



9 July 2024

The Treasury
Langton Crescent
PARKES ACT 2600

By email.

Dear Ms Kelly

Request for Markets-Related Legislative Reforms

AFMA writes in relation to a request for important reform of elements of the *Corporations Act 2001*.

These relate to the following four areas:

- Inadvertent wash trades.
- Equity swap trades ('give-ups').
- The ability to collect electronic payment instructions of target company shareholders for payments during takeovers.
- The market making exemption.

We are writing as these are long standing matters of significant importance to the industry that warrant legislative reform. ASIC has provided a 'no action' work around for the market making exemption and is considering providing one for inadvertent wash trades and has declined to provide one for equity swap trades. While welcome where granted these work arounds typically do not fully address all concerns and are a far from ideal arrangement in all cases. We understand that the current inability to collect electronic payment instructions for takeover targets is a direct outcome of legislation which we understand will require legislative action to address.

Our priorities for these matters are as follows:

1. Our current top priority is the resolution of the inadvertent wash trades issue. This long standing and well-known issue causes unavoidable technical Corporations Act breaches. These are directly at odds with the risk tolerance of international and local firms.

2. Equity swap trades – like inadvertent wash trades this item can be read to cause technical short sale breaches and significant market inefficiencies that are outside of firms’ risk tolerances. It is important that Australia’s regulatory environment allows firms to engage in standard practices without risk of technical breach, and with an eye to market efficiency.
3. Legislative changes to allow registries to collect electronic payment instructions to facilitate payments during takeovers is a critical step to enable the final phase-out of cheques. The phase out of cheques is scheduled by the Government for 2030 (at the latest), we suggest changes to the legislation should be in place two or three years before this date. As time passes the criticality of this item will increase.
4. Moving market making exemptions into their proper place in legislation is a good practice outcome, aligned with ALRC principles. It is last on our priority list only because it currently has a long-standing regulatory no-action work around.

Inadvertent wash trades

In March AFMA made an application to ASIC for ‘no action’ relief in relation to inadvertent wash trades. This application is still being processed. Even if approved, however, it will not fully address the unwarranted risks, and poor formulation of the *Corporations Act* in relation to inadvertent wash trades.

The drafting issues with section 1041B in relation to wash trading have been recognised since the Act was passed in 2001. Subsequent reviews including by CAMAC in 2009 and academic reviews have called for ‘urgent reform’¹ of the section. Treasury itself consulted on proposals in relation to s1041B reform in a paper (attached) in 2007²:

“3.42 There are concerns, however, that as a result of subsection 1041B(2), a defendant could incur civil and criminal liability for transactions that were entered into for legitimate purposes and did not create a false or misleading appearance.

3.43 There is some uncertainty as to how subsection 1041B(2) and section 5.6 of the Criminal Code interact, and what their combined effect is.”

We refer to our recent letters to ASIC (attached) for further discussion of the issue. The key takeaway is that an intent-based approach should be reinstated³ in the current Act.

¹ Armson, E. (2009). False trading and market rigging in Australia. *Company and Securities Law Journal*, 27(7), 411-425.

² Commonwealth of Australia, Department of the Treasury, Review of Sanctions in Corporate Law (5 March 2007), <https://webarchive.nla.gov.au/awa/20070910042200/http://pandora.nla.gov.au/pan/76542/20070910-1334/www.treasury.gov.au/contentitem.html> pp 39-42.

³ The Corporations Act 1989 had such an intent element although as Treasury’s consultation notes the formulation was not optimal as it was structured as a defence.

The simplest option for legislative reform would be to remove the deeming provisions. This would have the effect that a firm or natural person would need the requisite intent for an offence to be committed. This would be consistent with case law in recent years around the nexus between ‘false or misleading appearance’ and intention.

AFMA members take their regulatory obligations seriously, and none more so than those created by legislation. Many firms have a zero-tolerance approach for compliance. This is commendable, and understandable in the context of the large increase in penalties in recent years.

The unavoidable nature of some inadvertent wash trades does not sit appropriately with the current law, and with these creditable intentions of firms.

