Submission made by Simmons & Simmons

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9 May 2019

Dear Mr Bulman

Consultation on Proposed Amendments to Guidance Note 20 – Equity Derivatives

A dominant trend in major derivatives markets since the GFC has been a move towards greater transparency. This reflects a consensus amongst G20 rule-makers that information asymmetries are a handicap to efficient, competitive and informed markets. The amendments to GN 20 can be viewed as a logical and timely step within this larger trend. I am a lawyer with over 15 years of experience in the area of derivatives law and practice and welcome the opportunity to comment on this Takeovers Panel consultation paper. I would like to contribute some comments from the perspective of a practitioner active in M&A derivatives activity.

1. *Do you agree that the Panel should expect disclosure of all long positions over 5%? If not, what do you consider should be the Panel's policy position on disclosure of equity derivatives?*

In principle I agree that the Panel should expect disclosure of derivatives in the context of takeovers. The growth of, and innovation within, derivatives markets continues to be phenomenal. A takeovers disclosure regime which omits derivatives or does not keep up with market evolution is unlikely to be either effective or meaningful. Having said that, I do have some reservations regarding the Panel's proposed approach. The consultation paper proposes to require disclosure of long equity derivative positions forming part of a long position in 5% or more of the voting rights in an entity. My observations on this are as follows:

Definition of "long"

Paragraph 5 of the draft Guidance Note indicates that the Panel considers a taker to be "long" if it "is to benefit from an increase in the price of the underlying security". This is a somewhat narrow interpretation and I invite the Panel to consider a more expansive approach not only focussed on the benefit of price increases. I submit that:

(a) the holder of a deeply out-of-the-money option will arguably not "benefit" from price increases until the option becomes in-the-money. However such an option should nevertheless be disclosed;

(b) a person ought to be also considered "long" if that person would be economically disadvantaged by a decrease in the price of the underlying security; and

(c) it should be clarified that any such benefit or disadvantage may be absolute or conditional.

This expanded approach to long positions would close a potential loophole where derivatives are written which reduce the free float but do not require disclosure due to careful structuring of the payout. In recent years there has been an increasing trend towards the use of deal-contingent M&A hedging. The disclosure regime should also ensure that contingent derivatives are not used in a way that undermines Takeovers Panel policy.

"Equity derivative positions"

The Consultation Paper generally appears to be focussed on "equity derivatives".[1] I suggest that this is a rather narrow approach. The label "equity derivative" is not a legal term of art and it is not clear what definition the Panel will give to this term. A danger of referencing only this class of derivative is that it creates uncertainty as to whether other equity-like instruments, such as contracts for differences, spread bets and securitised derivatives in the form of structured products fall within the disclosure regime. An innovative structurer may be incentivised to create derivatives which give the holder a synthetic long equity position but which also contain other features which arguably bring it within a different asset class (for example by including credit default terms so that it resembles a credit derivative). To close this potential loophole I suggest

[1] There is some internal inconsistency in the draft Guidance Note because for example paragraphs 12(e) and 12(f) refer to a "derivative" whereas paragraphs 12(h) and 12(i), amongst other paragraphs, refer to an "equity derivative".

that the Guidance Note uniformly refer to a "derivative" rather than an "equity derivative", or alternatively include a broad definition of the term "equity derivative". This approach would also be more consistent with Chapter 6, Regulatory Guide 5 and Regulatory Guide 222 which generally refer to "derivatives" without any class distinction.

In addition the Panel should ensure that it is not possible to circumvent disclosure by using repos and securities lending transactions, as it is possible to create a synthetic long equity position using these products. Other techniques to consider are collateralisation transactions where equities are posted as collateral with respect to a non-equity derivative transaction (either on a title transfer or security interest basis), particularly where the terms include a right of use and/or right of appropriation. Unless such arrangements give rise to a relevant interest there may be a gap in the Panel's proposed disclosure regime.

Definition of "entity"

The jurisdictional reach of the Panel is a complex topic beyond the scope of this submission. For present purposes I note that the proposed definition of "entity" does not contain a geographical limit, although paragraph 16 contemplates only disclosure to ASX which perhaps implies that only ASX listed entities are in scope. I invite the Panel to consider the merits of providing more clarity on the jurisdiction and extraterritorial application of the Guidance Note, including whether derivatives traded offshore between two third country parties are in scope.

5% threshold

Calibrating the hard reporting threshold at 5% has its merits as it provides symmetry with substantial holding disclosures. Paragraph 10 indicates that disclosure of less than 5% could also be appropriate in some circumstances. I note that some overseas disclosure regimes have adopted a lower threshold which applies during offer periods. The calibration of the disclosure threshold ought to be based on a cost/benefit analysis.

2. *Do you agree with footnote 2? What further guidance (if any) do you think the Panel should provide in cases when a person obtains a long position of over 20%?*

I agree. Footnote 2 reserves the discretion of the Panel in its oversight role. It is difficult to identify what further guidance would be appropriate for long derivatives-based positions of over 20%. At this level of holding it might be useful if market participants could engage with the Panel on a confidential basis to the extent they have concerns that there may be unacceptable circumstances.

3. *Should there be more guidance provided in relation to what information is required to be disclosed (see paragraphs 11-17)? If yes, what guidance would assist? Should the taker of an equity derivative be expected to disclose the identity of the writer(s) of that derivative?*

Short positions

Paragraph 12 indicates that the Panel expects disclosure of short positions by holders of 5% long positions. I agree that disclosure of short positions is crucial in order for market participants to have an accurate understanding of the prevailing market dynamics.

Paragraph 5 indicates that the Panel considers a short position to be one where the taker "is to benefit from a decrease in the price of the underlying securities". As with my comments in the "*Long positions*" section above, I invite the Panel to adopt a more expansive definition of "short" whereby a person is also considered short if that person would be economically disadvantaged by an increase in the price of the underlying security; and clarifying that any such benefit or disadvantage may be absolute or conditional.

Paragraph 12(i) refers to derivative positions that offset physical positions. This is ambiguous since there are degrees of offsetting. Footnote 6 of the Guidance Note refers to netting and offsetting which indicates that the Panel views these as two different concepts. Footnote 6 suggests that offsetting nature, period and price would be required before netting can be recognised. The Panel may wish to clarify what exactly needs to be offset against physical positions – is it only the exposure to price increases, or do other features of the physical position also need to be offset, for example a right to exercise votes? What does "nature" mean in the context of footnote 6?

It is also unclear what constitutes a "physical position" and whether a long derivative position (either cash or physically settled) could be considered a physical position.

I suggest more clarity could be added to ensure there is no disclosure loophole based on technical arguments relating to the terms “offset”, “netting” and “physical positions”.

Gross versus net disclosure

Footnote 6 of the Guidance Note indicates that it will not normally be appropriate to net long and short positions for the purposes of disclosure. I generally agree with this policy approach. Reporting only net positions could present a misleading overall picture to the market, particularly during an offer period.

ISDA documentation

Paragraph 13 states that the Panel is unlikely to consider that standard ISDA documentation needs to be provided. A significant volume of derivative transactions are documented using non-ISDA documentation. I suggest that the reference to ISDA be replaced with a more generic reference to underlying derivative documentation.

Timing

The Guidance Note does not specify a fixed time at which a person is required to assess whether it has crossed a reporting threshold. Paragraph 15 indicates that the Panel has some discretion in considering whether timely and adequate disclosure has been made. It may be helpful for market participants if the Panel provides more guidance on its expectations in this regard, perhaps by stating that it expects a daily evaluation of positions to be made and possibly by specifying a fixed point in time at which that evaluation must be conducted such as at market close. If a party is dynamically hedging it is possible that it will cross the thresholds several times a day. In this situation I suggest that only one disclosure per day should generally be required in order to avoid voluminous disclosure being sent to the entity.

The Writer

I agree that the identity of the writer of a derivative need not generally be disclosed, although I mention in passing that in the case of put options the writer will be the long party.

4. *Are there any other changes you would make to the draft Guidance Note?*

Yes. As mentioned in footnote 1 above, there is some internal inconsistency in references to “derivative” in some places and to “equity derivative” in other places.

In addition paragraphs 21 and 22 appear to contain typos – the word “make” where it first appears in each paragraph should be “may”.

Thank you for the opportunity to participate in the development of this important area of market practice.

Yours sincerely,

Carl Baker

Submission made by MinterEllison

MinterEllison

28 May 2019

BY EMAIL

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Dear Panel Executive

Submissions in response to consultation paper on proposed revisions to Guidance Note 20 – Equity Derivatives

We refer to the Takeovers Panel's Consultation Paper dated 11 April 2019 inviting submissions on proposed revisions to Guidance Note 20 – Equity Derivatives (**GN 20**). MinterEllison thanks the Takeovers Panel for the opportunity to make these submissions.

Please note that the views expressed in these submissions do not represent the views of MinterEllison's clients.

1. Do you agree that the Panel should expect disclosure of all long positions over 5%? If not, what do you consider should be the Panel's policy position on disclosure of equity derivatives?

We submit that there is significant uncertainty whether the premise that "*the economic incentives for a writer to hedge is likely to give some form of effective control over the disposal of an equivalent number of the underlying securities*"[1] is still valid in the current market. In order for the Panel to expect disclosure of all long positions over 5%, the guidance should address the actual realities of how cash settled equity swaps are used in today's market, and the resultant effects (if any) on control.

We also submit that there is confusion as to whether the disclosure of long equity derivative positions is limited to situations where "*there is a control transaction*"[2]. The proposed guidance note is an opportunity for the Panel to definitively state its positon that the guidance applies to disclosure of equity derivatives outside of a control transaction occurring. This assumes that the Panel is comfortable that it has jurisdiction to require disclosure of equity derivatives outside of a control transaction occurring, which we consider is not free from doubt.

These submissions are explained below:

(a) Economic incentive to hedge and its control effect

We submit that the market has developed such that, in 2019, the economic incentive to hedge through a physical holding has been substantially weakened, so much so that it cannot be said with sufficient certainty that the taker of a cash settled long position has any effective control over

[1] See Takeovers Panel Discussion Paper – Equity Derivatives, dated 10 September 2007, at [52].
[2] See GN 20 at [9].

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the disposal of the underlying securities, or at least that any effective control is not substantial enough to justify the requirement to disclose cash settled long positions that is in effect equivalent to the disclosure requirement for an actual relevant interest.

The premise that there is an economic incentive for a writer to physically hedge a cash settled long position is reflected in paragraph 6 of the proposed guidance which states that:

> *"the writer usually has an economic incentive to hedge"*
>
> *"The hedge is often established by acquiring the underlying securities".*

This premise is fundamental to the Panel's policy as expressed in GN 20, as that policy relies on both the existence of an economic incentive to hedge through a physical holding, and that economic incentive then having a control effect.

This premise is used to justify the policy position that there should be disclosure of cash settled long equity derivative positions that is in effect equivalent to disclosure for an actual relevant interest, despite cash settled positions being recognised by the Panel as not necessarily conferring a relevant interest or voting power on the taker.

This premise may have been an accurate representation of the market in 2007 when the Panel first consulted on the proposed GN 20 and released its Discussion Paper. However, in the current market, writers of cash settled long positions have developed, and commonly use, other risk mitigation techniques that do not rely on simply holding physical positions as a hedge to their economic positions. In our experience:

(i) It is common for writers of cash settled long positions to hedge risk by taking further cash settled equity swaps and other derivatives (such as cash settled call options) referenced to the same underlying securities, so that losses / gains under the original cash settled long position are offset by gains / losses on those further cash settled equity swaps or other derivatives. This hedging technique is becoming increasingly popular amongst writers of cash settled long positions because it avoids the writer needing to outlay large amounts of capital that would be required to take a physical hedge position.

This is important because the proposed guidance note relies on the taker of a cash settled long position "*controlling the unwinding*" as a reason why a cash settled long position has an effect on the control or potential control of an entity. To be able to control the unwinding, it is necessary for the writer to hold a physical hedge, which is often not the case.

