

# **DOCUMENTATION REQUIREMENTS AND APPROVAL PROCESS FOR DEBT ISSUES**

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**THE FMDQ OTC SECURITIES EXCHANGE  
BOOTCAMP TRAINING**

**BY**

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*\* The views expressed in this paper do not necessarily represent the views of the Securities & Exchange Commission*

# OUTLINE

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- ❖ Legal and Regulatory framework
- ❖ Regulating bond issuance
- ❖ Methods of issuances
- ❖ Bond offering process
- ❖ Regulatory Development
- ❖ Issues of Concern
- ❖ Conclusion



# INTRODUCTION

- ❑ The Investment and Securities Act (ISA) 2007 provide the basis for regulating long term financing instruments issued by corporate entities and other categories of issuers as provided in the Act.
- ❑ The principal plank of regulating the issuance is to protect the investors
- ❑ The SEC has the mandate as provided in the ISA to regulate such issuances

# LEGAL AND REGULATORY FRAMEWORK

- ❑ The legal and regulatory framework facilitated the development of the Nigerian bond market;
- ❑ The Investments and Securities Act (ISA) 2007 provides for the regulation of the bond market by the SEC;
- ❑ Part 15 of the Act stipulates requirements for bond issuance by Federal, States, Local Governments and their Agencies through the capital market;
- ❑ The law requires the SEC to register and regulate all offers of securities (including bonds) by public companies;
- ❑ SEC makes rules to regulate the issuance of bonds;(Rule 567-568)
- ❑ Extensive changes have been made to the rules guiding bond issuances since the 2008 financial crisis;

# METHODS OF ISSUING BOND

- ☐ An offer for subscription.
- ☐ Private placement
- ☐ Rights issue
- ☐ Fixed
- ☐ Book Building

# THE BOND OFFERING PROCESS

## Preliminary house keeping matters:

- Issuer should determine financing needs. Capital market not for working capital financing.
- feasibility study of the proposed projects or existing projects if funds are needed for refinancing. This will be a guidance document and will be needed to prepare the prospectus. Also a requirement of SEC.
- If a corporate issuer get a board approval ,ensure you have adequate borrowing power in your Memart if not, get shareholders resolution. .
- a financial adviser would need to be engaged. Most often informal discussions would have commenced with a financial adviser on the need for funds and structure
- A transaction team is usually necessary to work with the advisers.
- various financing options would be examined with adviser in order to determine the best option.



# THE BOND OFFERING PROCESS CONT'D

- Only option to a government issuer is bond
- Option by a corporate issuer will usually be guided by:
  - Sensitivities about ownership and control.
  - Cost implications of the various options.
  - Status of the company, public or private, quoted or unquoted.
  - The financial state and business environment of the company.
  - The industrial sector, financial sector and economic environment.
  - Nature of project
  - State of the capital market
- Decision – once decided on the best option, in this case bond, the issuer will proceed with the process.
- Will have to comply with the Investment and Securities Act 2007, SEC rules and other relevant regulations

# THE BOND OFFERING PROCESS CONT'D



## Parties to the issue

- Issuing house (financial and lead adviser)
- Registrar
- Stock brokers
- Trustees
- Solicitor to the issue
- Solicitor to the company
- Solicitor to the trustee
- Reporting Accountants
- Underwriters (optional)
- Auditor
- Credit rating agency
- Receiving agents (not necessarily parties but useful to the success)
- Receiving bank



Issuing house should receive consent of all parties including directors of the companies or members of the state executive council.



Should conduct legal, financial and technical due diligence on the company or state.



# THE BOND OFFERING PROCESS CONT'D

## ❑ The issuing house:

- ✓ Organizes all parties meetings to discuss:
  - responsibilities of each of the parties including the issuer.
  - the offer time table and pricing.
  - draft prospectus prepared by it.
- ✓ Serves as a liaison between the issuer and the regulatory authorities .
- ✓ Should have a solid knowledge of regulatory requirements and market practices.
- ✓ Although it relies on the opinions of experts such as the solicitors and reporting accountants, it should have a broad knowledge of the functions of all the parties.

