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Australian Securities and Investments Commission
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By email: stub.equity@asic.gov.au

Dear Mr Demarte

ASIC CP 312 Stub equity in control transactions

The Australian Financial Markets Association (AFMA) is making comment on *Consultation Paper 312 - Stub equity in control transactions* (CP 312). AFMA is concerned with the second surprising proposal regarding offers of securities incorporating mandatory custody or securityholder arrangements. This proposal relates to public company relevant interests in custody arrangements and the exceptions to the general prohibition in section 611, not the proprietary scrip in control transactions provisions on which there has been previous consultation through *18-376MR consultation on measures to restrict offers to retail investors of stub-equity in proprietary companies*. This proposal is a significant modification to statutory law and exercise of administrative power to override Parliament's intention in section 611. It is very different in character to a review of an existing regulatory relief and its termination. Any change to the law by administrative action must be dealt with great caution and deference to Parliament's prerogatives.

AFMA does not agree at this point in time with the proposal to modify Chapter 6 of the Corporations Act by use of administrative power granted under section 655A so that the exceptions in items 1–4 (takeover bids) and 17 (schemes of arrangement) of section 611 are not available where securities are offered as consideration on terms (including terms in the constitution of the issuer) that require that scrip to be held by a custodian and/or subject to a securityholder agreement or similar arrangement, where doing so results in the issuer not be subject to the application of:

(a) the shareholder limit in section 113(1);

(b) section 606; or

(c) the disclosing entity provisions in Pt 1.2A.

AFMA has been a longstanding advocate for good policy process, as exampled by our articulation of the importance of the issue to the Financial System Inquiry. It is a cornerstone of high-quality public administration and is a subject on which successive governments have provided supporting statements. AFMA is vigilant for digressions from good practice as they entrench bad precedent.

The policy development process and consultation in CP 312 by ASIC in this matter is of grave concern and considered to be inadequate. It is not the case that the industry should have to justify a change to the law by ASIC through the regulatory impact assessment process. The burden is on ASIC to make out the case for major change through demonstration of the problem and fully articulate the options through a public consultation process. The reference to the need to carry out such an assessment in CP 312 following on from this consultation does not meet the basic threshold standard for policy analysis required for a modification to the law.

The consultation paper asserts that the use of legitimate custodian arrangements and securityholder agreements is being used to avoid investor protections despite securityholders being provided with adequate disclosure in connection with their decision to invest. No evidence is provided for the assertion that mandatory custody arrangements are being used as an avoidance device. AFMA has a neutral position with regard to whether this is case as there is no publicly available information to make an assessment on this question. The point being made is that it is the obligation of ASIC, as the supervising regulator with the powers to detect illegitimate avoidance activity relating to offers of securities incorporating mandatory custody or securityholder arrangements, to provide evidence empirical to the public and demonstrate the harm as justification before proceeding with its proposal.

AFMA notes that this proposal provides for differential treatment of Australian in contrast to overseas companies, as foreign body offering shares will generally not become a disclosing entity as a result of offers under a takeover bid or scheme. Accordingly, private equity bidders could still use foreign holding vehicles with the result target shareholders taking up the stub equity would be in the same position as is currently the case.

It is also noted that a statement on page 16 paragraph 44 has a serious error. *"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"* A Regulatory Guide is an interpretative guide to the law by ASIC. While a highly influential interpretation of the law, it cannot and should not be perceived as containing regulation other than as subject matter in commentary on actual rules. In other words, regulation cannot be made through a Regulatory Guide.

Please contact David Love either on or by email if further clarification or elaboration is desired.

Yours sincerely

David Love
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