(ii) It is common for writers of cash settled long positions who have taken physical positons as a hedge to then 'lend' the securities subject of that physical hedge. Securities subject of such lending can then be traded by the 'borrower' until the borrower is required to return the securities to the 'lender' at the end of the agreed period. Such borrowing of securities used to hedge cash settled long positions disrupts the premise that securities used to hedge cash settled long positions are 'taken out of the market'.

This is important as paragraph 7 of the proposed guidance relies on reduction in the 'free float' as a reason why a long equity derivative position may affect the market in the underlying securities.

(iii) It is not uncommon for writers of cash settled long positions to choose not to hedge through a physical holding, as hedging through a physical holding involves substantial upfront costs to the writer. This lack of any hedge is most often seen where the cash settled long position is in respect of a small number of shares of a company, and/or where the shares in that company are highly liquid. This is not economically irrational behaviour, but rather a trade-off between transaction costs and risk reduction.

As noted above, this is important because it limits the ability of the taker of a cash settled long position to be able to control the unwinding of that swap, and does not result in any reduction in the 'free float'.

Unless the Panel addresses in the proposed guidance note the actual realities of how cash settled long positions are written and hedged (or not) in today's market, the proposed guidance note in our submission risks failing to address the policy concerns it was designed to address.

(b) *Disclosure outside of control transactions*

When the Panel consulted on GN 20 in 2007, the position was not entirely settled as to whether the Panel had jurisdiction to require disclosure of equity derivatives outside of a control transaction occurring.

This doubt remained even after the Corporations Act was amended in 2007 to insert a new definition of 'substantial interest'.

The Panel acknowledged this doubt, and as a result, the Panel chose to apply GN 20 "*primarily*" to control transactions[3]. However, the Panel noted that it considered that there may be some circumstances involving the use of equity derivatives that are unacceptable in the light of the principles in section 602 of the Corporations Act outside the context of a control transaction. Therefore paragraph 11 of GN 20 provided that the Panel may still wish to examine situations where a person holds a long position above 5% even though there is no control transaction.

We submit that some market participants considered that the guidance only required disclosure of cash settled long equity derivative positions at the time when a control transaction first appeared.

This understanding is typically based on a reading of paragraph 9 of GN 20 which states:

> "*Where there is a control transaction, the Panel would expect that all long positions which already exist, or which are created, are disclosed unless they are under a notional 5%.*"

For example, Herbert Smith Freehills state the view that:

> "*The applicability of these disclosure requirements, however, were limited to a "control transaction" scenario.*" [4]

The proposed guidance note is an opportunity for the Panel to definitively state its positon that the guidance applies to disclosure of equity derivatives outside of a control transaction occurring.

However, the draft guidance note simply states at paragraph 9 that the Panel expects disclosure to be made where the long position is 5% or more, or changes by at least 1%. It does not state whether or not the existence of a control transaction is necessary to enliven that expectation.

We submit that the draft guidance note would ideally expressly state that the Panel expects disclosure to be made on and from entry into the long positon, regardless of whether there is a control transaction at the time of entry into that long position.

This would, of course, require the Panel to take a definitive view that it has jurisdiction to require (or expect) disclosure of equity derivatives outside of a control transaction occurring. We note that there is still some doubt about this.

For example, in submissions from the Corporations Committee of the Business Law Section of the Law Council of Australia in response to a 2009 Treasury issues paper, the Committee considered that the Panel's jurisdiction remained unclear, even after the 2007 amendments, and stated that:

> "*It would therefore appear that the only way to fully address the issue is to amend the [Corporations] Act to expressly include a disclosure regime for long positions under cash settled equity swaps…*" [5]

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[3] See page 2 of Takeovers Panel – Equity Derivatives – Public Consultation Response Statement Dated 11 May 2008.
[4] Clearer Guidance On The Way: The Takeovers Panel Seeks Submissions On Equity Derivatives Guidance Note – Legal Briefings – By Andrew Rich and Ken Ooi, dated 30 April 2019.
[5] Submissions on Issues Paper on Improving Australia's Framework for Disclosure of Equity Derivative Products, Corporations Committee of the Business Law Section of the Law Council of Australia, dated 4 August 2009, at page 5.

We note that the Corporations Act has never been amended as suggested by the Committee, so there remains doubt as to whether the Panel has jurisdiction to require disclosure of equity derivatives outside of a control transaction occurring.

2. Do you agree with footnote 2? What further guidance (if any) do you think the Panel should provide in cases when a person obtains a long position of over 20%?

We submit that the inclusion of footnote 2 would be extending the law and policy quite considerably from where it currently stands, which we submit is more properly the province of legislation. In our view, there is no policy or legislative basis for this. In short:

- the law does not apply the takeovers provisions to cash settled long positions above 20%;
- the existing policy, as expressed in GN 20, is not as extensive as the position represented by footnote 2;
- there is no evidence that the market for control of an entity has been adversely affected by persons holding cash settled long positions above 20%;
- disclosure of cash settled long positions above 20% is the appropriate approach, not defacto prohibition or making such positons effectively subject of the takeover provisions;
- it is inappropriate to extend the law and policy positon by including footnote 2 with no transitional period or 'grandfathering' of existing arrangements.

These submissions are explained below:

(a) The law does not prohibit the acquisition of a cash settled long position above 20%, or apply the takeovers provisions to such acquisitions

The law prohibits a person acquiring a relevant interest in shares in a public company that would increase that person, or another person's, voting power in the public company above 20%.

A cash settled long position does not per se confer a relevant interest or voting power on the taker. As such, the law currently allows the acquisition of a cash settled long position above 20%. That is the case even where part of that long position is physical, provided that the physical component does not itself breach the 20% prohibition.

We submit that the law has taken this approach because, even if cash settled long positions can give some form of effective control over the disposal of the underlying securities, that level of control is not sufficient to attract the application of the takeover provisions (and the resulting need to pay a control premium to other shareholders) or to be subject of some form of prohibition.

Importantly, in 2009 the Treasury released an issues paper which examined equity derivatives and GN 20.[6]

That issues paper specifically considered whether Chapter 6 should be applied to equity derivatives, and questioned:

> "*If substantial holder notice provisions were expanded to include equity derivative positions, should the law be amended so that positions over 20 per cent must also comply with the takeover provisions? Should the assessment consider whether the takeover provisions in the Corporations Act 2001 would benefit from an expansion to include equity derivatives holdings?*" [7]

Submissions were received in response to the issues, some of which argued against the need for any such legislative extension. The submissions from the Corporations Committee of the Business Law Section of the Law Council of Australia noted that there were differing views as to whether the Committee supported extension of the takeover provisions – in our submission this

[6] Issues Paper: Improving Australia's Framework for Disclosure of Equity Derivative Products, dated 5 June 2009.
[7] Issues Paper: Improving Australia's Framework for Disclosure of Equity Derivative Products, dated 5 June 2009, at Section 5.1, question xxii.

evidences the controversy of such a proposal, and further evidences that a prohibition of the acquisition of a cash settled long position above 20% is not a feature of the current law.

No legislative changes were made after the 2009 issues paper. Treasury concluded that such a step might not be necessary if improved disclosure would provide sufficient protection to investors:

> "*If the requirements for substantial holder notices are amended to incorporate equity derivative positions, it is arguable that this apparent gap in the takeover legislation may not be an issue because the market can be relied on to price in a control premium, thereby rewarding other shareholders with the premium that an acquirer of direct stakes normally has to offer in a takeover bid. Arguably, the Takeovers Panel could address such an issue when it arises in practice*." [8]

That is, the Treasury has carefully considered the position and determined that disclosure of cash settled long positions above 20% is the appropriate approach, not the application of the takeover provisions or some form of prohibition.

In 2012, the Treasury released a scoping paper which again examined equity derivatives[9]. Again, no legislative changes were made after the 2012 scoping paper.

As such, the law continues to permit the acquisition of cash settled long positions above 20% (provided that any physical component does not itself breach the 20% prohibition), nor does the law apply the takeovers provisions to such acquisitions.

(b) The existing policy, as expressed in GN 20, is not as extensive as the position represented by footnote 2

There is a material difference between, on the one hand, making an existing policy position that has been long accepted by the market more certain by expressly including it in written guidance, and on the other hand, re-writing the existing policy in order to materially extend its application.

GN 20 does not contain any statement in respect of the acquisition of a cash settled long position above 20% as definitive as the position set out in the proposed footnote 2.

The existing policy does not state that an acquisition of cash settled long positions above 20% may give rise to unacceptable circumstances, nor does the policy otherwise apply the takeovers provisions to such acquisitions.

At paragraph 11, GN 20 states that:

> "*the Panel may examine situations where a person holds a long position above 5% even though there is no control transaction*".

However, that statement does not go as far as the proposed footnote 2 to explicitly state that an acquisition of cash settled long positions above 20% may give rise to unacceptable circumstances.

Indeed, GN 20 mentions "unacceptable circumstances" approximately 13 times. In 10 of those instances where "unacceptable circumstances" is mentioned in GN 20, the discussion relates to disclosure of the long position. None of the other three instances where "unacceptable circumstances" is mentioned in GN 20 expressly state that an acquisition of cash settled long positions above 20% may give rise to unacceptable circumstances.

It may be that the policy position in GN 20 deliberately fell short of stating that an acquisition of cash settled long positions above 20% may give rise to unacceptable circumstances, because the residual concern that the Panel may not have jurisdiction to make a finding of unacceptable circumstances outside of a control transaction occurring also applies to the acquisition of cash settled long positions above 20% outside of a control transaction.

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[8] Issues Paper: Improving Australia's Framework for Disclosure of Equity Derivative Products, dated 5 June 2009, at [64].
[9] Takeovers issues – Treasury scoping paper, dated 5 October 2012.

As such, GN 20 as currently drafted focusses on the requirement (or expectation) that long positions above 5% are disclosed, rather than whether the acquisition of cash settled long positions above 20% may give rise to unacceptable circumstances.

The existing policy positon is important, as the Panel's consultation paper on the proposed changes to GN 20 describes the proposed changes as a:

> *"rewrite of the Guidance Note with the main of providing shorter and clearer guidance"*

However, as the existing policy is not as extensive or as definitive as footnote 2, the proposed inclusion of footnote 2 is not a mere rewrite, but would instead extend the policy considerably from the existing position as set out in GN 20.

We submit that it is not appropriate for footnote 2 to be included in the context of the above existing policy position, and if any such change of this nature is to be made (despite our submissions below that no such change is required), the appropriate process for introducing that change is legislative change by Parliament to amend the Corporations Act.

(c) There is no evidence that the market for control of an entity has been adversely affected by persons holding cash settled long positions above 20%

For the policy to be altered in such a material way as the proposed guidance is contemplating by the inclusion of footnote 2, there must be clear evidence of the adverse impact of cash settled long positions above 20% on the market for control, which we say is absent.

Since GN 20 was adopted by the Takeovers Panel in 2008, we are not aware of any examples in Australia of the market for control of an entity being adversely affected by persons holding cash settled long positions above 20%.

Most examples of cash settled long positions having an impact on control situations that we are aware of either pre-date the issue of GN 20 in 2008, or relate to cash settled long positions below 20%. We submit that this demonstrates that the current system, which focuses on the need for disclosure rather than defacto prohibition, is working.

In its submissions in response to the Treasury's 2009 issues paper, the Corporations Committee of the Business Law Section of the Law Council of Australia noted that:

> "*In the Committee's experience, the use by Australian based parties of cash settled equity swaps to avoid the substantial shareholding notification provisions has diminished since the introduction of the Panel's Guidance Note*…"[10]

We agree, and we submit that this continues to be the case today. As such, we question why there is any need to effectively prohibit the acquisition of cash settled long positions above 20% where the disclosure focussed regime is working as intended.

So, the proposed guidance seeks by the inclusion of footnote 2 to address a problem that simply does not exist in practice (if it does exist in some theoretical way, it does not have any material adverse impact on the market for control).

(d) Disclosure of cash settled long positions above 20% is the appropriate approach, not defacto prohibition or making such positons effectively subject of the takeover provisions

We submit that the proposed footnote 2 would, in effect, prohibit the acquisition of a cash settled long position above 20% because there will be no way (other than to purport to comply with the takeover provisions) to acquire such a position in a manner that allows the taker to avoid the risk of unacceptable circumstances arising (particularly as the proposed footnote 2 does not explain how such risk can be mitigated).

