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By email

Dear Sir

Corporations Amendment (Simple Corporate Bonds and Other Measures) Bill 2013: Exposure Draft

We attach our submissions on the above draft bill. Please contact the undersigned if you have any questions.

Yours sincerely

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Corporations Amendment (Simple Corporate Bonds and other measures) Bill 2013: Exposure Draft ("Draft Bill")

Submissions on general approach

We support the Government's initiative to support law reform to promote the development of a deep and liquid corporate bond market in Australia. The following general comments identify changes to the Draft Bill which we believe would better serve that policy objective without detracting from the integrity of the disclosure regime.

1 **Criteria**: The Draft Bill requires simple corporate bonds to satisfy a number of criteria. We make submissions on a number of these below, but wish to highlight the requirement that simple corporate bonds rank in the winding up of the issuer in priority to unsecured creditors. The inclusion of this requirement means that the simple corporate bond regime will not only be closed to subordinated bonds (as contemplated by the draft Explanatory Memorandum) but will be limited to secured bonds. As most Australian corporations of high credit standing borrow on an unsecured, negative pledge basis they would be unable to utilise the regime as currently proposed and accordingly the Government's policy objectives would be seriously compromised. In our view unsubordinated bonds should be eligible to be classified as simple corporate bonds.

2 **Flexibility**: The Draft Bill mandates the use of specific types of disclosure documents and processes for the issue of simple corporate bonds. Giving issuers the flexibility to choose the form of document and process that best suits their circumstances would assist to minimise the regulatory hurdles prospective issuers face without in any way reducing disclosure standards. Specific areas where flexibility could be enhanced are as follows:

   (a) use of the 'simple corporate bond prospectus': issuers should be able to use standard disclosure documents (including short form prospectuses and transaction specific prospectuses where the offer would otherwise be eligible to be made under such a prospectus) if they prefer; and

   (b) use of '2-part' prospectus: whilst the ability to have a 2-part prospectus is welcome, the use of such a prospectus should not be mandatory. Many issuers will have in mind only infrequent issues and the requirement to prepare a '2-part' prospectus is an unnecessary complication when all relevant disclosures could be included in a single disclosure document.

3 **Content**: The Draft Bill leaves the content requirements that will apply to simple corporate bond prospectuses to be prescribed by regulations.

   (a) The regulations should avoid a prescriptive approach to regulating content. The policy of Australia's existing disclosure laws is to require disclosure of material information rather than attempting to prescribe what that information is. We consider this approach sound and agree with ASIC's publicly stated views that the inclusion within prospectuses of immaterial information can tend to obscure rather than enhance effective disclosure of material information. Prescribed checklists of information to be disclosed would therefore be counter to the policy of promoting "clear, concise and effective" disclosure.

   (b) The Government should instead consider an approach which maintains the emphasis on disclosure of material information, but takes account of the fact that the issuer is already subject to a

continuous disclosure regime and recognises that what is material to a bond investor is the issuer's capacity to meet its obligations to pay interest and repay principal on the bond. An approach similar to that taken in Regulation 7.9.07A in relation to warrants may be appropriate – that would allow issuers to limit disclosure to matters material to holders of simple corporate bonds whilst in effect 'taking as read' information already disclosed to the market on the basis it was material to the holders of the issuers other securities.

We ask that the Government make the regulations available for a reasonable period of consultation prior to being formally introduced.

4 **Defences**: We doubt the utility of the defences which the Draft Bill adds to offences under sections 1308 and 1309 of the Corporations Act. To make out these offences the prosecution would already have to prove that a director had failed to take reasonable steps to avoid the proscribed result. In our view the new defences provide nothing in the way of additional comfort to directors given that they require the director to affirmatively prove conduct on his or her part conduct that on almost any conceivable view would constitute the taking of such reasonable care. If anything the new defences may make sections 1308 and 1309 more onerous by raising the bar on what conduct would be regarded as taking reasonable care so as to avoid an offence arising and by creating confusion as to the onus of proof.

5 **Use of credit ratings**: The Government should take this opportunity to modify the requirement of section 716(2) in its application to the inclusion of credit ratings in a simple corporate bond prospectus. The effect of this section is that credit ratings are currently unable to be referred to in the prospectuses. We submit that this is inappropriate as:

(a) Credit ratings are highly relevant information, and in the case of corporate credit ratings readily understood by investors. They are widely relied upon by sophisticated institutional investors in their overall assessment of an issuer. It seems counter to good disclosure policy to prevent this information being included in a prospectus for the benefit of all investors.

