ASIC
Australian Securities & Investments Commission

CONSULTATION PAPER 228

Collective action by investors: Update to RG 128

February 2015

About this paper

This consultation paper seeks feedback from institutional investors, companies, listed managed investment schemes and other interested parties on our proposal to update our guidance in Regulatory Guide 128 *Collective action by institutional investors* (RG 128). A draft updated version of RG 128 is available on our website at www.asic.gov.au/cp under CP 228.

We are also consulting on our proposal to discontinue the relief in Class Order [CO 00/455] *Collective action by institutional investors.* We do not propose to replace it with a new class order.

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.

Document history

This paper was issued on February 2015 and is based on the Corporations Act as at the date of issue.

Disclaimer

The proposals, explanations and examples in this paper do not constitute legal advice. They are also at a preliminary stage only. Our conclusions and views may change as a result of the comments we receive or as other circumstances change.

Contents

The consultation process

You are invited to comment on the proposals in this paper, which are only an indication of the approach we may take and are not our final policy.

As well as responding to the specific proposals and questions, we also ask you to describe any alternative approaches you think would achieve our objectives.

We are keen to fully understand and assess the financial and other impacts of our proposals and any alternative approaches. Therefore, we ask you to comment on:

- the likely compliance costs;
- the likely effect on competition; and
- other impacts, costs and benefits.

Where possible, we are seeking both quantitative and qualitative information.

We are also keen to hear from you on any other issues you consider important.

Your comments will help us finalise our guidance on collective action by institutional investors. In particular, any information about compliance costs, impacts on competition and other impacts, costs and benefits will be taken into account if we prepare a Regulation Impact Statement: see Section C, 'Regulatory and financial impact'.

Making a submission

You may choose to remain anonymous or use an alias when making a submission. However, if you do remain anonymous we will not be able to contact you to discuss your submission should we need to.

Please note we will not treat your submission as confidential unless you specifically request that we treat the whole or part of it (such as any personal or financial information) as confidential.

Please refer to our privacy policy at www.asic.gov.au/privacy for more information about how we handle personal information, your rights to seek access to and correct personal information, and your right to complain about breaches of privacy by ASIC.

Comments should be sent by 20 April 2015 to:

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What will happen next?

Stage 1	17 February 2015	ASIC consultation paper released
Stage 2	20 April 2015	Comments due on the consultation paper
Stage 3	June–July 2015	Updated regulatory guide released

A Background

Key points

We recognise the importance of investor engagement in maintaining good corporate governance, including through collective action. However, this must be balanced against the need to avoid control over an entity being acquired inappropriately.

Since Regulatory Guide 128 *Collective action by institutional investors* (RG 128) was released in 1998, modes of investor engagement have changed and a number of international jurisdictions have published guidance on investor engagement.

We are proposing to update the guidance in RG 128 so that it provides useful information on the circumstances in which investors can act collectively.

Collective action by investors

1 We recognise the importance of investor engagement in maintaining good corporate governance, including through collective action. Effective engagement can enhance the long-term performance and corporate value of an entity for all investors. However, facilitation of the ability of investors to engage effectively with entities needs to be balanced against the principles underlying the takeover and substantial holding provisions of the *Corporations Act 2001* (Corporations Act), which aim to avoid control over an entity being acquired inappropriately.

2 Following industry consultation in 1996, we released RG 128 and issued relief (in the form of Superseded Class Order [SCO 98/649] *Collective action by institutional investors*, which was superseded by Class Order [CO 00/455] *Collective action by institutional investors*) to facilitate collective action by institutional investors in settings that would not compromise the principles underlying Ch 6 of the Corporations Act.

3 Currently, RG 128 sets out:

(a) our legal view about when institutional investors can collectively discuss their intentions about voting at a meeting of a company in which they hold shares without becoming associates or entering into a relevant agreement for the purposes of Ch 6; and

(b) limited class order relief to facilitate two or more institutional investors entering an agreement to vote at a meeting of that company.

4 Under the *Legislative Instruments Act 2003*, legislative instruments cease automatically, or ‘sunset’, after 10 years, unless action is taken to exempt or

preserve them. [CO 00/455] is due to sunset on 1 October 2016. ASIC needs to remake the class order if it is to continue in effect from that date.

5 Recent feedback received by ASIC indicates that modes of investor engagement have now changed and the relief in [CO 00/455] is very rarely relied on. As far as we are aware, the class order relief has only been relied on once (in 1998, on [SCO 98/649]).

