



ASIC

Australian Securities &
Investments Commission

REPORT 706

Response to submissions on CP 319 and [CO 11/272] Securities lending by agents and substantial holding disclosure

November 2021

About this report

This report highlights the key issues that arose out of the submissions received on [Consultation Paper 319](#) *Securities lending by agents and substantial holding disclosure* (CP 319) and details our responses. It also covers our targeted consultation on the remake of Class Order [CO 11/272] *Substantial holding disclosure: Securities lending and prime broking*.

About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents.

Consultation papers: seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance.

Regulatory guides: give guidance to regulated entities by:

- explaining when and how ASIC will exercise specific powers under legislation (primarily the Corporations Act)
- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
- giving practical guidance (e.g. describing the steps of a process such as applying for a licence or giving practical examples of how regulated entities may decide to meet their obligations).

Information sheets: provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

Reports: describe ASIC compliance or relief activity or the results of a research project.

Disclaimer

This report does not constitute legal advice. We encourage you to seek your own professional advice to find out how the Corporations Act and other applicable laws apply to you, as it is your responsibility to determine your obligations.

This report does not contain ASIC policy. Please see [Regulatory Guide 222](#) *Substantial holding disclosure: Securities lending and prime broking* (RG 222).

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A Overview/Consultation process

Consultation on relief for agent lenders

- 1 We made [Class Order \[CO 11/272\]](#) *Substantial holding disclosure: Securities lending and prime broking* to ensure substantial holding disclosure by those involved in securities lending was more practical and meaningful. [Regulatory Guide 222](#) *Substantial holding disclosure: Securities lending and prime broking* (RG 222) explains how the relevant interest provisions operate in relation to securities lending and the relief we have provided.
- 2 In July 2019 we consulted on extending the type of relief provided by [CO 11/272]. [Consultation Paper 319](#) *Securities lending by agents and substantial holding disclosure* (CP 319) sought feedback on proposals to provide relief to intermediaries that act as agents in securities lending transactions (agent lenders). We proposed granting relief to agent lenders that was consistent with the type of relief that [CO 11/272] provided to other intermediaries involved in securities lending, such as prime brokers.
- 3 We received three confidential and two non-confidential responses to CP 319. We are grateful to respondents for taking the time to send us their comments.
- 4 For a list of the non-confidential respondents to CP 319, see the appendix. Copies of these submissions are currently on the [CP 319 page](#) on the ASIC website

Consultation on remake of [CO 11/272]

- 5 Under the *Legislation Act 2003*, legislative instruments are automatically repealed or ‘sunset’ after 10 years unless action is taken to preserve them. This ensures that legislative instruments are kept up to date and only remain in force while they are fit for purpose and relevant.
- 6 Before re-making a legislative instrument, appropriate consultation must be undertaken. This may include targeted consultation that draws on the knowledge of persons having expertise and ensures persons likely to be affected by the proposed instrument had an adequate opportunity to comment.
- 7 [CO 11/272] was due to sunset on 1 October 2021. We sought feedback directly from industry stakeholders about our proposal to remake

[CO 11/272], including our previous proposal canvassed in CP 319 to extend relief to agent lenders. We consulted with relevant industry and professional associations and investment and governance advisory bodies. We received eight confidential submissions in response. We are grateful to respondents for taking the time to send us their comments.

Responses to consultation

- 8 This report highlights the key issues that arose out of the submissions received on [CP 319](#), our further consultation on remaking [CO 11/272], and our responses to those issues. It is not a comprehensive summary of all responses received.
- 9 The main issues raised by respondents related to the scope of the proposed relief for agent lenders. Industry participants argued in favour of a broader exemption for agent lenders, while another submission objected to any exemption. We received feedback that [CO 11/272] did not require any significant amendment for other intermediaries involved in securities lending.

B Key issues arising from CP 319 and remaking [CO 11/272]

Key points

In CP 319, we proposed deferring the point in time that an agent lender acquires a relevant interest under an agent lending agreement (authorisation agreement) for the purposes of the substantial holding disclosure provisions in Ch 6C of the *Corporations Act 2001* (Corporations Act): see paragraphs 10–12.

Industry stakeholders supported relief, but some argued agent lenders should have a full exemption from the relevant interest provision (s608) and Ch 6C: see paragraphs 13–27.

In considering whether to remake [CO 11/272] or allow it to sunset, we sought feedback on whether it had been operating effectively and efficiently since it had first been made. Industry stakeholders overwhelmingly agreed that it had been operating effectively and efficiently, and that ASIC should remake [CO 11/272]: see paragraphs: 28–30.

