CONSULTATION PAPER 319

Securities lending by agents and substantial holding disclosure

July 2019

About this paper

We are seeking to improve substantial holding disclosure by agents involved in securities lending (agent lenders).

This paper explains how the concept of relevant interest in s608 and 609 of the Corporations Act applies to agent lending and the substantial holding disclosure requirements in s671B.

We are seeking feedback on whether we should give relief to agent lenders that is consistent with our policy in Regulatory Guide 222 *Substantial holding disclosure: Securities lending and prime broking* and the relief provided under Class Order [CO 11/272].

> Note: We are proposing to replace [CO 11/272] with a legislative instrument that includes all the relief currently in [CO 11/272] plus our proposed relief for agent lenders. The draft instrument is available on our website at www.asic.gov.au/cp under CP 319.

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 29 July 2019 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 develop our policy on substantial holding disclosure by agent lenders. 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 Monday, 9 September 2019 to:

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What will happen next?

Stage 1	29 July 2019	ASIC consultation paper released
Stage 2	9 September 2019	Comments due on the consultation paper
Stage 3	December 2019	Consultation response and legislative instrument made

A Background to the proposals

Key points

Our legislative relief in Class Order [CO 11/272] and our guidance in Regulatory Guide 222 *Substantial holding disclosure: Securities lending and prime broking* (RG 222) is currently focused on substantial holding disclosure by prime brokers.

In this paper, we are proposing to grant similar relief to intermediaries that act as agents in securities lending transactions (agent lenders)—to make substantial holding disclosure more practical and meaningful.

Substantial holding disclosure by prime brokers

1 'Securities lending' is a term used to describe a market transaction where securities are transferred from the owner (the lender) to another party (the borrower). The borrower is obliged to return the securities or equivalent securities to the lender either on demand or at the end of the loan term.

2 This type of transaction will usually result in both the lender and the borrower having a relevant interest in securities under s608 of the *Corporations Act 2001* (Corporations Act), which may trigger obligations to disclose a substantial holding in a listed entity or a change in substantial holding under s671B.

3 Disclosure of substantial holdings acquired through securities lending is important for an efficient, competitive and informed market in quoted securities because, as set out in RG 222 at RG 222.9:

(a) disclosure achieves transparency about the volume of a company's securities that are subject to these activities;

(b) relevant interests acquired through securities lending or prime broking may affect the control of a company;

(c) without appropriate disclosure, there is a risk that the market will be misled about the ownership and control of listed entities, particularly when a significant proportion of the entity's securities are subject to securities lending; and

(d) disclosure achieves transparency about the volume of securities that may be thought to be 'locked up' in investment funds but are actually at large in the market.

Previous consultation on securities lending

4 In July 2009, we published Consultation Paper 107 *Securities lending and substantial holding disclosure* (CP 107). This was due to differing interpretations of how the relevant interest provisions apply to intermediaries involved in securities lending and different practices for compliance with substantial holding disclosure under s671B.

5 CP 107 explained how the relevant interest provisions apply to prime brokers who engage in securities lending. We also consulted on improving substantial holding disclosure for prime brokers.

Guidance and legislative relief for prime brokers

6 Following submissions in response to CP 107 and further consultation with the market, we provided:

(a) legislative relief for the purposes of Pt 6C.1 in relation to s608, 609 and 671B for securities lending (see [CO 11/272]); and

(b) guidance in RG 222.

7 [CO 11/272] and RG 222 focus on securities lending undertaken by prime brokers. Prime broking is a commercial term for a package of services offered by an investment bank to professional clients. It typically includes custodial services, execution, financing and securities lending: see RG 222 at RG 222.47. Prime brokers generally have a non-exclusive right to borrow a client's securities under a securities lending arrangement. If a prime broker borrows a client's securities, it generally does so as principal.

8 The right to borrow securities gives a person a relevant interest in those securities: see s608(1)(c). This would ordinarily mean that:

(a) a prime broker acquires a relevant interest in the client's securities from the time it first enters into a prime broking agreement with the client (see RG 222 at RG 222.52);

(b) the prime broker's relevant interest does not change when it exercises its borrowing rights and borrows the client's securities as principal (only the way the relevant interest arises changes); and

(c) no fresh substantial holding notice is required when the prime broker borrows the securities (see RG 222 at RG 222.58).

