



ASIC

Australian Securities & Investments Commission

REPORT 173

Debentures: Second review of disclosure to investors

October 2009

About this report

This report outlines the findings of ASIC's second review of the unlisted, unrated debenture industry. It includes an analysis of the disclosures made by debenture issuers against the benchmarks set out in Regulatory Guide 69 *Debentures: Improving disclosure for retail investors* (RG 69).

This report covers disclosure against the benchmarks between March 2008 and September 2009 (the review period).

About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents.

Consultation papers: seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance.

Regulatory guides: give guidance to regulated entities by:

- explaining when and how ASIC will exercise specific powers under legislation (primarily the Corporations Act)
- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
- giving practical guidance (e.g. describing the steps of a process such as applying for a licence or giving practical examples of how regulated entities may decide to meet their obligations).

Information sheets: provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

Reports: describe ASIC compliance or relief activity or the results of a research project.

Disclaimer

This report does not constitute legal advice. We encourage you to seek your own professional advice to find out how the Corporations Act and other applicable laws apply to you, as it is your responsibility to determine your obligations.

This report does not contain ASIC policy. Please see Regulatory Guide 69 *Debentures: Improving disclosure for retail investors* (RG 69) and Regulatory Guide 156 *Debenture advertising* (RG 156).

Contents

Key findings	4
Executive summary	4
Industry overview	4
Disclosure benchmarks	5
Auditing and supervising debenture issuers	5
Investor education	6
Debenture advertising	6
A Second review of disclosure to investors	7
Scope of this report	7
ASIC's 3-point plan	7
Financial Services and Credit Reform Green Paper	9
B Industry overview	10
Debenture issuers	10
Debenture trustees	14
C Benchmark disclosure	15
ASIC's disclosure benchmarks	15
Second review of benchmark disclosures	16
Benchmark disclosures: liquidity	18
Benchmark disclosure of issuers in administration	18
D Auditing and supervising issuers	20
Auditor's benchmark report	20
Debenture trustees	21
E Investor education	23
ASIC's investor guide	23
Distribution of investor guide by issuers	23
Issuers' feedback	24
Investors' feedback	25
F Advertising	27
ASIC's advertising standards	27
Compliance with ASIC's advertising standards	28
Appendix 1: Debenture issuers in administration	30
Key terms	32
Related information	33

Key findings

Executive summary

- 1 This report sets out the findings of our second review of unlisted, unrated debenture issuers. It follows up on the progress of our '3-point plan' to improve disclosure for retail investors. It looks at the regulation of these debenture issuers generally, including disclosure benchmarks, audit and supervision issues, investor education, debenture advertising and ongoing disclosure.
- 2 Two years have passed since we first sought feedback on the introduction of our 'if not, why not' disclosure benchmarks for debenture issuers in Regulatory Guide 69 *Debentures: Improving disclosure for retail investors* (RG 69). Since then, we have noticed an improvement in the information issuers are providing to investors, especially information to help investors better understand investment risks. Looking forward, we also think there needs to be a greater focus on the ongoing disclosure of benchmark information to investors.
- 3 While the disclosure benchmarks have improved disclosure, there are also lessons to be *learnt* from the global financial crisis (GFC) and the failure of several debenture issuers over the last 18 months. We therefore propose to strengthen the disclosure benchmarks in RG 69 and have released Consultation Paper 123 *Debentures: Strengthening the disclosure benchmarks* (CP 123) outlining our proposals.

Industry overview

- 4 We estimate that the total amount of money invested in debentures in Australia reduced by 51% to \$16.9 billion between June 2006 and December 2008. This reduction is primarily due to investors withdrawing their money from debenture products.
- 5 The number of unlisted, unrated debenture issuers reduced by 21% to 63 issuers between March 2008 and September 2009 (the review period), and the amount of money invested in the sector reduced by 31% to \$4649 million over the same time.
- 6 Over the review period, 15 issuers were placed into external administration, with total debentures on issue of \$912 million. However, the amount lost by investors will be smaller—most are expected to recover some of their funds. The recovery of funds will vary between each issuer in external

administration, though most investors will receive part of their investment back as the administrations progress.

- 7 There are currently 10 entities that act as debenture trustees for unlisted, unrated debenture issuers. The 4 largest trustees together cover 89% of issuers (57 issuers) and 98% of debentures on issue (\$4554 million of debentures). For more industry overview information, see Section B.

Disclosure benchmarks

- 8 Our review of issuers' benchmark disclosures as at September 2009 shows that a higher proportion of issuers comply with benchmarks 1, 7 and 8 (i.e. equity capital, valuations and lending principles) than a year ago. The level of compliance with the other benchmarks remains largely unchanged.
- 9 We also found there had been a lower level of compliance with benchmarks 1, 2, 7 and 8 (i.e. equity capital, liquidity, valuations and lending principles) among the 15 issuers that were placed into external administration during the review period compared with ongoing issuers. For this reason, we are considering further guidance about compliance with these benchmarks. For more information on disclosure benchmarks, see Section C.

Table 1: Summary: percentage of issuers meeting benchmark disclosure for 2008 and 2009

Benchmark	September 2009	March 2008
1 Equity capital	60%	52%
2 Liquidity	98%	95%
3 Rollovers	100%	99%
4 Credit ratings	3%	2%
5 Loan portfolio	98%	95%
6 Related party transactions	100%	98%
7 Valuations	28%	16%
8 Lending principles	69%	61%

Auditing and supervising debenture issuers

- 10 We released an interim pro forma (Pro Forma 223 *Interim auditor's benchmark report* (PF 223)) for the audit of issuers' benchmark disclosure.

So far, we received 46 audit reports and have sought feedback from issuers and auditors on the pro forma.

- 11 We observed that some debenture trustees took a more active role in monitoring the financial position of issuers over the review period. This includes tailoring checklists to assist debenture issuers meet their ongoing reporting obligations under RG 69 and, where appropriate, exercising their rights under trust deeds to appoint receivers to debenture issuers. For more information on auditing and supervising debenture issuers, see Section D.

Investor education

- 12 We published a new guide, *Investing in debentures?*, to help those thinking of investing in debentures.
- 13 We sought to distribute the investor guide through issuers. So far, we provided 29,500 copies of the guide to 34 issuers for distribution. Our review found that 58% of issuers followed through with their plans to make the guide available on their website and 10% of issuers followed through with plans to post out the guide with their prospectus.
- 14 We received feedback from issuers and consumers on the investor guide. Issuers provided mixed comments, however, feedback from consumers has been overwhelmingly positive. For more information on investor education, see Section E.

