



**ASIC**

Australian Securities & Investments Commission

# **Facilitating debt raising Regulation Impact Statement**

**May 2010**

# What this Regulation Impact Statement is about

This Regulation Impact Statement (RIS) addresses the Australian Securities and Investments Commission's (ASIC's) proposed policy on facilitating debt raising. This follows a Consultation Paper published in December 2009 setting out our proposals for facilitating certain offers of corporate bonds to retail investors and offers of convertible notes to institutional investors: see Consultation Paper 126 *Facilitating debt raising* (CP 126).

In developing our final position, we need to consider the regulatory and financial impact of our proposals. We are aiming to strike an appropriate balance between:

- maintaining standards of consumer protection;
- expanding suitable investment opportunities for retail investors; and
- developing the Australian quoted debt market.

This RIS sets out our assessment of the regulatory and financial impacts of our proposed policy and our achievement of this balance. It deals with:

- the likely compliance costs;
- the likely effect on competition; and
- other impacts, costs and benefits.

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# Issues

## Background

### Consultation Paper 126 Facilitating debt raising

1. In Consultation Paper 126 *Facilitating debt raising* (CP 126), ASIC consulted on relief to facilitate certain offers of ‘vanilla’ corporate bonds.
2. We proposed to grant relief from the fundraising provisions in Ch 6D of the *Corporations Act* (all sections, chapters and parts referred to in this RIS are from the *Corporations Act* unless otherwise stated) to facilitate efficient corporate bond raisings by listed entities, provided that investor protection was not unduly compromised. We proposed relief to allow a listed entity to offer vanilla bonds using a simplified prospectus (vanilla bonds prospectus) with a similar level of content to a transaction-specific prospectus under section 713.
3. We proposed that our relief would only apply if various conditions were satisfied, relating to:
  - (a) the bonds – relief would only apply to vanilla bonds that would be quoted on issue and where the issue was for a total of at least \$100 million (following submissions, we are now proposing that this limit be \$50 million);
  - (b) the issuer – the issuer must be entitled to use a transaction-specific prospectus for an offer of continuously quoted securities, and the most recent financial statements of the issuer must be unmodified; and
  - (c) disclosure – point of sale disclosure must be provided for various matters (including key financial disclosures). Ongoing disclosure must also be provided for certain matters (including updates of key financial disclosures).
4. We also proposed relief to allow a vanilla bonds prospectus to be in two parts, comprising:
  - (a) a base prospectus, which could be used for several different offers; and
  - (b) a second part prospectus, which would relate to a particular offer.

5. Finally, we consulted on providing relief in relation to offers of convertible notes to wholesale investors. In practice, these offers require a prospectus so that the underlying quoted securities can be on-sold to retail investors. We proposed relief so that the underlying quoted securities can be on-sold without a prospectus if a cleansing notice containing prospectus-like disclosure is provided to the relevant market operator at the time the convertible notes are issued.

### **Corporate bonds and convertible notes**

6. A corporate bond is a debt instrument in which an investor loans money to a corporate entity for a defined period of time at a fixed or floating interest rate. The issuer identifies the interest rate payable, when it is payable and promises to repay the face value of the bond to the holder at maturity. For a fixed rate bond, the interest rate prevails for the life of the bond. For a floating rate bond, the interest rate payable usually varies according to a market determined base rate plus a margin (fixed at the time of issue).
7. Other types of corporate bond include a convertible note and a hybrid security. A convertible note is an interest paying debt security that converts to the issuer's ordinary shares at maturity (or earlier). A hybrid is a relatively complex bond structure that typically combines two or more types of instruments and may or may not require conversion to ordinary equity at a specified date.

### **Retail debt market**

8. There is currently only a limited retail debt market in Australia and retail investors have difficulty obtaining exposure to corporate bonds. Major companies often prefer the US or European debt markets or the Australian institutional market for reasons of price, cost and simplicity. An analysis by ASIC of the investment by retail investors in corporate bonds has identified that:
  - (a) Retail investors' direct exposure to corporate bonds is presently very limited – household investment in corporate bonds represents 0.26% of the value of their total financial assets. In contrast, for wholesale funds, fixed interest securities currently represent 32% of funds under management.
  - (b) Between January and November 2009, there were only five retail bond offerings totalling \$659 million, which constituted 0.87% of the total amount of corporate issuance in that period.