[10] Submissions on Issues Paper on Improving Australia's Framework for Disclosure of Equity Derivative Products, Corporations Committee of the Business Law Section of the Law Council of Australia, dated 4 August 2009, at page 4.

Prohibition, even in defacto form, is an extreme step in the arsenal of any regulator. We submit that the Panel should carefully consider whether it is appropriate to effectively prohibit something that the Treasury specifically considered and did not recommend prohibition in 2009 and again in 2012, with the relevant provisions of the Corporations Act remaining unchanged.

We submit that the proposed footnote 2 would also, in effect, make the acquisition of a cash settled long position above 20% effectively subject to the takeover provisions, as the only way to acquire such a position in a manner that allows the taker to avoid the risk of unacceptable circumstances arising would be to purport to comply with the takeover provisions.

We submit that the Panel should carefully consider whether it is appropriate to effectively extend the takeover provisions in a manner that the Treasury specifically considered and did not adopt in 2009 and again in 2012.

In our view, it is not necessary or appropriate for the Panel to make such a material change to the legal and policy position. If any such change of this nature is to be made (despite our submission that no such change is required), the appropriate process for introducing that change is legislative change by Parliament to amend the Corporations Act.

We submit that making GN 20 clearly require the disclosure of all long positions above 5%, regardless of whether there is a control transaction or not, will sufficiently address any issues that cash settled long positions above 20% may present. Such disclosure will allow the market to price any such positions, and will allow potential competitors for control to assess the position on a fully informed basis.

(e) It is inappropriate to introduce footnote 2 with no transitional period or 'grandfathering' of existing arrangements

There are currently situations in which persons hold cash settled long positions above 20% in public companies. Some of those situations have been in place for some time.

As explained above, the inclusion of footnote 2 extends the administration of the law and policy position quite considerably from where it currently stands. As such, the inclusion of footnote 2 would cause the takers of each of those cash settled long positions to immediately be subject of the risk of a declaration of unacceptable circumstances.

Many of the cash settled equity swaps and other derivatives that give rise to cash settled long positions above 20% are long dated contracts under which the taker may not have the unilateral ability to terminate early. In some cases, the taker can terminate early at some additional cost to the taker.

If despite our submissions footnote 2 is included in a revised GN 20, then it would be unfair to not include a transitional period in which existing cash settled long positons above 20% could remain or, worst case, be unwound in an orderly manner consistent with the underlying documentation.

3. Should there be more guidance provided in relation to what information is required to be disclosed (see paragraphs 11-17)? If yes, what guidance would assist? Should the taker of an equity derivative be expected to disclose the identity of the writer(s) of that derivative? Please explain.

We submit that paragraphs 11 to 17 of the proposed guidance note are generally appropriate.

We comment as follows:

(a) It should be made expressly clear that the requirement in paragraph 11 to disclose the extent to which the counterparty has hedged is only required if that information is known. In most cases, it will not be known and the counterparty will have no legal ability to require disclosure of that information. Footnote 5 goes some way to explain this, but the inclusion of express wording in paragraph 11 would be helpful to put the issue beyond doubt.

(b) There has long been suggestion in the market that there should be a prescribed form for disclosure of long positions in a manner similar to the prescribed form of disclosure for a substantial holding. We submit that a prescribed form is not required, as the market seems to be functioning well without a prescribed form.

We submit that the taker of an equity derivative should not be expected to disclose the identity of the writer(s) of that derivative, because the identity of the writer(s) of an equity derivative is not information that is required by investors to assess the control implications (if any) of the equity derivative.

4. Are there any other changes you would make to the draft Guidance Note? Please explain.

The proposed guidance note mentions in footnote 4 the factors that the Panel may have regard to in determining whether unacceptable circumstances have arisen. The footnote refers to various paragraphs of two Panel decisions.

We submit that the guidance note should set out in the body of the text the factors that the Panel may have regard to in determining whether unacceptable circumstances have arisen, and ideally provide some explanation and a clear exposition of the principles of how the Panel proposes to apply those factors. The aim is for readers to get a clear and concise understanding of the position by reading the guidance note itself, rather than having to elicit the principles from previous decisions of the Panel.

Yours faithfully
MinterEllison

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Submission made by Deutsche Bank

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31 May 2019

By email

Takeovers Panel
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Dear Sir/Madam

Consultation Paper – Guidance Note 20 – Equity Derivatives

Deutsche Bank AG (**Deutsche**) appreciates the opportunity to provide comments on the Takeover Panel's (**Panel**) proposed rewrite of Guidance Note 20 – Equity Derivatives (**GN 20**). This letter sets out Deutsche's comments on the draft GN 20 and certain questions raised in the Consultation Paper.

1. Overview

Deutsche agrees with and supports the Panel's proposals to revise GN 20 to provide clearer guidance about the Panel's approach to Equity Derivatives, and other than the points specifically discussed in this letter, agrees that the Panel's proposals to provide shorter and clearer guidance are appropriate and supports the proposed revisions to GN 20.

2. Deutsche's response to certain specific questions raised by the Panel

a. **Do you agree that the Panel should expect disclosure of all long positions over 5%? If not, what do you consider should be the Panel's policy position on disclosure of equity derivatives?**

Whilst we broadly agree that the Panel should expect disclosure of long positions over 5%, we do not think that this requirement should apply to market makers, either as the writer or taker.

The nature of the holding of a market maker is generally passive and, as the currently in force GN 20 states, "*the Panel will usually take the view that its role is a disinterested, professional one, compared to the taker who is likely to be interested*". As writer, if a market maker acquires shares to hedge the position it has written, it remains subject to the substantial shareholder disclosure requirements. Additionally, if it hedges through entering into another equity derivative, the currently in force GN 20 states that in such circumstances it will be treated in the same way as if it were a writer (i.e. it is not required to disclose its position). At present this is not clear in the proposed revisions to GN 20. Consistent with the current GN 20, imposing disclosure requirements on the non-market maker taker of the equity derivative should be sufficient for a fully informed market.

Consequently it would be useful for the Panel to clarify in the main text of GN 20 that the disclosure requirements will not apply to market makers and footnote 3 revised accordingly.

b. **Do you agree with footnote 2? What further guidance (if any) do you think the Panel should provide in cases when a person obtains a long position of over 20%?**

Yes. We agree with the approach of the Panel in footnote 2 clarifying that the acquisition of a long position, which if it were comprised entirely of a physical holding would contravene s.606 of the *Corporations Act 2001* (Cth), may give rise to unacceptable circumstances (even if the acquisition does not result in the person acquiring a relevant interest in contravention of s.606).

It would be helpful if the Panel could confirm that in taking into account both the application of s.606 and the exceptions set out in s.611 in its determinations of unacceptable circumstances relating to the acquisition of long positions, the Panel will consider both the long equity derivative positions together with the physical holdings of a person in aggregate (as if the long equity derivative positions as part of the holding were comprised entirely of physical holdings) without distinguishing between the long positions and the physical holdings.

By way of example, we would request that the Panel confirm that the exception contained in Item 9 of s.611 (**creep provisions**) applies in circumstances where a person holds at least 19% through a combination of physical holdings and long equity derivatives and that the 3% permitted acquisition in a 6 month period set out in the creep provisions could apply to permit acquisition of physical holdings or long equity derivatives (or a combination of both).

Please do not hesitate to contact me if you would like to discuss any aspects of this letter.

Yours faithfully

Ashley Seeto
Managing Director
co-Head of Equity Capital Markets Australia
Deutsche Bank AG

Submission made by Norges Bank

NORGES BANK
INVESTMENT MANAGEMENT

Australian Government Takeover Panel
Level 10
63 Exhibition Street
Melbourne, Victoria, 3000
Australia

Date: 31.05.2019

Consultation by the Australian Government Takeover Panel on all long positions in equity derivatives (revision of Guidance Note 20)

We refer to the consultation on Takeover Panels Guidance Note on Equity Derivatives, published on 10 April 2019, and we welcome the opportunity to contribute our perspective.

Norges Bank Investment Management (NBIM) is the investment management division of the Norwegian Central Bank (Norges Bank) and is responsible for investing the Norwegian Government Pension Fund Global. NBIM is a globally diversified investment manager with an equity portfolio consisting of minority stakes in more than 9,000 listed companies. Over AUD 18.8 billion are invested in 312 listed companies incorporated in the Australia[1]. NBIM is an active owner and aims to promote long-term value creation in the companies in which it invests.

As a participant in the Australian market, we welcome the Panel' efforts towards improved shareholding disclosure and market transparency rules, which can have a positive effect on the well-functioning of financial markets with benefits for shareholders, listed issuers and regulatory authorities alike.

Please find our feedback on the comments sought on the draft.

1. *Do you agree that the Panel should expect disclosure of all long positions over 5%? If not, what do you consider should be the Panel's policy position on disclosure of equity derivatives?*

   We agree that disclosure of all long positions over 5% is beneficial as it would contribute to greater transparency for market participants. Disclosure of all long positions would provide a fuller picture of the holdings and interests of investors.

2. *Do you agree with footnote 2? What further guidance (if any) do you think the Panel should provide in cases when a person obtains a long position of over 20%?*

[1] As at year-end 2018.

As the Management Mandate for the Government Pension Fund Global generally restricts investment to up 10% of the voting shares in a single company, we will abstain from comment on this question.

3. *Should there be more guidance provided in relation to what information is required to be disclosed (see paragraphs 11-17)? If yes, what guidance would assist? Should the taker of an equity derivative be expected to disclose the identity of the writer(s) of that derivative? Please explain.*

We see the guidance provided in paragraphs 11-17 as sufficient. While we believe that increased transparency benefits financial market participants, there should be a balance between disclosure requirements and the administrative burden on investors. As such, we do not advocate for the disclosure of the identity of the derivative writer(s).

In relation to paragraph 12(j), it is our understanding that disclosure of gross short positions at given thresholds is not common in other financial markets. We do find that disclosure of gross short positions increases market transparency and such positions can be provided together with the disclosure of long positions without additional administrative cost. However, we are not certain that disclosure of changes of gross short positions on their own necessitate a separate disclosure.

In relation to paragraph 15 we would like to point out that a next trading day disclosure deadline by 9.30 am may be difficult, if not impossible to meet for large international investors. In order to establish disclosure obligations, data is compiled and aggregated from various sources – internal and external investment managers, lending agents, etc. – which is time consuming. Further, time zone differences play a role as well. Our recommendation would be for a reporting requirement by the close of business on the next trading day.

4. *Are there any other changes you would make to the draft Guidance Note? Please explain.*

In general, it would be beneficial to have convergence of the rules governing the types of disclosable financial instruments under the statutory regime and the Panel regime as this would streamline the required compliance and disclosure processes as well as increase the uniformity of information provided to the market.

Yours faithfully,

Sai Aanandha Shankhar
Senior Advisor – Regulatory Compliance

Stanislav Boiadjiev
Head of Regulatory Compliance

Submission made by AFMA and clarifying email

31 May 2019

Takeovers Panel Secretariat
Level 10/63 Exhibition Street
Melbourne VIC 3000

By email: takeovers@takeovers.gov.au

To: Takeovers Panel Secretariat

Guidance Note 20 Equity Derivatives Consultation

The Australian Financial Markets Association (AFMA) welcomes the opportunity to make comment on the Takeover Panel's consultation on Guidance Note 20 Equity Derivatives.

AFMA welcomes the review of Guidance Note 20 Equity Derivatives as an opportunity to increase the clarity of guidance and thereby better serve companies, bidders and the market.

The aims of the revised draft according to the Consultation Paper are to:

- "rewrite the Guidance Note with the aim of providing shorter and clearer guidance;
- state the Panel's expectation that all long positions over 5% should be disclosed (irrespective of whether there is a control transaction); and
- provide guidance on the matters the Panel will take into account in considering what orders should be made if the Panel finds that non-disclosure of equity derivatives is unacceptable."

