

EXPLANATORY STATEMENT

Prepared by the Australian Securities and Investments Commission

Corporations Act 2001

The Australian Securities and Investments Commission (**ASIC**) makes the following legislative instruments under subsection 1075A(1) of the *Corporations Act 2001* (the **Act**):

- (a) *ASIC Corporations (Division 4 Financial Products) Instrument 2015/1030* (the **principal instrument**);
- (b) *ASIC Corporations (Repeal) Instrument 2015/1031* (the **repeal instrument**).

Subsection 1075A(1) of the Act provides that ASIC may, among other things, declare that Part 7.11 of the Act applies to a specified class of financial products as if specified provisions were omitted, modified or varied as specified in the declaration.

Subsection 1075A(2) of the Act requires ASIC to be satisfied in relation to the following two matters before it may make a declaration under subsection 1075A(1) in relation to financial products:

- the interests of the holders of the financial products or of financial products in that class, would continue to have adequate protection; and
- the declaration would make the transfer of those financial products or of financial products in that class, more efficient.

1. Background

Under the *Legislative Instruments Act 2003*, legislative instruments cease automatically, or ‘sunset’, after 10 years, unless action is taken to exempt or preserve them. To preserve its effect, a legislative instrument must be remade before the sunset date. The purpose of sunset is to ensure that instruments are kept up to date and only remain in force while they are fit for purpose, necessary and relevant.

ASIC Class Order [CO 02/312] (the **class order**) is a declaration that, among other things, regulates and facilitates the transfer through ASX Settlement Pty Ltd (**ASX Settlement**) of certain classes of financial products. The class order is due to sunset on 1 April 2017. ASIC has reviewed its policy underlying the class order. In light of this review and following public consultation, ASIC considers that this class order relief is necessary, fit-for-purpose and relevant. As such, ASIC has decided to reissue the relief underlying the class order into a new legislative instrument, being the principal instrument.

ASIC has also decided to extend the policy underlying the principal instrument to include warrants and interests in managed investment schemes that are not required to

be registered (each ***Chi-X products***) that will be admitted to quotation and traded on the market operated by Chi-X Australia Pty Ltd (***Chi-X***) in the classes of financial products that may be transferred through ASX Settlement.

2. Purpose of the legislative instruments

The purpose of the principal instrument is to:

- (a) broaden the class of financial products for the purposes of provisions that regulate and facilitate transfers of products through ASX Settlement;
- (b) disapply the application to certain warrants of certain subregulations that deal with circumstances under which such warrants would be taken to have ceased quotation on a financial market; and
- (c) clarify the operation of the regulations which deal with the effect on a transferee of a transfer through ASX Settlement of financial products that are rights.

The purpose of the repeal instrument is to discontinue the existing class order, which will be superseded by the principal instrument.

3. Operation of the legislative instruments

Division 4 of Part 7.11 of the Act, and regulations under the *Corporations Regulations 2001* (the ***Regulations***) made for the purposes of that Division, regulate and facilitate the transfer of certain classes of financial products — “Division 4 financial products” — effected through a prescribed clearing and settlement facility.

As at the commencement date of the principal instrument, ASX Settlement was the only clearing and settlement facility that had been prescribed by the regulations. ASX Settlement was previously known as ASX Settlement and Transfer Corporation Pty Limited (***ASTC***). As at the commencement date of the principal instrument, the Regulations continue to refer to ASTC.

ASIC considers that subsection 1075A(2) is satisfied in relation to the declaration that certain classes of financial products are Division 4 financial products because of the advantages of effecting a transfer of financial products in accordance with Division 4 of Part 7.11 of the Act through ASX Settlement. The main advantages are as follows:

- (a) legal certainty in relation to the effectiveness of the transfer, for example:
 - (i) a transfer effected through ASX Settlement in accordance with its operating rules is valid and effective for the purposes of any law or instrument governing or relating to the way in which the financial product may be transferred (see section 1074D of the Act);
 - (ii) a transfer effected through ASX Settlement in accordance with its operating rules may be effected to a trustee or legal representative (executor or administrator) despite any law or anything in the relevant

instrument appointing the trustee or legal representative
(see subsection 1074G(7) of the Act);

