2001: a capital markets odyssey
Will the capital markets in Australia in 2001 be the same as in 1999 ?

presented to the
16th Annual Banking Law and Practice Conference
10-11 June 1999

by

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One of the themes of the annual conferences organised by the Banking Law Association over the past 16 years has been the constancy of change and the need for practitioners (whether solicitors, barristers or bankers; whether in private practice or in-house) to be aware not only of changes in legislation and case law, but also of those major factors (the so-called drivers of change) which influence and bring about changes in market practices and procedures.

When earth breaks up and heaven expands,
How will the change strike you and me,
In the house not made with hands ? [1]

1999 is no different. Other papers have examined changes at the macro level (the international forces affecting our market as a whole) and at the micro level (important changes in the law of personal property security). My task in this paper involves a combination of the two: what specific changes might be expected in (i) the structure of the domestic debt capital markets, and (ii) the way in which debt securities are presently issued, distributed and traded in Australia, as a result of some current drivers of change.

As this is a banking law conference, my primary focus is on the debt capital markets, but it should not be assumed that there are deep divisions in Australia's capital markets or that there is a dichotomy between debt securities and equities. There are many similarities (for example, the content requirement for prospectuses[2] is the same, although what investors and their professional advisers would reasonably require will vary depending on the nature of the securities being offered for sale). In fact, one of my predictions is that there will be an increasing convergence in our debt and equity capital markets over the coming years. Many of the factors which influence and bring about change in the debt capital markets will have an equally profound effect on the equity markets.

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[1] Robert Browning, *By the Fire-side*, xxvii.

[2] Section 1022 of the *Corporations Law* applies equally to shares and other equities, debentures and other debt securities and interests in managed investment schemes. In relation to debentures it is important to note that section 78(4) of the *Corporations Law* provides that *"An acceptance by a body corporate of money deposited with, or lent to, the body constitutes the issue by the body of debentures of the body"*. In other words, there is no need for any paper transaction to have taken place or for a debenture in physical form to have been issued. The provision of the funds is sufficient to constitute an issue of debentures.

Predictions are a dangerous thing. As lawyers we are trained to look at events in the past. Our courts are frequently reminding us of what steps should have been taken by different parties (including lawyers) in particular historical circumstances. We include provisions in our documents to address a wide range of contingencies, usually in the light of the bitter experience of the past. In looking to the future, I am reminded of the words of Jesus Christ when he taught in the synagogue at Nazareth:

> *Only in his home town and in his own house is a prophet without honour.*[3]

As an Australian banking lawyer recently returned from several years overseas, I hope that you will regard my predictions and prophecies as food for thought and not as an excuse for the drowning of sorrows.

1 Powerful Drivers of Change

In a recent address to the Committee for Economic Development of Australia[4], the Chairman of the Australian Stock Exchange (**ASX**), Maurice Newman, used the phrase *paradigm shift* to describe what is happening in the financial services sector in Australia today. This phrase was originally coined by the American physicist and philosopher of science, Thomas Kuhn, in arguing that science did not proceed by the gradual and rational accumulation of knowledge as is commonly believed, but rather by revolutionary change when a commonly accepted world view (or paradigm) in which scientists work becomes untenable in the light of new knowledge[5].

A similar point of view was put forward in the *Financial System Inquiry Final Report* (the Wallis Report) which in its overview entitled *Towards 2010* stated:

> *Rapid technological innovation and an evolving business environment together with longer-term changes in customer needs and profiles are reshaping the financial system.*
>
> *The system will have a progressively greater array of participants, products and distribution channels which, in some cases, will expand beyond the traditional categories of banking, insurance and financial exchanges.*
>
> *Competition is emerging from new providers of financial services and through the increasing globalisation of financial markets. This generates increasing pressure for improved efficiency and performance.*[6]

One of my theses in this paper is that these factors will radically change our capital markets in much less than 13 years and we should expect changes to occur sooner rather than later. Things will be different in 2001.

This not to suggest that the Australian financial sector has not undergone profound change over the past decade or two. In the last 16 years, many of these changes have been discussed at previous conferences. Many of these changes have been due to the progressive deregulation of our markets. However, in considering what specific changes might be

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[3] Recorded in the *Gospel of Matthew*, chapter 13, verse 57 (New International Version).

[4] *Financial Services Restructure in Australia*, 4 May 1999 at the ANA Hotel, Sydney.

[5] *The Structure of Scientific Revolutions* (Second edition, The University of Chicago Press, 1970).

[6] *Financial System Inquiry Final Report* (AGPS, March 1997) at page 3.

expected in the way debt securities are issued, distributed and traded in Australia in the next few years, I intend focusing on different drivers of change. The four particular drivers are:

- globalisation;
- customer needs and demands;
- financial innovation; and
- technology.

In doing so, I hope you will forgive me for painting a picture with broad brush strokes, rather than the fine detail normally used by a lawyer. Perhaps this will enable me to claim in a few years that at least some of my predictions and prophecies were accurate.

2 Globalisation

2.1 *Background comments*

The phenomenal nature of the globalisation of the financial sector is evident from the statistics reported in our press every few days. Some examples[7] are:

- global outflows of foreign direct investment have increased 25-fold since the 1970's to US$350 billion per annum. A local example can be seen in the success of foreign investors in bidding for Victorian electricity and gas assets; and

- foreign investment in Australia and Australian investment abroad has quadrupled in ten years.

Deregulation of our markets, declining government budget deficits and occasional surpluses, compulsory superannuation contributions and diversified portfolio management have intensified the impacts of globalisation on Australia's debt capital markets.

Throughout much of the last 25 years Australia's domestic debt capital markets have been dominated by federal and semi-government issuers. Securities were issued domestically without significant disclosure and with minimal terms and conditions. Whilst offshore investors purchased the securities, little regard was paid to the impact of foreign securities laws and elaborate structures and arrangements were often used to ensure no Australian interest withholding tax was payable.

This is changing and some of the recent features of our domestic debt capital markets are:

(a) the (re)emergence (albeit slowly) of a corporate debt market;

(b) the greater participation in the market by US investment firms;

(c) an increase in primary issuance to offshore investors, particularly in the United States or to US persons (which is the reverse side of the same coin as has seen increasing issuance by Australian issuers in the US domestic capital markets);

(d) issuance by foreign issuers (the so-called 'matilda' and 'kangaroo' bonds), frequently as part of a global medium term issuance programme; and

[7] As quoted by Maurice Newman in *Financial Services Restructure in Australia*, supra.

(e) participation by Australian institutions in global issues.

How might these globalising trends impact us in the future ?

2.2 *The impact of US and other international securities laws*

Many issuers of debt securities in Australia have been forced to address the requirements of the US Securities Act of 1933 and the Securities Exchange Act of 1934 when issuing debt securities outside Australia. Prior to 1990 they did not generally do so when issuing debt securities in Australia.