9. Recently, there have been some successful retail bond issues listed on ASX. Companies are also expected to increase their issuance of bonds to refinance existing bank debt and seek to broaden their range of funding sources. Further, larger companies may seek to diversify their funding base to attract retail investors even if they presently have easy access to the wholesale debt markets.
10. Investing in corporate bond offers some advantages to retail investors, including allowing them to diversify their portfolio across equities and fixed income products. However, corporate bonds are also subject to a number of investment risks. Therefore, we have proposed that our relief will be subject to conditions relating to the issuer, the type of bonds that may be issued and disclosure.

### Current regulation of retail corporate bond offerings

11. An offer of corporate bonds to retail investors is regulated under the *Corporations Act*. A corporate bond is a debenture, so the obligations for the offer of securities in Ch 6D apply to the offer of corporate bonds, including the requirement to prepare a prospectus. Where the offer is made only to wholesale or professional investors, a prospectus is not required.
12. Chapter 2L imposes various requirements in relation to corporate bonds and other debentures that are issued under a prospectus, including the requirement that an issuer of corporate bonds must enter into a trust deed and appoint a trustee for the benefit of bondholders. Persons who suffer loss or damage as the result of a contravention of Ch 2L also have the right to recover such loss. We propose to provide minimal relief from these requirements in relation to an offer of vanilla bonds, namely relief so that the quarterly reports required to be prepared by issuers under s283BF do not need to contain certain information in relation to their subsidiaries (unless the information is material to the issuer or any guarantor).

### Prospectus disclosure

#### *Overview of s713*

13. The *Corporations Act* allows a disclosing entity that offers continuously quoted securities, options over such securities or convertible notes that convert into such securities to use a transaction-specific prospectus: s713 and Class Order [CO 00/195] *Offer of convertible securities under s713*.

14. A transaction-specific prospectus does not need to include all of the information that is contained in a full prospectus. It focuses on the terms of the offer and the effect of the offer on the entity. The key information required in a transaction-specific prospectus for an offer of securities includes:
- (a) the terms and conditions of the offer;
  - (b) the effect of the offer on the entity;
  - (c) the rights and liabilities attaching to the securities offered;
  - (d) if the securities are options, the rights and liabilities attaching to:
    - (1) the options themselves; and
    - (2) the underlying securities; and
  - (e) any other information not previously disclosed to the market, which covers information excluded from a continuous disclosure notice under the ASX Listing Rules.

Note: Other information is also prescribed by s711 and 713. Information that is prescribed by s710 but not by s713 may also need to be included in a transaction-specific prospectus in certain circumstances (e.g. if it is necessary to ensure that the prospectus is not misleading or deceptive).

15. The rationale for this reduced content requirement is that where a disclosing entity issues continuously quoted securities, the market will have already received relevant information through compliance with the continuous disclosure regime so that a full prospectus is not necessary: see Regulatory Guide 66 *Transaction-specific disclosure* (RG 66) at RG 66.7–66.8.

#### *Overview of s710*

16. By comparison, under s710 a full prospectus must contain all the information that investors and their professional advisers would reasonably require to make an informed assessment on:
- (a) the rights and liabilities attaching to the securities offered; and
  - (b) the assets and liabilities, financial position and performance, profits and losses, and prospects of the issuer.
17. The s710 requirements impose more onerous disclosure obligations on issuers than the s713 requirements. This is because the s713 requirements mandate only certain specific disclosures

(as noted above), and assume that the market has already obtained relevant information about the issuer through continuous disclosure. In contrast, the s710 obligations are designed to operate on the basis that the market has little or no information on the issuer. Accordingly, the scope of s710 is much wider and a prospectus prepared in accordance with that section will require more detailed disclosure on the company and its overall prospects.