# THE BOND OFFERING PROCESS CONT'D

- ❑ The parties led by the issuing house:
  - ❑ Prepare estimated time table of the offer.
  - ❑ All parties meetings will be held with the issuer to discuss the issue and progress.
  - ❑ Issuer has to be honest and transparent and should fully disclose all material information to the offer. Issuer is primary information source.
  - ❑ Determine the pricing method, whether through book building or fixed price.
  - ❑ In fixed price the price of the offer is fixed by the issuer and known in advance while with book building a price range is determined within which interested investors bid. The final offer price is then set by the issuer at the end of the book building period.
  - ❑ Shelf registration – allows the issuer file a programme of offering with the SEC for the same security over a two year period.
  - ❑ Parties must draft relevant documents such as trust deed, reporting accountants report, underwriting agreement, list of claims and litigations, material contracts etc. which will be integral in preparing the prospectus.
  - ❑ Credit rating and rating must be investment grade to be allowed to borrow.
  - ❑ A major document is the audited accounts for 5 years (or number of years in existence) and the latest must not be more than nine months old for PLCs and 12 months old for state bonds (however, if the bond is meant for institutional investors, the Commission considers latest management account where the latest audited account is more than 9 months old)

# THE BOND OFFERING PROCESS CONT'D



## **The type of bond to issue will be determined:**

- ☐ Fixed rate (fixed coupon payment throughout the life of the bond)
- ☐ Floating rate (coupon rate tied to a bench mark rate such as T-bill rate or MPR i.e. carries variable interest payment)
- ☐ Convertible bond (could be converted to equities of the company at a later date)
- ☐ Non-convertible (cannot be converted to the shares of the issuing company)
- ☐ Secured bond (backed by specific assets of the company to meet bond obligation in case of default)
- ☐ Unsecured bonds (not backed by specific assets of the issuer)
- ☐ Callable bond (can be redeemed before stated maturity date at the instant of the issuer)
- ☐ Puttable bond (allows the investors to demand for early redemption of bond)
- ☐ Zero coupon bond (do not pay periodic interest but sold at a deep discount to the face value)
- ☐ Bond with term maturity (the entire bond matures at the same day)
- ☐ Serial bond (maturity is instalment i.e. in piece meal as principal is paid over a period)
- ☐ Exchangeable bond (an investor can exchange the bond for the shares of another company such as the subsidiary of the issuer)
- ☐ Sukuk (Islamic bond – non interest bearing instrument)
- ☐ Bond with guarantee (provides third party guarantee such as insurance company to meet bond obligations in case of default)
- ☐ Subnational bonds have remained general obligation bonds.



## **The structure of the bond should include:**

- ☐ The size of the offer (principal plus cost of issuance)
- ☐ The coupon rate (pricing)
- ☐ Bond tenor (number of years)
- ☐ Maturity date
- ☐ Guarantees, if any



# THE BOND OFFERING PROCESS CONT'D

- ❑ After all information have been collected from the issuer and appropriate due diligence by all the parties, the issuing house prepares the draft prospectus:
  - ❑ The draft should be discussed at an all parties meeting or circulated to all parties for comments as part of the due diligence process of parties.
  - ❑ The draft should conform with regulatory requirements:
    - Investment and Securities Act 2007.
    - SEC Rules and Regulations.
    - listing requirements of FMDQ/NSE.
- ❑ Qualities of a prospectus
  - ❑ The prospectus must be:
    - 1) Accurate – all information in the prospectus must be correct; nothing untrue, no hidden facts.
    - 2) Full – must contain every material information about the issuer and issue; complete information must be provided i.e. no omissions.
    - 3) Devoid of misstatements – statements in the prospectus must not be misleading which could lead investors to wrong decisions.
    - 4) Unambiguous – words and statements should not be subject to misinterpretations or uncertainties; should be explicit and unequivocal.
    - 5) In plain English – should be written in simple, clear and concise language; no high flying words/language

# THE BOND OFFERING PROCESS CONT'D



## The prospectus

- There are civil and criminal liabilities for false and misleading statements in the prospectus.
- The trust deed should also be prepared by the solicitors. Indeed, the draft should have been prepared being necessary for the prospectus preparation. The trust deed is administered by the trustees who represent and protect the interest of bond investors. It is a major investor protection document.
- A sinking fund account is required to be opened in bond issues to be managed by the trustees into which monies for meeting the obligations of the bond would be paid
- Issue proceed accounts which should be interest yielding to be opened into which issue proceeds will be lodged. It should be in the name of the issuing house as the issuer can only lay claims to the funds after allotment and successful subscribers become bondholders.
- Investors such as pension funds, insurance companies, banks, collective investment schemes, private equities and high net worth individuals are usually targeted in a book building process

# THE BOND OFFERING PROCESS CONT'D

The following among other documents are important in packaging the issue and required to be filled with the SEC as per Rule 567-568)