The current state of regulatory affairs has also led to efforts by firms to minimise inadvertent wash trades which have introduced inefficiencies in the market. These include trading via brokers that might not offer the best liquidity.

‘No action’ commitments from the regulator (if granted), while welcome, are not a full solution as they do not address the underlying technical breach.

AFMA holds that the long-established issues with the drafting of 1041B warrant legislative work being commenced to address them.

Equity swap trades (‘give-ups’)

AFMA also sees a need for legislative reform for equity swap trades (also known as ‘give-ups’). These are an important standard trading practice in many leading jurisdictions including Australia that provides increased flexibility and efficiency for investors.

AFMA holds that equity swap trading should qualify for an exemption of a similar nature to that provided in the short-selling relief for market makers. We have sought relief from ASIC in the attached letter amongst other approaches. AFMA has for the past 5 years at various points pursued this matter with ASIC, but we have concluded that this process has now reached an end point.

ASIC’s positioning has been more to focus on the current state of the law in various areas as the main consideration for what should instead rightly be a matter of policy. We believe this is placing these matters in the incorrect order – the policy should drive the law, not the converse.

The legislative changes could readily be based on our proposal to ASIC for no action relief (see attached letter).

We note that at present equity swap trading does not fit particularly well with the wash trade provisions of 1041B either. Our proposed amendments outlined to that section would also address these frictions.

Changes to facilitate the phase out of cheques

The industry has already switched almost all payments away from cheques.

A residual area of cheques usage is in relation to payments to holders of securities of a company that is the process of being taken over.

The reasons for cheques continued use in this corner of the market is that legislated requirements do not require (or thereby facilitate) the provision of electronic payment instructions by target firm registries. As a practical matter these have the effect of requiring the usage of cheques which only require the information that is provided.

[Section 641](#) of the Corporations Act 2001 specifies the information that must be provided by the target registry. In AFMA's view it should be extended to include electronic payment instructions (this could include bank account details or New Payments Platform related information e.g. 'PayID'). This would address the bulk of the residual requirement for cheques in financial markets.

We also understand that some company constitutions may include clauses that stipulate how payments can be made or received, and thereby effectively limit payments to cheques. To facilitate the transition from cheques to electronic payments legislative changes to override these soon-to-be outdated company constitutions is appropriate.

We understand that Treasury has indicated a phase out date for cheques of June 2030 and an intention by the Government to cease usage by 2028.

To achieve the 2030 date, we advise that measures should be taken well in advance to remove legislative barriers.

Market Making Relief

A tightening of the Short Selling arrangements was made to the Corporations Act with the Corporations Amendment (Short Selling) Act 2008.

Subsequently ASIC [consulted on relief arrangements in 2009](#) to facilitate market making. These resulted in ASIC [granting relief](#), effectively reversing the legislative outcomes for a select range of market practices. Through a number of iterations this relief persists to this day, the currently in-force instrument being [ASIC Corporations \(Short Selling\) Instrument 2018/745](#).

This is a stable and well-formed relief that continues to function appropriately to support important market functions.

However, consistent with the principles advocated by the Australian Law Reform [Commission in Confronting Complexity: Reforming Corporations and Financial Services Legislation](#) and recognising the passage of 15 years these structures should be incorporated into the primary legislation.

This update to s 1020B should be straightforward as the relevant legislative changes are already well established in the legislative instrument.

Conclusion

The industry is committed to full compliance with the law. Provisions that create unavoidable breaches even if minor or subject to 'no-action' commitments by regulators, or that are a poor fit for standard international best practices, should be updated from time to time to support the industry in this commitment.

We would be pleased to assist supporting a process to address these matters, or to support the establishment of the appropriate machinery of government (e.g. a body like CAMAC) to systematically manage these type of matters more generally.

Yours sincerely

A handwritten signature in black ink that reads "Damian Jeffree". The signature is written in a cursive, slightly slanted style.

Damian Jeffree
Head of Financial Markets, Digital and Exchanges