6 In addition, to provide clarity, a number of international jurisdictions have recently published guidance on investor engagement and the forms of coordination or agreements that do or do not constitute acting in concert in the context of takeover rules.[1]

7 Both internationally and within Australia, in recent years there has been both a general appreciation that investor engagement can be positive for the financial market and concern about control-seeking behaviour of 'shareholder activists'.

8 The purpose of this consultation is to review the guidance in RG 128 so that it strikes the appropriate balance between facilitating investor engagement and maintaining the spirit of Ch 6, given changes in engagement practices and international developments.

[1] See, for example, European Securities and Markets Authority, *Information on shareholder cooperation and acting in concert under the Takeover Bids Directive—1st update* (ESMA/2014/677), public statement, 20 June 2014 and UK Takeover Panel, Practice Statement No. 26 *Shareholder activism*, practice statement, 9 September 2009.

B Our proposals

Key points

Our proposed revisions to RG 128 provide updated guidance on how the takeovers and substantial holding notice provisions apply to collective action by investors. The draft guidance also aims to provide more clarity about when we will consider that collective action may constitute unacceptable circumstances despite not contravening the Corporations Act.

We are proposing to include in our update to RG 128 an overview of other legal considerations under the Corporations Act that can also arise in relation to investor engagement.

We are also proposing to discontinue the relief in [CO 00/455], as we have found it has been very rarely used. We do not propose to replace it with a new class order.

Updates to RG 128

Proposal

B1 We propose to update RG 128 to provide revised guidance on how the takeovers and substantial holding notice provisions apply to collective action by investors.

Feedback

B1Q1 Do you agree with the approach we have taken? If you think that there is a preferable way of setting out our guidance, please suggest alternatives.

B2 We propose to provide illustrative examples of conduct where collective action is unlikely (Table 1 of the draft updated RG 128) or more likely (Table 2 of the draft updated RG 128) to trigger an associate relationship or constitute entering into a relevant agreement resulting in the acquisition of a relevant interest.

Feedback

B2Q1 Do you think that providing the illustrative examples in Table 1 and Table 2 of draft updated RG 128 is useful?

B2Q2 Do you agree with our inclusions and analysis in Table 1 and Table 2? Are there any other matters of practical guidance that should be included? Are there any matters that you think should be deleted? If so, please describe these matters and explain why you think they should be included or deleted.

B3 We propose to provide guidance on our approach to enforcement of the takeover and substantial holding provisions and taking action for unacceptable circumstances in the context of investor engagement: see draft updated RG 128.47–RG 128.52.

Feedback

B3Q1 Do you find our proposed guidance useful? If not, why not?

B4 We propose to provide an overview of other legal considerations under the Corporations Act that can also arise in relation to investor engagement: see Section C of the draft updated RG 128.

Feedback

B4Q1 Do you find the overview provided in Section C of the draft updated RG 128 useful?

B5 We propose to use the term 'collective action' to refer very broadly to a range of behaviour, including behaviour that is little more than investors being in contact with each other. This is consistent with the terminology in our existing RG 128.

Feedback

B5Q1 Do you think that the term 'collective action' is understood in this broad sense by relevant users of this guide, or should we use terminology that has less of an implication that investors will be acting together for a common purpose? If the latter, what would be a better term or phrase to use?

Rationale

9 RG 128 was released in 1998. Since then, modes of investor engagement have changed and a number of international jurisdictions have published guidance on shareholder engagement. We are proposing to update the guidance in RG 128, both in relation to the relevant legal provisions and to take into account developments in engagement and corporate governance practices.

10 We recognise the importance of investor engagement in maintaining good corporate governance and that institutional investors may wish to engage with companies in a variety of ways and on a variety of different issues. However, this must be balanced against the need to avoid control over an entity being acquired inappropriately.

11 To help investors and entities understand our approach, we have set out in the draft updated RG 128 examples of conduct that we consider unlikely or more likely to trigger the takeover and/or substantial holding provisions.

12 We have also provided some discussion about factors that we might consider in deciding whether to review conduct and take enforcement action.

13 We also recognise that investor engagement raises a number of regulatory issues for both investors and the entities they are engaging with, in addition to the takeover and substantial holding provisions. We have provided an overview of those arising under the Corporations Act in Section C of the draft updated RG 128.

Revocation of [CO 00/455]

Proposal

B6 We propose to revoke the class order relief in [CO 00/455] because it appears that it is very rarely being used. Informal feedback received by ASIC suggests that institutional investors are not choosing to rely on the relief in the class order because:

(a) institutional investors rarely seek to engage with companies at the meeting itself. Relevant investor engagement is usually done prior to or outside of meetings; and

(b) the condition imposed in the class order to disclose details of the voting agreement to ASX is unpalatable.

