
EXPLANATORY STATEMENT for ASIC Corporations (Amendment) Instrument 2018/3

Prepared by the Australian Securities and Investments Commission

Corporations Act 2001

The Australian Securities and Investments Commission (ASIC) makes ASIC Corporations (Amendment) Instrument 2018/3 (**Amending Instrument**) under subsections 601QA(1), 655A(1), 673(1) and 1020F(1) of the *Corporations Act 2001* (the **Act**).

The purpose of the Amending Instrument is to extend existing relief in a number of ASIC instruments to facilitate the quotation and trading of exchange traded funds (**ETFs**) on the market operated by Chi-X Australia Pty Ltd (**Chi-X**). The existing relief currently applies only to the market operated by ASX Limited (**ASX**).

Subsection 601QA(1) provides that ASIC may exempt a person from a provision of Chapter 5C, or declare that Chapter 5C applies to a person as if specified provisions were omitted, modified or varied as specified in the declaration.

Subsections 655A(1) and 673(1) provide that ASIC may exempt a person from a provision of Chapters 6 and 6C respectively or declare that the Chapter applies to a person as if specified provisions were omitted, modified or varied as specified in the declaration.

Subsection 1020F(1) provides that ASIC may exempt a person or a financial product (or class of persons or financial products) from all or specified provisions of Part 7.9 or declare that Part 7.9 applies in relation to a person or a financial product or a class of persons or financial products, as if specified provisions were omitted, modified or varied as specified in the declaration.

The Amending Instrument will amend the following instruments:

- ASIC Class Order [CO 10/288]
- ASIC Class Order [CO 13/655]
- ASIC Class Order [CO 13/721]
- ASIC Class Order [CO 13/1200]

(collectively **Relevant Instruments**)

In addition, ASIC has decided to extend the existing disclosure relief from section 1017B of the Act in [CO 13/721] to managed funds that are quoted and traded on the ASX market. This disclosure relief currently only applies in relation to ETFs on the ASX market.

The Amending Instrument also amends language used in the Relevant Instruments to make the terminology “market neutral” to ensure that it applies effectively to both the

ASX and Chi-X market. For example, the Relevant Instruments incorporated by reference various definitions from specific versions of the operating rules of the ASX. These definitions have been substituted with self-contained definitions that identify fundamental features of the defined terms as appropriate.

Under subsection 33(3) of the *Acts Interpretation Act 1901*, where an Act confers a power to make, grant or issue any instrument (including rules, regulations or by-laws), the power shall be construed as including a power exercisable in the like manner and subject to the like conditions (if any) to repeal, rescind, revoke, amend, or vary any such instrument.

1. Background

Chi-X holds an Australian market licence (AML) which enables it to operate a market through which participants may trade securities, and financial products that relate to a managed investment scheme.

Chi-X provide secondary trading services in securities and managed investment scheme interests that are listed, quoted and traded on the financial market operated by ASX. Chi-X also offers trading in warrants that have been admitted to quotation on the Chi-X market.

Chi-X is proposing to expand its services to include the quotation and trading of interests in ETFs on the Chi-X market.

Chi-X's proposed ETF framework will be broadly equivalent to that offered by the ASX for ETFs on the AQUA market. The AQUA market is the ASX market segment dedicated to the quotation and trading of interests in managed funds, ETFs and structured products.

ASIC has exercised its powers to grant relief from the requirements of certain provisions of the Act in order to facilitate the appropriate operation of the AQUA market by ASX. This relief currently operates specifically to the ASX market. The ETF services proposed by Chi-X will be broadly equivalent to that offered by the ASX. ASIC considers it appropriate to grant the same relief to facilitate the quotation and trading of interests in ETFs on the Chi-X market.

In addition, ASIC has decided to extend the existing disclosure relief from section 1017B of the Act in [CO 13/721] to managed funds that are quoted and traded on the ASX market. This disclosure relief currently only applies in relation to ETFs on the ASX market.

2. Purpose of the Amending Instrument

The purpose of the Amending Instrument is to extend the application of the Relevant Instruments to include ETFs on the Chi-X market.

ASIC Class Order [CO 10/288]

Class Order [CO 10/288] provides certain exemptions from the requirement under subsection 1020AB(3) to report a covered short sale transaction of a section 1020B product on a licensed market. Paragraph 4(b) of [CO 10/288] provides an exemption

for covered short sales of ETF interests or securities that are made in the course of making a market in those interests or securities on the ASX market e.g. on the AQUA market for ETFs.

We made [CO 10/288] because we considered that:

- (a) the cost to collect the reporting information in relation to these sales outweighs the benefit to the market; and
- (b) the relief promotes liquidity and confidence in Australian financial markets by helping market makers to efficiently hedge particular financial products.

