

The New Face of Securities Law

The Financial Markets Conduct Act 2013 ("FMC") was passed last year. It significantly changes the way securities (including shares, bonds and debt investments) have been offered in New Zealand for the last 35 years.

The FMC replaces various pieces of legislation including the Securities Act 1978 and Securities Markets Act 1988.

Understanding the new regime is particularly important for businesses offering investments and raising capital, investors, and financial and investment professionals.

Why is the law changing?

The principal objectives of the FMC are to facilitate capital market activity to help businesses grow, and promote confident and informed participation in the financial markets. The FMC seeks to do this by changing the way in which information on investment products is presented.

What changes?

There is a new disclosure regime under the FMC. Where an offer of securities is 'regulated' (similar to an existing offer to the public) a product disclosure statement ("PDS") must be prepared. The PDS will replace the prospectus and investment statement and is intended to be a more streamlined document focusing on the substance of the investment rather than form. The FMC also states when investments can be offered without a PDS, which allows for a more limited disclosure of information to an investor.

Because the FMC is being introduced in two parts (phase one will be introduced on 1 April 2014 and phase two on 1 December 2014) this article focuses on key exclusions in the FMC that enable investments to be offered without a PDS. These exclusions are expected to be introduced as part of phase one.

Key exclusions

A number of existing exclusions to the requirement for a prospectus and investment statement under the Securities Act have been clarified, which should provide greater certainty to those offering investments. An example is the introduction of a definition of a close business associate.

Some of the existing exclusions have had a significant shift in the financial requirements under the FMC, such as:

1. **Minimum Subscription:** The minimum subscription amount payable is being raised from \$500,000 to \$750,000.
2. **Wealthy to Large:** Under the current test an investor needed to have net assets of at least \$2 million or annual gross income of more than \$200,000 for each of the last two financial years. The new test, which measures both the investor and the entities controlled by the investor, requires at least \$5 million of net assets or turnover of at least \$5 million for each of the last two financial years. This significant shift in the threshold will mean this exclusion is used less often.
3. **Habitual Investor to Investment Activity:** The term 'habitually invests money' has been removed and replaced with the concept of meeting the investment activity criteria – which essentially requires the investor to have at least \$1 million invested in certain financial products.

There are also a number of new exclusions which businesses will be able to rely on:

1. **Employee Share Schemes:** The introduction of an Employee Share Scheme exclusion, rather than the present Exemption Notices. The exclusion restricts the number of shares issued under the scheme in any 12-month period to no more than 10 percent of the shares on issue. This is less restrictive than the current Exemption Notice, which has a limit on issue of five percent in any 12-month period in addition to a limit on the shares held by the pursuant to a share scheme of 15 percent of the ordinary shares of the company at any time.

2. **Small Offers:** The new concept of a 'Small Offer'. This involves an offer to persons connected with the company or that have an annual gross income of more than \$200,000 (for each of the last two years). Shares can be issued to investors where the company is raising up to \$2 million from not more than 20 investors (in a 12-month period) with restrictions around the type of investors who may be approached. Importantly in relation to small offers, they cannot be advertised.

There are a number of other exclusions including the transfer of a controlling interest, an issue where there is no consideration payable (e.g. bonus shares), dividend reinvestment plans and small management investment schemes.

Certification

Another positive for businesses raising capital is the introduction of a certification safe harbour for some exclusions, which will avoid the potential for investors to 'flip flop' on whether they fit within an exclusion. Self-certification is available for a 'wholesale investor' which includes those in the investment business, and who meet the investment activity criteria or are large. The certificate remains 'live' for two years. Businesses can rely on a certificate unless they know before issuing the securities that the applicant was not in fact a 'wholesale investor' at the time.

An investor can also certify in writing that they are an 'eligible investor' – someone that has previous experience in dealing with financial products that allows them to assess the merits of the transaction to obtain any information that they need. That certificate needs to set out the grounds upon which they rely in giving the certificate and must be confirmed by an authorised financial adviser, chartered accountant or lawyer. Once again, if the issuer knows that the investor does not have the requisite experience or that the relevant certifier was in some way associated with the issuer, then the certificate cannot be relied upon by the issuer.

Breaches

The FMC also introduces a wider range of potential penalties and civil remedies for breaches of the Act and generally increases the level of penalties able to be imposed against directors and issuers.

When do the exclusions apply?

The regulations, which are yet to be enacted, will clarify exactly which of the new exclusions will come into effect on 1 April 2014. The FMA has signalled that the exclusions relating to employee share schemes and small offers will be effective from then. This will give businesses offering investments a wider choice of exclusions from that date as some of the old exclusions still apply during the transition period. After 1 April 2014:

- **New Public Offers** – Issuers can choose to comply with the existing Securities Act and register prospectuses for new offers provided that they register by 1 April 2015 (1 April 2016 for continuous issuers). All offers must transition to the new regime by 1 April 2016. There is also a need for a statement in the prospectus to confirm the issuer's election.
- **New Non-public Offers** – Where no prospectus would be required under the Securities Act issuers can offer and allot securities before 1 April 2016 in reliance on some of those exceptions unless the issuer makes an election to comply with the FMC.

Further Information

Anderson Lloyd has been involved on behalf of clients in making submissions on various aspects of the new FMC regime throughout its development, and educating clients as to the effects of the new regime for their business. If you require further information please contact one of our partners with expert knowledge in this area – Anne McLeod, David Goodman, Ben Johnston or Paul Hubbard.

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