In 1990 the US Securities and Exchange Commission (**SEC**) adopted Regulation S under the Securities Act[8] which provides that certain offers and sales of securities made outside the United States need not be registered with the SEC. This seems a self-evident proposition. Why did it need to be stated at all and why has it generated changes in the practices and procedures followed in many foreign capital markets ?

Generally speaking, under Regulation S offerings directed solely to residents of a single country outside the United States (so-called "overseas directed offerings") need not be registered. I suspect that this is the principal reason issuers of debt securities in Australia have continued to ignore the requirements of the Securities Act. However, I also suspect that the fundamental premise of this reasoning is no longer true. Issues of debt securities in Australia are increasingly directed in part to residents of other countries and, accordingly, no longer qualify as overseas directed offerings for the purposes of Regulation S.

Many issues should now be regarded as international in character. I understand that because of the US federal structure, the jurisdictional basis for the Securities Act is the use of *"transportation or communication in interstate commerce or the mails"*[9]. It seems that many issues of debt securities in Australia may now attract the jurisdiction of the Securities Act. Although specific statutory exemptions exist for non-public transactions[10] and for transactions in specified types of securities[11], there is no statutory exemption for transactions which take place outside the United States. Concerns about the extra-territorial application of the Securities Act, especially concerns expressed by US investment firms operating outside the United States about the inadequacy of the SEC's prior attempts to narrow the application of the registration requirements to international financial transactions (for example, by the use of no action letters), were a major factor leading to the adoption of Regulation S.

In relation to offerings which do not qualify as overseas directed offerings, Regulation S contains specific safe harbours which prescribe the conditions under which the SEC will treat an offer of securities outside the United States as non-public and, accordingly, not subject to the registration requirements of the Securities Act. The detailed requirements of Regulation S in relation to both primary and secondary offerings are beyond the scope of this paper, but in essence differing conditions are prescribed for different categories of

[8] 17 C.F.R. § 230. 901-904.

[9] Section 5 of the Securities Act. The primary prohibition is on using such means or instruments to offer or sell securities unless a registration statement (ie. prospectus equivalent) filed with the SEC has become effective.

[10] For example, private placements made in accordance with section 4(2) of the Securities Act.

[11] For example, certain securities issued by banks in reliance on section 3 of the Securities Act.

issuer and securities issuance, depending on the likelihood that the relevant securities will be distributed in the United States[12].

There are two general conditions applying to all categories, which in summary require that:

- no offer is made to a person in the United States; and
- no marketing, selling or other activities are undertaken which could reasonably be expected or intended to condition the market in the United States with respect to the relevant securities.

In addition, for some categories it is necessary to include prohibitions on offers and sales in the United States or to US persons for a restricted period (approximately 40 days for debt securities) and certifications as to non-US beneficial ownership.

Additional and separate requirements apply under the so-called TEFRA rules[13] where bearer debt securities are issued.

As a result of the increasing participation in the domestic capital markets by US investment firms and the increase in primary issuance to offshore investors (particularly in the United States or US persons), there is no escaping the conclusion that in the future domestic information memoranda and other offering documents and related dealer and programme agreements will include more extensive US selling restrictions than has historically been the case. Prediction number two. The challenge for Australian lawyers is to understand and advise our clients on the nature of these restrictions.

In addition, to the extent issues of debt securities in Australia are increasingly directed in part to residents of countries other than the United States, greater attention will need to paid to the securities laws of those countries.

2.3 *Liability myths*

Retail issues of debt securities in Australia must comply with the prospectus provisions contained in Part 7.12 of the *Corporations Law*[14] and any breach of these provisions will attract the civil liability provisions of Part 7.11 (including the availability of certain due diligence defences). However, most issues of debt securities in Australia are currently structured as excluded issues or offers[15] and, until a retail debt market develops in Australia, the prospectus provisions will not be applicable to questions of liability.

There is a perception in some quarters that structuring transactions as excluded issues or offers effectively means that there are no substantive questions of liability in relation to the

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[12] A useful discussion of Regulation S and the impact of US securities laws on offers and sales of securities by foreign companies outside the United States is contained in chapter 3 of *United States Securities and Investments Regulation Handbook* (Graham & Trotman, 1992).

[13] US Treasury Regulations § 1.163-5(c)(2)(i)(C) and (D).

[14] See paragraph 3.2 below for a discussion of the disclosure requirements of these provisions.

[15] See section 66 of the *Corporations Law* and regulations 7.12.05 and 7.12.06 of the *Corporations Regulations*. In summary, the principal bases on which an issue or offer of debt securities in Australia is structured so as to constitute an excluded issue or offer is to require that either (a) the consideration payable in respect of any subscription or purchase of the debt securities be not less than A$500,000 (irrespective of the denomination of the debt securities), or (b) the debt securities be only offered or issued to certain defined categories of institutional investors.

information memoranda and other offering documents. The *Corporations Law* does not prescribe any content requirements for such documents, but that is not the end of the story. Possible sources of liability for issuers, directors, investment firms and others include the general liability provisions in the *Corporations Law* and related legislation and the common law[16].

Section 995 of the *Corporations Law* provides that a person shall not *engage in conduct that is misleading and deceptive or is likely to mislead or deceive* in connection with dealings with securities. This section is in similar terms to section 52 of the *Trade Practices Act* 1974 (Commonwealth) and other legislation[17]. Whether particular conduct is misleading or deceptive is a question of fact to be determined in the context of all the surrounding facts and circumstances. However, it is clear that silence may constitute misleading or deceptive conduct wherever a duty to reveal relevant facts exists.

Of course any consideration of sections 995 and 52 in this context would not be complete without a reference to the decision in **Fraser v NRMA Holdings Limited**[18] where the court found that silence may also amount to a breach of section 52, even absent a positive duty of disclosure:

> *Whilst section 52 does not by its terms impose an independent duty of disclosure which would require a corporation or its directors to give any particular indication to [investors]...where information for that purpose is promulgated, unless the information given constitutes full and fair disclosure of all the facts which are material to enable the [investor] to make an informed decision, the combination of what is said and what is left unsaid may, depending on the full circumstances, be likely to mislead or deceive [investors].*

Thus, in looking at any information memorandum or other offering document for an excluded issue or offer, it is necessary to examine whether there was a positive duty to disclose matters or whether in the circumstances the failure to disclose has left what was said misleading or deceptive or likely to mislead and deceive[19].

