other banned remuneration” is an unintended consequence of the Bill and does not reflect the original intention of Tranche 1 of the FOFA amendments. Please confirm why general advice has been included in the definition of “Other banned remuneration”.

We further submit that arrangements such as ours with our Partners and clients referred by Partners were not intended to be captured by the FOFA amendments. Our fees, commissions and rebates to our Partners are already transparent to the client and are not the kinds of payments which the legislation intends to restrict.

Suggested amendment: We suggest that the definition of “Other banned remuneration” should be amended to exclude general advice from the definition of “Other banned remuneration”. We understand that this might already be achieved by the exceptions in s964(2)(e) and (f) however we would require further clarification on the interpretation of these exceptions to understand how many of our Partners could benefit from it (see below).

We further suggest that the definition of “Other banned remuneration” be amended to align with the definition of conflicted remuneration by requiring that the remuneration might influence the choice of financial product recommended by the licensee, or might otherwise influence the financial product advice given to retail clients.

As a general comment, the intention of the exceptions in section 963 and 964 appear to be unclear i.e. the exception in section 963A(1)(c) is applicable to payments for execution only services, however section 964 precludes payment anyway by a product issuer.

3.5 Exemptions to Other banned remuneration

Sections 964(e) and (f) in relation to exemptions for education and training and IT software and support respectively may also be relevant for our Partner relationships however further clarification on the extent of these exemptions would be appreciated.

Submission: We submit that the Education & Training and IT Software & Support exemptions contained in sections 964(e) and (f) may apply to the affected parts of our business however we request further clarification on the extent of these exemptions.

3.6 Grandfathering and transitional arrangements

There is insufficient clarity in the Bill and EM on grandfathering provisions for dealing with existing contracts. Also, the FOFA FAQs note that there may be transitional arrangements from 1 July 2012 to allow industry sufficient time to implement the reforms.

Submission: We submit that further clarification is needed in respect of the grandfathering and transitional provisions in the Bill to deal with existing contracts. Please confirm the details of any transitional provisions and provisions relating to grandfathering provisions.

Please do not hesitate to contact me on (02) 8915 9308 should you have any questions.

Yours faithfully,



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