

9 June 2016

Diane Lewis
Senior Manager, Regulatory & Public Policy
Office of General Counsel
ASX Limited
20 Bridge Street
Sydney NSW 2000

Email: regulatorypolicy@asx.com.au

Dear Ms Lewis

Updating ASX's admission requirements for listed entities: Consultation paper

Governance Institute of Australia (Governance Institute) is the only independent professional association with a sole focus on whole-of-organisation governance. Our education, support and networking opportunities for directors, company secretaries, governance professionals and risk managers are unrivalled.

Our members have primary responsibility in listed companies to deal with the Australian Securities Exchange (ASX) and interpret and implement the listing rules. Our members hold primary responsibility within listed companies for developing governance policies and supporting the board on all governance matters.

Governance Institute welcomes the opportunity to provide feedback on the consultation paper.

General comments

Governance Institute is of the view that the policy objectives inherent in the consultation paper are to ensure that ASX operates a market of high quality, transparency and integrity, which retains its international competitiveness. Governance Institute is in agreement in principle with these policy objectives and the proposed changes to the admission requirements, as they support efforts to maintain the quality of companies listed on ASX.

Governance Institute is of the view that these are the policy objectives of the consultation paper, given that many of its proposals will make it harder for early-stage and start-up enterprises in emerging industries to meet the revised admissions requirements, thereby preventing them from sourcing capital through an ASX listing. Governance Institute does not disagree with the aim of the policy objectives as embodied in the consultation paper — we recognise that an ASX listing may not be the most appropriate or effective way for embryonic ventures to seek to raise capital from investors.

An ASX listing brings considerable scrutiny from the market and imposes significant compliance and disclosure obligations on entities, which can be a considerable drain on their resources at an early stage in the life cycle of the entity. A company with a market capitalisation of only \$10 million may be better advised to direct its limited resources and the focus of senior executive and directors towards building its business rather than complying with the obligations of a listed entity. We note, for example, that a company in the early stage of its life cycle could find the continuous disclosure requirements not only onerous, but with a high opportunity cost

attached, by drawing management attention more to compliance than to development of the embryonic business model.

Notwithstanding our support for the proposals, we note that provision needs to be made for early-stage and start-up enterprises to source capital other than by listing on ASX. We recognise that this is not the responsibility of ASX, which is keen to support the quality and integrity of the exchange, but note that without due consideration from the government and regulators as to how best to facilitate access to capital for early-stage and start-up enterprises, the current policy emphasis on fostering innovation will falter. The Australian Government's policy initiatives, which are aimed at fostering innovation and the development of digital technology by encouraging start-up business enterprises, will struggle to be realised if attention is not directed towards how these types of businesses access capital funding in the future.

We recognise that there are slowly evolving changes in the venture capital markets which are providing new and innovative forms of financing for emerging businesses, start-up enterprises and the commercialisation of intellectual property which can provide more appropriate access to capital without the more formal regulatory obligations of an ASX listing. We consider that there may be a need for a 'second-tier' securities exchange to enable companies which fall outside ASX's proposed listing criteria to access capital and pursue entrepreneurial activity. While such a suggestion is outside the scope of this consultation, we consider that the consequences of these proposed changes will need to be recognised and considered by ASX, regulators and government.

Consultation questions

Q1 Minimum free float

Governance Institute agrees with the introduction of a 20 per cent free float requirement to support market integrity and quality. We agree that a small free float percentage in early-stage entities can lead to increased price volatility and possible market distortion due to illiquidity in the market for those securities. Even with a free float requirement of 20 per cent, Governance Institute has concerns about the liquidity available for securities holders at the smaller end of the ASX list and the opportunity this presents for greater market distortion.

Q2 Voluntary escrow

Governance Institute supports ASX's approach to defining the free float requirement as the percentage of the entity's main class of securities that are not restricted securities and which are held by non-affiliated security holders. However, we query the inclusion of those holders who are otherwise a non-affiliated security holder and whose shares may be the subject of a voluntary escrow arrangement. Governance Institute notes that voluntary escrow arrangements can involve unrelated third parties and that excluding these security holders from the free float category may cause an entity to fail the free float test. This may create a barrier to listing for entities which would otherwise comply with the requirements. Governance Institute does not support the inclusion of non-affiliated holders of shares subject to voluntary escrow arrangements, and notes that ASX can always form a view that certain voluntary escrow holders are in fact affiliated security holders if it has concerns that the voluntary escrow provisions are being misused. In this event, ASX can exercise its discretion and treat such parties as affiliated with the entity.

