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Dear Mavis

Proposed rewrite of Guidance Note 8

Thank you for the opportunity to comment on the proposed rewrite of Guidance Note 8 and the proposed revisions to the disclosure related provisions in the Listing Rules. Our comments are set out below. At the outset though, we would like to make it clear that, in our view, the proposed rewrite represents a significant improvement in the guidance provided to listed entities on disclosure issues. Our comments below should therefore be read in that context.

1. The "reasonable person" test in Listing Rule 3.1A

While we understand the political difficulties in making any changes to the disclosure related provisions of the Listing Rules, our strong view remains that the "reasonable person" test should be deleted from LR 3.1A. This is so for the following reasons:

- This limb of LR 3.1A operates as a "catch all", so that information which is confidential and falls within one of the five specific categories of information in LR 3.1A.2 is still required to be disclosed. As is clear from the revised GN, it is very difficult to point to information which would fall into this category (as discussed below, the examples given are not in fact examples of circumstances where the reasonable person test itself would require disclosure).
- In our view, it is inappropriate to impose that additional very uncertain requirement in circumstances where the other two limbs of the LR 3.1A have been satisfied. Listed entities are required by the listing rules to make immediate judgements as to whether information is required to be disclosed or not and, if in doing so they rely on the LR 3.1A exemption, the "reasonable person" requirement will be tested by ASIC and/or the courts after the event with the benefit of hindsight. It is inappropriate to apply this uncertain test in this way in circumstances where the consequences for the listed entity in getting it wrong (or being alleged to have got it wrong) include civil penalty provisions; ASIC infringement notices; and class actions.[1]
- In addition to being inappropriate, we think that the "reasonable person" limb is totally unnecessary. It is not required in order to maintain the policy settings in LR 3.1. As discussed below, the purposes which are given in revised GN 8 for the

[1] While we are not aware of any decision where a court has found that the other two limbs of LR 3.1A are satisfied, but the "reasonable person" test is not, this is not a reason not to fix this now, before it becomes an issue.

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additional limb do not provide any support for it. Further, the examples that are given in the GN of situations where the other two limbs of LR 3.1A are satisfied, but the "reasonable person" test is not, are either not true examples of that or are, we believe, situations where disclosure should not be required under LR 3.1.

- We note that Listing Rule 3.1A is to be re-ordered, to put the "reasonable person" test last, so as to somehow show that it is less important than the other two limbs of LR 3.1A. This re-ordering does not, however, overcome the fundamental objections to the "reasonable person" test referred to above. We also doubt whether re-ordering the requirements will have the intended result. We are unaware of any principle of interpretation in which a court will give less weight to a particular requirement in a cumulative list simply because of its order in the list. We understand that the listing rule is not a statute, but section 674 of the Corporations Act gives it statutory backing, and it is likely that a court will interpret LR 3.1A in a way which ignores the order of the requirements.

- Section 4.9 of the revised GN 8 states that the "reasonable person" test serves a number of purposes. However, in our view, none of the stated purposes supports the retention of the test. For example, the first dot point in section 4.9 claims that the test "reinforces the fact that LR 3.1A does not apply to protect information from disclosure if it has ceased to be confidential". It is not clear why this reinforcement is necessary when there is a clear separate requirement that the information must be confidential as a matter of fact and ASX must not have formed the view that it has ceased to be confidential. Similarly, the second dot point in section 4.9 claims that the test "reinforces the fact that LR 3.1A does not protect information from disclosure if it is required to correct or prevent a false market". Again, it is not clear why this reinforcement is necessary when this is exactly what LR 3.1B deals with. The third dot point in section 4.9 merely restates the "reasonable person" test, and adds nothing as to its purpose.

- Section 4.9 goes on to state that examples H6; H7 and H8 in Annexure A illustrate the point that there may be circumstances in which the other two limbs of LR 3.1A are satisfied, but a "reasonable person" would still expect that information to be disclosed. However, for the reasons given in section 2 of this letter, we don't think that example H6 is a situation where disclosure should be required by the continuous disclosure regime. Also, we don't think that examples H7 and H8 would fall within any of the five situations in the second limb of LR 3.1A in any event, so that they do not support the need for an additional "reasonable person" test in the listing rule. More particularly:

  - In example H7, the fact that the two drill holes have returned negative assay results which adversely affect the potential mineralisation of the entire deposit is not information concerning an incomplete proposal. It is also difficult to see that it is information that is insufficiently definite to warrant disclosure, just because those drill holes are being retested (at least in the absence of some other factors which casts doubt on the results). The information which must be disclosed immediately is that the results were negative, but are being retested[2]. There is no need for a "reasonable person" test in LR 3.1A in order to reach that conclusion.

