

AUSTRALIAN CORPORATE FUNDING THROUGH THE U.S. PUBLIC DEBT MARKET

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INTRODUCTION

The issue of public debt securities in the U.S. is a capital raising technique that offers significant benefits to Australian corporate borrowers, particularly in terms of the enormous depth of the market, (largely made up of institutional investors) and its flexibility. The U.S. capital market is very receptive to foreign securities and also welcomes new and innovative public financing vehicles. For example, corporate debt may be publicly issued in the U.S. with features that include the following:

- long-term unsecured debentures (15-20 years) with fixed interest rates and with comparatively few restrictive covenants;
- debentures issued in the U.S. in currency demoninations of the issuer's own country;
- variable rate debentures that float with certain designated interest rates and that are convertible into fixed rate notes at the option of the issuer;
- zero coupon note obligations that do not pay any current interest.

Recently, debt instruments of non-U.S. issuers with some of the features referred to above have been successfully sold in the U.S. public debt market by non-U.S. companies receiving less than an investment grade rating from the U.S. rating agencies.

The accessibility of the U.S. public debt markets to Australian issuers reflects three facets of the current deregulation of the Australian financial system:

- (1) the exemption of registered debentures publicly issued outside Australia from non-resident withholding tax;
- (2) the floating of the Australian dollar, and
- (3) the effective elimination of Australia's foreign exchange controls.

The fact that a public issue of securities in the U.S. triggers the disclosure requirements of the U.S. federal securities laws should not discourage Australian borrowers from entering the U.S. market. A properly advised Australian issuer should experience neither great difficulty nor inordinate expense in complying with the U.S. securities laws. Moreover, once a non-U.S. borrower is in compliance with the U.S. securities laws, subsequent debt issues may be made with even less difficulty and in a shorter time period.

STRUCTURING A U.S. PUBLIC SECURITIES ISSUE BY A NON-U.S. BORROWER

Non-U.S. companies generally structure U.S. securities issues in one of three ways:

A Direct Issue where the securities are issued by the non-U.S. company, solely on its own credit, directly into the U.S. market. An example of this is the 1983 sale by The Swan Brewery Company Limited in the U.S., through a public offering, of \$135 million aggregate principal amount of 14% per cent Limited Subordination Debentures due December 15, 1998, the first direct issue by an Australian company of securities in the U.S. registered under the U.S. Securities Act of 1933.

An indirect issue not guaranteed by the non-U.S. parent where the non-U.S. issuer either incorporates or acquires a U.S. subsidiary, which issues the securities. Where the parent does not guarantee the securities of its U.S. subsidiary, this structure relieves the non-U.S. company from the disclosure requirements of the federal securities laws. A recent example of this is the 1984 U.S. public issue of \$40 million of 15¼ per cent Subordinated Debentures due December 15, 1999 by The Higbee Company, a wholly-owned subsidiary of Industrial Equity Limited of Australia and Brierley Investments Limited of New Zealand. The primary purpose of the Higbee offering was to

refinance indebtedness incurred by certain IEL and BIL subsidiaries in connection with their acquisition of Higbee in 1984.

An indirect issue guaranteed by the non-U.S. parent: the indirect structure is also frequently used where the foreign parent guarantees the issue. An example of this is the 1983 \$400 million total U.S. public note issue by Midland American Capital Corporation, a wholly-owned subsidiary of Midland Bank plc ("Midland"). MACC was a newly incorporated U.S. company formed by Midland for the purpose of issuing the Securities. Because Midland guaranteed the Securities, which were unsecured, Midland was subject to the disclosure requirements of the U.S. securities laws and the prospectus reflects this by concentrating upon Midland. This structure was used to make the securities more attractive to U.S. investors by establishing a domestic U.S. offering entity. In addition, by incorporating a new company, rather than using its already existing U.S. banking subsidiary, Midland avoided extensive disclosure as to its pre-existing U.S. operations.

PRACTICAL ASPECTS OF A PUBLIC OFFERING OF SECURITIES IN THE U.S.