18. For example, a s710 prospectus could be expected to contain detailed information on the company, its business (or proposed business), its financial standing and its prospects. A transaction-specific prospectus would not be required to include similar levels of information, as the market would be expected to already have an understanding of this information.
19. For both a transaction-specific prospectus and a s710 prospectus, the persons liable in relation to a prospectus are the company making the offer, each director of the company (and each proposed director named in the prospectus with their consent), an underwriter named in the prospectus with their consent and other persons named in the prospectus as having consented to the inclusion of statements by them in the prospectus.
20. An issuer is able to use a transaction-specific prospectus for an offer of corporate bonds that are in the same class as existing quoted corporate bonds: s713. In practice, the ability of issuers to make use of this exception is limited since:
  - (a) only a small number of entities have corporate bonds that are currently quoted; and
  - (b) if an issuer wishes to offer new corporate bonds that have a different term or a different rate of return to existing bonds, the new bonds will be in a different class and they will fall outside the transaction-specific prospectus provisions in s713.

### Current regulation of offers of convertible notes to institutional investors

21. Some offers of convertible notes are only marketed to institutional investors (including offshore institutional investors). These offers do not require a prospectus or a Product Disclosure Statement (PDS) because there is no retail participation. Similarly, the secondary sale of such convertible notes is limited to persons who do not require a prospectus or PDS.



22. In the last two years, there have been only a small number of offers of convertible notes to institutional investors in Australia. In contrast, there were approximately US\$75 billion worth of convertible notes issued globally in 2009 alone.
23. Although such issues and sales of convertible notes do not require a prospectus or a PDS, following conversion the underlying quoted securities may be on-sold to retail investors. Without relief, a prospectus or PDS would generally be required for an on-sale of the underlying securities to retail investors within 12 months of the conversion unless the issuer:
- (a) provides a cleansing notice on each conversion so that the on-sales fall within the exemption in s708A(5) or 1012DA(5); or
  - (b) has prepared a prospectus or PDS for the initial offer of the convertible notes so that the on-sale of the underlying securities falls within Class Order [CO 04/671] *Disclosure for on-sale of securities and other financial products*.

Note: A transaction-specific prospectus may be used if the issuer satisfies the requirements of [CO 00/195].

24. The option of providing a cleansing notice on each conversion is often unattractive to issuers because:
- (a) there may be multiple conversions that would each require a cleansing notice;
  - (b) the timing of the conversions may not be within the control of the issuer; and
  - (c) a cleansing notice may require disclosure of confidential information that would otherwise fall within an exception to ASX Listing Rule 3.1.
25. The option of preparing a prospectus for the issue of the convertible notes may also be unattractive. One reason for this is that there are a range of people who are potentially liable for a prospectus, not just the issuer: s729. This can make due diligence more involved than would be the case for an information memorandum prepared for institutional investors.

### Report by the Australian Financial Centre Forum

26. In January 2010, the Government released a report from Australian Financial Centre Forum, which provided various recommendations to boost trade in financial services and further

improve the competitiveness and efficiency of the financial sector (**AFCF report**). The AFCF report recommended relaxing regulatory requirements for the issue of certain corporate bonds. Our proposed relief for corporate bonds is broadly consistent with the recommendations in the AFCF report.

### ASIC's current policy

27. ASIC currently does not provide disclosure relief for offers of corporate bonds. Consequently, a full prospectus is required for an offer of corporate bonds unless they are in the same class as existing quoted bonds.
28. ASIC currently does not provide on-sale relief for quoted securities issued on the conversion of unquoted convertible securities where the convertible securities were issued pursuant to a cleansing notice.

### ***What is the issue/problem being addressed?***

29. There are currently only a limited number of offers of corporate bonds to retail investors. Suitable relief to facilitate certain offers of vanilla corporate bonds has the potential to assist issuers (by simplifying the time and expense involved in preparing a prospectus for such offers) and to benefit retail investors (by allowing them to diversify their investment portfolios to include greater direct investment in corporate bonds).
30. As mentioned in paragraphs 24-25 above, offers of convertible notes to wholesale investors can be unattractive to issuers because of the need to ensure that the underlying quoted securities can be on-sold to retail investors.

