



**ASIC**

Australian Securities & Investments Commission

## CONSULTATION PAPER 126

# Facilitating debt raising

December 2009

### About this paper

This consultation paper:

- sets out ASIC's proposals for relief to facilitate offers of quoted corporate bonds and convertible notes; and
- seeks feedback from stakeholders on how effectively annual reports are operating as a means of providing disclosure to investors.

This consultation paper seeks the views of stakeholders, including entities, industry associations, retail investors and their professional advisers.

### 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.

### Document history

This paper was issued on 7 December 2009 and is based on the *Corporations Act 2001* as at 7 December 2009.

### Disclaimer

The proposals, explanations and examples in this paper do not constitute legal advice. They are also at a preliminary stage only. Our conclusions and views may change as a result of the comments we receive or as other circumstances change.

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## The consultation process

You are invited to comment on the proposals in this paper, which are only an indication of the approach we may take and are not our final policy.

As well as responding to the specific proposals and questions, we also ask you to describe any alternative approaches you think would achieve our objectives.

We are keen to fully understand and assess the financial and other impacts of our proposals and any alternative approaches. Therefore, we ask you to comment on:

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

Where possible, we are seeking both quantitative and qualitative information.

We are also keen to hear from you on any other issues you consider important.

Your comments will help us develop our policy on debt capital raisings. In particular, any information about compliance costs, impacts on competition and other impacts, costs and benefits will be taken into account if we prepare a Business Cost Calculator Report and/or a Regulation Impact Statement: see Section F Regulatory and financial impact, p. 32.

### Making a submission

We will not treat your submission as confidential unless you specifically request that we treat the whole or part of it (such as any financial information) as confidential.

Comments should be sent by 19 February 2010 to:

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Corporations  
Australian Securities and Investments Commission  
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## What will happen next?

<b>Stage 1</b>	7 December 2009	ASIC consultation paper released
<b>Stage 2</b>	19 February 2010	Comments due on the consultation paper
	March 2010	Drafting of explanatory materials and any class orders
<b>Stage 3</b>	April 2010	Explanatory materials and any class orders released

## A Overview of ASIC proposals to facilitate debt raisings

### Key points

Recent market conditions have made it more difficult for companies to refinance their debt. ASIC has recently provided relief to facilitate equity capital raisings where there was adequate disclosure to the market and investor protections were not unduly compromised.

We are now consulting on whether we should provide relief to allow certain offers of 'vanilla' corporate bonds to be made to retail investors under a simplified prospectus (vanilla bonds prospectus) similar to a transaction-specific prospectus. As well as assisting issuers, this relief may provide retail investors with greater opportunities to invest in corporate bonds: see Section B.

We are also seeking your feedback on whether we should provide relief to allow listed issuers to use a two-part prospectus approach for offers of vanilla bonds. This approach would involve a base prospectus (which could be used for a number of different offers) and a relatively short offer document relating to a particular offer. Together, the two documents would need to contain all the information required for a vanilla bonds prospectus: see Section C.

In practice, a prospectus is often needed for an offer of convertible notes to institutional investors so that the underlying quoted securities can be on-sold to retail investors. We are proposing relief from the on-sale provisions so that the underlying quoted securities can be on-sold without a prospectus if a cleansing notice containing prospectus-like disclosure is lodged at the time the convertible notes are issued: see Section D.

Both our proposed relief and the existing transaction-specific prospectus regime rely on issuers providing relevant information to the market through annual reports and continuous disclosure announcements. We are seeking feedback on the level of disclosure provided to investors in annual reports and whether this could be improved in the future: see Section E.

## Introduction

- 1 As a result of the global financial crisis, many Australian companies have found it difficult to refinance existing banking facilities and access debt markets. Further, few retail investors have access to listed debt products. 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.

- 2 Earlier this year, ASIC responded to adverse market conditions by providing relief to facilitate equity capital raisings. In particular, we removed various regulatory impediments to rights issues, dividend reinvestment plans, share purchase plans and placements while, at the same time, not unduly compromising investor protection. This relief also increased the opportunity for retail investors to participate in equity capital raisings.
- 3 We believe that now is an appropriate time to consult on relief to facilitate certain offers of ‘vanilla’ corporate bonds. Retail investors currently have very limited direct exposure to corporate bonds. One objective of providing relief would be to increase the opportunities for retail investors to invest directly in quoted corporate bonds.
- 4 In proposing relief, our key considerations are:
- (a) to maintain standards of consumer protection;
  - (b) to expand suitable investment opportunities for retail investors; and
  - (c) to develop the Australian quoted debt market.
- 5 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 propose that any relief will be subject to conditions relating to the issuer, the type of bonds that may be issued and disclosure.
- 6 We would monitor any relief to assess whether it was operating effectively. If it was not, we could narrow or revoke the relief. Conversely, if relief was operating satisfactorily, we might consider broadening it to cover a wider range of bond issues.
- 7 Regardless of any ASIC relief, it is possible that market conditions will generate an increase in the number of corporate bond issues that are extended to retail investors. To assist retail investors who are considering investing in corporate bonds, ASIC has recently issued an investor guide: *Investing in corporate bonds?* This guide is available at [www.fido.asic.gov.au/corporate-bonds](http://www.fido.asic.gov.au/corporate-bonds).

## Regulatory requirements

- 8 In offering corporate bonds for issue, listed entities need to comply with:
- (a) the fundraising provisions in Ch 6D of the *Corporations Act 2001* (Corporations Act);
  - (b) the requirements relating to offers of debentures in Ch 2L of the Corporations Act; and

## (c) the ASX Listing Rules.

- 9 Offers of corporate bonds to retail investors generally require full prospectus disclosure. In contrast, a listed issuer generally only requires a transaction-specific prospectus for offers of quoted shares, options over quoted shares and securities that are convertible into quoted shares: s713 and Class Order [CO 00/195] *Offer of convertible securities under s713*.

Note 1: An offer of corporate bonds can be made using a transaction-specific prospectus if the bonds are in a class of continuously quoted securities: s713. However, if new corporate bonds have a different term or interest rate from existing bonds, they will be in a new class and a transaction-specific prospectus cannot be used.

Note 2: Offers of unlisted debentures require disclosure against key benchmarks on an 'if not, why not' basis: see Regulatory Guide 69 *Debentures: Improving disclosure for retail investors* (RG 69).

- 10 The existing regulatory requirements that apply to offers of corporate bonds play an important role in maintaining investor protection and promoting market transparency. However, the time and expense involved in complying with them may be factors that limit the extent to which offers of corporate bonds are extended to retail investors.