Not only is the person engaging in the misleading and deceptive conduct liable, but also anyone who has been involved in the conduct by[20]:

- aiding, abetting, counselling or procuring any contravention arising from the conduct. A person must or should have been aware of the facts that gave rise to the contravention. Proof of intent is not required;

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[16] A cause of action in negligence could arise on the basis of a breach of duty of care towards the potential investors when providing information. In cases of non-disclosure, an action in negligence may have some advantage in that the duty of care claimed is relevant to whether there was a misrepresentation by silence.
[17] For example, sections 12DA and 12GF of the *Australian Securities and Investments Commission Act* 1989 (Commonwealth) and sections 42 and 68 of the *Fair Trading Act* 1987 (NSW).
[18] 1985 ATPR 41 to 374.
[19] In this context it is important to note that section 765 of the *Corporations Law* provides that where a person makes a representation relating to a future matter, if that person did not have reasonable grounds for making the representation (and the onus is on that person to show that he had reasonable grounds), the representation will be taken to be misleading. The operation of this section, involving as it does a reversal of the onus of proof, is significant when considering the position in relation to forecasts and other future matters.
[20] Sections 1005 and 79 of the *Corporations Law*.

- inducing, whether by threats or promises or otherwise, the contravention:

  > *Inducing a contravention...connotes...some act of compulsion by force or threat of force or some act of persuasion or stimulation aimed at assuring that an act is committed which constitutes a contravention*[21].

- being in any way, by act or omission, directly or indirectly, knowingly concerned in, or party to the contravention (ie. participating in, or assenting to, the contravention with knowledge of the essential elements constituting the contravention); or

- conspiring with others to affect the contravention.

Thus, it can be seen that it is not only issuers and their directors who are at risk, but investment firms and other advisers as well. Readers may well be asking themselves about the disclaimers and statements limiting responsibility which are usually included in information memoranda and other offering documents for domestic issues of debt securities[22].

Three quick observations. First, I am reminded of the foreign currency borrower litigation[23] over the past decade or more. I suspect that in many cases investment firms and advisers will be found to have actually given advice or made representations outside the context of the information memorandum or other offering document which is covered by the disclaimer[24]. Liability will follow where the advice or representations are misleading or deceptive or likely to mislead or deceive or are negligent having regard to the duty of care owed by the investment firm or adviser.

Second, many issuers and their directors rely on investment firms and advisers in determining the scope of any disclosure. Liability to investors may not attach to such persons in relation to content, but liability to issuers (and, possibly, investors) may well follow if the scope of disclosure is inadequate[25].

Third, whilst any particular case will turn on its own facts and the wording of the relevant disclaimers and statements limiting responsibility[26], it would be a mistake to assume that a disclaimer is equivalent to a bulletproof vest. Investment firms also need to avoid adopting statements in a way which would negate any disclaimers and statements:

> *The innocent carriage of a false representation from one person to another in circumstances where the carrier is seen to be a mere conduit, does not involve him in making that representation....when, however, a representation is conveyed in*

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[21] **Yorke v Lucas** (1983) 49 ALR 672 at page 681.

[22] A typical disclaimer would be:

> *No information contained in this memorandum has been independently verified by [investment firm]. Accordingly, no representation, warranty or undertaking is made or may be implied, and no responsibility or liability is accepted, by [investment firm] or any officer or employee of [investment firm], to or for the origin, accuracy, completeness or distribution of, or any errors or omissions from this memorandum whether arising out of negligence or otherwise.*

[23] For a detailed discussion of these issues, see David Allan and Mark Darian-Smith, *Responsibility for Financial Advice* in *Australian Finance Law* (Fourth edition, LBC Information Services, 1999).

[24] See also *NatWest Australia Bank Limited v Tricontinental Corporation Limited* (1993) ACL Rep 45 Vic 5

[25] See also paragraph 3.2 below.

[26] A recent example is **Leda Holdings Pty Limited v Oraka Pty Limited** (1998) ATPR 41-601.

circumstances in which the carrier would be regarded by the relevant sections of the public as adopting it, then he makes that representation.[27].

As for most types of claim, it will also be necessary to prove a relevant nexus between the misleading and deceptive conduct and the loss or damage suffered[28].

In addition to claims based on misleading and deceptive conduct, it should be noted that other provisions of the *Corporations Law*[29] provide that a person shall not:

(a) enter into transactions (directly or indirectly) which are intended or likely to have the effect of increasing, maintaining, stabilising or decreasing the price of securities traded on a stock market with the intention of inducing other persons to buy or sell such securities;

(b) create (directly or indirectly) a false or misleading appearance of active trading, a market or the price of securities;

(c) make a false or misleading statement in relation to securities; or

(d) fraudulently induce or attempt to induce a person to deal in securities.

Finally, in light of my earlier remarks on the impact of United States and other foreign securities laws, it should not be forgotten that the distribution of offering documents and/or the offer or sale of debt securities in foreign countries may give rise to civil or criminal liability under such laws. In this context it is worth noting that Regulation S only provides relief from the registration provisions of the US Securities Act. The extraterritorial effect of the Act's anti-fraud and other liability provisions is unaffected.

The management of these risks in relation to information memoranda and other offering documents used in the domestic debt capital markets will be a more significant issue for issuers, directors, investment firms and lawyers in the future. Prediction number three.

2.4 *The abolition of the withholding tax dingo fence*

Notwithstanding the 1997 changes[30] to the interest withholding tax (**IWT**) exemption available under section 128F of the *Income Tax Assessment Act* 1936 (Commonwealth) (**ITAA**), there remains a barrier between the Australian capital markets and the

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[27] **Gardam v George Wills and Co. Limited** (1988) 82 ALR 415 at page 427. See also **Re Logie Brae Pty Ltd** 1992 Fed No. 748 Trade Practices.

[28] In **Kabwand Pty Ltd v National Australia Bank Ltd** (1989) ATPR 40-950 the court described this nexus:

> *For present purposes it is sufficient to say that a person claiming damages must show either that he has been induced to do something or to refrain from doing something which gives rise to damages ... or has been influenced to do or refrain from doing something giving rise to damages by the conduct contravening section 52.*

[29] Sections 997, 998, 999 and 1000.

[30] Those changes involved (a) replacing the previous "wide distribution" test with a "public offer" test, (b) removing the requirement that the proceeds of an issue be used in an Australian business, (c) providing that the IWT exemption is not available if debt securities are issued to an "associate" or resident of Australia, or interest is paid to an associate, where the issuer is aware, or should have been aware, that such a person was an associate or Australian resident, and (d) introducing self assessment procedures for claiming the IWT exemption.

international markets, particularly for Australian resident issuers. Currently 100% of an issue of debentures must take place outside Australia in order to qualify for the exemption.

This barrier should be removed later this year. In December 1997, the Prime Minister announced the Commonwealth Government's intention to implement additional reforms to facilitate the deepening and greater liquidity of the Australian debt capital markets by enabling Australian corporate issuers to issue debt securities under a global programme with no tax discrimination between the various markets. The new regime will not apply to securities issued in Australia by government or semi-government issuers.

