

**THE SECURITIES ACT 1978 - POSSIBLE
AMENDMENTS**

A DISCUSSION PAPER

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Introduction

In accordance with its function under section 10(b) of the Securities Act 1978 the Securities Commission is undertaking a review of the provisions of the Securities Act 1978. This discussion paper sets out the Commission's preliminary suggestions for possible amendments to the Securities Act and raises some issues which the Commission considers should be addressed.

Definitions:

"Books and papers"

"Books and papers" or "books or papers" includes all books, accounts, rolls, files, vouchers, receipts, cheques, records, registers, papers, cards, documents, photographic plates, microfilms, photostatic negatives, prints, tapes, discs, computer reels, perforated rolls, and any other type of record whatsoever; and also includes all papers and other records relating to accounting operations and practice:

The term appears in section 18 and subsection 18A(4) of the Act, under which the Commission can compel the production of books and papers.

The Companies Act 1955 contains a similar definition of "books and papers". However the Companies Act 1993 omits the term and replaces it with a new comprehensive definition of 'document'

"Document" means a document in any form; and includes -

- (a) Any writing on any material; and*
- (b) Information recorded or stored by means of a tape-recorder, computer, or other device and material subsequently derived from information so recorded or stored; and*
- (c) A book, graph, or drawing; and*
- (d) A photograph, film, negative, tape or other device in which one or more visual images are embodied so as to be capable (with or without the aid of equipment) of being reproduced:*

This seems more serviceable than the term "books and papers" with its present definition.

Alternative definitions for the word documents can be found in overseas legislation, but they are substantially the same as the definition used in the Companies Act 1993.

We suggest that the term "books and papers" and "books or papers" be replaced wherever it appears in the Act with the word "document" and the definition of "document" contained in the Companies Act 1993 be inserted in the definitions.

"Chattel"

"Chattel" includes livestock

"Chattel" arises in section 5(1)(c) of the Act which provides that nothing in Part II shall apply in respect of "any proprietary right to chattels (other than any such right that forms part of a contributory scheme)".

It is unclear why livestock is expressly stated and whether any other chattels have the same legal character as livestock.

For the purposes of the Securities Act it may be appropriate to adopt part of the definition of chattel in the Chattels Transfer Act 1924 as follows:

"Chattels" means any personal property that can be completely transferred by delivery, and includes machinery, stock and the natural increase of stock as hereinafter mentioned, crops and wool and also includes book debts, but does not include -

- (a) Shares and interests in the stock, funds, or securities of any Government or local authority; or*
- (b) Shares and interests in the capital or property of any company or other corporate body.*

It is not immediately obvious whether "book debts" should be included in the definition of "chattel" for the purposes of securities law or whether alternative provision should be made in the Act for book debts. We invite comment on this matter.

"Crown" and "Government Department"

The Crown includes a Government Department. "Government Department" includes the Public Trustee and the Maori Trustee. The Crown is exempted from compliance with much of Part II of the Act. The Commission considers that the Public Trustee, an active issuer to the public, should no longer be exempted from compliance with Part II of the Act. The Maori Trustee under the Maori Trustee Act 1953 may at its discretion receive money for investment on behalf of any Maori. The Commission has not ascertained the extent to which the Maori Trustee offers securities to the public and the importance to him of the Securities Act exemption. We invite comment on the continuing need for the exemptions of:

- (a) the Public Trustee; and
- (b) the Maori Trustee.

"Debt security" and "Equity security"

"Debt security" means any interest in or right to be paid money that is, or is to be, deposited with, lent to, or otherwise owing by, any person (whether or not the interest or right is secured by a charge over any property); and includes -

- (a) *A debenture, debenture stock, bond, note, certificate of deposit, and convertible note;*
- (b) *Any renewal or variation of the terms or conditions of any existing debt security; and*
- (c) *Any security that is declared by the Governor-General, by Order in Council, to be debt security of the purposes of this Act;-*

but does not include an interest in a contributory mortgage where the interest is offered by a contributory mortgage broker:"

It would appear from this definition that all debt securities that are convertible into equity securities are intended to be considered debt securities for the purposes of this definition.

"Equity security" means any interest in or right to a share in the share capital of a company; and includes -

- (a) *A preference share, and company stock;*
- (b) *Any renewal or variation of the terms or conditions of any existing equity security; and*
- (c) *Any security that is declared by the Governor-General, by Order in Council, to be an equity security for the purposes of this Act:"*

The Securities Act does not state explicitly whether a contingent entitlement, including an option, constitutes an "interest" for the purposes of the definition of "equity security" (or, for that matter, for the purposes of the definition of "security" or of "debt security" or "participatory security"). We believe that option holders should have the benefit of the Act and this should be clearly stated.

A convertible security may be said to confer a contingent entitlement to an equity security, once the conditions of conversion are satisfied. However, this does not affect the primary character of the convertible note as a debt security and we do not propose a change to the definition of "debt securities" in this regard.

We invite comment on these two matters.

