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24 September 2009

Jeffrey Dinwoodie
David P. Bloom
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Re: Panel on Securities Lending and Investor Protection Concerns, File No. 4-590.

Dear Mr. Dinwoodie:

On behalf of the International Corporate Governance Network we are writing to submit to the SEC our Securities Lending Code, to amplify upon those of its key recommendations particularly relevant to the current discussion on market rules, and to emphasize why we think this debate is of critical importance to the cause of better corporate governance in the United States.

The International Corporate Governance Network (ICGN) is a global organization dedicated to the cause of improving governance standards throughout the world. Its members are key individuals, representing investment organizations with approximately $9.5 trillion in assets, of which approximately $5 trillion is invested in the U.S. alone. Over a third of our almost 500 members come from the United States. They include fund managers, corporate governance specialists, attorneys, service providers, and senior executives at some of the leading pension funds and private asset managers in this country. To the best of our knowledge, the ICGN is the only international organization representing investors active in the cause of better governance.

We became involved with the issue of securities and especially stock lending in early 2003, as a result of several of our members expressing concern that lending activity had become so important that it was impeding share voting, and interfering with corporate governance engagements generally. In order to investigate how serious the problem actually was, and whether standards of best practice might be called for, we appointed a committee to investigate the issues, under the chairmanship of Andrew Clearfield, then of TIAA-CREF, and one of the authors of this letter. The committee of 20 was constituted with representatives of leading institutional investors, custodial banks, proxy advisors, and at least one major borrower.

The members of the committee during the year the Code was written, were as follows:

Member	Institution
Andrew Clearfield, Chairman	TIAA-CREF
Jennifer Choi	Investment Companies' Institute (ICI)
Stephen Deane	ISS (now RiskMetrics)
Harry Frost	ADP Investor Communication Services
Renato Grandmont	Deutsche Bank
Catherine Jackson	Ontario Teachers' Pension Plan [Canada]
Christian Kremer	Clifford Chance LLP [Luxembourg]
Paul Lee	Hermes Investment Advisors [UK]
Pierre-Henri Leroy	Proxinvest [France]
Bob McCormick	Fidelity Management and Research
Peter Montagnon	Association of British Insurers [UK]
Taiji Okusu	Credit Suisse [Japan]
Elaine Orr	Morgan Stanley
Cynthia Richson	Ohio Public Employees Retirement System
Hans van Roekel	SPF Beheer [Netherlands]
Charlie Ruffel	Plan Sponsor, Inc.
Tim Smith	Axa Investment Management [UK]
Sheila Somerville-Ford	JP Morgan [UK]
James Templeman	Barclays Global Investors [UK]
John Wilcox (ex-officio)	Georgeson Shareholder Communications

The Securities Lending Code which had been drawn up after two years' study, was adopted by the ICGN in 2005, and slightly amended in 2007. The amended Code is incorporated at the end of this document.

In anticipation of central issues pertaining to the specific topic of "Securities Lending and Investor Protection Concerns," we would like to respond to some potential questions with which regulators may need to deal. First, however, we should emphasize that major parts of the arrangements for lending are so *ad hoc* that some generalizations are difficult. Much of our concern, and of the rationale behind our Code stems from our findings that so much of the procedure surrounding lending has grown up ‘under the radar,’ that the process has evaded the scrutiny and risk analysis which are generally part of institutional investment activities.

Q. *What are the risks to lenders posed by cash collateral reinvestment? Are there meaningful alternatives?*

A. The principal risk is that in quest of an improved return, the agent or department involved in lending might increase the residual risk more than had been envisioned by fund management, by investing collateral more aggressively. It is also possible that if lending is being conducted on a large scale, the risk profile of the portfolio or the fund might be significantly altered without fund management being aware of the fact. In the United Kingdom, where lending is also highly developed, collateral is often merely that, and need not earn the fee, which is paid separately. This may be safer, but does substitute further questions of counterparty risk.

Q. *How are lending agent compensation and fee splits typically negotiated? What controls are placed on fees paid to affiliates?*

A. We found that fees were negotiated based only upon the limited portion of the market visible to the lenders: the range of bids they were shown by a small group of prime brokers. They had no knowledge of the rest of the market, no idea of why there might be special demand for certain stocks, nor how profitable the loans were to other parties to the transaction. They were therefore in a weak position to negotiate fees on a particular loan.

As for agent compensation: the agent’s portion of the fee was typically unknown to the lender. All that had been negotiated was usually a certain return promised the lender by the agent. These negotiations were almost always carried on by back office and cash-management representatives, without the knowledge or approval of portfolio management. In fact, the lack of transparency in all these arrangements is one of our greatest concerns in the lending market.

Q. *Who votes the proxies of shares that are loaned? Are there impediments to lenders voting the proxies of loaned shares? Are there manipulative activities that can occur as a result of the voting of proxies of loaned securities?*

A. The votes normally move with the share; that is, the proxy will normally be sent to the new owner of record, who is never the lender, except in extraordinary circumstances. Legally, a lender has given up title to the shares, and has lost the right to vote. In some cases, when proxies are sent out before the shares have been re-recorded, the lender may receive the proxies instead: in such cases, as one survey has found, the lender will probably vote them, without worrying whether it is entitled to or not. It may not even know that the shares have been lent. Since the new owner might also claim the right to vote the shares, especially if the trade date was before the record date, the possibility of double voting occurs. When the Bank of America had an extraordinary attempted over-vote of 106% in 2008, its investigations indicated that many of the extra votes came from lent shares.

There are several documented instances in which shares have been borrowed for the primary purpose of voting them. One can invent other means by which loans could be used to manipulate the results of a shareholder vote. Given the lack of transparency in the lending market, it is impossible to ascertain how often this might have happened, and we wonder how confidently one can actually claim that such incidents are rare. This is also true for any other alleged market manipulation involving borrowed shares. One of the primary reasons for requiring greater transparency in this market is that it would free it from most allegations of manipulation or abuse, and would give greater confidence in the integrity of close shareholder votes and of securities markets generally.

Q. *Are lenders harmed if a borrower defaults? What protections do they have?*

A. In the United States, the protections now seem reasonably good. One concern, that a bankruptcy judge might impound collateral given for a loan, or that lent securities not yet settled might be similarly held up in bankruptcy proceedings, seems to have been dealt with by statute. However, if the lent shares had become illiquid due to some sudden transformational event, and could not be repurchased with the collateral on hand—and this would require extraordinary circumstances—it might be difficult to obtain full restitution from a defaulting borrower; we don't feel qualified to comment upon what might happen in such circumstances.