The draft legislation to implement the further changes is now known as the *Taxation Laws Amendment Bill (No. 2)* 1999. It is hoped that it will be enacted later this year, but there seems to be an impasse in the Senate at the moment regarding the passage of certain tax legislation which is causing some delay. If passed, the amendments to section 128F of ITAA will apply in relation to issues of debt securities made after 2 July 1998.

ITAA is to be amended so that in order to qualify for an exemption from IWT:

- debt securities will no longer be required to be issued outside Australia;
- interest will no longer be required to be paid outside Australia; and
- debt securities will able to be sold to Australian residents (in both the primary and secondary markets). The prohibition on sales to associates is to be retained.

The *Taxation Laws Amendment Bill (No. 2)* will also amend section 126 of ITAA so that it applies to the payment of interest under any bearer debt securities *wherever issued* if the securities are held by an Australian resident or a non-resident that carries on business in Australia. The tax file number provisions of ITAA[31] will continue to apply.

The main consequence of these changes is that Australian corporate issuers will be able to structure and document issues simultaneously in the domestic and international debt capital markets under the one programme. As a consequence, liquidity in the domestic markets is likely to be enhanced, maturities will be extended and pricing is more likely to track the pricing available in overseas markets. Other implications include:

(a) the potential to reduce legal and establishment costs for issues of debt securities by Australian residents in offshore markets. It will be possible to negotiate and sign all documents in Australia whether investors are overseas or local. We may also see an increased use of an Australian law as the governing law;

(b) debt securities will be able to be listed on the ASX in addition to or instead of an overseas exchange (traditionally either London or Luxembourg);

(c) in time it should be possible for such debt securities to be settled and cleared through the Austraclear system (rather than Euroclear, Cedelbank or another offshore custodian or nominee); and

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[31] Part VA of the ITAA.

(d) all investors will be entitled to receive Australian dollar interest payments by way of a direct credit to accounts in Australia or a cheque mailed to an address in Australia.

The issuance options which will be available to Australian corporate issuers assuming the amendments are enacted can be summarised as follows:

SECURITIES ISSUED IN REGISTERED FORM

issued to offshore investors only

- must satisfy section 128F - no sales to associates
- section 126 does not apply
- tax file numbers not required

issued to onshore investors only

- IWT does not apply
- section 126 does not apply
- must provide tax file numbers

issued to offshore and onshore investors

- must satisfy section 128F - no sales to associates
- section 126 does not apply
- must provide tax file numbers for onshore investors

SECURITIES ISSUED IN BEARER FORM

issued to offshore investors only

- must satisfy section 128F - no sales to associates
- section 126 should not apply (if securities held in Euroclear/ Cedelbank)

issued to onshore investors only

- IWT does not apply
- section 126 applies
- tax file numbers not required

issued to offshore and onshore investors

- must satisfy section 128F - no sales to associates
- section 126 will apply if an Australian resident or a non-resident carrying on business in Australia is the "holder"
- tax file numbers not required

I remain confident that the changes will be enacted in time and so prediction number four is that there will be a significant increase in the use of global medium term note and similar programmes by Australian corporate issuers which take advantage of the more liberal IWT regime. Again, a challenge for lawyers to respond to a changing environment, but one with many opportunities.

2.5 *The European experiment*

Europe has been a major focus of developments in the international capital markets since the early 1960's and this remains true today. The commencement of the third stage of European Economic and Monetary Union (**EMU**) on 1 January 1999 was the latest in a long line of significant steps. In the years leading up to the introduction of a single currency, there was a vast amount of discussion and debate in legal circles:

> *The voluntary adoption by a significant number of sovereign states of a single, new currency is unprecedented and has caused bankers, businessmen and lawyers to ask whether this momentous step poses legal problems. Few, if any, initiatives in European history have attracted so much interest in the legal aspects of a change in financial relationships.*[32]

Fortunately, it appears that there are no insurmountable legal problems. Concerns about the frustration of contracts, the applicability of the *lex monetae* principle to the old European Currency Unit (an accounting unit, rather than a currency) and doctrines of impossibility etc. have largely dissipated[33]. In Australia, the prevailing consensus is that it is unlikely that contracts will be frustrated as a result of the adoption of the single currency[34].

However, I would not want to suggest that there are no issues or challenges for Australia's domestic capital markets as a result of the introduction of the Euro.

Difficulties may arise in the interpretation or implementation as a result of:

- unanticipated conversion and rounding issues;
- disappearing or changing price sources;
- the need for redenomination, renominalisation or reconventioning; or
- the disappearance of underlying commercial rationale of a contract.

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[32] Clifford Dammers (Secretary General, International Primary Markets Association), *The Euro: eliminating legal uncertainty* in *The Euro*, ed. Paul Templeton (Second edition, John Wiley & Sons, 1998).

[33] In relation to the member states these issues have been largely resolved. The Article 235 Regulation (EC/1101/97) relating to conversion and continuity of contract is in force in all member states of the European Union and the Article 1091(4) Regulation (EC/974/98) relating to questions of legal tender is in force in the eleven member states participating in the third stage of EMU. It is probable that many of the provisions of the Article 1091(4) Regulation will also apply in the other member states by virtue of the *lex monetae* principle.

[34] The leading Australian authority on the doctrine of frustration is the decision of the High Court of Australia in *Codelfa Constructions Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337. However, for an example of possible problems in relation to guarantees and third party security interests, see *Papua New Guinea Development Bank v Manton* [1982] VR 1000. See also Greg Hammond, *An Australian view of the new EMU* (1999, forthcoming in the Journal of International Banking Law).

Each of these matters carries the risk of increased costs, time delays in settlement and possible disputes and supports the desirability of a currency continuity clause. Apart from relying on the existing law (particularly the *lex monetae* principle), the following are the main approaches available under Australian law to address questions of uncertainty:

(a) the negotiation of bilateral amendments. An example is that, in the context of OTC derivatives governed by an ISDA Master Agreement, the leading participants in the Australian OTC market have acceded to the ISDA EMU Protocol[35];

(b) reliance on the business efficacy rule. Under Australian law, a court may be prepared to imply a term in a contract when it is necessary to give business efficacy to the transaction. An early Australian statement of the rule was:

> *It is a general rule applicable to every contract that each party agrees, by implication, to do all things as are necessary on his part to enable the other party to have the benefit of the contract.*[36]

(c) reliance on an implied duty to act in good faith in contractual relations[37]. Such a duty would be in addition to the well accepted principle of the common law that parties to a contract must act honestly.

Perhaps the bigger challenge for Australian lawyers is to understand the changes in the European financial system in preparing documentation which provides for the issuance of debt securities in Euro. These include the conversion and rounding principles in the Article 235 Regulation[38], the new price sources (EuroLIBOR and EURIBOR and the differences between them) and the operating structure of the new payment and settlement systems (the Trans-european Automated Real-time Gross settlement Express Transfer system (TARGET) and Euro CHAPS in the UK).