[2] It would seem from footnote 213 of the revised GN that ASX is of the same view.

- Likewise, in example H8, disclosure is required of the fact that the listed entity's earnings for a particular period will differ materially from market expectations, because that information does not fall within the "information generated for internal management purposes" exception. This is specifically acknowledged in the last paragraph of section 4.6 of the revised GN 8, which correctly states that while management accounts and forecasts may have been created for that purpose, market sensitive information they may reveal about a material difference in earnings compared to market expectations does not. See also footnote 136 on page 35. This example therefore does not support the need for an additional and very uncertain "reasonable person" test in the rule.

2. Example H6 – Non-binding indicative proposal received during the course of a takeover bid

Even if ASX does not accept our submission that the "reasonable person" test should be deleted from LR 3.1A, we believe that Example H6 should be deleted. The reasons for this are as follows:

- LR 3.1A allows a listed entity not to disclose a confidential incomplete proposal or negotiation, despite the fact that such non-disclosure means that the entity's securities are not trading on a fully informed basis. The policy basis for this is that, without it, listed entities may be unable to negotiate transactions which are for the benefit of their security holders as a whole, because that negotiation would need to be played out in the public arena, and counterparties may simply refuse to enter into negotiations with the listed entitiy. This policy basis is seen as being sufficiently important that it overrides, in those limited circumstances, the policy basis of LR 3.1: that of ensuring trading occurs on a fully informed basis.
- It is then not clear why this position should be any different simply because there is an existing takeover bid on the table. If anything, that is the exact time when target directors are likely to need the ability to negotiate with other potential bidders in confidence in order to obtain a superior proposal for the benefit of shareholders. If the target directors cannot negotiate with other potential bidders in confidence, there is a very real risk that those other potential bidders will not be willing to approach or engage with the target board, because they will not want their involvement made known to the market prior to announcement of an agreed transaction. We are very concerned therefore that by requiring immediate disclosure of the receipt of a confidential proposal while a hostile bid is on the table, the balance of power in a hostile takeover bid will be turned firmly in favour of the hostile bidder and against target boards seeking to obtain a superior proposal. This is a serious and, we believe, unintended consequence of this example.
- It is also unclear how far example H6 should be applied in circumstances where a hostile bid has been received. Does it mean that once that occurs, any information which would have a material effect on price or value but which the company has withheld from disclosure because it falls within one of the situations referred to in LR 3.1A.3 becomes immediately disclosable? We assume that that is not ASX's intention, but it is not clear why ASX wishes to remove the benefit of the LR 3.1A carve out for one category of information referred to in LR 3.1A.3 and not another (of course, we would say it should be neither).

- Even if example H6 were to be retained, the stated facts beg the question of what happens if the hostile takeover offer remains subject to material regulatory conditions or there is a long period of time remaining in the offer period, and shareholders are not likely to accept until the last week of the bid anyway. Does the receipt of an indicative non-binding proposal in those circumstances still require immediate disclosure?
- We also note that immediate disclosure during a hostile takeover bid of the receipt of an non-binding indicative proposal may not, in fact, result in a fully informed market. Rather, that disclosure may potentially mislead, or provoke an exaggerated market response (particularly if the listed entity remains concerned with the credibility or deliverability of that non-binding indicative proposal), despite appropriate qualifications that may be made in the ASX disclosure. Recent experience has demonstrated this.

3. Effect of a trading halt on an entity's continuous disclosure obligations

Under LR 18.6, the listing rules (including LR 3.1) continue to apply to an entity, even though the entity's securities are in trading halt. ASX states in section 3.7 of the revised GN 8 that provided that the entity has sought a trading halt promptly after becoming obliged to disclose the information, and after the halt is granted acts quickly to issue an announcement to lift the halt, ASX will regard the entity as having complied with the spirit, intention and purpose of LR 3.1. However, as footnote 43 on page 13 acknowledges, "the fact that ASX may regard the entity as having complied with the spirit, intention and purpose of LR 3.1 will not preclude ASIC or a civil litigant from taking a different view and arguing that the entity has failed to comply with its disclosure obligations under LR 3.1 or section 674".

We acknowledge that the risk of a class action in relation to non-disclosure by a listed entity while it is in trading halt may be low, but we do not think that this is a risk that listed entities should be exposed to. We would therefore suggest that the amendments to the rules include an amendment to LR 18.6 to make it clear that LR 3.1 does not apply to a listed entity while it is in trading halt and it is taking reasonable steps to put itself in a position that it can make an announcement that would lift the halt. This would be a sensible amendment and would not detract in any way from the policy setting reflected in LR 3.1.