AFMA would agree that the current Guidance Note could well be expected to benefit from a revision that aims to increase clarity.

AFMA also considers it is appropriate that guidance be provided by the Panel on the matters it would take into account when considering what orders should be made if the Panel finds that non-disclosure of equity derivatives is unacceptable.

1. Do you agree that the Panel should expect disclosure of all long positions over 5%? If not, what do you consider should be the Panel's policy position on disclosure of equity derivatives?

We note some reservations around the second point – to state the Panel's expectation that all long positions over 5% should be disclosed irrespective of whether there is a control transaction.

To the extent a derivative writer acquires shares to hedge the option positions, the writer remains subject to substantial shareholder disclosure requirements.

As a general principle AFMA recommends against public reporting of equity derivative positions when there is no control transaction, as reporting of these positions could discourage market activity and positions that have no connection to takeovers.

Reporting, whether it be by a writer or a taker of an equity derivative, could expose the writer of the derivative to trading risk around the derivative. This could discourage investment and liquidity in the markets. AFMA queries whether disclosure in the absence of a control transaction delivers any additional relevant informational value to justify these risks.

The current in force Guidance Note 20 states "The Panel is generally not concerned with transactions that have little to do with control"[1], but notes that the Panel may examine circumstances where there is no control transaction in certain circumstances depending on *inter alia* "the type of equity derivative, the parties involved and the relationship of the derivative transaction to a control transaction".

The approach of the existing Guidance note 20 is broadly consistent with the legislative framework and the expectations of Parliament. The Corporations Act at 659AA states "The object of sections 659B and 659C is to make the Panel the main forum for resolving disputes about a takeover bid until the bid period has ended." This intention was acknowledged by the Panel in Auris Minerals Limited [2018] ATP 7 footnote 10 "We note, for example, that there is no takeover bid on foot or proposed and accordingly this is not a dispute that Parliament intended the Panel to be the "main forum" to resolve (see sections 659AA, 659B and 659C)".

However, in Tribune Resources Ltd, [2018] ATP 18 at 67 the Panel held that while in deciding on whether to make a declaration it would need to consider "s602, the provisions of Chapter 6 and, more broadly, the role Parliament intended the Panel to perform". In footnote 18 it held that "It does not follow, however that we are precluded from considering whether circumstances are unacceptable on the basis of a contravention of Chapter 6C merely because the Court also has jurisdiction or there is no control transaction on foot".

The proposed draft of Guidance Note 20 would appear to suggest that the Panel is minded to extend this reasoning to require, in the absence of a control transaction, general reporting requirements that go beyond those that have been set by the Corporations Act. That is where there is no control transaction and an equity derivative exposure (where the securities to which the derivative relates exceeds the 5% level).

It is not clear that this reporting direction is soundly-based in a guidance note of the Panel. If it is the case that the Panel is within its powers to consider circumstances outside of

[1] Guidance Note 20, p. 3.

control transactions it does not necessarily follow that it is within scope to create reporting directions for the market more generally merely because substantial equity derivative positions are established.

While it may be appropriate for Panel guidance to inform market practices during a takeover period, this is a period of direct relevance to the Panel. When there is no control transaction the broader market activity might be harmed by reporting directions from Panel guidance.

For situations where there is no control transaction different parties may take different views on the applicability and relevance of Panel guidance, and if even only some market participants and investors hold that matters outside of control transactions might not be within the mandate of the Panel (given its primary purpose as a dispute resolution body for takeover bid disputes during the takeover period) then investors will not be able to be sure that derivative positions are being included and reported.

For these reasons we would suggest that the Panel restrict any guidance around directions to report equity derivative positions by the taker of equity derivatives to periods where there is a control transaction.

2. Do you agree with footnote 2? What further guidance (if any) do you think the Panel should provide in cases when a person obtains a long position of over 20%?

It would be helpful if the Panel provided more clarity on which particular circumstances they would view a transaction of that nature to be unacceptable circumstances.

3. Should there be more guidance provided in relation to what information is required to be disclosed (see paragraphs 11-17)? If yes, what guidance would assist? Should the taker of an equity derivative be expected to disclose the identity of the writer(s) of that derivative? Please explain.

We note the risks for gaming of derivative positions around the strike price in the event that they exposed either by the writer or taker of the derivative. Increasing risks of gaming decreases interest in providing these financial services and increases their cost.

The writers of equity derivatives should not be required to report the derivative. We find the ‘usually apply’ wording in footnote 3 creates uncertainty and should be removed. We suggest that the wording be moved to the body of the guidance (such as in the current GN20 paragraph 15) so that it is clearer the writer is carved out of the directions.

Writers of equity derivatives do not necessarily have a view of all of the holdings of a bidder which may be held with multiple counterparties and through other market participants. The taker is the party with the view of their total exposure. Further, writers of derivatives might accumulate significant derivative exposures as part of a market making or flow business that would not be related to a control bid. It may create a misleading impression and detract from the clarity of information around equity derivative reporting if these positions are required to be reported.

AFMA queries the removal of the exception for market makers that is the current version of the guidance. Market makers are not concerned with control transactions and any net positions that they gain (in the circumstances outlined in the previous guidance) should be excluded from any reporting direction.

4. Are there any other changes you would make to the draft Guidance Note? Please explain.

AFMA seeks clarity that the writer is not obliged to disclose to the taker its hedge positions. This is proprietary information of the writer that is not customarily shared with external parties and as stated in footnote 5, the hedge status might change frequently or the hedge may not be the underlying security.

AFMA also seeks clarity around whether the 5% holding is just for one derivative or also includes aggregate derivatives for disclosure, where a person may accumulate small positions across a number of derivative providers. It is not clear how this would apply for institutional clients who may be managing a portfolio of derivatives and positions and inadvertently gaining a net 5% exposure and not taking on one derivative which results in an exposure to 5% of the company.

Conclusion

We thank you for the opportunity to comment on the proposed revisions to Guidance Note 20 Equity Derivatives. AFMA supports efforts to bring greater clarity to the panel's expectations around equity derivatives and their interactions with takeovers. As discussed above we do have concerns about guidance changes that would seek to reform reporting practices where there is no control transactions, and seek a clearer carve out for writers of derivatives.

We trust our comments are of assistance, and would be pleased to provide further information if desired. In this regard please contact me at djeffree at afma.com.au.

Yours sincerely

Damian Jeffree

Director of Policy

From: Damian Jeffree
To: Takeovers
Subject: Clarifying Email from AFMA Regarding Guidance Note 20 Submission
Date: Friday, 28 June 2019 4:04:04 PM

To: Takeovers Panel Secretariat
Dear Sir/Madam
Thank you for the opportunity to submit this clarifying email that supplements our previous submission.
AFMA made its original submission to the consultation on Guidance Note 20 – Equity Derivatives on 31 May 2019. Subsequent to the initial submission, we have come to understand that the drafters of the Guidance Note intended, and it was not an inadvertent outcome, to capture regular institutional client flow in the reporting regime envisaged by the draft Guidance Note. As such we would like to supplement our previous submission with the points addressed in this email.
A variety of practical difficulties may be created by the proposed regime for investors wishing to use equity derivatives to invest in the Australian market. Investors who are not interested in a control transaction are typically more active and under the proposed regime will be required to track and report a potentially large number of derivative transactions and these transactions may be held with a number of market markers.
We expect many of these investors do not currently have the systems to track and report their positions and may need additional information technology, operational and compliance resources to do so. This could discourage trading and liquidity in the Australian market if such tracking and reporting is required for non-controlled transactions.
We made the case in our initial submission for clarity to be provided that it would be a requirement only on the taker of an equity derivative transaction to disclose. If the intention is to capture flow equity derivatives that are unrelated to control transactions, then this point becomes even more important because of the expanded scope and increased number of writers of equity derivatives who will be impacted. An express clear exclusion on placing any obligation on the writer of the equity derivative to disclose would reduce the circumstances in which reporting (essentially of a duplicate of what has already been reported by the taker of the equity derivative) would be required and thereby limit the regulatory burden on the writer of the equity derivative.
We note that where equity derivatives are written by a financial institution these are often then backed-out to a related entity for risk management purposes. Such transactions should not be included as their reporting could lead to a misleading picture of exposures. For example, the financial institution might write an equity derivative for an equivalent of 5% of a company. In transferring this exposure to an intra-group entity, the writer of the equity derivative would become a taker of the equity derivative for reporting purposes and potentially fall within reporting scope. The entity that writes this second derivative may then hedge with a physical 5% shareholding which would also then be reportable. This may create a misleading impression that the writer of the original equity derivative has a 10% exposure within its corporate group. We would submit that it would be appropriate to carve out this type of intra group trading to avoid misleading outcomes and to ensure that transactions that are entered into for risk management and not control transaction purposes are not captured. If this approach were to be adopted, it would be consistent with the current Guidance Note 20 – Equity Derivatives where the market maker is treated the same way as a writer of the equity derivative where it has hedged its equity derivative that it has written.
More generally, it may be appropriate for market makers, who provide equity derivatives products, to be carved out of the proposed regime. Market makers are carved out under the current Guidance Note 20 – Equity Derivatives when the equity derivative is written at arm's length, for clients with which the market maker is not associated or acting in concert in relation to the relevant company, and for whom the market maker is not acting in a corporate advisory capacity or if it is there is an effective Chinese wall in place. We consider this to be a helpful and an appropriate approach.
AFMA suggests that there may be benefit in the Takeovers Panel approaching future consultations in a multistage manner. An issues paper stage can assist in ensuring a common

understanding of the objectives, issues and potential downsides to regulatory reform. Where a draft Guidance Note is presented without an issues paper preceding it, there can be lost opportunities for constructive engagement with key stakeholders and impacted parties.
We trust this additional email is of assistance and would be pleased to offer further information if required.

Yours sincerely

Damian Jeffree

Damian Jeffree

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Building Australia's financial markets by promoting efficiency, integrity and professionalism.

Submission made by Herbert Smith Freehills

HERBERT SMITH FREEHILLS

Submission in response to the Takeovers Panel's consultation paper on equity derivatives

1 Introduction

1.1 Nature of this submission

This submission is being made in response to an invitation for comments by the Takeovers Panel (the **Panel**) on its consultation paper dated 10 April 2019 relating to its draft guidance note on equity derivatives (**Proposed Guidance Note 20**), which is proposed will replace the current Guidance Note 20.

The views expressed in this submission are the views of the authors only, and as noted below, do not represent the views of all Herbert Smith Freehills partners. Nor do they necessarily represent the views of any of our clients.

1.2 General observations

We are pleased to provide this submission and thank the Panel for the opportunity to provide our comments. Our view is that the proposed amendments are generally sensible and welcome changes.

Our responses to the particular issues identified in the consultation paper are set out below in section 2.

2 Specific submissions

2.1 Do you agree that the Panel should expect disclosure of all long positions over 5%? If not, what do you consider should be the Panel's policy position on disclosure of equity derivatives?

We agree that the Panel should expect disclosure of all long positions of over 5%.

Although the current Guidance Note 20 already requires the disclosure of long positions, this is limited to where there is a "control transaction". The precise scope and application of this limitation is unclear for market participants.

Paragraph 10 of the current version of Guidance Note 20 explains when a "control transaction" commences. Limb (a) of that paragraph is clear and objective – it provides a bright line test. However, limb (b) and (c) refer to the acquisition or announcement of the acquisition of "a substantial interest".

A "substantial interest" is, in turn, defined in paragraph 6 to mean a parcel of securities that "forms a step in the direction of takeover or change in corporate control" – this is an uncertain and unclear test. For this reason, removing this limitation is a welcome amendment.

Additionally, this amendment provides for a consistent treatment between all derivatives and a physical interest in securities.

We note that some of our partners are of the view that disclosure requirements in respect of derivatives outside the context of a control transaction should be a matter for law reform and not the role of the Panel. We would respectfully disagree. In any event, the current Guidance Note 20, albeit in the context of a control transaction, already requires disclosure of equity derivatives, despite this disclosure not being technically required under the black letter of the substantial holding rules in the *Corporations Act 2001* (Cth).