## ASIC proposals

### Vanilla bonds prospectus relief

- 11 We are considering providing relief from the fundraising provisions in Ch 6D to facilitate efficient corporate bond raisings by listed entities, provided that investor protection is not unduly compromised.
- 12 In particular, we are proposing class order relief to allow a listed entity to offer corporate bonds using a simplified prospectus (vanilla bonds prospectus) with a similar level of content to a transaction-specific prospectus: see Section B.

### Two-part prospectus relief

- 13 We are also considering relief to allow a vanilla bonds prospectus for an offer of corporate bonds to be in two parts, comprising:
- (a) a base prospectus, which could be used for several different offers; and
  - (b) a second part, which relates to the terms of a particular offer.

Note: See Section C.

## Conditions of vanilla bonds relief

- 14 Any relief for offers of vanilla bonds will only apply if various conditions are satisfied. These conditions relate to:
- (a) the bonds—relief will only apply to vanilla bonds that will be quoted on issue and where the issue is for a total of at least \$100 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

Note: Auditing Standard ASA 700 sets out when the auditor's report of the financial statements is unmodified. Auditing Standard ASRE 2410 sets out when the auditor's review report of the financial statements is unmodified.

- (c) disclosure—point-of-sale disclosure must be provided for the matters set out in Appendix 1. Ongoing disclosure must also be provided for certain matters (including quarterly updates of key financial disclosures and the quarterly reports required under s283BF).

## Disclosure relief for offers of convertible notes to institutional investors

- 15 The final area in which we are considering relief relates to offers of convertible notes to institutional investors. Although, of themselves, such wholesale offers do not require prospectus disclosure, a prospectus is often needed so that the underlying quoted securities can be on-sold to retail investors.
- 16 We are proposing relief from the on-sale provisions 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: see Section D. A proposed condition of this relief involves enhanced annual reporting disclosure.

## Review of annual reporting disclosure

- 17 Our proposed relief (and, more generally, the transaction-specific prospectus regime) depends on the market receiving information through annual reporting and continuous disclosure. Beyond this, annual reports are a key information document for a company's investors and for the market.
- 18 We are seeking views on how well the annual reporting regime is operating and whether annual reports could become a more effective source of information for investors. Our proposals aim to improve annual reports

published by issuers that rely on our proposed relief by requiring that their future annual reports include updates of key financial disclosures. There may also be scope for broader improvements in the annual reporting regime by enhancing the role of the annual report as a disclosure document.

- 19 In Section E we seek feedback on the current operation of the annual reporting regime and whether there are any potential improvements that would make annual reports more useful for investors. Your feedback will be relevant to our proposed relief and to our understanding of annual report disclosures.

## B Vanilla bonds prospectus relief

### Key points

We propose providing relief to allow an offer of corporate bonds to be made using a vanilla bonds prospectus provided that:

- 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;
- the corporate bonds are 'vanilla' bonds that will be quoted on issue;
- the aggregate size of the bond issue is at least \$100 million;
- the auditor's report on the most recent annual financial report, and any subsequent half-yearly financial report, is unmodified;
- the vanilla bonds prospectus discloses the matters specified in Appendix 1 (including key financial disclosures); and
- the issuer facilitates investor access to ongoing disclosure (including quarterly updates of key financial disclosures).

## Vanilla bonds prospectus relief

### Overview of s713

- 20 The Corporations Act allows a disclosing entity that offers continuously quoted securities or options over such securities to use a transaction-specific prospectus: s713.
- 21 Transaction-specific prospectuses do not need to include all of the information that is contained in a full prospectus. The key information required in a transaction-specific prospectus for an offer of securities includes:
- (a) the effect of the offer on the entity;
  - (b) the rights and liabilities attaching to the securities offered;
  - (c) if the securities are options, the rights and liabilities attaching to:
    - (i) the options themselves; and
    - (ii) the underlying securities; and
  - (d) 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). For details of the content and presentation requirements for a transaction-specific prospectus, see Regulatory Guide 66 *Transaction-specific disclosure* (RG 66) at RG 66.40-66.56.

- 22 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 RG 66.7–66.8.

### Overview of s710

- 23 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.

Note: Additional information is also prescribed by s711.

### Existing relief in [CO 00/195] for offers of convertible securities

- 24 ASIC has given class order relief to allow the use of a transaction-specific prospectus for offers of certain convertible securities which can be converted into underlying quoted securities: see [CO 00/195]. The class order requires disclosure of:
- (a) the information required under s713 in relation to the underlying continuously quoted securities; and
  - (b) the information required under s713(2) for the convertible securities (i.e. the rights and liabilities attaching to the convertible securities).

- 25 The relief available in [CO 00/195] does not impose conditions as extensive as those we are proposing for the vanilla bonds disclosure relief. We will consider whether we should impose additional conditions in the future under [CO 00/195] for offers of convertible securities, based on our experience of these offerings and any relief we may provide for offers of vanilla bonds.

### Using a simplified prospectus for offers of vanilla bonds

- 26 An issuer is able to use a transaction-specific prospectus for an offer of corporate bonds that is 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 companies have corporate bonds that are currently quoted; and
- (b) if an issuer wants 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.

27 There are potential benefits for issuers and retail investors in facilitating issues of quoted corporate bonds. Accordingly, we are proposing relief to allow certain offers of vanilla bonds to be made under a simplified prospectus (vanilla bonds prospectus) similar to a transaction-specific prospectus.

## Overview of proposed relief

### Proposal

**B1** We propose to provide relief permitting an issuer to use a vanilla bonds prospectus for an offer of corporate bonds provided that certain conditions are satisfied relating to the bond issuer, the type of bonds issued and the disclosure regarding those bonds (see proposals B2-B4). We do not propose to provide any relief from the exposure period for the vanilla bonds prospectus or from the requirement to appoint a debenture trustee.

#### *Your feedback*

##### **General**

**B1Q1** Do you agree with our proposed relief allowing a vanilla bonds prospectus to be used for offers of corporate bonds? Why? If relief is given, would a class order or case-by-case relief be preferable?

**B1Q2** Would our proposed relief be of commercial benefit to issuers? Would the relief make it more likely that issuers would extend offers of quoted corporate bonds to retail investors?

**B1Q3** What are the risks and benefits of our proposed relief for investors?

##### **Exposure period**

**B1Q4** Do you agree with our proposal not to provide relief from the exposure period required under s727(3)? Why?

##### **Debenture trustee requirement**

**B1Q5** Do you agree with our proposal not to provide relief from the requirement to appoint a debenture trustee for offers of vanilla bonds? Why?