Debenture advertising

- 15 Over the last 2 years, debenture issuers are advertising less in print media and at least half of them are using their website for debenture advertising.
- 16 Over the last 12 months, we took regulatory action over our concerns about the advertisements of 11 debenture issuers. We also reminded a number of other debenture issuers about various aspects of our advertising policy. For more information on debenture advertising, see Section F.

A Second review of disclosure to investors

Key points

This report sets out the findings of our second review of unlisted, unrated debenture issuers. It follows up on the progress of our '3-point plan' to improve disclosure for retail investors: see paragraphs 17–20.

Our recent work on unlisted, unrated debentures includes publishing an investor guide, updating RG 69 as well as monitoring debenture issuers and their disclosure: see paragraphs 21–26.

In August 2008, the Government released their *Financial Services and Credit Reform Green Paper*, which proposed changes to the regulation of debentures: see paragraphs 27–28.

Scope of this report

- 17 This report sets out the findings of our second review of the disclosures given by unlisted, unrated debenture issuers. It also updates information on the debenture industry since our first report and covers the progress of other aspects of our '3-point plan' such as investor education and debenture advertising.
- 18 Our first review of disclosure of debenture issuers was released in April 2008: see Report 127 *Debentures: Improving disclosure for retail investors* (REP 127).

ASIC's 3-point plan

- 19 This report follows up on the progress of our '3-point plan' we outlined in August 2007. This plan involves improving disclosure for retail investors to help them understand and assess unlisted unrated debentures, while maintaining the flexibility of the public fundraising process: see Consultation Paper 89 *Unlisted unrated debentures: Improving disclosure for retail investors* (CP 89).
- 20 The '3-point plan' addresses:
- (a) existing debenture issuers in the retail sector;
 - (b) new debenture issues to retail investors; and
 - (c) investor education.

Regulatory Guide 69

- 21 RG 69 sets out 8 benchmarks we expect issuers to disclose against to help retail investors assess the risks and make informed decisions about whether or not to invest: see Section C for more information.
- 22 In August 2008, we released an updated version of RG 69 to clarify the benchmarks and make them simpler for issuers to implement. The refinements took into account our experience working with issuers, trustees and auditors. This included clarifying:
- (a) disclosure benchmarks for: equity capital, liquidity, loan portfolio, valuations, and lending principles;
 - (b) disclosure obligations for issuers who on-lend funds indirectly through a related party;
 - (c) that the guide does not apply to debentures that are to be quoted on a financial market, or to debentures that can be converted into listed securities at the discretion of the investor; and
 - (d) requirements for the auditors' report on the benchmarks. The changes concerning the role of auditors included us releasing an interim pro forma report in relation to the benchmarks: see Section D for more information.

Regulatory Guide 156

- 23 Regulatory Guide 156 *Debenture advertising* (RG 156) sets out our expectations for debenture issuers advertising debentures to retail investors. RG 156 aims to promote investor understanding and minimise the risk of mis-selling by setting standards for debenture advertising: see Section F for more information.

New guide to help investors

- 24 In April 2008, we published a new guide, *Investing in debentures?*, to help those thinking of investing in unlisted debentures. The guide is designed to assist people to use the 8 benchmarks to assess the risks of and to make an informed decision about whether or not to invest: see Section E for more information.

Monitoring issuers and their disclosure

- 25 Upon releasing REP 127 in April 2008, we said we would continue to monitor issuers' disclosure and foreshadowed that we would conduct another series of visits to and reviews with issuers in late 2008.
- 26 Our work over the review period includes:

- (a) analysing information in quarterly reports, new prospectuses and benchmark audit reports of all unlisted, unrated debenture issuers;
- (b) meeting or speaking on the telephone with a large majority of issuers and several trustees on numerous occasions. This included meeting with 4 trustees and 16 issuers in December 2008 to discuss their disclosures, liquidity and arrears position; and
- (c) reviewing debenture advertisements in print media and on issuers' websites.

Financial Services and Credit Reform Green Paper

- 27 In August 2008, the Government released their *Financial Services and Credit Reform Green Paper*. For debentures, the paper proposed:
 - (a) harmonising the regulation of promissory notes, regardless of their value;
 - (b) extending the licensing requirement for debenture issuers;
 - (c) requiring debenture trustee companies to be licensed; and
 - (d) reviewing trustees' duties.
- 28 In May 2009, the Government released draft legislation for the creation of a register of debenture trustees.

B Industry overview

Key points

We estimate the total amount of money invested in debentures in Australia has reduced by 51% to \$16.9 billion between June 2006 and December 2008. The reduction is primarily due to investors withdrawing their money from debenture products: see paragraphs 29–32.

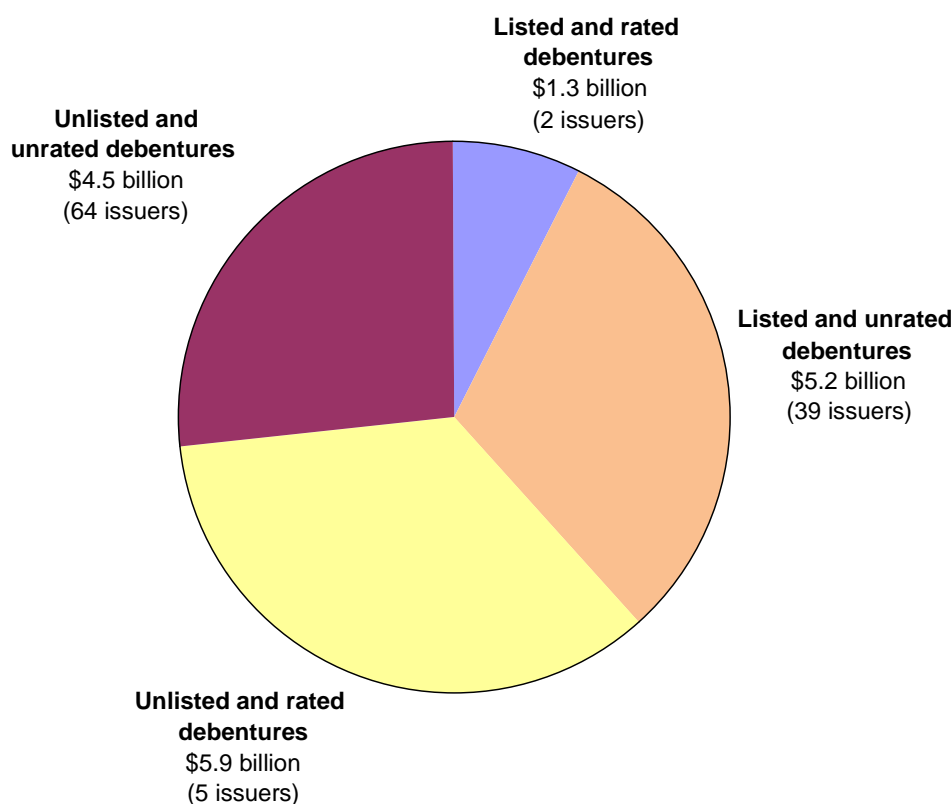
The number of unlisted, unrated debenture issuers has reduced by 21% to 63 issuers during the review period, while the amount of money invested in the sector has reduced by 31% to \$4649 million: see paragraphs 33–34.