Feedback

B6Q1 Do you agree with our proposed revocation of [CO 00/455]? If not, why not?

B6Q2 Have you relied on the class order relief in [CO 00/455]? If yes, how often have you relied on the relief?

B6Q3 Do you agree that institutional investors are reluctant to rely on the class order due to the reasons set out above?

B6Q4 Are there any other reasons why institutional investors may be reluctant to rely on [CO 00/455]? For example, do you believe that institutional investors prefer to engage individually?

Rationale

14 [CO 00/455] grants relief from s606 and the substantial holding provisions to certain institutional investors that have entered into an agreement about voting at a meeting of a company in which the investors have voting power (by providing that those investors will not become associates or gain a relevant interest purely as a result of entering into the agreement). The relief applies from the time the agreement is entered into until the end of the meeting.

15 Specific conditions apply to the relief:

(a) The relief is restricted to institutional investors that pool the funds of persons to whom the body corporate owes a fiduciary duty or a contractual duty under a life policy, and that invest the funds in a

registered scheme, superannuation fund or statutory fund of a life insurance company.

(b) The substantial holding relief only relates to changes purely caused by the voting agreement, and the institutional investors must report other changes to their holdings (individually and collectively).

(c) The parties to the agreement must make an announcement to ASX at least seven days before the meeting and, if the company is listed, must make the announcement before 9.30 am the day after the voting agreement was entered into. The announcement must list the names of the institutional investors, the company the subject of the voting agreement, the date of the meeting, the matter to be voted on, the objective of the action, how the investors propose to vote and the relevant interest held by each investor and collectively.

(d) There must be no consideration passing between the parties to the agreement.

(e) The institutional investors cannot be collectively entitled to 20% or more of the voting shares in the relevant company as principal.

(f) The agreement must:

(i) relate to voting in a particular way or abstaining from voting at a specified meeting;

(ii) be terminable by any party to the agreement at will; and

(iii) terminate at the close of the meeting.

16 Informal feedback received from industry suggests the reason the relief is very rarely used is that the conditions imposed by the class order are unpalatable, and also because engagement practices now more typically take place outside the context of a meeting.

New potential relief

Proposal

B7 We propose to not replace the class order relief in [CO 00/455] with another class order.

Feedback

B7Q1 Do you consider any other ASIC class order relief would be desirable (either similar to [CO 00/455] or otherwise)? If so, please specify the possible scope and terms of such relief. For example, if class order relief for investors to collectively raise matters of corporate governance with the entity is desirable, how would ‘corporate governance’ be defined in the class order and on what terms would that relief be granted?

B7Q2 Are there other steps we could take to facilitate investor engagement?

B8 We propose to indicate that we may grant individual relief where the nature of the conduct is not concerned with the acquisition of a substantial interest in or control over an entity: see draft updated RG 128.53–RG 128.55. Any relief granted is likely to require disclosure to the market.

Feedback

B8Q1 Do you agree with our proposal? If not, why not?

B8Q2 Are there any circumstances under which institutional investors are likely to apply for individual relief to facilitate collective action? If so, please outline these circumstances. What conditions of relief would be appropriate in these circumstances?

B8Q3 In what ways (if any) do engagement practices of members of managed investment schemes differ from that of shareholders of companies?

Rationale

17 We have reviewed our internal records, and applications for individual relief in relation to investor engagement about governance issues appear very rare. Discussions with key stakeholders have also suggested that it is unlikely that there is a desire for significant relief. In addition, we see some practical issues with obtaining all the information we would need to provide relief in a timely way.

18 For this reason we do not consider it necessary to issue a replacement class order or to discuss in detail other potential relief we may give in our updated RG 128. Of course, if an individual application was made regarding collective action, we would decide that matter on its merits.

19 We note that it is very rare for ASIC to give relief from requiring substantial holding notice disclosure to the market, although we have given relief to amend the terms of particular disclosures in substantial holding notices.

C Regulatory and financial impact

20 In developing the proposals in this paper, we have carefully considered their regulatory and financial impact. On the information currently available to us we think they will strike an appropriate balance between:

(a) the ability of investors to engage effectively with entities; and

(b) the principles underlying the takeover and substantial holding provisions of the Corporations Act, as set out in s602(a).