9 [CO 11/272] aims to make substantial holding disclosure for prime brokers more meaningful by deferring a prime broker's relevant interest arising from its borrowing rights under a prime broking agreement to the time at which the prime broker exercises that borrowing right. This aligns any substantial holding notification with the timing of changes in control of the securities: see RG 222 at RG 222.60.

Substantial holding disclosure by agent lenders

10 Following the release of RG 222, we have received applications for relief in relation to substantial holding disclosure from intermediaries that act as agents in securities lending transactions. We have granted individual relief to one agent lender on the terms proposed in this paper and, due to subsequent applications, we are now proposing to grant legislative relief.

11 We understand that agent lenders negotiate and settle securities lending transactions with third party borrowers on behalf of their clients. An agent lender does not generally have a right to borrow the client's securities (although it may do so) and, unlike a prime broker, it is not party to the securities lending transaction as principal.

12 The agent lending agreement (termed 'authorisation agreement' in this paper) will set the client's parameters on:

(a) the type of securities that can be lent (lending pool securities);

(b) the type of entities that can borrow the securities (i.e. exposure and credit limits);

(c) the acceptable collateral; and

(d) how and when securities lending transactions can be terminated.

13 Authorisation agreements contain detailed provisions for the agent lender to act on client instructions. We understand that many of the agent lender's functions are exercised automatically via computer programs (e.g. to match lending pool securities with borrow requests from acceptable counterparties). However, an agent lender also usually has broad discretion over various matters relating to securities lending. For example, it usually has an unfettered discretion to terminate a loan without prior notice to the client.

Relevant interests and agent lending

14 There is detailed guidance in RG 222 on how the relevant interest provisions in s608 and 609 generally apply to prime broking arrangements and securities lending: see RG 222 at RG 222.51–RG 222.56. Section 608 applies to prime brokers and agent lenders in a similar way (despite a prime broker having a right to borrow its clients' securities and doing so as principal). This is because:

(a) s608(1) is drafted in broad terms and expressly states that it does not matter how remote a relevant interest is or how it arises and that, if two or more people can jointly exercise one of the powers, each of them is taken to have that power;

(b) s608(2) extends the application of s608(1) by saying that 'power or control' over voting or disposal includes power or control that is

indirect and power or control that is subject to restraint or restriction; and

(c) s608(8) accelerates the acquisition of a relevant interest when a person has been given future rights over securities.

15 Section 609 does not contain any exception that would apply to agent lenders. In particular, we do not consider the bare trustee exception in s609(2), which can be relied on by custodians in their trustee capacity, applies to intermediaries that have discretion like agent lenders.

16 An authorisation agreement of the type outlined in paragraphs 12–13 will therefore result in the agent lender acquiring a relevant interest in the lending pool securities (i.e. the securities within the parameters suitable for loan) at the time of entry into an authorisation agreement with the client (and when the client acquires further securities that are added to the lending pool). This is because the agent lender has power to exercise control over the disposal of the lending pool securities. The client will also have a relevant interest in the lending pool securities.

17 If the agent lender has discretion to terminate loans under the authorisation agreement, it will also have a relevant interest in:

(a) the securities that have been loaned to a borrower under the authorisation agreement (loaned securities);

(b) any securities delivered by the borrower as collateral (collateral securities); and

(c) any securities purchased with cash collateral provided by the borrower (purchased securities).

18 This is because termination of the securities loan will result in recall of the loaned securities for the client and return of the collateral securities to the borrower. The agent lender would also ordinarily be authorised to sell any purchased securities in order to return cash collateral to the borrower.

Substantial holding and agent lending

19 Section 671B requires a person to give an initial substantial holding notice to the listed entity and market operator when they and their associates have a ‘relevant interest’ in voting shares or interests carrying 5% or more of the total votes in a listed entity. The substantial holder is then required to give a notice if there is a change of 1% or more in its holding.

20 Section 671B requires an agent lender to aggregate its own direct relevant interest in securities (i.e. relevant interests arising because it holds the securities) with the relevant interest it has in its clients’ securities through agency and other intermediary agreements. The agent also needs to take into account the relevant interests of associates.

