

ASIC CLASS ORDER [CO 09/39]

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 09/39] under s1020F(1)(c) of the *Corporations Act 2001* (the *Act*).

Section 1020F(1)(c) relevantly provides that ASIC may declare that Part 7.9 of the Act applies in relation to a person as if specified provisions were omitted, modified or varied.

1. Background

People sometimes sell (*short sell*) securities which they do not own with a view to profiting by repurchasing them later at a lower price. One approach to facilitating this practice is for the people (the *borrowers*) to have in place an arrangement (a *securities lending arrangement*) whereby another person (the *lender*) makes securities available to settle the initial sale. Under the arrangement, the borrower will have an obligation to transfer equivalent securities to the lender at a later time. The practice of short selling securities with an arrangement of this kind in place is referred to as *covered short selling*.

In September 2008, ASIC responded to conditions in international and Australian financial markets by introducing measures aimed at limiting the potential for Australian markets to become disorderly due to short selling. Under ASIC Class Order [CO 08/751], ASIC prohibited covered short selling of all securities, managed investment products and stapled securities quoted on licensed markets in Australia, subject to certain exceptions. Where covered short selling is permitted, the short selling transaction is subject to a reporting regime in accordance with ASIC Class Order [CO 08/751].

ASIC lifted the ban on covered short selling of non-financial securities on 19 November 2008. ASIC indicated the ban on covered short selling of financial securities would remain in place until at least 27 January 2009. ASIC decided it was appropriate to extend the operation of the ban in January and again in March, given the conditions of the Australian and international markets. On 6 March, ASIC advised the market that the ban would continue under review until 31 May 2009.

2. Purpose of the class order

This instrument:

- removes the ban on covered short selling of financial securities; and

- makes technical amendments to clarify that disclosure and reporting apply to covered short sales as opposed to 'exempt covered short sales' as exemptions to permit covered short selling will not be needed once the ban is lifted.

The Act recognises that short selling has a legitimate role in the market. The ban on covered short selling was a temporary measure aimed at limiting the potential for the Australian markets to become disorderly due to short selling during a time of turmoil in the global financial markets. ASIC has now decided that that it is not warranted for the ban to continue. In reaching this decision, ASIC considered the current conditions of the Australian and global financial markets and the potential for aggressive or predatory practices via short selling. ASIC also had regard to the possible loss of some market efficiency or price discovery through the continuation of the ban.

3. Operation of the class order

This instrument varies ASIC Class Order [CO 08/751] by omitting notional s1020BD of the Act. Notional s1020BD prohibits the covered short selling of certain securities, subject to some exemptions. Upon commencement of this instrument, the prohibition no longer applies. The exemptions from the ban and related definitions are also omitted.

This instrument also makes two variations to the disclosure and reporting requirements. Firstly, it varies ASIC Class Order [CO 08/751] by removing references to 'a short sale' and 'an exempt covered short sale' at notional s1020BC(2) and (3) and their definitions at s1020BC(6). This is replaced with references to and definitions of a 'covered short sale'. The effect of this is that a participant in the market (*broker*) who receives a request to sell s1020B products is required to record whether the sale is a long sale or a covered short sale (instead of whether the sale is a long sale, short sale or an exempt covered short sale). The person (*client*) making the request must inform the broker which of the two types of sales is being requested. As before, if the client does not volunteer this information, the broker is required to ask.

The instrument also varies ASIC Class Order [CO 08/751] by amending the definition of 'reportable short sale' in notional s1020BC(6). The effect of this is that brokers will be required to report each day to the ASX by 9am the following trading day the total number of products sold pursuant to covered short sales and naked short sales that occur as a result of the exercise of an ASX exchange traded option.

4. Documents incorporated by reference

No documents are incorporated by reference.

5. Consultation

ASIC received input from industry representative bodies and other regulators before making this instrument.