During the review period, 15 issuers were placed into external administration with total debentures on issue of \$912 million. However, the amount lost by investors will be smaller—most are expected to recover some of their funds: see paragraphs 35–36.

There are currently 10 entities that act as debenture trustees for unlisted, unrated debenture issuers. The 4 largest trustees together cover 89% of these issuers (57 issuers) and 98% of debentures on issue (\$4554 million of debentures): see paragraphs 38–40.

Debenture issuers

- 29 We estimate that, as at 31 December 2008, the total face value of debentures on issue in Australia was \$16.9 billion and that there were 109 debenture issuers. Our estimate has been adjusted to exclude issuers in external administration (including these issuers would add \$2.8 billion to the estimate).
- 30 The market shrank by \$8 billion or 32% over the 6 months from June 2008, which was a period of tight liquidity. Between December 2006, when we first estimated the size of the market, and December 2008, the market has contracted 51%, from \$34.3 billion.

Figure 1: Face value of debentures on issue (December 2008)

- 31 The segment with the largest change over the 6 months to December 2008 was unlisted rated debentures. Over this period, the face value of their debentures fell 40% (from \$9.8 billion to \$5.9 billion). One issuer ceased issuing new debentures in October 2007 and another issuer ceased issuing in March 2009.
- 32 We estimate that over the 9 months to 30 September 2009, the size of the unlisted rated segment shrank by a further \$3.7 billion due to the maturing of existing debentures issued by these 2 issuers. This reduces the segment's size to \$2 billion, a decline of 80% from June 2008.

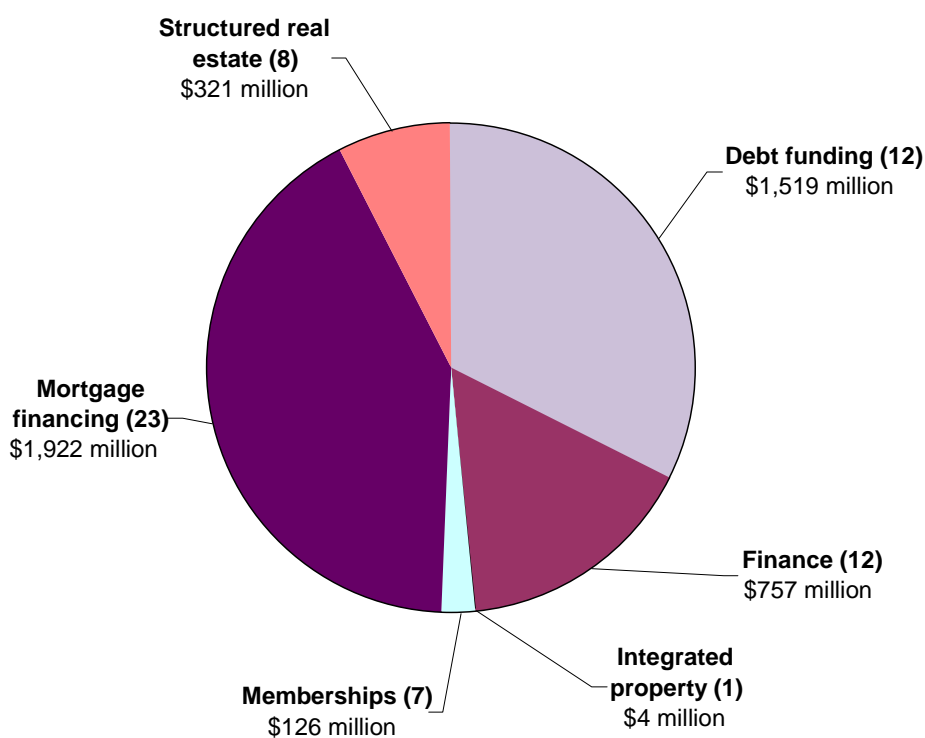
Issuers of unlisted, unrated debentures

- 33 As of September 2009, there were 63 issuers of unlisted, unrated debentures. Over the preceding 12 months, the number of debenture issuers reduced by 21% (17 fewer issuers) and the total amount of debentures on issue reduced by 31% (\$2064 million). Table 2 shows the number of issuers and amount of debentures on issue in each category over the period since August 2007.
- 34 Twenty-five unlisted, unrated debenture issuers (39%) currently hold an Australian financial services (AFS) licence. Of these:
- (a) 22 issuers are authorised to deal and/or provide financial product advice in debentures;

- (b) 2 issuers have licence authorisations to operate a managed investment scheme (both are authorised for mortgage schemes); and
- (c) 1 issuer has a licence authorisation to deal and provide financial product advice in relation to general and life insurance products.

Table 2: Number of issuers and amounts on issue of unlisted, unrated debentures

Category	September 2009		March 2008		August 2007	
	No. of issuers	\$ (millions)	No. of issuers	\$ (millions)	No. of issuers	\$ (millions)
Debt capital funding	12	\$1,519	17	\$2,656	21	\$2,682
Finance	12	\$757	16	\$911	15	\$885
Integrated property	1	\$4	2	\$29	3	\$73
Memberships	7	\$126	7	\$108	7	\$82
Mortgage financing	23	\$1,922	31	\$2,679	36	\$3,206
Structured real estate investments	8	\$321	9	\$330	10	\$680
Total	63	\$4,649	80	\$6,713	92	\$7,609

Figure 2: Unlisted, unrated debentures by sector (September 2009)

- 35 Over the review period, the number of unlisted, unrated debenture issuers had reduced by 17 issuers. The change in the number of issuers during this period was made up of:
- (a) 3 new issuers entering the unlisted, unrated debenture market;
 - (b) 5 issuers exiting the market because they repaid or converted their debentures or merged with another issuer; and
 - (c) 15 issuers being placed into external administration.
- 36 Table 3 gives a breakdown of the 15 issuers entering external administration since March 2008. Of the 15 issuers:
- (a) almost half (7 issuers) held AFS licences authorising them to deal and/or provide financial product advice in relation to debentures; and
 - (b) a majority (8 issuers) were involved in mortgage financing. This sector also had the highest proportion of issuers with an AFS licence.
- 37 The 15 issuers in external administration are at various stages of the external administration process. While the total amount of debentures they had on issue was \$912 million, a percentage of this amount will be repaid to investors. The amount of money repaid to investors will vary between issuers: see Appendix 1 for a list of debenture issuers that have entered external administration during the review period, together with details of estimated distributions to investors.