## Rationale

- 28 We consider that allowing a vanilla bonds prospectus to be used for certain offers of corporate bonds would reduce the time and expense involved for issuers who wish to make these offers available to retail investors. Moreover, we consider that there are potential benefits in providing retail investors with the opportunity to invest in quoted corporate bonds. Our proposed relief would make it more likely that such offers would be extended to retail investors.
- 29 We recognise that offers of quoted corporate bonds may raise investor protection concerns. Although quoted corporate bonds are generally less risky than shares, they are subject to a number of investment risks including credit risk, interest rate risk, liquidity risk and prepayment risk.
- 30 Our proposed conditions for relief aim to ensure that investors will be adequately informed about the bonds being offered where a vanilla bonds prospectus is being used. We have also been mindful of maintaining standards of consumer protection. We have therefore proposed conditions that apply to:
- (a) the issuer;
  - (b) the bonds being offered; and
  - (c) the disclosure that must be provided.

### No exposure period relief

- 31 We do not propose to provide relief from the exposure period of between seven and 14 days provided for in s727(3). An exposure period allows ASIC and market participants the time to scrutinise disclosure documents before they can be used for fundraising: Regulatory Guide 152 *Lodgement of disclosure documents* (RG 152) at RG 152.19. We do not provide relief from s727(3) for offers of convertible securities to retail investors, even though we provide transaction-specific prospectus relief for such offers.
- 32 Although we provide relief in Class Order [CO 00/843] *Options over listed securities: Exposure period relief* so that offers of options over quoted securities are not subject to an exposure period, we consider that there is a benefit in having an exposure period for offers of corporate bonds and convertible securities. Corporate bonds and convertible securities have a more remote connection with the relevant quoted securities than an offer of options. Accordingly, we consider that it is appropriate to maintain the requirement for an exposure period to allow scrutiny of a vanilla bonds prospectus or transaction-specific prospectus for such securities.

### No debenture trustee relief

- 33 We are not proposing any relief from the requirements of Ch 2L, including the requirement that an issuer of corporate bonds must enter into a trust deed

and appoint a trustee for the benefit of bondholders. Chapter 2L provides important protections for retail investors, including requiring a trustee to be appointed and imposing various duties on the issuer, the trustee and any guarantor. Persons who suffer loss or damage as the result of a contravention of Ch 2L also have the right to recover such loss. We consider that while simplified disclosure may be justified for an offer of vanilla bonds, it is not a reason to remove the protections afforded by Ch 2L.

- 34 We are also seeking to strengthen the protections contained in Ch 2L by requiring the quarterly report under s283BF to be published on the issuer's website and on ASX. We consider that facilitating access to the quarterly report will assist bondholders and the market to monitor the performance of the bonds and identify matters that may adversely affect the interests of bondholders.

## Conditions applying to the issuer

### Proposal

- B2** We propose that an issuer should only be allowed to use a vanilla bonds prospectus if:
- (a) that issuer is entitled to use a transaction-specific prospectus for the offer of an existing class of its securities (e.g. ordinary shares that are continuously quoted securities). Amongst other things this will require that the listed securities have been quoted for at least 3 months;
  - (b) trading in the issuer's continuously quoted securities has not been suspended for more than five days during the shorter of the following:
    - (i) the period during which that class of securities was quoted; or
    - (ii) the period of 12 months before the day on which the offer is made; and
  - (c) the auditor's report on the most recent annual financial report, and any subsequent half-yearly financial report, is unmodified.

#### *Your feedback*

##### **Issuer conditions**

- B2Q1** Do you agree with the proposed conditions that must be satisfied in relation to the issuer and its existing continuously quoted securities? Are there any additional conditions that should be required?
- B2Q2** Should we require the bond issuer to satisfy a minimum level of net tangible assets? If so, what is an appropriate minimum?

B2Q3 Should we also require the issuer to satisfy minimum conditions based on key financial metrics (e.g. gearing ratio, interest cover and working capital ratio)? If so, what conditions should be applied?

B2Q4 Should relief extend to foreign issuers that are listed on an approved foreign market and that are proposing to issue vanilla bonds that will be quoted on the approved foreign market or on a prescribed financial market?

## Rationale

35 We propose that our relief will only apply to companies that already have continuously quoted securities on issue and that would be able to use a transaction-specific prospectus for an offer of those securities. It would not be appropriate to permit the use of a vanilla bonds prospectus for an offer of corporate bonds if the issuer was not entitled to use a transaction-specific prospectus for any other securities.

36 Our proposals aim to strengthen the quality of issuers that will be able to rely on our relief by requiring that:

- (a) the issuer's continuously quoted securities have not been suspended for more than five days in the previous 12 months; and

Note: There are corresponding requirements for disclosure exemptions relating to rights issues in s708AA(2)(c) and on-sales in s708A(5)(b).

- (b) the auditor's report on the issuer's most recent financial statements has not been modified.

## Conditions applying to the corporate bonds

### Proposal

B3 We propose that an issuer can only use a vanilla bonds prospectus if the following conditions are met relating to the bonds:

- (a) the corporate bonds being offered are vanilla bonds that will be quoted when issued—we propose that bonds will be vanilla bonds if they:
  - (i) are denominated in Australian dollars;
  - (ii) have a fixed term of no more than 10 years with the principal plus any accrued interest payable at the expiry of the term;
  - (iii) have a fixed rate of return or a floating rate of return that comprises a variable market determined rate (e.g. the three-month bank bill rate) plus a fixed margin;
  - (iv) provide for interest to be paid periodically on the dates specified in the prospectus;

- (v) rank at least equally with amounts owing to unsecured and unsubordinated creditors of the issuer (i.e. the bonds are not subordinated);
  - (vi) are not convertible into any other securities; and
  - (vii) are issued to all investors at the same price;
- (b) the aggregate size of the bond issue will be at least \$100 million; and

Note: If an issuer is not able to meet this minimum subscription requirement within four months of the date of the vanilla bonds prospectus, our relief would require the issuer to refund any subscription money received.

- (c) the bonds will be governed by a trust deed that requires the bond issuer to update the key financial disclosures contained in the vanilla bonds prospectus on a quarterly basis and to provide these updates, together with the quarterly reports required under s283BF, to ASX and to include them on the issuer's website.

#### *Your feedback*

##### **Corporate bond conditions**

- B3Q1 Do you agree that relief should be limited to offers of 'vanilla' bonds? Do you agree with our proposed conditions for vanilla bonds? Are there any other conditions that should be satisfied?
- B3Q2 Should Australian Prudential Regulation Authority (APRA) regulated entities that are issuing bonds for regulatory capital be exempt from the requirement for bonds to be vanilla bonds? For example, should we permit APRA regulated entities to raise regulatory capital by issuing subordinated debt under a vanilla bonds prospectus?
- B3Q3 Do you agree with the requirement for the issue to be a minimum subscription size? If so, is \$100 million an appropriate minimum amount?
- B3Q4 Should we require that, on issue, there is no secured debt that ranks ahead of the corporate bonds? Alternatively, should any additional conditions apply if the issuer has existing secured debt that ranks ahead of the bonds? If so, what conditions should apply (e.g. conditions restricting the level of secured debt that can be on issue)?
- B3Q5 Should we prohibit the issuer from issuing any new debt that would rank ahead of the corporate bonds? Should we also prohibit the issuer from providing any further security that would cause existing debt to rank ahead of the corporate bonds?
- B3Q6 Are there any circumstances in which the terms of issue of vanilla bonds should permit interest to be deferred? Please provide details.
- B3Q7 Are there any circumstances in which the terms of issue of vanilla bonds should permit early redemption? Please provide details.