## Objectives

31. ASIC is seeking to strike an appropriate balance between:
  - (a) maintaining standards of consumer protection;
  - (b) expanding suitable investment opportunities for retail investors; and
  - (c) developing the Australian quoted debt market.

# Options

## ***Option 1 – do nothing***

32. One option is that ASIC not provide any relief in relation to offers of corporate bonds or convertible notes. Under this option, ASIC would continue to administer the law under its current policy settings. For example, a full prospectus would continue to be required for offers of corporate bonds unless they were in the same class as existing quoted bonds.

## ***Option 2 – provide disclosure relief for offers of corporate bonds (subject to conditions relating to the bonds that may be issued, the issuer and disclosure) and provide on-sale relief for wholesale offers of convertible notes***

33. This option seeks to provide relief that will facilitate offers of corporate bonds to retail investors and offers of convertible notes to wholesale investors, while maintaining market integrity and investor protection.

34. Under this option, we would provide relief:

- (a) to allow offers of corporate bonds to be made using a ‘vanilla bonds prospectus’, which has similar content requirements to a transaction-specific prospectus. The conditions for relief include that:
  - (1) the issuer is entitled to use a transaction-specific prospectus for an offer of its existing quoted securities (e.g. its ordinary shares) and trading in those securities has not been suspended for more than five days in the previous 12 months;
  - (2) the corporate bonds are ‘vanilla’ bonds that do not have complex features (e.g. would not be subordinated or convertible into other securities and would have a maximum term of 10 years) and that would be quoted on issue;
  - (3) the aggregate size of the bond issue is at least \$50 million (this condition would lapse after 2 years unless renewed);

- (4) the auditor's report on the most recent annual financial report, and any subsequent half-yearly financial report, is unmodified;
  - (5) the vanilla bonds prospectus discloses certain specified matters (including key financial disclosures); and
  - (6) the issuer facilitates investor access to ongoing disclosure (including half-yearly and annual updates of key financial information);
- (b) to allow issuers who are entitled to use a vanilla bonds prospectus to issue bonds under a two-part vanilla bonds prospectus that comprises a base prospectus (that could be used for a number of different offers) and a second part prospectus (that contains information on a specific offer of bonds). Together, the base prospectus and the second part prospectus must contain all the information that would be required in a vanilla bonds prospectus. The base prospectus would have a maximum life of 2 years;
- (c) so that a prospectus for an offer of vanilla bonds is not subject to an exposure period of between 7 and 14 days under s727(3) if the bonds would be in the same class as existing quoted bonds but for differences in the term, interest rate and interest payment dates. That is, applications could be accepted under the prospectus from the date of the prospectus; and
- (d) for offers of convertible notes to institutional investors, so that the underlying securities can be on-sold to retail investors without a prospectus or PDS. Instead, the issuer would need to provide a cleansing notice containing prospectus-like disclosure at the time the convertible securities were issued. A further condition of the relief would require certain ongoing disclosures to be included in the annual report of the issuer during the term of the convertible notes.

## Impact analysis

### *Affected parties*

35. The key parties affected by the proposed policy would be:

- (a) companies issuing corporate bonds to retail investors or convertible notes to wholesale investors; and
- (b) retail investors who wish to invest in corporate bonds.

### ***Costs and benefits of each option***

#### Option 1 – do nothing

#### **Benefits**

##### *Benefits to business*

36. There are no direct benefits that would accrue to business by not implementing the proposed relief. The proposed relief is designed to reduce the burdens placed on companies in offering corporate bonds to retail investors and offering convertible securities to wholesale investors. By maintaining the status quo these burdens would not be reduced.