However, we must add that many U.S. institutions also lend shares held abroad, and there the laws are not quite so clear. In the U.K., for example, we have been told that in bankruptcy such shares might be impounded, and there have been examples where Lehman clients have been waiting months for their shares or their money.

These specific questions aside, we are also concerned that lending activity as it is presently conducted is causing certain other problems in the conduct of corporate governance activities by portfolio investors, and may be seen as having a detrimental effect upon investor responsibility generally. Since it was the unanimous belief of the committee that lending in and of itself could be highly beneficial, and that short selling was important in furthering price discovery, we did not intend to curtail lending, but rather to recommend improved procedures which could cure the defects of the present system. It was to address these issues that we drafted the ICGN Code.

<u>Issues</u>

Impact of Lending: The findings of our investigation were unsettling. Lending was usually assumed by institutions to be a marginal activity. In fact it had grown in principal markets to encompass from 2 - 3% of all quoted lendable shares, but was frequently at the 9 - 10% level for major companies at peak seasons of the year including record dates. In special situations it could rise to sustained levels of over 20%. Despite the growing importance of stock lending, most institutional investors had no written policy regarding lending, attempted no reconciliation between their lending activity and their voting policy, and were largely unaware of the specifics of their lending activity. Some trustees and chief executives were even under the impression that they could still vote their lent shares!

We found cases where lending had grown to the point where share voting had been totally abandoned, so that all shares might be available for loan at a moment's notice. We found cases where lending activity worth several tens of thousands of dollars was allowed to outweigh important institutional interests regarding the outcome of key shareholder votes, despite the complaints of portfolio managers. We also found that many governance engagements with companies were undermined by the discrepancy between a lender's theoretical holding in a company and its considerably smaller presence on the company register.

Effect upon Risk: While industry practices involved reasonable security for stock loans, almost no lenders had considered what residual risks they might be running on the investment of collateral they received for a loan, the risks of sequestration of the position under extreme situations (such as last year's Lehman bankruptcy), nor had they clarified their internal procedures for recall of lent shares. Frequently, lending had been 'sold' to boards as an absolutely risk-free way of enhancing return, and had grown outside the scrutiny of boards and senior executives as a riskless, back-office activity. Index funds, in particular, relied upon it to offset the inevitable frictional costs of a real portfolio. It had become an expected component of annual return at many institutions, without its side effects ever being examined.

Loss of Control: Lending is most often conducted by third parties—custodians or specialized lending agents. Sometimes the contracts specify that lending is to be done within certain parameters. Sometimes the lending is to be done at the discretion of the custodian, and a check mailed to the client institution at the end of the quarter. Sometimes it is to be netted against custodial fees, and the client never knows what has been lent and when. There are also reports of lending being done without the client's knowledge or consent. There is often no record available to the client and no way to retrace lending activity, and therefore no way to know if any guidelines or constraints have been adhered to.

Of course, these third parties' objective is solely to maximize the return from lending. The majority function entirely without guidelines concerning client activity in corporate governance, stewardship, or socially responsible issues. A study conducted by RiskMetrics of its own clients found that a majority of even those which had a formal lending policy had made no attempt to reconcile it with their voting policies.

Typically, lending agents are under no obligation to talk to anyone actually charged with the responsibilities for managing and voting a position: they report through a different channel entirely. Some of us have been involved in situations where important shareholder initiatives were undermined by last-minute lending activity, and representatives of major funds showed up at shareholder meetings with a fraction of the votes they thought they had, to great embarrassment. It is safe to make the generalization that in the great majority of circumstances, lending activity is completely disjunct from portfolio management.

The lending industry seems to prefer it that way. The majority of investors seem content to be getting something for nothing, ask no questions, impose no demands, and never even inquire whether they are being fairly compensated for their stock loans, or how much their agents and counterparties are making from those transactions. At a major conference on lending one prime broker summarized his organization's attitude toward lenders, "We liked them big, and we liked them dumb."

Recall of Loans: The first counter-argument that is usually cited when one expresses concerns regarding lending is that shares can always be recalled. Indeed, standard lending contracts all allow for recall on demand, and often specify penalty arrangements if shares are not returned in a timely fashion. We found that it doesn't always work that way in practice.

If the shares are somewhat illiquid, the borrower may not be able to find them in time. If the lender is recalling its shares in order to sell them, the borrower (usually a prime broker) would often sell the shares short for the benefit of the customer, hoping to find them before settlement has failed for too long. But this is no help at all if the recall is for the purpose of voting; without the actual shares, there are no voting rights. Moreover, prime brokers do not want lenders to recall shares: they will either have to find other shares to borrow, or they will have to unwind a position; either their own or one for the benefit of a client.

For this reason, borrowers and lending agents wanted to know the purpose of a recall. The general *modus operandi* was that if the recall was for sale of the shares, the borrower would try hard to comply; if it was merely for a vote, it would try to talk the borrower out of the recall. There were sometimes veiled threats that if the lender did this too often the borrower (usually a prime broker) would stop doing business with the lender. In some cases, it might take weeks for the lender to return the shares. While contracts may provide for damages, in practice they were almost never demanded, because the lender did not want to anger the borrower, as there were many lenders and only a few large borrowers. At least one very large pension fund, and numerous smaller ones, told us that they had stopped lending altogether because of frequent recall problems.

But the primary effect of the recall mechanism upon corporate governance was more corrosive than occasional failures to recall on time. If the lending was done by a third party (and often even if it was done in-house), the manager making the decision to vote might not know that the shares had to be recalled until there was very little time left. If the lending was being conducted by the custodian, the manager might never know: the custodian simply voted the residual shares still left in the account, and reported to the manager that the voting instructions were complied with. This of course was also the rule in reporting vote internally or to clients: the whole theoretical position was reported to have been voted even if only a small percentage actually was.

In either case, the back office of the lender was likely to remind the manager and his or her superiors that money—hard cash—would be lost by recalling shares for a vote, while the benefits of voting were entirely intangible. Moreover, they would claim that the relationship between the lender and the borrower would suffer irreparable harm. Without clear guidelines and a proper resolution method to govern such conflicts, lending created a rival force within an institution that competed relentlessly with governance objectives.