- (iii) the authority of a participant to effect a disposal of a financial product is continued notwithstanding that the client has died
(see regulations 7.11.25 and 7.11.26 of the Regulations);
- (b) legal certainty in relation to the determination of the holder of Division 4 financial products for the purposes of meetings, and of the conferral of benefits, such as dividends or distributions, on holders of such products
(see regulation 7.11.37 – 7.11.39 of the Regulations);
- (c) various warranties and obligations apply in relation to the transfer, for example:
 - (i) a participant effecting a transfer warrants to have the authority and be legally entitled to transfer the financial products
(see regulation 7.11.29 of the Regulations);
 - (ii) an indemnity to various persons, including the transferor and the transferee, if the warranty made under regulation 7.11.29 is not true
(see regulation 7.11.32 of the Regulations).

The kinds of financial products that are Division 4 financial products include:

- shares in a company;
- debentures of a company;
- interests in a registered scheme;
- rights to acquire any of the above by way of issue;
- Commonwealth Government Security (**CGS**) depository interests; and
- simple corporate bonds depository interests.

A class of financial products declared by ASIC under section 1075A of the Act to be financial products the transfer of which will be effected through ASX Settlement are also Division 4 financial products. This principal instrument, which is a declaration under section 1075A of the Act, has the effect that the following financial products are also Division 4 financial products:

- warrants traded on the market operated by ASX Limited (**ASX**) or Chi-X;
- warrants admitted to the AQUA Quote Display Board;
- interests in unregistered managed investment schemes traded on ASX or Chi-X or admitted to the AQUA Quote Display Board;

- certain shares and debentures quoted on ASX issued by entities that are not companies under the Act, and by foreign companies; and
- depository interests in relation to securities issued by a foreign company or foreign scheme products.

The principal instrument also disapplies the operation of subregulations 7.11.03(4) and (5) in relation to warrants that are able to be traded on the financial market operated by ASX or Chi-X, and warrants that are admitted to the AQUA Quote Display Board. Those kinds of financial products are Division 4 financial products as a result of the declaration made by the principal instrument.

These subregulations provide that if a Division 4 financial product is suspended from quotation (which does not, of itself, mean that the financial product has stopped being quoted – see regulation 7.11.03(3)) and, during the suspension, the issuer in relation to the product ceases to be included in the official list of the market on which the product is traded, then the product is taken to stop being quoted when the issuer ceases to be included in the official list. The application of these subregulations to warrants is inappropriate because the issuer of the warrants will not be the issuer of the underlying financial product to which the warrant relates. Furthermore, the financial market operated by Chi-X is not a listing market. ASIC considers that subsection 1075A(2) is satisfied in relation to this part of the declaration because it removes uncertainty in the operation of the law.

The principal instrument also modifies the operation of regulation 7.11.28, which deals with the effect on a transferee of a transfer through ASX Settlement of a Division 4 financial product that is a “right”. A “right” is generally defined to mean a right of a person to have a share, debenture or interest in a registered scheme issued to the person, whether or not on payment of any money or for any other consideration.

Subregulations 7.11.28(1), (2) and (3) contain certain deeming provisions in relation to transfers through ASX Settlement of Division 4 financial products that are rights. The deeming provisions relate to when the transferee of the rights is taken:

- to have applied for the issue of, and agreed to accept, the Division 4 financial products to which the rights relate; and
- to have agreed to become a member of the company or scheme (as applicable);
- to be bound by the company’s or scheme’ constitution (as applicable).

The deeming provisions take effect at the time the transfer of the rights take effect, irrespective of whether and when the transferee makes payment of the application money to the issuer in relation to the rights.

Under the modified operation of the subregulation 7.11.28(1), (2) and (3) these deeming provisions only apply where a transfer of rights through ASX Settlement has taken effect and, at that time or a later time (each the relevant payment time), the transferee makes a payment of application money (or, in the case of rights that are assignable options to acquire, by way of issue, shares in a company on payment of an exercise price) to the issuer of the right. The principal instrument also provides further clarification in relation to the effect of a transfer through ASX Settlement of a Division 4 financial product that is a right on the transferee. Where a transfer of a

right takes effect at a particular time, the transferee is taken to have agreed at that time to accept the rights themselves subject to the terms and conditions on which the transferor held the right immediately before that time. ASIC considers that subsection 1075A(2) is satisfied in relation to the part of the declaration that modifies the operation of regulation 7.11.28 because it provides clarification and removes uncertainty in the operation of the law regarding transfers of rights through ASX Settlement.