My fifth prediction is that the Australian debt capital markets are yet to fully experience and absorb the consequences of the third stage of EMU.

The third stage of EMU is not the only European development of which we need to be aware. The proposed EU withholding tax directive[39] is the subject of considerable political debate at the moment. The draft provides that each member state must introduce in its national law either a "withholding tax system" or an "information system" in relation to any payments of interest (including in respect of debt securities) made by a "paying agent" established in that member state for the immediate benefit of an individual who beneficially owns the interest and is resident for tax purposes in another member state. If there is a

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[35] A list of institutions acceding to the ISDA EMU Protocol is available from ISDA's website: www.isda.org. There are five annexes to the ISDA EMU Protocol each dealing with a separate issue and parties must state which (or all) of the annexes that they accept as amending ISDA Master Agreements with other parties acceding to the Protocol. The annexes deal with the inclusion of a continuity provision, replacement price sources, payment netting, the adoption of various EMU definitions and the inclusion of provisions dealing with bond options.

[36] Chief Justice Griffith in *Butt v McDonald* (1896) 7 QLJ 68 at 70-71 as approved by the High Court of Australia in *Secured Income Real Estate (Australia) Ltd v St Martins Investments Pty Ltd* (1979) 144 CLR 596.

[37] See, for example, the judgment of Justice McHugh in *Integrated Computer Services Pty Ltd v Digital Equipment Corp (Australia) Pty Ltd* (1988) 5 BPR 11,110.

[38] See note 33 supra.

[39] Proposal for a Council Directive to ensure a minimum of effective taxation of savings income in the form of interest payments within the Community *COM (98) 295* 20 May 1998.

significant increase in the use of global medium term note and similar programmes by Australian corporate issuers which take advantage of a more liberal IWT regime[40], then the Australian market will need to monitor and understand the implications of this directive.

3 Customer needs and demands

3.1 *Background comments*

In considering the question of changing customer needs, the *Financial System Inquiry Final Report* concluded:

> *The combination of changing demographics and work patterns are altering the features that customers will seek from financial products. Their increasing willingness to adopt new technology will shape the way in which those services are delivered, while greater focus on value will mean that only those suppliers will prosper who offer products with desired features at an attractive price.*
>
> *The increasing holdings of financial assets and liabilities by households mean that consumers now have greater exposure to the financial system than in the past.*
>
> *Success in the future will flow to those organisations which are able to sense these changing customer needs and which can meet their customers' price, service and delivery expectations.*[41]

In the domestic debt capital markets, there are two principal categories of customer: the sophisticated institutional investor who participates in excluded issues (see above) and the retail investor. I remain intrigued by the attitude of some players in the primary distribution of debt securities in the wholesale market who use terms such as "stuffees" and "punters" to describe investors. Not retail investors, but institutional investors. There seems to be a presumption that as little information as possible needs be made available.

I believe this is naive. The information age dawned some time ago and there are many information sources regarding products, services and corporate performance which are available to investors. Investors are becoming more discerning and it will be those market participants who manage the provision of information in a timely, consistent and reassuring way who will be successful in the future.

What does the changing needs of customers mean for the future ? I hope to summarise some of these more quickly than the impacts of globalisation.

3.2 *Disclosure standards*

As noted above in relation to liability myths[42], the Corporations Law does not prescribe any content requirements for domestic information memoranda and other offering documents for excluded issues or offers. The result has been a proliferation of different approaches:

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[40] See paragraph 2.4 above.
[41] supra, at page 91.
[42] See paragraph 2.3 above.

- no disclosure about the issuer other than its name and ACN. The theory being that potential investors can then make their own queries, particularly where the issuer is listed on the ASX;

- a short one or two page summary about the issuer (particularly common for short term commercial paper programmes) on the basis that investors will (exclusively) rely on the rating of the debt securities by Standard & Poor's Ratings Group and/or Moody's Investors Service, Inc. (notwithstanding that both rating agencies go to considerable lengths to discourage investors from doing so;

- the use of a such a summary, together with the incorporation by reference of other documents published by the issuer (for example, annual audited financial statements and announcements to the ASX, particularly where the issuer is subject to continuous disclosure obligations);

- the disclosure of the same information as is made available by the issuer to investors in offshore capital markets. This approach is frequently adopted by foreign issuers accessing the Australian debt capital markets. The information disclosed is usually the same as is included in Euromarket prospectuses or offering circulars for those issuers.

  The irony of this approach is that the disclosure standard in the Euromarkets for medium term notes (especially those listed on the London or Luxembourg stock exchange) is to all intents and purposes identical to the retail disclosure standard in section 1022 the *Corporations Law*: all such information as investors and their professional advisers would reasonably require, and reasonably expect to find in the prospectus or offering circular, for the purpose of making an informed assessment of (i) the assets and liabilities, financial position, profits and losses and prospects of the issuer, and (ii) the rights attaching to the debt securities[43]; and

- the preparation of a prospectus complying with the provisions of the *Corporations Law*. Whilst only required in Australia for a retail issue, the offering of part of an issue in foreign countries has led some issuers to conclude that this is an effective risk minimisation technique, particularly if they had recently been required to prepare an Australian prospectus (or equivalent) for another purpose.

These last two approaches also reflect the view of some finance directors that investors in different markets are entitled to receive the same information.

This proliferation of different approaches has a number of effects. First, investment firms who advise issuers and their directors as to the scope of the disclosure required may be exposed to greater liability[44]. This exposure is different to risk for the actual content of information memoranda and other offering documents.

Second, investors increasingly are requiring greater disclosure in particular transactions if such disclosure has been made in other transactions. An overall raising of standards driven by investor demand. The decline in the issuance of government fixed interest securities in the domestic capital markets has resulted in a diversification by investors and, in turn, the

[43] See, for example, section 146 of the Financial Services Act 1986 (UK).

[44] See paragraph 2.3 above.

need for greater internal credit and risk analysis. This requires greater disclosure and the provision of more information.

My sense (and, hence, my sixth prediction) is that there will be greater consistency in disclosure and an overall raising of standards in information memoranda and other offering documents for excluded offers and issues in the next two years. The Australian Financial Markets Association is already looking at the issue from the perspective of the needs of issuers, investment firms and investors.

3.3 *The dominance or decline of ratings*

Ratings have been an important feature of domestic issuance in recent years, but for the reasons outlined earlier in this paper, in the future they will be less important in an overall sense. Prediction number seven. Investors will rely on a wider range of information sources in making investment decisions in relation to particular issuers and debt securities.

Another factor which will drive this change (and the need for greater consistency in disclosure and an overall raising of standards in information memoranda and other offering documents) is the prudential regulation of many investors in the domestic market: superannuation funds, managed funds and insurance companies. For example, the *Superannuation Industry (Supervision) Act* 1993 (Commonwealth) sets the legal framework which governs how trustees should manage superannuation funds. The Act imposes legal obligations on them and also on the auditors of the funds. One such obligation is the requirement to develop and implement an investment strategy.

