

Reverse Takeovers

Shareholder Approval Requirements - Exposure Draft Listing
Rule Amendments

RESPONSE TO CONSULTATION

12 APRIL 2017



Invitation to comment

ASX is seeking feedback on the Exposure Draft Listing Rule Amendments set out in this paper. Submissions should be sent to:

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Attention: Janine Ryan

ASX prefers to receive submissions in electronic form. Submissions not marked as 'confidential' will be made publicly available on ASX's website.

If you would like your submission, or any part of it, to be treated as 'confidential', please indicate this clearly in your submission.

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1. Executive Summary

1.1. Executive Summary

ASX proposes to amend its Listing Rules to require a bidder to obtain shareholder approval for a reverse takeover. This paper exposes for public comment the proposed amendments to the ASX Listing Rules to implement this proposal. These proposed amendments will enhance the framework for investor protection whilst supporting the efficiency and competitiveness of Australian listed companies in the market for corporate control.

The proposed amendments follow a comprehensive public consultation process which included the release in November 2015 of the consultation paper [Reverse Takeovers – Consultation on Shareholder Approval Requirements for Listed Company Mergers](#). The consultation paper sought feedback on a consultation proposal to amend the Listing Rules to require a listed bidder to seek shareholder approval for a reverse takeover i.e. a takeover bid or scheme of arrangement where the bidder issues securities in excess of 100% of existing capital as consideration, resulting in the target's shareholders owning more than 50% of the bidder post-takeover.

ASX received 14 written submissions in response to the consultation paper. ASX also held a number of consultation meetings with interested stakeholders. As anticipated, there was a significant divergence of views amongst stakeholders in relation to this issue.

Stakeholders looking at this question from an investor's perspective generally supported the introduction of a bidder shareholder approval requirement for listed company mergers, but suggested that shareholder approval should be required for issues of securities exceeding 20-50% of existing capital, in line with some other major international exchanges.

Stakeholders looking at this question from the perspective of listed entities were not supportive of the proposed changes, primarily on the basis that any regulatory benefits in terms of investor protection were outweighed by the potential costs and market inefficiencies that would result from imposing a shareholder approval requirement.

Having considered the responses to consultation, ASX proposes to proceed with the consultation proposal to require shareholder approval for reverse takeovers.

ASX is of the view that this proposal strikes an appropriate balance between providing additional investor protection by enabling bidder shareholders to have a say on a transaction in which they are effectively in the position of the target without imposing a significant and unknown impact on the broader market for corporate control in Australia. ASX's proposal would have captured the high profile reverse takeovers that have attracted public criticism in recent years.

ASX gave serious consideration to the feedback from investor and governance groups that a threshold lower than 100% should be adopted. In assessing this feedback, ASX considered a number of matters including:

- The potential impact of a shareholder approval requirement at different dilution thresholds on the Australian market for corporate control, both in terms of the number of transactions likely to be affected and the potential costs of obtaining shareholder approval
- The position adopted by other international exchanges.

ASX's market analysis indicated that requiring shareholder approval at a lower threshold of 25-50% of existing capital would affect 40-70% of scrip bids (and 30-50% of all bids) by Australian listed bidders for Australian listed

companies¹. Given the significant number of transactions likely to be affected, ASX considers that adoption of a lower threshold would represent a fundamental change in the regulation of control transactions in Australia. ASX considers that the regulatory benefits of such a significant amendment must clearly outweigh the potential costs.

The responses to consultation highlighted a number of potential direct and indirect costs that may result from a shareholder approval requirement. ASX agrees with the view that the direct costs are unlikely to be material in the context of the transaction. However, ASX considers that the indirect costs could be significant and could have a material impact on the ability of Australian listed entities to compete in the market for corporate control.

ASX's further analysis of the position adopted by other international exchanges² highlighted the diversity of practice across main and second boards in other jurisdictions, and the broader regulatory context for control transactions and capital raisings in other jurisdictions. ASX considers that the proposed amendments will ensure that ASX is not an outlier relative to other international exchanges and is appropriately positioned, having regard to the broader regulatory settings in the Australian market for corporate control.

ASX also considers that the Corporations Act, ASIC and the Takeovers Panel are, and should remain, the primary source of regulation for takeovers in Australia. ASX should be cautious about adopting a shareholder approval requirement that would significantly reduce the flexibility provided by the Corporations Act and that may entrench existing substantial shareholdings in a bidder.

For similar reasons, ASX has formed the view that it should not depart from its longstanding policy in relation to significant transactions by listed entities, by extending the shareholder approval requirement to wholly cash transactions by adopting a threshold based on net assets or other criteria apart from dilution.