Most corporate governance specialists have learned not to protest. One major public pension fund completely stopped voting and sharply curtailed its governance activities after its board was persuaded to adopt a more aggressive lending program by a third-party lender. Yet the fund never told its beneficiaries that it was backtracking on its public commitments to improve corporate governance and promote socially responsible investing.

Fees: Another problem was that the fee structure was often obscure, that clients had no idea what lending was worth to intermediaries or to the prime brokers assembling loans, and that returns were often buried within custodial fees, as well as hidden within investment returns as reported to beneficiaries. Most lenders had no idea how profitable loans were to their agents, to custodians, or to prime brokers. In fact, stock loans are enormously profitable for prime brokers, quite profitable for lending intermediaries, and pay minimal returns to the lenders themselves, yet it is only the lenders which are giving up something when they lend. Given the lack of transparency in the market, it has often been easy for borrowers to pay small amounts for shares which are relatively illiquid, and would be difficult to recall if the lender should desire to do so.

We found that more than a few fund trustees did not understand that the fee for the loan is actually earned, by the lender or its agent, through reinvestment of the collateral, and that in fact there is usually a remission of a part of the income from the collateral to the borrower. This arrangement has tempted some lenders to invest the collateral in less-than risk free instruments in order to enhance the return. Often, the lender's risk management team had no idea where the collateral is invested, due to the industry practice of not carrying the effect of loans on the reports distributed to managers.

Market Abuse: We also discovered a small number of cases where lending had aided some party to abuse market positions, or to vote shares they should not have voted. We were assured that such cases were rare, but no one could actually demonstrate that they were, because no one had any information as to who had borrowed the shares or when. There also seem to have been some cases where managements or their allies may have borrowed shares simply to guarantee a quiet meeting. Most worrying of all, we found that almost no one actually knew how important their lending activity was in a particular stock, and very often had no idea whether their positions had been lent out or not, due to an absence of adequate reporting, and the lack of transparency in the whole lending market.

The problems accompanying this area were all rendered more difficult by the defensive attitudes of those specifically involved in lending. They had found a back-office area that had become a profit center, and frequently opposed to any sort of scrutiny or control.

Thinking Behind the Code

As a result of these findings, almost all the members of the committee agreed that more transparency should be a prime requisite for improved practice in this area. Two kinds of transparency were called for. *Internal transparency* within the asset management chain was necessary, so that the left hand would know what the right hand was doing, so that funds would know what their managers, custodians and agents were doing, and so that clients would eventually know how their assets were being managed and where their returns were coming from. *External*, or *market transparency* was necessary, so that regulators would know that the market was being conducted honestly, whether naked shorting was being employed, whether standards regulating voting and manipulation such as Regulation T were being adhered to, and so that companies and shareholders could trust the integrity of shareholder elections.

Another concern of the committee was that most fund beneficiaries had no idea whether their funds were voting most of their shares or lending most of them, because votes were always disclosed as if 100% of the theoretical position were actually voted. No inconsistency or conflict between a fund's corporate governance and social responsibility policies and its lending activity was ever reported to beneficiaries; one gets the impression that trustees did not want to know about them either. Within a manager or a fund, there were often only *ad hoc* mechanisms to decide whether shares should be recalled in order to vote them, or whether they should be left out on loan.

We felt very strongly that *consistency* was necessary. If a fund wished to maximize its short-term return and therefore resolved all conflicts by leaving shares on loan, it should state publicly that this was its policy. If a fund would weigh the longer-term benefits against the return from voting, as so many funds claimed to do, it should have written policies, and a mechanism to actually conduct such a policy. If a fund felt it was preferable to always vote all shares, or to vote all shares when certain particular issues were involved, regardless of lost lending returns, it should also state this publicly, and make sure that this was what it did. Departures from stated policies should be communicated to shareholders as part of the annual reporting mechanism.

Integrity of the Lending Market

We also felt that institutional investors of all kinds should be committed to avoid all situations where there was an obvious potential for market abuse. While these situations were likely to be much rarer, we knew of occasions when shares had been lent out at large premiums to the going rate, at the last minute before a key vote or record date, and with unusual settlement instructions. We thought that conscientious investors should pledge to avoid lending under such circumstances.

Finally, we realized that there were two specific problems which strongly affected lending and voting, were entirely outside the control of investors, but could be solved very simply by issuers and their regulators. *One was the coincidence of record dates for both voting and dividends.* Dividend arbitrage created an incentive to lend shares instead of voting them which had nothing to do with short selling or any other activity involving transfer of full ownership rights. Our recommendation was that standard issuer practice should be changed to separate the record dates for dividends and for voting, so that those wishing to conduct an arbitrage could do so without sacrificing their voting rights. We would hope that regulators, such as the SEC, remove whatever obstacles or concerns might be in the way of such a shift on the part of issuers.

The other was particularly important to the United States, which practices a system with greatly advanced record dates. It was that issuers be required to post their meeting agendas, with resolutions to be put to a vote, sufficiently *before* the record date so that theoretical owners who have lent out their shares be on sufficient notice so that they can make a reasoned decision whether to recall them. At present, almost no one knows whether there will be an issue of sufficient importance to them at a shareholders' meeting, and they cannot know whether they perceive it in their interest to recall or not. We have written the SEC separately regarding this issue, which we also believe to be of prime importance.

Structure of the Code

While these principles were easy to state, we had discovered that most fund sponsors, managers, and custodians were unaware of all their implications. There was a risk that investors might approve the principles but remain unaware of practices which would violate them. Thus, we began with a brief statement of our basic aims and the principles which we felt ought to be applied. This may be considered the Code proper. We then appended an analysis of the responsibilities appropriate to each party in a lending transaction. Guidance regarding specific steps of lending followed in a second Appendix, so that it should be clear to those involved what we considered proper application of the Code. Finally, we appended a list of definitions of the terms involved in lending, since some had special meanings in this technical area, and others would be unfamiliar to those not directly involved in back-office operations.

Reception of the Code

Investor response was favorable, albeit infrequent. In accordance with its prevailing practice, the ICGN did not ask organizations specifically to sign on to the document, but rather to use it as guidance for their own practice. The *Financial Times* covered its issuance, and was positive. The *Wall Street Journal* did not cover the issue at all. Custodians and lending agents were publicly silent upon the issues.

