

ASIC CLASS ORDER [CO 08/752]

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 08/752] 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 a form of **covered short selling**.

On Friday 19 September 2008, ASIC issued ASIC Class Order [CO 08/751] which declared that Part 7.9 of the Act has effect as if it included a s1020BC as set out in that instrument. That section requires the disclosure of aggregate information about certain covered short sales on a daily basis. To support this requirement, s1020BC also requires:

- a person (the **client**) asking a financial services licensee (the **broker**) to sell securities in circumstances that make the sale a covered short sale to tell the broker that it is such a sale;
- before selling securities on behalf of a client, a broker must ask the client whether the sale would be a covered short sale.

Since the making of ASIC Class Order [CO 08/751], ASIC has continued to assess moves by other international regulators. Relevant developments include the following:

- The Securities Exchange Commission of the United States prohibited the short selling of securities in certain quoted financial firms.

- The Financial Services Authority of the United Kingdom introduced new provisions prohibiting any active creation or increase of net short positions in certain quoted financial companies.
- Regulatory agencies in other jurisdictions, such as France, Germany, Ireland and Ontario, have similarly introduced measures to restrict short selling in securities of certain quoted financial sector issuers.

Other regulators are assessing their responses.

2. Purpose of the class order

The regulatory developments in overseas markets, in effect, restrict short selling activity in those markets. This intensifies the risks for the Australian market. Because global funds can move quickly, the risk of unwarranted short selling activity on the Australian market has increased as the opportunities to profit from short selling activity elsewhere have been limited. This risk has been assessed by ASIC in the context of the small size, relative to other markets, of the Australian market. It extends beyond financial stocks.

This class order is aimed at limiting the potential for the Australian markets to becoming disorderly due to short selling.

3. Operation of the class order

The class order varies ASIC Class Order [CO 08/751] with the effect that Part 7.9 of the Act has effect as if it also included a new s1020BD. That section has the effect of prohibiting covered short selling of all securities traded on licensed financial markets in Australia. There is an exception for short selling, for hedging purposes, by official market makers in ASX market traded options and warrants. This only applies in relation to the hedging of positions they have taken in their capacity as market makers under the ASX Market Rules.

ASIC Class Order [CO 08/752] also amends notional s1020BC(3) to include an obligation for brokers to record in written or electronic form, their client's answers on whether a sale order involves a covered short sale. This requirement is aimed at enhancing compliance with the prohibition on such sales.

The instrument commences on the date it is registered. This is expected to be 22 September 2008.

4. Documents incorporated by reference

No documents are incorporated by reference.

5. Consultation

ASIC informally consulted with the ASX before making the instrument. No further consultation was undertaken given the urgency and exceptional circumstances of the matter.

The making of the instrument was announced on the day it was made, namely Sunday 21 September 2008 while markets were closed. After the announcement, participants in the ASX market and securities lenders were advised, through their representative bodies of the making and effect of the instrument.

ASIC will reassess the position and advise the market in 30 days of the making of the instrument, whether or not it will at that time, or at a later date, lift the prohibition for covered short sales for non-financial stocks.