

---

1 December 2008

## **CAPITAL MARKET DEVELOPMENT TASKFORCE RELEASES ITS INTERIM RESPONSE TO THE FINANCIAL CRISIS**

The Capital Market Development Taskforce interim report released on Friday contains a package of proposals designed to boost access to capital for New Zealand businesses and reduce the cost of raising capital.

While the taskforce is not due to report its findings until September next year, it decided to produce an interim report in response to the financial crisis, with taskforce chairman Rob Cameron noting that, in the current environment, access to capital will be a key issue in determining business survival. While there are a wide range of interventions that governments can take and are taking to reduce the impact of the crisis, capital markets are an important piece of the picture, he said.

The CMD Taskforce's proposals include recommendations for changes to the NZX Listing Rules, developed with the NZX. They feature in a separate consultation paper released by the NZX last week.

The recommendations concentrate on easing barriers to raising capital without undermining investor protection. A number will require changes to legislation. The taskforce has separated its recommendations into those it considers can be implemented quickly and others which it acknowledges may require further work (but which it suggests should be progressed urgently).

In making recommendations, the taskforce noted that it had reference to two broad principles:

- (a) That relevant information about public issuers which are already subject to (and comply with) continuous disclosure obligations will be known to the market. As a result, much prospectus-level disclosure is costly duplication and a simpler offer document could be used which contains relevant information without undermining investor protection. This is in keeping with practice in Australia.
- (b) A number of the existing exemptions enabling public issuers to issue securities without offer documents can be simplified and clarified.

The interim report also identifies a number of additional changes which the CMD Taskforce considers has merit but require further consideration.

The CMD Taskforce has summarised its recommendations for urgent change in the table set out below:

<b>Recommendations for urgent change</b>			
<b>Proposal</b>	<b>Reduces cost and time with capital issuance</b>	<b>Potential impacts on investors</b>	<b>Other impacts</b>
Ease requirements for listed debt issues	✓	Minimal	
Raise threshold for subsequent equity issues by listed companies before prospectus disclosure and shareholder approval is required	✓	Minimal	
Reduce timeframes for rights issues	✓	Minimal	
Increase the amount of capital that can be raised in secondary offerings without shareholder approval	✓	Minimal	
Allow remuneration of employees and directors by stock		Positive	Helps cash flow
Making exemption for non-public issue offers more practical	✓		Reduces risk for issuers
Amend Securities Act to allow persons who have invested \$500,000 to make incremental investments without a prospectus or investment statement	✓		
Amend the wording of financial assets test in “eligible persons” exception to cover trusts	✓		
New power for the Securities Commission to issue “no action” letters	✓		
Focus prospectus disclosure on meaningful items	✓	Minimal	
Streamlining Overseas Investment Commission consent	✓		

## Urgently recommended changes for listed companies

The interim report discusses briefly each of the recommended changes. These are summarised as follows:

1. **Ease requirements for listed debt issues.** The taskforce notes the restrictions on normal debt funding from banks and suggests it is critical to allow debt issues to proceed as rapidly as possible with minimum compliance costs. Therefore, instead of an investment statement and prospectus, listed issuers should only be required to produce the following for (listed) debt issues:

- (a) a simple term sheet offering document listing the terms of the debt issue;
- (b) a warranty from a CEO, CFO and Board of Directors that the issuer has complied with its continuous disclosure obligations under the NZX Listing Rules – including that that they have no knowledge of any information which, if disclosed, would be relevant to an assessment of the offer (and any new material developments during the offer period would be disclosed to the NZX).

This is similar to the NZX recommendations made last week.

2. **Raise threshold for subsequent equity issues.** The taskforce recommends the raising of the threshold for shareholder approval and disclosure documents for subsequent equity issues to existing shareholders from NZ\$5,000 to NZ\$25,000. As an alternative, the taskforce suggests that the requirement for listed issuers to prepare a prospectus before issuing equity to existing shareholders be removed entirely because the issuer is already subject to continuous disclosure.

3. **Reduce timeframes for rights issues.** This recommendation is similar to the proposals made by the NZX last week – the taskforce recommends reducing the timeframe for approval of offering documents and the period that a rights issue must remain open for acceptance.

4. **Increase the amount of capital that can be raised in secondary offerings without shareholding approval.** Again this recommendation is similar to the NZX recommendations last week. The taskforce recommends increasing the threshold for secondary offerings without shareholder approval from 15% of market capitalisation per year to 20%.

5. **Allow remuneration of employees and directors by stock.** The taskforce recommends allowing greater flexibility for remuneration of employees and directors by stock, helping align management and shareholder interests and providing flexibility for businesses which are cash constrained. The recommendation would allow listed issuers to pay in stock at levels approved by shareholders at an annual meeting.

6. **Making the exemptions for non-public offers more practical.** The taskforce recommends the removal of the current restriction preventing an issuer making an offer at the same time to persons who are deemed not to be members of the public in terms of section 3(2) of the Securities Act and “eligible persons” under section 5(2CB) of the Securities Act.

