INTERNATIONAL SECURITIES LENDING ASSOCIATION

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PO Box 2072
Rayleigh
Essex SS6 9NQ

Tel: +44 (0)1268 741222
+44 (0)20 7742 0250

admin@isla.co.uk

The Editor,
Wall Street Journal

Dear Sir,

Securities lending and shareholder votes

We are concerned that the Wall Street Journal article 'How borrowed shares swing company votes; SEC and others fear hedge-fund strategy may subvert elections' (26 January 2007) exaggerated and, in some important respects, misrepresented the impact of securities lending on shareholder voting. Securities lending does involve the absolute transfer of title. But lenders have the contractual right to recall securities from the borrower at any time. Securities lending does not therefore disenfranchise lenders, such as pension funds and insurance companies, if they wish to exercise their voting rights.

The article claimed that 'it is routine for hedge funds and other investors to borrow shares to vote them'. We do not believe this to be true. In the United Kingdom, the Securities Lending Code of Guidance, produced by the Securities Lending and Repo Committee, comprising market participants, the Financial Services Authority and the Bank of England, states that 'there is a consensus in the market that securities should not be borrowed solely for the purpose of exercising the voting rights at, for example, an AGM or EGM. Lenders should also consider their corporate governance responsibilities before lending stock over a period in which an AGM or EGM is expected to be hold. Beneficial owners need to ensure that any agents they have made responsible for voting and for securities lending act in a co-ordinated way'.

Market participants have made great efforts in recent years to ensure that securities lending can be consistent with good corporate governance, both individually and at an industry level. For example, in 2005 the International Securities Lending Association published 'Securities Lending and Corporate Governance', setting out good practices for lenders and their agents.

Securities lending provides liquidity to the equity, bond and money markets, placing it at the heart of the financial system. The increase in liquidity reduces the cost of trading, benefiting all. The ability to lend and borrow securities underpins the services that securities dealers offer their customers and the trading strategies of dealers, hedge funds and asset managers. Securities lending forms a growing part of the revenue of pension funds, insurance companies and banks. As the article correctly stated, the market is important, global, large – with securities on loan in excess of US$2.5 trillion by one recent estimate – and growing rapidly. But securities are rarely borrowed for the purpose of influencing shareholder votes and the cases in which borrowed shares can be shown to have influenced a shareholder vote are rarer still. Shares belonging to organisations and individuals with robust corporate governance policies should never be involved.

Yours faithfully

Richard Steele
Chairman
International Securities Lending Association

Note to Editors:

The International Securities Lending Association is a trade Association established in 1989 to represent the common interests of the Securities lending industry. ISLA assists in the orderly, efficient and competitive development of the International securities lending market. In this regard, ISLA works closely with regulators and in the UK has representation on the Stock Lending and Repo Committee, a committee of market practitioners chaired by the Bank of England. The Association has contributed to a number of major market initiatives, including the development of the UK Stock Borrowing and Lending Code of Guidance and the industry standard lending agreements, the Overseas Securities Lending Agreement (OSLA) and the Global Master Securities Lending Agreement (GMSLA).
Today, ISLA has over 80 members comprising insurance companies, pension funds, asset managers, banks and custodians, representing more than 4,000 clients. In September 2004, ISLA changed its constitution to allow borrowers to become members for the first time: to date almost 20 borrowers have joined. Whilst based in London, the geographic spread of ISLA's client base is global in nature, comprising substantial representation from the UK and the other EU member states in addition to other major financial centres such as Switzerland and the United States.
A full list of our members may be found here: www.isla.co.uk/members.asp.

The Stock Lending and Repo Committee (SLRC) was formed in 1990, originally under the guise of the Stock Borrowing and Lending Committee (SBLC) (which was chaired by the Bank of England). Its name was changed in 1996 to reflect the Committee's wider remit following the development of the Gilt Repo market. In 2004, the name was changed again to Securities Lending and Repo Committee.

In its present capacity, it is a UK based committee of international repo and securities lending practitioners, together with bodies such as CREST, the Debt Management Office, the Inland Revenue, the London Clearing House and the London Stock Exchange. The committee provides a forum in which structural (including legal) developments in the relevant markets can be discussed by practitioners and the authorities. It continues to be chaired and administered by the Bank of England.