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24 April 2008

ASX Regulatory & Public Policy Unit  
Level 7, 20 Bridge Street  
SYDNEY NSW 2000

Dear Sir/Madam

## **ASX CONSULTATION PAPER ON SHORT SELLING**

The Australasian Investor Relations Association would like to thank the ASX for the opportunity to comment on its consultation on short selling.

The Australasian Investor Relations Association (AIRA) was formed with the object of advancing the awareness of and best practice in investor relations in Australasia and thereby improving the relationship between listed entities and the investment community. Among other aims, it seeks to act as a united voice for the investor relations community, in areas advancing professional standards, including in best practice disclosure. AIRA's 110 corporate members represent approximately two-thirds of the market capitalization listed on ASX.

We welcome the fact that ASX is consulting the market on short selling at the present time, in light of recent controversial events. AIRA members feel strongly that changes in existing regulations are urgently needed, whether these are enacted through changes in ASX rules, and/or through changes to the Corporations Act.

The current absence of transparency in "naked" or uncovered short selling transactions (which we understand to represent the majority of total short selling) is of great concern to ASX listed companies and to their investor relations (IR) teams, whose key task is to engage with those interested in the company. Directors of companies look to their in-house IR team to provide analysis of who owns – or can influence – the company's shares. With the huge – and controversial – increase in short selling and the related stock lending, up to 40% of a company's issued capital may be on loan at any given moment. With an unknown proportion of this lending activity being related to (invisible) short selling, this IR task has become almost impossible.

AIRA and its members fully support the principles of transparency and the regulations that underpin it. Australian and New Zealand listed companies have been subject to a hugely changed regime in the last few years, with vast tracts of new regulation affecting companies. This has led to substantially increased compliance costs.

The members of AIRA believe therefore that the same concepts and principles should apply equally to brokers and investors. Companies feel strongly that they – and the wider market – should have an unrestricted right to know and a clear line of sight as to who owns or has influence over their shares.

The increased use of derivative instruments, the practice of short selling and the increase in volatility, has made it more difficult for listed entities to comply with their continuous disclosure obligations.

AIRA considers that short selling has a role to play in creating an efficient market place, providing liquidity, driving down overpriced securities, providing top quality research and generally increasing the efficiency of price formation.

**However AIRA believes that *naked* short selling detracts from the advantages above, and should be outlawed.** Selling shares they do not own, with no guarantee that the stock can be delivered in time for proper settlement, provides manipulators with tools to force stock prices down without regard for normal stock supply/demand patterns.

It is noteworthy that other major markets have means of controlling naked short selling. In the US, it is prohibited for brokers to arrange a sale without having the necessary stock to deliver. This is in the process of being reinforced through SEC Regulation SHO, by requiring the same of brokers' clients, and by establishing penalties.

In the UK, naked short sales are controlled through transparency. Also, through the "buy in" procedures if a transaction for guaranteed delivery does not settle, the buyer can submit a "buy-in" request to the Exchange, who will then buy in the securities.

A further broad concern is in voting. The growth of activism is well documented, and companies put a lot of effort into ensuring the maximum participation in votes. AIRA members are concerned about the emerging international practice known as 'empty voting', where investors borrow a companies shares and then vote to influence.

If the lending investor is not aware that their stock has been lent out, they may have problems voting. Custodians may not be able to return the stock in time for the vote, and in the absence of instructions, brokers may simply abstain. And of course, speculators have been known to borrow stock to vote it in line with their investment strategy – not necessarily in line with the best interests of the company. There may also be double counting of votes.

As a consequence, investor relations managers seeking to build investor relationships, especially with a significant vote approaching, find it difficult to judge voting intentions.

## SUMMARY

AIRA would like to see a changed market framework.

1. The increased use of derivative instruments, the practice of covered and uncovered short selling and the increase in market volatility, has made it more difficult for listed entities to comply with their continuous disclosure obligations. AIRA believes ASX should reintroduce the disclosure of broker identification codes on an-intra day basis.
2. AIRA is a strong believer in the principle of transparency of market information. All participants in the market (issuers, brokers, investors) should be able to see the true level of short selling that is occurring in the market.

AIRA therefore supports the notion that clients borrowing securities should be required by law to reveal to the lenders that they are shorting the stock. This information should in turn be provided to CHESSE.