## Rationale

- 37 Our relief will only apply to offers of bonds that will be quoted on issue. These types of bonds do not raise the same investor protection concerns as unlisted debentures. That is because under our relief:
- (a) the issuer will have been (and will continue to be) subject to continuous disclosure requirements and supervised by the relevant market operator. The issuer will already have supplied the market with much of the information that would be relevant to a holder of the corporate bonds;
  - (b) the market operator will need to assess and, if appropriate, admit the corporate bonds to quotation;
  - (c) there is more likely to be a liquid secondary market for the corporate bonds following their issue than for an offer of unlisted debentures; and
  - (d) there is a requirement that the corporate bonds must be vanilla bonds, which have relatively simple features.

Note: If the bonds being offered will not be quoted, the requirements in RG 69 will apply and disclosure must be made using a full prospectus against key benchmarks on an 'if not, why not' basis.

- 38 We propose that our relief will only apply to offers of vanilla bonds, which do not have complex or unusual terms and conditions. For example, our relief will only apply to bonds with a fixed term that offer regular payments of interest at a fixed rate or at a rate that is a fixed margin above a base market rate. Retail investors are more likely to understand the risks and features of vanilla bonds than they are for more complex bonds.
- 39 We have also proposed that the aggregate amount being raised by the issuer must be at least \$100 million. This condition is intended to make it more likely that:
- (a) there will be a liquid market for the bonds once they are issued; and
  - (b) there will be institutional participation in the bond issue, which will further assist in the accurate pricing of the bonds.

## Disclosure conditions

### Proposal

- B4** We propose that, under our relief, the vanilla bonds prospectus must contain the following matters, as identified in Appendix 1:
- (a) disclosure of the key features, risks and benefits of the bonds;

- (b) the following key financial disclosures:
  - (i) details of any debt ranking ahead of the bonds;
  - (ii) whether the issuer is in breach of any loan covenants or has defaulted on previous debt obligations as specified in Appendix 1;
  - (iii) the gearing ratio, determined as specified in Appendix 2;
  - (iv) the interest cover, determined as specified in Appendix 2; and
  - (v) the working capital ratio, determined as specified in Appendix 2;
- (c) a commitment to update these financial disclosures on a quarterly basis and provide these updates, together with the quarterly reports required under s283BF, to ASX and to include them on the issuer's website;
- (d) a statement that all information of the type referred to in s713(5)(b) has been disclosed to the market or is in the prospectus (to the extent that it is reasonable to find that information in a prospectus);
- (e) disclosure of any other information that would be required under a transaction-specific prospectus if the corporate bonds were continuously quoted securities;
- (f) a facility allowing investors to receive email notification when new ongoing information is published; and
- (g) a statement that ASIC has published an investor guide for retail investors who are considering investing in corporate bonds and that a copy of the guide is available from ASIC free of charge.

#### *Your feedback*

##### **Disclosure conditions**

- B4Q1 Do you agree that our relief should be conditional on point-of-sale disclosure of the key matters identified in Appendix 1? Are there any other key matters for which disclosure should be required?
- B4Q2 Should we require the key matters in Appendix 1 to be disclosed in a particular order to assist investors in comparing different offer documents?
- B4Q3 Do you agree with our proposals in relation to disclosure of the gearing ratio, interest cover and working capital ratio, as outlined in Appendix 2? Are there any other financial metrics that should be included for use by either retail or institutional investors? If so, what are they and why are they needed? Are there any entities for which disclosure of these metrics may not assist retail investors (e.g. APRA regulated entities)?
- B4Q4 Do you agree that our relief should be conditional on the ongoing quarterly disclosure of key financial information and the quarterly reports required under s283BF? Are there any other matters for which ongoing disclosure should be required?

## Rationale

- 40 Appendix 1 sets out the matters that we propose will need to be disclosed in a vanilla bonds prospectus. We believe that disclosure of these matters will provide investors with important information about the key risks and features of the bonds. The required information includes details about interest coverage, gearing, working capital and the amount of other debt that ranks ahead of the bonds offered or that may rank ahead of those bonds in particular circumstances.
- 41 We encourage all issuers of quoted corporate bonds to consider our proposed disclosure requirements when preparing a prospectus, regardless of whether or not we ultimately provide relief. The greater the consistency between prospectuses, the easier it will be for investors to compare different bond offerings and make informed investment decisions.
- 42 We are also proposing that issuers must meet ongoing disclosure requirements in order to assist investors. In particular, issuers must:
- (a) provide quarterly updates of the key financial disclosures;
  - (b) publish on their website and on ASX the quarterly reports provided to ASIC and the trustees under s283BF;
  - (c) publish on their website copies of ongoing disclosures (e.g. annual and half-yearly reports, continuous disclosure notices, quarterly reports under s283BF and quarterly reports updating key financial disclosures); and
  - (d) give investors the option of receiving email notification when new ongoing disclosures regarding the bonds are published on the issuer's website.
- Note: In considering good principles for website disclosure, the general guidance in Regulatory Guide 198 *Unlisted disclosing entities: Continuous disclosure obligations* (RG 198) may be of assistance.
- 43 Whether or not we provide relief, we consider that all investors in corporate bonds would benefit from receiving updates of key information, as outlined in paragraph 42.

## C Two-part prospectus relief

### Key points

Some jurisdictions allow the use of a two-part prospectus for offers of corporate bonds. Offers are made via a general-purpose base prospectus (which can be used for a number of different offers) together with a short pricing supplement containing the details of a particular offer.

We are seeking your feedback on whether we should provide relief to facilitate a two-part prospectus approach for offers of vanilla bonds in Australia.

A two-part prospectus approach could assist issuers that were likely to make a number of offers over the life of the base prospectus.

## Two-part prospectus relief

### Two-part offers in the US and the UK

- 44 In the US and the UK, companies are able to continuously offer corporate bonds to retail investors from an initial base prospectus. Each subsequent offer is made under a relatively short pricing supplement.
- 45 The UK has a detailed ‘building block’ disclosure regime for debt offerings, which prescribes content requirements for both the base prospectus and the pricing supplement. By comparison, the US has a less prescriptive approach, which gives issuers greater flexibility in deciding whether it is more appropriate to include information in the base prospectus or in the pricing supplement. In addition, a base prospectus in the US can have an expiry date of up to three years. This means that offers of debt in the US can occur continuously for three years under a single prospectus. In the UK, the base prospectus has a 12-month life span.