The Amending Instrument extends the relief in paragraph 4(b) of [CO 10/288] to ETF market makers on the licensed market operated by Chi-X.

ASIC Class Order [CO 13/655]

Class Order [CO 13/655] modifies the application of Chapter 5C of the Act as it applies to a responsible entity. Relevantly, paragraph 4 of the class order notionally inserts subsection 601GAE.

Subsection s601GAE(1) allows a responsible entity to exercise certain discretions in determining the amount of consideration to acquire an interest in the scheme when it uses a formula or method that complies with subsection 601GAE(2).

The basis of the formula or method is determined in part on whether the interests in the scheme are in a class of interests that are AQUA products under the operating rules of ASX.

The Amending Instrument will ensure that notional s601GAE operates in relation to ETFs traded and quoted on the Chi-X market in the same manner as it currently does for AQUA products on the ASX.

ASIC Class Order [CO 13/721]

The following relief is provided under Class Order [CO 13/721]:

(a) Equal treatment relief in withdrawal from an ETF

Paragraph 601FC(1)(d) of the Act requires the responsible entity of a registered scheme to treat members of the scheme who hold interests of the same class equally and members who hold interests of different classes fairly, when exercising its powers and carrying out its duties. Class Order [13/721] provides two exemptions from this requirement.

Paragraph 4 of [CO 13/172] permits a responsible entity of an AQUA ETF to require that only an authorised participant can make a withdrawal from the fund. The relief applies in specified circumstances set out in [CO 13/721]. The relief reflects the fact that retail investors generally engage in ETF trading on the relevant secondary market and are usually prohibited from dealing directly with a responsible entity. The relief also seeks to promote market

liquidity in ETFs and to facilitate the pricing of interests in ETFs on the secondary market.

The Amending Instrument extends the relief to interests in an ETF with a comparable trading status under the operating rules of Chi-X.

(b) Equal treatment relief for the provision of information to authorised participants

The second exemption from the general requirement in paragraph 601FC(1)(d) of the Act is in paragraph 6 of [CO 13/721]. This allows the responsible entity of an AQUA ETF to provide index or portfolio information to authorised participants before other members. The relief applies in circumstances specified in [CO 13/721].

The relief addresses the risk of front running occurring as a result of the responsible entity being required to disclose information that would enable particular trading to be predicted or enable real time calculation by the public of an index that may be sold under subscription.

The Amending Instrument extends this relief to interests in an ETF with a comparable trading status under the operating rules of Chi-X.

(c) Ongoing disclosure relief

Section 1017B of the Act requires an issuer of a financial product to notify retail clients who hold the product, of material changes and significant events. This obligation does not apply if the financial product is a managed investment product that is an enhanced disclosure (ED) security under section 111AFA of the Act (see section 1017B(2))

Due to the uncertainty regarding classification of certain AQUA ETF products as ED securities under section 111AFA, ASIC provided relief from the notification obligations under section 1017B in the context of AQUA ETFs.

This relief is appropriate as the relevant issuers are subject to continuous disclosure obligations under the operating rules of the ASX and section 675 of the Act.

The Amending Instrument will extend the relief to ETFs that are able to be traded on the financial market operated by Chi-X.

The Amending Instrument will also extend this aspect of the relief to quoted ASX managed funds. We consider that the rationale for granting relief from section 1017B of the Act to responsible entities of ETFs also applies to managed funds quoted on the ASX market.

This relief for ETFs and managed funds is granted on the condition that the responsible entity complies with section 675 of the Act as if the scheme were an unlisted disclosing entity and that this is communicated in the product disclosure statements for interests in the scheme.

(d) Relevant interest relief

Section 606 of the Act prohibits (amongst other things) the acquisition of a relevant interest in voting interests in specified securities in specified circumstances. The circumstances are where the acquisition would result in an increase in voting power:

- (i) from 20% or below to more than 20%; or
- (ii) from a starting point that is above 20% and below 90%

The prohibition does not apply if the interest was acquired under one of the exceptions in s611 of the Act.

Paragraph 11 of [CO 13/721] modifies the effect of Chapter 6 and 6C of the Act by applying it to all persons as if subsections 609(19A) – 609(19E) were inserted.

The purpose of this relief is to enable authorised participants who are members of the ETF to lodge a withdrawal request under an acquisition and withdrawal facility offered by the scheme without contravening section 606 of the Act. The relief only applies when the ETF tracks a published index and in which no security is expected to represent more than 10% by value of scheme property.

Without the relief in [CO 13/721], the prohibition would extend to relevant interests in the underlying securities of an ETF acquired by reason of acquiring an interest in the ETF. We consider that the relief is appropriate because the rights attached to interests in an ETF in respect of the underlying securities of the ETF are sufficiently remote or tenuous that they are unlikely to be used as a means of gaining control of the issuer of those securities.