"Expert"

"Expert" means any person who holds himself out to be of a profession or calling that gives authority to a statement made by him; and includes an accountant, engineer, valuer, quantity surveyor; and geologist; but does not include a person acting in his capacity as an auditor or as a director or officer of a body:

The list in this definition is not particularly helpful. The listing of a few possible types of experts does not constitute a definition. If a geologist is mentioned what is the status of other persons practising in related descriptions? In any event the issuer is required to include the expert's statement of qualifications in the offer document. In the context of this disclosure a restrictive definition of expert does not seem necessary.

The following definition is suggested:

"Expert" means any person who holds himself or herself out to be of a profession or calling that gives authority to a statement made by that person; but this does not include a person acting in his or her capacity as an auditor or director or officer of a body

"Life insurance company"

"Life insurance company" means any person or association of persons, whether incorporated or unincorporated, which in the course of business issues, or is liable under, life insurance policies. "Life insurance policy" means a policy of life or endowment insurance and a policy securing an annuity.

These terms arise under section 7A which provides for the exemption of Life Insurance Companies from provisions of the Act. It is proposed that section 7A be repealed (see discussion under sections 7A and 7B). Whether or not this occurs it may be necessary to retain this definition to accommodate the Working Group proposals on disclosure by life insurance companies.

"Local authority"

"Local authority" means a body that is a local authority for the purposes of Part I of the Local Authorities Loans Act 1956:

The definition of 'local authority' in the Local Authorities Loans Act contains includes:

"any other public bodies as are from time to time declared by any other Act or by the Governor-General, by Order in Council, to be local authorities for the purposes of this Act"

To determine whether a particular public body is a local authority for the purposes of the Local Government Loans Act requires a search for declarations that a body is a local authority for the purposes of any other Act or any Order in Council.

The Local Government Act 1974 contains an up-to-date list of all local authorities in the First Schedule. Amending the definition of 'local authority' to mean an entity which is "a local authority for the purpose of the Local Government Act 1974" would be simpler.

It may be observed, however, that the Local Government Reform Bill, currently before Parliament, provides for the revocation of the exemption contained in section 5(3)(b) of the Securities Act for local authorities. If this Bill is passed in its present form then there will be no need for the definition of "local authority". This has been brought to the attention of the Select Committee considering that bill

"Manager"

"Manager", in relation to a participatory security, means the person or persons acting in the promotion or management of the arrangement or scheme to which the security relates

The definition of manager in the Securities Regulations 1983 is different:

"Manager", in relation to a participatory security, means the person or persons acting in the management of the scheme to which the security relates.

The Act refers to "the promotion or management" of a scheme. The Regulations refer only to "the management". It may be necessary to distinguish between a "manager" who is a promoter of the offer of securities and a manager who is responsible for the day to day management of the ongoing business. Sections 51 to 54 of the Act contain provisions relating to the administrative duties of issuers. There are generally on-going duties which a promoter may not be involved with. Sections 55 to 66 outline the liability of issuers. A promoter who is not the continuing manager will be a party to the preparation of the prospectus and should be liable for misstatements. However, he or she may have no continuing responsibility for the ongoing business. The continuing manager, conversely, may have had no involvement in the offer of securities but may be responsible for the ongoing management of the business including attending to some or all of the matters referred to in sections 51 to 54.

The Commission believes it may be necessary to amend the definitions of "manager" and "promoter" to address this problem. We seek comments on this.

"Promoter"

"Promoter" in relation to securities offered to the public for subscription,-

- (a) Means a person who is instrumental in the formulation of a plan or programme pursuant to which the securities are offered to the public; and*
- (b) Where a body corporate is a promoter, includes every person who is a director thereof; but*
- (c) Does not include a director or officer of the issuer of the securities or a person acting solely in his professional capacity*

It has been suggested that (b) should include "principal officer" rather than "director". The definition of principal officer in the Act includes a director, and also a person in accordance with whose directions or instructions any or all of the directors of the body are accustomed to act. The definition of principal officer is as follows:

"Principal officer" in relation to a body corporate or other body, means-

- (a) A director of the body; or*
- (b) A person in accordance with whose directions or instructions any or all of the directors of the body are accustomed to act; or*
- (c) In relation to any particular requirement of this Act, any person whose function*

it is, or who has undertaken, to ensure that that requirement is complied with by the body:

Provided that for the purposes of the Act, a person shall be regarded as a person in accordance with whose directions or instructions any or all of the directors of a body are accustomed to act by reason only that the directors act on advice given by him solely in a professional capacity

Promoters can incur civil liability under section 56 and criminal liability under sections 58 and 59 of the Act. It seems that a person in accordance with whose directions the directors act should also be subject to liability if it arises as a result of their instructions to the directors. We suggest that paragraph (b) of the definition of "promoter" be amended by replacing the word "director" with the word "principal officer".

It is said to be unclear whether the words '*acting solely in his professional capacity*' in paragraph (c) of the definition of "promoter" are meant to carry back to the words "director or officer". Directors of the issuer already have disclosure obligations under the Act. The inference may be drawn that the words "acting solely in his professional capacity" are not intended to carry back to directors or officers. Inserting a comma after the word 'securities' would clarify this point.

