NEW ZEALAND BANKERS ASSOCIATION

Submission

to the

NZX

on the

Continuous Disclosure Guidance Note Consultation

16 November 2018

NEW ZEALAND BANKERS ASSOCIATION
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About NZBA

1. NZBA works on behalf of the New Zealand banking industry in conjunction with its member banks. NZBA develops and promotes policy outcomes that contribute to a strong and stable banking system that benefits New Zealanders and the New Zealand economy.

2. The following seventeen registered banks in New Zealand are members of NZBA:

- ANZ Bank New Zealand Limited
- ASB Bank Limited
- Bank of China (NZ) Limited
- Bank of New Zealand
- MUFG Bank, Ltd
- China Construction Bank
- Citibank, N.A.
- The Co-operative Bank Limited
- Heartland Bank Limited
- The Hongkong and Shanghai Banking Corporation Limited
- Industrial and Commercial Bank of China (New Zealand) Limited
- JPMorgan Chase Bank, N.A.
- Kiwibank Limited
- Rabobank New Zealand Limited
- SBS Bank
- TSB Bank Limited
- Westpac New Zealand Limited

Background

3. NZBA welcomes the opportunity to provide feedback to NZX on its draft Continuous Disclosure Guidance Note (*Guidance Note*).

4. If you would like to discuss any aspect of the submission further, please contact:

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Introduction

5. NZBA supports NZX's publication of updated guidance on continuous disclosure, particularly in light of the new "constructive knowledge" test for Material Information. In addition, we also support using this opportunity to modernise the general practical guidance and examples in the guidance. We discuss each of these points below.

6. These submissions focus on significant matters identified in relation to Quoted Debt Securities, in the time available for the consultation. NZBA would be happy to discuss the Guidance Note further after this submission.

7. Capitalised terms that are used but not defined have the same meaning as in the Guidance Note or the Listing Rules (as applicable). Specific Listing Rule references are to those Rules as in effect from 1 January 2019.

Guidance on constructive knowledge test

Scope of test should be further clarified

8. NZBA supports NZX's decision to provide clear guidance on the intended requirements of the constructive knowledge test, particularly the comments in section 4 (page 16) that this test is intended to require issuers to have appropriate policies, procedures, systems and controls in place so that material information is escalated to senior managers efficiently. This conveys the intention that policies etc should be fit for purpose and reasonable.

9. There are several other places in the Guidance Note where the constructive knowledge test is discussed, but the scope of the obligations does not appear to include a reasonableness element, and should be clarified accordingly.

10. The inclusion of "reasonably" in the constructive knowledge test makes it clear that senior management is not deemed to be aware of all material (or potentially) material matters; only where it is reasonable for senior management to be aware of it. The Guidance Note needs to be very clear on the scope of this obligation.

11. In particular:

    (a) In section 3.3:

        (i) The first paragraph (page 11) should be amended to read "*… ~~H~~However, if an issuer requires further information in order to determine whether or not initial information is material information, the ~~additional information~~issuer must ~~be sought~~ take reasonable steps to seek such information as soon as possible*".

        (ii) The second paragraph should be amended to read "*… If an issuer determines (or is reasonably able to determine) that it holds …*"

        (iii) The final paragraph (page 12) should be amended to read "… *Furthermore, the extension of an issuer's awareness to information that a~~n~~ senior manager ought reasonably have come into ~~position~~ possession of will effectively require the issuer, when it is on notice of information that potentially could be material information, to make any further enquiries or obtain any expert advice ~~needed~~ that are reasonable in the circumstances to confirm whether it is material information within a reasonable period*."

    (b) Section 4.1 (page 16) should be amended to read *"….senior managers "ought ~~to have~~ reasonably to have, come into possession of"…"* This would then be consistent with the Listing Rules and section 3.3.

(c) Section 7.2 (page 24) should be amended to read "*… it should be designed to ensure that information which may be material information and which may require disclosure under Listing Rule 3.1 …*"

Guidance on appropriate policies in section 7 should be expanded

12. NZBA notes that section 7 of the Guidance Note sets out a broad description of recommended procedures to enable release of information as soon as the issuer becomes aware of it, with some useful practical guidance.

13. However, it would be helpful if this section was expanded to more explicitly cover the constructive knowledge element of the test as well. For instance, although there is a brief mention of "Enabling identification of price sensitive information in different areas of the business", it would be helpful to:

(a) Amend the opening paragraph to read "*As indicated above, it is recommended that issuers put in place appropriate systems and processes to enable release of material information ~~as soon as~~ promptly and without delay after they become aware of it (or ought reasonably to be aware of it). This will allow issuers to manage continue disclosure obligations. These systems and processes should deal with the following matters …*"

(b) Expanding the first bullet point to read "*Enabling identification of price sensitive information in different areas of the business, including appropriate policies for escalation (as discussed in section 7.2 below)*", and see our comments above in relation to the drafting of section 7.2.