ASX acknowledges the views of respondents that a threshold based on increase in share capital could result in transactions being restructured to avoid the shareholder approval requirement. ASX notes that it will closely monitor transactions that appear to be deliberately structured to avoid the shareholder approval requirement for reverse takeovers and reserves the right to exercise its discretionary powers under the Listing Rules in these circumstances.

ASX also sought feedback on a number of technical aspects of how a shareholder approval requirement should be implemented. Consistent with this feedback, ASX has decided:

- **Disclosure in notice of meeting** – ASX will not require entities to obtain an independent expert's report in relation to the reverse takeover for inclusion in the notice of meeting. However, ASX will require reasonably detailed disclosure in the notice of meeting to approve a reverse takeover to maintain consistency with the disclosure provided to target shareholders. Further detail is set out in section 5 below.
- **Voting** – the target and its associates will not be permitted to vote in favour of the resolution approving the reverse takeover. Common shareholders of the bidder and target will generally be entitled to vote on the resolution to approve the reverse takeover unless they are receiving a material benefit (excluding a benefit solely by reason of being a holder of ordinary securities in the bidder or the target). However, a common shareholder who has a controlling shareholding in the target will be excluded from voting on the resolution by virtue of being an associate of the target. Again, further detail is set out in section 5 below.

¹ Analysis of takeovers and schemes by Australian listed bidders for Australian listed companies for the period from 1 January 2012 to 31 August 2016. Refer to Section 3 and Annexure B for further detail.

² Refer to Section 3 and Appendix A for further detail.

ASX's review of voting exclusions in the context of reverse takeovers has also highlighted amendments to the Listing Rules that ASX considers should apply to voting exclusions for all transactions including:

- **Voting against a proposal** – the Listing Rules currently prohibit an excluded person from voting on a resolution, whether for or against. ASX proposes to amend the Listing Rules to provide that excluded persons are only precluded from voting *in favour* of the resolution. Those persons will be permitted to vote *against* the resolution. Further detail is set out in section 5 below.
- **Associates** – as noted above, associates of a person excluded from voting are also excluded from voting. The definition of associate in the Listing Rules currently includes bodies corporate that control, or are controlled by, excluded persons. It does not include other entities (including natural persons) who control, or are controlled by excluded persons. ASX proposes to amend the definition of associate to address this anomaly. Further detail is set out in section 5 below.

1.2. ASX review of capital raising rules

ASX is currently undertaking a broader review of the Listing Rules governing the issue of new securities, including Chapter 7 of the Listing Rules. Following completion of that review, ASX intends to issue a consultation paper outlining proposed amendments to the Listing Rules and a draft new Guidance Note 21 *The Restrictions on Issuing Equity Securities in Chapter 7 of the Listing Rules*. To the extent these broader changes affect the proposed changes in relation to shareholder approval for reverse takeovers, they are outlined in this paper.

1.3. Next steps

The Exposure Draft Listing Rule Amendments are available on the public consultation page of the ASX website at <http://www.asx.com.au/documents/resources/reverse-takeover-rule-amendments.pdf>.

ASX seeks comments on the Exposure Draft Listing Rule Amendments by Friday 26 May 2017. ASX is interested in feedback on the practical operational of the proposed amendments, in particular, the disclosure requirements and voting exclusions. However, ASX is not seeking any further feedback on whether an alternative threshold should be adopted for applying the requirement for shareholder approval to a listed company merger. That issue has been determined following the initial consultation in 2015.

ASX also welcomes the opportunity to discuss the Exposure Draft Listing Rules with interested parties. ASX contact details are listed on page 2.

ASX is looking to introduce these amendments with effect from 1 October 2017, subject to regulatory clearance. The proposed amendments would not apply to any transaction that is announced before the implementation date. The broader amendments to the Listing Rules governing the issue of new securities mentioned above will likely come into effect later in the year.

2. Current regulatory framework

2.1. Introduction

Takeovers and schemes of arrangements in Australia are governed by the Corporations Act and, where the bidder or target is listed, the ASX Listing Rules.

Neither the Corporations Act nor the ASX Listing Rules generally require bidder shareholder approval for reverse takeovers³.