2.2 Do you agree with footnote 2? What further guidance (if any) do you think the Panel should provide in cases when a person obtains a long position of over 20%?

We agree with footnote 2 in the Proposed Guidance Note 20.

The guidance that the accumulation of an aggregate long position (whether capable of physical or cash settlement) in excess of 20% may constitute unacceptable circumstances is helpful clarification.

2.3 Should there be more guidance provided in relation to what information is required to be disclosed (see paragraphs 11-17)? If yes, what guidance would assist? Should the taker of an equity derivative be expected to disclose the identity of the writer(s) of that derivative? Please explain.

We do not wish to make any comments in response to this question.

2.4 Are there any other changes you would make to the draft Guidance Note? Please explain.

There are no other comments that we would make.

10 June 2019

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Submission made by ASIC

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28 June 2019

Allan Bulman
Director
Takeovers Panel
Level 10, 63 Exhibition Street
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By email: takeovers@takeovers.gov.au

Dear Mr Bulman

Takeovers Panel Consultation Paper – Guidance Note 20 – Equity Derivatives

ASIC appreciates the opportunity to provide comments on the Takeovers Panel's proposed revisions to Guidance Note 20—Equity Derivatives (**GN 20**). This letter sets out ASIC's comments on the draft revisions to GN 20 and the questions raised in the Panel's consultation paper.

1. Overview

1.1. ASIC recognises that equity derivatives can be a useful financial tool for legitimate financial investment and risk management. Many equity derivative arrangements do not, or are not entered into in order to, frustrate the objectives of the substantial holding or takeover provisions of the *Corporations Act 2001* (**Act**).

1.2. However, ASIC shares the Panel's concerns with the potential use of equity derivatives to avoid important disclosure requirements and market protections and favours the view that, in principle:

(a) long positions under financial instruments that reference, or provide economic exposure equivalent to holding, a substantial number of voting shares or interests in a listed company, body or managed investment scheme should be disclosed to the market; and

(b) disclosure of such interests should be required in a similar way to interests forming part of a substantial holding under the substantial holding provisions in Part 6C.1 of the Act.[1]

[1] See also Treasury, 'Takeovers issues – Treasury Scoping Paper' (5 October 2012), which notes the current treatment of equity derivatives under the takeovers and substantial holding provisions as an area about which ASIC has previously expressed concerns.

1.3. While disclosure is presently required in some circumstances, in many cases the nature of the equity derivative means disclosure is not required—or is delayed.

1.4. Large equity derivative positions—whether settled for cash or physical—can influence both the market for, and control of, listed shares or interests via the inherent incentives they create for a counterparty to deal in, and maintain a holding of, underlying securities. There is a strong case that influence of this kind in relation to a substantial number of securities will often be sufficiently material and relevant to the market to warrant disclosure.

1.5. Market observations of the continued use of equity derivatives by persons with an apparent interest in influencing the outcome of a control transaction, negotiation or other affairs of an entity in a way that ultimately depends on a real or perceived ability to control voting or disposal of the underlying securities, further supports this view.

1.6. The substantial holding disclosure regimes of a number of comparable jurisdictions such as Hong Kong,[2] New Zealand,[3] Switzerland,[4] the United Kingdom[5] and various other EU countries,[6] currently take into account, and require disclosure of, interests under cash-settled equity swaps and other derivatives that do not include an express right or option to acquire underlying securities.

1.7. For these reasons, ASIC welcomes the Panel's proposed revisions to GN 20 in the interests of enhancing the transparency of Australia's financial markets.

2. Response to Consultation Paper Questions

1. Do you agree that the Panel should expect disclosure of all long positions over 5%? If not, what do you consider should be the Panel's policy position on disclosure of equity derivatives?

2.1. ASIC agrees with the Panel's proposal to indicate it expects all long positions under equity derivatives to be disclosed if the overall long position held equates to at least 5% or more of the voting rights in an entity—irrespective of whether a control transaction is considered to have commenced.

[2] *Securities and Futures Ordinance,* Cap. 571 (Hong Kong), ss311(2), 322(8)–(9) and 326(2).
[3] *Financial Markets Conduct Act 2013* (New Zealand), s275 and *Financial Markets Conduct Regulations 2014* (New Zealand), r132.
[4] Ordinance of the Swiss Financial Market Supervisory Authority on Financial Market Infrastructures and Market Conduct in Securities and Derivatives Trading of 3 December 2015 (CC 958.111), Articles 14 and 15.
[5] Financial Conduct Authority (UK), Disclosure Guidance and Transparency Rules (DTRs), DTR 5.3.1 made under the *Financial Services and Markets Act 2000* (UK), ss89A and 89B.
[6] Being those jurisdictions that have implemented Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 as amended by Directive 2013/50/EU of 22 October 2013: see Article 13(1).

2.2. GN 20 recognises that writers of equity derivatives have an economic incentive to hedge their position and to unwind any hedge upon the closing out of their position. Hedging, whilst not necessarily universal, will in many cases occur through the acquisition of the underlying securities by the writer.[7] Equity derivative positions referencing a substantial holding may be more likely to result in hedging of this kind given the greater exposure of the counterparty.

2.3. As noted in the revised draft GN 20, the entry into long equity derivative positions and the resulting incentive to hedge may impact the availability and the pricing of the underlying securities—which in turn may affect the acquisition of control of, or a substantial interest in, the relevant entity.[8]

2.4. ASIC agrees that these impacts on the market for an entity's securities are an important reason in favour of requiring disclosure—particularly in the context of a control transaction where the maintenance of an efficient, competitive and informed market is paramount. However, ASIC notes that the relevance to listed entity boards and investors of substantial long equity derivative positions is not necessarily limited to the effect of hedging activity on general market 'free-float' and trading.

2.5. The potential practical influence that the taker of a long equity derivative has over underlying securities acquired as a hedge (**Hedge Securities**) puts the taker in a unique position of proximity to the Hedge Securities—even in the absence of any express contractual right in relation to them. This position of influence itself is arguably also relevant to a market that has a legitimate interest in knowing not only when a person may be accumulating significant interests in an entity ahead of a potential control transaction, but also about the existence, dealings and interests of persons who may have a substantial influence over the entity's future direction: see ASIC Regulatory Guide 5 *Relevant interests and substantial holding notices* (**RG 5**) at RG 5.284—5.285.

2.6. The potential for a long equity derivative taker to materially influence Hedge Securities may manifest in a number of ways—for example:

(a) By maintaining the long position itself, a taker may exercise a degree of effective control over disposal of the Hedge Securities given the likely reluctance of the counterparty to reduce its exposure to the Hedge Securities unless and until the equity derivative is unwound. The resulting influence over the disposal of the holding may be sufficient to discourage or block a potential or proposed control transaction;

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[7] In some cases the acquisition of the underlying as a hedge by the writer may be a feature of the derivative: for example in the case of some 'contract for difference' (CFD) products operating on a direct market access model.

[8] Draft GN 20 (10 April 2019), paragraph 7.

(b) Where the equity derivative is cash-settled, the taker may take advantage of the commercial incentives that are created by the equity derivative, and within the control of the taker, to acquire Hedge Securities at a convenient time in the future:

(i) a sale of Hedge Securities by the writer to the taker in connection with unwinding the equity derivative position will often be the most convenient, low-risk and cost-effective way to dispose of the Hedge Shares. This is particularly so where the holding is large and/or the market for the underlying securities relatively illiquid. In the context of a control transaction a taker who is a bidder or acquirer may be the only practical buyer where the derivative is unwound at a point where control has passed;

(ii) as the taker will often be able to control when the equity derivative is unwound it has an informational and strategic advantage vis-a-vis the rest of the market in positioning itself to acquire the securities from the writer.[9] This includes, for example, the opportunity throughout the life of a cash-settled derivative to negotiate the addition of a physical settlement option; and

(iii) a writer in the business of offering equity derivative products may have an additional motivation to accommodate any request from the taker for physical settlement in recognition of the desirability of maintaining good relations with its client;[10]

(c) it is possible that the commercial circumstances created by the equity derivative arrangement may enable the taker to indirectly influence voting of the Hedge Securities. The writer may have a practice or policy that it abstains from voting Hedge Securities—effectively removing them from the voting pool and altering the power of remaining votes. Alternatively, a taker that is seeking to effect an outcome through a shareholder vote may have an expectation that Hedge Securities will be voted in a way that is consistent with the apparent objectives of the taker. The writer (which due to the equity derivative could, in effect, have little or no economic interest in the Hedge Securities or the entity in respect of which they are voting) may be influenced by this real or perceived expectation and vote in a way that is most conducive to maintaining future business with the client.

2.7. In principle, if it is accepted that disclosure is warranted for the purpose of ensuring an efficient, competitive and informed market where there is a control transaction on foot, it would seem there is a similar justification to require disclosure even when there is no control transaction given:

(a) such positions may impact whether a control transaction can, or is likely to, occur in the first place;

[9] See also Takeovers Panel, *Discussion Paper: Equity derivatives* (10 September 2007), [29]-[30].
[10] See eg *Ithaca (Custodians) Ltd v Perry Corporation* [2004] NZLR 731 at [63].

(b) one of the objectives of the substantial holding disclosure provisions is to provide an early warning to the market concerning the accumulation of interests that may lead to a control transaction in advance of the transaction (as well as relevant details of the acquisitions as they progress); and

(c) the influence and market impact resulting from the taking of such a substantial position will, in many cases, be of relevant informational value to the market irrespective of whether a control transaction eventuates having regard to:

   (i) the underlying objective of the substantial holding disclosure provisions of ensuring information is available to the market regarding the interests and dealings of persons who may have substantial influence over the entity and its future direction; and

   (ii) the broad definition, and anti-avoidance nature, of the relevant concepts currently used to determine when the substantial holding disclosure requirements are triggered.[11]

2. Do you agree with footnote 2? What further guidance (if any) do you think the Panel should provide in cases when a person obtains a long position of over 20%?

2.8. ASIC agrees with the position outlined in footnote 2.

2.9. The same rationale underlying the case for disclosure of a substantial long equity derivative position discussed in relation to Question 1 is relevant to considering whether the acquisition of the position itself is unacceptable due to the effect it has on:

(a) control, or potential control, of a listed body or scheme; or

(b) the acquisition of a substantial interest in the listed body or scheme (including the ultimate acquisition of any underlying securities held as a hedge).

2.10. Very large exposure via an equity derivative can, as a result of the influence of the long position taker, affect control of the issuer of the underlying securities. As such, even where entrance into an equity derivative position may not necessarily result in a contravention of the Act, the effect the derivative position has on the underlying securities may nonetheless undermine the objectives of the takeover provisions.

2.11. Similarly, the acquisition of a long position under an equity derivative at a time when a person is accumulating a potentially controlling stake in reliance on the exemptions in s611 may also give rise to unacceptable circumstances on the grounds that it undermines the relevant exemptions. For example:

[11] See eg RG 5 at RG 5.6–RG 5.8.

(a) a bidder who launches a bid with a direct holding of 20% and a long position under a cash-settled equity derivative referencing another 15% would potentially have, or be seen to have, a level of influence over the 15% which would factor into perceptions that the bid is more likely to be successful at the price offered. This may coerce some target holders into accepting at the bid price where they otherwise would not have—in turn enabling the bidder to offer a lower premium than might have been required to achieve control of the target; and[12]

(b) an investor who holds a 20% stake and has a long equity derivative position may be able to 'lock in' the price at which it makes future acquisitions in reliance on the creep exemption.[13]

2.12. ASIC recognises that some equity derivatives fall within a point of distinction between the takeover and substantial holding provisions. Under s609(6)[14] relevant interests in securities that would otherwise arise solely from listed options, listed call warrants or 'a right to acquire the securities given by a derivative' are excluded for the purposes of the takeover provisions (but not the substantial holding provisions)[15] prior to the obligation to make or take delivery of the securities.