It seems probable that effective monitoring of investment strategies by a superannuation trustee's board of directors or the external compliance committee for a managed investment scheme will require the provision of more information to the fund at the time of the initial investment.

This would be consistent with the experience of a number of overseas markets where ratings are a necessary pre-requisite, but not a sufficient basis for the purposes of investors making an informed assessment.

3.4 *A domestic private placement market ?*

As a result of the exemption in section 4(2) of the US Securities Act for transactions not involving any public offering, a substantial private placement market has developed in the United States for medium to long term debt securities. The main investors in this market are insurance companies and a wide range of managed funds. The market has some similarities with aspects of the excluded issue or offer market in Australia.

There is typically a disclosure document called a private placement memorandum which varies in the degree of detail, but must meet the standards of the anti-fraud provisions of the Securities Act. The amount of disclosure provided to offerees varies from a sophisticated US registration statement style (or, depending on the requirements of the investors, in some cases even more extensive) through Euromarket style documentation to fairly superficial disclosure.

A key difference between the debt securities issued in this market and both (i) debt securities offered in public markets, and (ii) those currently offered in the Australian domestic debt capital markets, is the provision of more extensive representations and warranties, financial covenants and other undertakings and events of default which enable the investors to monitor their investment. In many ways such representations and warranties, financial covenants, undertakings and events of default have more in common with bilateral and syndicated loan agreements than they do with traditional debt securities.

In the event that an issuer encounters financial difficulties, investors in this market take a much more active role in the resolution of those difficulties than has traditionally been the case with public bondholders.

Prediction number eight is that with the increasing flow of funds into compulsory superannuation and other funds in Australia, a domestic private placement market will develop in the medium term.

3.5 *Listed debt securities - a new era for the ASX ?*

Relatively few issuers in the domestic debt capital markets have sought to list their securities on the ASX[45]. The ASX Listing Rules do not specifically cater for the listing of debt securities in a manner which encourages issuers to obtain a listing.

Unlike investors in some European and other offshore markets, Australian investors are rarely subject to a legal or prudential requirement which restricts investments to listed debt securities. Thus, there is less commercial incentive for an issuer to obtain an ASX listing. However, the need to obtain a listing may increase with greater participation by foreign investors in Australia's debt capital markets.

In addition, if there is a significant increase in the use of global medium term note and similar programmes by Australian corporate issuers which take advantage of a more liberal IWT regime[46], then the challenge for the ASX is to develop specific rules and procedures for the listing of debt securities which make it a more viable and attractive alternative to the London and Luxembourg stock exchanges on which Australian issuers have traditionally listed their debt securities which are offered outside Australia. In doing so, the advantages of listing domestic offerings may become more apparent.

A failure to address these issues will see a dominance of overseas listings for domestic debt securities. Prediction number nine and an extremely bizarre possibility.

4 Financial Innovation

4.1 *Background comments*

Australian markets have long been at the forefront of new techniques and products. From the use of tender panels for the distribution of bank accepted bills of exchange in the 1970's and 80's to the development of securitisation structures and derivative products in the 1990's.

Nevertheless, the range of fixed income products and debt securities available in offshore markets is generally broader than available in Australia. These include high-yield

[45] A number of foreign issuers have done so, including Statens Bostadsfinansieringsaktiebolag, SBAB (Swedish National Housing Finance Corporation) and Deutsche Siedlungs-und Landesrentenbank (DSL).
[46] See paragraph 2.4 above.

securities, dual currency instruments and indexed linked products. At a general level, it could be anticipated that increased depth and liquidity in the Australian markets will see greater issuance of these types of products.

However, it is in this area of financial innovation that my crystal ball is clouded. It seems clear that the innovators will continue to be encouraged, but what will the innovations be ? The major driver may well be changes to the Australian tax system, particularly whether the Federal Government is prepared to introduce reforms to facilitate the development of Australia as a leading regional financial centre. This is a minefield and a subject which I will not canvass further in this paper.

Whilst you ponder this question, let me suggest two areas in which I expect new challenges to emerge for lawyers advising market participants ?

4.2 *Competition laws versus distribution procedures*

The procedures by which debt securities are distributed in the Australian capital markets have evolved over time and vary in some respects from those used in offshore markets. For example, in the Euromarkets investment firms are permitted to over-allot or effect transactions which stabilise or maintain the market price of debt securities at a level which might not otherwise prevail[47]. In Australia, such conduct would almost certainly involve misleading and deceptive conduct and/or a contravention of the market manipulation provisions contained in the *Corporations Law*[48].

Similarly, a number of practices and procedures commonly adopted in overseas capital markets may give rise to other questions under both the *Corporations Law* and the *Trade Practices Act*. These include:

- whether trading in certain types of debt securities in particular circumstances prior to their issuance in the so-called "grey market" constitutes short-selling in contravention of section 846 of the *Corporations Law*[49] on the basis that the seller does not have a presently exercisable and unconditional right to vest the securities in the buyer;
- the use of fixed price re-offering arrangements may in certain circumstances breach the prohibitions in sections 45 and 45A on arrangements having the purpose, or likely to have the effect of, substantially lessening competition[50]; and

[47] Such stabilisation activities in the United Kingdom are only permitted by virtue of an express exemption from the prohibitions otherwise contained in the *Financial Services Act* 1986.
[48] See paragraph 2.3 above and sections 997, 998, 999 and 1000 of the *Corporations Law*.
[49] Sub-section (1) provides as follows: *Subject to this section and the regulations, a person shall not sell securities to a buyer unless, at the time of the sale (a) the person has or, where the person is selling as agent, the person's principal has; or (b) the person believes on reasonable grounds that the person has, or where the person is selling as agent, the person's principal has, a presently exercisable and unconditional right to vest the securities in the buyer.*
[50] In this context it is important to remember that an arrangement is deemed to have this effect if it has the purpose or likely effect of fixing, controlling or maintaining the price for services (including the sale of debt securities) to be supplied by parties to the arrangement in competition with each other.

- lock-up periods, restrictions on other issues and certain multiple party arrangements may infringe the exclusive dealing or third line forcing prohibitions in the *Trade Practices Act*[51].

Whilst current practices in the Australian debt capital markets are unlikely to result in such problems, it will be important to assess changing practices and procedures as a result of globalisation and other drivers of change against our competition laws. It should not be assumed that practices and procedures permitted in overseas markets will necessarily be permitted in Australia. For better or worse, I envisage that the Australian Consumer and Competition Commission (**ACCC**) will be a more important regulator in these markets in the future. Prediction number ten.