"Qualified Auditor"

"Qualified Auditor" means a member of the New Zealand Society of Accountants who holds a certificate of public practice, the Audit Office, or a member, fellow, or associate of an association of accountants constituted outside New Zealand who is for the time being approved for the purposes of this Act by the Minister by notice in the Gazette:

Provided that -

(a) None of the following persons shall be qualified for appointment as auditor of the accounting or other records of an issuer of securities:

(i) The issuer, or a principal officer, officer, or employee of the issuer:

(ii) A person who is a partner of or in the employment of a person specified in subparagraph (i) of this paragraph:

(iii) A body corporate:

(b) A person shall not be qualified for appointment as auditor of an issuer of securities if he is by virtue of paragraph (a) of this proviso, disqualified for appointment as auditor of any person that is the issuer's subsidiary or holding company or a subsidiary of the issuer's holding company, or would be so qualified if that person were a company:

The following definition, based on the format of section 199 of the Companies Act 1993, would be more orderly:

"Qualified Auditor" means a person who is-

(a) A member of the New Zealand Society of Accountants who holds a certificate of public practice; or

(b) An officer of the Audit Department authorised in writing by the Controller and Auditor-General to be an auditor of a company for the purposes of this section; or

(c) A member, fellow, or associate of an association of accountants constituted outside New Zealand where both the member, fellow, or associate and the association are approved for the time being for the purposes of this section by the Minister of Justice in the Gazette

and does not include a person who is-

(d) An issuer, or a principal officer, officer, or employee of the issuer:

(e) A person who is a partner, or in the employment, of a issuer, principal officer, officer, or employee of the issuer:

(f) A body corporate:

(g) A person who by virtue of paragraph (a) or paragraph (b) of this subsection, may not be appointed or act as auditor of a related company of the issuer.

(h) Any other person who has a material interest in the affairs of the issuer.

Section 3 - Construction of references to offering securities to the public

This section has not always been easy to apply in practice and the precise boundaries of what constitutes "the public" in any given situation have not always been clear. There is now a good deal of case law on the subject but the decisions of the courts are in some respects contradictory. Suggestions have been made to us from time to time that section 3 needs to be reviewed. However, we are engaged in proceedings in the Court of Appeal on this subject at the present time, in the *Kiwi Co-operative Dairies Limited* litigation. We propose to review the position when this litigation is completed.

It has been suggested that in subsection (2)(a) the conjunction of "relatives" and "close business associates" may cause interpretation problems. Subsection (2)(a) provides that :

3(2) [When not an offer] None of the following offers shall constitute an offer of securities to the public:

(a) An offer of securities made to any or all of the following persons only:

(i) Relatives or close business associates of the issuer:

(ii) Persons whose principal business is the investment of money, or who, in the course of and for the purposes of their business, habitually invest money:

(iii) Any other person who in all the circumstances can properly be regarded as having been selected otherwise than as a member of the public:

"Relative" is defined as having the same meaning as in the Income Tax Act 1994, namely:

"Relative"-

(a) Except in the international tax rules, in relation to any person, means any other person connected with the first-mentioned person by blood relationship, marriage, or adoption; and includes a trustee for a relative;...

"Close business associate" is not a defined term and therefore may need to be interpreted in the context of the object and scheme of the Act.

The two terms are not closely related, notwithstanding that they are grouped together. It is suggested that subsection (2) be amended by listing the two terms separately.

We are at present considering the adequacy of subsection (3), in particular the classes of persons identified in it.

Section 4 Application of this Act

4(1) [Application] The provisions of this Act shall have effect notwithstanding anything to the contrary in any other enactment or in any deed, agreement, application, prospectus, registered prospectus, or advertisement.

4(2) [Void requirements] A condition of any agreement requiring or binding an applicant for securities to waive compliance with any requirement of this Act, or purporting to affect him with notice of any contract, document, or matter relating to the securities that is not specifically referred to in a prospectus or registered prospectus, shall be void.

Section 7(1) of the Illegal Contracts Act 1970 confers wide discretions on the Courts to grant relief to the parties to an illegal contract including, but not limited to, validation of the contract. Section 7(1) of the Illegal Contracts Act is, however, expressed to be "subject to the express provisions of any other enactment". In *Re AIC Merchant Finance Ltd* it was held that section 4 of the Securities Act precludes section 7(1) of the Illegal Contracts Act from being used to validate an allotment which is invalid under section 37(4) of the Securities Act. It was also held, however, that section 4 of the Securities Act does not preclude other forms of relief under section 7(1) of the Illegal Contracts Act.

The Commission is presently engaged in proceedings in which one of the issues concerns the application of the Illegal Contracts Act to a contract to allot securities (*Westpac Financial Services Ltd v Securities Commission*). We propose to review the position when this litigation is completed. However our present preference is that the Court should have power to validate an allotment.

Section 5(1)(e) Exemption for a Professional Company

5(1) Nothing in Part II of this Act shall apply in respect of -

(e) Any interest or right to participate in the capital, assets, earnings, royalties, or other property of any company, partnership, or other person whose sole undertaking is the practice, conduct, or operation of any one or more of the professions, occupations, or businesses that may in law be practised, conducted, or operated only by persons having or possessing qualifications specified in the Second Schedule to this Act;

Review of this subsection is desirable for three reasons. First, as it is presently drafted it is not clear whether there is a limitation on persons to whom the company or partnership may make an offer of securities. The intent of the section is to limit investment in such enterprises to persons practising the same profession or occupation as those persons offering the security.