To the best of our knowledge, no one has raised a serious criticism of the Code to this day. Several of our larger institutions have told us that they were already in substantial compliance with it. Several others stated they have modified their procedures somewhat, to bring them more in compliance with the Code. Issuers' associations have received it favorably, and expressed their verbal support for the two proposals involving them directly. Most importantly, the European Commission, in its ongoing examination of stock lending, has named it a "document of reference," which they plan to use in devising their own lending standards.

Opposition to the ICGN Code

When we circulated the final draft of the Code to several lending agents and custodial banks we received almost no reaction and no criticism of the Code. The exception was the association of lending agents based in London called ISLA, the International Securities Lending Association. Though one of their members had been involved with the committee from the start, they wrote us only after it was finished that the whole thing was impractical to implement, would render most lending activity impossible, and that it assumed an unnecessarily negative tone. Since they had not furnished such criticisms until the writing of the Code was complete, and since their critique had been echoed by no other custodian or lender, we chose to disregard this *prima facie* objection as rising from unreasonable fears, and perhaps being motivated by a desire on the part of some members that no constraints upon lending, no matter how reasonable, be proposed.

However, one major investor in the U.K. said that when they showed a copy to their custodian—a major bank which had been one of the participants in the committee, and which had made no comment when we circulated it a copy of the final draft before ratification—this custodian responded that the whole thing was impossible to implement, although their only specific criticisms were that the Code called upon issuers to change their procedures, yet custodians had no power over that (as we had clearly stated), and that the Code asked intermediaries to warn lenders in those cases which seemed obviously suspicious, while they said that custodians couldn't know where the shares were going. Since we had only asked that custodians and other lending agents report circumstances which were *in their judgment* suspicious, this criticism seemed beside the point, and certainly did not invalidate the rest of the Code. In general, it seemed that the lending industry was trying to pretend the Code did not exist, or if confronted with it, that it was totally impractical, without being specific, so that they would never have to deal with the core issues it raised.

Implications of Adoption of the Proposed Lending Procedures

From the outset, we were concerned that any recommended practices not burden lending activity more than necessary. The Securities Lending Committee was unanimously of the opinion that lending was fundamentally beneficial, provided more liquidity to markets, and that short selling in particular was beneficial in aiding price discovery.

Our concerns were primarily that, as it has been conducted at present, stock lending interfered unnecessarily with voting and governance activity in general. Specifically, current procedures made it difficult for investors engaged in lending to vote on important issues, competed with board mandates regarding governance engagements and stewardship, was insufficiently transparent to both portfolio managers and fund beneficiaries, and could not be reviewed retrospectively to detect incidents of market abuse and fraud, or even to determine if shares had been properly voted in accordance with instructions.

Certain custodial practices conducted in conjunction with lending, including the use of omnibus pooled accounts, increase the risk that votes could be misallocated or mislaid entirely, that over-voting might occur, with consequent proportional reduction of some investors' voting, and that the sum total of these procedures might compromise the integrity of the shareholders' meeting. An ancillary concern was that boards and risk managers were insufficiently aware of the actual procedures involved, and had in some cases never examined how their lending activity, with attendant re-investment of collateral, could alter portfolio risk.

To implement the transparency required could, we knew, create significant extra expenses for custodians. We felt that such costs should enter into the rates and services negotiated between custodians and their clients. It was our concern that these negotiations have typically been conducted entirely between back offices and custodians, and that prevailing arrangements have been tailored to minimize costs without sufficient attention being given to the needs of either the investment staff or those concerned with governance and stewardship.

It is our intention, if the procedures recommended are implemented, that voting would increase on controversial issues, while potentially declining on routine matters and those of little interest to particular investors. Currently, there are a significant number of large institutions which refrain from lending altogether, or recall all shares before the major proxy season, so that they might not miss critical votes. If advance notification were improved, if lenders knew with certainty whether shares had been lent, and if recall provisions were tightened, these institutions could lend with the assurance that their loans were not being voted in a manner contrary to their beneficiaries' interests, and that they were not missing the opportunity to vote on issues of institutional concern.

Summary

It is our finding, based upon both our research and our own experience as investors, that stock lending, as it is presently conducted, has a significant detrimental impact upon share voting and upon the normal attributes of responsible ownership. We also believe that in a non-trivial number of cases, lending activity may have compromised the integrity of the shareholders' meeting. While no reasonable set of procedures can prevent every possible problem, we think that the procedures proposed would go a long way toward improving the instances of responsible share voting, reduce the incidence of unnecessary recall of loans, lead to a more reasonable fee structure, and improve the integrity of both the lending process and the process of recording shareholder votes.

Further, we believe that the procedures recommended would not unduly burden stock lending activity, and would improve the orderly functioning of markets. For all these reasons, we respectfully recommend that the SEC support, and where necessary, enable the reforms in stock lending indicated in the ICGN Code.

We would like to thank the Commission for inviting us to participate in this consultation, and in the panel on Securities Lending and Investor Protection. The text of the Code and any other information needed regarding the ICGN or pertaining to our other positions on corporate governance and share owner rights can be found at our website, www.icgn.org. For further information and any follow-up, please contact the Chairman of the ICGN, Christianna Wood, at christianna.wood@icgn.org, telephone (in the United States) 303-526-1367.

Sincerely yours,

Christianna Wood
Chairman of the International Corporate Governance Network

Andrew Clearfield
Chairman, Securities Lending Task Force of the ICGN

INTERNATIONAL CORPORATE
GOVERNANCE NETWORK

ICGN Securities Lending Code of Best Practice

INTERNATIONAL CORPORATE GOVERNANCE NETWORK

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SECURITIES LENDING COMMITTEE 2006/2007

Chair: **Andrew Clearfield**, President, Investment Initiatives LLC

Members:

Hye-Won Choi, TIAA-CREF, USA

Stephen Deane, ISS Research Institute, USA

Catherine Jackson, Ontario Teachers' Pension Plan, Canada

Paul Lee, Hermes, UK

Pierre-Henri Leroy, President, Proxinvest, France

Robert McCormick, Glass Lewis, USA

Peter Montagnon, Association of British Insurers, UK

Taiji Okusu, Credit Suisse, Japan

Cynthia Richson, Ohio Public Employees Retirement System, USA (formerly)

Sheila Somerville-Ford, JP Morgan, UK

Chad Spitler, Barclays Global Investors, USA

Daniel Summerfield, Universities Superannuation Fund, UK

John Wilcox, TIAA-CREFF, USA

Anne Simpson, ICGN (ex officio)

Please forward comments and questions to:Anne Simpson at execdirector@icgn.org

ICGN Securities Lending Code of Best Practice

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If you would like further information about the ICGN please contact Anne Simpson on execdirector@icgn.org

For membership enquiries contact Elizabeth Bagger, Membership Secretary on secretariat@icgn.org or visit our website for more details www.icgn.org

About ICGN

The International Corporate Governance Network is a not-for-profit body, founded in 1995 that has evolved into a global membership organisation of more than 500 leaders in corporate governance. Its members are based in 38 countries from around the world, and include professionals, corporations, policy makers and institutional investors with capital under management in excess of $US 10 trillion.