Table 3: Issuers entering external administration since March 2008

Category	No. of issuers	Amount on issue (\$ millions)	No. of AFS licensees
Debt capital funding	4	\$253	1
Finance	2	\$208	0
Integrated property	0	0	0
Memberships	0	0	0
Mortgage financing	8	\$441	6
Structured real estate investments	1	10	0
Total	15	\$912	7

Debenture trustees

- 38 At the end of the review period, there were 10 entities acting as debenture trustees for the 63 unlisted, unrated debenture issuers. The 4 largest trustees together cover 89% of these issuers (57 issuers) and 98% of the unlisted, unrated debentures on issue (\$4554 million of debentures).
- 39 Of the 10 trustees:
- (a) 5 trustees acted for only 1 issuer, and 1 trustee acted for 2 issuers;
 - (b) 4 trustees acted for between 7 and 25 issuers; and
 - (c) 1 trustee did not hold an AFS licence.
- 40 There were 5 trustee appointments during the review period due to:
- (a) 2 debenture issuers replacing their trustees through entering into a new trust deed; and
 - (b) 3 new debenture issuers entering the unlisted, unrated debenture market: see paragraph 35(a).

C Benchmark disclosure

Key points

Our review of issuers' benchmark disclosures as at September 2009 shows that a higher proportion of issuers comply with benchmarks 1, 7 and 8 (i.e. equity capital, valuations and lending principles) than 18 months ago. The level of compliance with the other benchmarks remains largely unchanged.

We also found there was a lower level of compliance with benchmarks 1, 2, 7 and 8 (i.e. equity capital, liquidity, valuations and lending principles) among the 15 issuers that were placed into external administration during the review period compared with the ongoing issuers. These benchmarks are of particular importance for issuers involved in mortgage financing.

ASIC's disclosure benchmarks

- 41 Each issuer of unlisted, unrated debentures is expected to disclose against the 8 benchmarks set out in RG 69:
- (a) in any disclosure documents (e.g. prospectus); and
 - (b) at least twice a year in the issuer's quarterly reports to the trustee.
- 42 This disclosure should set out the issuer's performance against the benchmarks by either:
- (d) stating that they met the benchmark; or
 - (e) explaining:
 - (i) that they did not meet the benchmark; and
 - (ii) how and why the issuer deals with the business factors or issues underlying the benchmark in another way ('if not, why not' disclosure).
- Note: For guidance on the benchmark disclosure regime, see Section A of RG 69.
- 43 Benchmarks 1, 2 and 4 are relevant to all issuers. However, benchmarks 1 and 2 can have particular importance to issuers involved in mortgage lending and other on-lending activities (e.g. finance companies) because of the risk of default by borrowers and the need to 'match' cash flows to and from investors with those to and from borrowers.
- 44 Not all of the other benchmarks apply to some issuers because of their particular business model—for example, benchmarks 5 and 6 only apply to issuers that on-lend money, and benchmarks 7 and 8 only apply to issuers who use or lend money for property-related activities such as mortgage financing.

Table 4: Disclosure benchmarks for debenture issuers

General benchmarks for all issuers of unlisted debentures	1 Equity capital	Benchmarks 1 and 2 address the issuer's financial structure and ability to meet loan obligations on time.
	2 Liquidity	
	3 Rollovers	Benchmark 3 addresses the transparency of the issuer's approach to 'rollovers' and early redemptions of investments.
	4 Credit ratings	Benchmark 4 relates to ratings provided by experts in assessing credit risk.
Additional benchmarks for lenders	5 Loan portfolio	Benchmark 5 addresses the issuer's lending practices.
	6 Related party transactions	Benchmark 6 addresses a specific area of lending risk.
Additional benchmarks for property-related debentures	7 Valuations	Benchmarks 7 and 8 address the issuer's property-related practices.
	8 Lending principles—loan-to-value ratios	

Second review of benchmark disclosures

- 45 We analysed the most recent benchmark disclosure by each unlisted, unrated debenture issuer. Depending on the issuer, this was generally either their latest quarterly report in which the issuer updated their benchmark disclosure or their current prospectus.
- 46 We also:
- (a) reviewed audit reports of benchmark disclosure, where available;
 - (b) obtained documents from 30 issuers to assist in verifying their compliance with certain benchmarks; and
 - (f) met with 16 issuers to discuss their benchmark compliance, and compliance issues generally.
- 47 Figure 3 and Figure 4 show the overall results of our analysis as at September 2009.
- 48 We identified a limited number of instances where an issuer had met a particular benchmark at both March 2008 and September 2009 but did not meet the benchmark for a period in between. This highlights the importance of issuers providing ongoing disclosure to the market of any material changes to their benchmark disclosures.

Ongoing disclosures

- 49 Where there are any material changes to an issuer’s performance against the benchmarks, including against the issuer’s alternative approach to meeting the benchmarks, the issuer should explain this in a supplementary prospectus, replacement prospectus or continuous disclosure notice.
- 50 In addition, an issuer’s quarterly reports should, at least twice a year, specifically explain any material changes to the issuer’s performance against the benchmarks. This includes any changes against the issuer’s alternative approach to meeting the benchmarks.
- Note: For guidance about the ongoing disclosure obligations of issuers, see RG 69.95–RG 69.104 and Regulatory Guide 198 *Unlisted disclosing entities: Continuous disclosure obligations* (RG 198). Issuers should make ongoing disclosure documents (including those lodged with ASIC) available to all debenture holders (e.g. by issuers posting disclosure documents on their website).
- 51 In the 5 months to September 2009, 46 issuers (73% of issuers) provided ongoing disclosure about their performance against the benchmarks. This was done through either disclosure in their quarterly report to the trustee and ASIC, prospectus disclosure or continuous disclosure notices.
- 52 In many cases, certain trustees assisted issuers with the ongoing reporting process by developing template documents.

