

RIALTO TOWERS 525 COLLINS STREET MELBOURNE  
GPO BOX 769G MELBOURNE VIC 3001 AUSTRALIA  
DX 204 MELBOURNE www.minterellison.com  
TELEPHONE +61 3 8608 2000 FACSIMILE +61 3 8608 1000

1 July 2008

**BY EMAIL: [financialservicesgreenpaper@treasury.gov.au](mailto:financialservicesgreenpaper@treasury.gov.au)**

Mr Geoff Miller  
General Manager  
Corporations and Financial Services Division  
Treasury  
Langton Crescent  
PARKES ACT 2600

Dear Mr Miller

## **Submission - Green Paper on Financial Services and Credit Reform**

We refer to the Green Paper on Financial Services and Credit Reform (**Green Paper**) that was released by the Commonwealth Department of Treasury on 3 June 2008.

We submit the following comments in relation to Section 4 of the Green Paper regarding debentures.

### **1. Part A – Background**

We note that the Green Paper is based on 'a number of high-profile collapses of property development companies, starting with Westpoint and followed by Fincorp, ACR and Bridgecorp' (page 35). In particular, a case study is provided regarding Westpoint.

It is our submission that these case studies do not provide sufficient relevant background for the types of reforms that the Green Paper outlines in Section 4 in relation to debentures. For example, Westpoint is not a typical case of an unlisted offering of debentures as is demonstrated by the High Court decision which concluded that Westpoint had misconceived the nature and structure of its offering to the public, ie the offering should not have been made in the form of promissory notes but structured as a managed investment scheme. Clearly, most debenture offerings in the market place are not so misconstrued and are not misleading to investors in any way. This means that while the nature of the disclosure about the offering made in the Westpoint case was misleading to potential investors, it does not follow that all issuers fail to make appropriate disclosure in accordance with the corporations law regime.



That being the case, it is our further submission that the current requirements for disclosure about debenture offerings under the corporations law regime are consistent in character with those operating in relation to fund raising by way of share and equity offerings. We base this submission on our view that a more accurate analogy may be drawn between debenture offerings and share and equity offerings rather than, as the Green Paper indicates, between debenture offerings and managed investment schemes.

In our view, debenture offerings under the current corporations law regime carry no greater risk for debentures (when such offerings are properly structured and in relation to which appropriate disclosures are made) than do current share or equity offerings.

## 2. Part B – Current arrangements

In relation to unlisted issues of debentures, we submit that the risks associated with this type of offering are no greater than for those associated with share or equity offerings in privately owned companies in accordance with our view that such offerings of shares and equities in privately owned companies are a better analogy with unlisted debentures than is the potential analogy between investments in managed investment schemes and unlisted debentures on which the conclusions in Section 4 of the Green Paper rely.

The risks that are listed in Part B under the heading 'Unlisted Issues of Debentures' (page 37) can be seen to be comparable with those of offerings by privately owned companies, being that investors do not have the benefit of the market to provide:

- *a readily available value for the debenture;*
- *public scrutiny of the ongoing performance of the issuer either through market forces or via listing rules, as would be the case if the issue were in the public domain; and*
- *an easy market for the sale of their interests, particularly where the investor may have lost confidence in their investment.*

Further, the potential risk to investors that funds raised through unlisted debenture offerings may be on-lent is raised. Again, further supporting our preferred analogy between unlisted debentures and private share or equity offerings, funds raised through share or equity offerings in privately owned companies may similarly be on-lent.

## 3. Part C – Current issues

While we agree with the contention outlined in subsection (i) of Part C, 'Systemic risks with collapses in this sector', that collapses in the financial market do have serious consequences including a loss of investor consequences, we note that these consequences arise from a collapse of any sector of the securities markets and so are not an especially compelling or cogent argument as to the necessity of the proposed reforms outlined in Part D of Section 4 of the Green Paper. Equally, as recent financial history has shown, collapses occur even in areas of the financial markets that might be regarded as more extensively regulated. Such cases suggest that while regulation is an essential to the fair and effective operation of public offerings, it is not a guarantee against the collapse by any particular business offering investments to the investor markets.

Further, we note that the Green Paper does not suggest that the increased regulation that would result from the reforms suggested in Part D of Section 4 of the Green Paper would enable any entity to guarantee any degree of safety with regard to an investment – be it governmental by way of (for example) the operation of the Corporations Act, by ASIC through its powers of scrutiny and enforcement of regulations or by any entity complying with such regulations – nor does the Green Paper suggest that it would be fair to require any such guarantee from any such entity. The premise underlying the suggested reforms is that, given that regulation exists to manage the risk of investing in offerings (of any kind) to the public, there is a corollary between increased risk and the more effective or fairer operation of the investments in the marketplace. However, we submit that this relationship between regulation and risk does not operate as a non-ending continuum, so that the greater the regulation, the more minimal the risk, nor does such a principle inform the operation of the financial markets – indeed, one of the fundamental principles underlying our economic system is that 'over-regulation' may be an inhibiting cause to the effective and fair operation of markets. One of the consequences is that it may generally have an anti-competitive effect, in that certain providers of investment offerings will be removed from the marketplace with the further consequence of limiting choice for consumers, and consequently their participation in investment markets.