Underwriting

The initial step normally taken by any company, whether non-U.S. or U.S., considering issuing securities in the U.S. is the selection of a U.S. investment banker to coordinate the underwriting process and to serve as managing underwriter. Generally, the investment banker also implements a marketing strategy to create significant U.S. retail and institutional interest in the company and, following the offering, typically will be an active market maker in the company's securities.

After a proposed public offering is found to be feasible, its structure is determined. The underwriters generally agree to a "firm commitment" offering, in which they buy all the securities being offered.

Listing the Securities

Another early determination to be made in connection with an initial public offering is whether to list the issuer's securities for trading on a U.S. national securities exchange. There is no longer any significant disadvantage in not being listed on a national exchange, since the depth of the over-the-counter market has considerably increased, making it an important trading forum for both domestic U.S. and non-U.S. securities.

Principal Documents Required for a Public Issue of Securities in the U.S.

● **The Prospectus and Registration Statement**

The principal document required for a public offering in the U.S. is the prospectus, containing a detailed outline of the terms of the offering and the business and financial status of the issuer. The prospectus forms the core of the registration statement which generally contains a small amount of additional information. The registration statement is "wrapped" around the prospectus and filed with the U.S. Securities and Exchange Commission (the "SEC") in Washington, D.C. The SEC reviews the registration statement and if it complies with applicable federal law will declare it effective, at which time the securities may be sold to the public.

● **The Underwriting Agreement**

The underwriting agreement, a legally binding contract between the issuer and the underwriters, is signed prior to the registration statement becoming effective, and, subject to certain conditions, generally obligates the underwriter to buy the securities. The issuer is called upon by the underwriting agreement to make representations as to many aspects of its business, particularly those with direct legal consequences, and, additionally, to warrant the accuracy of the information contained in the registration statement. The issuer must also covenant to comply with various requirements of federal and state securities laws and formally agree to pay certain expenses. Finally, the underwriting agreement sets out the various conditions to the closing, such as the furnishing of specified opinions of counsel, letters from accountants and certificates of officers of the company.

Because of possible changes in market conditions and the extended length of the registration period, the exact price to be paid by the underwriters for the securities to be offered is generally not set until after the securities markets have closed on the day before the registration statement becomes effective. Thus, the issuer assumes the risk of changes in market conditions.

● **The Indenture**

In a public offering of debt securities, an issuer is required to qualify under the federal Trust Indenture Act of 1939 an indenture, the terms of which are negotiated with the underwriters and a trust company in the U.S., which will act as trustee under the indenture. The indenture will provide for, among other things, the following: terms of the debts, including any subordination, redemption and purchase

provisions; payments on debentures and exchange and transfer of debentures; covenants of the issuer, which may include limitations on future dividends and other restrictions; remedies of the trustee and debenture holders; rights and duties of the trustee; satisfaction and discharge of the indenture; and reports by the issuer and trustee to debenture holders.

Sensitivity of the Registration Process:

Once a company has determined to offer securities in the U.S. and begun to assemble a team to prepare the registration statement for filing with the SEC, that company is deemed to be "in registration". The U.S. federal securities laws prohibit any offer of securities until a registration statement has been filed with the SEC. Because the SEC considers every communication that has the effect of creating interest in the purchase of a security to be an offer, it is critical that a company maintain a low public profile while it is "in registration".

Issuers should also attempt to "stand still", to the extent practicable, during the registration process. Because a registration statement must convey all material information about an issuer's business up to the date of its use, material corporate transactions, such as acquisitions or dispositions of part of the issuer's business, that take place while the registration statement is being prepared may delay the registration process.

United States Jurisdiction

If a non-U.S. issuer has no presence in the U.S., it must appoint an agent for service of process in the U.S., submit to the jurisdiction of U.S. courts and waive objections to venue for actions brought in the U.S.

