Australian Private Equity &
Venture Capital Association Limited

01 July 2016

Diane Lewis
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ASX Limited
20 Bridge Street
SYDNEY, NSW 2000

Dear Diane,

Thank you for the opportunity to put forward a submission in relation to the proposals outlined in the *Updating ASX's admission requirements for listed entities* paper released on 12 May 2016 (Consultation Paper).

The Australian Private Equity & Venture Capital Association (AVCAL) is a national association which represents the private equity and venture capital industries. AVCAL's members comprise most of the active private equity and venture capital firms in Australia, who together manage over A$28 billion on behalf of Australian and offshore superannuation and pension funds, sovereign wealth funds and family offices.

Private equity (PE) and venture capital (VC) firms provide capital for early stage companies, later stage expansion capital, and capital for management buyouts of established companies. These businesses help contribute more than 4% per annum to Australia's national output and support, both directly and indirectly, over 500,000 jobs.[1] In the financial year ending 30 June 2015 alone, PE and VC funds invested A$3.3bn into Australia.

1. Background – importance of private equity and venture capital to the proposed reforms

We believe that PE and VC funds can play a critical role in Australia's transition to an innovation-focused economy. Much of the capital invested by PE and VC funds is in smaller, high growth Australian companies, with a particular focus on commercialisation of research & development, and innovating and expanding established businesses.

The PE and VC business model involves fundraising, investing in portfolio companies, value-adding, and then exiting. In the case of PE, an exit is achieved by means such as a trade-sale or initial public offering (IPO). Typically the life of a PE fund is around ten years.

In February 2016, research released by AVCAL, in association with Rothschild, showed that 30 of the 67 IPOs that took place on the ASX, in the years 2013 to 2015 inclusive (minimum offer size of A$100m), were PE-backed (i.e. 45% of all IPOs). The research further showed that since 2013, PE-backed IPOs:

- have achieved an average return of 40.9% and a weighted average return of 26.4%, outperforming non-PE backed IPOs by around 15% and 8% respectively;
- have outperformed non-PE backed IPOs by around 23% on both an average and weighted average basis after the first year of listing; and
- have accounted for eight of the top ten performing IPOs (to 31 December 2015).

This data underscores the importance of a well-functioning listed market to the PE industry, both in terms of an avenue for offering high performing companies to the public, and as an exit means for PE investors.

Accordingly, AVCAL, and its members, have a strong interest in ensuring that the ASX Listing Rules set an appropriately high bar for listing – commensurate with the responsibility inherent in offering equity to retail investors – while not unnecessarily hampering the ability of companies to raise equity funding via a share-market listing.

[1] Deloitte Access Economics, *The Economic Contribution of Private Equity in Australia*, 2013

2. Summary – need for an appropriately high bar to listing

AVCAL supports the ASX's efforts in seeking to review the admission requirements for listed entities, with the aim of ensuring that the market continues to be one of quality and integrity, and remains internationally competitive.

We agree that it is imperative that entities meet certain minimum standards before they are allowed onto the ASX, and thereby able to attract equity investment from retail investors.

Our key points of feedback in relation to the Consultation Paper are as follows:

- AVCAL supports increasing the financial thresholds for listing so as to ensure the quality of the IPO market and adequately protect retail investors from the inherent risks in investing in start-up or early stage companies;
- For similar reasons, AVCAL supports the extended application of the A$1.5m working capital requirement to all asset test entities;
- ASX should show flexibility when applying its proposed audited accounts requirement to companies which the issuer intends to acquire prior to or as part of an IPO, or risk distorting market behaviour.

Our more detailed comments are outlined below.

3. Increasing the financial thresholds for listing

We note that under the ASX's proposed changes to the profit test, the consolidated profit threshold for the 12 months prior to admission will be lifted to at least A$500,000, while the other aspects of the profit test threshold will remain unchanged. We note that these thresholds have not changed since 1994.

We support this modest increase, and believe that the thresholds should be reviewed regularly (say every five years) to ensure that the bar remains sufficiently high, and allows only those entities of sufficient size and scale to list on the ASX. This will be crucial to maintaining the confidence and integrity of the listed market.

AVCAL also supports the proposal to increase the asset test thresholds to an NTA of at least A$5m or a market capitalisation of at least A$20m. While it is important that start-up and early stage companies be afforded the flexibility to seek equity financing via the ASX, it is equally important that retail investors only be offered access to companies with sufficient capital to carry on their businesses for a reasonable period post-listing.