ICGN's Mission

The ICGN's mission is to develop and encourage adherence to corporate governance standards and guidelines, and to promote good corporate governance worldwide.

The ICGN exchanges ideas and information across borders, commissions research, develops best practices and is an advocate for good corporate governance with both the market and policy makers.

The ICGN promotes understanding through its annual and mid-year meetings in different countries around the world, which bring together those engaged with reform in order to improve understanding. ICGN's working committees develop best practice, carry out research and advocate policy reforms to support raising of standards.

In seeking to achieve this mission, the ICGN can draw on three unique strengths:

- **the breadth and expertise of its membership base**, which extends across the capital markets and beyond to include senior decision makers and opinion leaders in the practice of corporate governance;

- **its international institutional investor members** who collectively represent funds under management in excess of US$10 trillion, giving a focus upon the role and responsibilities of fiduciaries responsible for the long term savings of the wider community;

- **the geographic diversity of its membership**, with members drawn from over 38 countries from every region – North America, Europe, East and South Asia, Latin America, Africa and even the Middle East.

ICGN Securities Lending Code of Best Practice

Revised and approved by ICGN members at the 2007 AGM in Cape Town, South Africa.

The lending of securities and especially of common shares is an increasingly important practice which improves market liquidity, reduces the risk of failed trades, and adds significantly to the incremental return of investors. However, we have found that there is widespread misunderstanding of securities lending transactions on the part of those not directly involved in the process. The word 'lending' has itself misled many as in law the transaction is in fact an absolute transfer of title against an undertaking to return equivalent securities. Misconceptions as to its nature have led to loss of shareholder votes in important situations, as well as to cases of shares being voted by parties who have no equity capital at risk in the issuing company, and thus, no long-term interest in the company's welfare. Lenders' corporate governance policies may also be undermined through lack of coordination with lending activity. It is also imperative that there be as little risk as possible that a poll of the shareholders may be compromised through misuse of the borrowing process. To address these concerns the ICGN proposes this Code of Best Practice to its members. It encourages other concerned investors, market intermediaries, and public companies to take account of the Code where appropriate.

Three broad principles which apply to all areas of investment practice are here used to clarify the responsibilities of all parties engaged in stock lending. With their relevant applications in this area, they are:

First, **transparency**: the lending process, frequently handled today as a purely mechanical adjustment to custodial arrangements, should become subject to the same visibility and safeguards as any other transaction conducted on an owner's or beneficiary's behalf in a securities account.

Second, **consistency**: it is unreasonable to expect that lending agents can make subtle judgements as to when they should sacrifice some income in order to protect the lender's long-term economic interests and stewardship commitments. A clear set of policies which indicates with as little ambiguity as possible when shares shall be lent and when they shall be withheld from lending or recalled is necessary in order to ensure that similar situations are handled in the same way. Clear mechanisms should be set up to handle borderline situations. Neither the long-term economic interest in better governance nor the interest in maximising short-term remuneration should be allowed to exceed the parameters set for each by the stated policy of the primary lender.*

* An asterisk indicates when a term defined in Appendix III is used in the text for the first time.

Third, **responsibility**: responsible shareholders have a duty to see that the votes associated with their shareholdings are not cast in a manner contrary to their stated policies and economic interests. While fiduciaries have a duty to maximise economic returns to their beneficiaries, they equally have a fiduciary duty to protect their long-term interests through voting and other actions sometimes precluding lending. Fiduciaries also have a duty to ensure that the pursuit of more income is not subjecting their beneficiaries to greater risks. These responsibilities must be appropriately balanced according to the primary lender's voting policy, in accordance with its ultimate beneficiaries' preferences. This responsibility lies with the primary lender, and not with its agents.

By properly following these broad principles best practice with regard to share lending can be achieved. The difficulty lies in applying them thoroughly. Staffers or agents responsible for voting and investment decisions should always have full transparency whether and what percentage of shares have been lent. Beneficiaries should always know which percentage their manager has voted of its position in a given portfolio company. Consistency may be lost when a lender with a policy to recall shares to vote "on important issues" cannot know in a particular country with an early record date what the issues to be voted upon will be. (This is the case in the United States and Canada.) Responsibility has been ignored when lenders, drawn by suddenly rising demand, lend shares under circumstances in which it is highly probable that they are being borrowed in order to alter the result at a shareholders' meeting, possibly to their own detriment.

Specific aspects of best practice follow from these broad principles. While simple to state, their application may be complex and involve many unsuspected technical adjustments. We have therefore sought to provide more detailed guidance and explanation in the attached appendices. The basic tenets of best practice, however, are:

1 **All share lending activity should be based upon the realisation that lending inherently entails transfer of title from the lender to the borrower for the duration of the loan.** Most economic rights of the lender can be preserved through contractual agreements with the borrower. Those involving the issuer, however, such as the right to vote, or one's continuity on the share register, **cannot** be preserved in this way. If an investor wishes to vote its lent shares or protect its legal interests as a registered shareholder, it **must** recall the shares.

2 **During the period of a stock loan, lenders may protect their rights only with the borrower, since they have no rights with the issuer of the shares which have been lent.** Stock loans are normally collateralised at more than 100% of the current market value of the loan. The collateral may be cash, high-quality debt securities, or equivalent equity securities. Lenders must ensure that this collateral, together with any contractual claims upon the borrower, adequately protects their interests for the duration of the loan.

3 **Institutional shareholders should have a clear policy with respect to lending, especially insofar as it involves voting.** A lending policy should clearly state, *inter alia*, the lender's policy with regard to recall of lent shares for the purpose of voting them. All lending conducted by the institution or on its behalf should be done in accordance with this stated policy.

4 **Lending policy should be mandated by the ultimate beneficial owners of an institution's shares,** whether they be another institution or corporate body or an assemblage of individuals.