The Amending Instrument extends this relief in relation to interests in a scheme that are ETF securities with a comparable trading status under the operating rules of Chi-X.

(e) Substantial holding relief and beneficial trading

Section 671B of the Act requires a person to provide information to a listed company, or the responsible entity of a listed managed investment scheme, in certain circumstances, including if the person begins to have or ceases to have a substantial holding in the company or scheme. The information must also be provided if the person has a substantial holding in the scheme and there is a movement of at least 1% in their holding.

Class Order [CO 13/721] assists compliance with these obligations by removing the uncertainty that may result from any fluctuations in the composition of the index being tracked by the ETF and therefore fluctuations in a person's interest in the underlying securities, that may occur during the day.

The Amending Instrument extends this relief in relation to interests in ETFs that are traded on the financial market operated by Chi-X.

ASIC Class Order [CO 13/1200]

Section 1017D of the Act requires issuers of financial products that have an investment component to give retail investors periodic statements when either the product was offered or the holder applied for the product in this jurisdiction. The obligation applies to a number of financial products including interests in registered managed investment schemes.

Class Order [CO 13/1200] provides relief for issuers of registered schemes including ETFs and managed funds that are quoted on the AQUA market.

The relief recognises the practical difficulties that issuers of interests in these schemes face when preparing such statements. These difficulties mainly arise because issuers are unaware of the transaction price at which an investor bought or sold their interest.

The Amending Instrument extends the relief to issuers of ETFs that are able to be traded on the financial market operated by Chi-X.

3. Operation of the instrument

ASIC Class Order [CO 10/288]

The Amending Instrument amends subparagraph 4(b) and paragraph 5. The amendments have the effect of replacing ASX specific terminology with market neutral terminology and extending the relief from the covered short sale transaction reporting obligation under s1020AB(3) to ETF market makers who are registered to make a market in ETFs on the Chi- X market.

We note that the definition of ‘exchange traded fund’ in [CO 10/288] is slightly different from the definition of ‘exchange traded fund’ in [CO 13/655], [CO 13/721] and [CO 13/1200]. This variance is to ensure that the new, market neutral, definition of ‘exchange traded fund’ in [CO 10/288] aligns with the definition that was incorporated by reference in [CO 10/288] from the ASX Market Rules as at 21 April 2010.

ASIC Class Order [CO 13/655]

The Amending Instrument amends subparagraph 4(b). The amendments have the effect of replacing ASX specific terminology with market neutral terminology and applying the discretionary relief under notional s601GAE of the Act to responsible entities of ETFs that are able to be traded on the financial market operated by Chi-X.

ASIC Class Order [CO 13/721]

The Amending Instrument amends paragraph 4, subparagraphs 5(a), 5(a)(ii) and 5(a)(iii), subparagraph 5(b), paragraph 6, subparagraph 6(b), subparagraph 7(a), subparagraph 8(a) subparagraph 8(b), subparagraph 8(b)(i), paragraph 9, paragraph

10, subparagraph 10(b), paragraph 11, subparagraph 12(a), subparagraph 12(b) and paragraph 13.

The amendments have the effect of replacing ASX specific terminology with market neutral terminology and extending the following relief to responsible entities of ETFs that are able to be traded on the Chi-X market:

- Exemption from section 601FC(1)(d) of the Act when responsible entities permit authorised participants to withdraw from an ETF;
- Exemption from section 601FC(1)(d) of the Act when responsible entities provide index or portfolio information to authorised participants before other members; and
- Exemption from the requirements in section 1017B of the Act to notify holders of ETF products of material changes and significant events in relation to their ETF.

The amendments also modify Chapters 6 and 6C of the Act to cover ETFs that are able to be traded on the financial market operated by Chi-X. Chapters 6 and 6C of the Act is modified so that the ability to lodge withdrawal requests by the authorised participants who are members of the ETF under the acquisition and withdrawal facility offered by a scheme does not by itself give these members a relevant interest in any securities held by the ETF.

In addition, [CO 13/721] provides by declaration further clarity on the obligations in relation to beneficial tracing.

The amendments also extend the exemption from s1017B of the Act to issuers of quoted ASX managed funds.

ASIC Class Order [CO 13/1200]

The Amending Instrument amends paragraphs 1, paragraphs 4-7, subparagraphs 8(a) and (b) and paragraph 9.

The amendments have the effect of replacing ASX specific terminology with market neutral terminology and extending the relief in [CO 13/1200] to responsible entities of ETFs that are able to be traded on the Chi-X market. This modifies their obligations in regards to periodic reporting requirements.

