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JSE Debt Listing Requirements: Improvements are still missing
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The standards and practices of the JSE's credit (debt) market are functionally biased in favour of issuers and against investors. This is a long-standing problem, which has been emphasised in recent years by corporate financial and governance failures. Futuregrowth, alongside our industry colleagues (represented at ASISA), has been seeking to improve investor protections for our clients' benefit.

On 31 July 2020, the JSE issued a SENS notifying the market about the implementation of the amended Debt Listings Requirements (DLR). We have previously written extensively about the process the JSE undertook to amend the regulations. This note is an update on the latest developments, and presents our thoughts on the outcome.

In September 2018, the JSE issued the first draft of amendments to the DLR for public comment. Since then, the process has been long and often frustrating, culminating in the final version (v5) earlier this year.

While the JSE did indeed solicit four rounds of public comment during the amendment process, from an investor's perspective, the final version (v5) submitted to the FSCA[1] in February 2020 for their "consultation process" is substantially the same as the version that investors objected to in October 2020 (v4).

Key shortfalls

Amongst others, we identified the following significant shortcomings in investor protections in both v4 and v5 of the JSE's proposed debt listing requirements:

1. investors remain unable to properly negotiate terms and conditions of loan documentation with borrowers, and;
2. investors - not borrowers - are required to pay for legal advice when the borrower defaults or intends amending the terms of the loan agreement.

Taken together, these terms essentially mean that borrowers are able to write their own loan agreements, avoid negotiation of those agreements with their funders, and when things go awry, avoid the costs of enforcement.

As we previously expressed, the above JSE provisions are at odds with all standard unlisted loan documentation. It remains inexplicable to us that this situation is allowed to persist in a public capital market – where the nation's savings are invested.

A flawed process

The ASISA[2] FISC[3] submitted written objections to the FSCA in April 2020, in which we detailed our collective objections to the amendments proposed in v5, as well as our objection to the process followed by the JSE in arriving at the version they submitted to the FSCA. Despite our material and clear objections, with the exception of some minor wording changes in clauses 2.4(b), 4.1 and 5.2, the version submitted to the FSCA is the final published version of the DLR. And so, investor's concerns have not been adequately addressed by either the JSE or FSCA.

[1] Financial Sector Conduct Authority
[2] Association for Savings and Investment South Africa
[3] Fixed Income Standing Committee

ASISA FISC members, including Futuregrowth, expected that the FSCA's consultation process would include direct consultation and engagement with objectors, as well as a formal written response to the ASISA members' written objections. Despite a written representation to the FSCA, this engagement did not happen. The FSCA only (by their own admission) had further direct engagement with the JSE. Thus, the ASISA FISC has now requested a reply from FSCA on the substance of our objections, as well as their rationale for not engaging with objectors before publishing the final version of the DLR. That the FSCA saw fit to only consult and engage with the JSE before the publishing of the final set of regulations, while arguably within their statutory rights, does not appear fair, suitable or reasonable to us.

Our view at Futuregrowth is that the JSE has a direct economic interest in promoting listings – and reducing investor protections is potentially one of its strongest marketing tools. Therefore, we believe that the JSE cannot be an impartial decision-maker on the final outcome. Since September 2018, investors have raised their objections to the proposed amendments directly with the JSE and these have not been adequately addressed. The JSE is not an objective arbiter. We believe it has acted in a manner that results in a set of regulations that protects borrowers over lenders, hereby prejudicing investor rights. This means that investors will not be afforded the appropriate levels of protection or fair treatment, relative to borrowers.

What's next?

First we will pursue direct engagement with FSCA on the process followed by the JSE and themselves. Further, in the meantime, the ASISA FISC is exploring the development of a set of "ASISA-approved" bond market documentation (including DMTNs[4]) which it is hoped, in the absence of more robust regulations, will become the market standard - much like the LMA[5] loan documents that have become market standard in the unlisted loan market.

Parallel to that, we will explore mechanisms with National Treasury to amend the FMA[6] so as to ensure that appropriate investor protections are embedded in the over-arching regulations which govern all exchanges where listed debt trades. This will create consistency between exchanges and avoid the possibility of regulatory arbitrage (where issuers may seek to list their bonds on the exchange with the most lenient, and hence weakest from an investor's perspective, standard).

If we, as institutional investors, are to ensure that our clients' money is adequately protected and to mitigate the pain of defaults[7], then we need to continue to maintain focus on embedding improved investor protections and advocating a fair and level playing field for the pension fund money that invests in debt instruments on the bond market in South Africa.

Published on www.futuregrowth.co.za/newsroom.

[4] Domestic Medium Term Note Programme
[5] Loan Market Association
[6] Financial Markets Act
[7] Like the Land Bank, which is the most recent JSE-listed issuer to default on its obligations