21 Before settling on a final policy, we will comply with the Australian Government's regulatory impact analysis (RIA) requirements by:

(a) considering all feasible options, including examining the likely impacts of the range of alternative options which could meet our policy objectives;

(b) if regulatory options are under consideration, notifying the Office of Best Practice Regulation (OBPR); and

(c) if our proposed option has more than minor or machinery impact on business or the not-for-profit sector, preparing a Regulation Impact Statement (RIS).

22 All RISs are submitted to the OBPR for approval before we make any final decision. Without an approved RIS, ASIC is unable to give relief or make any other form of regulation, including issuing a regulatory guide that contains regulation.

23 To ensure that we are in a position to properly complete any required RIS, please give us as much information as you can about our proposals or any alternative approaches, including:

(a) the likely compliance costs;

(b) the likely effect on competition; and

(c) other impacts, costs and benefits.

See 'The consultation process', p. 4.

List of proposals and questions

Proposal		Your feedback	
B1	We propose to update RG 128 to provide revised guidance on how the takeovers and substantial holding notice provisions apply to collective action by investors.	B1Q1	Do you agree with the approach we have taken? If you think that there is a preferable way of setting out our guidance, please suggest alternatives.
B2	We propose to provide illustrative examples of conduct where collective action is unlikely (Table 1 of the draft updated RG 128) or more likely (Table 2 of the draft updated RG 128) to trigger an associate relationship or constitute entering into a relevant agreement resulting in the acquisition of a relevant interest.	B2Q1	Do you think that providing the illustrative examples in Table 1 and Table 2 of draft updated RG 128 is useful?
		B2Q2	Do you agree with our inclusions and analysis in Table 1 and Table 2? Are there any other matters of practical guidance that should be included? Are there any matters that you think should be deleted? If so, please describe these matters and explain why you think they should be included or deleted.
B3	We propose to provide guidance on our approach to enforcement of the takeover and substantial holding provisions and taking action for unacceptable circumstances in the context of investor engagement: see draft updated RG 128.47–RG 128.52.	B3Q1	Do you find our proposed guidance useful? If not, why not?
B4	We propose to provide an overview of other legal considerations under the Corporations Act that can also arise in relation to investor engagement: see Section C of the draft updated RG 128.	B4Q1	Do you find the overview provided in Section C of the draft updated RG 128 useful?
B5	We propose to use the term ‘collective action’ to refer very broadly to a range of behaviour, including behaviour that is little more than investors being in contact with each other. This is consistent with the terminology in our existing RG 128.	B5Q1	Do you think that the term ‘collective action’ is understood in this broad sense by relevant users of this guide, or should we use terminology that has less of an implication that investors will be acting together for a common purpose? If the latter, what would be a better term or phrase to use?

Proposal	Your feedback
B6 We propose to revoke the class order relief in [CO 00/455] because it appears that it is very rarely being used. Informal feedback received by ASIC suggests that institutional investors are not choosing to rely on the relief in the class order because: (a) institutional investors rarely seek to engage with companies at the meeting itself. Relevant investor engagement is usually done prior to or outside of meetings; and (b) the condition imposed in the class order to disclose details of the voting agreement to ASX is unpalatable.	B6Q1 Do you agree with our proposed revocation of [CO 00/455]? If not, why not? B6Q2 Have you relied on the class order relief in [CO 00/455]? If yes, how often have you relied on the relief? B6Q3 Do you agree that institutional investors are reluctant to rely on the class order due to the reasons set out above? B6Q4 Are there any other reasons why institutional investors may be reluctant to rely on [CO 00/455]? For example, do you believe that institutional investors prefer to engage individually?
B7 We propose to not replace the class order relief in [CO 00/455] with another class order.	B7Q1 Do you consider any other ASIC class order relief would be desirable (either similar to [CO 00/455] or otherwise)? If so, please specify the possible scope and terms of such relief. For example, if class order relief for investors to collectively raise matters of corporate governance with the entity is desirable, how would 'corporate governance' be defined in the class order and on what terms would that relief be granted? B7Q2 Are there other steps we could take to facilitate investor engagement?
B8 We propose to indicate that we may grant individual relief where the nature of the conduct is not concerned with the acquisition of a substantial interest in or control over an entity: see draft updated RG 128.53–RG 128.55. Any relief granted is likely to require disclosure to the market.	B8Q1 Do you agree with our proposal? If not, why not? B8Q2 Are there any circumstances under which institutional investors are likely to apply for individual relief to facilitate collective action? If so, please outline these circumstances. What conditions of relief would be appropriate in these circumstances? B8Q3 In what ways (if any) do engagement practices of members of managed investment schemes differ from that of shareholders of companies?