



SECURITIES INSTITUTE

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Dear Ms Smith

DISCUSSION PAPER: TRANS-TASMAN MUTUAL RECOGNITION OF OFFERS OF SECURITIES AND MANAGED INVESTMENT SCHEME INTERESTS

The Securities Institute of Australia is pleased to provide comments on the joint Australian Department of the Treasury and New Zealand Ministry of Economic Development Discussion Paper *Trans-Tasman Mutual Recognition of Offers of Securities and Managed Investment Scheme Interests*.

The proposed regime for mutual recognition of offers of securities and managed investment scheme interests will allow issuers to offer securities in both Australia and New Zealand using the same regulated offer document produced in the home jurisdiction. The aim is to remove unnecessary regulatory barriers to trans-Tasman securities offerings.

The Institute believes that this initiative will support greater investment between Australia and New Zealand, enhance competition in our capital markets and reduce compliance costs for business. Through greater co-operation, co-ordination and integration the proposed regime offers an opportunity for Australia and New Zealand to consider how both countries can strengthen investor confidence, encourage economic efficiencies and promote regional market integrity by building on the dynamic nature of our capital markets.

The Institute supports the general concept of mutual recognition. However, vital to the success of the proposed mutual recognition regime is ensuring the high-level principles are adequately reflected in the practical application of the framework through the inter-governmental agreement, legislation and memorandum of understanding between the securities regulators.

We endorse initiatives that provide an effective mechanism for promoting improved capital raising opportunities for issuers as well as encouraging increased investment choice for consumers. However, we believe that as a strategy to benefit Australia in the global marketplace it is equally important to improve market efficiencies, remove unnecessary legal and regulatory barriers, promote greater activity in the market for corporate control and reduce the cost of raising capital domestically.

If you have any queries about the comments in our submission, please contact me on (02) 8248 7651 or the Institute's Senior Manager, Policy & Government Relations, Diane Tate on (02) 8248 7556 or via email d.tate@securities.edu.au.

Yours sincerely

Brian Salter ASIA
Chief Executive Officer

General observations

By building on the commitment between the Australian and New Zealand Governments (made in the Australia-New Zealand Closer Economic Relations (CER) Trade Agreement), the objective of the trans-Tasman reform is to “deepen the trans-Tasman relationship within a global market, through increased co-ordination of business law, thereby creating a mutually beneficial trans-Tasman commercial environment”¹.

The proposed mutual recognition regime aims to benefit businesses and individuals by removing barriers to greater integration of trans-Tasman commercial activity. The mutual recognition regime will advance the broader goal of achieving a single market for goods, services and capital. The Institute supports the concept of mutual recognition, as it will allow entities in each jurisdiction to operate with the benefit of complying with a single regulatory framework.

The main advantage of the mutual recognition regime for issuers is the reduction in the cost of raising capital. This cost efficiency is generated by removing the need for issuers in Australia and New Zealand to produce multiple disclosure documents and meet different regulatory requirements in order to offer securities in each respective country.

At present Australian and New Zealand issuers cannot use the disclosure document produced in their home jurisdiction when making a trans-Tasman offer of securities (shares, debentures, participatory securities, options to acquire securities) or managed investment scheme interests. That is, unless the offer is being conducted under an exemption, the issuer must also comply with the fundraising requirements in the host jurisdiction.

Importantly the proposal for integrating the fundraising requirements for Australian and New Zealand issuers will overcome inconsistent requirements between respective regulatory frameworks, which pursue the same policy objectives but perhaps in different ways. The significance of developing a mutual recognition approach is to adopt a regime that acknowledges the importance of the underlying policy goals of market integrity and consumer protection.

One of the key risks to the proposal is ensuring the legislative framework in each country supports the mutual recognition approach. Unlike harmonisation in Europe, where there are EU Directives and a platform seeking common legal and regulatory provisions, the mutual recognition regime proposed in the discussion paper attempts to align regulation but maintain separate legal authority. Therefore, unlike a “harmonisation” approach, the risk with an “integration” or co-ordination approach is that laws change in one country and create a conflict with the legal and regulatory framework in the other country.