Deferral relief for agent lenders

- 10 In Proposal B1 of [CP 319](#) we sought feedback on a proposed legislative instrument that would defer the point at which an agent lender acquires a relevant interest in their client’s securities for the purposes of the substantial holding disclosure provisions in Ch 6C of the Corporations Act. This proposed deferral relief for agent lenders was analogous to the deferral relief in [CO 11/272] for intermediaries who may borrow their clients’ securities.
- 11 The relief would mean that, for Ch 6C disclosure purposes, an agent lender does not acquire a relevant interest in their client’s securities at the point those securities become available for potential lending (lending pool securities). Instead, the agent lender would acquire a relevant interest when the client’s securities are actually lent out. In effect, the relief would postpone or defer the point in time when an agent lender acquires a relevant interest in the client’s securities. This ‘deferral relief’ may in turn defer the point at which substantial holding disclosure is required under s671B.
- 12 We consider that an agent lender has more substantive control over securities that have been lent out than the agent has over securities that are merely in the lending pool. This is because, under the authorisation agreement with the client, an agent lender usually has discretion to terminate the securities lending transactions and recall securities (whereas securities in the lending pool are generally matched to appropriate borrowers in an automated way).

Feedback on our proposals

Proposed deferral relief for lending pool securities

- 13 The Australian Shareholders Association (ASA) agreed that the potential for securities to be on-lent was not important in the context of control. However, they argued that it could be important in terms of informing beneficial holders about the potential for their securities to be on-lent. The ASA considered this would give beneficial holders information about their exposure to counterparty risk through securities lending and would also flag to the market the potential greater volatility of the securities (when compared to other companies with major holders who do not participate in securities lending).
- 14 Industry stakeholders (who either represent those who participate in securities lending or act as agent lenders) supported deferral relief. However, these respondents argued that agent lenders should not have a relevant interest at all and should be granted a broad exemption from s608. This is because agent lenders generally act on client instructions and rarely exercise unfettered discretion over the client's securities. These respondents argued that substantial holding disclosure by agent lenders was not useful to the market.
- 15 Industry stakeholders also highlighted the differences between prime broking and agent lending arrangements. They said that relief granted for agent lenders should be different from that given to prime brokers, because agent lenders are not a party to the securities lending transaction and do not obtain full legal title to the loaned securities.

ASIC's response

We have introduced the deferral relief: see [ASIC Corporations \(Securities Lending Arrangements\) Instrument 2021/821](#).

Why deferral relief is more appropriate than no relief

We consider that it would be inappropriate not to give agent lenders relief. In the absence of deferral relief, an agent lender would acquire a relevant interest when securities are added to their lending pool and may need to give substantial holding disclosure at this point. However, there would ordinarily be no change in the agent's relevant interest when the securities are lent out and, therefore, no additional disclosure obligation. Our deferral relief seeks to more closely align the agent lender's Ch 6C disclosure obligations with the more substantive change in their control over securities.

For this reason, it is more consistent with the aims of Ch 6C to give agent lenders deferral relief than to not. We note this does

affect the disclosure that lenders should give underlying beneficial holders about their securities lending practices: see RG 222.17.

It would also be inconsistent with our policy in RG 222 to withhold relief from intermediaries who act as agent lenders when intermediaries who act as prime brokers have deferral relief. We have already given agent lenders individual relief for this reason.

Why we do not consider that a broad exemption is justified

Despite submissions from industry stakeholders, we are not in favour of a broad exemption from the substantial holder obligations for agent lenders. This is because we consider that agent lenders are analogous to prime brokers for the purposes of Ch 6C. In particular, agent lenders have a broad discretion to terminate securities transactions and, therefore, an important discretion over the recall of loaned securities.

Although there may be differences in the roles that agent lenders and prime brokers play in securities lending, we do not consider these differences justify granting a broad exemption from the substantial holding disclosure obligations to agent lenders.

It would also be inconsistent with ASIC's policy to grant a broad exemption from s608 where a person has active discretion over securities (e.g. see [Regulatory Guide 5 Relevant interests and substantial holding notices](#) (RG 5) at RG 5.86–RG 5.87).

Proposed extension of deferral relief to collateral securities

- 16 In Proposal B4 of [CP 319](#), we sought feedback on whether our proposed deferral relief should extend to other securities, including securities delivered by a borrower as collateral for securities lending (collateral securities) and securities purchased with cash collateral delivered by the borrower (purchased securities).
- 17 Industry stakeholders supported broader relief from s608, so that it applies to *any* securities that an agent lender has a relevant interest in due to their authorisation agreement with a client lender. It was submitted that if relief was only granted for lending pool securities, agent lenders would still have to incur significant costs for IT systems to monitor the relevant disclosure data. It was argued that these costs would significantly outweigh any regulatory benefit.
- 18 One respondent said that an agent lender should not have a relevant interest in collateral securities where a triparty collateral manager has been appointed. According to the respondent, the appointment of such a manager removes a lot of the agent lender's role regarding collateral or purchased securities. The respondent provided the example that the triparty collateral manager ensures collateral posted by the borrower satisfies the lender's criteria, ensures the collateral remains sufficient and will not allow the agent lender to deal in the collateral before an event of default.