##### *Benefits to retail investors*

37. There are no direct benefits that would accrue to retail investors by not implementing the proposed relief. Maintaining the status quo would not increase the likelihood of issuers offering corporate bonds to retail investors. However, doing nothing would mean that retail investors would continue to receive full prospectus disclosure for offers of corporate bonds that were made to them.

#### **Costs**

##### *Costs to business*

38. There are no direct costs that would be imposed on business by not implementing the proposed relief. However, the existing costs of offering corporate bonds to retail investors would remain, and the current impediments to offers of corporate bonds to retail investors and offers of convertible notes to wholesale investors would remain.

39. The AFCF report noted that the costs associated with issuing corporate bonds to retail investors may discourage such issues and make it difficult for listed companies to compete with bank deposits and other asset classes: see page 94. Submissions to CP 126 also noted the onerous regulatory requirements faced by companies relative to other sources of debt capital in offering

corporate bonds to retail investors, and suggested that a reduction in the cost of compliance with such regulatory requirements may assist in the development of a liquid and diverse retail corporate bond market.

*Costs to retail investors*

40. There are no costs that would be imposed on retail investors by not implementing the relief. However, investors would also not be given increased opportunities to participate directly in offers of corporate bonds. This in turn would mean that investors would not be afforded greater opportunities to diversify their investment portfolios by investing in corporate bonds.

Option 2 – provide disclosure relief for offers of corporate bonds (subject to conditions relating to the bonds that may be issued, the issuer and disclosure) and provide on-sale relief for wholesale offers of convertible notes

**Benefits**

*Benefits to business*

41. There are a number of benefits available to business through the implementation of the proposed relief and submissions to CP 126 generally supported relief (although raising matters of detail). One of the main benefits would be a reduction in compliance costs, as companies would no longer be required to make full prospectus disclosure in relation to an offer of corporate bonds to retail investors. Instead, companies would be entitled to issue a vanilla bonds prospectus with similar content requirements to that of a prospectus prepared in accordance with section 713 of the *Corporations Act*. The disclosures required in a vanilla bonds prospectus as proposed are less onerous than the level of disclosure required in a prospectus prepared under section 710 of the *Corporations Act*. For example, a vanilla bonds prospectus would not need to include the level of detail that an issuer would be required to disclose under s710 in relation to the company, its activities, its financial standing and its prospects.
42. Although reduced disclosure requirements should benefit business, we note that there are other factors that are relevant to whether an issuer seeks debt financing from retail investors or some other source (e.g. bank finance or institutional investors). These other factors include the availability and certainty of funding from different sources, the interest rate the borrower will be required to pay, the time it is likely to take for a debt issue to be subscribed,

the level of disclosure required by the issuer and the potential liability of the issuer and its directors in relation to such disclosure.

43. The AFCF report stated that ‘Treasurers for both large and small companies shared the view that, at the retail level, prospectus requirements were onerous’: page 40. The AFCF report also stated that ‘the Forum considers that the prospectus requirements for listed companies issuing *listed* debt securities to retail investors should not be more onerous than for the same companies issuing further shares to retail investors’. A transaction-specific prospectus under s713 can currently be used for offers of quoted shares, options over quoted shares and convertible notes that convert into quoted shares.
44. Consistent with this, the AFCF report also noted that an objective in relaxing the regulatory requirements for issues of corporate bonds would also be to significantly improve speed to market, allowing companies to take advantage of market opportunities and respond to their financing requirements in a timely manner: page 94.
45. The development of a retail corporate bond market would also increase funding flexibility for companies by offering them an alternative method of debt financing. Submissions to CP 126 noted that the development of a retail corporate bond market would mitigate the dependence on offshore funding and bank lending for debt financing.
46. Finally, developing the corporate bond market might have more general benefits for business. The AFCF report noted (at page 39) that ‘If Australia is to develop into a leading financial centre that provides liquid and efficient financial services across a broad range of products and asset classes, then a more diversified and liquid bond market should be part of that vision.’
47. The ability to use a two-part prospectus for offers of vanilla bonds should benefit issuers who are undertaking multiple issues of vanilla bonds. Having a base prospectus which can be used for a number of offers should increase speed to market.
48. The key benefit in our proposal to facilitate offers of convertible notes to wholesale investors is that the due diligence process for such offers would be simplified, potentially allowing such offers to be made within a shorter timeframe than is currently the case. Submissions to CP 126 generally supported relief for such offers.