21 We consider that compliance with s671B is important for all intermediaries involved in securities lending, whether they act as principal to the transaction or as an agent with active discretions. In particular, it is important for the market to know if an intermediary has the right to influence the disposal of a substantial volume of a listed entity's securities.

22 It appears that agent lenders, which frequently include custodians, are taking different approaches to compliance with s671B, and that some may be relying entirely on the 'bare trustee' exception in s609(2), both in relation to relevant interests:

(a) in securities held in custody; and

(b) arising through authorisation agreements.

Proposed legislative relief for agent lenders

23 In this paper, we are proposing to provide legislative relief for agent lenders to make substantial holding disclosure more practical and meaningful. We are seeking feedback on a proposal to grant relief to agent lenders that is consistent with the type of relief that [CO 11/272] provides for prime brokers and principal lenders.

24 We are proposing to replace [CO 11/272] with a legislative instrument that includes all the relief currently in [CO 11/272] plus our proposed relief for agent lenders. The full text of the proposed instrument is attached to this paper (available on our website at www.asic.gov.au/cp under CP 319). Our proposed relief for agent lenders is identified in the draft instrument as blue text that is underlined.

25 We are also seeking feedback on granting a broader exemption for agent lenders, although currently this is not our proposed form of relief.

Guidance and future monitoring of compliance

26 We will provide guidance in RG 222 for agent lenders on compliance with Ch 6C of the Corporations Act, as modified by the terms of any legislative relief.

27 Following legislative relief and guidance, we plan to conduct surveillance on compliance with Ch 6C by agent lenders. As noted in RG 222 at RG 222.18, persons who fail to comply with s671B commit an offence of strict liability and may be liable to compensate investors for any loss suffered from the contravention.

B Proposed relief for agent lenders

Key points

Consistent with [CO 11/272], we are proposing to:

- modify s609 for the purposes of the substantial holding provisions to defer the time when an agent lender acquires a relevant interest in securities under authorisation agreements;
- modify s608 for the purposes of the substantial holding provisions so that an agent lender retains a relevant interest in loaned securities if its client does so; and
- modify s671B so that an agent lender can provide key details of its agent lending agreement, rather than attach the agreement.

We are not proposing to grant a broader exemption for agent lenders because we consider they are analogous to prime brokers for substantial holding disclosure purposes.

We are also seeking feedback on how agent lenders currently comply with diverse international disclosure obligations.

Deferring relevant interest until lending authorisation is exercised

Proposal

B1 For substantial holding disclosure purposes under Pt 6C.1, we propose to:

(a) modify s609 so that an agent lender does not acquire a relevant interest in lending pool securities at the time of entry into an authorisation agreement, but instead defer the time at which the agent lender acquires a relevant interest to the time at which the agent actually exercises its lending authority in respect of securities; and

(b) make this 'deferral relief' conditional on:

(i) the owner lender (referred to as the 'client') having unrestricted rights to deal in the lending pool securities; and

(ii) the agent's lending authority arising in the ordinary course of business.

See proposed s609(10C) in the draft legislative instrument attached to this paper.

Your feedback

B1Q1 Do you have any comments on the terms of the deferral relief in proposed s609(10C)?

B1Q2 Will the proposed deferral relief make substantial holding disclosure more practical for agent lenders?

B1Q3 Will the proposed deferral relief deprive the market of useful information about an agent's relevant interest in lending pool securities?

B1Q4 Will proposed s609(10C) cover most agent lending arrangements? If not, please explain why not and what type of agent lending arrangements will not be covered.

B1Q5 Proposed s609(10C) refers to the agent providing services to the lender 'as part of carrying on a custodial business'. Does the definition of 'custodial business' in proposed s609(10E) adequately describe the business of agent lenders? If not, please explain why not.

B1Q6 Our proposed relief (including proposed s609(10C) and 671B(4B)) uses the term 'authorisation agreement', which is defined in proposed s671B(4C). Will our proposed definition of authorisation agreement cover most agreements used by agent lenders? If not, please explain how the definition should be amended.