Secondly, as a matter of law, corporations are not able to practise many professions and this may prove an inappropriate restriction on the use of the exemption

Thirdly, it may be desirable to extend the application of this exemption and for this purpose to review the Second Schedule to the Act.

Section 5(3) [Further exemptions]

Nothing in sections 33(2), 33(3), 34 to 37, 37A, 39 to 44, 44B to 54, and 57A to 69 of this Act shall apply in respect of any security the issuer of which is -

- (a) The Crown; or*
- (b) A local authority; or*
- (c) The National Provident Fund Board established by the National Provident Fund Act 1950;*
- (d) The Reserve Bank of New Zealand constituted under the Reserve Bank of New Zealand Act 1964; or*
- (e) The Housing Corporation of New Zealand established by the Housing Corporation Act 1964;*

Subsection (3) exempts the Crown and certain other issuers from the need to issue a prospectus, to have a trust deed for debt securities, to have a deed of participation for participatory securities, and certain other provisions. The exemption for the Rural Bank is no longer justified, since its privatisation. The National Provident Fund and the Housing Corporation are now corporatised, and none of their new securities will be Government guaranteed. Arguably these bodies should not enjoy an exemption under this subsection. It should be noted that if the Local Government Law Reform Bill is passed in its present form local authorities will lose their present exemption.

Section 7A [Exemption for life insurance companies] and Section 7B [Terms and conditions of authorisation]

The Working Group on Improved Product and Investment Advice Disclosure is currently reviewing Life Insurance disclosure requirements. The Working Group is expected to recommend that prospectuses be required in respect of the offer of life insurance policies that are offered to the public. Consequently sections 7A and 7B may be repealed.

Sections 15 & 16 Meetings of Commission and Assent to Resolution without a meeting

15(1) [Convening] Subject to this section, the Chairman shall convene such meetings of the Commission as he thinks necessary for the efficient performance of the functions assigned to it.

15(2) [Meeting Places] Meetings of the Commission shall be held at such places as the Chairman determines.

15(3) [Chairman presides] The Chairman shall preside at all meetings of the Commission at which he is present.

15(4) [Chairman absent] In the absence of the Chairman from any meeting the members shall appoint one of their number to be the chairman for the purposes of the meeting.

15(5) [Quorum] At any meeting of the Commission, the quorum necessary for the transaction of business shall be 3 members.

15(6) [Votes] All questions arising at any meeting of the Commission shall be decided by a majority of votes of the members present and voting. The presiding member shall have a deliberative vote and, in the event of an equality of votes, shall also have a casting vote.

15(7) [Procedures] Subject to the provisions of this Act, the Commission may regulate its procedure in such manner as it thinks fit.

An additional subsection should be included to empower the Commission to meet by telephone. A conference telephone meeting will save time and money if a physical quorum is not available, particularly when a meeting is called at short notice or is expected to be of short duration. The following proposed amendment to subsection (2), based upon the wording of clause 3 of the First Schedule to the Companies Act 1993, is suggested. It allows for tele-conferences and other types of communication technology that may become available to the Commission in the future:

15(2) Meetings of the Commission shall be held either-

(a) By a number of Members, who constitute a quorum, being assembled together at a place, date and time appointed for the meeting by the Chairman; or

(b) By means of audio, or audio and visual, communication by which all Members participating and constituting a quorum can simultaneously hear each other throughout the meeting.

The Commission has encountered circumstances where a meeting validly commenced with a quorum of three has been unable to complete its business due to the illness or unavoidable incapacity of a Member or to the completion of the term of office of a Member. From time to time it may be convenient to arrange for an additional Member to join the quorum. However, this will not be practical where the enquiry has been substantially but not wholly heard and the additional Member will not be eligible to participate in any decision in accordance with the rules of natural justice unless the quorum rehears the evidence. The following wording may be appropriate to meet this type of situation-

15(5A) In the course of any inquiry or proceedings of the Commission which has commenced with a quorum of at least three members but is reduced to less than three members due to the illness or unavoidable incapacity of a Member or the expiry of the term of a Member, the two remaining Members may constitute a quorum for the purposes of concluding the inquiry or proceedings including receiving any evidence or making any decision in relation to the inquiry or proceedings.

Section 16 provides as follows:

16 A resolution in writing signed, or assented to by letter, telegram, cable or telex message by all the members of the Commission shall be as valid and effectual as if it had been passed at a meeting of the Commission duly called and constituted.

This provision is designed to enable the Commission to act speedily. It is not routinely possible to obtain the assent of all the members of the Commission. It may be more practical if the section is amended to provide that the quorum of three people is sufficient. Provision should also be made under section 16 for resolutions assented to by facsimile to be valid and effectual.

It may be desirable to include a proviso that neither the proposed sections 15(2)(b) and 15(5A) nor the proposed extension of section 16 apply in respect of decisions taken under sections 44(1)(b), 44A, 44B(2) and 69 where it is particularly important to be able to demonstrate that the rules of fairness, as appropriate, have been observed.

Section 19 Provisions relating to certain proceedings before the Commission

19(3) [Public Meeting] Except as provided by subsections (4) and (5) of this section, every meeting of the Commission for the purposes of section 69 of this Act shall be held in public.