2.2. Corporations Act

The Corporations Act contains the primary obligations in relation to the conduct of takeover bids and schemes of arrangement in Australia. Takeover bids are governed by Chapter 6, and schemes of arrangement are governed by Part 5.1 of the Corporations Act. These provisions are primarily focussed on the impact of takeovers and schemes on control of an entity, rather than dilution of existing shareholders, and as such do not generally require a bidder to obtain shareholder approval to offer its shares as the consideration under a takeover or scheme of arrangement, regardless of the number of shares being issued. This is consistent with the Corporations Act generally, which does not impose restrictions on issues of securities other than in limited circumstances.

2.3. Listing Rules

The ASX Listing Rules regulate the circumstances in which share issues by listed entities require shareholder approval. Listing Rule 7.1 requires shareholder approval for issues of securities in excess of 15% of an entity's existing ordinary share capital over a 12 month period unless an exception applies.

ASX Listing Rule 7.2, exception 5 currently provides an exception from this requirement for securities issued under an off-market bid or scheme of arrangement. Similarly, ASX Listing Rule 7.2, exception 6 currently provides an exception for an issue of securities to fund the cash consideration for a takeover bid or scheme of arrangement if the terms of the issue are disclosed in the bid/merger documents.

Therefore, shareholder approval is not currently required under the Listing Rules for a bidder who issues securities as consideration for an acquisition under a takeover bid or scheme of arrangement, regardless of the number of shares issued. The policy underlying these exceptions is that the imposition of a requirement for shareholder approval could put a listed bidder at a significant disadvantage to a non-listed bidder in a contested takeover situation.

2.4. Discretionary powers of the Takeovers Panel and ASIC

The Takeovers Panel and ASIC have certain discretionary powers in relation to takeovers generally, including reverse takeovers. Under the Corporations Act, these discretionary powers are primarily focussed on issues relating to control of an entity rather than dilution of existing shareholders.

³ This assumes there are no extenuating circumstances which would result in a need for approvals under other provisions of the Corporations Act or the ASX Listing Rules such as related party transactions.

Takeovers Panel

Section 657A of the Act enables the Takeovers Panel to make a declaration of unacceptable circumstances in relation to a transaction having regard, among other things, to effect of the transaction on control of a company or to the principles set out in section 602.

Under these provisions, the Takeovers Panel has jurisdiction to make a declaration in relation to a reverse takeover (including where it is being undertaken by a scheme of arrangement) if it gives rise to unacceptable circumstances.

Takeovers Panel Guidance Note 1⁴ notes the following on reverse takeovers:

- A change of control, or a material effect on control, by an issue of shares as consideration for a bid, that either disenfranchises shareholders or does not meet the policy of Chapter 6 (even if it strictly it satisfies item 4 of section 611) may give rise to unacceptable circumstances
- A reverse takeover may also offend the principles in sections 602(a) and (c). It may “lock up” the bidder and adversely affect competition. The Panel takes into account whether the transaction is subject to the approval of bidder shareholders and/or is subject to a condition that allows a superior proposal to be considered by those shareholders.

ASIC

ASIC Regulatory Guide 60 (Schemes of Arrangement)⁵ sets out ASIC’s view in relation to reverse takeovers undertaken by way of a scheme of arrangement. ASIC notes that “a scheme results in a reverse takeover if:

- a) Consideration for the members of the company proposing the scheme (the target company) is shares in the offeror company; and
- b) The scheme results in a change in control of the offeror company or has a material effect on control of the offeror company.”

ASIC further notes that:

“We encourage any person proposing a scheme that will result in a member in the scheme company obtaining voting power in the offeror company of more than 20% to consult with us very early in the planning stage. We will consider such schemes on a case-by-case basis to determine if they result in a change in control of the offeror company, or have a material effect on control of the offeror company and therefore whether they result in a reverse takeover. We will monitor this area and, if it becomes necessary, will consider providing further guidance in the future.”

Based on current guidance, dilution of existing bidder shareholders through a reverse takeover may not of itself trigger a requirement for shareholder approval unless there is a broader change in, or material effect on, control. This position is driven by the Corporations Act’s focus on acquisition of control rather than dilution of existing shareholders. However, the Takeovers Panel has left the door open to require shareholder approval for reverse takeovers if the particular circumstances give rise to unacceptable circumstances.

⁴ http://www.takeovers.gov.au/content/Guidance_Notes/Current/downloads/GN01_2010.pdf

⁵ <http://download.asic.gov.au/media/1239045/rg60-published-22-september-2011.pdf>

3. Consultation feedback

3.1. Consultation proposal

In its November 2015 consultation paper [Reverse Takeovers – Consultation on Shareholder Approval Requirements for Listed Company Mergers](#), ASX sought feedback on a consultation proposal to amend the Listing Rules to require a listed bidder to seek shareholder approval for a reverse takeover i.e. a takeover bid or scheme of arrangement where the bidder issues securities in excess of 100% of existing capital as consideration, resulting in the target’s shareholders owning more than 50% of the bidder post–takeover.