4. Definition of "information"

The proposed amendments to the listing rules include the inclusion in LR 19.12 of a definition of "information" which states that for the purposes of LR 3.1 – 3.1B, information includes matters of supposition and other matters that are insufficiently definite to warrant disclosure to the market; and matters relating to intentions or likely intentions of a person. The materials published by ASX in support of the proposed amendment states that this is designed to address "a possible drafting gap in the Corporations Act" in that it includes this definition of "information" for the purposes of the insider trading provisions of the Corporations Act but not for the purposes of the continuous disclosure provisions in Chapter 6C of the Act.

We disagree with this proposed amendment, and with the suggestion that there is any drafting gap in the Corporations Act on this point. We also don't understand why it is ASX's role to fix a drafting gap in the Corporations Act, even if there is one.

In our view, it is more likely that the legislature intended to use the broader definition of 'information' in the insider trading provisions so as to deter people trading in securities while in possession of

matters of supposition or matters which may be insufficiently definite to warrant disclosure to the market generally, but did not intend to labour all listed entities with a requirement to disclose matters of supposition or matters insufficiently definite to warrant disclosure to the market. This would be consistent with the intent of the insider trading provisions, which limit trading by individuals with an information advantage, as opposed to the continuous disclosure provisions which are designed to establish a general market disclosure regime.

5. Example H1 – breach of financial ratios

Example H1 is a good one in that it is a fact situation which has arisen many times since the onset of the GFC. However, what the example doesn't (and should) deal with is whether the listed entity can rely on the carve out in LR 3.1A to support a decision not to disclose in these circumstances.

The fact that a listed entity is in breach of its financial ratios, even if it is confident that its lenders will waive the breach as a one-off event caused by temporary factors (and perhaps payment of a consent fee), will typically be information that would be likely to influence investors in deciding whether to buy or sell the entity's securities. This would not necessarily be the outcome if the listed entity could explain its confidence in obtaining a waiver, and if markets behaved rationally. However, in the markets which have prevailed since the onset of the GFC it is highly likely that, even with all of the caveats about likely waiver, the disclosure will have a material effect on price.

The question then becomes whether the carve out in LR 3.1A is available or not in these circumstances. We are aware that borrowers are sometimes advised in this situation that:

(a) if the fact that the entity has breached its financial ratios remains confidential; and

(b) if the entity believes on reasonable grounds that the lenders will waive the breach without material penalty,

then the information is, at that point in time, either information concerning an incomplete negotiation (with the lenders) or a matter of supposition or insufficiently definite to warrant disclosure; and a reasonable person would not expect the information to be disclosed (in part because of the unwarranted impact it will have on the entity and its share price). The advice is therefore that disclosure is not required.

In our view, the guidance should deal with whether or not the carve out in LR 3.1A is available in these circumstances.

6. Example B2 – Decision to reject a confidential non-binding indicative offer

This deals with the situation where a listed entity has received but rejected an indicative non-binding proposal to acquire the securities in that entity at a substantial premium to the market price. The revised guidance states that whether disclosure is required depends on the circumstances, and suggests that disclosure of that information will have a material effect on price if it would lead to speculation that the bidder or a third party will make a further offer.

However, assuming for the moment that, in the circumstances, a reasonable person would expect disclosure of the information to have a material effect on price, the question becomes whether the carve out in LR 3.1A is available or not in those circumstances. The wording in the example suggests that it may be. While we think that would be the preferable position from a policy point of view, we don't think that the reasoning given in the example supports that conclusion. It suggests that because the question of whether or not there will be a subsequent bid is a matter of

supposition, the "matters of supposition or insufficiently definite to warrant disclosure" limb of LR 3.1A is satisfied. However, under LR 3.1A it is the information (i.e. the fact that the proposal has been received and rejected) which must be a matter of supposition or insufficiently definite to warrant disclosure, not the question the market will ask after the information is disclosed. Here, the fact that the proposal has been received and rejected is not a matter of supposition or indefinite in any way.

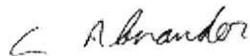
One way to deal with this uncertainty around the application of LR 3.1A in these circumstances would be to strengthen the wording in example B2 in the following manner:

> *Whether disclosure of that information is required will depend on the circumstances. It is important though that C not create a false market through such a disclosure. In ASX's view, a listed entity would be justified in not announcing that the proposal had been received and rejected unless it is reasonably clear the rejection will lead to C making a hostile offer for D or a third party making an offer for D.*

This would emphasise that it is only in clear circumstances that the entity should be disclosing the rejection.

Please let us know if you have any questions in relation to the matters dealt with in this submission, if you would like to discuss any aspect of it.

Yours sincerely



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