Clarify interaction with FMCA requirements

14. Lastly, it would be helpful to cross-refer in the Guidance Note to the potential liability for non-compliance of Directors under the FMCA, and the due diligence defences available to them.

15. Although NZBA appreciates that the Listing Rules are intended to impose corporate/issuer liability, the design of an appropriate policy will necessarily be influenced by the FMCA defence requirements and the Guidance Note should at least refer to this.

Meaning of Material Information

Reasonable person tests

16. In section 3 (page 7), the "reasonable person" definition provided by NZXR does not appear to have an explicit objective or reasonable element, and just refers to a person who commonly invests in securities. NZBA submits that a specific objective/reasonable reference should be included for clarity, as specific examples of persons who commonly invest may not by definition meet the definition of a "reasonable person".

17. Further, we note that a separate discussion of a person who "commonly invests in securities" is included at the bottom of page 9, and again of a "reasonable person" on page 19. It is not entirely clear from the Guidance Note how these definitions are intended to interact with the "reasonable person" definition on page 7.

Comments on de minimis price movements should be reinserted

18. NZBA notes that the previous comments that price movements of less than 5% are unlikely to be reviewed by NZXR have been removed. The previous guidance was very clear that such a comment was not a safe harbour; however it did provide some useful practical guidance for Issuers when designing their policies and testing them in hindsight. NZBA submits that this guidance should be reinstated (with such qualifications as NZX considers necessary to maintain the fact that this is not a safe harbour).

Particular information

19. On page 9, the Guidance Note refers to material information originating from a third party, and then states that the Issuer must disclose such information promptly and without delay upon becoming aware of it. NZBA submits that the Guidance Note should make it clear that such information only requires disclosure by the Issuer if it is not already generally available to the market (see for instance, the first paragraph of section 6.3 on page 21).

Guidance on Third Party disclosures should be clarified

20. NZBA notes that section 6.3 of the Guidance Note sets out guidance on third party disclosures.

21. However, if would be helpful if it could be clarified that the references to releasing third party information that is not "generally available" is not intended to capture general analyst reports (and similar material) which might be sent to:

    (a) subscribers behind a paywall; or

    (b) a specific subscriber list for free.

    The current drafting could be read as implying NZX expects material of this nature to be released through MAP.

22. Guidance on how the constructive knowledge test for senior manager applies in this scenario would also be useful. For example, what expectation does NZX have in relation to monitoring of analyst reporting by senior managers?

Materiality examples

The list of debt Material Information examples should be revised

23. NZBA agrees with the general description of material information in the context of debt securities, as set out in the introductory paragraph of the "Debt Securities" section on page 10.

24. However, NZBA notes that several additional examples of information that is potentially material to debt securities have been added to section 3.2 (pages 10 to 11). We submit that the final four examples are highly likely to add further confusion to the market, as they are likely to be material only in specific, limited scenarios, rather than by their nature. NZBA does not consider that these examples meet the description of material information set out in the introductory paragraph.

(a) *New bond issues*: To the extent relevant in practice, this is already covered by the first example in the list (material changes in the overall level and nature of debt being serviced). The fact that a new bond issue is planned should not, without other factors, be expected to influence the price of existing Quoted Financial Products, and ordinary course announcement is separately addressed in Rule 3.13.1. If NZX has a specific matter in mind (for instance, a 'tap' of existing Quoted Debt Securities increasing liquidity in those Quoted Debt Securities) then it should specify this; otherwise we submit that the example should be removed.

(b) *Margin announcements*: Assuming this is referring to an issue margin, such information is largely relevant to the new bonds to be issued only (which will not at that time be Quoted or trading). In addition, pricing typically occurs within narrow indicative guidelines published at launch of the offer, which further reduces the possibility that final pricing information would be material to investors in existing Quoted Financial Products. If this example is referring to a rate reset after the relevant bonds have been Quoted, or to margin announcements outside of the indicated range (which may be an indication of a change in availability of funding sources – a matter which is the subject of a different example in the list) then this should be clarified.

(c) *Interest rates on bonds*: Similar to the above comments on margin announcements, it is not clear why setting the interest rate on a new bond offer is expected to be material to existing Quoted Financial Products. We submit that it would be material only in very unusual circumstances, and is therefore not a good example of information that may be material for Quoted Debt Securities.

(d) *Oversubscription percentage*: We note that the Listing Rules have been amended to specifically make disclosure of oversubscription at the discretion of issuers (Rule 3.17.3). The inclusion of this matter in the list of examples seems to imply that issuers will need to disclose this information regardless. NZBA submits that this example should be removed – to the extent it may be relevant to existing Quoted Financial Products (for instance, because of a change in availability of funding sources) it is already covered by other clearer examples, and the number of bonds to be issued (which, conceivably, may eventually be relevant to liquidity of those bonds on issue) will be known to the market through the general announcement requirements in Rule 3.13.1.