#### *Benefits to retail investors*

49. To the extent that it facilitated offers of corporate bonds to retail investors, our relief would provide retail investors with a greater opportunity to invest directly in corporate bonds and diversify their investment portfolios than is currently the case. As discussed in paragraph 8, at present retail investors only have a very limited direct exposure to corporate bonds. However, as mentioned in paragraph 42, there are a number of other factors that are relevant to how an issuer seeks to obtain debt financing. Although not requiring the same level of disclosure as a full prospectus, we consider that the conditions of our proposed relief for offers of corporate bonds will benefit retail investors in the following ways:
- (a) Our relief will mandate certain key financial disclosures (e.g. gearing ratio, interest cover and working capital ratio). These will provide useful information to investors and there is currently no specific requirement for these to be included in a prospectus for an offer of corporate bonds. Further, these ratios will be disclosed in a consistent fashion by issuers that rely on our relief, assisting investors to compare offers of vanilla bonds.
  - (b) Our relief will also require investors to be provided with half-year and annual updates of the key financial disclosures, which will assist investors to monitor their investment.
  - (c) ASIC prepared an example of a vanilla bonds prospectus, which was the subject of consumer testing. During consumer testing, participants gave strong favourable feedback on the document's structure, layout and content. They were also particularly supportive of the information in it dealing with the issuer's financial capability, including financial ratios.
50. The proposal to facilitate offers of convertible notes to wholesale investors should not have a material impact on retail investors. The convertible notes may only be issued or transferred to wholesale investors and prospectus-like disclosure in relation to the convertible notes and underlying quoted securities will continue to be provided to the market.

## Costs

### *Costs to business*

51. The reduction in costs under the proposed relief for corporate bonds is one of the key benefits that would accrue to business. There would be nonetheless be start-up and ongoing costs involved in the establishment and maintenance of a listed



corporate debt program. However, compliance with the requirements of the proposed relief should be less onerous than compliance with the current requirements of the *Corporations Act*. Further, it would be open to companies to continue to comply with the existing requirements if they preferred.

52. As discussed in paragraph 48, our proposed relief for offers of convertible notes to wholesale investors should also reduce costs for issuers. Nonetheless, it would be open to issuers to continue to comply with the existing disclosure regime if they considered that the costs of our relief outweighed the benefits.

*Costs to retail investors*

53. Under our relief, retail investors would not receive a full s710 prospectus for offers of corporate bonds. However, we consider that retail investors should still receive sufficient disclosure to make an informed investment decision. The reasons for this are:
- (a) The conditions on the relief will mean that only those issuers who already have a class of continuously quoted securities on issue will be able to rely on the relief. This will ensure that there is a substantial amount of information already in the market regarding the issuer prior to any offer of corporate bonds to retail investors. Further, we have mandated that only ‘vanilla’ bonds may be offered under the relief – these are bonds that do not have complex or unusual terms and conditions. Retail investors are more likely to understand the risks and features of vanilla bonds than they are for more complex bonds.
  - (b) Under the relief, a prospectus for vanilla bonds must contain disclosure on a number of matters, including: the key features, risks and benefits of the bonds; a number of key financial disclosures, including various ratios; the effect of the offer on the issuer; and disclosure of any other information that would be required under a transaction-specific prospectus as if the bonds were continuously quoted securities. Disclosure of these matters will provide investors with important information about the key risks and features of the bonds.
  - (c) Issuers must also comply with various ongoing disclosure requirements, including publishing half-yearly updates of the key financial disclosures and quarterly reports on their website and providing these updates to ASX. The issuer must also publish copies of other ongoing disclosures on their

website. Furthermore, issuers must give investors the option of receiving email notification of all continuous disclosure notices published by the issuer on ASX.