Figure 3: Summary of benchmark disclosures (September 2009)

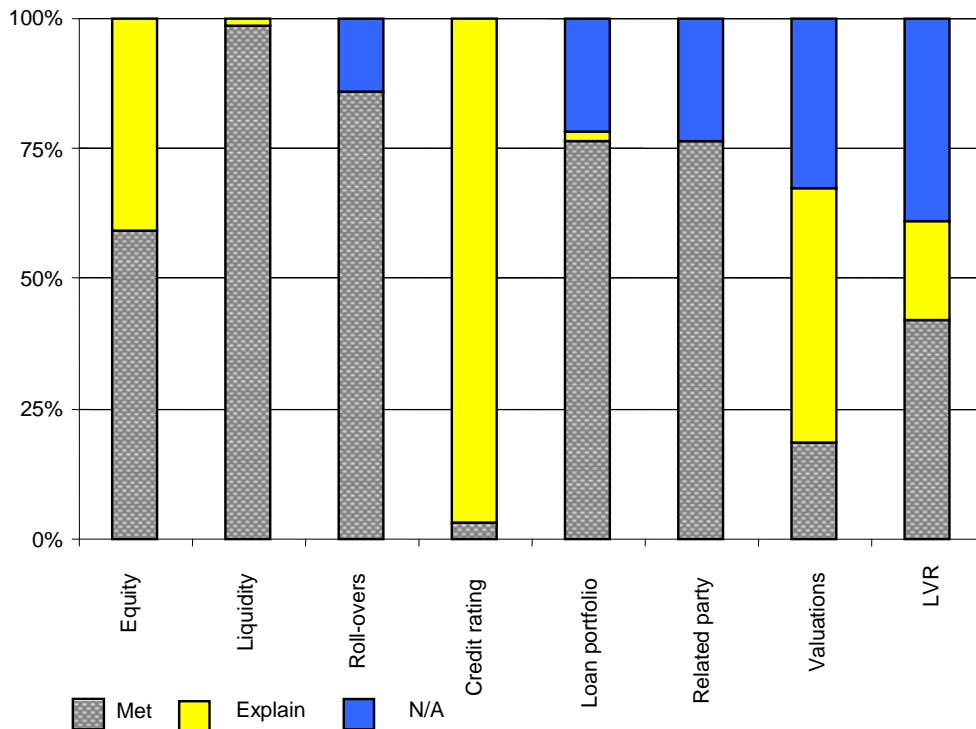
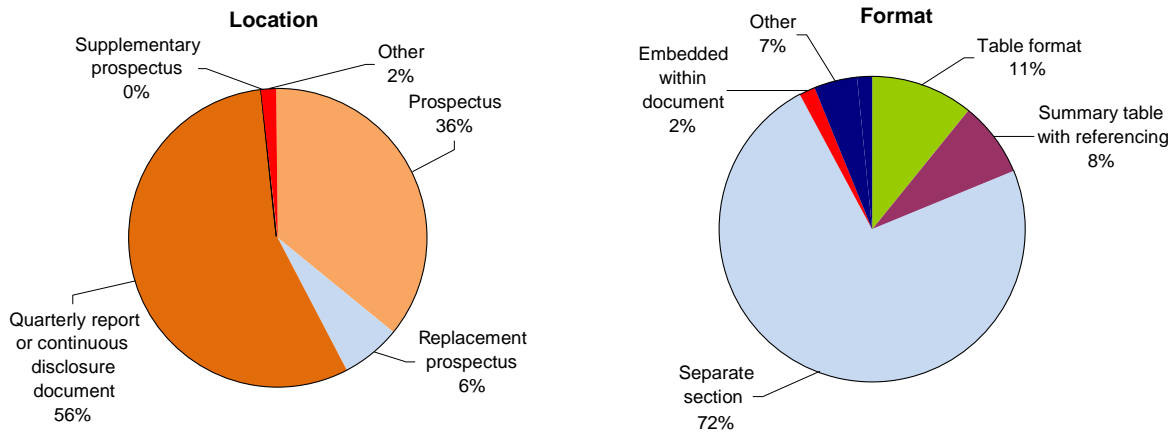


Figure 4: Location and format of benchmark disclosure



Benchmark disclosures: liquidity

- 53 We undertook a more detailed review of the impact of the GFC on the liquidity of debenture issuers during November 2008 to January 2009. In total, we met with 16 issuers, obtained financial records from another 30 issuers and met with 4 debenture trustees. This collectively covered more than 90% of the unlisted, unrated debentures on issue.
- 54 The overall trend was that, all issuers appeared confident that they had sufficient liquidity despite reduced cash flows in many cases. Several issuers had increased their cash reserves as a precautionary measure.
- 55 Of the 16 issuers we met, 11 reported a decrease in rollovers of invested funds in October and November 2008. All appeared confident that liquidity was not an immediate concern.
- 56 Similarly, for those from whom we obtained financial records, 25 of the 30 had enough cash or cash equivalents to cover 3 months of operations while 3 had relied on the assumption of new debenture funds in their cash flow forecasts.
- 57 Of these 30 issuers, new debenture funds decreased for 13 during October and November 2008, with 12 experiencing an increase in redemptions or a decrease in rollovers. Seventeen of the 30 issuers discussed liquidity concerns during board meetings and 15 also discussed strategies to deal with these concerns.

Benchmark disclosure of issuers in administration

- 58 During the review period, 15 issuers were placed into external administration: see paragraphs 36–37 and Table 3.

59 We analysed how these 15 issuers reported against the benchmarks before their
external administration to identify if there were particular trends in their
benchmark compliance.

60 5 compares the benchmark compliance of issuers that subsequently went into
external administration, with issuers that remain in business.

61 Overall, there was a lower level of compliance with benchmarks 1, 2, 7 and 8
among the issuers in external administration than for ongoing issuers. The key
areas impacting these issuers were:

- (a) insufficient equity levels—only 5 issuers met the equity benchmark, and the level of equity for those issuers who did not was significantly lower than the benchmark;
- (b) issues with liquidity;
- (c) related party transactions—several issuers had significant related party loans and, while these were generally disclosed, the existence of the related party loans presented significant risks and directly contributed to the failure of at least two issuers; and
- (d) poor valuation practices—many of the issuers had poor valuation practices which impacted on the management and recoverability of the loan portfolio and the loan-to-valuation ratios.

This highlights the importance of maintaining adequate equity and liquidity levels and having robust procedures to deal with related party transactions and valuation.

Table 5: Comparison of benchmark compliance of issuers in external administration and ongoing issuers

Benchmark	Ongoing (% met benchmark)	External admin. (% met benchmark)
1 Equity capital	60%	36%
2 Liquidity	98%	79%
3 Rollovers	100%	92%
4 Credit ratings	2%	0%
5 Loan portfolio	98%	100%
6 Related party transactions	100%	100%
7 Valuations	28%	9%
8 Lending principles	69%	45%

Note: For benchmarks 3, 5, 6, 7 and 8, the percentages in this table only take into account the issuers for which the benchmark was relevant. This excludes 1 issuer in external administration who did not provide any benchmark disclosure.

D Auditing and supervising issuers

Key points

We released an interim pro forma for the audit of issuers' benchmark disclosure. So far, we received 41 audit reports and sought feedback from issuers and auditors on the pro forma.

We also observed that some debenture trustees are taking a more active role in monitoring the financial position of issuers during the past year. This includes, where appropriate, exercising their rights under trust deeds to appoint receivers to debenture issuers.