1. The certificate of incorporation showing a Plc status.
2. The memorandum and articles of association.
3. Shareholders resolution (where applicable)
4. Board resolution.
5. Project feasibility study/business plan/corporate strategy etc.
6. Vending Agreement\Material agreements and contracts.
7. Claims and litigations.
8. Share capital history.(CAC C02)
9. Particulars of directors(CAC C07)..
10. Annual reports and audited accounts, recent management accounts .
11. Reporting accountants report
12. Going concern determination by reporting accountant.
13. Shelf prospectus and Pricing memorandum.
14. Declaration by the issuer of disclosure of all material fact in the offer documents.
15. Consents of directors and other parties to be mentioned in the prospectus.
16. Trust deed for debt instruments.
17. Irrevocable Standing Payment Order (ISPO) for state bonds.
18. State house of assembly edict authorizing the bond/gazette of the edict and particulars of the bond (for state bonds)
19. Rating report.
20. Joint Issuing House Agreement

For banks and insurance companies post balance sheet information and confirmation of directors are received by the SEC directly from the CBN and NAICOM respectively



# THE BOND OFFERING PROCESS CONT'D

## ❑ Book building

- ✓ Preliminary prospectus is submitted to SEC and book building process begins, if book building is choice.
- ✓ Determine the price of offer with the issuing house at the end of the book building period.
- ✓ After book building process is completed, final prospectus filing with SEC is done.
- ✓ Execute offer documents (completion board meeting) and same day allot securities to QIBs. Issue proceed to be transferred within 24 hours to issuer.
- ✓ Only qualified institutional investors and high net worth individuals as defined by SEC can participates in book building.
- ✓ If the offer has a retail component, it should open at the end of the book building for not more than 10 working days and be offered at the same price as the book building price.

# THE BOND OFFERING PROCESS CONT'D

## ❑ Where offer is non-book building:

- ✓ Submit Applications to the SEC.
- ✓ After all deficiencies have been corrected and if the application meets the minimum disclosure requirements of the Commission, approval would be granted.
- ✓ Hold completion board meeting/signing ceremony.
- ✓ **By giving consent, parties will also be liable for any false statement or misstatement in their areas of advice/competence. Directors take full responsibilities for all information provided in the offer documents.**
- ✓ Signed and perfected document should be filed with the Commission 48hours after the completion board meeting for cross checking and where there are no variations with original documents, approved by the Commission will be granted:
  - The securities are then registered.
  - Approval given for the offer to open.
  - Public offerings opens for a maximum of 28 working days.
  - Right issues opens for a maximum of 28 working days.
  - Private placement by public companies opens for 10 working days.
  - Extension can be requested for and granted under certain conditions.

# THE BOND OFFERING PROCESS CONT'D

- ☐ Once approval to open is given in a fixed price offer:
  - ✓ marketing starts using:
    - Newspapers
    - Television
    - Radio
    - Posters
    - Road shows
    - Personal contacts
    - Internet
  - ✓ All advertisements must be cleared with the Commission in line with the guidelines on the advertisements
- ☐ In marketing, issuers target:
  - ✓ Some identified investors.
  - ✓ Institutional investors such as a pension funds, banks, insurance companies, and private equities .
  - ✓ High net worth individuals.
  - ✓ Retail investors.
- ☐ Marketing should bring out the qualities of the issuer without exaggerating facts.
- ☐ Applications are distributed by receiving agents (banks and operators).
- ☐ Separate interest bearing accounts to be opened by issuing house with receiving bankers for receipt of proceeds of offer.



# THE BOND OFFERING PROCESS CONT'D

- ☐ When offer closes:
  - ✓ Collation of returns starts.
  - ✓ Submission of allotment proposal to the SEC for clearance.
  - ✓ If allotment is fair and meets the SEC requirements, it is cleared.
  - ✓ Allotment is a responsibility of the issuer and the issuing house.
  - ✓ Both must sign off.
  - ✓ Both should agree to the proposal submitted to the SEC.
  - ✓ Issue is aborted if subscription is less than 50% of proceeds.
- ☐ If issue is for listing:
  - ✓ The stock broker to the issue will handle all offer listing issues on behalf of the issuer.
  - ✓ The issuer would have received a prior NSE listing approval or FMDQ quotation approval for secondary trading
- ☐ Note that issuers will have to meet continuous post issuance and listing/quotation reporting requirements of the SEC and NSE or FMDQ.
- ☐ The SEC conducts periodic inspections of the projects for which funds are raised.

# THE BOND OFFERING PROCESS CONT'D

- ❑ Book building and fixed price offer:
  - ✓ Book building is a process which allows the issuer through the issuing house (book runner) discover the price and quantity investors are willing to buy the securities. The issuer and issuing house set a floor price or a band and receive bids during the book building period from high net worth and institutional investors based on a preliminary prospectus (red herring prospectus). Investors bids are collated after the book building process to determine the final price. The preliminary prospectus contains all material information with the exception of the price and quantity which are determined at the end of the book building process. As it is filed with the SEC, book building process can commence simultaneously. Reduces under subscription of offers. This is the most popular offering process in Nigeria and considerably reduced the use of underwriters.
  - ✓ Fixed price offer process allows the issuer in conjunction with the issuing house fix the price of the offer. Opportunity is not given to investors to have any input in the determination of the price. No need for preliminary prospectus since price is predetermined. Use of underwriting more common in fixed price offers

