PROPOSED AMENDMENTS TO ASX GUIDANCE NOTE 8 ON CONTINUOUS DISCLOSURE

BOARDWORX

Introduction

In light of the recent focus by ASIC, the Federal Court of Australia and the Australian Investor Relations Association on the risks of selective disclosure of market sensitive information, ASX has released a consultation paper in relation to proposed changes to its continuous disclosure guidance.

The ASX is concerned that the revised Guidance Note 8 (from May 2013) is not being correctly interpreted or applied by some listed entities in relation to providing earnings guidance, dealing with analyst forecasts and estimates and investor and analyst briefings.

ASX is concerned that this may be causing some entities to:

- "Manoeuvre" analyst forecasts in a non-public or selective manner to align with their internal projections in order to reduce the perceived risk that they need to give an earnings update; and
- Disseminate analyst forecasts or consensus estimates in a manner that may be interpreted as "quasi earnings guidance" pursuant to a policy to not give earnings guidance to the market.

To clarify ASX's guidance on all these matters, ASX is proposing amendments to its Guidance Note 8, as set out below.

Earnings Guidance

ASX is proposing additional wording for the Guidance Note to clarify that under Listing Rule 3.1, an entity is not required to release its internal budgets or earnings projections to the market, provided they are generated for internal purposes and remain confidential. It is perfectly acceptable for entities to have a policy of not providing earnings guidance to the market.

There are qualifiers to this position where:

- an entity which has such a policy gives de facto earnings guidance; or
- an announcement is necessary because of a market sensitive earnings surprise; and

- such a policy does not take precedence over the entitie's continuous disclosure obligations to disclose market sensitive information unless an exception applies.

De Facto Earnings Guidance

ASX cautions entities that have a policy of not providing earnings guidance, against making statements that could be construed as de facto earnings guidance. If they do, a disclosure obligation may be triggered.

Examples of De Facto Earnings Guidance	Consequences
• The entity makes a statement to security holders, analysts or the press that it is "happy" with or expects its earnings to be "in line with" analyst forecasts or consensus estimates, or with the corresponding prior period.	• If that statement was not made to the market ASX may require it be made to the market or ASX may ask the entity to clarify in the statement which analyst's forecasts are being commented on, the range and where within the range the entity expects its earnings to fall. • Constitutes an **implied endorsement of the forecast or estimate**.
• The entity publishes a single analyst forecast or single consensus estimate on ASX.	• Generally, ASX does not allow an entity to publish this information without a detailed explanation of the reasons why the entity considers the information to be market sensitive.

Market Sensitive Earning Surprises

ASX is proposing to clarify that an earnings surprise will only need to be notified to the market under Listing Rule 3.1 if it is "market sensitive". That is, the entity becomes aware that its earnings for the current reporting period will differ so significantly from market expectations that a reasonable person would expect information about its actual or projected earnings to have a material effect on the price or value of its securities.

To assess whether an earnings surprise is market sensitive, ASX provides a list of factors to be considered, with two proposed additions since the previous guidance:

- the extent of the earnings surprise; and

- whether the earnings surprise relates to earnings guidance published by the entity or some other measure of expected earnings, such as analyst forecasts - ASX considers that the market will expect earnings guidance from an entity itself to be inherently more authoritative and reliable than other measures of expected earnings and is therefore likely to take a comparatively smaller variation for that to be considered market sensitive.

Where an entity has published earnings guidance, that guidance will be a basis for the market's expectations and if it expects there to be a material difference between its actual or projected earnings and the published guidance, it should update its guidance to the market. For these purposes, ASX suggests the following as a guide to materiality:

- Treat an expected variation of 10% or more as material;
- Treat an expected variation of 5% or less as not being material;
- For a variation between 5% and 10%, the entity needs to form a judgement as to whether it is material.

If the entity has not published earnings guidance, the fact that internal earnings projections may differ from analyst forecast or prior corresponding period earnings by those materiality thresholds will not necessarily be market sensitive and does not need to be disclosed.

Where an entity has not published guidance, ASX does not lay down any general rule of thumb or thresholds on when a variation in earnings compared to market expectations will be 'market sensitive'. Instead ASX suggests that two questions be asked and where an answer of 'yes' to either of them should be a cautionary indication that the information may be market sensitive:

- Would this information influence my decision to buy or sell securities in the entity at their current market price?; and
- Would I feel exposed to an action for insider trading if I were to buy or sell securities in the entity at their current market price, knowing this information had not been disclosed to the market?

Correcting Analyst Forecasts and Consensus Estimates

In its proposed amendments, ASX clarifies that, other than in relation to market sensitive earnings surprises (as set out above), an entity, under the Listing Rules or otherwise, has no obligation:

- To correct the earnings forecast of any individual analyst or the consensus estimate of any individual market data vendor to bring into line with the entity's internal earnings projections; or

- To publish its internal earnings projections just because they happen to differ from an analyst's forecast or a consensus estimate of analysts' forecasts.

ASX states that it is not concerned with these differences as ASX understands they arise from an analyst's own assumptions on a data set that is typically less complete and less up-to-date than the one available to the entity. However, analyst forecasts and consensus estimates are a relevant indication of market expectations and an entity will have an obligation to make an announcement if it becomes aware that its earnings for the current reporting period are likely to differ so significantly from market expectations that information about the difference is market sensitive.

Where an individual analyst's forecast differs significantly from other analysts' forecasts because of a factual or computational error or missing an announcement the entity has made to the market, ASX states that an entity may point out the error to the analyst (so long as no market sensitive information is disclosed to the analyst).