25. As described above, although these matters may be material to the relevant new bonds to be issued, the Guidance Note should be clear that Material Information disclosure requirements apply to Financial Products that are Quoted at the time. These examples currently confuse this point, and should be removed. Further, encouraging issuers to flag new bond offers as material in relation to existing Quoted Financial Products on NZX (without an actual assessment of materiality) could also create confusion in the New Zealand market and overseas, particularly for issuers have also have securities listed on other exchanges with similar obligations to disclose material information (but where such information would not be expected to be flagged as material).

The list of equity Material Information examples should be revised

26. Although this submission focuses on Debt Securities, we also make the following submissions in relation to the examples of potentially Material Information for Equity Securities (section 3.1, page 6):

    (a) The "appointment of a receiver, manager, [or] liquidator in respect of any loan, trade credit, trade debt, borrowing or securities held by the Issuer or any of its Subsidiaries" is relatively unclear. It appears to be focused on assets of the Issuer becoming impaired (i.e. bonds etc held by the Issuer) rather than the Issuer's assets being the subject of receivership. Assuming this is the intended meaning, a specific materiality threshold should be included. For banks, some impaired loans are to be expected in the ordinary course of business. Only very large impairments may be expected to be material.

    (b) It would be helpful to provide further guidance on the reference to "any proposed change in the general nature of the business of an Issuer or its group", and the materiality of changes that this is intended to cover. For instance, it should be clear that an additional product or business line would not generally be considered a change in the general nature of the Issuer's business.

Other submissions

27. NZBA also makes the following additional technical and drafting submissions:

    (a) There are several remaining references to "immediate" or "as soon as possible". These should be amended to consistently refer to "promptly and without delay".

    (b) In section 2 (page 5):

        (i) The Guidance Note states that "All issuers must comply with the continuous disclosure rules, except for Foreign Exempt issuers". Issuers on the wholesale debt market should also be excluded here.

        (ii) The Guidance Note sets out five key elements in bullet points. The first step (currently the second) should logically be that the issuer must be "aware" of the information. Only then can the issuer assess whether the information is Material Information.

    (c) In the second last sentence on page 9 there is a minor typo, "colation" should be "collation".

    (d) In footnote 5 (page 13) there is a reference to paragraph 3.9 which has been deleted. NZX should clarify where issuers, including those who do not publish their own forecasts and are not subject to third party forecasts or estimates, should refer to.

    (e) At the end of section 6.2 (page 21), the final paragraph is unclear as to how it is intended to apply as an exception. The previous paragraph refers to the fact that, outside of trading hours, Material Information can be submitted to

NZX at any time prior to 8:30am on the next trading day. If the Issuer is listed on another exchange, the guidance implies that the Issuer must instead provide the information to NZX "immediately" – e.g. at 9:30pm – even though the information will still not be released on NZX until 8:30am the following morning. It is not clear why a distinction should be drawn here, and NZBA submits that the treatment should be the same regardless of whether there is a second listing venue.

(f) In section 9.3 (page 27), the word "full" should be removed from the suggested response in point 1, so that the issuer confirms it is "in compliance with its continuous disclosure obligations". Although the meaning is the same, it is not entirely clear what inclusion of the word "full" is intended to add.

(g) In section 12 (page 31), NZBA submits that a price enquiry should only be released to the market where NZX considers it necessary or relevant to do so. If a price enquiry is made and the Issuer provides a reasonable explanation, or it is otherwise determined that no breach occurred, it is unclear why NZX would always feel it necessary to release such information to the market.

(h) In Appendix 2 (page 34), the "awareness" step and "generally available" step in the continuous disclosure process appear to have been omitted.

(i) In Example 2 on page 36, it should be clarified that non-disclosure is relying primarily on negotiations being incomplete (and not solely on the fact that a reasonable person would be unlikely to expect disclosure). As NZX notes elsewhere in the Guidance Note, this "reasonable person" element is very narrow in practice, and focusing on it in the response to Example 2 (without mentioning the incomplete proposal exception) provides it with undue prominence.

(j) In Example 5 on page 37, it would be helpful to clarify how this disclosure requirement interacts with the information that is already generally available to the market. That is, providing investors with certainty as to the matters disseminated by the relevant newspaper.

(k) In Example 7 on page 38, it is unclear why disclosure would be required where financial results have differed materially from the previous period, if such results are in line with prospective financial information/guidance otherwise provided to the market.

(l) In Example 10 on page 39, it would help to include a discussion of "awareness" of the relevant information, particularly as the likelihood of adjustments/write-downs becomes more certain during the audit process.