

## COMPANIES AND SECURITIES ADVISORY COMMITTEE

The Companies and Securities Advisory Committee ("the Advisory Committee") is established under the Australian Securities Commission Act 1989.

Section 148 of this Act specifies the functions of the Committee:

"148(1) - The Advisory Committee's functions are, on its own initiative or when requested by the Minister, to advise the Minister, and to make to the Minister such recommendations as it thinks fit, about any matter connected with:

- (a) a proposal to make a national scheme law, or to make amendments of a national scheme law;
- (b) the operation or administration of a national scheme law;
- (c) law reform in relation to a national scheme law;
- (d) companies, securities or the futures industry; or
- (e) a proposal for improving the efficiency of the securities markets or futures markets."

The members of the Committee as of the date of this Report are:

- Mark Burrows (Convenor)
- Don Argus
- Tim Besley
- Kevin Driscoll
- William Gurry
- Leigh Hall
- Tony Hartnell
- Dick Lester
- Wayne Lonergan
- John McIntosh

The members of the Executive of the Committee involved in the preparation of this Report are:

- John Kluver (Executive Director)
- Mark Blair

# COMPANIES AND SECURITIES ADVISORY COMMITTEE

## REPORT ON AN ENHANCED STATUTORY DISCLOSURE SYSTEM

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## Summary

In June 1991 the Federal Attorney-General, Michael Duffy, requested the Companies and Securities Advisory Committee to examine the need for a legislatively-based continuous disclosure regime, and the nature of any such scheme. The Committee was asked to report within 2 months.

In response the Committee has prepared this Report, in four Parts:

Part A outlines the general disclosure requirements imposed by the Corporations Law and the Australian Stock Exchange (ASX) Listing Rules.

Part B discusses the rationale for an enhanced statutory disclosure system. The benefits of the proposed system include the protection of the interests of equity and debt investors, the promotion of efficient management, and a better functioning capital market.

Part C details the specific policy recommendations of the Advisory Committee for improving the quality of disclosure. The Committee's proposals have three main elements:

- an affirmative obligation on directors of "disclosing entities" to make a timely disclosure of any "material matter" to the ASC and, where applicable, to the ASX. A draft pro-forma Statement of Material Matter is set out in Annexure 1;
- a requirement for disclosing entities to lodge detailed half-yearly financial reports; and
- more comprehensive annual disclosure requirements for disclosing entities and exempt proprietary companies.

Part D provides a commentary on various recommendations contained in Part C.

In preparing its Report, the Committee noted the content of two ASX Papers: "Improved Reporting by Listed Companies" (October 1990) (hereafter the ASX October 1990 Paper) and "Proposed Listing Rule Amendments To Become

Operative Late 1991" (June 1991) (hereafter the ASX June 1991 Paper). The Committee also reviewed continuous disclosure and interim reporting requirements in overseas jurisdictions, including the United Kingdom, the USA, and Canada. A summary of the North American provisions is set out in Annexure 2.

## PART A

### EXISTING DISCLOSURE REQUIREMENTS

#### The Corporations Law

##### Continuous Disclosure

The Corporations Law does not contain a comprehensive scheme for the full and accurate disclosure of material matters on a timely basis. Various provisions require disclosure in particular circumstances: for example, fundraising pursuant to a prospectus (Part 7.12 Division 2); entry into schemes of arrangement (Part 5.1); undertaking or responding to takeover bids (Part 6); or written offers or invitations concerning securities (ss 1079(1), 1080). However, there is no general continuous disclosure requirement for the benefit of those engaged in the secondary trading of securities.

##### Interim Reporting

While the idea of introducing a legislative requirement for Australian public companies to furnish interim reports is not new<sup>1</sup>, the Corporations Law does not generally require companies or trusts to lodge either quarterly or half-yearly reports. However one exception is found in s 1058, which requires directors of specified borrowing corporations to lodge quarterly and half-yearly reports.

##### Annual Reporting

There is a general requirement for companies to lodge annual returns with the ASC: s 335. Exempt proprietary companies must prepare accounts in accordance with the Corporations Law Part 3.6 Div 4, but need not attach these to their annual returns: Corporations Regulation 3.8.02. However, exempt proprietary companies that have not appointed an auditor must include key financial data in their annual returns: Corporations Regulation 3.8.01(r).

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1. On 18 November, 1976 the then Opposition introduced the *Companies and Securities Industry Bill* to Federal Parliament. The Bill proposed that public companies provide quarterly reports within 6 weeks of their quarter-year end. The Bill lapsed.

## **ASX Listing Rules**

### Continuous Disclosure

The Australian Stock Exchange (ASX) Listing Rule 3A(1) provides that a listed company or trust must notify its home exchange "immediately" of any information concerning its activities or those of its subsidiaries that is either:

- necessary to avoid the establishment of a false market in its securities; or
- likely to materially affect the price of those securities.

The ASX June 1991 Paper proposes to add a further category of information to be disclosed:

- information that is of material significance for interested parties wishing to be apprised of the financial position and/or performance of the company or trust.