4. Consultation

In Consultation Paper 235 *Proposed amendments to ASIC market integrity rules and instruments for the Chi-X investment product market (CP 235)*, ASIC consulted on a number of proposals in relation to the quotation and trading of ETFs on the Chi-X market.

One of the proposals was to extend existing ASIC relief applicable to ETFs quoted on the ASX market to ETFs admitted to quotation on the Chi-X market. This included extending existing relief in the Relevant Instruments.

We also consulted on our proposal to extend the relief under [CO 13/271] currently available to AQUA ETFs to AQUA managed fund products quoted on the ASX market in CP 235.

In addition, we engaged in a targeted consultation with relevant industry bodies and market operators on draft amendments to the Relevant Instruments.

Consultation feedback was supportive of ASIC's proposal to extend existing relief applicable to ETFs quoted on the market operated by ASX to ETFs admitted to quotation on the Chi-X market. We have incorporated relevant feedback in finalising the Amending Instrument.

Statement of Compatibility with Human Rights

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

ASIC Corporations (Amendment) Instrument 2018/3

The ASIC Corporations (Amendment) Instrument 2018/3 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

Chi-X exchange traded funds

Chi-X Australia Pty Ltd (**Chi-X**) holds an Australian market licence which enables it to provide secondary trading services in securities and managed investment scheme interests that are listed, quoted and traded on the financial market operated by ASX Limited (**ASX**).

Chi-X is expanding its services to include trading in exchange traded funds (**ETFs**) that have been admitted to quotation on the Chi-X market. This service is broadly equivalent to that offered by the ASX in relation to ETFs on its AQUA market that have been admitted to quotation on the financial market operated by ASX.

ASIC has exercised its powers to grant relief from the requirements of certain provisions of the *Corporations Act 2001 (the Act)* in order to facilitate the appropriate operation of the AQUA market by ASX. This relief currently operates specifically to the ASX market. The ETF services proposed by Chi-X will be broadly equivalent to that offered by the ASX. ASIC considers it appropriate to grant the same relief to facilitate the quotation and trading of interests in ETFs on the Chi-X market. ASIC Corporations (Amendment) Instrument 2018/3 therefore amends the following instruments to extend their application to ETFs quoted and traded on the Chi-X market.

(a) **ASIC Class Order [CO 10/288]:**

This Class Order gives relief to ETF market makers from the requirement in s1020AB(3) of the Act to report covered short sales in the course of making a market. The relief recognises that the cost to collect the reporting information in relation to these sales outweighs the benefit to the market.

(b) **ASIC Class Order [CO 13/655]:**

This Class Order modifies the application of Chapter 5C of the Act as it applies to a responsible entity. Relevantly, paragraph 4 of the class order notionally inserts subsection 601GAE.

Subsection s601GAE(1) allows a responsible entity to exercise certain discretions in determining the amount of consideration to acquire an interest in the scheme when it uses a formula or method that complies with subsection 601GAE(2).

(c) **ASIC Class Order [CO 13/721]:**

This Class Order makes the following exemptions to provide relief to responsible entities of ETFs:

- Exemption from the requirement in s601FC(1)(d) of the Act to provide equal treatment of members when responsible entities permit authorised participants to withdraw from an ETF;
- Exemption from the requirement in s601FC(1)(d) of the Act to provide equal treatment of members when responsible entities provide index or portfolio information to authorised participants before other members; and
- Exemption from the requirement in s1017B of the Act to notify retail clients of material changes and significant events in relation to their ETF.

This Class Order also modifies Chapters 6 and 6C of the Act so that the ability to lodge a withdrawal request by an authorised participant who is a member of the ETF under the acquisition and withdrawal facility offered by a scheme does not by itself give the member a relevant interest in any securities held by the ETF.

In addition, CO 13/721 provides by declaration further clarity on the obligations in relation to beneficial tracing.

(d) **ASIC Class Order [CO 13/1200]:**

This Class Order modifies the obligations under s1017D of the Act in regards to periodic statement reporting requirements for issuers of quoted ETFs. This relief reflects the practical difficulties issuers face in preparing these periodic statements.

ASX managed funds

ASIC has also exercised its powers to extend the existing disclosure relief from section 1017B of the Act in [CO 13/721] to issuers of managed funds that are quoted and traded on the ASX market. This disclosure relief currently only applies in relation to ETFs quoted and traded on the ASX market. ASIC considers that the rationale for granting relief from s1017B of the Act to responsible entities of ETFs also applies to managed funds quoted on the ASX market. As such, ASIC Corporations (Amendment) Instrument 2018/3 also provides an exemption from s1017B of the Act to issuers of quoted ASX managed funds.

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.

Australian Securities and Investments Commission