Rationale

28 As explained at paragraph 16, without deferral relief, an agent lender will acquire a relevant interest in its client's lending pool securities at the time it enters into an authorisation agreement. The agent lender's relevant interests do not change if it exercises rights under the authorisation agreement to arrange a securities loan. This can result in the agent lender needing to give a substantial holding notice over all the lending pool securities when it enters into an authorisation agreement, but not when it exercises rights over specific securities under that agreement.

29 Our proposed relief would remove the agent's relevant interest in lending pool securities arising at the time of entering into an authorisation agreement for the purposes of substantial holding disclosure. The agent lender would instead acquire a relevant interest in securities when it exercises its lending authority under the authorisation agreement and settles a securities lending transaction with a borrower.

30 In this way, proposed s609(10C) will align the timing of any required substantial holding notification with the time the agent lender exercises its lending authority.

31 The proposed relief is similar to notional s609(10A) inserted by [CO 11/272] and will ensure the relevant interest regime applies to securities lending intermediaries in a consistent way. Neither notional s609(10A) nor proposed s609(10C) affect an intermediary's relevant interests for the purposes of Ch 6 and the takeovers limit in s606.

Retention of relevant interest when securities on-lent

Proposal

B2 For substantial holding disclosure purposes, we propose to modify s608 so that an agent lender retains a relevant interest in loaned securities when the client retains a relevant interest due to notional s608(8A): see proposed s608(8B) in the draft instrument attached to this paper.

Your feedback

B2Q1 Do you have any comments on our proposal to modify s608 so that an agent lender retains a relevant interest in loaned securities when its client retains a relevant interest due to notional s608(8A)?

B2Q2 Will this make substantial holding disclosure more practical for an agent lender?

Rationale

32 Ordinarily, a lender would lose its relevant interest in loaned securities if the borrower disposes of them, even though the lender retains a right to recall equivalent securities. Further, a lender may have difficulty reporting its relevant interest in loaned securities because it does not know how the borrower has dealt with them.

33 Notional s608(8A) inserted by [CO 11/272] modifies s608 for the purposes of Pt 6C.1 so that a lender's relevant interest in loaned securities is not affected by the borrower's subsequent actions. The relief recognises the lender's right of recall of equivalent securities and the fact that it often does not know what the borrower does with loaned securities after transfer from the lender: see RG 222 at RG 222.34–RG 222.37. For these reasons, we consider that it would be appropriate to modify s608 so that an agent lender retains a relevant interest in loaned securities for so long as the client has a relevant interest.

Relief from the requirements to disclose consideration and attach agent lending agreements

Proposal

B3 We propose to:

(a) give relief so that a substantial holder does not need to disclose consideration relating to a substantial holding derived from agent lending, which is consistent with our relief for securities lending in notional s671B(3A) inserted by [CO 11/272] (see proposed s671B(3B) in the draft legislative instrument attached to this paper);

(b) give relief from s671B(4) so that an agent lender does not need to attach a copy of its authorisation agreement to the substantial holding notice, which is analogous to notional s671B(4A) inserted by [CO 11/272] (see proposed s671B(4B) in the draft legislative instrument attached to this paper); and

(c) make the relief in proposed s671B(4B) conditional on the substantial holding notice giving disclosure about key terms of the authorisation agreement, such as:

(i) the type of agreement;

(ii) the parties to the agreement;

(iii) the circumstances when the agent lender can exercise its lending authority;

(iv) the circumstances when the agent lender can exercise the right of recall on behalf of its client;

(v) the circumstances when the parties can exercise voting rights; and

(vi) any restrictions on the client's ability to deal with the securities (see proposed s671B(4B)(a)–(c) in the draft legislative instrument attached to this paper).

Feedback

B3Q1 Do you have any comments on our proposal to give agent lenders relief from the need to disclose consideration relating to a substantial holding under proposed s671B(3B)?

B3Q2 Will our proposal to give relief under proposed s671B(4B), so that authorisation agreements do not need to be attached to a substantial holding notice, make compliance with s671B(4) easier?

B3Q3 Is proposed s671B(4B) likely to deprive the market of useful information?

B3Q4 Our proposed relief is conditional on the substantial holder providing ASIC or the listed entity with a copy of the full documentation on request. Is this reasonable?