- (d) The level of information to be provided to retail investors in a vanilla bonds prospectus would be greater than for a transaction-specific prospectus, which can currently be used for offers of quoted shares and for securities that are convertible into quoted shares. Quoted bonds are generally a less risky investment than quoted shares since bondholders rank above shareholders in a liquidation. Convertible notes are a more complex product than vanilla bonds.
- (e) ASIC has published an investor guide, *Investing in corporate bonds?* Our relief will require that a vanilla bonds prospectus must give investors information about how to obtain this guide. This should assist retail investors in vanilla bonds to make better informed investment decisions.
- (f) As mentioned in paragraph 49(c), consumer testing of an example of a vanilla bonds prospectus prepared by ASIC received strong favourable feedback on the document's structure, layout and content.
- (g) The ability of issuers to use a two-part prospectus should not disadvantage investors. A two-part prospectus is subject to the same information requirements as a vanilla bonds prospectus and the information must be presented in a clear, concise and effective manner.

*Wider impacts on the retail bond market*

- 54. Our relief could lead to an increase in the number of offers of corporate bonds to retail investors (although the factors discussed in paragraph 42 will also be relevant to how an issuer chooses to raise funds). Given the current limited ability of retail investor to invest in corporate bonds, we think there would be potential benefits for retail investors in providing them with a greater ability to invest in corporate bonds and diversify their investment portfolios.
- 55. As discussed in paragraph 50, our proposals in relation to offers of convertible notes should not have a material impact on retail investors.
- 56. Overall, we consider that the regulatory benefit of Option 2 – the lower cost to issuers with a history of continuous disclosure, mandating certain disclosures and potentially increasing the ability

of retail investors to invest in vanilla bonds – outweighs the risks involved in reducing the amount of information that is currently required to be included in a prospectus for vanilla bonds.

## Consultation

57. In December 2009, ASIC published Consultation Paper 126 *Facilitating debt raising* (CP 126), which set out our proposals for simplifying the disclosure requirements for certain offers of corporate bonds and facilitating issues of convertible notes to wholesale investors. ASIC invited submissions comments on our proposed policy and asked for quantitative and qualitative information. As mentioned in paragraph 49(c), ASIC also prepared an example of a vanilla bonds prospectus which was the subject of consumer testing.

58. The consultation period ended on 19 February 2010. ASIC received 31 written submissions from stakeholders, including industry associations, industry participants and law firms. There was general support for our proposals to facilitate corporate bond raisings and offers of convertible notes, although submissions raised matters of detail. The following are examples of some of the views expressed in the written submissions:

- (a) The majority of respondents were in favour of disclosure relief for issues of corporate bonds (subject to certain suggested changes), and noted that relief would benefit issuers by lowering costs and increasing speed to market. Some mentioned, however, the risk that relief may be underutilised due to the competitiveness of other debt funding sources, and the directors' liability and disclosure requirements associated with the prospectus regime (directors of an issuer have statutory liability for the content of a prospectus under the prospectus provisions – they may not be subject to the same level of personal liability for other types of offer). Respondents also noted the associated benefits available to retail investors, including greater access for retail investors to bond issues and a greater ability to diversify investment portfolios.
- (b) A number of respondents considered that subordinated bonds should be able to qualify as vanilla bonds, particularly if they were issued by APRA-regulated entities for regulatory capital purposes. We do not propose to extend our relief to subordinated bonds at this stage due to the greater risk of a

capital loss or a failure to meet interest payments than for senior debt. We intend to review how our relief is operating and, in light of that information, consult further within the next 12 months on whether relief should extend to offers of subordinated bonds (including offers of subordinated bonds by APRA-regulated entities for regulatory capital purposes).