2.13. While acknowledging the broad reference to derivatives that give a right to a security in s609(6), which may include many physically settled OTC equity derivatives, ASIC does not believe this should prevent the Panel from finding that the influence arising under such a derivative cannot give rise to unacceptable circumstances—consistent with the position in GN 20 at present.[16] This is particularly so given the increased scrutiny of the role of equity derivatives in control transactions since the provision was last amended.

2.14. ASIC also understands that the approach of taking into account long-equity derivative positions in determining whether the takeover threshold has been reached is consistent with the takeover regimes of the United Kingdom[17] and Singapore.[18]

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[12] In ASIC's experience it is likely that bidders already recognise the risk of unacceptable circumstances arising in such a situation and do not typically acquire interests through equity derivative positions in order to launch bids from a combined long position of greater than 20%.

[13] ASIC notes the Panel has previously expressed concerns regarding the potential effect on control of a future entitlement to securities that may be used to 'bank' creep entitlements (but do not give rise to a relevant interest prior to exercise): see eg *Bullseye Mining Limited 02* [2018] ATP 20 at [49] and *Merlin Diamonds Limited* [2016] ATP 18 at [121].

[14] As modified by ASIC Class Order [CO 13/526].

[15] See s671B(7)(a) and sub-paragraph (a)(ii)(A) of the definition of 'substantial holding' in s9 of the Act as modified by ASIC Class Order [CO 13/520].

[16] GN 20, paras 31-32.

[17] The Panel on Takeovers and Mergers, *The Takeover Code* (UK), definition of 'interests in securities', rule 5.1 and rule 9.1.

[18] Monetary Authority of Singapore, *Singapore Code on Take-overs and Mergers*, Note 16 to Rule 14.1.

3. Should there be more guidance provided in relation to what information is required to be disclosed (see paragraphs 11-17)? If yes, what guidance would assist? Should the taker of an equity derivative be expected to disclose the identity of the writer(s) of that derivative? Please explain.

2.15. Paragraph 12(a) of revised GN 20 provides that the Panel considers that only the identity of the taker is required to be disclosed. ASIC considers that there may be instances where disclosure of the identity of the writer should be made when disclosing a substantial long derivative position.

2.16. It is ultimately the actions of the writer in purchasing underlying securities which has the effect on the market with which the Panel's proposed disclosure requirements are concerned. Particularly in cases where the equity position is large the market should have access to information necessary to assess the impact of the incentive created by the long equity derivative position—including:

(a) what acquisitions in the underlying securities it may have already led the writer to make;[19] and

(b) whether it is unlikely to result in further market interventions by the writer (because the writer already has sufficient exposure to interests in underlying securities to cover the position) or its potential impact on the market is yet to play out.[20]

2.17. Without knowing the identity of the writer there is risk that in many cases the market will not know (but the taker will know) whether substantial holding disclosures made by the writer likely relate to the equity derivative position or not.

2.18. Disclosing the identity of the writer is also consistent with the requirements that apply where a long equity derivative position is related to the acquisition or disposal of a relevant interest in underlying securities and therefore attracts the operation of Part 6C.1. OTC equity derivative arrangements are typically recorded in a document that would identify the writer, along with other details of the equity derivative, which would otherwise generally be expected to accompany a substantial holding notice in such circumstances: s671B(4).[21]

[19] Which may be relevant, for example, for market observers and regulators in considering whether there may have be a breach of the Act or unacceptable circumstances. For example, it may be that acquisitions by the writer should be closely examined for the purposes of considering whether the requirements of, and principles underlying, the minimum bid price rule in s621(3) of the Act have been observed.
[20] The value of this information is also reflected in paragraph 11 of the draft GN 20 where the Panel notes the extent to which the counterparty has hedged should be disclosed to the extent it can be so that the market fully understands the nature of the taker's long position.
[21] ASIC's comments on the information that the Panel should require to be disclosed in GN 20 should not be taken to suggest that disclosure regarding an equity derivative arrangement limited to that information is necessarily sufficient where a disclosure obligation arises under Part 6C.1 of the Act. Reference should always be made to the requirements of the Act, the instructions in the prescribed forms and relevant ASIC guidance.

4. Are there any other changes you would make to the draft Guidance Note? Please explain.

Transition period

2.19. ASIC notes that the revised GN 20 does not indicate whether there will be any transition period following the Panel's decision whether to proceed with the foreshadowed amendments to the guidance note.

2.20. While the Panel's proposal has been available to the market since April, given the scope of the changes proposed, and the possibility that some market participants may wish to alter their positions in response to the new guidance note depending on the position ultimately adopted by the Panel, if the guidance note is issued in the near future it is possible that there are a number of affected persons who will not have had a chance to consider and/or come into compliance with the Panel's expectations at the time the guidance note commences.

2.21. ASIC suggests the Panel may wish to provide the market with a set transition period following publication of the new guidance note to allow time for the Panel's expectations to be considered and necessary disclosures to be made.

Other comments

2.22. ASIC notes that paragraph 16 of revised GN 20 provides that the Panel expects an entity will disclose any written notice it receives to the ASX.

2.23. Given that the requirements should apply to all listed bodies and managed investment schemes ASIC suggests that the Panel should consider amending this paragraph by removing the reference to "*ASX*" and providing that written notices must be disclosed to "each prescribed financial market operator on which the entity is listed".

3. Contact

3.1. ASIC would be happy to discuss the contents of this submission and any queries the Panel may have regarding the comments and suggestions made.

Yours sincerely,

Kim Demarte
Senior Specialist – Mergers & Acquisitions
Corporations
Australian Securities and Investments Commission

Submission made by Rod Halstead in his own capacity

Mr Rod Halstead
Level 15, 1 Bligh Street
SYDNEY NSW 2000

10 July 2019

Email

Mr Allan Bulman
Director
Takeovers Panel
Level 10, 63 Exhibition Street
MELBOURNE VIC 3000

takeovers@takeovers.gov.au

Dear Mr Bulman

Submission in response to Takeovers Panel Consultation Paper on Guidance Note 20 - Equity Derivatives

I welcome the opportunity to respond to the proposals and questions set out in the Takeovers Panel (**Panel**) Consultation Paper on the proposed rewrite of Guidance Note 20 relating to Equity Derivatives (**Consultation Paper**).[1]

Summary

I am supportive of the Panel's decision to revive for consultation, the issue that equity derivatives could be used in a way which undermines the policy of Chapter 6 of the Corporations Act 2001 (Cth) (**Corporations Act**)[2].

I share the Panel's concerns relating to the effects of equity derivatives and hedging on the "free float" of a company. It is common practice for writers of equity derivatives to take a hedge by acquiring the underlying entity's physical securities or by entering into another equity derivative with another party who may do so. This, together with the subsequent "unwinding" of the derivative affects the actual supply or "free float" of an entity's securities, unbeknown to the rest of the market that these securities are not actually free to be dealt with without restriction.

I also share the Panel's concern about how equity derivatives can be used in control or potential control transactions to blind-side the market, for example, by enabling a potential bidder to build a pre-bid stake in the target for a long period of time, unbeknown to the target and the rest of the market. The potential bidder may already have an interest in combination with existing holdings in the target via holdings of physical securities (less than a substantive shareholding) or equity derivatives which would not need to be disclosed to the market unless and until the derivatives were physically settled or a control intention arises.

Overall I support the proposed changes in the Consultation Paper as they clarify and strengthen the current position and expectations of the market through a greater transparency with respect to a listed entity's securities.

However, there are matters that require further consideration to enable effective implementation of the proposed changes. Firstly, the Panel will need to consider how it can effectively enforce the proposed changes and what remedies the Panel can order, particularly in situations outside of control transactions. Secondly, the Consultation Paper has been written to predominantly contemplate disclosure of bespoke transactions, this raises compliance issues for investment management entities such as those who frequently enter into derivative transaction. These considerations are discussed further below.

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[1] This submission is made by Rod Halstead in his own capacity.

[2] All subsequent statutory references to sections and chapters are to the Corporations Act.

1. **Do you agree that the Panel should expect disclosure of all long positions over 5%? If not, what do you consider should be the Panel's policy position on disclosure of equity derivatives?**

I agree that disclosure of all long positions over 5% endorses best market practice and will result in a more informed market. However, I have reservations as to how the proposed changes to Guidance Note as outlined in the Consultation Paper can be effectively enforced, and what remedies can be provided in situations outside of control transactions together with the compliance difficulties and practical implications for some investors.

Enforcement

The Panel contemplates that the onus would be on the taker of the derivative to disclose to the entity who's securities underlie the derivative, and then for that entity to tell ASX. I query how the Panel might enforce this under the current legislative regime. Under the current regime, disclosure to the market is entirely dependent on notice being promptly given by the entity to ASX. The investor who holds a derivative cannot lodge a notice directly on the entity's ASX announcement platform unless the law or ASX Listing Rules permit it to do so. The Panel may consider whether the ASX should introduce a Listing Rule to address this, similar to Listing Rule 3.19A.

Enforcement relies on an interested party making an application to the Panel. If an investor does not disclose a long position or improperly complies with the disclosure requirements, then the Panel would be unable to take action, without an interested party first making an application to the Panel under the usual Panel process. As the Panel is aware, this would require the applicant to provide material to the Panel which is of sufficient veracity to enable a Sitting Panel to determine that the circumstances are such that the Panel's intervention is required. It is likely that this would include the need to demonstrate that there are underlying physical securities acquired as a consequence of the derivative by way of a hedge. Under the current regime, ASIC is likely to be the only entity who will be able to present this material to a Sitting Panel either through an exercise of its investigatory powers or otherwise. The mere acquisition of an economic interest through a derivative is unlikely to provide a basis for a declaration of unacceptable circumstances in the current legislative framework.

Under section 657A, circumstances are unacceptable having regard to the effect of the circumstances on the control, or potential control of the company, or on the acquisition or proposed acquisition of a substantial interest, or if there has been a contravention of a provision in Chapters 6, 6A, 6B or 6C, or are otherwise unacceptable having regard to the purposes of Chapter 6, as set out in section 602. These purposes are fundamentally focused on circumstances that relate to a change of control or the acquisition of a substantial interest. It remains uncertain whether a mere failure to disclose an economic interest arising outside of a control transaction, or a transaction pursuant to which a person proposes to acquire a substantial interest in securities, could give rise to unacceptable circumstances in the context contemplated in section 657A.

Remedy

It is unsettled how the Panel can remedy a mere failure to disclose. The Panel may only order remedies following a declaration of unacceptable circumstances (in respect of which, see my comments above). If in the circumstances, the Panel does make a declaration of unacceptable circumstances, the most likely and potentially only order that could be made, would be one requiring disclosure.

It is likely to be challenging for the Panel to attempt to make an order that impacts in any way on any physical securities held (for example by the writer of a derivative as a hedge) in the absence of circumstances that demonstrate a direct participation by that person (or, in the case of multiple writers, those persons) in the circumstances which have been found to be unacceptable. The writing of a derivative and the acquisition of a hedge should not be sufficient for that purpose.

Compliance

I envisage that many large scale global investors will express concerns on how they can comply with the disclosure requirements proposed by the Consultation Paper. For example, the level of detail required in paragraph 12 and method of disclosure proposed by paragraph 14, suggests careful and manual entry, and appears to be based on bespoke transactions. This would not be feasible for many large global investment management firms who conduct large volumes of transactions every day and have automated systems that directly communicate substantial holding notices to ASX. Complying with the requirements proposed by the Consultation Paper means additional administrative burdens and costs and the potential investment and implementation of new systems.

While such investors are likely to seek to co-operate with Panel initiatives to improve market transparency, if the implementation is too costly or simply cannot be practically complied with, such investors may ask themselves whether the Guidance is jurisdictional overreach by the Panel (for the reasons articulated above) and elect to ignore the Guidance unless the positions themselves (as a result of the particular surrounding circumstances) pose a real risk of amounting to unacceptable circumstances.

In this regard, it may be appropriate for the Panel to consider the nature of disclosures of equity derivative positions that are required to be made in larger capital markets internationally so as to endeavour to remain in step with relevant "best practice" disclosure elsewhere.