B3Q5 Unlike other securities lending agreements, we understand there are no standard authorisation agreements for agency arrangements. Should our relief be conditional on the agent lender posting the form of agreement it uses on its website?

Rationale

34 The aim of our proposed relief in relation to the details that need to be disclosed about agent lending is to:

(a) make substantial holding disclosure more practical for agent lenders; and

(b) improve compliance without compromising market transparency.

Relief so that consideration does not need to be disclosed

35 The prescribed form for notification of substantial holdings requires disclosure of 'any and all benefits' relating to the acquisition or disposal of relevant interests. See the notes to:

(a) Form 603 *Notice of initial substantial holder*;

(b) Form 604 *Notice of change of interests of substantial holder*; and

(c) Form 605 *Notice of ceasing to be a substantial holder*.

36 This could extend to fees the agent lender obtains for organising securities loans.

37 We consider it is appropriate to remove any requirement to disclose fees relating to agent lending because:

(a) it may be difficult for an agent lender to assess how much of a fee is referrable to a particular transaction; and

(b) this commercial information is unrelated to the relevant interest provisions.

38 This is consistent with the relief provided for securities lending and prime broking by notional s671B(3A).

Relief so that agreements do not need to be attached to notices

39 We have granted relief from the content requirements of s671B(4) for intermediaries that act as a principal in securities lending so that they do not need to attach a copy of the securities lending master agreements: see notional s671B(4A).

40 Our deferral relief for prime brokers means that disclosure of any substantial holding arising from the exercise of the borrowing right would occur after the actual borrowing and this in turn means the prime broking agreement does not need to be attached to the substantial holder notice. Due to notional s671B(4A), a summary of the securities lending transaction needs to be attached: see RG 222 at RG 222.70–RG 222.75.

41 Our rationale for granting relief from s671B(4) for principal lenders also applies to agent lenders. Authorisation agreements are lengthy, complex documents and many of the terms are not relevant to the agent lender's interest in loaned securities or collateral securities. As with other intermediaries, agent lenders may be party to a number of these agreements with different clients and may enter into many transactions within a short period of time.

Scope of our proposed exemption

Issue

B4 We do not propose to grant agent lenders an exemption from s608 or 671B for:

(a) securities that have been loaned under the agent lender's lending authorisation (loaned securities);

(b) securities delivered by a borrower as collateral for securities lending (collateral securities); or

(c) securities purchased (purchased securities) with cash collateral delivered by the borrower.

Your feedback

B4Q1 Do you consider that we should give a broader exemption from s608 so that an agent lender does not acquire a relevant interest in any securities under authorisation agreements? Please address the issues set out in paragraphs 43–44 and in Table 1.

B4Q2 Do you consider that we should grant an exemption from s671B for loaned securities and collateral securities so that agent lenders are still subject to s606 for these securities, but do not need to disclose substantial holdings?

B4Q3 Would an exemption from s671B for these securities deprive the market of useful information about agent lenders' substantial holdings?

Rationale

42 Some intermediaries have suggested that agent lenders should have a complete exemption from s608 for any relevant interest they acquire through agent lending on standard terms, or at least an exemption from s671B. This is on the basis that agent lenders have a remote form of relevant interest in these securities.

43 We do not currently consider it would be appropriate to grant agent lenders an exemption from s608 for loaned securities and collateral securities if agent lenders have a broad discretion over these securities that is not expressly limited. An exemption from s608 would allow an agent lender to have power over the disposal of 20% or more of a listed entity's voting securities.

44 Similarly, we consider an exemption from s671B would undermine the substantial holding provisions and the principle in s602(a) that the acquisition of control of listed entities takes place in an informed market.