However, as set out in the MOU, “co-ordination is multi-faceted and does not necessarily mean the adoption of identical laws, but rather finding a way to deal with any differences so they do not create barriers to trade and investment. In working towards greater co-ordination, the efforts of both Governments will focus on reducing transaction costs, lessening compliance costs and uncertainty, and increasing competition”.

Specific comments

What costs do the current requirements for trans-Tasman offers of securities impose on Australian and New Zealand issuers?

Pursuant to Chapter 6D of the *Corporations Act 2001*, an offer of securities in Australia is to be accompanied by the relevant disclosure document². An offer relating to the issue of other classes of financial products (including managed investment scheme interests) is made under Part 7.9 of the *Corporations Act* and is generally accompanied by a Product Disclosure Statement (PDS). The Australian Securities and Investments Commission (ASIC) has the power to exempt a person from any of the fundraising provisions of Chapter 6D and Part 7.9.

Pursuant to the *Securities Act 1978*, a security cannot be offered to the public in New Zealand unless accompanied by a registered prospectus and an investment statement relating to the security. The New Zealand Securities Commission can issue an exemption notice under the *Securities Act*.

¹ The Memorandum of Understanding Between the Government of Australia and the Government of New Zealand on Coordination of Business Law signed on 31 August 2000 replaces the Memorandum of Understanding Between the Government of Australia and the Government of New Zealand on Harmonisation of Business Law signed on 1 July 1988.

² Section 708 sets out offers that do not need disclosure, including small-scale offerings, offers to sophisticated or professional investors, etc. The type of disclosure document is dependent on the nature of the offer e.g. Prospectus, Short Form Prospectus, Profile Statement, Offer Information Statement.

The effect of the current capital raising regime as under the Corporations Act (Australia) and Securities Act (New Zealand) is that an entity seeking to raise capital in both countries will need to comply with the specific regulatory framework of each jurisdiction. That is, without an exemption, Australian and New Zealand issuers cannot use their home jurisdiction disclosure document and must meet the relevant requirements when making a trans-Tasman offer of securities or interests in a managed investment scheme into the host jurisdiction.

Usually an entity in Australia will structure an offshore offering from Australia. That means that associated services (e.g. legal fees, corporate advisory services, underwriting arrangements, producing and disseminating disclosure documents, etc) are undertaken in Australia. Therefore, as there is a requirement to meet the regulatory framework in each jurisdiction, the compliance costs associated with making an offshore offer is a substantial factor for consideration within the structure of the offer. In some cases it is determined not to extend the offer from the home to the other jurisdiction. This impediment means that issuers are not able to access a larger investor base and investors do not have access to investment choice.

The cost of raising capital is dependent on a number of factors specific to the offer (e.g. complexity, conditions, etc). However, anecdotal evidence suggests that transaction costs, largely due to compliance costs, can place limitations on trans-Tasman offerings. Therefore, we believe the mutual recognition regime has the potential to significantly impact on the structure of offers to Australian and New Zealand investors, as offers become more transportable cross-border. The proposed regime will reduce the costs for issuers seeking to make an offer of securities or managed investment scheme interests in both countries.

The reduction in the cost of raising capital for issuers will be both due to the removal of the need to facilitate the offer by complying with the specific legal and regulatory requirements of the home country and host country and due to gaining access to a greater investor base and improving the certainty for the fundraising outcome.

Furthermore, all things being equal, the need for dual-listing between the markets will not be necessary under the mutual recognition regime, as the ability to access both home and host investor bases will provide the benefits of dual listing without the cost of listing on each exchange.

Should Australia and New Zealand put in place a mutual recognition regime for offers of securities and interests in managed investment schemes broadly along the lines described in this paper?

The Institute considers that it is appropriate for the mutual recognition regime to allow issuers making trans-Tasman offers to be able to use the regulated disclosure document of their home jurisdiction also in the host jurisdiction.

The primary feature of the proposed mutual recognition regime is the ability to comply with the legal requirements of making an offer of securities or managed investment scheme interests in one jurisdiction by meeting the requirements of the corresponding laws of another jurisdiction.

Therefore, the main objective of the mutual recognition regime is to remove unnecessary regulatory barriers to trans-Tasman offers of securities and managed investment scheme interests, thereby facilitating greater investment and commercial activities, enhancing competition in capital markets, reducing costs for business and increasing investment choice for consumers.