### Current ability to use a two-part prospectus approach

- 46 Entities that issue debentures in the ordinary course of their business currently have a limited ability to adopt a two-part prospectus approach. ASIC has given class order relief to allow a prospectus for an offer of debentures not to include interest rate and term information, where the prospectus is accompanied by the most recent application form containing this information that has been lodged with ASIC: *Class Order [CO 00/173] Debenture prospectuses: Incorporation of information on application forms.*

- 47 There are various regulatory impediments to the use of a more flexible two-part prospectus approach for offers of corporate bonds in Australia. These include:
- (a) a prospectus must include all the terms and conditions of an offer: s711(3). Without relief, this requirement would not be satisfied until the second-part prospectus was lodged;
  - (b) if a supplementary prospectus is lodged, the prospectus is taken to be the initial prospectus together with the supplementary prospectus: s719(4). This provision could create difficulties if there were a number of supplementary prospectuses, each relating to a separate offer; and
  - (c) the life of a prospectus is limited to 13 months: s711(6). A two-part prospectus approach would most benefit issuers that are likely to make more than one offer of securities over the life of the base prospectus.
- 48 We are interested in your feedback on whether we should provide relief to permit a two-part prospectus approach and, if so, what conditions should be applied.
- 49 We do not propose to provide any relief from the prospectus liability provisions in Div 1 of Pt 6D.3 of the Corporations Act. Where an offer was made using a base prospectus together with a second-part prospectus, these liability provisions would apply in the same way as they currently apply to an offer made using a prospectus together with a supplementary prospectus.

## Proposal

- c1** ASIC is considering relief to permit a two-part prospectus approach to be used for offers of vanilla bonds. Under this approach, an issuer could offer vanilla bonds under a base prospectus (which could be used for a number of offers) together with a second-part prospectus (which would relate to a particular offer). Together, the base prospectus and the second-part prospectus would need to satisfy the content requirements for a vanilla bonds prospectus.

Note: This relief would only be available to issuers who were entitled to use a vanilla bonds prospectus for the offer.

### *Your feedback*

#### **Relief to extend operation of [CO 00/173]**

- C1Q1** Should we extend the operation of [CO 00/173] so that it applies to listed entities that are entitled to use a vanilla bonds prospectus but do not issue debentures in the ordinary course of their business? This would enable interest rate and term information to be set out in an application form and facilitate 'rolling' bond issues.

C1Q2 Would providing such relief be of commercial benefit to listed entities? Why?

C1Q3 Would providing such relief raise any investor protection concerns?

#### **General two-part vanilla bonds prospectus relief**

C1Q4 Should we provide relief to allow an issuer that is entitled to use a vanilla bonds prospectus to:

- (a) lodge a base prospectus which does not relate to any particular offer of corporate bonds and does not contain all the information required to be included in a vanilla bonds prospectus for any particular offer; and
- (b) (when making a particular offer of quoted corporate bonds) lodge a supplementary prospectus which, together with the base prospectus, contains all the information that is required to be disclosed in a vanilla bonds prospectus for the offer?

C1Q5 If a two-part prospectus approach were available, what information would issuers be likely to include in:

- (a) the base prospectus; and
- (b) the second-part prospectus?

C1Q6 Are any investor protection concerns raised by the use of a two-part offer document for offers of quoted corporate bonds? Are there any conditions that could address these concerns, while preserving the benefits of a two-part prospectus approach (e.g. conditions mandating that particular disclosures must be made in the second-part prospectus)?

C1Q7 To what extent does the 13-month time limit for prospectuses reduce the benefit of a two-part prospectus? Is there another maximum term that would strike an appropriate balance between flexibility for issuers and investor protection?

## **Rationale**

### **Advantages and disadvantages of a two-part prospectus approach**

50 A two-part prospectus approach could assist issuers that were likely to make a number of offers over the life of the base prospectus. Once the base prospectus had been prepared, subsequent offers could potentially be made more quickly than if a completely new prospectus were required for each subsequent offer.

51 On the other hand, our proposed vanilla bonds prospectus would reduce current prospectus content requirements. It will focus on the details of a particular offer rather than on historical information. Providing vanilla bonds

prospectus relief would be likely to reduce the potential benefit for issuers in adopting a two-part prospectus approach.

- 52 Facilitating a two-part prospectus approach may also raise investor protection concerns. For example, some retail investors may only read the specific offer document, rather than also reading the general base prospectus. This would be a concern if, for example, key risks about investing in the company's bonds were contained in the base prospectus rather than in the second-part prospectus.

#### **Content requirements under a two-part prospectus approach**

- 53 When read together, the base prospectus and the second-part prospectus would need to satisfy all the content requirements for a vanilla bonds prospectus. This would mean that the second-part prospectus in relation to an offer of corporate bonds would need to contain the following information to the extent that it was not included in the base prospectus:
- (a) the terms of the particular corporate bonds being offered;
  - (b) details of the effect of the offer on the issuer;
  - (c) any information excluded from a continuous disclosure notice in accordance with the ASX Listing Rules;
  - (d) any supplementary disclosure necessary to update the information in the base prospectus; and
  - (e) any other information required to be included in a vanilla bonds prospectus.
- 54 Issuers would also need to ensure that, when read together, the base prospectus and the second-part prospectus were worded and presented in a clear, concise and effective manner: s715A.

## D Disclosure relief for offers of convertible notes to institutional investors

### Key points

Although a prospectus is not strictly required for an offer of convertible notes to institutional investors, in practice a transaction-specific prospectus will often be necessary to allow the underlying quoted securities to be on-sold to retail investors.

The need to prepare a transaction-specific prospectus may act as an impediment to entities that wish to raise funds by issuing convertible notes to institutional investors.

We are proposing relief from the on-sale provisions. This will facilitate institutional offers of convertible notes that are accompanied by a cleansing notice providing prospectus-like disclosure. A proposed condition of relief would be that certain ongoing disclosures are included in the annual report of the issuer during the term of the convertible notes.

### Institutional offers of convertible notes

55 Some offers of convertible notes are only marketed to institutional investors (including offshore institutional investors). These offers do not require a prospectus since there is no retail participation. Similarly, the secondary sale of convertible notes is limited to institutional investors and does not require a prospectus.

56 Although the issue and sale of convertible notes do not require a prospectus, following their conversion the underlying quoted securities may be on-sold to retail investors. So that a prospectus is not required for the on-sale of the underlying securities within 12 months of the conversion, the issuer will generally need to:

- (a) prepare a prospectus for the 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*; or

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

- (b) issue a cleansing notice on each conversion so that the on-sales fall within the exemption in s708A(5).

