



OWNERSHIP MATTERS

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24 January 2012

Katie Ryder
Australian Securities & Investments Commission

Email: katie.ryder@asic.gov.au

RE: Submission on disclosure of substantial shareholdings under securities lending arrangements

Dear Ms Ryder,

Thank you for the opportunity to comment on the issue of disclosure of substantial shareholdings arising as a result of securities lending arrangements. Ownership Matters (OM) is an Australian owned governance advisory firm serving institutional investors that was formed in 2011. In 2009, two of OM's principals, while employees of RiskMetrics (now ISS), were involved in preparing a submission to ASIC's original consultation paper on substantial shareholding disclosure.¹

OM is broadly supportive of the amended disclosure regime in Class Order 11/272 for substantial shareholdings for lending intermediaries (such as prime brokers) that arise as a result of securities lending arrangements. From submissions from other firms to the original 2009 consultation, and from public commentary by market participants, OM is aware that a number of participants in the securities lending industry remain opposed to any requirement for disclosure of substantial shareholdings arising for intermediaries as a result of securities lending arrangements. This opposition appears based on the regulatory burden arising from the disclosure requirement, the view that securities lending intermediaries have no real influence on the economic and voting control of listed entities and that the short selling disclosure and substantial shareholder regime for beneficial owners provides adequate information to the market on the control implications of securities lending transactions. OM submits however that there is compelling public interest in requiring securities lending intermediaries to comply with the amended substantial shareholder regime as laid out in the Class Order for the following reasons:

- Securities are borrowed not only for the purposes of covering short sales. This means that certain types of activity – such as borrowing securities in the context of a competitive takeover offer not for short selling purposes but to influence the transaction on behalf of technically 'unrelated' parties – would be caught only through the disclosure of substantial interests by intermediaries.² Borrowing in such a scenario could be designed to reduce liquidity in an entity's securities therefore reducing the potential for competing interests to influence a control transaction (and making difficult traditional arbitrage strategies by

¹ The RiskMetrics submission is available at

[http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/cp107-RiskMetrics-submission.pdf/\\$file/cp107-RiskMetrics-submission.pdf](http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/cp107-RiskMetrics-submission.pdf/$file/cp107-RiskMetrics-submission.pdf).

² In February 2007 broking house Tricom became a substantial shareholder in Alinta Limited, then a takeover target, through borrowing arrangements. Tricom was closely allied, although not formally associated with, then ASX listed financial services group Babcock & Brown, part of the consortium that eventually acquired Alinta. In May 2007 ASIC required Tricom to provide a revised substantial shareholder notice including details of the lending agreement under which Tricom's interest had arisen.

investors such as hedge funds betting on the outcome of a takeover offer or attempting to extract a higher offer price). Requiring disclosure of 'prime broker' substantial interests provides information to the market in this situation – such as which entity has lending 'inventory' available - that can be verified against other disclosures and allow participants to assess the impact on a control transaction of stock borrowing at or close to the time the substantial borrowing activity has occurred. The importance of disclosure in these circumstances is increased due to the fact most control transactions now occur through shareholder votes under schemes of arrangement and not through formal takeover offers under the Corporations Act.

- The fact there is high demand for borrowing of a particular entity's securities, resulting in a substantial interest disclosure for a lending intermediary such a prime broker is valuable information for the market. As noted above, borrowing of securities can occur for a myriad of purposes and not simply for short selling, and so disclosure of lending related shareholdings provides additional information to market participants. There is no evidence to suggest these types of shareholding disclosures are not understood by market participants (OM is aware opponents of requiring such disclosures have argued they are 'confusing' to the market).³

Requiring disclosure of substantial interests arising as a result of securities lending arrangements unquestionably imposes a compliance burden on intermediaries such as prime brokers. OM is not aware of any public information on the costs of this burden to intermediaries and notes that the disclosure regime under Class Order 11/272 specifically exempts from disclosure certain interests that arise through strict interpretation of the Corporations Act (such as situations where a prime broker has the right to borrow securities in an entity under a lending arrangement but has not exercised that right). Intermediaries such as prime brokers have operated in the Australian market for many years under the existing (and now streamlined) disclosure requirements and the compliance burden does not appear to have unduly restricted their capacity to operate. Without compelling empirical evidence of cost burdens from the 'prime broker' substantial shareholding disclosure requirements leading to negative consequences for the market generally there is an over-riding public (and general market) interest in having this information publicly available.

Yours sincerely,

Dean Paatsch & Martin Lawrence

Ownership Matters Pty Ltd

³ See, for example, Andrew Main, 'ASIC move on substantial notices on stock lending creates 'confusion': industry group', *The Australian*, 15 April 2011, available at <http://www.theaustralian.com.au/archive/business-old/asic-move-on-stock-lending-upsets-intermediaries/story-e6frg96f-1226039786376>.