Auditor's benchmark report

- 62 Each unlisted, unrated debenture issuer is expected to enlist their auditor to prepare an auditor's report relating to benchmark information when auditing the issuer's financial report.

Note: For further guidance, see RG 69.126–RG 69.129.

- 63 In August 2008, we released pro-forma 223 and revised RG 69 to clarify our expectations for reporting by auditors on benchmark information. PF 223 was issued in an interim form, with the original aim of reviewing the initial experience in using this interim pro forma and releasing an updated version of the pro forma.

Lodgement of benchmark audit reports

- 64 We received 30 audit reports for the 30 June 2008 period (approximately 50% of issuers), 1 for 30 September 2008, 10 for 31 December 2008 and 5 for 30 June 2009.
- 65 We received 1 qualified audit report indicating that an issuer incorrectly disclosed that it met one of the benchmarks, when in fact it had not.

Feedback on our pro forma

- 66 We discussed PF 223 with a number of issuers, auditors and the Auditing and Assurance Standards Board. We received a range of comments regarding why some issuers did not obtain benchmark audit reports and other feedback on PF 223. These included:
- (a) suggestions for minor refinements to PF 223 to clarify the references to previous fundraising and other documents containing benchmark

statements, and covering cases where a modified benchmark should be available;

- (b) queries about the nature of the opinion and structure of the report; and
- (c) comments on whether there should be a requirement for including a directors' benchmark statement with the financial reports.

67 We are considering further changes to PF 223, including whether there is a need for law reform to fully achieve its objectives. In the meantime, we expect issuers will continue to enlist their auditor to prepare an auditor's report for benchmark information using the interim pro forma. We consider the audit report to be an important element for assisting us and debenture trustees to understand an issuer's disclosure.

Debenture trustees

68 Trustees have a duty under the trust deed and the *Corporations Act 2001* (Corporations Act) to exercise reasonable diligence in monitoring the issuer's ability to repay debentures (e.g. its financial position and performance). This includes actively monitoring debenture issuers. Recent market events also demonstrate the importance of ongoing and regular monitoring of the financial position and performance of debenture issuers.

Appointment of receivers and other remedial action

69 Fifteen issuers entered external administration over the review period. In each of these cases, the trustee exercised their rights under the trust deed to appoint a receiver and manager to the issuer. Each appointment of a receiver followed a breach of covenants under the trust deed. Generally, this involved the trustee obtaining relevant financial records from the issuer and sometimes taking advice from investigating accountants, insolvency practitioners and legal advisers.

70 During the review period, there was also one instance where the trustee commenced court action seeking orders against the issuer, and another instance where the trustee called a meeting of debenture holders to vote on a proposal to vary scheduled repayments.

Monitoring of issuers

71 Over the review period, we observed that some trustees took a more active role in monitoring issuers. This includes requiring issuers to provide monthly key management reports, monitoring the impact of prevailing economic conditions on issuers, developing quarterly reporting templates to receive key information relating to benchmarks; and conducting on-site reviews on issuers' businesses.

72 We encountered one recent example where an issuer did not provide access to certain financial records requested by the trustee. Under the Corporations Act, issuers are required to make all of their financial and other records available for inspection by the trustee and give the trustee any information, explanations or other assistance that they require about matters relating to those records: see s283BB(3). These provisions are designed to ensure that the trustee is able to obtain all information it believes relevant to its role.

E Investor education

Key points

We published an investor guide to help people who are thinking of investing in debentures.

We distributed the guide through issuers. So far, we have provided 29,500 copies of the guide to 34 issuers for distribution. This review found that 58% of issuers followed through with their plans to make the guide available on their website and 10% of issuers followed through with plans to post out the guide with their prospectus.

We received feedback from issuers and consumers on the investor guide. Issuers provided mixed comments, however, feedback from consumers was overwhelmingly positive.

ASIC's investor guide

- 73 In April 2008, we published a new investor guide, *Investing in debentures?*, to help those thinking of investing in unlisted debentures. The guide is designed to assist people use the 8 benchmarks, assess the risks and make an informed decision about whether or not to invest.
- 74 The investor guide was developed as part of ASIC's '3-point plan' and is supported by the results of investor research commissioned by us to better understand the profile and motivations of unlisted, unrated debenture investors. As part of our research, those consulted generally supported the guide and said it should be used when making an investment decision. The guide was also developed in consultation with a wide range of external stakeholders.
- 75 The investor guide is available to retail investors free of charge from FIDO, ASIC's dedicated website for consumers and investors (www.fido.gov.au), as well as through ASIC's Infoline on 1300 300 630.

Distribution of investor guide by issuers

- 76 We worked with issuers to distribute the guide directly to those thinking of investing in debentures.
- 77 In June 2008, we wrote to 78 debenture issuers seeking their assistance in distributing the guide to actual and potential investors. Of the 36 issuers that responded, 34 asked for copies of the guide and 2 advised that they did not require any copies (one was in the process of paying investors out in full, and the other no longer had a current prospectus).

- 78 So far, we have provided 29,500 copies of the guide to issuers. The highest number of requests for the guide was received from Victoria (56%), followed by New South Wales and Queensland (both 17.5%).

Distribution methods

- 79 Issuers who requested copies of the guide were asked to tell us how they planned to distribute it. As shown in Table 6, the majority of respondents (85%) proposed using multiple strategies to distribute the guide.

Table 6: Issuers' planned distribution strategy

Distribution strategy	No. of responses	Percentage
Distribute with prospectus	20	59%
Make generally available to investors (e.g. on front counter)	21	62%
Link and/or make available via website	19	56%
No plans for electronic distribution	6	18%
Other (e.g. send out letters, promote via newsletter)	3	9%

Distribution via issuers' websites

- 80 We reviewed the issuers' websites in February 2009 and found that 58% of the issuers (11 issuers) who said they planned to make the investor guide available through their website had done so.

Distribution with prospectus

- 81 We undertook a 'shadow calling' exercise in March 2009 to find out whether or not issuers who said they planned to post out the investor guide with their prospectus were doing so. This process involved an ASIC staff member making an anonymous request for a prospectus from issuers who had requested copies of the guide.
- 82 We received a total of 18 prospectuses through the shadow calling exercise. Of the 18 issuers, 10 had previously informed us that they planned to post out the guide to new investors with their prospectuses. However only 2 issuers (10%) actually followed through on their intention to provide the guide with the prospectus.

Issuers' feedback

- 83 Issuers provided us with a range of feedback about the investor guide. Some issuers were more positive than others. For example, we received comments that:

- (a) 'We think the investor guide is a brilliant initiative which we would be only too willing to forward onto our existing and future debenture holders.'
- (b) 'We agree with ASIC that investor education is an important aspect of prudent investment decision making. We are happy to include the new guide in the material available to our investors.'
- (c) 'We applaud ASIC's efforts to better educate and inform retail investors about the products they may choose to invest in. We agree that both industry participants and the investors themselves benefit from making informed choices and decisions about their investments.'