The approach to securities regulation in Australia and New Zealand is essentially based on "regulation of conduct" and is administered through the disclosure of information (including risks) about financial and investment products. Therefore, it is reasonable that a mutual recognition regime commence with the acknowledgement of the disclosure standards as adopted in each country. While the form of the disclosure may be different, the policy goals are commensurate.

The Institute believes that the mutual recognition regime would provide a number of benefits for issuers and consumers in both countries.

The benefits associated with the mutual recognition regime for issuers include:

- Reduced costs of compliance and lower cost of raising capital
- Removal of unnecessary regulatory barriers
- Greater investor base access

The benefits associated with the mutual recognition regime for consumers include:

- Increased range of investment choices
- Greater opportunity to diversify investments

Both issuers and consumers will benefit from the efficiencies gained from transparency of costs and greater competition in the capital markets.

Will the proposed mutual recognition arrangement positively impact on the financial services industry and wider economy in Australia?

Globalisation is driving greater connectivity between marketplaces. As identified above, pursuing policies that facilitate increased integration can provide benefits for both issuers and consumers. However, it is vital that high standards of market integrity and investor protection remain key characteristics of any changes to the legal and regulatory framework for our capital markets.

Greater integration between Australia and New Zealand's capital markets will provide cost efficiencies for fundraising activities associated with multiple market participation. Streamlined processes, coupled with reduced transaction costs is likely to lead to increased activity with a flow-on effect to other financial markets (e.g. foreign exchange, derivatives, etc).

Enhanced activity in our capital markets can provide increased benefits to Australia's financial services industry and wider economy through improved allocation of capital. In doing so, the benefits of integration can assist in promoting Australia's market as a financial centre for the Asia-Pacific region.

Alternatively, the changed fundraising regime may have unintended consequences for the structure of offerings in Australia and New Zealand. It is important to ensure that the practical differences between the legal and regulatory frameworks (i.e. disclosure requirements for forecasts and accounting standards) do not artificially generate offers to be structured in particular ways. The mutual recognition regime will allow entities to access investors in both countries. Therefore, this may impact on an entity's decision on where to locate (including the exchange a listed entity seeks a listing), how to structure the offer, and so on.

Are there any features of the proposal set out in this paper which you see as particularly important in order to ensure that the regime achieves the objectives of facilitating investment between the two countries, enhancing competition in capital markets, reducing compliance costs for business, and increasing choice for investors?

The Institute believes that it is important to ensure that high standards of market integrity and investor protection are not compromised by the adoption of the mutual recognition regime. Therefore, we believe that it is appropriate for the regime to be implemented based on an issuer meeting initial requirements and complying with ongoing requirements.

The proposed regime outlines a fundraising process where a regulated offer in one country can be lawfully made in the other country. The basis for the regime is that an issuer must: (1) meet the entry requirements and (2) comply with the ongoing requirements. Where an issuer cannot satisfy the initial and ongoing requirements, it is appropriate that the offer takes place outside the mutual recognition regime and be treated as an ordinary domestic offer.

We consider that the mutual recognition regime should only apply to offers of securities or managed investment scheme interests that are regulated under the securities laws of both Australia and New Zealand and where a regulated offer document is required in both countries.

The Institute recognises that the proposed mutual recognition regime adopts an alternative framework to either incorporation of foreign law or disapplication of domestic law. We consider that a model that applied foreign law would generate legal confusion and potentially be unconstitutional. Similarly, regulating the offer solely by the law of the home jurisdiction would compromise the ability for the regulator of the host jurisdiction to apply its supervisory and enforcement powers. Therefore, the Institute supports the proposed model as an appropriate framework to implement the mutual recognition arrangement with certainty.

However, it is vital that the mutual recognition regime balance certainty and flexibility. To ensure the cost efficiencies for offerings conducted under the mutual recognition regime are not negated, the regime should encompass the activities already inherent with making an offer. In the case where the framework obstructs or impedes the fundraising process, or where costs associated with the meeting and complying with the initial and ongoing requirements outweigh conducting an offer outside the mutual recognition regime, then there would not be the same motivation for continuing with the mutual recognition arrangement.