# REGULATORY INITIATIVES ON DEBT ISSUANCE

- ❑ Improved regulatory framework through new rules and rule amendments
  - ✓ Introduction of book building issuance process
  - ✓ Introduction of Shelf Registration
    - Most bond issues have been through shelf filing;
    - Quickens issuances process as only supplementary filings are required;
    - Both shelf registration and book building have encouraged bond issuance.
  - ✓ Separated the rules on corporate bonds from those of equities thereby providing more clarity for bond issuance;
  - ✓ Introduced and defined Qualified Institutional Buyers (QIB) in the rule book. Most bond issues have been sold to QIBs which include Pension Funds, banks, insurance companies, collective investment schemes, stock brokers and high-net-worth investors (individuals with N300 million in Net worth);



## REGULATORY INITIATIVES ON DEBT ISSUANCE CONT'D

- ✓ Eliminated the need for AGM or EGM for shareholders approval of non-convertible bonds provided that the memo and articles of the issuer contains borrowing power by the directors. This has reduced the cost and improved the process of issuance;
- ✓ Eliminated the requirements for mandatory underwriting;
- ✓ Mandatory credit rating for corporate and sub-national bonds issued to the public. Issue must be investment grade to be sold to the public. Rating is however, optional for privately placed bonds.
- ✓ International credit rating agencies can now rate Nigerian bonds without having offices or incorporation in Nigeria;
- ✓ Recognition of inter-dealer broker as a registrable function for bonds and derivatives;

## REGULATORY INITIATIVES ON DEBT ISSUANCE CONT'D.

- ❑ Encouraging bond issuance and improving the regulatory framework:
  - ✓ Holistic reduced transaction cost including (bonds and equities);
  - ✓ Developed corporate bond prospectus template and posted on the SEC website to guide issuers and financial advisers;
  - ✓ Introduced template on pricing supplement to shelf prospectus and posted on the SEC website. This is expected to be filed whenever a supplementary issue to the shelf prospectus is made;
  - ✓ Introduced guide on corporate bond issuance and posted on the SEC website;
  - ✓ Conducts post approval on-and-off site monitoring of bonds;

# OTHER DEVELOPMENTS ON THE BOND MARKET

## ❑ Improving the demand side :

- ✓ Pension reform with current pension assets of over N8 trillion more than half of which is invested in bonds by Pension Fund Administrators;
- ✓ Growing collective investment schemes and few bond funds with sizeable bond portfolio.;
- ✓ Insurance companies are yet to be significant players in the bond market. The Commission has engaged the National Insurance Commission (NAICOM) on the need for insurance companies to invest in bonds as a major asset class given their long term liabilities;
- ✓ CBN elimination of the 1 year minimum holding period of government bonds by foreign investors.



# SOME ISSUES OF CONCERN

- ❑ Some issues of concerns that delay timely processing of application:
  - ✓ Defective resolution given by the issuing entity
  - ✓ Incomplete statutory and general information provided in offering document by the issuer
  - ✓ Incomplete CAC documentation
    - Certificate of incorporation
    - MEMART
    - Forms CO202 and CO207
  - ✓ Defective consent letters of Directors of Issuing Company
  - ✓ Issuers having outstanding penalty with the Commission

# CONCLUSION

## ❑ Work-in-Progress

- ✓ Issues are mostly plain vanilla and fixed rate bonds;
- ✓ Liquidity still an issue;
- ✓ Relatively few corporate issuers although increasing sub-national;
- ✓ Increased investor participation needed;
- ✓ Education of issuers and other stakeholders;
- ✓ More bonds with credit enhancement;
- ✓ Electronic filing to fast track issuance process;
- ✓ Introduction of market makers for corporate and sub-nationals.
- ✓ In an effort to improve issuance process, the Commission in collaboration with FMDQ, NSE and other stakeholders is harmonizing the issuance process with a view to address concerns on time to market

# CONCLUSION

## ❑ Concluding remarks

- ✓ Securities regulation is to protect investors, ensure transparency, fairness, efficiency and prevent systemic risk (IOSCO).
- ✓ Securities offering process is full disclosure based where the responsibility to determine the merit of an issue lies with the investor having been given all material information.
- ✓ All parties must conduct due diligence and the issuer must be willing to provide all material information truthfully.
- ✓ Directors are liable for false or misleading information, such liabilities are both civil and criminal.
- ✓ Other parties also carry liabilities.
- ✓ There is no compromise for integrity, honesty and transparency on which the market thrives.



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**Thank You**  
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