- 57 The requirement to prepare a prospectus for the convertible notes or issue a cleansing notice on each conversion can make it less attractive for companies to raise funds from institutional investors via an issue of convertible notes.
- 58 We are considering providing relief from the requirement to prepare a transaction-specific prospectus in relation to offers of convertible notes to institutional investors. Instead, a cleansing notice containing prospectus-like disclosure would be required at the time the convertible securities were issued. A proposed condition of our relief would be for certain ongoing disclosures to be included in the annual report of the issuer during the term of the convertible notes.

### Proposal

- D1** We propose to provide relief from the on-sale provisions for the on-sale of underlying quoted securities issued on the conversion of convertible notes where:
- (a) the issuer would have been entitled to use a transaction-specific prospectus for the offer of the convertible notes under [CO 00/195];
  - (b) trading in the underlying quoted securities has not been suspended for more than five days during the previous 12 months;
  - (c) the offer of the convertible notes does not require a disclosure document;
  - (d) the convertible notes may not be on-sold to retail investors;
  - (e) the issuer provides a cleansing notice to the relevant market operator which:
    - (i) contains the information required by s713(2) in relation to the convertible notes;
    - (ii) contains the information required by s713(2)–(5) in relation to the underlying securities;
    - (iii) is worded in a clear, concise and effective manner;
    - (iv) satisfies the requirements of 716(2) in relation to statements by third parties; and
    - (v) is given to the relevant market operator on the same day as, or within two business days before, the day on which the convertible notes are first issued;
  - (f) the conversion of the convertible notes does not involve any further offer; and
  - (g) the annual report of the issuer contains information about:
    - (i) how many notes can still be converted, the number of underlying securities they will convert into, the price (if any) to be paid on conversion and the circumstances in which conversion may occur;
    - (ii) the issuer's remaining liability to make payments under the notes;

- (iii) the average conversion price (if any) paid for any notes converted during the previous 12 months and the number of underlying securities issued on conversion; and
- (iv) any other matters relating to the notes that holders of the issuer's ordinary shares or other ED (enhanced disclosure) securities would reasonably require to make an informed assessment of the issuer's financial position and its prospects for future financial years.

Note: Some of the information referred to in paragraph D1(g) may also be required by relevant accounting standards.

#### *Your feedback*

- D1Q1 Do you agree with our proposed relief? Why? If relief is given, would a class order or case-by-case relief be preferable?
- D1Q2 To what extent is the requirement to prepare a transaction-specific prospectus in order to come within the on-sale relief in [CO 04/671] an impediment to offers of convertible notes to institutional investors? Would our proposed relief simplify the offer process?
- D1Q3 Do you agree with the proposed conditions for our relief? Should we require any additional disclosures to be made or impose any additional conditions?

## **Rationale**

- 59 In the absence of relief, an issuer's ability to issue convertible notes to institutional investors is limited by the fact that the underlying securities may generally only be on-sold to retail investors within 12 months if the issuer provides:
- (a) a transaction-specific prospectus in relation to the convertible notes; or
  - (b) a cleansing notice on each conversion.
- 60 We have received submissions from industry that the option of providing a cleansing notice on each conversion is often unattractive to issuers since:
- (a) there may be multiple conversions that 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.
- 61 We have received submissions that the option of preparing a transaction-specific prospectus is also 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.

62 In our view, our proposed relief should make it easier for entities to issue convertible notes without undermining protection for retail investors. This is because:

- (a) the convertible notes will not be issued or on-sold to retail investors—it is only the underlying quoted securities that may be held by retail investors;
- (b) the issuer will be subject to continuous disclosure obligations and there will be prospectus-like disclosure at the time the convertible notes are issued, meaning that the market should receive sufficient information about the issue of convertible notes;
- (c) it is unlikely that an issuer that relied on our relief would have the purpose of seeking to avoid disclosure to retail investors, contrary to the policy behind the on-sale provisions; and
- (d) we have proposed ongoing disclosures contained in the issuer's annual report that will assist investors in deciding whether or not to purchase shares sold after conversion of the convertible notes.

## E Review of annual reporting disclosure

### Key points

Both the transaction-specific prospectus provisions and our proposed relief rely on issuers providing the market with relevant information through the provision of annual reports and continuous disclosure announcements.

Our proposals aim to make annual reports more useful for investors in corporate bonds by requiring issuers that rely on our relief to provide updates of key financial disclosures in their annual report.

Our proposals also aim to make annual reports more useful for investors purchasing shares issued under convertible securities by requiring issuers that rely on our relief to provide certain ongoing information in their annual report.

We are interested in your feedback on how effective annual reports are as a source of information for investors and whether there is scope to improve them by enhancing the level of information that they currently provide.

### Need for effective annual reports

- 63 A key assumption underpinning our proposed relief from the requirement to provide full prospectus disclosure is that issuers will have already provided the market with relevant information through their annual financial report, half-yearly financial report and subsequent continuous disclosure notices. This assumption also forms the basis for the lower level of disclosure required under the transaction-specific prospectus regime.
- 64 Beyond the context of our proposed relief and the transaction-specific prospectus regime, annual reports are a vital source of information for existing investors and the market in general. As well as information about the company's financial position and performance, an annual report for a listed company must contain the information required by s299, 299A, 300 and 300A. This includes:
- (a) a review of the company's operations during the year;
  - (b) details of significant changes in the company's state of affairs during the year;
  - (c) the company's principal activities during the year and any significant changes in the nature of those activities during the year;
  - (d) details of any matter or circumstance that has arisen since the end of the year that has significantly affected, or may significantly

affect in future financial years, the company's operations, the results of those operations or the company's state of affairs;

- (e) likely developments in the company's operations in future financial years and the expected results of those operations;
- (f) information that members would reasonably require to make an informed assessment of the company's operations, financial position, business strategies and prospects; and
- (g) where subject to environmental regulation, the company's performance in relation to those environmental laws.

Note: An annual report may omit certain information if including it would be likely to result in unreasonable prejudice to the company: s299(3) and 299A(3).

65 We consider that annual reports best serve the interests of investors when they:

- (a) act as a balanced and objective source of information for investors—they should not be a marketing document whose primary focus is to promote a positive image of the company;
- (b) contain meaningful forward-looking information about the company, rather than focusing on the company's historical performance. They should provide a similar level of forward-looking information as other disclosures that deal with the company's position and performance (e.g. the chairman's and CEO's addresses to the annual general meeting and investor briefings);
- (c) do not simply provide data on the company's performance, but include analysis from management that gives context to the data and assists investors to understand its implications;
- (d) as well as highlighting positive aspects of a company's performance and prospects, give prominence to risks and areas of poor performance; and
- (e) are structured in a way that makes it easy for investors to navigate and find relevant information.