45 Table 1 summarises some arguments in favour of a broad exemption and our response in more detail.

Table 1: Arguments for and against a broad exemption

Reasons for a broad exemption	Our response
Agent lenders do not enter into agent lending arrangements, or use their lending authority, to influence or gain control of listed entities.	Section 608 is based on powers that a person has over the voting or disposal of securities, not the person's intentions. Similarly, s671B is important for market integrity in a broad sense and not solely for the control of listed entities.
Agent lenders only have a remote interest in securities that are the subject of agent lending transactions. They do not have voting rights over any of these securities.	The relevant interest provisions are intended to have a broad application, as evidenced by the drafting of s608 and the narrow exceptions available in s609. For this reason, we rarely grant an exemption from s608.
An agent lender's discretion to act without client instructions is restricted by: • the general law of agents and fiduciaries; and • Australian financial services (AFS) licensee obligations, such as the requirement to manage conflicts of interest and act fairly. In the rare circumstances when an agent lender does act without instructions to terminate a securities loan, it only does so in the client's best interests.	Section 609 only exempts bare trustees. Other trustees who owe a fiduciary duty to beneficiaries are not exempt from the relevant interest provisions. This shows that fiduciary obligations are not a sufficient reason to grant a broad exemption. Similarly, other intermediaries involved in securities lending are subject to AFS licensee obligations, but do not have an exemption from the relevant interest provisions under s609 or ASIC legislative relief.
Although an agent lender may have the right to terminate securities loans without instructions, this is intended as a backstop to protect client interests when instructions cannot be obtained. It is rarely used in practice. Further, an agent lender is motivated to give effect to client instructions whenever possible. An agent lender would not recall loaned securities without good reason because it would lose revenue from the loan being terminated early and there is a risk of alienating the client.	We consider it is appropriate to assess legislative relief based on a person's legal rights, rather than representations as to how those rights are exercised in practice. The exercise of legal rights can be inconsistent across industry participants and can change over time. Based on the authorisation agreements we have reviewed, an agent lender's discretion over loaned securities and collateral securities (i.e. to terminate securities loans) is broad and not subject to restrictions.
Substantial holding disclosure by agent lenders is not useful for the market. An exemption from s671B would remove any duplication of reporting (given the client and borrower may also need to disclose).	Substantial holding disclosure by agent lenders and other intermediaries can be important, especially when a listed entity is subject to a control transaction. An agent lender's substantial holding disclosure will not usually duplicate the client's disclosure (because they have different relevant interests). The nature of the agent lender's interest should be made clear.

Reasons for a broad exemption	Our response
Agent lenders are analogous to other persons who are exempt from s608, either under s609 or ASIC legislative relief, including: (a) investor directed portfolio service (IDPS) operators under ASIC Corporations (IDPS—Relevant Interests) Instrument 2015/1067; (b) bare trustees (see s609(2)); (c) AFS licensees acting on clients' sale instructions (see Class Order [CO 13/520] *Relevant interests, voting power and exceptions to the general prohibition*); (d) warrant trustees (see Class Order [CO 13/526] *Warrants: Relevant interests and associations*); and (e) proxies (see s609(5)).	We consider agent lenders are more analogous to prime brokers for substantial holding disclosure purposes than any of the exemptions and that to grant a broad exemption would be inconsistent with our policy in RG 222. Our responses are: (a) IDPS operators have the power to deal with securities but only on their clients' instructions: see the definition of IDPS in s912AD(42) (as notionally inserted by Class Order [CO 13/763] *Investor directed portfolio services*). (b) Bare trustees merely hold property on behalf of a beneficiary without exercising active discretions. (c) [CO 13/520] provides relief when an AFS licensee receives specific instructions from a client directing the disposal of securities. It does not extend to when the licensee has a right of recall over the securities. (d) Although warrant trustees have discretion to engage in securities lending, [CO 13/526] only applies to quoted warrants over listed securities: see Regulatory Guide 5 *Relevant interests and substantial holding notices* (RG 5) at RG 5.235. Many of the preconditions for relief—such as standardised contracts, disclosure by issuers and anonymous markets—apply only to quoted warrants. In addition, the relief for warrant trustees dates back almost 20 years and preceded ASIC's review of securities lending and substantial holding disclosure in 2009. The quoted warrants market is small, whereas there are many agent lenders. (e) The proxies exemption in s609(5) is limited to voting as proxy for a single shareholder meeting only, and the discretion of the proxy is limited to the resolutions being considered at that meeting.

Compliance with international and other requirements

Issue

B5 Internationally, we understand that disclosure and monitoring obligations for agent lenders differ depending on the jurisdiction. Some jurisdictions have reduced substantial holding disclosure obligations for financial institutions and other eligible investors. Other jurisdictions have a regulatory test that is based on voting rights, which usually means agent lenders have no substantial holding disclosure obligations. However, agent lenders may have significant obligations under other foreign disclosure regimes that require sophisticated monitoring of their holdings.