(b) Credit ratings are already publicly available and so their exclusion from prospectuses means investors (usually less sophisticated investors) relying solely on a prospectus miss out on information that is available to more sophisticated investors.

(c) The widely reported criticisms that have been directed to credit rating agencies have arisen in the context of structured credit ratings. Unstructured corporate credit ratings, of the kind that would be relevant to simple corporate bonds, have not experienced the same issues.

Submissions on specific issues

The following comments are directed to specific aspects of the Draft Bill which we believe could be clarified or improved.

6 Item 8 (definition of simple corporate bonds depository nominee): paragraph (b) of the proposed new definition of simple corporate bonds depository nominee refers to "a simple corporate bonds depository interest in simple corporate bonds, *where the simple corporate bonds were issued under a two part simple corporate bonds prospectus*" (emphasis added). We query the rationale for the inclusion of the emphasised words and whether this is consistent with the intention of the provision. Where an issue of bonds is structured as an issue via

a depository then there may be no occasion for the bonds themselves to be issued under a prospectus as the offer would be of the depository interests rather than the bonds.

7 Item 10 (section 705): please see our general submission on the mandatory nature of the proposed amendment.

8 Item 12 (section 708(14A)): we query the policy rationale for the exclusion in sub-paragraph (a) where the offer is made to holders of simple corporate bonds. The sub-paragraph should read "an offer of simple corporate bonds if the offer is made to holders of debentures other than simple corporate bonds".

9 Items 15 and 16 (section 709(2A) and 709(4)): we query the policy rationale for excluding the use of profile statements and offer information statements in relation to simple corporate bonds. Why mandate the use of a prospectus for offers made in circumstances where an offer of shares (or other securities) could be made under these alternative disclosure documents?

10 Items 19 and 20 (sections 712(6) and 713(7)): we query the policy rationale for excluding the use of short form prospectuses and the special prospectus content rules for continuously quoted securities in relation to simple corporate bonds. If the securities otherwise satisfy the requirements of these sections why should they not be eligible simply because they are simple corporate bonds?

11 Item 21 (section 713A):

(a) Under subsection (1) the regime is only available for issue offers. We believe the regime should also be available for sale offers (although the utility of this will be limited unless the simple corporate bond prospectus regime is extended to a single document rather than two part prospectuses as proposed in our submission above).

(b) Subsection (3) requires amendment as the stated condition would not be satisfied if the issue was structured as an issue of depository interests as the bonds themselves would not be quoted.

(c) Subsection (6) should include an exception for issues of further tranches in an existing issue where the original issue was more than $50 million.

(d) Subsection (14)(c) should also contemplate changes in administration of laws: the "would" standard should be changed to a "would, or maybe" system with the standard applied to loss of tax deductibility in the previous paragraph.

(e) In subsection (14)(e) and (f) the requirements that all bonds under the offer be redeemed should exclude bonds previously redeemed or repurchased.

(f) For the reasons outlined in our general submissions subsection (15) should require only that the bonds not rank behind unsecured creditors rather than that they rank in priority to them. However, even if the government chooses to retain the requirement that simple corporate bonds enjoy priority over unsecured creditors then the subsection (15) should be redrafted as in its current form it could technically never be satisfied. Under the Corporations Act all debts (other than certain preferred claims such as employee claims) rank equally in a winding up. The 'priority' that secured creditors enjoy is limited to recovering under their security outside the winding up process – secured creditors have only limited capacity to recover their debts in the winding up itself and then they rank equally with other unsecured claims. The same ranking requirement that applies in

relation to the issuer should also apply in relation to the required holding company guarantee where the holding company is the issuer of the relevant other continuously quoted securities that enable to the bonds to be classified as simple corporate bonds.

(g) Subsection (16) should only apply where it is the holding company's securities that make the issue eligible for treatment as simple corporate bonds (ie a subsidiary is relying on a parent's status as issuer of continuously quoted securities).

(h) General: it is standard for terms of bonds to include amendment provisions that permit the bondholders to approve changes to their terms. As these provisions would theoretically permit such things as a lowering of the interest rate or extension of the term to more than 10 years, it should be clarified that the existence of such an amending power is to be ignored for the purposes of determining whether the bond is a 'simple corporate bond'.