19(4) [Private deliberations] The Commission may deliberate in private as to its decisions in any matter or as to any question arising in the course of any proceedings before it.

19(5) [Order prohibiting publication] The Commission may, of its own motion or on the application of any party to the proceedings, -

(a) Order that any proceedings or any class of proceedings held by it be heard in private, either as to the whole or any portion thereof;

(b) Make an order (which may be expressed to have effect from the commencement of any inquiry or other proceedings of the Commission to the determination of such inquiry or proceedings) prohibiting -

(i) The publication or communication of any information or document or evidence which is furnished or given or tendered to, or obtained by the Commission in connection with that inquiry or those proceedings:

(ii) The giving of evidence involving any such information, document, or evidence.

19(6) [Application of Official Information Act] Notwithstanding anything in subsection (5)(b) of this section, at the conclusion of any inquiry or proceedings of the Commission, the provisions of the Official Information Act 1982 shall apply in respect of any information or document or evidence that was the subject of an order made under subsection (5)(b) of this section.

An additional provision to section (5)(b) could be inserted stating explicitly that the Official Information Act does not apply where, a section 19(5) order applying, the enquiry has not yet concluded.

Section 20 Employees of Commission

(1) Subject to the provisions of this section, the Commission may from time to time appoint such officers and employees, including acting or temporary or casual officers and employees, as it thinks necessary for the efficient carrying out of its functions, powers, and duties under this Act or any other enactment.

(2) The number of officers and employees who may be appointed under subsection (1) of this section, whether generally or in respect of any specified duties, shall from time to time be determined by the Minister.

(3) Officers and employees appointed under subsection (1) of this section shall be paid such salaries and allowances as the Commission from time to time determines in agreement with the State Services Commission, or as the Minister from time to time determines in any case where the Commission and the State Services Commission fail to agree.

(4) Any determination under subsection (3) of this section shall take effect on such date (whether the date thereof or any earlier or later date) as may be specified therein. If no date is so specified the determination shall take effect in the date thereof.

The Minister's power to approve employees appears to be unnecessary and has occasionally caused undue rigidity for limited periods. For all practical purposes the number of officers and employees appointed is determined according to the money available to fund the Commission. The Members of the Commission are well qualified to determine the expenditure priorities of the Commission on an ongoing basis.

Section 20 (2) might conveniently be revoked.

The State Services Commission no longer approves salaries and allowances of staff of Crown Agencies as a routine function. The State Services Commission considers that the Members of the Securities Commission are well able to settle these matters, within the context of determinations by the Higher Salaries Commission, in relation to the remuneration of the Chairman and other Members. The State Services Commission's role under subsection (3) might be redefined, for example, as a power of review, one more consistent with its more general role under the State Sector Act 1988.

Section 23 Application of Certain Acts to Members and Staff of the Commission

No person shall be deemed to be employed in the service of Her Majesty for the purposes of the State Services Act 1962 or the Government Superannuation Fund Act 1956 by reason of his appointment as a member of the Commission, or an officer or employee of the Commission, or a person appointed by the Commission under section 21 of this Act.

The State Services Act 1962 was repealed and replaced by the State Sector Act 1988. A reference to the new Act is needed.

Section 27 Delegation of powers by Commission

(1) The Commission may from time to time, by writing under the hand of the Chairman, delegate to any person any of the Commission's powers under this Act or any other enactment, except this power of delegation and the powers conferred by section 5(5), 44, 44A, 44B(2), 67, 69 of this Act.

This section is awkwardly drafted and contains an ambiguity. An equivalent section is set out more clearly in section 23 of the State Sector Act which states:

23. Delegation of functions or powers - (1) The Commission may from time to time, either generally or particularly, delegate to any of its members or to any other person or persons any of its functions or powers, including functions or powers delegated to the Commission under any Act.

(2) Every delegation under this section shall be in writing.

(3) No delegation under this section shall include -

(a) The power to delegate under this section; or

(b) The Commission's powers under section

It is suggested that the section 27 power of delegation be reworded and that the reference to section 67, Registrar's Powers of Inspection, should be deleted from this section and hence this power could be delegated.

Section 28 Proceedings Privileged

28(1) [No liability] No proceedings, civil or criminal, shall lie against the Commission for anything it may do or fail to do in the course of the exercise or intended exercise of its functions, unless it is shown that it acted in bad faith or without reasonable care.

28(2) [Exception] Subject to subsection (3) of this section, no proceedings, civil or criminal, shall lie against any member of the Commission for anything he may do or say or fail to do or say in the course of the operation of the Commission, unless it is shown that he acted in bad faith.

28(3) [Exception] No proceedings, civil or criminal, shall lie against any member of the Commission for anything he may do or say or fail to do or say in the exercise or intended exercise of any function under section 10(c) of this Act in relation to any inquiry by the Commission into a particular transaction, activity, or practice, unless it is shown that he acted in bad faith or without reasonable care.

28(4) [Evidence] No member of the Commission, or officer or employee thereof, or person appointed under section 21 of this Act, or person to whom a power of the Commission has been delegated under section 27 of this Act, shall be required to give evidence in any Court, or in any proceedings of a judicial nature, in respect of anything coming to his knowledge in the course of the operations of the Commission.