66 We are interested in your feedback on how the annual reporting regime is currently working. Our proposals aim to make annual reports more useful for investors in corporate bonds by requiring issuers that rely on our relief to include an update of key financial disclosures in their annual report. Our proposed relief aims to promote ongoing disclosure in other ways, such as requiring quarterly updates of key financial disclosures and allowing bondholders to be notified of new information via email. There may be benefits in considering more extensive changes to annual reports so that they are a more useful source of information for investors in corporate bonds and other quoted securities.

## Proposal

- E1 We propose to review the current operation of the annual reporting regime and examine how annual reports might be improved as an effective source of information for investors.

### *Your feedback*

- E1Q1 How useful are annual reports as a source of information for investors in corporate bonds and other quoted securities? Are there any common features of the presentation or content of annual reports that detract from their effectiveness? What improvements could be made to annual reports to make them a more useful source of information?
- E1Q2 Certain content requirements for annual reports focus on information reasonably required by members: s299A. Holders of corporate bonds are not members. Other than the updates to the key financial disclosures identified in Appendix 1, is there any other information reasonably required by holders of corporate bonds that is not currently required to be included in an annual report?
- E1Q3 Would there be benefits for investors in expanding the role of annual reports so that they provided a more detailed update of key information about a company and its securities? Are there any matters not currently included in the annual report that would be particularly useful to investors and that are required to be included in a prospectus under s710?

## F Regulatory and financial impact

67 In developing the proposals in this paper, we have carefully considered their regulatory and financial impact. On the information currently available to us we think they will strike an appropriate balance between facilitating efficient offers of debt securities and investor protection concerns.

68 Before settling on a final policy, we will comply with the requirements of the Office of Best Practice Regulation (OBPR) by:

- (a) if regulatory options are under consideration, undertaking a preliminary assessment of the impacts of the options on business and individuals or the economy;
- (b) if our proposed option has more than low impact on business and individuals or the economy, consulting with OBPR to determine the appropriate level of regulatory analysis; and
- (c) conducting the appropriate level of regulatory analysis—that is, complete a Business Cost Calculator report (BCC report) and/or a Regulation Impact Statement (RIS).

69 All BCC reports and RISs are submitted to the OBPR for approval before we make any final decision. Without an approved BCC Report and/or RIS, ASIC is unable to give relief or make any other form of regulation, including issuing a regulatory guide that contains regulation.

70 To ensure that we are in a position to properly complete any required BCC report or RIS, we ask you to provide us with as much information as you can about:

- (a) the likely compliance costs;
- (b) the likely effect on competition; and
- (c) other impacts, costs and benefits,

of our proposals or any alternative approaches: see ‘The consultation process’ p. 4.

# Appendix 1

## Proposed vanilla bonds prospectus requirements

- 1 A statement that ASIC has published an investor guide for retail investors who are considering investing in corporate bonds and that a copy of the guide can be obtained free of charge from our FIDO website at [www.fido.asic.gov.au/corporate-bonds](http://www.fido.asic.gov.au/corporate-bonds) or by contacting ASIC on 1300 300 630.
- 2 A statement that, in addition to the information contained in the prospectus, the following information is, and will be, available on ASX's website and on the issuer's website:
  - (a) continuous disclosure announcements lodged with ASX;
  - (b) annual financial report and half-yearly financial report; and
  - (c) quarterly reports that will be made available during the term of the bonds and that will contain:
    - (i) information relating to the bonds included in the quarterly report provided to the trustee and ASIC under s283BF of the Corporations Act;
    - (ii) the following key financial disclosures, determined as at the end of each quarter:
      - (A) details of any debt ranking ahead of the bonds or that is proposed to rank ahead of the bonds in the future (e.g. existing debt that may become secured, or new secured debt that is proposed to be issued in the future); and
      - (B) whether the issuer has materially breached any loan covenants or debt obligations during the period covered in the quarterly report; and
    - (iii) the key financial metrics for the issuer, determined as specified in Appendix 2.
- 3 A statement that investors who wish to receive email notification when new ongoing information is published can elect to do so by providing the issuer with their email address where indicated on the application form for the bonds.
- 4 A timetable setting out the key dates in relation to the offer (e.g. offer period, issue date, commencement of trading of the bonds, first interest payment date, and maturity date).
- 5 The key features of the offer, including details of:
  - (a) the issuer;

- (b) the term and maturity date of the bonds;
  - (c) the aggregate amount being raised;
  - (d) the minimum subscription amount and a statement that if this amount is not met application money will be refunded;
  - (e) the interest rate payable on the bonds;
  - (f) the interest payment dates;
  - (g) the fact that the face value of the bonds will be repaid on the maturity date;
  - (h) the fees and charges payable in relation to the bonds, together with a general statement regarding taxation of interest on the bonds;
  - (i) whether the bonds are secured or unsecured and what this means for investors;
  - (j) the ranking of the bonds in relation to the other debt obligations of the issuer, together with a description of what this means for investors in the event of a liquidation;
  - (k) whether the issuer may issue secured debt in the future or grant any security in relation to existing unsecured debt, the circumstances in which this may occur and what this means for investors;
  - (l) the amount of other debt that would need to be paid in priority to the bonds in the event of a liquidation or that may need to be paid in priority to the bonds in particular circumstances;
  - (m) any guarantee of the issuer's obligations in relation to the bonds and any significant limitations (including financial limitations) that apply to the guarantee;
  - (n) the voting rights of bondholders;
  - (o) the prescribed financial market on which the bonds will be listed; and
  - (p) the legal framework governing the bonds, including any material provisions relating to the bonds in the debenture trust deed.
- 6 Information about the material risks of investing in the bonds, including:
- (a) the risks associated with bonds generally and with the issuer's bonds in particular; and
  - (b) the risks associated with the issuer's business that may affect the bonds.
- 7 Information about the benefits of investing in the bonds.
- 8 A corporate profile and description of the financial position of the issuer relevant to the bond issue, including:
- (a) brief details of the issuer's business;

- (b) the purpose of the bond issue and the effect of the issue on the issuer, including details of the issuer's debt profile following the issue of the bonds;
- (c) the issuer's financial capacity to meet its obligations under the bonds;
- (d) the gearing ratio for the issuer, determined as specified in Appendix 2, together with an explanation of what this means for investors;
- (e) the interest cover for the issuer, determined as specified in Appendix 2, together with an explanation of what this means for investors;
- (f) the working capital ratio for the issuer, determined as specified in Appendix 2, together with an explanation of what this means for investors; and
- (g) details of whether the issuer has materially breached any loan covenants or debt obligations in the two years prior to the date of the prospectus.

