

Office of General Counsel,
ASX Limited,
20 Bridge Street,
Sydney NSW 2000.
Via email: regulatorypolicy@asx.com.au

25 May 2017

Attention Janine Ryan

Dear Ms Ryan,

Reverse Takeovers – Shareholder Approval Requirements

This is a submission by the Corporations Committee of the Business Law Section of the Law Council of Australia (the **Committee**) in response to the Exposure Draft Listing Rule Amendments (the **EDLA**) proposed as part of the Response to Consultation Paper published on 12 April 2017.

The Committee notes ASX is interested in feedback on the practical operation of the proposed amendments, in particular the disclosure requirements and voting exclusions, and is not seeking any further feedback on the appropriate threshold for shareholder approval to a listed company merger. Accordingly, we have set out our specific comments on the EDLA below. But we would first like to briefly express our support for the decision ASX has made following its initial consultation in 2015. In particular:

- While the Committee remains of the view expressed in our previous submission that the costs and detriments of imposing a shareholder approval requirement on reverse takeovers are likely to outweigh any benefits likely to be achieved, we believe the threshold ASX has adopted strikes a reasonable balance between the desire of a number of investor and governance groups to give shareholders a right to vote on certain significant transactions and the need to avoid imposing a significant and unknown impact on the broader market for corporate control in Australia. In the Committee's view, the adoption of a lower approval threshold would be likely to have a very detrimental effect on the regulation of control transactions in Australia – effectively mandating an option for bidders to walk away from a high proportion of announced bids by recommending their shareholders do not vote in favour of the transaction. In the Committee's view, the indirect costs of this change would be very substantial.

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- The Committee supports ASX's decision not to depart from its longstanding policy in relation to significant transactions by listed entities to extend the shareholder approval requirement to wholly cash transactions. The argument in favour of a shareholder approval requirement for reverse takeovers has been based on voting dilution and this issue is completely absent in wholly cash transactions. In light of this, the Committee cautions against ASX's foreshadowed willingness to exercise its discretionary powers in relation to transactions "that appear to be deliberately structured to avoid the shareholder approval requirement". Once it is accepted a wholly cash bid does not require shareholder approval, the Committee submits a mixed cash and scrip bid should likewise not require approval even though the scrip component of the consideration may be capped just below the 100% threshold. As with Listing Rule 10.1.5, ASX's discretion should not be used to substitute a lower approval threshold even if it is only slightly below the mandated threshold in the Listing Rules. In the Committee's view, a bright line test is required in the interests of certainty and it should only be in truly exceptional circumstances that ASX should exercise any residual discretion to require shareholder approval when that is not otherwise required under the bright line test.
- For similar reasons, the Committee also supports ASX's view that shareholder approval not be required for a pro rata issue to fund a reverse takeover because the pro rata offer gives shareholders the opportunity to participate in the capital raising to avoid dilution.

Turning to the terms of the proposed EDLA, our comments are as follows:

1. **Definition of "reverse takeover"** – The Committee notes the proposed definition currently applies the 100% formula "at the date of announcement of the takeover bid or scheme". We are concerned that, in some circumstances, this may have anomalous consequences. For example, if a transaction were to involve a pro rata issue that will be completed before the entity issues or agrees to issue any equity securities under the bid or scheme, the Committee believes the denominator in the formula should include any securities issued under this pro rata issue. As with the current formula in Listing Rule 7.1, the denominator should include any securities issued under an exception in rule 7.2 before the entity issues or agrees to issue securities under the reverse takeover.
2. **Aggregation of separate transactions** – The Committee notes ASX has stated whether a transaction is a reverse takeover will be assessed on a transaction by transaction basis, but ASX will retain the power to aggregate separate transactions if, in ASX's opinion, they form part of the same commercial transaction. The Committee supports this position, but we submit the power to aggregate transactions should only be exercised in exceptional circumstances. The definition of "reverse takeover" is principally relevant to the proposed qualifications to Exceptions 5 and 6 in Listing Rule 7.2 and we believe it would be very rare for there to be multiple takeover bids or scheme mergers that might appropriately be aggregated to give effect to the policy of these provisions.
3. **Application to trust schemes and foreign takeovers** – The Committee agrees the same underlying policy should apply equally in relation to both trust schemes and takeovers and mergers subject to equivalent foreign laws. But we believe it

