

ASIC CLASS ORDER [CO 10/288] 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 10/288] under paragraph 1020F(1)(a) of the *Corporations Act 2001 (Act)*.

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

1. Background

People sometimes sell (**short sell**) financial products that they do not own with a view to repurchasing them later at a lower price.

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

Generally, the Act permits a person to execute a short sale (**covered short sale**) where the person relies on an existing securities lending arrangement to have a ‘presently exercisable and unconditional right to vest’ the products in the buyer at the time of sale.

A market maker may make a covered short sale of a section 1020B product in the course of their market making activities.

If a market maker makes a covered short sale of a section 1020B product on a licensed market, the market maker may be required to report their short position to ASIC in accordance with Division 5B of Part 7.9 of the Act and Division 15 of Part 7.9 of the *Corporations Regulations 2001 (Regulations)*.

Under the paragraph 1020AB of the Act, a short sale transaction must be reported if:

- a ‘seller’ makes a sale of section 1020B products to a buyer on a licensed market in Australia; and
- before the time of sale, the seller had entered into or gained the benefit of a securities lending arrangement; and
- at the time of the sale the seller intends that the securities lending arrangement will ensure that some or all of the section 1020B products can be vested in the buyer.

2. Purpose of the class order

The class order is relevant for short sale transaction reporting and does not affect short position reporting obligations.

This class order exempts a market maker from reporting a covered short sale transaction in course of:

- (a) hedging risks arising from its market making activities; or
- (b) performing its function as a market maker of an ETF.

3. Operation of the class order

This class order exempts a market maker from the obligation under s1020AB(3) to report a covered short sale transaction where:

- (a) the market maker makes a market for a financial product;
- (b) the market maker holds, or is exempt from holding an Australian financial services licence for making a market;
- (c) naked short sales made by the market maker is a bona fide transaction to hedge the risks arising from the market maker's market making activities.

This class order also exempts a market maker from the obligation under s1020AB(3) to report a covered short sale transaction of an ETF security where:

- (a) the sale is made by the market maker in the course of making a market in the ETF security; and
- (b) the market maker
 - (i) is an AQUA Product Market Making Agent appointed by the issuer of the ETF security to make a market in the ETF security; or
 - (ii) has entered into an agreement with ASX Limited in relation to making a market in the ETF security.

4. Commencement

This class order commences on the date it is registered under the *Legislative Instruments Act 2003*.

5. Consultation

In Consultation Paper 106 *Short selling to hedge risk from market making activities*, ASIC consulted on whether, among other things, ASIC should require market makers to report naked short sale transactions to hedge risks arising from market making activities. The submitting parties generally did not support requiring market makers to report short sale transactions. Details of the submissions to CP 106 are contained in REP 167 *Response to submissions on CP 106 Short selling to hedge risk from market making activities*, which is available on our website at www.asic.gov.au.