Your feedback

B5Q1 How do agent lenders comply with diverse international disclosure obligations? For example, do agent lenders need to monitor holdings on a jurisdiction-specific basis to comply with various international requirements?

B5Q2 What systems do agent lenders have for monitoring their holdings and transactions for complying with international regulatory requirements? Can these systems be used for compliance with Ch 6C obligations?

B5Q3 What systems do agent lenders currently have for monitoring their holdings and transactions in Australia:

(a) to comply with substantial holding requirements; or

(b) for other purposes (e.g. compliance with contractual obligations or AFS licence obligations)?

Rationale

46 International requirements for substantial holding disclosure by financial institutions, including securities lending participants, are diverse. This is mostly due to different regulatory frameworks within which disclosure obligations arise, rather than specific disclosure exemptions for securities lending participants, such as agent lenders or prime brokers.

47 We do not consider that international regimes are determinative of ASIC's approach to granting relief from Australian requirements in Ch 6C that arise from the broad relevant interest test in s608. However, we wish to consider how international intermediaries comply with these diverse disclosure obligations.

C Regulatory and financial impact

48 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) ensuring the market has important information on substantial holdings acquired through agent lending; and

(b) facilitating disclosure so that it can be made in a timely and cost effective way.

49 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).

50 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.

51 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.

Key terms

Term	Meaning in this document
agent lender	An intermediary that has entered into an agreement with a client in the ordinary course of the intermediary's business under which the intermediary will arrange securities lending transactions as agent for the client
AFS licence	An Australian financial services licence under s913B of the Corporations Act that authorises a person who carries on a financial services business to provide financial services Note: This is a definition contained in s761A.
AFS licensee	A person who holds an AFS licence under s913B of the Corporations Act
ASIC	Australian Securities and Investments Commission
authorisation agreement	An agreement between an agent lender and a client that authorises the agent to manage securities lending for the client Note: See the more detailed definition in proposed s671B(4C) of the draft instrument attached to this paper.
collateral securities	Securities provided by a borrower to a lender as collateral for a securities lending transaction
Corporations Act	*Corporations Act 2001*, including regulations made for the purposes of that Act
lending pool securities	The client's securities that an agent lender is permitted to lend to borrowers under an authorisation agreement
loaned securities	The securities that an agent lender has lent to a borrower under an authorisation agreement
purchased securities	Securities purchased with cash collateral provided by the borrower
s605 (for example)	A section of the Corporations Act (in this example numbered 605), unless otherwise specified

List of proposals and questions

Proposal	Your feedback
B1 For substantial holding disclosure purposes under Pt 6C.1, we propose to: (a) modify s609 so that an agent lender does not acquire a relevant interest in lending pool securities at the time of entry into an authorisation agreement, but instead defer the time at which the agent lender acquires a relevant interest to the time at which the agent actually exercises its lending authority in respect of securities; and (b) make this 'deferral relief' conditional on: (i) the owner lender (referred to as the 'client') having unrestricted rights to deal in the lending pool securities; and (ii) the agent's lending authority arising in the ordinary course of business. See proposed s609(10C) in the draft legislative instrument attached to this paper.	B1Q1 Do you have any comments on the terms of the deferral relief in proposed s609(10C)? B1Q2 Will the proposed deferral relief make substantial holding disclosure more practical for agent lenders? B1Q3 Will the proposed deferral relief deprive the market of useful information about an agent's relevant interest in lending pool securities? B1Q4 Will proposed s609(10C) cover most agent lending arrangements? If not, please explain why not and what type of agent lending arrangements will not be covered. B1Q5 Proposed s609(10C) refers to the agent providing services to the lender 'as part of carrying on a custodial business'. Does the definition of 'custodial business' in proposed s609(10E) adequately describe the business of agent lenders? If not, please explain why not. B1Q6 Our proposed relief (including proposed s609(10C) and 671B(4B)) uses the term 'authorisation agreement', which is defined in proposed s671B(4C). Will our proposed definition of authorisation agreement cover most agreements used by agent lenders? If not, please explain how the definition should be amended.
B2 For substantial holding disclosure purposes, we propose to modify s608 so that an agent lender retains a relevant interest in loaned securities when the client retains a relevant interest due to notional s608(8A): see proposed s608(8B) in the draft instrument attached to this paper.	B2Q1 Do you have any comments on our proposal to modify s608 so that an agent lender retains a relevant interest in loaned securities when its client retains a relevant interest due to notional s608(8A)? B2Q2 Will this make substantial holding disclosure more practical for an agent lender?