Overall comments

It is important to remember that the predominant purpose of Chapter 6 is to promote an efficient, competitive and informed market in relation to the acquisition of control. I suggest that considerable additional thought will be required to ensure that Guidance Note 20 establishes a regime which is readily enforceable by the Panel and involves the imposition of appropriate remedies. I comment later on whether legislative intervention would be more appropriate.

2. **Do you agree with footnote 2? What further guidance (if any) do you think the Panel should provide in cases when a person obtains a long position of over 20%?**

If the question contemplates the position of whether the acquisition of economic interests which represent in excess of 20% of the securities on issue should be unacceptable, that would represent a significant change in the policy underlying Chapter 6, which is clearly focused on matters relating to the control of a company or the acquisition of a substantial physical interest in securities.

The taking of a long position in certain equity derivative is specifically excluded under section 609 as a situation not giving rise to a relevant interest until an obligation to make or take the delivery of the securities arises.

The proposition that the acquisition of economic interests without more, such as an impact on control, is a change in the underlying policy which would require legislative intervention. Having said that, it should remembered that the underlying policy of Chapter 6 is based on the Eggleston Principles which were formulated in 1969 by the Company Law Advisory Committee. It may be that it is time for these principles to be reviewed in light of current market practices.

3. **Should there be more guidance provided in relation to what information is required to be disclosed (see paragraphs 11-17)? If yes, what guidance would assist? Should the taker of an equity derivative be expected to disclose the identity of the writer(s) of that derivative? Please explain.**

See our earlier comments with respect to the issues which arises as a consequence of disclosure which the Guidance Note presently contemplates.

I recommend the Panel consults widely with bodies representing investors in derivatives to ensure that the information which is required to be disclosed is appropriate and does not impose an unacceptable compliance and regulatory burden on participants in the market for equity derivatives.

Clearly the Panel would not seek a result which discourages trading in derivative securities.

4. Are there any other changes you would make to the draft Guidance Note? Please explain.

I suggest that paragraph 15 should be amended to better reflect the wording of section 671B(6), such that the words "of the relevant financial market after becoming aware of the information" is included after "trading day" in the Consultant Paper.

Conclusion

Overall, I remain supportive of the objective of securing additional disclosure which underlies the revised Guidance Note. However as indicated above, I believe that there are a number of issues that need to be considered in the implementation of the Guidance Note, in particular so as to ensure that it does not unnecessarily interfere with the conduct of an active market in derivative securities.

Finally I believe that is likely that legislative intervention will be required to address the difficulties identified above particularly in relation to enforcement. The Panel should be encouraged to write to the Treasurer pointing out the unsatisfactory state of the law in this regard and request that the Treasurer require Treasury Officers give this matter urgent attention so that appropriate legislation can be introduced.

I trust that these observations will be useful.

Please contact me if you require any further information or clarification.

Yours sincerely

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Submission by Blackrock

From:	Gleeson, Maureen
To:	Takeovers
Cc:	+APAC RED Consultations
Subject:	Takeover Panel's Consultation Paper dated 10 April 2019 on its proposed revised Guidance Note 20 on Equity Derivatives
Date:	Friday, 12 July 2019 5:51:05 PM

Dear Sir or Madam,

BLACKROCK, INC. AND ITS DIRECT AND INDIRECT SUBSIDIARIES ("BLACKROCK") ARE GRATEFUL FOR THE OPPORTUNITY TO COMMENT IN RESPONSE TO THE TAKEOVER PANEL'S CONSULTATION PAPER DATED 10 APRIL 2019 IN RELATION TO ITS PROPOSED REVISED GUIDANCE NOTE 20 ON EQUITY DERIVATIVES ("GN 20").

BLACKROCK IS A LEADER IN INVESTMENT MANAGEMENT, RISK MANAGEMENT AND ADVISORY SERVICES FOR INSTITUTIONAL AND RETAIL CLIENTS WORLDWIDE. AS AT 31 MARCH 2019, BLACKROCK'S AUM WAS USD 6.515 TRILLION ACROSS EQUITY, FIXED INCOME, CASH MANAGEMENT, ALTERNATIVE INVESTMENT, REAL ESTATE AND ADVISORY STRATEGIES. BLACKROCK HELPS CLIENTS MEET THEIR GOALS AND OVERCOME CHALLENGES WITH A RANGE OF PRODUCTS THAT INCLUDE SEPARATE ACCOUNTS, MUTUAL FUNDS, ISHARES® (EXCHANGE-TRADED FUNDS), AND OTHER POOLED INVESTMENT VEHICLES. BLACKROCK ALSO OFFERS RISK MANAGEMENT, ADVISORY AND ENTERPRISE INVESTMENT SYSTEM SERVICES TO A BROAD BASE OF INSTITUTIONAL INVESTORS THROUGH BLACKROCK SOLUTIONS®. HEADQUARTERED IN NEW YORK CITY, AS OF 31 MARCH 2019, THE FIRM HAD APPROXIMATELY 14,700 EMPLOYEES IN MORE THAN 30 COUNTRIES AND A MAJOR PRESENCE IN KEY GLOBAL MARKETS, INCLUDING NORTH AND SOUTH AMERICA, EUROPE, ASIA, AUSTRALIA AND THE MIDDLE EAST AND AFRICA.

BlackRock understands that the Takeovers Panel (**Panel**) proposes to rewrite GN 20 in relation to providing guidance on the long disclosure of equity derivatives. BlackRock has seen the operation of disclosure across multiple jurisdictions and supports full disclosure of long positions in equity derivatives during a controlled transaction or takeover but does not support the creation of a further disclosure regime in relation to equity derivatives to run alongside the current Substantial Shareholder disclosure regime regardless of whether a takeover offer period is currently under way or not.

In response to the Panel's queries, in particular:

1. **Do you agree that the Panel should expect disclosure of all long positions over 5%?**

   As a global asset manager, we note the share disclosure obligations in Australia should remain consistent with those of other jurisdictions. We are supportive of any measure to increase market transparency but not to the extent this creates an unreasonable administrative burden in Australia which would be out of line with other comparable jurisdictions and could undermine the Australian Government's efforts to enhance the competitive position of Australian financial markets. Furthermore, we would point out that equity disclosure regimes are usually meant to give the market and regulator an early warning of any person accumulating a position that could eventually give them the ability to exert influence or control the issuer. Such influence or control takes place through the exercise of voting rights so the calculation of holdings for ordinary equity disclosure purposes should not include any derivatives which do not confer voting control in the relevant issuer.

   BlackRock is, however, supportive of enhanced disclosures of transactions during a takeover offer period. In the response to question 4 below, we set out the additional information that could reasonably be provided to the market in line with the accelerated disclosures of dealings during takeovers involving Hong Kong and Singapore issuers.

***Timing of disclosure* –** We note the expectation of the Panel that all long positions over 5% should be disclosed (irrespective of whether there is a control transaction). The Panel appears to be proposing an ongoing disclosure obligation to run alongside the current Substantial Shareholder disclosures requirements regardless of whether any takeover offer period has been announced. We are unaware of any other jurisdiction where there is such an ongoing disclosure requirement. While full accelerated disclosure of all trades during a takeover offer period is required in certain other jurisdictions such as Hong Kong and Singapore, the Panel has not explained why there is currently any deficiency from a takeover perspective in disclosures currently required outside of a control transaction and why the existing substantial shareholder regime under Part 6C.1 of the *Corporations Act 2001* (“**Corporations Act”**) does not provide sufficient ongoing disclosure to the market.

BlackRock would support the Panel’s proposal for enhanced and comprehensive disclosure of all long positions during a control transaction which would enhance market transparency and be consistent with the requirements in other comparable jurisdictions. BlackRock does not, however, support the creation of an additional long disclosure regime, outside of any control transaction or takeover offer period, to run in parallel with the existing Substantial Shareholder disclosure regime.

***Administrative burden* –** It appears that the Panel’s proposed disclosure requirements would operate independently of the Substantial Shareholding disclosure regime under Part 6C.1 of the Corporations Act. This means that the current regime with which the industry complies by lodging substantial holding notices will need to be amended at the very lease and perhaps even rewritten given the Panel’s new disclosure requirements could be triggered in the absence of any Substantial Shareholding disclosure obligation being triggered under the Corporations Act. Market participants will have to develop monitoring and disclosure infrastructure necessary to report this additional information to issuers and the market. Unlike the substantial holder regime, there will be no prescribed format for such disclosures which is likely to result in inconsistencies in disclosures which could cause market confusion.

As one example of the administrative challenge GN20 poses, it is proposed that the taker of the derivative would disclose the underlying securities of the derivative to the issuer. Unlike statutory substantial holding notices, Blackrock would not be able lodge this new notice directly on the entity's ASX announcement platform. Blackrock's systems are, however, built to communicate with identifiable market operator or regulator platforms (such as ASX) and thus manage its disclosure obligations in respect of holdings in a large number of listed entities. For example, BlackRock currently has substantial holding notices lodged with ASX in respect of over 70 ASX listed issuers. Blackrock does not have any process to systematically collect and maintain the relevant contact details of every Australian issuer to enable it to lodge these new notices directly with issuers when the need arises.

Please see our response to question three below in relation to the information required to be disclosed. The administrative burden and substantial cost of building the required systems to monitor and disclose this additional information on an ongoing basis would greatly outweigh any benefit derived from such additional disclosures outside of any takeover offer period.

2. **Do you agree with footnote 2? What further guidance (if any) do you think the Panel should provide in cases when a person obtains a long position of**

over 20%?

Given GN 20 requires disclosure outside of a takeover offer period, BlackRock would welcome further guidance as to how disclosures during the period before the takeover would be viewed in a determination of unacceptable circumstances as well as what action could be taken by the Panel, especially in relation a person who is not already involved in an application before the Panel.

3. **Should there be more guidance provided in relation to what information is required to be disclosed (see paragraphs 11-17)? If yes, what guidance would assist? Should the taker of an equity derivative be expected to disclose the identity of the writer(s) of that derivative? Please explain.**

As a global asset manager with hundreds of funds and accounts under management, BlackRock carries out a substantial volume of trades and it will not therefore be possible, from a practical perspective, to provide the level of detail required under the proposed paragraph 12 of GN 20 in relation to each derivative transaction (e.g. identity of the taker, price and entry date). Short and long equity derivative positions can be disclosed on behalf of the whole BlackRock group but it would not be reasonably practicable to track each short equity derivative to the long position that it is designed to offset.

4. **Are there any other changes you would make to the draft Guidance Note? Please explain.**

Instead of the proposed additional disclosure requirements, BlackRock would be supportive of enhanced disclosures of transactions during a takeover offer period in line with the Hong Kong and Singapore dealings disclosure regimes described below:

Hong Kong:

In Hong Kong, any person who owns or controls 5% or more of any class of securities of an offeree (or, in a securities exchange offer, the offeror) must disclose any dealings (however small) during the offer period in securities of the offeree (or, in the case of a securities exchange offer, the offeror or a company whose securities are being offered as consideration for the offer).

A list of offeror and offeree companies within scope is publicly available on the website of the Securities and Futures Commission. Disclosure is only required to be made to the Securities and Futures Commission as opposed to the offeror and the offeree and their financial advisers. There are no thresholds for disclosures under Rule 22. Any dealing in the following "relevant securities" (however small) must be disclosed:

(i) Securities of the offeree company which are being offered for or which carry voting rights;

(ii) Equity share capital of the offeree company and, in a securities exchange offer only, of an offeror or of a company the securities of which are to be offered as consideration for the offer (as the case may be);

(iii) Securities of an offeror or of a company the securities of which are to be offered as consideration for the offer (as the case may be), which carry the same or substantially the same rights as any to be issued as consideration for the offer;

(iv) Securities carrying conversion or subscription rights into any of the foregoing; and

(v) Options and derivatives in respect of any of the foregoing.

The taking, granting, exercising, lapsing or closing out of an option (including a traded option contract) in respect of any of the foregoing or the exercise or conversion of any security under (iv) above whether in respect of new or existing securities and the acquisition of, entering into, closing out, exercise (by either party) of any rights under, or issue or variation of, a derivative is regarded as a dealing in relevant securities.