3.2. Consultation feedback

ASX received 14 written submissions in response to the consultation. The submissions that were made on a non-confidential basis are available at <http://www.asx.com.au/regulation/public-consultations.htm>.

ASX thanks all those who shared their views and expertise during the consultation period. ASX appreciates the constructive engagement and comprehensive, high quality written submissions received from respondents. In the interests of efficiency, ASX does not propose to discuss in detail all of the comments received in response to the consultation. However, ASX has set out the key themes emerging from those submissions.

Gap in the regulatory framework for reverse takeovers

ASX sought submissions on whether there was a gap in the regulatory framework in relation to reverse takeovers that warranted a change from the status quo.

Investor and governance groups submitted that there was a gap in the regulatory framework in relation to shareholder approval for listed company mergers in Australia, both at an absolute level, in that shareholders should have a right to vote on transactions that are “significant”, “fundamentally change the company in question” or “are of a transforming nature”, and at a comparative level, where ASX was characterised as an outlier relative to its peers in comparable jurisdictions.

Some respondents further commented that the structure of reverse takeovers is fundamentally unfair because bidder shareholders do not get a say, while target shareholders do, even though the bidder is effectively in the position of the target. If the transaction had been structured in the usual way, the bidder shareholders would have had a say.

A number of respondents noted that, although reverse takeovers have been relatively rare in the past, there has been an increase in the number of reverse takeovers in recent years.

Investor and governance groups submitted that the proposed 100% threshold is too high and a lower threshold of between 20-50% (with the majority suggesting 20-30%) of existing capital should be adopted, in line with other major international exchanges. A number of respondents also submitted that the threshold should be based on an expansion in the entity’s net asset base (not just its capital) on the basis that shareholder approval should be required for all “major” transactions, regardless of how they are funded. It was also noted that this would reduce the risk of deal structuring to avoid a shareholder approval requirement.

Other respondents expressed the contrary view that there is not a gap in the regulatory framework that warrants a change from the status quo for reasons including that:

- The regulatory benefits are likely to be very limited while the costs and inefficiencies are likely to be substantial

- The board of directors is the appropriate body to determine whether to pursue a reverse takeover
- Reverse takeovers are an unremarkable feature of Australian corporate life and there are valid reasons for undertaking them
- Relatively few reverse takeovers have raised controversy, generally where there is a substantial holder in the bidder
- Decisions may be made by shareholders who are not bound to act in the best interests of the company and some of whom may have vested interests not aligned to shareholders as a whole (e.g. a substantial shareholder who may wish to protect its own controlling stake)
- The international comparison needs to be considered in the context of the broader regulatory context in the relevant jurisdictions
- ASIC and the Takeovers Panel have significant powers to address any unacceptable conduct in relation to a reverse takeover.

Costs of a shareholder approval requirement

ASX sought submissions on the direct and indirect costs of imposing a shareholder approval requirement for reverse takeovers and whether such a requirement would have a material impact on the ability of ASX listed bidders to compete effectively in the market for corporate control.

Some of the potential direct and indirect costs/consequences of a shareholder approval requirement noted by respondents included:

- Direct costs of holding shareholder meetings
- Increased time and uncertainty to complete transactions
- Bidders may be required to offer more attractive terms (for example, increasing consideration, offering break fees or additional deal protection mechanisms) to counteract deal uncertainty
- Bidders may have reduced flexibility to vary offer terms if the variation results in a requirement to seek further shareholder approval.
- Seeking up front shareholder approval for the maximum number of shares that may be offered would put the bidder at a disadvantage by showing its hand
- Bidders may seek to structure transactions in sub-optimal ways (for example, by offering less scrip and utilising cash or debt financing) that may involve additional cost
- The bidder's negotiating position may be weakened by the requirement to explain to its shareholders why the transaction is in their best interests
- Deals may not proceed or may be vetoed by strategic shareholders for reasons that do not reflect the interests of all shareholders, resulting in all shareholders missing out on the potential benefits of the transaction.