9 Details of how investors can apply for the bonds.

10 A statement that all information that investors and their professional advisers would reasonably require to make an informed assessment of:

- (a) the assets and liabilities, financial position and performance, profits and losses, and prospects of the issuer; and
- (b) the rights and liabilities attaching to the bonds being offered,

has been disclosed in the prospectus or has been previously disclosed to the market operator.

The prospectus must contain this information only to the extent to which it is reasonable for investors and their professional advisers to expect such information in the prospectus.

11 Any other information that would need to be included in a transaction-specific prospectus if the bonds were continuously quoted securities.

## Appendix 2

### Key financial metrics

#### Gearing ratio

1 A gearing ratio indicates the extent to which an issuer is funded by debt. It gives an indication of the potential risks the issuer faces in terms of its level of borrowings due, for example, to an increase in interest rates.

2 The gearing ratio should be calculated using the following formula:

$$\text{Gearing ratio} = \frac{\text{Total liabilities}}{\text{Total equity}}$$

3 If the issuer prepares consolidated financial statements, the gearing ratio should be based on the consolidated figures. If the issuer has a current prospectus for bonds, the gearing ratio should be calculated both before and after the effect of the proposed bond issue.

4 The gearing ratio provided in the annual report, quarterly reports and vanilla bonds prospectus should be based on the issuer's latest financial statements. The latest financial statements would usually be the latest audited or reviewed financial statements, except where the issuer is aware of material changes since those statements. However, for the quarterly reports to members, the financial statements need not be audited or reviewed.

5 If the issuer has material off balance sheet financing, the issuer should disclose the following gearing ratios:

- (a) a 'look through' gearing ratio that takes into account such financing; and
- (b) a gearing ratio based on the liabilities disclosed in the issuer's financial statements.

Note: Examples of off balance sheet financing include borrowings of equity accounted investments.

6 Issuers should also explain to investors what the ratio means in practical terms and how investors can use the ratio to determine the level of risk.

#### Interest cover

7 The interest cover gives an indication of an issuer's ability to meet its interest payments from earnings. It therefore provides important information

about the issuer's financial sustainability and the risks associated with the issuer's level of borrowing. A low interest cover ratio may indicate that the issuer could face difficulties in servicing its debt if earnings decrease or interest rates increase.

8 The interest cover should be calculated using the following formula:

$$\text{Interest cover} = \frac{\text{EBITDA}}{\text{Net interest expense}}$$

9 If the issuer prepares consolidated financial statements, the interest cover should be based on the consolidated figures. If the issuer has a current prospectus for bonds, the net interest expense should be calculated both before and after the effect of the proposed bond issue. The net interest expense is the interest expense net of interest revenue. Net interest expense calculations should take into account any related hedging arrangements recognised in the profit and loss statements.

10 EBITDA (earnings before net interest expense, taxes, depreciation and amortisation) and the net interest expense used to calculate the interest cover in the annual report, quarterly reports and vanilla bonds prospectus should be consistent with disclosures in the issuer's latest financial statements. The latest financial statements would usually be the latest audited or reviewed financial statements, except where the issuer is aware of material changes since those statements. However, for the quarterly reports to members, the financial statements need not be audited or reviewed.

11 For the quarterly reports to members, EBITDA and net interest expense should be calculated over the period commencing on the first day of the current financial year and ending on the last day of the quarter.

12 Issuers should also explain how investors can use the interest cover to assess the issuer's ability to meet its interest payments.

### **Working capital ratio**

13 A working capital ratio indicates whether an issuer has sufficient short-term assets to meet its short-term liabilities. Generally, a higher ratio indicates a greater ability to meet liabilities over the short term (including unexpected liabilities).

14 The working capital ratio should be calculated using the following formula:

$$\text{Working capital ratio} = \frac{\text{Current assets}}{\text{Current liabilities}}$$

- 15 If the issuer prepares consolidated financial statements, the working capital ratio should be based on the consolidated figures. If the issuer has a current prospectus for bonds, the working capital ratio should be calculated both before and after the effect of the proposed bond issue.
- 16 The working capital ratio provided in the annual report, quarterly reports and vanilla bonds prospectus should be based on the issuer's latest financial statements. The latest financial statements would usually be the latest audited or reviewed financial statements, except where the issuer is aware of material changes since those statements. However, for the quarterly reports to members, the financial statements need not be audited or reviewed.
- 17 Issuers should also explain to investors what the ratio means in practical terms and how investors can use the ratio to determine the level of risk.

## Key terms

Term	Meaning in this document
APRA	Australian Prudential Regulation Authority
ASIC	Australian Securities and Investments Commission
Ch 6D (for example)	A chapter of the Corporations Act (in this example, numbered 6D)
[CO 00/195] (for example)	An ASIC class order (in this example, numbered 00/195)
Corporations Act	<i>Corporations Act 2001</i> , including regulations made for the purposes of the Act
key financial disclosures	The following key financial disclosures for the issuer: <ul style="list-style-type: none"> <li>• details of any debt ranking ahead of the bonds or that is proposed to rank ahead of the bonds in the future;</li> <li>• whether the issuer is in material breach of loan covenants or debt obligations;</li> <li>• the key financial metrics for the issuer, determined as specified in Appendix 2</li> </ul>
key financial metrics	The following key financial metrics for the issuer, determined as specified in Appendix 2: <ul style="list-style-type: none"> <li>• gearing ratio;</li> <li>• interest cover; and</li> <li>• working capital ratio</li> </ul>
quoted corporate bonds	Corporate bonds: <ul style="list-style-type: none"> <li>• that have been admitted to quotation on a prescribed financial market;</li> <li>• for which an application for admission to quotation on that financial market has been made to the operator of that market; or</li> <li>• for which an application for admission to quotation on that financial market will be made to the operator of that market within seven days after the date of the prospectus offering the corporate bonds</li> </ul>
RG 69 (for example)	An ASIC regulatory guide (in this example, numbered 69)
s713 (for example)	A section of the Corporations Act (in this example, numbered 713)

Term	Meaning in this document
vanilla bonds	Corporate bonds that: <ul style="list-style-type: none"> <li>• are denominated in Australian dollars;</li> <li>• have a fixed term of no more than 10 years with the principal plus any accrued interest payable at the expiry of the term;</li> <li>• have a fixed rate of return or a floating rate of return that comprises a variable market determined rate (e.g. the three-month bank bill rate) plus a fixed margin;</li> <li>• provide for interest to be paid periodically on the dates specified in the prospectus;</li> <li>• rank at least equally with amounts owing to unsecured and unsubordinated creditors of the issuer (i.e. the bonds are not subordinated);</li> <li>• are not convertible into any other securities; and</li> <li>• are issued to all investors at the same price</li> </ul>
vanilla bonds prospectus	A prospectus for an offer of vanilla bonds that satisfies the content requirements specified in Appendix 1