4.3 *A challenge for prudential and other regulation*

The are a number of prudential requirements which presently impact Australia's debt capital markets. I have already mentioned the restrictions which impact the investment of superannuation funds and the new controls on managed investment schemes contained in chapter 5C of the *Corporations Law*. Other controls impact the use of OTC and exchange traded derivatives by organisations subject to regulation by the Australian Prudential Regulation Authority (**APRA**).

In addition, there are the more formal prudential statements relating to capital adequacy, securitisation and market risk[52] which can impact the issuance of a wide range of debt securities.

Already in 1999, APRA has released for comment two Policy Discussion Papers. The first on the prudential supervision of conglomerates and the second on the capital-adequacy treatment of credit derivatives transacted by authorised deposit-taking institutions.. In the press release in relation to the Policy Discussion Paper relating to banking conglomerates it was stated:

> *As prudential supervisor of the bulk of financial institutions in Australia, APRA is vitally concerned with the quality of the systems used by those institutions to identify, measure and manage the various risks which arise in their business. Amongst other things, it seeks also to ensure that capital held by financial institutions is commensurate with risk arising from their business activities. Increasingly, however, both in Australia and internationally, financial services of all types are being offered not by single, stand-alone institutions but within conglomerate or group structures containing different types of financial institutions and activities, often with differing risk profiles.*[53]

These concerns are not unique to Australia and APRA's proposals reflect international concerns, especially concerning contagion (where problems in part of a conglomerate might be transmitted to another part, including through reputational and financial linkages), and organisational and structural risks.

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[51] Section 47.
[52] Prudential Statement C1 *Capital Adequacy of Banks* (particularly Attachment II in relation to hybrid (debt/equity) capital instruments), Prudential Statement C2 *Funds Management and Securitisation* and Prudential Statement C3 *Capital Adequacy of Banks: Market Risk*.
[53] Press release of 11 March 1999.

Once comments on the Policy Discussion Paper on credit derivatives have been considered, APRA plans to release final guidelines in the form of amendments to Prudential Statements C1 and C3.

APRA believes that the framework of prudential supervision must evolve with market developments and recognises some matters will need to be considered on a case-by-case basis. It would be a mistake to assume that prudential regulation going forward will be the same as in the past. I believe that the publication of these two Policy Discussion Papers indicates that APRA will take an active interest in innovations in the debt capital markets and that interaction with APRA will required as new products are developed and brought to the market. A more sophisticated regulatory regime. Prediction number eleven.

5 Technology

5.1 *Background comments*

The issue, distribution and trading of debt securities in Australia has traditionally relied on written documents and/or oral communications (roadshows and telephone calls). Many types of securities issued in the domestic markets must be in writing: a promissory note (or commercial paper) must be *an unconditional promise in writing*[54] Offering documents have traditionally been in writing and a prospectus under the *Corporations Law* must not only be in writing, but must be printed in a type of a size not less than eight point Times (unless the Australian Securities and Investments Commission (**ASIC**) certifies another size are legible and satisfactory)[55]. Even when electronic prospectuses have been permitted, they are essentially e-mailed copies of a document which must be available in hard copy[56].

Although the Australian markets have long been used to dematerialised book entry securities[57] and have developed electronic trading systems[58] in recent years, our markets are still dominated by the concept of writing and verbal communication. We now define 'writing' to include any mode or representing or reproducing words, figures, drawings or symbols in a visible form[59], but this only the beginning.

As we look forward, a telling figure is the increasing use of data transmission. In the United States, three years ago, voice traffic exceeded data. Today, data is approaching double the volume of voice and is forecast to be three times voice within five years. The cost of data transmission is in rapid decline, whilst at the same time functionality and reliability is rapidly increasing. We see this in the rapid growth of the Internet: if you have a computer, modem and telephone, you can and buy and sell international equities without the intervention of a stockbroker.

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[54] Section 89(1) of the *Bills of Exchange Act* 1909 (Commonwealth).
[55] Section 1021(1).
[56] ASIC Policy Statement 107 *Electronic Prospectus* and ASIC Class Order 96/1578
[57] Such as Commonwealth Government securities issued under the *Commonwealth Inscribed Stock Act* 1911 (Commonwealth).
[58] The Reserve Bank Information and Transfer System (RITS) and the Financial Transactions Recording and Clearance System (FINTRACS) for debt securities operated by the Reserve Bank of Australia and Austraclear Limited and the Clearing House Electronic Sub-register System (CHESS) for equities operated by a subsidiary of the ASX. See also Greg Hammond and Craig Wappett, *Dematerialised and Immobilised Securities* in *Australian Finance Law* (Fourth edition, LBC Information Services, 1999).
[59] See, for example, section 25 of the *Acts Interpretation Act* 1901 (Commonwealth) and the definition in section 9 of the *Corporations Law*.

What about our debt markets ?

5.2 *Electronic securities*

Recent years have seen the domestic medium term debt capital markets move (perhaps exclusively) to registered book entry securities by using deed polls or global debt securities to constitute each series of debt securities with the holders of particular debt securities being inscribed in a register. No physical securities are issued. However, money market debt securities are still issued in physical form.

Austraclear Limited has recently introduced a facility for the issue and trading of dematerialised debt securities within the Austraclear system. Such securities take the form of electronic bank accepted bills of exchange, electronic non-bank promissory notes or electronic bank and non-bank certificates of deposit. and by virtue of the contractual relationships established between the parties by the amended Austraclear Regulations and Operating Manual, such dematerialised debt securities are recognised in, and are capable of being traded utilising the Austraclear System in substantially the same manner as their physical counterparts[60].

Austraclear has obtained an exemption from ASIC which ensures that such dematerialisied debt securities are not subject to the prospectus provisions of the *Corporations Law* and a no action statement in relation to the possible conduct of an unauthorised stock market. I also understand that Austraclear will be seeking legislative recognition that certain types of dematerialised debt securities will be regarded as equivalent to their physical counterparts for the purposes of the *Bills of Exchange Act* 1909 (Commonwealth).

Dematerialised debt Securities will be enforceable in the same manner as the equivalent physical securities if they are uplifted in the manner prescribed by the amended Austraclear Regulations and Operating Manual. If it becomes necessary to draw, issue or make an equivalent physical security, for example because of a default in payment at the maturity date, the lodging Member of the relevant Dematerialised Security must do so. Unless and until a valid and complete equivalent physical security is brought into existence, the contractual rights arising by reason of the dematerialised debt security continue in full force and effect. This may have consequences concerning the manner of enforcement and the ability to enforce dematerialised debt securities.

This recent development is to be welcomed as the perceived benefits of the further dematerialisation of money market debt securities include printing, custodian, safe keeping, security, administration and audit expenses.

There is a now a real possibility that within the next two years physical certificates will cease to be issued for any debt securities issued in Australia. Prediction number twelve.