Proposal	Your feedback
B3 We propose to: (a) give relief so that a substantial holder does not need to disclose consideration relating to a substantial holding derived from agent lending, which is consistent with our relief for securities lending in notional s671B(3A) inserted by [CO 11/272] (see proposed s671B(3B) in the draft legislative instrument attached to this paper); (b) give relief from s671B(4) so that an agent lender does not need to attach a copy of its authorisation agreement to the substantial holding notice, which is analogous to notional s671B(4A) inserted by [CO 11/272] (see proposed s671B(4B) in the draft legislative instrument attached to this paper); and (c) make the relief in proposed s671B(4B) conditional on the substantial holding notice giving disclosure about key terms of the authorisation agreement, such as: (i) the type of agreement; (ii) the parties to the agreement; (iii) the circumstances when the agent lender can exercise its lending authority; (iv) the circumstances when the agent lender can exercise the right of recall on behalf of its client; (v) the circumstances when the parties can exercise voting rights; and (vi) any restrictions on the client's ability to deal with the securities (see proposed s671B(4B)(a)–(c) in the draft legislative instrument attached to this paper).	B3Q1 Do you have any comments on our proposal to give agent lenders relief from the need to disclose consideration relating to a substantial holding under proposed s671B(3B)? B3Q2 Will our proposal to give relief under proposed s671B(4B), so that authorisation agreements do not need to be attached to a substantial holding notice, make compliance with s671B(4) easier? B3Q3 Is proposed s671B(4B) likely to deprive the market of useful information? B3Q4 Our proposed relief is conditional on the substantial holder providing ASIC or the listed entity with a copy of the full documentation on request. Is this reasonable? B3Q5 Unlike other securities lending agreements, we understand there are no standard authorisation agreements for agency arrangements. Should our relief be conditional on the agent lender posting the form of agreement it uses on its website?

Proposal	Your feedback
B4 We do not propose to grant agent lenders an exemption from s608 or 671B for: (a) securities that have been loaned under the agent lender's lending authorisation (loaned securities); (b) securities delivered by a borrower as collateral for securities lending (collateral securities); or (c) securities purchased (purchased securities) with cash collateral delivered by the borrower.	B4Q1 Do you consider that we should give a broader exemption from s608 so that an agent lender does not acquire a relevant interest in any securities under authorisation agreements? Please address the issues set out in paragraphs 43–44 and in Table 1. B4Q2 Do you consider that we should grant an exemption from s671B for loaned securities and collateral securities so that agent lenders are still subject to s606 for these securities, but do not need to disclose substantial holdings? B4Q3 Would an exemption from s671B for these securities deprive the market of useful information about agent lenders' substantial holdings?
B5 Internationally, we understand that disclosure and monitoring obligations for agent lenders differ depending on the jurisdiction. Some jurisdictions have reduced substantial holding disclosure obligations for financial institutions and other eligible investors. Other jurisdictions have a regulatory test that is based on voting rights, which usually means agent lenders have no substantial holding disclosure obligations. However, agent lenders may have significant obligations under other foreign disclosure regimes that require sophisticated monitoring of their holdings.	B5Q1 How do agent lenders comply with diverse international disclosure obligations? For example, do agent lenders need to monitor holdings on a jurisdiction-specific basis to comply with various international requirements? B5Q2 What systems do agent lenders have for monitoring their holdings and transactions for complying with international regulatory requirements? Can these systems be used for compliance with Ch 6C obligations? B5Q3 What systems do agent lenders currently have for monitoring their holdings and transactions in Australia: (a) to comply with substantial holding requirements; or (b) for other purposes (e.g. compliance with contractual obligations or AFS licence obligations)?