#### 4. Part D – Reform

##### *Subsection i – Proposed changes*

It is our submission that the proposed changes set out in subsection (i) of Part D, 'Reform', are both unnecessary and inappropriate given our view that, contrary to analogy drawn between debentures and managed investment schemes in the Green Paper, the more realistic context of debenture offerings is analogous with share and equity offerings by unlisted companies.

Taking the proposed reforms in turn:

- *Harmonisation of regulation of promissory notes*

We note that increasing the regulation of promissory notes regardless of their value is inconsistent with the rest of the corporations law regime which invariably makes a distinction between the nature of the offering (including the amount requested by the particular investment offering) and the level of risk; ie, in our view the proposed change is discriminatory without sufficient basis between promissory notes offerings and other types of investment offerings under the Corporations Act. Disclosure and licensing requirements are always matched to the level of risk carried by such investments, one of the key features of risk is the amount required to invest and that key feature is being ignored here;

- *Licensing of debenture issuers*

It is in our view inappropriate to extend the licensing requirements for all debenture issuers, given our submission that the appropriate investment analogy in respect of debentures is between debenture issuers and unlisted companies. Obtaining a licence under the Australian Financial Services licensing regime is an onerous task, usually associated with a timeframe of at least three months and a capital cost to implement additional compliance systems. These time delays and monetary costs would be necessarily built into the investment products, making investments less attractive and potentially less valuable to retail investors. Requiring a listed entity to have an Australian Financial Services licence is unnecessary given the extensive

regulation to which a listed entity is already subject. We suggest that it would have the effect of stifling debt capital markets and restrict the proper business funding mechanisms of listed entities; and

- *Licensing of trustees and review of trustee duties*

Our comments in relation to debenture issuers apply to trustee companies. Both suggestions regarding trustee companies would have the effect of significantly increasing their costs and therefore increasing their fees for their services, which increased costs would again in turn be passed on to investors, without in our view either sufficient grounds currently existing for the need for such reforms and insufficient evidence that such extensively increased regulation would in fact assist in achieving the aim of minimising risk to investors. Should this proposed reform be implemented, we suggest that all current forms of state based licensing should be made redundant.

### *Subsection ii – Analysis of proposed changes*

Again, discussing the analysis in subsection ii in respect of each proposed reform:

- *Harmonisation of regulation of promissory notes*

We note in relation to the proposed harmonisation of regulation of promissory notes that the Green Paper notes that the proposed amendment is not expected to effect this market as participants are largely professional investors (page 40). This being the case, the question arises as to why the proposed reform is necessary as professional investors are more sophisticated than retail investors and generally exempt from certain disclosure requirements under the corporation law regime on that basis.

- *Licensing of debenture issuers*

The Green Paper justifies the proposed reform on the basis that 'the licensing requirements for debenture issuers lack consistency, particularly when compared to operators of registered managed investment schemes' (page 40). Managed investment schemes are a very specific investment structure and the extensive duties imposed on responsible entities under Chapter 5C of the Corporations Act reflects the peculiar nature of a managed investment scheme structure and which duties are relevantly not applicable to offerors of debentures or to trustee companies. The suggested analogy in the Green Paper between debenture issuers and trustee companies with that of responsible entities has no realistic basis when looked at the place that these investments occupy in the market place. Investments offered by companies that are unlisted carry similar risks to debenture offerings and to require debentures offerors to be licensed and not to require unlisted or listed companies to be licensed seems in our view inconsistent and discriminatory.

- *Licensing of trustees and review of trustee duties*

We note that the duties imposed on trustees under Chapter 2L of the Corporations Act are limited. Such duties do not correspond with the duties generally carried by licensee holders under the Australian Financial Services licensing regime nor with the duties prescribed for responsible entities under Chapter 5C. In our view, it would unfairly onerous to expect debenture offerors to be licensed and to maintain

a licensing regime in order to comply with their Chapter 2L duties – indeed, the licensing requirements are not necessary for trustee companies to carry out these debenture duties adequately.

We note that the suggested expanded duties of trustee holders still fall below those of a responsible entity, again indicating that no real analogy can be drawn between debenture offerors and responsible entities offering investment in managed investment schemes. Again, it is our submission that even with the expanded duties suggested by ASIC in its new Regulatory Guide 69, 'Debentures – improving disclosure for retail investors', are still in no way parallel to the duties of a responsible entity under Chapter 5C. Further, it is our submission that the expanded disclosure for retail investors under RG 69 should adequately inform them of the risks carried by investing in debentures.

We would be happy to discuss any matter raised in this submission and review any further discussion papers or draft legislation. If you have any queries, please contact Bart Oude-Vrielink or Tony Dhar.

Yours faithfully

**MINTER ELLISON**



Contact: Bart Oude-Vrielink Direct phone: +61 3 8608 2942  
Email: bart.oude-vrielink@minterellison.com

Contact: Tony Dhar Direct phone: +61 3 8608 2910  
Email: tony.dhar@minterellison.com