ASIC's response

After considering the responses to CP 319, we maintain the view that relief should only be granted for lending pool securities and not extend to collateral securities. This is because an agent lender has similar power over the disposal of both loaned securities and collateral securities. The agent's discretion to terminate a securities lending transaction will result in disposal of the loaned securities (which are returned to the client) and collateral securities (which are returned to the borrower or sold).

Based on information available, we did not form any definitive view on the role that triparty collateral managers may play. If triparty collateral managers do reduce another intermediary's discretion over collateral, then it is likely the manager itself may have a relevant interest in the securities and therefore potential substantial holding disclosure obligations.

Feedback on the proposed legislative instrument for agent lenders

Proposed definition of 'authorisation agreement'

- 19 In Proposal B1 of [CP 319](#), we sought feedback on the definition of 'authorisation agreement' in the proposed legislative instrument.
- 20 Some respondents suggested that the definition of 'authorisation agreement' in the proposed legislative instrument was too prescriptive and could result in agent lenders not being able to rely on the legislative relief if they do not satisfy the definition.

ASIC's response

We have inserted a less prescriptive definition of 'authorisation agreement' in the legislative instrument: see s6 of [ASIC Instrument 2021/821](#). This recognises that there are no standard authorisation agreements for agency arrangements. From a policy perspective, there is no need for the definition to be prescriptive.

Proposed definition of 'custodial business'

- 21 In Proposal B1 of [CP 319](#), we sought feedback on whether the definition of 'custodial business' in the proposed legislative instrument adequately described the business of agent lenders.
- 22 Most respondents suggested that the definition was inappropriate, because not all agent lenders carry on a custodial business.

ASIC's response

We have inserted notional s609(10C) to ensure that the business of agent lenders is adequately described and is not overly prescriptive: see s7 of [ASIC Instrument 2021/821](#). This is to ensure that agent lenders providing genuine agent lending services can rely on our relief.

Retention of relevant interest when securities on-lent

- 23 In Proposal B2 of [CP 319](#), we sought feedback on whether to modify s608 so that the agent lender retains a relevant interest in loaned securities in a similar way to the client's retention of a relevant interest due to notional s608(8A) that was inserted by [CO 11/272]. This modification was intended to make monitoring relevant interests more practical, and recognises that the lender of securities often does not know about the borrower's subsequent transactions.
- 24 Some respondents agreed that the proposed modification would make it more practical for agent lenders to monitor their relevant interests. Other respondents reiterated their comments that agent lenders should have a complete exemption from s608 for loaned securities.

ASIC's response

We have modified s608 so that the agent lender retains a relevant interest in loaned securities: see s6 of [ASIC Instrument 2021/821](#). We are not prepared to give agent lenders a broader exemption.

Relief from requirements to disclose consideration and attach agent lending agreements

- 25 In Proposal B3 of [CP 319](#), we sought feedback on:
- (a) removing the requirement to disclose fees for agent lending; and
 - (b) requiring a summary of the key terms of the authorisation agreement, instead of the full authorisation agreement, to be attached to the substantial holding notice.
- 26 We asked whether the relief should be conditional on the agent lender agreeing to provide the authorisation agreement to the listed entity or ASIC on request. This is because, unlike other securities lending agreements, there is no standard form agreement.
- 27 Respondents to this proposal supported relief, but were opposed to providing the agreement on request. They pointed out that such agreements are confidential, and ASIC has powers to obtain documents if necessary.

ASIC's response

After considering responses to CP 319, we concluded that it would be more appropriate for ASIC to procure authorisation agreements using ASIC's compulsory powers if the need arises, rather than require agent lenders to provide the agreement on request.

Feedback on remaking [CO 11/272]

- 28 We directly sought feedback from a wide variety of sources on whether to remake [CO 11/272] or allow it to sunset.
- 29 The feedback from industry stakeholders confirmed that [CO 11/272] had been operating efficiently and effectively, and that ASIC should remake [CO 11/272] incorporating an extension of the relief to agent lenders (discussed at paragraphs 13–27).
- 30 Industry stakeholders suggested a minor amendment to the definition of 'masters securities agreement' in [CO 11/272]. We did not receive any feedback that [CO 11/272] required significant technical amendment (although we note that industry stakeholders would have been in favour of even broader relief).

ASIC's response

We have remade [CO 11/272] as [ASIC Instrument 2021/821](#) with the requested amendment to the definition of 'masters securities agreement'. We have also included the extension of relief discussed at paragraphs 13–27.

Appendix: List of non-confidential respondents to CP 319

- Australian Financial Markets Authority (AFMA)
- Australian Shareholders' Association (ASA)