84 Other issuers were less positive. For example:

- (a) One issuer did not see the guide as useful and another thought it was 'a waste of taxpayers' money'.
- (b) One issuer expressed concern about the warning on the back of the guide and 2 others said it was unfortunate that ASIC had decided to put the orange traffic light on the front of the guide.
- (c) One issuer was concerned that the investor guide potentially contained financial product advice.
- (d) One issuer was not distributing the guide because it thought the guide to be very 'negative' and did not wish to provide too many warnings to investors. This issuer believed that it would create a fearful environment and saw it as ASIC's role to educate investors, therefore it shouldn't be up to issuers to distribute the guide.

85 Where appropriate, we amended the investor guide to address any concerns raised with us. A revised version of the guide was released in December 2008.

86 Even though some issuers had reservations about the investor guide, 14 out the 16 issuers we met with in December 2008 are distributing the guide. In one case, an issuer placed copies of the investor guide at their front desk even though they thought parts of it 'appeared a little harsh'. On balance, the issuer said they did not have any objections to the guide.

Investors' feedback

87 As with all our consumer publications, freepost feedback forms were included with all guides distributed, inviting investors to give us their assessment of how useful they found the booklets. To date, 20 feedback forms have been returned by investors.

88 Investors' feedback has been overwhelmingly positive. This suggests that the guide is being well received by investors, with 100% of respondents reporting that:

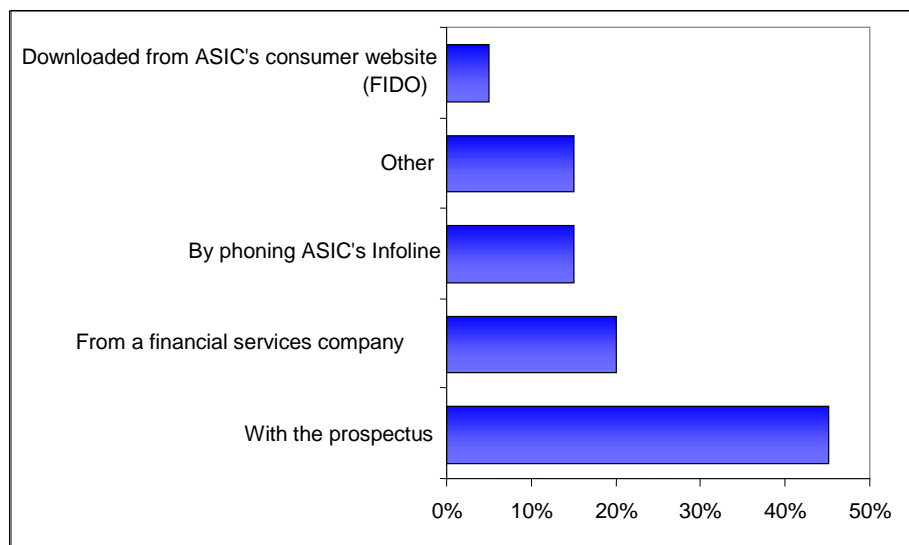
- (a) the guide was helpful in making their investment decision and in understanding unlisted debentures;

- (b) the overall look of the guide was appealing and it was easy to use; and
- (c) they would recommend the guide to others.

Given investors’ perceived importance of the guide, we will consider whether some of the key messages in the guide should be provided through other means, for example, through prospectus disclosure.

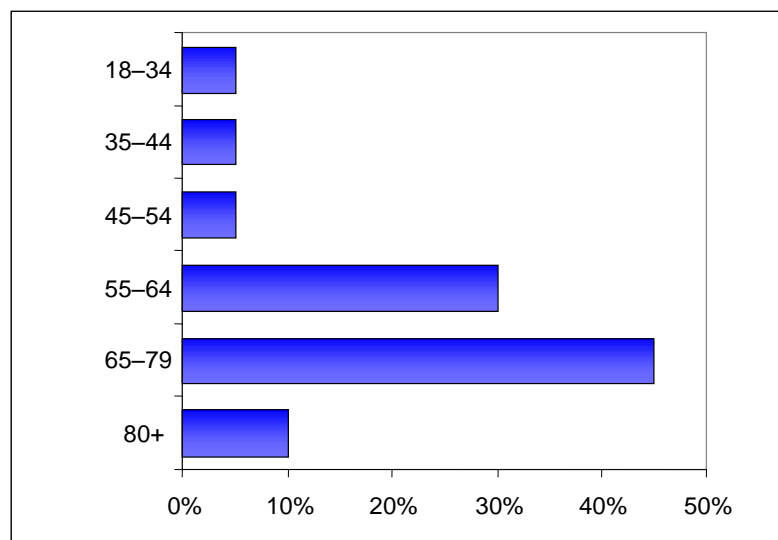
89 Figure 5 shows that most investors obtained the guide enclosed with a prospectus (45%) or from a financial services company (20%), with a smaller proportion going through ASIC’s Infoline (15%) or downloading it from ASIC’s FIDO website (5%).

Figure 5: How investors obtained the guide



90 Figure 6 shows that the guide is reaching the target audience of pre-retirees and retirees, with 45% of the sample aged 65–79 years and 30% aged 55–64 years.

Figure 6: Investors’ age profile



F Advertising

Key points

Over the last 2 years, debenture issuers are advertising less in print media and at least half of them are using their website for debenture advertising: see paragraphs 91–95.

Over the last 12 months, we took regulatory action over concerns about advertisements of 11 debenture issuers: see paragraphs 96–98.

ASIC's advertising standards

91 RG 156 provides guidance on the standards we consider issuers need to meet when advertising debentures. Table 7 summarises these standards.

Table 7: Advertising standards for issuers offering debentures to retail investors

Area	Summary of standard
Repayment of principal investment	Advertisements should include a prominent statement to the effect that investors risk losing some or all of their principal investment.
Interest rates, credit ratings and investment ratings	Advertisements should only quote interest rates if the interest rate is accompanied by prominent disclosure of either: <ul style="list-style-type: none"> • a current credit rating of the debenture from a recognised credit rating agency (and what it means or where to find this out); or • a statement that the debenture does not have a credit rating and what this means. Advertisements should not refer to investment ratings of the debenture or the issuer, or credit ratings issued by an entity other than a recognised credit rating agency.
Comparisons with bank deposits and 'risk free' suggestions	Advertisements should state that the debenture is not a bank deposit. They should also not suggest that: <ul style="list-style-type: none"> • the debenture is, or compares favourably to, a bank deposit; or • there is no or little risk of the investor losing their principal or not being repaid.
Suitability statements	Advertisements should not state or imply that the investment is suitable for a particular class of investor.
Consistency with prospectus disclosure	Statements in advertisements should be consistent with the corresponding disclosures on that subject matter in the prospectus.
Telephone inquiries	Statements made in response to inquiries are subject to the same regulation regarding misleading and deceptive conduct as the advertisements.

