

ASIC CLASS ORDER [CO 08/764]

EXPLANATORY STATEMENT

Prepared by the Australian Securities and Investments Commission

Corporations Act 2001

The Australian Securities and Investments Commission (*ASIC*) makes ASIC Class Order [CO 08/764] under s1020F(1)(a) of the *Corporations Act 2001* (the *Act*).

Section 1020F(1)(a) relevantly provides that ASIC may exempt a person or class of persons from specified provisions of Part 7.9 of the Act.

1. Background

Section 1020B regulates the short selling of certain financial products. That provision has the effect of prohibiting a person from selling these financial products unless they have a “presently exercisable and unconditional right to vest” the product.

There are some exceptions to the short selling prohibition.

An exception to the prohibition includes where the seller has effected the sale in accordance with the ASX Market Rules (*ASX short selling exception*) – see s1020B(4)(e). ASX Market Rule 19 allows a trading participant to short sell products declared as an 'approved short sale product', subject to certain additional reporting and pricing requirements.

Prior to Monday 22 September 2008, persons holding options (*ETOs*) registered with the Australian Clearing House Pty Limited were able to exercise those ETOs in reliance on the ASX short selling exception.

On Friday 19 September 2008, ASX decided to remove its list of approved short sale products, effective from Monday 22 September 2008. As a result, from Monday 22 September 2008, a person could no longer rely on the ASX short selling exception to short sell.

2. Purpose of the class order

This instrument is required to address an unintended consequence of removing the ASX approved short sale products list. An unintended consequence of removing the list was that persons could no longer exercise ETOs that would eventuate in a short sale under s1020B. For example, the exercise of a long put option or the exercise of a short call option.

This instrument allows a person to exercise an ETO (which would technically breach the short selling prohibition at s1020B) without having to comply with the need to

have a "presently exercisable and unconditional right to vest" the product under s1020B(2).

3. Operation of the class order

This instrument provides that a person does not have to comply with the short selling prohibition at s1020B(2) where the transaction effecting the sale of the security or managed investment product is the result of the exercise of an ETO. The instrument also has the following effect:

- before selling the a security or managed investment product on behalf of another person (*client*), a financial services licensee (*broker*) must ask the client whether the sale is a result of the exercise of an ETO. The broker must record, in written or electronic form, their client's answer;
- when making a request to sell a security or managed investment product as a result of the exercise of an ETO, the client must tell the broker that it is a such sale and made in reliance on paragraph 4 of the class order; and
- at the time a person is required to make a sale of the product as a result of the exercise of the ETO, that person must tell the broker that the sale is a sale of that kind and made in reliance on paragraph 4 of the class order.

These conditions are broadly consistent with existing market practice and the ASX Market Rules.

The exemption on the requirement to comply with s1020B(2) commences on the date it is registered. This was 23 September 2008. The conditions attached to the exemption commence on the day after the instrument is registered, being 24 September 2008.

4. Documents incorporated by reference

No documents are incorporated by reference.

5. Consultation

Since 19 September 2008, ASIC has had the opportunity to consult with the finance industry, individually and/or through their representative bodies, on this issue. ASIC also informally consulted with the ASX about providing relief before the making the instrument.

The making of the instrument was announced on the day it was made, namely Tuesday 23 September 2008. Prior to commencement of trading on Tuesday 23 September 2008, ASIC requested ASX to advise all market participants immediately and simultaneously of the intended effect of this instrument.