28(5) [Exceptions] Nothing in subsection (1) to (4) of this section applies in respect of proceedings for -

(a) An offence against section 78 or section 78A(1) or section 105 or section 105A or section 105B of the Crimes Act 1961; or

(b) The offence of conspiring to commit an offence against section 78 or section 78A(1) or section 105 or section 105A or section 105B of the Crimes Act 1961; or

(c) The offence of attempting to commit an offence against section 78 or section 78A(1) or section 105 or section 105A or section 105B of the Crimes Act 1961

28(6) [Privileged information] Anything said or any information supplied or any book or paper produced by any person in the course of any proceedings before the Commission shall be privileged in the same manner as if the proceedings were proceedings in a Court.

28(7) [Deemed official report] For the purposes of clause 3 of Part II of the First Schedule

to the Defamation Act 1992, or any report or comment made by the Commission in the course of the exercise or intended exercise of its functions shall be deemed to be an official report made by a person holding an inquiry under the authority of the Parliament of New Zealand.

At present no civil or criminal proceedings may be brought against members of the Securities Commission unless it is shown that the Commission acted in bad faith or without reasonable care. However, the nature of any liability of the Commission, where it is alleged that the Commission has failed to act with reasonable care, is not stated. It seems undesirable that the Commission and equivalent Crown agencies should be impeded in their work by the threat of a negligence action. There are already adequate procedures for administrative review where there is reason to believe that the Commission has acted unfairly or outside the terms of the statute. Equivalent organisations overseas are immune from actions in negligence. Specifically, we propose amending subsection 28(1) by deleting the words "or without reasonable care". This would result in the Commission being liable for actions only when it acted in bad faith. Similarly, the words "without reasonable care" in subsection 28(3) should be deleted.

There is no immunity for employees of the Securities Commission in subsections 28(2) and (3). These provisions should extend to staff of the Commission.

Section 28(6) will also have to be amended if the term "book or paper" is replaced with "document" as is proposed.

Section 28A Commission may publish reports

28A(1) [Authorised to publish reports] Subject to subsection (2) of this section the Commission may publish any report or comment made by the Commission in the course of the exercise or intended exercise of its functions.

28A(2) [Exception] Notwithstanding subsection (1) of this section, the Commission shall not publish any report containing a recommendation made by it under section 10(b) of this Act.

It is suggested that section 28A(2) should be repealed. The relative concerns and interests of the Minister, the Commission and the general public can, we think, be addressed quite satisfactorily under the Official Information Act.

Section 31B Bank Accounts

(1) The Commission shall open at any bank or banks such accounts as are necessary for the exercise of its functions and powers.

(2) All money received by the Commission, or by any employee of the Commission shall, as soon as practicable after it has been received, be paid into such accounts of the Commission as the Commission from time to time determines

(3) The withdrawal or payment of money from any such account shall be authorised by a prior resolution of the Commission, or shall be submitted to the commission for confirmation at its first ordinary meeting after the date of payment.

(4) The withdrawal of payment of money from any such accounts shall be by cheque signed by such person or persons as the Commission may from time to time authorise.

Section 31B(3) sets down a restrictive procedure for obtaining approval for withdrawals or payments from the Commission's bank accounts. It is not always possible to ensure confirmation at the first ordinary meeting after the date of payment, especially if the responsible employee is absent or ill. If the procedure was relaxed slightly by changing the confirmation from the 'first ordinary meeting' to, for example, 'as soon as practicable' there would be flexibility albeit while still ensuring Commission members are able to supervise expenditure in accordance with the policy of the Act. Section 31B(4) provides for withdrawal of money by cheque only. This should be reviewed

Section 31C Accounts and audit

The Public Finance Act 1989, Part II Banking And Investment has now superseded the relevant sections of the Public Finance Act 1977. The reference to the Public Finance Act in section 31C(1) should be redated.

Section 32 Offences

Every person commits an offence and is liable on summary conviction to a fine not exceeding \$1,000 who -

- (a) Having been summoned to appear before the Commission for the purposes of any matter, refuses or wilfully neglects to appear before the Commission in pursuance of the summons, or to take an oath or make an affirmation as a witness, or to answer any question put to him concerning the matter, or to produce to the Commission any book or paper that he is required to produce; or*
- (b) Deceives or attempts to deceive or knowingly misleads the Commission on any evidence given or otherwise proffered to it; or*
- (c) Acts in contravention of any order made by the Commission under paragraph (b) of section 19(5) of this Act;*

Section 111 of the Crimes Act states :

111. False statements or declarations - Every one is liable to imprisonment for a term not exceeding 3 years who, on any occasion on which he is required or permitted by law to make any statement or declaration before any officer or person authorised by law to take or receive it, or before any notary public to be certified by him as such notary, makes a statement or declaration that would amount to perjury if made on oath in a judicial proceeding.

Section 111 of the Crimes Act prescribes a more severe penalty for actions which are substantially the same as those to which section 32(b) of the Securities Act applies.

There are significantly higher fines prescribed under the Companies Act for offences which are similar to those in the Securities Act. For example, under section 365 of the Companies Act

1993 it is an offence to obstruct or hinder the Registrar or a person authorised by the Registrar in exercising powers of inspection. It will result in a fine of up to \$10,000 where a similar action under section 32(b) of the Securities Act would result in a fine of up to \$1,000.