If a significant difference emerges between the entity's internal earnings projections and the earnings forecasts of a significant proportion of analysts and/or consensus estimates, ASX expects the entity to ask why that might be so. There are reasons why this might be so which do not trigger a disclosure obligation (for instance, where the entity's forecast incorporates information which has not been disclosed to the market for legitimate reasons). On the other hand, the difference in projections may suggest the market is not aware of all of the material information it needs to estimate the entity's earnings, and in turn, the price or value of the entity's securities.

ASX suggests that if this is the case, the entity should consider whether:

- There is any information, not protected by the disclosure carve-outs in Listing Rule 3.1A, that should be disclosed to the market; or
- The market has not fully appreciated the importance of previously disclosed information, and a further announcement with more information is required.

Publishing Analyst Forecasts and Consensus Estimates

A single analyst's forecasts or a single consensus estimate is not information that is required to be or should be disclosed under Listing Rule 3.1. In some circumstances, disclosure may be required under other Listing Rules (e.g., Listing Rule 3.10.4 where the forecast has been included in a prospectus or product disclosure statement).

Publishing this information implies it is market sensitive and constitutes an implied endorsement of the forecast or estimate and amounts to de facto earnings guidance. Thus, if such information is to be published on ASX it must be accompanied by a detailed and acceptable explanation as to why the entity considers the information to be market sensitive.

ASX states that it has no objection to an entity publishing a single analyst forecast or single consensus estimate on the entity's website. However, ASX notes that if an entity does this it may be interpreted as a tacit representation that an entity's results will be close to the forecast or estimate.

The risk that publishing a consensus estimate will be seen as de facto earnings guidance increases further if the entity has selective discussions with analysts or investors referring to the estimate.

If an entity wishes to publish information about analyst forecasts then, to reduce the risk of information being considered de facto earnings guidance, ASX's proposal is to recommend that instead of an entity publishing a single analyst's forecast or single consensus estimate, the entity publishes on its website and/or ASX (which ASX will allow):

- A list of the individual earnings forecasts of the analysts covering the stock; or
- A range showing the low, average (or consensus) and high earnings forecasts (including any outlier forecasts) of the analysts covering the stock,

together with the source and currency of the information, and a disclaimer which makes it clear that the entity does not endorse, confirm or express a view as to the accuracy of, the forecasts nor does it make any representation that its earnings will fall within the range of forecasts provided. An entity will need to consider how frequently it updates this information if it publishes it, recognising that analyst forecasts are updated from time to time.

Analyst and Investor Briefings

Care needs to be taken to avoid selective disclosure. ASX is proposing to update its guidance to emphasise that it is prudent practice to do the following:

- Before an analyst or investor briefing, entities should give any "new" presentation or printed materials to ASX and publish the materials on the ASX Market Announcements Platform, even if the entity believes that the materials do not contain market sensitive information that has not already been released to ASX;

- After an analyst or investor briefing, the entity should review all responses given during the briefing to check whether any market sensitive information has been inadvertently disclosed. If so, the entity should ensure the information is published immediately on ASX, and then on its website; and

- An entity should not blacklist or ban an analyst that it does not favour from an analyst briefing. ASX believes an entity should not provide preferential treatment to favoured analysts.

Other Financial Forecasts and Exploration and Production Targets

While a large part of the current Guidance Note 8 focuses on "earnings guidance", it makes clear that the same principles and guidance apply to "exploration and production targets" issued by mining or oil and gas entities. ASX proposes clarifying that its guidance is equally applicable to other financial forecasts that an entity may make, such as forecast operational or capital expenditure.

Parties to a Material Contract

It is also worth noting that in its proposed amendments to Guidance Note 8, ASX is proposing to add 'the parties to the contract' to the list of items that ASX generally expects to be disclosed in an announcement about the signing of a contract relating to a significant acquisition or disposal.

Submissions and Finalisation

ASX sought submissions on its proposed amendments by Friday, 24 April 2015. It anticipates publishing a revised version of Guidance Note 8 in time to take effect on 1 July 2015.

It has been reported that the submissions generally support ASX's proposed changes. That said, they also offer some suggestions and criticisms. The Australasian Investor Relations Association, (AIRA), in particular, disagrees with some of the new guidance, stating that 'under the proposal the ASX makes the rules more complicated while also telling companies that they can ignore big errors in consensus analyst expectations if the company doesn't provide any guidance of its own'.

In its submission to the ASX, AIRA elaborates further and believes that the amendments are unhelpful because they:

- go beyond the level of guidance that is necessary and appropriate from ASX in so far as the "guidance" relates to provisions of the Corporations Law and not the Listing Rules;

- fail to appreciate that what the ASX views as “guidance” will be viewed by many if not most listed entities as tantamount to regulatory requirements; and

- (as a consequence of the preceding two bullet points) will result in a less informed market and greater potential for earnings surprises- contrary to the best interests of both issuers and investors.

It remains to be seen if ASX incorporates some of the feedback it received into the final version of Guidance Note 8.

What Should You be Doing? There are Seven Key Tips….

1. There is no general requirement to provide earnings guidance.

2. Be careful not to give ‘de facto earnings guidance’.

3. Only ‘market sensitive’ earnings surprises trigger disclosure obligations.

4. There is no general obligation to correcting analyst forecasts and consensus estimates.

5. Take an all or nothing approach to publishing analyst forecasts and consensus estimates.

6. Any presentation materials should first be provided to the ASX before any investor presentation or analyst briefing (even if you think there is no market sensitive information).

7. The parties to a material contract may need to be disclosed.

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