"Derivative" under the Takeovers Code "includes any financial product whose value in whole or in part is determined directly or indirectly by reference to the price of an underlying security or securities and which does not include the possibility of delivery of such underlying security or securities". Dealings in both cash-settled and physically-settled derivatives must therefore be disclosed under this regime.

Singapore:

In Singapore, there is an enhanced disclosure regime for persons connected to the bidder or target, including 'associates' which normally include holders of 5% or more of the equity share capital of the offeror company or the offeree company. Listed companies which are subject to a takeover would generally be required to make an announcement under the SGX-ST Listing Manual. The announcements of such takeovers can normally be found at the SGX-ST's webpage.

Any dealings, acquisitions or disposals of equity shares, convertible preference shares and any type of derivative transactions (except for derivatives referenced to a basket or index of securities where certain conditions are fulfilled) by the "associates" for their own accounts or for the accounts of discretionary investment clients during the relevant offer period must be publicly disclosed to the SGX-ST, the Securities Industry Council and the press no later than 12 noon on the next dealing day.

BlackRock would welcome the opportunity to engage further with the Panel in this regard. Please do not hesitate to contact Maureen Gleeson, Director, BlackRock at Maureen.gleeson@blackrock.com or Tel: +852 39032829 should you require any further information or wish to discuss this matter further.

Best regards,

Maureen

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Submission by Law Council

Law Council
OF AUSTRALIA

Business Law Section

19 July 2019

Allan Bulman, Director
Takeovers Panel
Level 10
63 Exhibition Street
MELBOURNE VIC 3000

By email: takeovers@takeovers.gov.au

Dear Mr Bulman

Submission in response to Consultation Paper on proposed rewrite of Guidance Note 20 – Equity Derivatives

The Corporations Law Committee of the Business Law Section of the Law Council of Australia (**Committee**) welcomes the opportunity to provide this submission to the Takeovers Panel (**Panel**) on the Consultation Paper on Guidance Note 20 – Equity Derivatives (**Consultation Paper**).

Summary

While acknowledging a diversity of views in the market and amongst its members, the Committee is generally supportive of the Panel's approach to equity derivatives set out in the Consultation Paper.

The Committee agrees with the Panel that disclosure of all long positions in equity derivatives (aggregated with any relevant interest in the underlying voting shares) over 5% will promote an efficient, competitive and informed market, in line with the purposes of Chapter 6 of the *Corporations Act 2001* (Cth) (**Corporations Act**).

However, the Committee submits that the position of the Panel outlined in the draft Guidance Note is an expansion of the position set out in the current issue of Guidance Note 20, and that the market would benefit from the changes being more clearly enunciated in the final version of Guidance Note 20.

We set out below the Committee's responses to the specific questions posed by the Panel in the Consultation Paper, together with suggestions regarding possible clarifications to the draft Guidance Note. Even if the Panel is unable to accommodate the views expressed by the Committee in these specific responses, the Committee overall remains supportive of the Panel issuing the draft Guidance Note.

1. Do you agree that the Panel should expect disclosure of all long positions over 5%? If not, what do you consider should be the Panel's policy position on disclosure of equity derivatives?

There is a general consensus within the Committee that the Panel should expect disclosure of all aggregated long positions over 5%.

Application of the substantial holding regime to equity derivatives

The Committee agrees that the substantial holding notice regime generally does not apply to equity derivatives that are compulsorily cash-settled if:

- the writer and the taker are not associates; and
- the taker does not acquire a relevant interest in any securities in which the writer has a relevant interest (including as a result of section 608(8) of the Corporations Act).

Practical effect of settlement of an equity derivative

In our experience, the writer of a cash-settled equity derivative is not ordinarily contractually obliged by the taker to dispose of the underlying securities upon settlement of the derivative (in contrast, it is common for the taker explicitly to acknowledge that the writer is not required to hedge its position). However, again in our experience, the writers of a cash-settled equity derivative do often hedge all or most of their position under the derivative by acquiring the underlying securities.

Further, as the draft Guidance Note acknowledges at paragraph 6, the writer does have an economic incentive to unwind the hedge and dispose of the underlying securities on settlement. The taker therefore may seek to acquire securities on-market at that time.

The Committee considers it material from a policy position that, whether or not a taker acquires the underlying securities from the writer on settlement, the taker will have effectively “locked in” an effective purchase price for the parcel of underlying securities to which that equity derivative is referable. After taking into account the cash flows on the unwind of the derivative, a taker will be able to acquire securities for a net value broadly equal to the strike price of the derivative, even if the share price has increased following entry into the derivative. A taker has an economic interest – even if it does not have a relevant interest – in the underlying securities.

Irrespective of what occurs on settlement of an equity derivative, the majority of the Committee considers that the way in which cash-settled equity derivatives operate means that entry into, and the material terms of, equity derivatives should be disclosed to the market, to facilitate an efficient, competitive and informed market for control of voting securities. The majority of the Committee therefore considers that the Panel should expect disclosure of all aggregated long positions over 5%, regardless of whether the position is held directly through a relevant interest in “securities” (including a physical derivative) or through a cash-settled equity derivative. The Committee notes that this would be consistent with the disclosure positions adopted in analogous jurisdictions, such as the United Kingdom, Hong Kong and New Zealand.

Enunciation of the Panel’s updated policy position

The Committee unanimously considers that, if the Panel’s policy position is that the Panel expects disclosure of all aggregated long positions over 5%, then this should be clearly stated in the revised issue of Guidance Note 20. This would be helpful in promoting consistency in disclosure and to achieve the purposes set out in section 602 of the Corporations Act, given current market practice and existing guidance.

In this regard, the Committee notes that the current issue of Guidance Note 20 (at paragraph 9) states:

> "*Where there is a control transaction, the Panel would expect that all long positions which already exist, or which are created, are disclosed unless they are under a notional 5%*" (emphasis added)

The Committee considers that the Consultation Paper reflects an "updated" policy position of the Panel, which differs significantly to the position set out in the current issue of Guidance Note 20. The Committee further considers that if the Panel's "updated" policy position is adopted through the issue of a revised version of Guidance Note 20, then this change should be made clearer and more explicitly in the text of the revised version of Guidance Note 20, for example by amending paragraph 2 so that it states:

> "*If an equity derivative gives the taker a relevant interest in any underlying securities, the disclosure regime in Chapter 6C applies. This note applies to equity derivatives that may not require disclosure under Chapter 6C, and applies irrespective of whether a control transaction has commenced.*" (footnotes omitted)

The Committee considers that the proposed Guidance Note 20 is an important opportunity for the Panel to state its position that the guidance applies to disclosure of equity derivatives outside of a control transaction occurring, and that this change would provide greater clarity to the market and thereby facilitate increased consistency in market practice.

2. Do you agree with footnote 2? What further guidance (if any) do you think the Panel should provide in cases when a person obtains a long position of over 20%?

There is a general consensus within the Committee that the text of footnote 2 should be retained. However, the general consensus of the Committee is also that, given the significance of this guidance, it should be given greater prominence and included in the body of Guidance Note 20, not as a footnote.

The Committee notes that section 606 of the Corporations Act prohibits a person from acquiring a relevant interest in issued voting shares if (inter alia) that acquisition will result in a person's voting power increasing from 20% or below to more than 20%, or from a starting point that is above 20% and below 90%, unless one of the exceptions set out in section 611 of the Corporations Act applies.

However, as discussed in section 1 of this submission, in the experience of Committee members, writers of cash-settled equity derivatives often hedge their position by acquiring some or all of the underlying securities, and have an economic incentive to unwind the hedge and dispose of the underlying securities on settlement. Further, takers may seek to acquire securities on-market at the time of settlement.

In this context, the Committee could envisage circumstances in which a person holds an equity derivative (or a combination of securities and equity derivatives) in an entity and, due to the number of underlying securities of that entity to which the equity derivative is referable (either alone or in aggregate with the number of securities in which that person holds a physical position), the person is interested in greater than 20% of securities in that entity. For example, if a person held a physical position of 19% of the voting shares of an entity, and took a cash-settled equity derivative in relation to 10% of the voting shares of that entity.

The Committee agrees with the Panel (at paragraph 7 of the draft Guidance Note) that this could affect:

- control or potential control of the entity;
- the acquisition or proposed acquisition of a substantial interest in the entity; or
- the efficient, competitive and informed market for control of the entity's voting securities,

contrary to the purposes of Chapter 6 of the Corporations Act and the other stated policy positions of the Panel.

The majority of the Committee therefore agrees with the Panel's position that the acquisition of an aggregate long position that would contravene section 606 of the Corporations Act if it were comprised entirely of a physical holding may give rise to unacceptable circumstances (even if the acquisition does not result in a person acquiring a relevant interest in contravention of section 606 of the Corporations Act).

The Committee considers that this position is a significant departure from the position expressed in the current issue of Guidance Note 20, and is of sufficient import, that if the text of footnote 2 is retained by the Panel then this text should be set out in the body of Guidance Note 20, not in a footnote.

The Committee discussed at length whether, if the Panel retains the text of footnote 2, then the Panel should provide examples of circumstances arising from the acquisition of a long position that may (or may not) give rise to unacceptable circumstances. One of the examples discussed at length by the Panel was that members of the Committee would expect that the acquisition of a long position under one of the exceptions set out in section 611 of the Corporations Act (e.g. Item 9), as if the long position was comprised entirely of a physical holding, would be unlikely to give rise to unacceptable circumstances.

The risk is that, without examples, market participants could not be properly advised as to how to ensure that they do not take a position that may give rise to unacceptable circumstances, in which case footnote 2 could have the effect of being a de facto prohibition.

The Committee considers that it would assist the market if the Panel provided examples of, or further guidance regarding, the situations in which the acquisition of an aggregate long position of over 20% is likely to give rise to unacceptable circumstances. However, the Committee acknowledges that it would be difficult for the Panel to provide examples while keeping the guidance concise. The Committee further acknowledges that whether the acquisition of an aggregate long position of over 20% will give rise to unacceptable circumstances will need to be considered by the Panel on a principled, case-by-case basis. If the Panel does not provide examples of situations in which the acquisition of an aggregate long position of over 20% is likely to give rise to unacceptable circumstances, the Committee would suggest that the Panel add a further sentence after the text of footnote 2, which states "*The Panel will consider whether such an acquisition has given rise to unacceptable circumstances on a case-by-case basis*".

3. Should there be more guidance provided in relation to what information is required to be disclosed (see paragraphs 11-17)? If yes, what guidance would assist? Should the taker of an equity derivative be expected to disclose the identity of the writer(s) of that derivative?

The Committee considers that the guidance in paragraphs 11-17 regarding the information to be disclosed will be helpful to market participants. The Committee has the following comments on these paragraphs:

- Paragraph 12(i) should be amended by replacing the words "physical positions" with the words "long physical or other equity derivative positions" in recognition that derivative positions may be offset against other derivative positions.
- It would be useful for the Panel to clarify, at paragraph 13, whether the swap confirm (as opposed to the standard ISDA master) is to be attached to the notice. The Committee notes that there are mixed views amongst market participants regarding the disclosure of this document.
- The majority of Committee members do not consider that disclosure of the identity of the writer(s) of the derivative would necessarily assist in informing the market, and accordingly the Committee does not consider that the taker should be expected to disclose this information.

4. Are there any other changes you would make to the draft Guidance Note? Please explain.

Apart from the changes discussed above, the Committee would also suggest that the Panel makes one change to footnote 4. Footnote 4 currently refers market participants to the factors noted in *Tribune Resources Limited* [2018] ATP 18 and *Auris Minerals Limited* [2018] ATL 7. The Committee would recommend the Panel consider expressly enunciating those factors in footnote 4, as this would be more helpful to market participants. The Panel may wish to consider enunciating these in the body of the Guidance Note.

The Committee is otherwise generally supportive of the draft Guidance Note.

I trust these observations are of assistance.

Please contact Shannon Finch, Chair of the Corporations Committee at shannonfinch@jonesday.com or on +61 428 894 002, or David Friedlander at David.Friedlander@au.kwm.com or on +61 2 9296 2444, if you require further information or clarification.

Yours sincerely,

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