A review of the penalties in the Securities Act appears appropriate.

Section 34 Restrictions on Distribution of Prospectuses

*34 No registered prospectus shall be distributed by or on behalf of an issuer, -
 (a) After it has been amended unless all the amendments have been incorporated in every copy of the registered prospectus that is so distributed;*

There is doubt whether this section requires the registered prospectus to be redone or a memorandum of amendments to be attached to it. The use of the word 'incorporate' suggests the first. However, this may be inappropriate if the amendments are brief. We query whether it is necessary to specify the procedures for amending a registered prospectus in the law provided that the memorandum has been registered, the amendment is in a permanent form, is contained in or attached to the prospectus and is comprehensible in the context of the prospectus as a whole.

Section 37 Void Irregular Allotments

37(1) [Registered prospectus required] No allotment of a security offered to the public for subscription shall be made unless at the time of the subscription for the security there was a registered prospectus relating to the security.

37(2) [Minimum subscription] No allotment shall be made of an equity security or a participatory security offered to the public unless the amount stated in the registered prospectus relating thereto as the minimum amount which, in the opinion of the directors of the issuer, must be raised by the issue of the securities in order to provide for the matters specified in regulations made under this Act, is subscribed and that amount is paid to, and received by, the issuer within 4 months after the date of the registered prospectus; and, for the purposes of this subsection -

(a) A sum shall be deemed to have been paid to, and received by, the issuer if a cheque for that sum is received in good faith by the issuer and the directors of the issuer have no reason to suspect that the cheque will not be paid;

(b) The amount so stated in the registered prospectus shall be reckoned exclusively of any amount payable otherwise than in cash.

37(3) [Written authorisation] No allotment of a participatory security offered to the public for subscription shall be made unless, at the time of allotment the statutory supervisor holds a written statement signed by the subscriber authorising the subscription for that particular security.

There has been confusion over an apparent inconsistency between sections 37(3) and 37A(1)(b). Section 37A(1)(b) makes an allotment void if the issuer of the securities does not hold, in respect of the security, a form of application that is both properly completed and signed by or on behalf of the subscriber. Section 37(3) makes an allotment void if at the time of allotment the Statutory

Supervisor does not hold a written statement signed by the subscriber authorising subscription for the security. Generally, the only written statement of the subscriber is the form of application.

The Commission's preference is to repeal section 37(3). This appears consistent with the basic policy that a statutory supervisor's role is to supervise, not to manage, the process of allotment of securities.

37(4) [Invalid allotments] Any allotment made in contravention of the provisions of this section shall be invalid and of no effect.

37(5) [Trust account] Where subscriptions for securities are received by or on behalf of an issuer, but, by virtue of this section, the securities may not be allotted, or for any reason the securities are not allotted, the issuer shall ensure that -

(a) At all times while held by it, the subscriptions are kept in a trust account on behalf of the subscribers; and

(b) The subscriptions, together with such interest (if any) as has been earned thereon, are repaid to the subscribers as soon as reasonably practicable.

Section 37(5) imposes a requirement that, where the securities may not be allotted, the subscription money must be kept in a trust account. The Commission has a policy preference to extend the policy of this section to all subscription moneys by establishing a positive obligation on all issuers to keep all subscription moneys in a trust account immediately upon receipt where they are to be held pending allotment.

The Act does not specify what constitutes a trust account. It seems necessary to include a definition of a trust account. A trust account should, we think, possess the following characteristics:

- The account will be separate from all other accounts of the issuer and the moneys therein will be used for the sole purpose of the trust;
- The terms of acceptance and dealing with the funds in the account will be such as raise the presumption that those funds do not belong to the issuer;
- The bank at which the trust account is maintained will be informed that it is a trust account and that any rights of the third party against the issuer will not apply against funds in the trust account.

37(6) [Liability for repayment] If any subscriptions to which this section applies are not so repaid within 2 months after the date on which the subscriptions were received by or on behalf of the issuer (or, in any case to which subsection (2) of this section applies, within 5 months after the date of the registered prospectus), the issuer and all the directors thereof shall be jointly and severally liable to repay the subscriptions, together with interest at the rate of 10 percent per annum from the date on which the subscriptions were received by or on behalf of the issuer:

Provided that a director shall not be so liable if he proves that the default in the repayment of the subscriptions was not due to any misconduct or negligence on his part.

The Law Commission proposes to replace the words "at the rate of 10% per annum" in sections 37(6), 37A(7) and 44(7) with the words "at the same rate and on the same terms as are provided for the award of interest underthe Interest on Money Claims Act 1994" The Commission is

of the view that the Law Commission's proposed amendments are appropriate.

Section 38 Authorised Advertisements

38 In this Act the term 'authorised advertisement' means an advertisement that -

- (a) Refers to a registered prospectus that relates to all the securities referred to in the advertisement, and states the date of registration thereof; and*
- (b) States that allotments of the securities shall be made only on receipt of a form of application forming part of, or issued with, a registered prospectus; and*
- (c) Specifies the place or places at which a registered prospectus may be obtained, or contains a coupon or coupons to be completed by any person who wishes to be sent a registered prospectus, or both; and*
- (d) Complies with this Act and with all regulations made under this Act relating to advertisements:*

Provided that paragraphs (a) to (c) of this section shall not apply in respect of any advertisement relating only to securities exempted from certain provisions of this Act by virtue of subsections (2A), (2B), (3), and (4) of section 5 and subsection (1) of section 7A of this Act.