5 **Where lending activity may alter the risk characteristics of a portfolio, the policy should state the extent to which this is permitted.** This involves the extent of lending activity, the quality of the borrowers, the quality of the collateral accepted for loans, and its nature: cash, other securities, or a combination of the two, as well as any questions as to changes in the duration of the portfolio, as well as its other risk characteristics.

6 **The returns from lending should be disclosed separately from other investment returns when reporting to clients or beneficiaries. They should not be hidden under management and other costs.** As lending has become an important source of revenue, it behoves institutions to disclose its extent to their clients or beneficiaries, as well as the extent to which investment returns and cost ratios are being driven by or ameliorated by the returns from lending.

7 **It is bad practice to borrow shares for the purpose of voting. Lenders and their agents, therefore, should make best endeavours to discourage such practice.** Borrowers have every right to sell the shares they have acquired. Equally the subsequent purchaser has every right to exercise the vote. However, the exercise of a vote by a borrower who has, by private contract, only a temporary interest in the shares, can distort the result of general meetings, bring the governance process into disrepute and ultimately undermine confidence in the market.

The ICGN affirms the principle that companies should know who controls the votes at their general meetings, and that this transparency should benefit all market participants. Considering the availability of market instruments that separate economic ownership from control, the ICGN believes that it has become desirable for companies and the broader market to be able to track significant divergence of voting power from declared economic ownership**. The ICGN therefore invites the relevant market authorities to consider amending their holdings disclosure regimes to include the transfer of actual or contingent voting rights executed through the use of securities lending and derivatives**.

The attached appendices attempt to delineate in full the responsibilities of the different parties, the sorts of circumstances under which the above principles might be compromised, and how these situations should be handled in accordance with best practice. They are intended as guidance. Best practice may be achieved by other mechanisms as long as the principles are kept in mind in devising appropriate procedures.

Appendix I

Duties of the Respective Parties to a Lending Transaction

A. Lender's Responsibilities

Policy on Voting and Recall of Loaned Shares – The fund, fund sponsor, or principal manager* of a portfolio or fund from which shares are loaned (hereafter the primary lender*) should be responsible for drafting and publishing a general policy that clearly sets forth the scope of lending activity, and under what circumstances, if any, this activity is to be subordinated to voting and to the lender's duties as a long-term shareholder.

Terms of Master Agreement – A Master Lending Agreement among the primary lender, the borrower,* and any custodians, agents or other parties involved in the loan transaction should implement these policies, the attendant procedures, including the procedures for recalling* shares and whatever penalties there are for non-compliance, and indicate the likelihood that shares may be recalled for voting purposes. Needless to say, the Master Lending Agreement should protect the lender's and the borrower's economic interests to the greatest extent possible in the jurisdiction involved.

*Disclosure within the Lender's Ownership Chain** – The primary lender's trustees or directors should effectively communicate their policies and procedures to designated executives at the lending institution and at any agent organisations involved in the investment, lending, or voting of those shares, as well as with those responsible for corporate governance for the portfolio or fund in question. All changes in actual positions due to any lending activity should be updated daily to all those executives charged with investing or voting the shares.

Responsibility for Compliance – The primary lender should be responsible for ensuring that its policies and procedures are practicable, that they fulfil the principles expressed herein, and that they are properly administered no matter what the lender's structure and division of responsibilities among different business units or agent companies.

Dispute Resolution – The primary lender or its principal manager should establish and administer specific procedures to resolve disputes that may arise in connection with the implementation of its lending policy. A record should be kept of each of these disputed cases and the decision should be communicated to all the designated parties within the lender's organisation.

External Disclosure – The revenues from lending activity should be disclosed separately to the portfolio's or the fund's beneficiaries. If the jurisdiction is one in which voting must be disclosed to beneficiaries, lenders should also disclose when shares were not voted because they were out on loan.

Lending Agents – The obligations of any agent charged with conducting lending activity on behalf of a primary lender are normally set out in a contract. It is important that primary lenders ensure contracts are worded so as to incorporate the maintenance of best practice, including, where appropriate, the terms and conditions of the Master Lending Agreement. Ultimate responsibility for maintaining best practice in lending policy is the duty of the primary lender.

B. Borrower's Responsibilities

Recall of Borrowed Shares – Borrowers should agree to return equivalent shares to those borrowed promptly upon the lender's request whether these are in the borrower's possession or more likely must be purchased in the market. All properly executed requests for recall must be treated as equally valid.

Non-Voting of Borrowed Shares – It is never good practice for borrowers to exercise voting rights with respect to shares they have borrowed, except in the rare circumstances where they are acting pursuant to the lender's specific instructions. This limitation is not binding upon a subsequent *bona fide* purchaser of borrowed shares.

Special Terms of Agreement – Borrowers should comply with any additional terms agreed with the lender and should, to the extent possible, communicate these terms to other parties on whose behalf they are carrying out the borrowing.

Accountability and Prevention of Abuses – When borrowing shares for a third party client, borrowers should use their best efforts to ensure that the principals on whose behalf they are acting understand that they are supposed to comply with best practice, as set forth in this Code.

C. Recommended Actions for Issuers to Ameliorate the Effects of Lending

Timely Notice of Shareholder Meetings and Other Transactions – Issuers should publish and distribute a Notice of Meeting, Agenda and other disclosure documents in sufficient time for lenders and borrowers of shares to comply with their policies and best practices as set forth in this document, including public notice of the issues well before any significantly advanced record date.

Separation of Record Dates for Dividend Payments and Shareholder Meetings – To minimise the effect of share lending for dividend swaps* upon shareholder participation and share voting, issuers should not set dividend record dates less than 30 days in advance of a shareholder meeting or record date (whichever is relevant for voting) nor less than 15 days after the shareholder meeting (or record date).

Tabulation – Issuers have a duty of care in their record keeping and administration of shareholder voting to identify and expose abuses in the voting of borrowed shares and to prevent double voting of shares. If the custodians' practice of using commingled accounts interferes with that responsibility, issuers have a duty to call public attention to the problem, and to work with custodians to ameliorate it wherever practicable.

Appendix II

Guidance on Best Practices Associated with the Responsibilities of Primary Lenders, Lending Agents, and Borrowers

1 *Voting and share lending*.