In terms of initial requirements, we consider it is appropriate that the offer be subject to the home jurisdiction's regulatory framework and it is practical to apply criteria as prescribed by the host jurisdiction. We also consider that it is reasonable to ensure that an issuer must opt into the mutual recognition regime with regards to a particular offer by filing a notice with the host jurisdiction (containing the prescribed information).

In terms of ongoing requirements, it is practical to apply the fundraising laws of the home jurisdiction as well as ensuring compliance with certain ongoing criteria as specified in the legislation of the host jurisdiction. This means that the regulator of the home jurisdiction regulator will have the primary responsibility of supervising cross-border offers (by ensuring substantive requirements with the securities law) and the host jurisdiction regulator will be responsible for compliance with ongoing requirements.

The proposed regime is intended to apply only to issuers of securities or managed investment scheme interests, and not to other parties (e.g. persons who provide financial advice or those who deal). We acknowledge that the Australian and New Zealand legal requirements in respect of the provision of financial advice or dealing are not sufficiently similar to allow mutual recognition in this regard. The Institute believes that this is appropriate to ensure the integrity of the financial services licensing regime.

Are there any features of the proposal that you see as inappropriate or undesirable, and that you consider should be changed? How should they be changed?

It is vital that the scope of the proposed mutual recognition regime is clear. This includes how home and host jurisdiction law applies to offerings and how each jurisdiction's securities regulator will administer the law with little or no overlap. We envisage that the inter-government agreement will set out the scope of the mutual recognition regime and will be implemented through appropriate amendment to domestic laws. It is essential that issuers can participate with confidence.

Furthermore, the Institute recommends that the framework include a review of the application of the mutual recognition regime after a reasonable period. Such a review would aim to assess operability of the mutual recognition regime and to ensure market integrity and investor protection standards. In the instance where the mutual recognition regime compromised standards within our marketplace (and thereby did not provide the benefits identified for issuers or consumers), it would be appropriate to terminate the arrangement. In the circumstance where the framework was found to be deficient, it would be appropriate to revise the detail of its application to ensure it delivers against the high-level principle objectives.

Are the proposed exemptions from the standard domestic requirements of each country's fundraising laws for offers made under the mutual recognition regime appropriate? Should additional requirements be excluded? Should any of these requirements continue to apply to offers under the mutual recognition regime?

The proposed mutual recognition arrangement aims to facilitate trans-Tasman offerings by reducing regulatory barriers. The Institute considers that it is reasonable and practical to adopt a framework that eliminates the need to produce multiple disclosure documents, where the offer (and disclosure document) is regulated. The principle of the mutual recognition approach is to acknowledge the fundraising regulatory framework of the home jurisdiction as an appropriate standard for the specific activity, in this case offering securities and managed investment scheme interests.

Currently an Australian issuer making an offer in New Zealand (and a New Zealand issuer making an offer in Australia) can do so by seeking an exemption from the respective securities regulator. This mutual recognition regime would implement an approach that instead of being case-by-case would allow for a broader application of relief from the fundraising laws of the respective country, where certain requirements are satisfied. We consider this to be an appropriate regulatory approach for offers of securities and managed investment scheme interests.

However, it is essential that the primary policy objectives continue to be monitored to ensure that standards of market integrity and investor protection are not compromised. For example, would the application of the mutual recognition model compromise the standard of offer documents and thus the level of disclosure for investors? Would the mutual recognition arrangement generate unreasonable costs for issuers? A review of the mutual recognition regime would ensure formal consideration of these policy objectives.

The proposed mutual recognition regime is a step to further co-ordinate business law between Australia and New Zealand. The potential risk with an integration approach is that the laws of one country will change and affect the application of equivalence of the regulatory regimes. This could give rise to concerns regarding the continuance of the mutual recognition regime.

The discussion paper indicates that an inter-governmental agreement would require each jurisdiction to give the other jurisdiction advance notice of any proposed legislative changes that have implications for the mutual recognition regime; provide for consultation where a proposed change in one jurisdiction gives rise to concerns in the other about the operation of the regime; and, enable either country to terminate the mutual recognition arrangement, in the unlikely event that serious concerns arise and cannot be resolved. The Institute recognises that the inter-governmental agreement is fundamental to the success of the mutual recognition arrangement.