- (c) Respondents were divided on the appropriate level of minimum subscription for vanilla bond issues, with some suggesting that at least \$100 million would be necessary in order to provide sufficient liquidity in the secondary market. Others considered that the level should be no higher than \$50 million in order to promote participation by smaller entities (who may otherwise be disqualified by the proposed \$100 million minimum). We have reduced the minimum subscription size from \$100 million to \$50 million in order to make our relief available to a greater range of issuers. The minimum subscription requirement will lapse after 2 years and we will review it prior to that time in light of how our relief is operating.
- (d) A number of respondents submitted that the proposed key financial metrics we are requiring to be disclosed may not be able to be compared across industries and may not be understood by investors. Other respondents noted that the metrics were commonly used and appropriate. Consumer testing undertaken by us supported the disclosure of key metrics to retail investors. We have retained the requirement for the metrics to be disclosed as we think they will provide useful information for investors.
- (e) A number of respondents submitted that rather than requiring issuers to satisfy financial metrics in order to rely on the relief, ASIC should impose a requirement that the bonds have an investment-grade credit rating. Some submissions considered that a credit rating is a better assessment of the creditworthiness than the financial metrics proposed. We have not required that corporate bonds must have an investment-grade credit rating in order for issuers to be able to rely on our relief. There are currently no credit rating agencies with an Australian financial services licence that covers the provision of credit ratings to retail investors. Accordingly, if our relief required a credit rating to be obtained and provided to retail investors, it could not be used.
- (f) There was a significant level of support for our proposed two-part prospectus relief. Respondents noted that this would

provide greater flexibility to issuers while not diminishing investor protections, and that this aspect of the proposed relief was key to building depth in the market and reducing transaction costs. It was remarked that this relief would provide medium term cost benefits for issuers that could justify the establishment of retail debt programs.

- (g) The responses were generally in favour of granting relief in relation to offers of convertible notes to wholesale investors. One reason for this is that there are a range of people who are potentially liable for a prospectus, not just the issuer: s729. This can make due diligence more involved than would be the case for an information memorandum prepared for institutional investors. Some submissions disagreed with the proposed condition to require prospectus-like disclosure in a cleansing statement. Other responses considered the cleansing notice should only contain details of the underlying securities and not the convertible notes themselves. We propose to retain the requirement that relief is conditional on the cleansing notice containing prospectus level disclosure in relation to the convertible notes and underlying securities. We consider that this information will be relevant to security holders.

## Conclusion and recommended options

59. ASIC considers that Option 2 (*provide disclosure relief for offers of corporate bonds (subject to conditions relating to the bonds that may be issued, the issuer and disclosure) and provide on-sale relief for wholesale offers of convertible notes*) is the preferable option. Option 2 provides a holistic package that is designed to benefit issuers of corporate bonds and convertible notes and increase the ability of retail investors to invest in corporate bonds. We consider that implementing Option 2 has the potential to accelerate the development of a retail corporate bond market. In order to promote investor protection, there are conditions attached to our relief that relate to the issuer, the nature of the bonds and upfront and ongoing disclosure. We consider that our proposals will reduce the cost and time involved in issues of corporate bonds and convertible notes and contain sufficient protections so that retail investors will be able to make informed investment decisions. We think these factors outweigh any risk to retail investors by reducing the level of disclosures that currently needs

to be included in a prospectus for corporate bonds. This conclusion is supported by submissions to CP 126, the recommendations of the AFCF report and our consumer testing of an example vanilla bonds prospectus.

60. We do not recommend Option 1 (*do nothing*). Option 1 does not provide any solutions to the regulatory impediments facing issuers of corporate bonds and convertible notes and does not have the potential to increase the ability of retail investors to invest directly in corporate bonds.

## Implementation and review

### *Implementing proposals*

61. ASIC would implement its proposals by providing class order relief. The relief would be available from the date the class orders are registered under the *Legislative Instruments Act 2003*.
62. Once relief was operative, issuers could choose to rely on the relief or could continue to offer corporate bonds and convertible notes under the existing disclosure regime.

### *ASIC guidance*

63. Our proposed policy will be implemented by publishing the following documents:
- (a) a regulatory guide describing our relief and the policy behind it; and
  - (b) class orders implementing our relief.
64. ASIC has already published an investor guide for investors in corporate bonds: *Investing in corporate bonds?*