1.1 The voting right is normally inseparable from the share in which it inheres.

1.2 Accordingly, except in the rare case in which some private treaty provides for the separation of voting right from the share (and this is permitted by the issuer and by any applicable law), the primary lender of a share loses its voting right for that share. Until and unless a recall is executed, and an equivalent share is delivered to the lender, they are disenfranchised with respect to that share.

1.3 Any subsequent bona fide purchaser of that share, whether its ownership come as a result of purchase of a share sold short* by the borrower, or of delivery in lieu of a failed settlement,* acquires the voting right together with all the other indicia of ownership. As a matter of market practice, they will have no idea that their share had formerly been borrowed from someone else. As far as the issuer is concerned, the share has changed hands.

1.4 With respect to ownership rights, the initial borrower is in a different position than any subsequent owner to whom the shares are sold, as the initial borrower knows that the shares were borrowed, and that it retains rights over the collateral* posted in lieu of payment.

2 *Improper Lending Practices.*

2.1 The borrowing of shares for the primary purpose of exerting influence or gaining control of a company without sharing the risks of ownership is a violation of best practice. Similarly, the borrowing of shares in order to deliberately reduce or suppress the vote at a shareholders' meeting is bad practice.

2.2 Accordingly, the borrowing of shares for the purpose of exercising the right of the shareholder's vote is to be discouraged by all lenders.

2.3 The borrower of a share, for whatever purpose, should not vote that share without the express permission of the lender, and in accordance with his instructions.

2.4 Similarly, the holder of a share as collateral should not vote that share, unless specifically given the exclusive right to do so by private treaty with the borrower who provided the collateral.

2.5 The lender's Master Lending Agreement should specify that shares are not being lent for the principal purpose of voting those shares, and should provide clear guidance as to what circumstances might permit a borrower to vote borrowed shares as well as what the responsibilities of any lending agents might be in those circumstances.

2.6 No lender or lending agent should knowingly enter into a scheme in which it is making shares available to a borrower for the primary purpose of voting them, or of otherwise attempting to exert control upon the issuing company by means of the voting right attached to the borrowed shares.

3 *Lending policy, lending contracts, transparency, and disclosure.*

3.1 Policy on lending, and in what circumstances lending is to be considered subordinate to voting, should be a responsibility of the trustees or the directors of the fund or portfolio from which shares are to be lent.

3.1.1 A written statement of the lending policy should be communicated to any other entities up and down the chain of ownership which might have any reason to become involved with lending or voting decisions.

3.1.2 The lending policy statement should also be made available to the ultimate beneficiaries of the portfolio or fund. This document should make clear under what general circumstances loans are likely to be recalled for voting purposes, and the approximate extent of loan activity envisioned.

3.2 The lending contract should be negotiated with the full knowledge and active participation of the primary lender of the securities if the lending is to be done by an agent. Any subsequent changes to the contract or other departures from standard practice should be discussed beforehand with the primary lender or its manager responsible for the shares in question.

3.3 It is recommended that lenders rely upon a contract which protects their rights and provides full compensation or damages with respect to all corporate actions, as well as allowing for recall in the event of a vote the lender deems controversial and appropriate for recall.

3.4 In the event of failure to deliver like shares when they have been recalled for the purpose of voting, the penalties should be the same as for failure to deliver for any other reason.

4 *Communication of lending activity.*

4.1 It should be incumbent upon whoever is responsible for actual lending—whether it be a division of the primary manager, the primary manager's custodian, or any other agent of the primary manager or the holding chain—to update the data on any lending activity and on attendant changes in the relevant portfolio. This data should be furnished to all those personnel responsible for management of that portfolio, and to those responsible for voting decisions and for the implementation of corporate governance policy.

4.2 Such data should be made available in a timely fashion, normally by the close of business each day.

4.3 If responsibility for portfolio management and/or voting decisions has been delegated by the primary manager to another agent not in the chain of control between the primary manager and the lending agent, a separate chain of communication should be set up, and the lending agent required to inform directly this entity (or these entities) of lending activity and changes in the composition of the portfolio resulting therefrom.

5 *Communication regarding proxy material, record or blocking dates, and decision dates.*

5.1 The following personnel are potentially in need of information regarding meeting agendas and dates, the text of proposals, key decision dates, and parameters for any proxy vote or other corporate action which might trigger a recall:

(a) The portfolio manager directly responsible for buy and sell decisions concerning the stock in question
(b) Whoever is responsible for proxy voting decisions regarding the same security
(c) The party responsible for implementing corporate governance policy
(d) The principal manager of the fund involved if different from above.

5.2 Primary lenders should ensure that the proper mechanisms for timely dissemination of this information are in place, so that all of these key decision makers are informed sufficiently ahead of decision deadlines that they may make appropriate judgments in accordance with their particular mandates. This may require some sort of routine distribution of communications from the custodian, and/or from other services.

6 *Resolution of disputes involving recall.*

6.1 The Primary Lender's Policy Statement, as well as the Master Lending Agreement, should prescribe a formal mechanism to resolve any dispute arising from a difference of opinion as to whether a given share should be left out on loan or recalled.

6.2 Such a dispute-resolving mechanism should fairly represent the different perspectives of investment managers, corporate governance staff, and the exigencies of lending.

6.3 Decisions should be made in accordance with the primary lender's stated lending policy, its governance policy, and the explicit objectives of the fund. The object is to resolve the conflict between short-term revenue maximization and longer-term investment or governance goals.

6.4 The decisions of the resolving mechanism should be a matter of record to be communicated to those responsible for setting and enforcing corporate governance policy at the primary lender or its manager.

7 *Record dates.*

7.1 Record dates pose a special challenge to the lender of securities, as they may be significantly divorced in time from the date of the actual vote.

7.2 In those jurisdictions in which it has been the practice for the issuer to publish and distribute proxy material and the agenda of the shareholders' meeting only after the record date and only to shareholders of record on that date, it may be difficult or impossible for lenders to know whether they might want to recall shares for voting in advance of the record date.

7.2.1 To circumvent this conundrum, issuers should promulgate the agenda for upcoming shareholders' meetings publicly (e.g., by posting at the company's website) sufficiently in advance of the record date that lenders may have time to recall should they decide to do so. This is in keeping with the "Issuer's Recommended Actions" delineated in Appendix I. C. above.

7.2.2 In the absence of such provision by issuers, lending institutions in those jurisdictions can only make reasonable efforts to learn whether an upcoming shareholder vote is likely to be sufficiently controversial under their own voting guidelines that they should consider recalling the relevant share in advance of the record date.