Q3 Spread test

Governance Institute notes ASX's proposal to increase the value from \$2,000 to \$5,000 of securities which each security holder counted towards spread must hold. We consider that the logical consequence of this proposed amendment is to exclude 'mum and dad' investors and friends of promoters from investing in new listings. If the minimum holding requirement for spread is increased, we consider that smaller market cap issuers will tailor their offerings so that shares can only be applied for in \$5,000 parcels to ensure that they satisfy the spread requirement. Governance Institute considers that the difference between an investment of \$2,000 and one of \$5,000 is material and will exclude many small retail investors from

participation in floats. For example, many retail investors would probably not have participated in the Medibank float if the parcels of securities on offer were \$5,000. It may be that ASX prefers retail investors to purchase securities once the price is settled and the market fully informed, but if this is the ASX's objective, we would prefer this to be clearly stated.

If ASX wants to encourage small retail investors to participate in new issues, Governance Institute recommends that ASX could include a second option and amend its spread requirements to require a larger spread but with smaller parcel sizes. For example, the admission requirements could be changed to include a requirement that each security holder counted towards spread to hold a parcel of securities with a value of at least \$3,000 and to require a minimum spread of 400 security holders. This option could be added to the current proposal that the parcel of securities should have a value of \$5,000 with a minimum spread of 200 security holders if less than \$50 million or 100 security holders if more than \$50 million.

Q4 Profit test

Governance Institute agrees with the increase in the last year's profit element of the profit test and notes that the profit test thresholds have not changed since 1994.

Q5—7 Assets test and working capital

Governance Institute notes the significant increase in the assets test thresholds and the additional working capital requirements and refers to our comments made in the 'General Comments' section of this submission. While we support an informed and transparent market which facilitates efficient capital raising, we note that the proposed changes to the admission requirements clearly signal a move by the ASX away from the listing of early-stage entities and start-up enterprises, which are unlikely to be able to satisfy the new financial requirements for listing.

Q8—10 Audited accounts

Governance Institute recognises that the proposals in this section of the consultation paper are intended to align with the proposals put forward by the Australian Securities and Investments Commission (ASIC) in *Consultation paper 257: Improving disclosure of historical financial information in prospectuses — Update to RG 228*.

Notwithstanding this, we have concerns that the ASIC consultation paper does not make any reference to early-stage and start-up enterprises in rapidly evolving industries which may have been operating for less than three years, although it does make reference to 'back door' listings. We recognise that the existing and draft Regulatory Guide 228 does contain reference to start-ups. In 228.101 of draft RG228 it states: 'If you are a start-up company that does not have an operating history, you should include your most recent statement of financial position. You should also provide a pro-forma statement of financial information showing the effect of the offer'. We also recognise that ASX does recognise companies which do not have a history of audited accounts.

Notwithstanding this, we reiterate that consideration needs to be given by ASIC and the government as to how best to facilitate access to capital for early-stage and start-up enterprises, given that the proposals from ASX will make it harder to source capital through an ASX listing.

Q11 Overseas home exchanges

Governance Institute agrees with the list of overseas home exchanges as proposed, as this suggests a narrowing of comparable exchanges as part of the move to ensure quality listings.

Q12 ASX foreign exempt listings

Governance Institute agrees with the proposal which would encourage high quality foreign exempt entities from other jurisdictions to list on ASX. However, we note that market capitalisation itself should not be the only criterion for listing. Governance Institute recommends that in addition to having a market capitalisation of at least \$2,000 million, such entities would

need to satisfy the corporate governance standards currently applying to listed entities in Australia before being accepted as an ASX foreign exempt listing.

Q13 Certificated registers

Governance Institute does not consider that the removal of the requirement for foreign entities listed on the ASX to maintain a certificated register would raise any specific issues or concerns.

Q14 Transition date of 1 September

Governance Institute considers that a transition date of 1 September will create significant difficulties for any entities currently engaged in the process of seeking listing. Under ASX's own timetable, the proposed listing rule changes will not be released until early August. Our view is that a typical listing process takes about three to six months from start to finish.

Governance Institute recommends a transition date of 1 January 2017. A later transition date in our opinion allows business time to adjust to the new requirements.

Q15 Reinforcing ASX's discretion to refuse admission to the official list

Governance Institute notes that in the proposed amendments to Guidance Note 1, ASX may exercise its discretion not to admit an entity to the official list where an applicant is established in an emerging market and 'ASX is not satisfied that the level of corporate regulation in that market is appropriate for a listed entity'. We note our earlier comments that any entities from emerging markets would need to satisfy the corporate governance standards currently applying to listed entities in Australia before being accepted as an ASX foreign exempt listing.

We also note that many early-stage and start-up enterprises operate in emerging industries and that there can be a considerable time lag between business activity and corporate regulation. That is, corporate regulation in new and evolving markets and industries can often take years to be introduced — the introduction of this regulation is outside of the entity's control. While the consultation paper references emerging markets, we are of the view that there could also be an issue in relation to emerging industries. Governance Institute recommends that ASX clarify that it will exercise its discretion carefully in these instances.

3 Conclusion

We look forward to the release of the proposed changes to the relevant listing rules and guidance notes.

Yours sincerely



Steve Burrell
Chief Executive