7. **Facilitate incremental investments.** The taskforce recommends the amendment of section 3(2)(a)(iia) of the Securities Act to allow subsequent incremental offers to persons who have invested at least \$500,000 - without a prospectus or investment statement.
8. **Amendment of the “eligible persons” exception to cover trusts.** The taskforce recommends amending section 5(2CB) of the Securities Act to make it clear that “eligible persons” includes a trust. A similar concession is permitted in Australia. In addition, in keeping with Australian legislation, it is recommended that the certification regime required under the “eligible persons” provisions apply for 12 months (rather than 6) limiting the number of times that such certificates need to be refreshed.
9. **Enable the Securities Commission to issue “no action letters”.** The taskforce notes that it has received market feedback that the inability of the Commission to issue no action letters has stifled the introduction of new products.
10. **Focus on meaningful disclosure.** The taskforce recommends a number of simple changes to the Securities Regulations to reduce the cost to issuers without reducing investor protections:
  - (a) amending the restrictions in Regulation 12 limiting references to more up-to-date financial information – which is problematic for an issuer whose business is deteriorating;
  - (b) removing the limits in Regulation 15 on providing prospective financial information other than by means of a prospectus; and
  - (c) fast-tracking the Securities Commission’s current review of required changes to the Securities Regulations to reduce compliance costs.
11. **Streamlining OIO consent.** The taskforce notes that virtually every law firm, adviser and business person who has provided feedback has recommended the OIO regime be reviewed and simplified because of the additional costs and delays being incurred. The taskforce notes that, given that the overwhelming majority of transactions are approved, these delays provide little or no benefit to New Zealand. While suggesting that the regime needs a fundamental review, the taskforce asks the relevant Ministers to speed up the process to facilitate transactions where there are no sensitive issues.

## Changes requiring further consideration

There are a number of changes the taskforce recommends for further analysis and urgent consideration. Briefly these are:

1. **Eliminate the overuse of appraisal reports** which the Taskforce sees as often adding costs but not additional investor protection in circumstances where boards should make their own decision.
2. **Increase the thresholds applicable to related party transactions** because of concern that a threshold of 5% of Average Market Capitalisation is a burden for smaller-cap companies.

3. **Considering a new “registered investors” exception to the non-public offers provisions in the Securities Act** allowing (with certain safeguards) persons to become “registered investors” who do not require the protection of the Securities Act disclosure regime.
4. **Consider adding an addition exception equivalent to the Australian 20:12 rule** enabling companies to make offers to up to 20 people in any 12 month period up to a certain threshold (\$A2 million in Australia) without the need for a prospectus.
5. **Amend the Securities Act to define investments in limited partnerships as equity investments** removing the need for a statutory supervisor.
6. **Review the Securities Act and Securities Regulations to make disclosure in prospectus’ more meaningful** removing unnecessary disclosures and costs.
7. **Provide the Securities Commission with a retrospective exemption power** which is particularly relevant in the case of minor/technical breaches.
8. **Amend the provisions in the Financial Reporting Act requiring companies with 25% or more overseas ownership to file financial statements with the Companies Office** to remove a requirement placing such companies at a significant competitive disadvantage.
9. **Tax changes.** The taskforce notes that there are a number of tax issues which it considers require urgent attention. However, it recognises the need for such changes to be considered within the context of overall taxation policy (which will be considered in the taskforce’s final report).

## Viewpoint

The taskforce should be applauded for the speed in which it has come up with a series of recommendations that address a number of impediments to capital-raising, particularly by listed issuers. The measures suggested are practical, conceptually sound and will significantly reduce the barriers to capital raisings by listed issuers.

As well as dealing with the problems that are being evidenced by the severe difficulties many businesses are encountering in seeking to access capital, the interim report also tackles a number of issues that have long been problematic with a Securities Act disclosure regime which has failed to keep up with developments in fund-raising activities. These problems are particularly evident in the case of listed issuers which are subject to continuous disclosure obligations. As a result, many of the recommendations are more in the nature of keeping up with developments in comparable markets rather than radical reforms.

The interim report also, quite rightly, poses the question whether a number of legislative provisions identified as impediments to fund-raising actually provide enhanced investor protection (and therefore whether investors would be disadvantaged by their removal). In our view, the changes suggested will not have this effect.

Finally, the taskforce recommendations appear to leave open a number of wider issues which, we expect, will be addressed in the further analysis that is called for in the interim report. When undertaking that analysis, we

would hope that the CMD Taskforce, the Securities Commission and others not only address the needs of the 'big end of town' represented by listed issuers but also think about SMEs which contribute roughly 40% of New Zealand's GDP and which are also being badly affected by the contraction in the availability of credit.

## Next steps

A number of the CMD Taskforce recommendations will require legislative amendments. Bell Gully understands that the Securities Commission has indicated, informally, that it is generally supportive of a number of the key recommendations and therefore it seems that, with the support of Simon Power the new Minister of Commerce and officials from the Ministry of Economic Development, there could be a groundswell of support to implement the recommendations quickly.

If you would like to discuss any aspect of the CMD Taskforce interim report, please contact one of our team:

### AUCKLAND

**Anna Buchly** 64 9 916 8649 [anna.buchly@bellgully.com](mailto:anna.buchly@bellgully.com)

**David Flacks** 64 9 916 8957 [david.flacks@bellgully.com](mailto:david.flacks@bellgully.com)

**James Gibson** 64 9 916 8692 [james.gibson@bellgully.com](mailto:james.gibson@bellgully.com)

**Brynn Gilbertson** 64 9 916 8948 [brynn.gilbertson@bellgully.com](mailto:brynn.gilbertson@bellgully.com)

**Glenn Joblin** 64 9 916 8955 [glenn.joblin@bellgully.com](mailto:glenn.joblin@bellgully.com)

**Gavin Macdonald** 64 9 916 8938 [gavin.macdonald@bellgully.com](mailto:gavin.macdonald@bellgully.com)

**Haydn Wong** 64 9 916 8918 [haydn.wong@bellgully.com](mailto:haydn.wong@bellgully.com)

### WELLINGTON

**Andrew Brown** 64 4 915 6848 [andrew.brown@bellgully.com](mailto:andrew.brown@bellgully.com)

**Mark Freeman** 64 4 915 6963 [mark.freeman@bellgully.com](mailto:mark.freeman@bellgully.com)

**Chris Gordon** 64 4 915 6836 [chris.gordon@bellgully.com](mailto:chris.gordon@bellgully.com)