[60] It is important to note that such dematerialisied debt securities are not bills of exchange or promissory notes within the meaning of the *Bills of Exchange Act* 1909 (Commonwealth) or otherwise negotiable instruments under the law merchant. It will be important for issuers (particularly entities not incorporated under the *Corporations Law* to ensure that their constitutional documents permit them to issue such dematerialised debt securities.

5.3 *Electronic offering*

If correct, then the majority of issuers will be able to issue debt securities of any maturity in electronic dematerialisied form and such debt securities will be able to be traded within electronic trading systems and payment and settlement can be effected electronically[61].

Although specific exemptions from the prospectus provisions of the *Corporations Law* are required for electronic prospectuses, there is no reason why information memoranda and other offering documents for excluded issues and offers cannot be totally electronic. Issuers and investment firms could develop web sites or pages with hypertext links to an issuer's own world wide web site, the ASX's world web site, sites maintained by other stock exchanges, regulators and information providers which contain details about the issuer (for example, copies of SEC filings on the world wide web), other sites containing broker's research reports and other analysis about the issuer and other relevant sites.

Such sites or the details of any particular offer could be provided on the basis that only certain categories of investors could access the site (for example pre-registered institutional investors who are provided with a password) and/or the consideration payable in respect of any subscription of the debt securities could be not less than A$500,000. I believe that the liability issues arising from such an arrangement would be no greater (and possibly less) than exist under current market practices and procedures. Such an arrangement may be a much more effective way of providing comprehensive and meaningful information to potential investors.

My thirteenth prediction is that such a total electronic offering for an excluded issue will occur within the next two years.

5.4 *Securities depositaries and clearance*

Austraclear Limited has also responded to the drivers of change I have outlined by becoming a participant in the two dominant international securities clearance and settlements systems: the Euroclear System[62] and Cedelbank[63].

Amendments to Austraclear's Regulations and Operating Manual enable members to lodge, uplift and record transactions (including encumbrances and other security interests) in respect of entitlements to certain Australian dollar denominated debt securities issued in the Euromarkets. These entitlements reflect the property and contractual rights acquired under Belgian and Luxembourg law by Austraclear as a result of the relevant debt securities be held in Austraclear's securities accounts within the Euroclear System or Cedelbank, as the case may be[64]. It is anticipated that the Reserve Bank of Australia (**RBA**) will approve certain of these entitlements as eligible collateral for repurchase transactions in the domestic money markets.

[61] Using either the SWIFT Payment delivery System operated by the Australian Payments Clearing Association, the Reserve Bank Information and Transfer System (RITS) or Austraclear's FINTRACS system.

[62] Operated by Morgan Guaranty Trust Company of New York in Brussels.

[63] Based in Luxembourg.

[64] A useful introduction to, and discussion of, these rights is contained in Randall Guynn *Modernizing Securities Ownership, Transfer and Pledging Laws*, a discussion paper published by the Capital Markets Forum of the International Bar Association (1996).

At the moment these arrangements are limited to Australian dollar denominated debt securities and do not provide for two-way transfers of debt securities. Further linkages between Austraclear and international securities depositaries (not just the Euroclear System and Cedelbank) and/or the establishment of alternative securities clearance and settlement systems in Australia will occur in the coming years. My penultimate prediction.

5.5 *RTGS and beyond: continuous linked settlement*

In common with many countries around the world, Australia's payment system has changed significantly in recent years. The establishment of the Australian Payments Clearing Association in 1992, the introduction of new regulations and procedures for the exchange, clearing and settlement of both cheques and other paper based payment instructions and direct debits and credits, the move to a real time gross settlement system for high-value payments and the formation of the Payments Systems Board within the RBA as a result of the findings of the Financial System Inquiry are some of the changes.

In part, these changes have been a response to technological change, but it has been the result of a reform process which has sought to enhance the safety and integrity of the system. The overwhelming consensus is that this has been achieved at the domestic level, but the payment and settlements risks in cross-border and foreign exchange transactions remain.

A new reform process, continuous linked settlement, is under way in the United States and Europe to address these issues. In its initial phase, CLS will only apply to transactions involving two of US dollars, the Euro, pounds Sterling, Japanese Yen, Swiss francs and Canadian dollars. However, it is expected the Australian dollars will be covered by the arrangements in the second phase.

The interlinking of Australia's domestic payments system in a new global continuous linked settlement system may see changes to the number of foreign currency debt securities issued in Australia and the number of foreign investors willing to participate in our market for Australian dollar denominated debt securities. A final, but perhaps more speculative, prediction.

6 Prophecies revisited

In this paper, I have been bold enough to make fifteen prophecies about future developments in (i) the structure of the domestic debt capital markets, and (ii) the way in which debt securities are presently issued, distributed and traded in Australia. They were:

Market Structure	Over the coming years there will be an increasing convergence in Australia's debt and equity capital markets.
Globalisation	Domestic information memoranda and other offering documents and related dealer and programme agreements will include more extensive selling restrictions in relation to the securities laws of the United States and other foreign countries than has historically been the case.

	The risks in relation to information memoranda and other offering documents potentially being misleading and deceptive will be a more significant issue for issuers, directors, investment firms and advisers in the future.
	There will be a significant increase in the use of global medium term note and similar programmes by Australian corporate issuers in order to take advantage of a more liberal IWT regime.
	Australian debt capital markets are yet to fully experience and absorb the consequences of the third stage of EMU and, if adopted, the EU withholding tax directive.
Customer needs and demands	There will be greater consistency in disclosure and an overall raising of standards in information memoranda and other offering documents for excluded offers and issues in the next two years.
	Ratings will be less important in an overall sense in the future.
	A domestic private placement market will develop in the medium term.
	A failure by the ASX to provide an effective regime for listing debt securities will see a dominance of overseas listings for domestic debt securities.
Financial Innovation	The ACCC will be a more important regulator in the domestic debt capital markets in the future.
	APRA will take an active interest in innovations in the debt capital markets and that interaction with APRA will required as new products are developed and brought to the market.
Technology	There is a now a real possibility that within the next two years physical certificates will cease to be issued for any debt securities issued in Australia.
	A total electronic offering for an excluded issue of debt securities will occur within the next two years.
	Further linkages between Austraclear and international securities depositaries and/or the establishment of alternative securities clearance and settlement systems will occur in the coming years.
	The new global continuous linked settlement system may see changes to the number of foreign currency debt securities issued in Australia and the number of foreign investors willing to participate in our domestic markets.

I look forward with confidence that at least some of them will be fulfilled.

Concluding remarks

In some respects none of these predictions or prophecies are startling or novel, but collectively they represent a major challenge for our markets. Lawyers and other market participants will come of age if they see this challenge as an opportunity.

If the opportunity is grasped, then our profession will much more able to contribute to the development of Australia as a leading global financial centre and to the development of viable regional capital markets.