It must be acknowledged that in the eyes of some retail investors, the admission of a company to the ASX carries with it a level of endorsement or surety as to the company's business model and financial viability. If companies are permitted to list prematurely it could allow retail investors exposure to high risk companies, with disclosure heavily relied upon to protect them. It is important that only those companies that are ready to publicly list are permitted to.

4. Working capital requirements

For the same reasons as outlined above, we support the proposal to standardise the A$1.5m working capital requirement across all entities admitted to the ASX under the assets test. This will help ensure that only those companies that have sufficient working capital can access equity funding via the ASX.

5. Requiring audited accounts from assets test entities

We note that the ASX proposes to revise the requirements for entities seeking admission under the assets test so that (a) the entity must produce audited accounts for the last three full financial years (unless ASX agrees that such accounts are not needed); (b) for any entity or business to be acquired by the entity at or ahead of listing, the entity must produce three full financial years of audited accounts for that business or entity (unless ASX agrees that such accounts are not needed); and (c) an audit report or review must not contain a modified opinion, emphasis of matter or other matter paragraph that ASX considers unacceptable.

While we support the rationale behind proposal (a) above, namely to provide greater assurance to investors of the financial condition of the entity seeking admission to the ASX, and greater consistency across the board, it is important that it is not applied too narrowly so as to prevent companies from listing, that may otherwise be appropriate candidates for an IPO. This will be particularly relevant to start-up or earlier-stage companies who may be viable listing candidates, notwithstanding that they do not have three years of audited accounts at the time of admission.

Accordingly, we support ASX (or, if ASX in inclined to defer to ASIC on such matters, ASIC) retaining flexibility to allow admission, under the assets test in appropriate circumstances, for those entities which do not have three years of audited accounts. This is particularly the case where the relevant entity is an otherwise suitable company with the potential to produce a return on investment for investors and which otherwise satisfies the relevant ASX Listing Rule requirements and Corporations Act disclosure requirements.

That said, we have concerns that proposals (b) and (c) may have unintended consequences, particularly for some private equity-backed IPOs. It is frequently part of a PE fund's strategy to cause an investee company to make 'bolt-on acquisitions' (i.e. where an investee grows its business by acquiring companies in the same or similar industry which provide complementary services, technology or geographic footprint diversification) as a way of adding value. This may occur prior to or as part of an IPO process.

In some cases, the bolt-on acquisition may be a company with limited record-keeping, for example a family-run business, which could prevent the provision of an unqualified audit opinion for the necessary three financial years. In other bolt-on cases, the issuer may not have been able to negotiate full access to the financial records of the complementary business to be acquired, despite its best endeavours.

In such circumstances, we do not believe it would be appropriate to prevent the relevant entity from listing, particularly if the company to be acquired (as part of a bolt-on acquisition) is not material in terms of size and/or overall role in the company's future business strategy. Furthermore, a qualified audit opinion in and of itself should not prevent a listing so long as the auditor does not have significant concerns regarding the integrity of the information it has examined, which would materially compromise its ability to provide a professional opinion, or the information is irrelevant to the investor's decision-making (for example, it relates to the operating history of a company whose activities are unrelated to those the issuer intends to engage in following IPO). These issues will be particularly relevant where it is the first time that the auditor has audited the company.

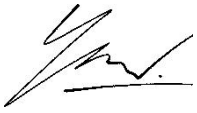
Consequently, AVCAL cautions against the ASX adopting a rigid approach which could prevent suitable companies from being able to list on the ASX, denying them a level-playing field, and investors the potential benefits of an IPO. Indeed, adopting a strict test may have market-distorting effects including blocking otherwise value-adding transactions from taking place for fear that such an acquisition would prevent the company from listing.

Noting that ASIC is currently consulting on improving disclosure of historical financial information in prospectuses (Consultation Paper 257, May 2016), we support a coordinated, consistent approach by the two regulators (ASIC and ASX).

6. Next steps

We would like to thank you for considering this submission, and look forward to continuing our engagement with you on these issues, and other matters concerned with maintaining the integrity of the ASX. If you have any queries in relation to this submission, please contact Christian Gergis, Head of Policy & Research, on 02 8243 7010 or alternatively myself on 02 8243 7000.

Yours sincerely



Yasser El-Ansary
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