An Overview of the Requirements of the U.S. Federal Securities Laws

The core of the U.S. federal securities laws consists of two statutes, the Securities Act of 1933 (the "1933 Act") and the Securities Exchange Act of 1934 (the "1934 Act"). The 1933 Act regulates the offer and sale of securities by issuers and their affiliates to the public and requires registration of the offering unless an exemption is available. Unless an exemption is available, the 1934 Act imposes periodic reporting and other obligations on non-U.S. issuers

- (a) whose securities are registered on a U.S. national securities exchange, or

- (b) who have assets worth more than \$1 million and whose securities are held by more than 300 U.S. residents, or
- (c) who have publicly issued securities in the U.S.

The 1934 Act also regulates securities trading markets and broker-dealers and, together with the 1933 Act, is the source of authority for the SEC, the administrative agency charged with enforcing the federal securities laws.

The 1933 Act is the heart of the regulatory scheme governing the public offer and sale of any securities in the United States. The goals of the 1933 Act are, first, to provide full and fair disclosure of the character of securities sold so that investors may make investment decisions on a reasonably informed basis, and, second, to prevent fraud in the sale of securities. Thus, the 1933 Act does not regulate the nature of securities so long as issuers and other participants disclose to investors a specified range of material information relating to the offer and sale of securities to the public.

The concept of the 1934 Act disclosure requirements is to assure the regular public availability of adequate information about companies with publicly traded securities. The 1934 Act requirements are significant for two reasons. First, by making a public offering registered under the 1933 Act an issuer will be come subject to the periodic reporting requirements of the 1934 Act, at least for a short period of time. Second, the SEC has recently adopted a so-called "integrated disclosure system", for both domestic and non-U.S. issuers, which attempts to create consistency between the disclosure requirements of the 1933 Act and the 1934 Act and which allows a simpler registration process under the 1933 Act by permitting incorporation by reference of 1934 Act documents into 1933 Act filings. Thus, an issuer that has completed an initial U.S. public offering and has been complying with the reporting requirements of the 1934 Act for a specified period of time will be able to engage in additional public offerings of its securities with less extensive disclosure in the registration statement for the offering and in a shorter period of time.

THE 1933 ACT — REGISTRATION OF PUBLIC OFFERINGS

Registration Forms

In 1982, the SEC adopted special forms F-1, F-2 and F-3 for use by foreign private issuers, which are non-governmental entities incorporated outside the U.S. As a result of the abbreviated disclosures required in the registration statements of non-U.S. issuers who

qualify to use Forms F-2 and F-3, the time required and expense involved in preparing such offerings may be substantially reduced from those applicable to a Form F-1 filing. However, since Form F-1 is the basic SEC form requiring the widest range of disclosure, this article will only review the requirements of Form F-1.

Preparing a Form F-1 Registration Statement

● Description of Business

The heart of the narrative portion of a Form F-1 prospectus is the description of the issuer's business. This description must include:

- the general development of the issuer's business during the preceding five years;
- if the issuer has not received revenues for three full years, a business plan for a specified time period;
- the principal products produced and services rendered by the issuer;
- breakdowns of sales and revenues by categories of activity and geographical markets (with sales to unaffiliated customers shown separately);
- research and development activities; and
- capital expenditure commitments.

● Other Non-Financial Disclosure

Form F-1 also requires a description in the prospectus of, among others, the following:

- the location and general character of the principal physical properties of the issuer, directed primarily to whether such properties are suitable and adequate for the issuer's business;
- any material legal proceedings involving the issuer;
- the nature of the trading markets outside the U.S. for all classes of securities to be registered in the U.S., including high and low sales price data for the preceding two fiscal years;
- the intended use of the proceeds of the offering;
- the identity and background of the issuer's directors and officers, the identity of any controlling shareholders or holders of more than 10 per cent of the issuer's voting securities, and the voting securities held by all officers and directors as a group; and
- any material transactions between the issuer and its directors, officers, controlling shareholders and relatives of the foregoing.