The repeal instrument discontinues ASIC Class Order [CO 02/312], being the instrument that gave effect to ASIC's previous policy, and which will be superseded by the principal instrument.

4. Consultation

On 24 August 2015, ASIC released Consultation Paper 236 *Remaking ASIC class orders on dematerialised securities and CHESS units of foreign securities (CP 236)* seeking feedback on a proposal to continue the policy underlying the class order.

ASIC received written submissions in response to CP 236, including public submissions from ASX, Securities Exchanges Guarantee Corporation Limited (the **SEGC**), being the administrator of the National Guarantee Fund (the **NGF**) and Asia Pacific Stock Exchange Limited (the **APX**).

Some submissions indicated that the underlying policy would need to be extended to Chi-X products if they were proposed to be transferred through ASX Settlement.

Some submissions expressed concern that extending the coverage of the underlying policy to Chi-X products may mean that those products may be the subject of compensation claims on the NGF, in circumstances where Chi-X is not yet a member of the SEGC.

ASIC's view is that extending the underlying policy to cover products that are only tradeable on Chi-X will not have any impact on claims that may be made against the NGF under Division 4 of Part 7.5 of the Act, until Chi-X becomes a member of the SEGC.

The basis of ASIC's view is that:

- section 887A of the Act (as modified by Schedule 8C to the Regulations) provides that Division 4 of Part 7.5 applies to a financial market that is operated by a body corporate that is a member of the SEGC or a subsidiary;
- consequently, until Chi-X is a member of the SEGC, Division 4 of Part 7.5 of the Act will not apply to the market operated by Chi-X market;
- section 888A of the Act provides that:
 - the situations in which compensation may be claimed in respect of a loss that is connected with a financial market to which Division 4

applies are as specified in the Regulations; and

- without limitation, a loss is connected with a financial market if it is caused by a participant, or past participant, in the market;
- currently, the only member of the SEGC is ASX;
- accordingly, while Chi-X is not a member of the SEGC, compensation may only be claimed in respect of a loss in relation to Chi-X products if the loss is connected to ASX;
- a loss will not be connected to ASX if:
 - it is caused by a person undertaking a transaction in relation to products that are only tradeable on the market operated by Chi-X and that are not tradeable on the market operated by ASX; and
 - it is caused by a participant in the market operated by Chi-X acting solely in that capacity (and not acting in the capacity of a participant in the market operated by ASX).

APX requested that the underlying policy be made “market neutral” so that it could in future extend to products it may come to list on its market. ASIC’s position is that it will look at market licensees on a case by case basis, upon an application being made to ASIC to support an extended coverage.

Further details of the non-confidential submission received are available on ASIC’s website at www.asic.gov.au.

Statement of Compatibility with Human Rights

Prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011

ASIC Corporations (Division 4 Financial Products) Instrument 2015/1030 ASIC Corporations (Repeal) Instrument 2015/1031

The following legislative instruments are compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*:

- ASIC Corporations (Division 4 Financial Products) Instrument 2015/1030;
- ASIC Corporations (Repeal) Instrument 2015/1031

Overview

ASIC Corporations (Division 4 Financial Products) Instrument 2015/1030:

- (a) broadens the class of financial products for the purposes of provisions that regulate and facilitate transfers of products through ASX Settlement;
- (b) disapplies the application to certain warrants of certain provisions that deal with circumstances under which such warrants would be taken to have ceased quotation on a financial market; and
- (c) clarifies the operation of the provisions which deal with the effect on a transferee of a transfer through ASX Settlement of financial products that are rights.

ASIC Corporations (Repeal) Instrument 2015/1031 discontinues ASIC Class Order [CO 02/312], being the instrument that gave effect to ASIC's previous policy, and which will be superseded by ASIC Corporations (Division 4 Financial Products) Instrument 2015/1030.

Human rights implications

The legislative instruments do not engage any of the applicable rights or freedoms.

Conclusion

The legislative instruments are compatible with human rights as they do not raise any human rights issues.

Australian Securities and Investments Commission