92 Our review found that debenture issuers advertise their debentures in a variety of ways, which mainly include:

- (a) print media;
- (b) their websites; and
- (c) financial advisers or entities affiliated with the issuer (e.g. a law firm).

Print media

- 93 There has been a decline in the number of unlisted, unrated debenture issuers advertising in print media over the last 2 years, as shown by Table 8. The reduction is partly due to some issuers since being placed into external administration—6 of the issuers advertising between March 2007 and February 2008 are now in external administration, and one issuer advertising between March 2008 and February 2009 is now in external administration.
- 94 The reduction in the number of issuers advertising is also broadly consistent with the feedback we received when we met with 16 issuers in December 2008, which was that some issuers were not currently actively advertising their debentures due to market conditions.

Table 8: Issuers advertising in print media

Period	Issuers advertising
March 2008 to February 2009	17 % of issuers (11 issuers)
March 2007 to February 2008	23% of issuers (19 issuers)

Websites

- 95 Our review of the websites of unlisted, unrated debenture issuers found that at least half of issuers use their website to advertise debentures: see Table 9.

Table 9: Issuers advertising on their websites

Date	Issuers advertising
February 2009	51% of issuers (32 issuers)
February 2008	51% of issuers (45 issuers)

Compliance with ASIC's advertising standards

- 96 We reviewed recent print media and website advertisements of issuers against our advertising standards regarding:
- (a) repayment of principal;
 - (b) interest rates, credit ratings and investment ratings; and

(c) comparisons with bank deposits and 'risk free' suggestions.

- 97 Our review of print media advertising for the period March 2007 to March 2008 indicated there were 19 issuers who advertised in print media during that period. Only 4 issuers advertised immediately after RG 156 was released in December 2007, and they all complied with our advertising standards.
- 98 We regularly monitor debenture advertising. Over the last year, we took regulatory action over concerns about the advertisements of 11 debenture issuers. Generally, we also worked with debenture issuers and industry groups to improve the advertising standards.

Appendix 1: Debenture issuers in administration

Table 10: Debenture issuers that have entered external administration since March 2008

Issuer	Category	Debentures on issue (approx \$ millions)	Date of external administration	Estimated distribution to investors
Asset Loans Limited	Mortgage financing	\$12	September 2008	External administrator estimates that, under a liquidation scenario, investors may receive between 34 and 42 cents/dollar.
Australian Secured Investments Limited	Mortgage financing	\$5	August 2008	Not available.
Bidgee Finance Limited	Finance	\$18	November 2008	External administrator estimates investors should receive a 'significant return', but this has not been quantified.
Cymbis Finance Australia Limited	Debt capital funding	\$64	August 2008	Investors have already received 20 cents/dollar. External administrator says it expects to pay another 5 cents/dollar, but further distributions remain unclear.
Diverseport Fixed Income Limited	Debt capital funding	\$107	May 2008	Investors have received a distribution of 45 cents/dollar. It is unclear whether there will be further distributions.
Elderslie Finance Corporation Limited and Elderslie Financial Services Limited	Finance	\$150	July 2008	External administrator estimates debenture holders will receive less than 10 cents/dollar and that unsecured noteholders should not expect any return.
First Capital Securities Limited	Mortgage financing	\$15	July 2008	Not available

Issuer	Category	Debentures on issue (approx \$ millions)	Date of external administration	Estimated distribution to investors
Grenfell Securities Limited	Mortgage financing	\$57	November 2008	External administrator estimates the return to investors would be between 60 and 75 cents/dollar for those who held debentures with Grenfell First Mortgage Fund and between 35 and 50 cents/dollar for those who held debentures with Grenfell General Fund.
Hastings Capital Limited	Mortgage financing	\$33	August 2008	Investors have been paid 10 cents/dollar and the external administrator estimates a total dividend of 55 to 65 cents/dollar.
LKM Capital Limited	Mortgage financing	\$63	August 2008	Investors were paid a first distribution of 7.98 cents/dollar and a further distribution is estimated by the external administrator to be 8 to 10 cents/dollar.
Mariner Treasury Limited	Debt capital funding	\$22	October 2008	External administrator estimates that there will be no return to investors.
Momentum Mortgages Limited	Mortgage financing	\$36	October 2008	External administrator estimates a distribution of 65 cents/dollar, although this may vary.
South Eastern Secured Investments Limited	Mortgage financing	\$178	February 2009	Investors have already received 30 cents/dollar. The external administrator says the estimated return to investors is unclear although the information available suggests that investors should receive a substantial return of their principal over time.
Timbercorp Limited	Structured Real Estate Investment	\$10	April 2009	Not available

Note: The information relating to the estimated distributions to investors is based on documents lodged with ASIC or is on the website of the relevant external administrator.

Key terms

Term	Meaning in this document
ASIC	Australian Securities and Investments Commission
Corporations Act	<i>Corporations Act 2001</i>
CP 89	ASIC consultation paper (in this example, numbered 89)
PF 223	ASIC pro forma (in this example, numbered 223)
REP 127	ASIC report (in this example, numbered 127)
review period	the period over which this second review of disclosure to investors took place, being March 2008 to September 2009
RG 69	an ASIC regulatory guide (in this example, numbered 69)
rollovers	when an existing investor keeps their money in the existing debenture investment for an additional term (whether on the same or slightly different terms)
s710 (for example)	a section of the Corporations Act (in this example, numbered 710)

Related information

Headnotes

Debentures, unlisted unrated debentures, benchmark disclosure, debenture trustees, investor education, investor guide, advertising

Pro formas

PF 223 *Interim auditor's benchmark report*

Regulatory guides

RG 69 *Debentures: Improving disclosure for retail investors*

RG 156 *Debenture advertising*

Legislation

Chs 2L and 6D of the *Corporations Act 2001*

Consultation papers and reports

CP 89 *Unlisted, unrated debentures: Improving disclosure for retail investors*

CP 94 *Debenture advertising*

REP 38 *High-yield debentures*

REP 108 *Report on submissions for CP 89 Unlisted, unrated debentures*

REP 113 *Report on submissions for CP 94 Debenture advertising*

REP 126 *Debentures: Understanding investors in the unlisted, unrated debenture (UUD) market*

REP 127 *Debentures: Improving disclosure for retail investors*