The ASX June 1991 Paper also proposes to extend the reporting obligations to "entities" with which the company or trust is "associated" (as opposed to merely its subsidiaries). The purpose of this extension is to ensure that, to fully comply with Rule 3A(1), listed entities must take into account their interests in these other entities.

### Interim Reporting

The ASX Listing Rule 3B(1) states that a listed company (other than a trust or a mining exploration company) must provide the Home Exchange with a consolidated half-yearly report within 3 months of the company's half-year end. These reports must be prepared according to ASX statements (see Appendix 3 of the Listing Rules), although they need not be audited.

ASX Listing Rule 2F(6) states that the management company of a listed trust must forward audited half-yearly accounts to unit holders within 2 months of the half-year end in the case of a property trust, and 3 months in the case of all other

trusts. A number of rules specify the contents of these reports (eg Listing Rules 2F(6), 2F(7) and 3(2C)).

ASX Listing Rule 3B(5) states that a mining company must lodge a quarterly report with the Home Exchange within one month of the company's quarter year-end, including full details of production, development and exploration activities. ASX Listing Rule 3B(10) requires a mining exploration company to also complete a working capital report within one month of its quarter year-end.

The ASX June 1991 Paper proposes the following additional requirements for half-yearly reporting by listed entities:

- a cash flow statement, once an accounting standard has been introduced;
- a condensed balance sheet describing major items of current and non-current assets and liabilities;
- segmental information; and
- greater detail regarding receipts/outlays and revenue/expenses for the half year.

### Annual Reporting

The ASX Listing Rules 3C(1) requires a listed company to issue a printed annual report to its shareholders, and lodge that annual report with the Home Exchange within 4 months of the end of the company's financial year. The details to be included in the annual report are set out in Listing Rules 3C(2) and 3C(3), and also, in the case of mining companies, Listing Rule 3M. Listing Rules 3B (2B), 3B (2C) and 2F(6) set out the annual reporting requirements for unit trusts.

**PART B****RATIONALE FOR AN ENHANCED DISCLOSURE SYSTEM****Forms of Disclosure**

The Committee favours the introduction of a statutory-based enhanced disclosure system, having three principal elements:

- an affirmative obligation on directors of "disclosing entities" to make a timely disclosure of any "material matter" to the Australian Securities Commission (ASC);
- a requirement that disclosing entities lodge comprehensive half-yearly financial reports; and
- a requirement that disclosing entities include further consequential details in their annual returns and that all exempt proprietary companies lodge accounting records and key financial data in their returns.

Given these proposals, the majority of the Committee feels that a quarterly reporting requirement is not warranted at this stage. However quarterly reporting should be kept under constant review.

Enhanced disclosure will benefit a variety of users, including:

- existing and potential equity holders;
- existing and potential secured or unsecured creditors;
- existing and potential secured or unsecured debenture holders; and
- the management of the disclosing entity.

**Benefits of Continuous Disclosure**

A statutory-based system of continuous disclosure will promote investor confidence in the integrity of Australian capital markets and provide benefits to

market participants, and management, in various interrelated ways. It will:

- overcome the inability of general market forces to guarantee adequate and timely disclosure by disclosing entities;
- encourage greater securities research by investors and advisors, thereby ensuring that securities prices more closely, and quickly, reflect underlying economic values;
- ensure that equity and loan resources in the Australian market are more effectively channelled into appropriate investments, and that funds are withheld or withdrawn from poorly performing disclosing entities. This will promote capital market efficiency;
- assist debtholders in monitoring the performance of disclosing entities and thereby determine whether, or when, to exercise any right to withdraw or reinvest their loan funds, or convert debt to equity;
- act as a further, or substitute, warning device for holders of charges over corporate assets, that breaches in covenants may have taken place, or the risk of default has increased;
- assist potential equity or debt holders of disclosing entities to better evaluate their investment alternatives;
- lessen the possible distorting effects of rumour on securities prices;
- minimize the opportunities for perpetrating insider trading or similar market abuses;
- improve managerial performance and accountability by providing the market with more timely indicators of corporate performance;
- encourage the growth of information systems within disclosing entities, thereby assisting directors in their decision making and compliance with their fiduciary duties; and
- reduce the time and costs involved in preparing takeover and prospectuses documents.

**Benefits of Half-Yearly Reports**

A comprehensive periodic reporting system would complement and enhance the benefits derived from continuous disclosure. Half-yearly reports would:

- act as a partial summary of, and a checking mechanism on compliance with, the continuous disclosure obligations;
- assist in assessing the longer-term implications of prior disclosure statements;
- promote a more informed assessment of the likely future financial performance of disclosing entities;
- require disclosing entities to disclose various facts which in combination, though not necessarily individually, may be material in assessing the value of their securities; and
- help investors to more accurately compare the performance of various disclosing entities through standardised reporting criteria.

**Benefits of Enhanced Annual Reports**

An upgraded annual reporting requirement would:

- complement the proposed changes to continuous and half-yearly reporting; and
- ensure that the ASC database contains comprehensive financial information on all Australian companies.