would be helpful if Exceptions 5 and 6 were amended to deal explicitly with these transactions (possibly drawing on ASIC's approval of relevant financial markets for the purposes of item 14 of s611 to identify relevant foreign legal regimes). Waivers would then only be required on a case by case basis in accordance with current policy for transactions involving targets in other jurisdictions.

4. **Content of notice of meeting:**

- a. The Committee agrees there is no need to impose a requirement for an independent expert's report (**IER**). An IER is generally mandated where shareholders need to be provided with independent analysis of a transaction with a related party or other person of influence and this is not inherently a feature of reverse takeovers.
- b. Given its significance, the Committee submits that proposed Guidance Note 21 should be exposed for comment before it is issued and, accordingly, the Committee has reserved its detailed comments on its foreshadowed contents for that process.¹ However, as a general principle, we do not believe the Guidance Note should operate as a prescriptive checklist regarding the information to be included in notices of meeting. In our view, the general law obligation to give full and proper disclosure, to fully and fairly inform members of the nature of the proposed resolution and enable members to judge for themselves whether to attend the meeting and vote for or against the resolution is more appropriate than a checklist that may not suit the circumstances of a particular case. By way of illustration, the Committee is concerned that "information about the likely effect of the proposed issue and the reverse takeover on the entity, including its consolidated total assets, total equity interests, annual revenue, annual expenditure and annual profit before tax" may be more extensive than the information required to be provided to target shareholders about the merged entity and might even be taken to suggest a bidder will generally be required to include forecasts and projections, even in cases where the transaction is a hostile bid and the bidder does not have access to non-public information about the target. In the Committee's view, given the underlying scrip takeover or merger will be required to include all material that would be required for a prospectus under ss710 to 713, the Committee suggests the relevant disclosure standards should be aligned with those mandated under s713.² And they should clearly only apply to the extent the listed entity is aware of the relevant information.
- c. The Committee also questions whether it will always be necessary or desirable to disclose details of any person who may acquire voting power of more than 20% in the merged entity as a result of the transaction. In many cases, the listed entity will not have a pre-existing relationship with shareholders in the target and, as a result, will not have access to all the information typically disclosed in relation to a resolution under item 7 of s611. In those instances, the entity will only have recourse to publicly

¹ In this regard, the Committee refers to its previous submissions about appropriate consultation processes in the context of ASX's removal of appeal rights in relation to decisions under ASX Listing Rules.

² See s636(1)(g) and ASIC Regulatory Guide 60.66. Section 713 is typically relevant because a listed entity will normally offer continuously quoted securities as bid consideration. Similar disclosure obligations will normally also apply if a listed entity relies on Exception 6 to make an issue to fund the cash consideration under a bid or scheme.

available information (such as substantial holder notices) that may be difficult to interpret and verify and it will not be able disclose anything about the relevant shareholder's intentions. Accordingly, if it is to be retained, the relevant disclosure obligation should be expressed in terms that are capable of being flexibly adapted to suit the particular circumstances.