In addition to ensuring ongoing legality of the mutual recognition regime, it is important that the proposed regime provides adequate statutory protections for investors and ensures that investors can pursue statutory remedies in both the courts of the home and host jurisdiction, as appropriate.

It is essential that where a breach of the offence provisions occurs, that there is legal certainty for both issuers and investors regarding jurisdiction for pursuit of offences as well as legal certainty regarding statutory interpretation of the law of contract, law of tort and other laws (e.g. misleading and deceptive conduct). Maintaining adequate protections highlights the importance of ensuring modifications to offering requirements and fundraising law is effectively legislated. It is essential that investors can participate with confidence.

Is it appropriate to provide for special arrangements for enforcement of civil and/or criminal penalties for breach of the host jurisdiction's ongoing requirements?

As identified above, it is vital that there is certainty regarding the responsibilities of each securities regulator, the application of securities law and how breaches will be treated under the trans-Tasman arrangement. The Institute recognises the co-regulatory role of the securities regulators as fundamental to the success of the mutual recognition arrangement.

The discussion paper outlines that a failure to comply with the ongoing requirements would result in a breach of the host jurisdiction's laws (with the consequences of non-compliance specified in the legislation of the host jurisdiction)³. In addition, the discussion paper outlines that a breach of the home jurisdiction's securities laws in connection with an offer made to an investor in the host jurisdiction under the mutual recognition regime would also expose the issuer to criminal sanctions, civil action or other enforcement action in the home jurisdiction in the same manner as if the breach had occurred in the home jurisdiction.

It is envisaged that the host jurisdiction regulator would have primary responsibility for taking action against issuers for failure to comply with the ongoing requirements (other than the home jurisdiction initial compliance requirement) and that the home jurisdiction regulator would have primary responsibility for supervising a cross-border offer and taking action in respect of breaches of the substantive requirements of the home jurisdiction securities laws.

The complex nexus between application of securities law, potential breaches of law and enforcement actions of securities regulators highlights the potentially complicated structure for administering the mutual recognition regime. It is imperative that cross-jurisdictional arrangements are legislated and that there is co-ordination and co-operation between the securities regulators. To ensure the success of the mutual recognition regime it is essential that Australia and New Zealand work together to establish the framework through drafting the inter-governmental agreement and the necessary legislative provisions.

The discussion paper sets out that the agreement will encourage regulators to enter into understandings with regard to communication and the co-ordination of enforcement activity. The Institute believes that the Australian Securities and Investments Commission (ASIC) and the New Zealand Securities Commission must implement formal arrangements through a Memorandum of Understanding (MOU). It is vital that issuers and investors are confident in relation to their participation in an offer made under the mutual recognition regime. Otherwise there is the potential to expose issuers and investors to unintended consequences or impose unnecessary costs.

Trans-Tasman enforcement of fines and penalties?

The discussion paper proposes that the mutual recognition regime could facilitate trans-Tasman enforcement of fines and penalties by providing a mechanism for enforcing in the home jurisdiction fines or penalties relating to breaches of the mutual recognition regime requirements imposed by the courts of the host jurisdiction. Generally, the application of this mechanism would need to be limited to the particular offer under the mutual recognition agreement and align the fundraising regulatory treatment that would be applicable with an ordinary domestic offer.

In assessing the merit of introducing a trans-Tasman mechanism for fines and penalties, we suggest that practical issues such as information sharing processes, cross-jurisdictional investigations and extra-territorial powers, would also need to be considered.

Are there any other aspects of this proposal on which you wish to comment?

The proposed mutual recognition regime represents a change in the regulatory approach to securities law. In the past, "mutual recognition" has generally tended to focus on the application level, rather than on an underlying policy objectives level. The Institute believes that this shift towards market integration will provide significant benefits for Australian issuers and investors.

³ The consequences of non-compliance would include criminal sanctions, civil liabilities and/or administrative penalties (e.g. stop orders issued by the host jurisdiction regulator).

However, the Institute believes that integration is not the only approach that will enhance activity in our capital market. We consider that it is also important to improve market efficiencies, remove unnecessary legal and regulatory barriers, promote greater activity in the market for corporate control and reduce the cost of raising capital domestically. This strategy will also benefit issuers and investors and enhance Australia's position in the global marketplace. It is vital that Australia maintain a strong, dynamic and growing economy.