3. In parallel, AIRA supports the ASX option that CHESSE should publish stock lending data as a proxy for short selling. (We note that this was the conclusion of the UK's FSA consultation in 2003, limited value notwithstanding). It was implemented in late 2003.
4. AIRA supports proposed changes to the Corporations Act, clarifying the definition of short selling to include covered short selling, and including cash settled derivatives in the definition of relevant interest for the purposes of Section 672 of the Corporations Act, and hence subject to proactive disclosure enquiries by the company.
5. "Naked" or uncovered short selling should be outlawed. Brokers' clients should be obliged to ensure that they can deliver the stock for settlement.
6. As noted above, AIRA supports the process of short selling for financial purposes. So, if the exclusive reason for the borrower is ownership of the share for settlement, then we would encourage a change in the rules stating that voting rights of lent stock (along with dividends and other adherent rights) continue to reside with the lender. This may require an amendment to the standard securities lending agreement.
7. Finally, AIRA would encourage regulators to monitor and then punish those distributing negative financial rumours as market abuse. Systems should be able to identify beneficiaries of short positions prior to movement.

Thank you again for the opportunity to comment; we are happy to provide any clarifications needed.

Yours sincerely,



Ian Matheson  
Chief Executive officer

## ANSWERS TO THE SPECIFIC QUESTIONS

### 1. *The two alternative short-term approaches considered by ASX, and the reasons provided for not proceeding with these options.*

As noted above, AIRA believes that clients borrowing securities should reveal to the lenders that they are shorting the stock. This information should in turn be published to the market through CHESSE.

### 2. *What information should be included in the daily short sale report submitted to ASX and what detailed guidance should ASX provide on the calculation of that information to ensure uniformity of reporting?*

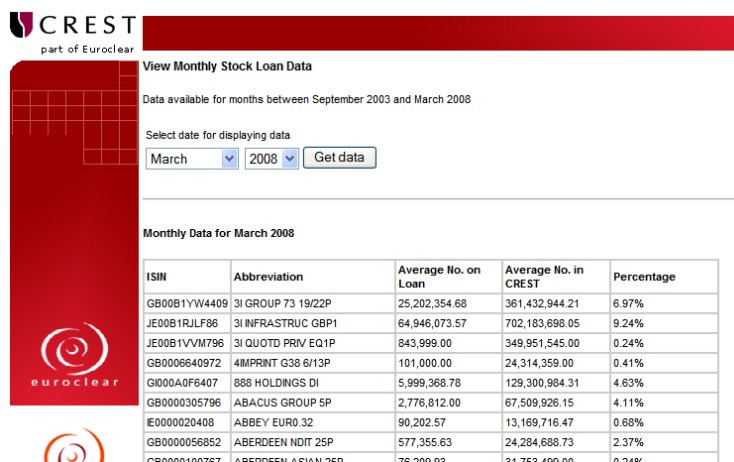
As an example, here is the detail from a short interest report issued by NASDAQ.

#### Microsoft Corporation - Common Stock

Settlement Date	Short Interest	Percent Change	Average Daily Share Volume	Days to Cover
03/14/2008	123,090,091	6.37	87,966,979	1.40
02/29/2008	115,720,569	3.04	97,863,725	1.18
02/15/2008	112,304,066	25.21	131,368,801	1.00
01/31/2008	89,692,603	(16.38)	106,511,001	1.00
01/15/2008	107,267,300	(4.33)	66,065,066	1.62
12/31/2007	112,119,787	(1.24)	47,458,515	2.36
12/14/2007	113,527,745	0.57	59,503,758	1.91
11/30/2007	112,882,010	3.70	73,584,598	1.53
11/15/2007	108,854,781	7.46	93,874,036	1.16

### 3. *What information should be included in the daily short sale report published by ASX?*

The key focus should be on ensuring that aggregate open loan and short position for each security reaches the market. The CREST report serves as an example.