Aside from these issuer-directed disclosures, Form F-1 requires disclosure of distinctive factors applicable to a non-U.S. issuer particular to its country or organization, including, among other things, the following:

- a history of exchange rates between the currency in which the issuer's financial statements are presented and the U.S. dollar;
- an explanation of any exchange controls or prohibitions that will impact the issuer's ability to pay interest or dividends to U.S. security holders in U.S. dollars (or prevent conversion into U.S. dollars);
- all taxes to which U.S. security holders will be subject under the laws of the country in which the issuer is organized;
- any political risks that may affect the issuer's operations outside the U.S.; and
- any distinctive non-U.S. law factors, such as a comparison of bankruptcy laws applicable to a non-issuer with U.S. bankruptcy laws where there are material differences.

Certain other information is required to be disclosed in the registration statement (but not in the prospectus), such as information on all sales of securities during the previous three years that were not registered under the 1933 Act. In addition, the issuer is required to file as exhibits to the registration statement numerous documents, including its articles of association and by-laws, material contracts, material foreign patents and instruments that define the rights of its security holders (e.g. indentures). The exhibits to the registration statements are also publicly available.

It should be noted finally that, in addition to the specified information required in a registration statement, a requirement applicable to every disclosure form promulgated by the SEC provides that a registrant must disclose any information that would be material to a potential investor.

● Financial Information

A prospectus must include the following financial information about the issuer, presented on a consolidated basis, including the parent company and all subsidiaries:

- two years' audited balance sheets;
- three years' audited income statements;
- five years' summary financial statements;

- a reconciliation of the issuer's financial statements to U.S. generally accepted accounting principles ("U.S. GAAP") and Regulation S-X, the SEC's financial disclosure rule; and
- a detailed and searching management discussion and analysis of the issuer's financial condition for three years and any interim periods for which financial statements are presented in the prospectus.

The reconciliation to U.S. GAAP must include a discussion of the material variations in U.S. and foreign accounting practices, principles and methods and must be quantified, both as to the income statement and balance sheet. All other information required by U.S. GAAP and Regulation S-X must be included in the issuer's financial statements, unless non-U.S. issuers are specifically exempted from any given requirement.

THE 1934 ACT — CONTINUOUS REPORTING REQUIREMENTS.

A non-U.S. issuer subject to the reporting requirements of the 1934 Act must make the following reports to the SEC:

Annual Reports: A non-U.S. issuer generally must file a registration statement on Form 20-F within six months after the end of the fiscal year in which it effects a public offering of its securities in the U.S. registered under the 1933 Act, and after the end of each subsequent year. The Form 20-F is a consolidated registration statement and annual report with requirements similar to the Form 10-K annual report used by domestic U.S. issuers, although significant disclosure accommodations in the Form 20-F have been made for non-U.S. issuers. Annual audited financial statements must be included in Form 20-F filings.

Interim Reports: Non-U.S. issuers subject to annual reporting obligations are not required to file interim reports on a regular basis as domestic U.S. issuers must, but are required to furnish reports on Form 6-K, an interim reporting form requiring disclosure of certain information (not previously furnished to the SEC) that is:

- (1) made public by the issuer under the laws of its domicile or country of incorporation,
- (2) filed with and made public by a non-U.S. securities exchange, or
- (3) distributed by the issuer to its security holders.

Form 6-K's are typically prepared by "wrapping" the cover of the form around the non-U.S. company's press release of any material development.

State Blue Sky and Legal Investment Laws

In addition to the requirements of the federal securities laws, non-U.S. issuers must comply with the registration requirements of the securities laws of each of the individual states "Blue Sky" in which their securities are to be offered for sale to the public.

In addition, "Legal investment" laws in the various states generally provide the standards that qualify corporate securities as eligible investments for certain institutional investors.

CONCLUSION

The United States debt capital markets offer a very large capital resource to Australian companies that has been made still more attractive by deregulation of the Australian financial system. As is demonstrated above, United States regulatory requirements should not discourage a properly advised Australian issuer from entering the American market. Moreover, once an Australian company is in compliance with the United States securities laws, subsequent issues may be made more quickly and with abbreviated disclosures.