The Reserve Bank Amendment Bill, presently before Parliament, makes provision for a further (and very similar) section defining an "authorised advertisement" for the purposes of an offer of a debt security by a registered bank. The change is necessary as the banks, whilst remaining subject to the advertising requirements of the Securities Act and Regulations, will in future comply with the Reserve Bank of New Zealand Act 1989 provisions relating to disclosure statements and not the Securities Act provisions relating to registered prospectuses. The new definition of an "authorised advertisement" is the same as the present one except that in a case of an offer of debt security by a bank the advertisement will refer to the most recent disclosure statement (rather than the most recent registered prospectus).

Section 52 Rights of Inspection of Registers of Securities and to copies of Registers and Deeds

52(1) [Inspection] Every register kept under section 51 of this Act shall, except when duly closed (but subject to such reasonable restrictions as the issuer may impose, so that not less than 2 hours in each day shall be allowed for inspection), be open to the inspection of any holder of the securities without fee, and of any other person on payment of the prescribed fee.

52(2) [Copies] Any person may require a copy of a register kept under section 51 of this Act, or any part thereof, on payment of the prescribed fee.

There is a need to ensure that this provision sets the right balance between the rights of market participants to a well informed market and the rights of investors to privacy of personal information in relation to:

- (a) equity securities;
- (b) debt securities; and

- (c) participatory securities.

The Commission has come some distance in practice in modifying the application of this provision to debt securities by its various exemption notices. We would welcome the views of market participants on section 52 in its present form.

Section 53 Issuers to keep proper accounting records

The obligation to keep proper accounting records and ensure that they are audited may overlap with the obligations contained in the Financial Reporting Act 1993. The Working Group on Improved Product and Investment Advice Disclosure has proposed that the rules of law about financial statements in the various statutes, in particular, the Securities Act and Regulations and the Financial Reporting Act, are properly harmonised. A review will be necessary to determine whether any rules of law should be modified.

Section 54 Issuers to issue certificates evidencing securities

54(1) [Evidence of security] Every issuer of a security offered to the public shall send or cause to be sent, to the security holder either the security or a certificate of the security within one month of the allotment, or receipt by or on behalf of the issuer of a registerable transfer, of the security.

54(2) [Certificate executed] Every security or certificate sent to a security holder pursuant to this section shall be executed by or on behalf of the issuer of the security:

Provided that it shall be sufficient compliance with the provisions of this subsection requiring a security or certificate to be executed by any person if a facsimile of the required signature and seal (if any) is reproduced on the security or certificate.

54(3) ["Certificate"] In this section, the term "certificate" means a certificate or other document that properly evidences the nature, ownership, terms, and conditions of the security.

The need for the issue of a certificate that evidences title to securities has been questioned. The provisions of the Securities Transfer Act 1991 are material to listed securities. The Commission would welcome receiving observations and comment on the requirement for certificates in respect of:

- (a) non-listed equity securities;
- (b) debt securities; and
- (c) participatory securities.

Section 55 Interpretation of Provisions relating to prospectuses

For the purposes of this Act-

(a) A statement included in an advertisement or registered prospectus shall be deemed to be untrue if-

- (i) It is misleading in the form and context in which it is included; or*

(ii) *It is misleading by reason of the omission of a particular which is material to the statement in the form and context in which it is included;*

(b) A statement shall be deemed to be included in any advertisement or registered prospectus if it is contained therein, or on the face thereof, or in any report, memorandum, or any document accompanying the advertisement or registered prospectus or by reference incorporated therein or distributed therewith.

The word "statement" is not defined but it is suggested that it should be in order to determine what this section applies to. The intention of the section is to prevent advertisements from misleading the public. Photographs, illustrations and diagrams, indeed, the content of any document as defined in page 2 of this paper, are capable of conveying messages. They should be included in the definition of statement as well as the spoken and written word.

Section 67 Registrar's Powers of Inspection

(1) Subject to subsections (2) and (3) of this section, the Registrar or any person authorised by him may, for the purposes of this Act,

(a) Require any issuer or promoter of securities offered to the public, or any director, officer, or employee thereof, to produce for inspection any book or paper or other document kept by the issuer or the promoter;

(b) Require any person to produce for inspection any book or paper or other document that contains information relating to any money or other property that is managed, supervised, controlled, or held in trust by any such issuer or promoter.

It is suggested that the power under section 67(1)(a) should be extended explicitly to trustees and auditors of an issuer. This could be effected by extending section 67(1)(a) to documents kept by trustees and auditors. It may be observed that the Working Group has proposed that section 67 also apply in respect of "investment advisers" and "investment brokers" as those terms have been defined in the Consultative Paper of February 1995.

INVITATION

The Commission invites submissions and comments from interested persons on the matters raised in this discussion paper.

All replies should be in writing and be forwarded to the Commission at the following address by Monday 21 August 1995 -

Marion Hemphill
Securities Commission
P.O. Box 1179
WELLINGTON