**CREST**  
part of Euroclear

**View Monthly Stock Loan Data**

Data available for months between September 2003 and March 2008

Select date for displaying data

March 2008

**Monthly Data for March 2008**

ISIN	Abbreviation	Average No. on Loan	Average No. in CREST	Percentage
GB00B1YW4409	3I GROUP 73 19/22P	25,202,354.68	361,432,944.21	6.97%
JE00B1RJLF86	3I INFRASTRUC GBP1	64,946,073.57	702,183,698.05	9.24%
JE00B1VVM796	3I QUOTD PRIV EQ1P	843,999.00	349,951,545.00	0.24%
GB0006640972	4IMPRINT G38 6/13P	101,000.00	24,314,359.00	0.41%
GI000A0F6407	888 HOLDINGS DI	5,999,368.78	129,300,984.31	4.63%
GB0000305796	ABACUS GROUP 5P	2,776,812.00	67,509,926.15	4.11%
IE0000020408	ABBNEY EURO.32	90,202.57	13,169,716.47	0.68%
GB0000056852	ABERDEEN NDI 25P	577,355.63	24,284,688.73	2.37%
GB0000000000	ABERDEEN ASIAN 25P	78,200.00	24,753,400.00	0.24%

**4. What time should the short sale report be published each day?**

On market opening.

**5. Any other measures to improve transparency in relation to short selling activity.**

See other responses

**6. Whether the tick test should be retained, including whether it should be retained for all securities, or only retained for some securities (e.g. those not in the Approved List), and why this should be the case?****7. Whether the tick test should apply to all types of short sale, or only in relation to some types of short sale, and why this should be the case?**

The tick test is only necessary in the current absence of transparency. With appropriate transparency, it should be dispensed with.

**8. Whether the Approved List current market capitalisation and liquidity tests remain relevant?**

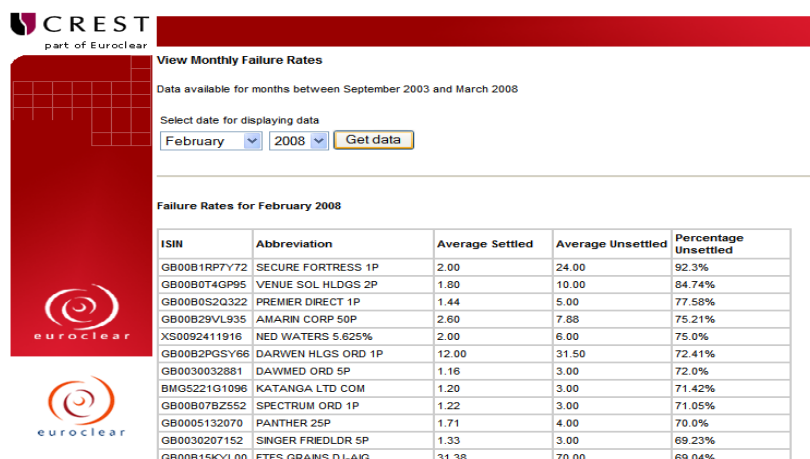
Under the circumstances of full transparency of the covered sale market, and the ending of the naked short sale market, the Approved List is redundant.

**9. Comments on the principles which ASX proposes will underpin the new fail fee regime?**

The fail fee is connected (almost) exclusively to naked short selling. Consequently, the 'management of settlement risks' should no longer be essential, in the same way.

**10. Views on other mechanisms to further improve timely settlement of equity trades.**

Publish failed trade information as per the attached.



**CREST**  
part of Euroclear

**View Monthly Failure Rates**

Data available for months between September 2003 and March 2008

Select date for displaying data

February 2008

**Failure Rates for February 2008**

ISIN	Abbreviation	Average Settled	Average Unsettled	Percentage Unsettled
GB00B1RP7Y72	SECURE FORTRESS 1P	2.00	24.00	92.3%
GB00B0T4GP95	VENUE SOL HLDGS 2P	1.80	10.00	84.74%
GB00B0S2Q3Z2	PREMIER DIRECT 1P	1.44	5.00	77.58%
GB00B29VL935	AMARIN CORP 50P	2.60	7.88	75.21%
XS0092411916	NED WATERS 5.625%	2.00	6.00	75.0%
GB00B2PGSY66	DARWEN HLGS ORD 1P	12.00	31.50	72.41%
GB0030032881	DAWMED ORD 5P	1.16	3.00	72.0%
BMGS221G1096	KATANGA LTD COM	1.20	3.00	71.42%
GB00B07BZ552	SPECTRUM ORD 1P	1.22	3.00	71.05%
GB0005132070	PANTHER 25P	1.71	4.00	70.0%
GB0030207152	SINGER FRIEDLDR 5P	1.33	3.00	69.23%
GB00B15KYL00	ETFS GRAINS DJ-AIG	31.38	70.00	69.04%