5. Supplementary disclosures:

- a. The Committee is concerned that Listing Rule 7.3 would seem to require a notice of meeting to set out the maximum number of securities to be issued under a reverse takeover (or the formula for calculating the number of securities to be issued). In the context of a hostile bid or an auction for control, where a bidder may need to consider improving the terms of its offer in order to succeed, this may create serious practical problems and place the bidder in a reverse takeover at a significant commercial disadvantage. A bidder will not want to tip its hand as to the extent of any improvement in its offer that it may be willing to contemplate. But if it does not do so, it may find the approval it obtains ultimately does not satisfy the rule. In the context of a reverse takeover, the Committee suggests it should be sufficient if shareholders approve an announced transaction (including any variation of its terms approved by the entity's board) in all but the most exceptional of circumstances.³ The express requirement for a fresh shareholder approval if there is a material increase in the consideration being offered in a reverse takeover should be removed or adjusted accordingly.
- b. In addition, the Committee does not support the express adoption of ASIC's guidance that shareholders should receive supplementary disclosures at least 10 days before they are required to vote. There are many instances where Courts have not followed this guidance in approving supplementary disclosures in relation to schemes and the requirements in any particular case should be left to the general law regarding the conduct of shareholder meetings, which can flexibly adapt to the circumstances of an individual case.
- c. The reference to shareholders "receiving" supplementary information also tends to imply that new or different information will invariably be sent to shareholders in the same manner as the original notice of meeting. Once again, Courts have approved a variety of different arrangements for bringing new information (such as, for example, financial results scheduled to be released during the notice period) to shareholders' attention prior to a meeting, including by announcing information to ASX. And the Committee submits this flexibility should also be accommodated here.⁴

6. Time within which securities must be issued – Given a takeover offer under Ch. 6 of the Corporations Act may remain open for not more than 12 months, the Committee believes the time period for issuing securities should be extended to

³ If need be, ASX could provide guidance on what may constitute "exceptional circumstances" for these purposes, but this should accommodate an improvement to offer terms that is broadly consistent with market practice.

⁴ It should also be clarified that not every change to information included in a notice of meeting in accordance with Guidance Note 21 will necessarily require some form of supplementary disclosure unless it is sufficiently material from the point of view of the entity's shareholders.

align with this (and allow for the issue of securities as consideration under any post-bid compulsory acquisition process).

7. Voting exclusions and voting against a resolution:

- a. The Committee agrees bidder shareholders should be permitted to vote on the resolution even if they also hold shares in the target (unless they are an associate of the target or Listing Rule 10.1 applies).⁵
- b. The Committee also supports the proposed amendments to the list of excluded persons for the purposes of the relevant voting exclusion and the associated ancillary amendments to definitions.
- c. However, the Committee is concerned there may be unintended consequences of changing voting exclusions so they would prohibit excluded persons from voting in favour of resolutions but permit them to vote against. For example, in a hostile bid for an externally managed investment scheme, this would allow an associate of the target's responsible entity to vote any stake it may hold in the bidder against the required resolution by reference to its interest in the target rather than the interests of shareholders in the bidder. There may be similar difficulties in the context of other voting exclusions that we have not considered in the course of this submission. Accordingly, the Committee suggests ASX only proceed with this change after careful considerations of the implications.

- 8. Transitional arrangements** – The Committee notes ASX has stated the amendments will not apply to transactions announced before their implementation date. For the sake of clarity, the Committee recommends ASX make it clear this will be the case even if there is a change in the terms of an announced transaction (subject, if necessary, to a qualification along the lines noted in note 3).

The Committee would be pleased to discuss this submission if that would be helpful. In the first instance, please contact the Committee Chair, Rebecca Maslen-Stannage, on (02) 9225 5500 or via email: rebecca.maslen-stannage@hsf.com if you would like to do so.

Yours sincerely,



Rebecca Maslen-Stannage, Acting Chair
Business Law Section

⁵ The Committee notes ASX Compliance Update 12/15 stated that ASX intended to update Guidance Note 24 to clarify the application of Listing Rule 10.1 to bids where a connected party of the bidder has a substantial holding in the target. Given some of the uncertainties surrounding the application of Listing Rule 10.1 in these circumstances, the Committee would welcome the early release of an exposure draft of an updated Guidance Note on this topic. In the Committee's view, consistently with the EDLA, shareholder approval under Listing Rule 10.1 should not generally be required simply because a non-associated shareholder of a bidder (that does not have board representation or the capacity to exert influence over the terms of the transaction) is a substantial shareholder in the target.