

EXPLANATORY STATEMENT for
ASIC CLASS RULE WAIVER (AMENDMENT) [CW 17/0617]

Prepared by the Australian Securities and Investments Commission

Corporations Act 2001

The Australian Securities and Investments Commission (**ASIC**) makes ASIC Class Rule Waiver (Amendment) [CW 17/0617] (**this instrument**) under subrule 1.2.1(1) of the *ASIC Market Integrity Rules (ASX Market) 2010* (the **Rules**). Under subrule 1.2.1(1) of the Rules ASIC may relieve any person or class of persons from the obligation to comply with a provision of the Rules. Under Rule 1.2.3 ASIC may specify the period during which any relief from the obligation to comply with a provision of the Rules may apply.

This instrument amends ASIC Class Rule Waiver [CW 14-1091]. Defined terms in this explanatory statement have the same meaning as in the Rules, unless the context requires otherwise.

1. Background

On 27 October 2014, ASIC made Class Rule Waiver [CW 14-1091] (**Class Rule Waiver**), providing relief to Participants of the Market operated by ASX Limited (ACN 008 624 691) (**ASX**) from the requirement to give confirmations to clients in Rule 3.4.1 in relation to Derivatives Markets Contracts, subject to certain conditions.

Reasons for granting the original Class Rule Waiver

On 5 August 2013, ASIC amended Rule 3.4.3 of the Rules which provides that a Market Participant does not need to comply with Rule 3.4.1 for clients other than Retail Clients, if certain information is given to the clients. The amendment to Rule 3.4.3 was to address regulatory issues arising from recent market developments, including the growing number of Market Participants establishing and operating automated services (referred to as “Crossing Systems”) that match or execute orders of their clients otherwise than on an Order Book of an exchange market (see the *ASIC Market Integrity Rules (ASX Market) Amendment 2013 (No. 2)*).

The Class Rule Waiver was originally granted because Participants who complied with Rule 3.4.3 and accordingly did not have to comply with Rule 3.4.1 queried

whether it was ASIC's intention for Rule 3.4.3(1)(b) to apply to Derivative Market Contracts, as well as Cash Market Products. Rule 3.4.3 refers to Market Transactions, which is defined as "a transaction for one or more Products, entered into on a Trading Platform or reported to the Market Operator under the Market Operating Rules." Further, "Product" is defined as a "Cash Market Product or a Derivatives Market Contract, as applicable." Rule 3.4.3(1)(b), by virtue of the definition of Product, does apply to Derivatives Markets Contracts.

The Class Rule Waiver was granted to allow for consultation on that question, particularly in relation to the intended operation of the rule, the need for IT development and time for that IT development to occur. The effect of the Class Rule Waiver was to provide relief from the requirement to comply with 3.4.1 for Derivative Market Contracts, in circumstances other than those set out in Rule 3.4.3.

Reasons for extending the original Class Rule Waiver

On 29 April 2016, ASIC made Class Rule Waiver 16/0359 which extended the operation of the Class Rule Waiver [CW 14-1091] to 30 June 2017, from its original expiry date of 30 April 2016. This was due to the consultation in relation to Rule 3.4.3(1)(b) forming part of a broader package of regulatory reform. An extension to the waiver was deemed necessary to allow sufficient time for the reform package to become operational.

ASIC has consulted with a wide variety of stakeholders, including Market Operators, Market Participants and Wholesale Clients about withdrawing Class Rule Waiver [CW 14-1091] and the operation of Rule 3.4.3(1)(b) as part of Consultation Paper 277 *Proposals to consolidate the ASIC market integrity rules*, (CP 277) published on 24 January 2017.

The feedback from CP 277 highlighted uncertainty about the intended benefits provided by the two elements of the alternative disclosure which may be given to a client under Rule 3.4.3, whether or not the Market Participant entered into the Market Transaction as principal, and the venue of execution of the Market Transaction. The reasons given for this uncertainty were:

- (a) The exchange traded options market on ASX are the only Derivative Market Contracts that this disclosure would affect;
- (b) Derivative Market Contract crossings transacted on the ASX's exchange traded option market most often involve trading against principal. This is particularly the case if the wholesale client is seeking liquidity and therefore generally assumes the liquidity provider is acting as principal.
- (c) Given there is currently only one functioning trading platform for exchange traded options, detailing the venue of execution is not needed at this point in time. Crossing rules for Derivatives Market Contracts also currently exclude these financial products from crossing systems as alternative execution venues.

ASIC maintains the view that it is important for Retail and Wholesale Clients to understand the capacity in which a Market Participant has filled their order, particularly where the transaction is with the Market Participant as principal. This helps ensure conflicts of interest arising from information asymmetry are appropriately managed by way of disclosure.

ASIC acknowledges, however, that the issue of information asymmetry is mitigated somewhat at present due to the different characteristics of the market for Derivative Market Contracts when compared with other markets.

In recognition of these different characteristics ASIC has decided to extend the operation of Class Rule Waiver [CW 14-1091] to 30 June 2020.

Prior to 30 June 2020 ASIC will review the circumstances of the market for Derivative Market Contracts to consider whether the relief in [CW 14-1091] remains appropriate. Examples of changing circumstances which may affect ASIC's view of the appropriateness of continuing the relief in [CW 14-1091] include changes in market liquidity, commencement of alternative trading venues and product innovation.

2. Purpose of the instrument

This Class Rule Waiver varies [CW 14-1091] by extending the relief from the obligation to comply with the notification requirements in relation to Derivative Market Contracts in subrule 3.4.1 of the Rules until 30 June 2020.

3. Operation of the instrument

The instrument substitutes the expiration date stated in paragraph 6 of [CW 14-1091] of "30 June 2017", with "30 June 2020".

4. Consultation

ASIC consulted on this instrument in Consultation Paper 277: *Consolidating the market integrity rules*, published on 24 January 2017.

ASIC Class Rule Waiver [CW 14-1091] is minor and machinery in nature. A Regulation Impact Statement was not required for this instrument as it is minor or machinery in nature and does not alter the existing requirements for Market Participants.

Statement of Compatibility with Human Rights

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

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ASIC Class Rule Waiver (Amendment) [CW 17/0617] is 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*.

Overview

This Legislative Instrument amends ASIC Class Rule Waiver [CW 14-1091] by extending the relief granted by the instrument from 30 June 2017 to 30 June 2020.

ASIC Class Rule Waiver [CW 14-1091] grants relief for a Market Participant from the requirement to notify clients, other than Retail clients, both:

- (a) when it enters into the client's Market Transaction as Principal; and
- (b) the execution code of the execution venue for the Crossing if the Market Transaction was executed as a Crossing.

Human rights implications

This Legislative Instrument does not engage any of the applicable rights or freedoms.

Conclusion

This legislative instrument is compatible with human rights as it does not raise any human rights issues.