7.2.3 Absent resources for such information gathering, it may be impossible for lenders to pursue a policy of recalling lent shares 'in the event of an important or controversial vote.'

7.3 When the record date or its functional equivalent is near in time to the shareholders' meeting, and the agenda has already been distributed some time before, this problem does not arise.

8 *Dividend dates.*

8.1 Another common use of lending is for dividend swaps. For this strategy to be employed, the share must be lent over a dividend record date. Obviously, the lender loses the vote over that period, which may coincide with the meeting date, or the record date for voting in a record date jurisdiction.

8.2 Lending institutions should be aware of this hidden consequence of such a lending transaction.

8.3 Issuers are also urged to separate dividend record dates sufficiently from voting record dates or whatever other dates are ruling for eligibility to vote (e.g., reconciliation date, the date of the meeting, etc.), so that transactions of this type do not reduce the valid shareholder vote, or confuse the question of who is the proper beneficial owner entitled to vote.

9 *Lending policy and risk.*

9.1 By lending shares, a portfolio's risk characteristics may be changed significantly. Normally, the standard contracts and practices in use successfully counter that possibility, but exceptions may exist.

9.2 In those markets in which the lender's margins are determined or affected by the reinvestment of the collateral required for the loan, additional assessments of risk are necessary, and additional controls may be warranted to ensure that lending agents do not exceed the risk parameters appropriate for that portfolio.

10 *Disclosure of lending activity.*

10.1 As a general matter, lending activity is not reported to outside parties or to individual fund beneficiaries, except where provided for by contract or by law.

10.2 However, the net income obtained from lending ought to be separately accounted for in regular reports to beneficiaries, since it is neither appropriate to regard it as a part of investment return, nor should it be allowed to conceal the actual costs of custody, transfer, and other administrative costs, or the costs attendant upon the actual lending program itself.

10.3 Additionally, in any public report on voting decisions made during the preceding year, the instances in which shares were not voted because they were out on loan, and the resultant 'under-vote' of shares, by percentage or by actual number, ought to be disclosed to beneficiaries of the reporting funds.

Appendix III

Definitions

Mechanics of lending:
A **stock loan** is any transaction in which the owner of a share or his or her authorised agent transfers control and use of the security to a counter-party, the borrower, in exchange for an agreement for a similar share to be delivered to him or her at a future date, normally with further agreement with the borrower to be made whole for the equivalent of any distributions made to the shareholders in the interim. Although legally different, a stock loan somewhat resembles a sale and repurchase agreement. Unlike a sale and repurchase agreement, however, the borrower usually deposits collateral with the lender normally worth 102% to 105% of the value of the lent securities. Also unlike a sale and repurchase, the rights of the lender with respect to this collateral may be greatly limited.

Collateral for the loan may be either cash or securities, or a combination of the two. It is sometimes the case that the return the lender expects to obtain from the collateral for the duration of the loan is the lender's margin of profit on the transaction. In these cases, the use put to the collateral may alter the risk characteristics of the portfolio from which shares have been lent. The collateral is normally adjusted on at least a daily basis to compensate for fluctuations in the market price of the share.

Recall of a securities loan can normally be initiated by the original lender at any time, on varying terms and within a time frame depending upon the lending contract. 'Recall' is also normally a misnomer, as most of the time equivalent shares to those loaned will have to be purchased in the market to satisfy the recall. At the same time, the borrower's collateral must be returned; thus, the whole lending transaction is unwound upon recall.

Parties to a lending transaction:
The **lender** of a security is the party, whether the beneficial owner, its agent, or a whole hierarchy of agents appointed to exercise control over beneficial owners' investments, which surrenders control of the share in exchange for specific agreements to be made whole at some (usually indefinite) future date. The **primary lender** of this same security is the beneficial owner of that security authorising the lending of it, or the most senior agent of those individuals who are collectively beneficial owners of that security. The **lending agent** is a party other than the beneficial owner or primary lender which is charged with effecting loans on behalf of the primary lender.

The **ownership chain** is the totality of the structure (which may be very complex, especially in the case of cross-border investments) of the fiduciaries, trustees, principal managers, sub-managers, custodians, sub-custodians, nominees, proxy agents, and other entities ultimately responsible for the management, administration, custody, voting, and lending of an ultimate beneficiary's securities, and responsible, directly or indirectly, to that ultimate beneficiary. Not all of these agents are necessarily a part of the same hierarchy; e.g., there may be separate chains for custody and for portfolio management, both reporting to a principal manager or fund higher up in the chain.

The **principal manager** is that party highest in the ownership chain which is authorised to make portfolio management decisions on behalf of the beneficial owner(s). Often the principal manager is authorised to make voting decisions and sometimes to set governance policy as well. The principal manager may or may not be the same as the primary lender.

The **borrower** of the security is the party entering into the agreement which takes receipt of the borrowed stock. The borrower may be a principal borrowing for its own account, or be acting on behalf of a client; more often it is the latter.

The **registered owner** or **owner of record** is the shareowner whose name appears on the books of the company as entitled to vote shares and to receive dividends. When a share has been sold short in the market, or has been tendered in lieu of a fail, the new *bona fide* purchaser becomes the owner of record, in place of the lender. Thus, during the period of a loan, the lender will not be the owner of record, and cannot vote those shares.

Uses of lending:

Short selling is the practice by which a borrower of stock hopes to profit from a decline in the price per share by selling borrowed shares in the market, and repurchasing equivalent shares subsequently for delivery back to the lender at a lower price. Short selling may also be employed as part of a hedging strategy, in which the seller is merely trying to protect itself against the risk of loss from a share price decline. In either case, an essential part of this strategy is the borrowing of shares.

Hypothecation is the practice in which a securities market intermediary deposits liquid securities in a special blocked account in order to meet a regulatory requirement with respect to the ratio of securities held as a percentage of the total obligations of that intermediary. This is another common reason for borrowing shares.

A **fail** is the industry term for the situation in which a securities intermediary cannot deliver securities to the counter-party purchaser in a valid trade. This is yet another important reason for borrowing shares.

Dividend swaps are employed when an investor cannot take advantage of tax benefits which may accrue to another, or cannot use investment opportunities (such as a scrip dividend alternative) more valuable to another investor, and decides to lend the shares to a borrower for whom the dividend is more valuable. Thus, both share in the benefit.