A number of respondents indicated that, although there were likely to be additional direct and indirect costs of a shareholder approval requirement, they did not expect such a requirement to have a material impact on the

ability of Australian companies to compete effectively in the market for corporate control. Some of the factors raised in support of this position included:

- The direct costs (such as convening shareholder meetings) would generally be a relatively small component of overall transaction costs. It was recognised that these costs may be proportionately larger for smaller deals. However, some respondents noted that smaller companies commonly hold shareholder meetings to approve less significant proposals
- The experience in overseas jurisdictions, where bidder shareholder approval requirements are not perceived to have impeded listed company mergers
- The fact that foreign bidders have successfully bid for Australian companies despite requiring bidder shareholder approval
- There is likely to be no material impact on timing for recommended schemes of arrangement since target shareholder approval is also required
- Off market takeover bids are usually subject to a number of conditions including regulatory approvals which would take time to satisfy, thereby reducing the timing impact of a requirement to obtain bidder shareholder approval. In particular, it was noted that foreign bids will often be subject to FIRB approval.

A number of those respondents further submitted that, to the extent there were additional potential costs, the shareholder protections of a shareholder approval requirement outweigh the potential costs.

The contrary view expressed was that the costs and inefficiencies are likely to be substantial and would be likely to reduce the ability of ASX listed companies to compete effectively in the market for corporate control.

4. ASX's response to consultation feedback

Having considered the responses to consultation, ASX proposes to proceed with the consultation proposal to require shareholder approval for reverse takeovers (i.e. issues of securities in excess of 100% of existing capital).

ASX is of the view that this proposal strikes an appropriate balance between providing additional protection to investors by enabling them to vote on reverse takeovers, without imposing a significant and unknown impact on the broader market for corporate control in Australia.

ASX acknowledges the legitimate concerns of stakeholders that bidder shareholders should have a say on transactions in which they are effectively the target and that shareholders should not be subject to unlimited dilution as a result of a takeover.

Respondents noted an increase in the number of reverse takeovers in recent years. ASX's analysis indicates that, during the period from 1 January 2012 to 31 August 2016, there were approximately 18 proposed reverse takeovers by Australian listed bidders for Australian listed companies⁶. This represents approximately 20% of all scrip bids⁷, and approximately 14% of all bids (cash and/or scrip), by Australian listed bidders for Australian listed companies. These transactions, if completed, would have resulted in share issues from 100% up to over 500% of existing capital.

ASX considers that the number of reverse takeovers, and the size of potential dilution under those reverse takeovers, over the last 5 years indicates that there is a sufficient case to warrant a change in the regulatory framework for reverse takeovers.

ASX gave serious consideration to the feedback from investor and governance groups that a lower dilution threshold should be adopted. In considering this feedback, ASX considered a number of matters including:

- The potential impact of a shareholder approval requirement at different dilution thresholds on the Australian market for corporate control⁸, both in terms of the number of transactions likely to be affected and the potential costs
- ASX's position relative to other international exchanges.

ASX's market analysis indicated that:

- If a lower threshold of 50% was adopted, shareholder approval would have been required in approximately 40% of scrip bids (or 30% of all bids) by Australian listed bidders for Australian listed companies
- If a lower threshold of 25% was adopted, shareholder approval would have been required in approximately 70% of scrip bids (or nearly 50% of all bids) by Australian listed bidders for Australian listed companies

The responses to consultation highlighted a number of potential direct and indirect costs and consequences that may result from the imposition of a shareholder approval requirement. ASX acknowledges that the direct costs (such as costs of convening the meeting) are generally not likely to be material in the context of the overall transaction. However, ASX believes that the indirect costs could be significant and could have a material impact on the ability of Australian listed entities to compete in the market for corporate control.

⁶ ASX analysis of takeovers and schemes by Australian listed bidders of Australian listed companies for the period from 1 January 2012 to 31 August 2016. ASX is aware of only one further proposed reverse takeover following the review period.

⁷ References to scrip bids includes takeovers and schemes where scrip or combination of cash and scrip is offered as consideration.

⁸ ASX analysis of takeovers and schemes by Australian listed bidders of Australian listed companies for the period from 1 January 2012 to 31 August 2016.

ASX considers that adopting a lower threshold would represent a fundamental change in the regulation of control transactions in Australia and that a convincing case has not yet been made for such a fundamental change. ASX therefore considers that it should be cautious about imposing a requirement where the potential impacts are unknown.

A number of respondent's characterised ASX's approval requirements as an outlier relative to other major exchanges. ASX's further analysis of shareholder approval requirements in other jurisdictions (as set out in Appendix A) has highlighted that the international comparison is more nuanced than the position stated by respondents and in particular that:

- While a majority of main boards require shareholder approval at a lower threshold, some main boards and most "second" board either require shareholder approval at a threshold of 100% or, in some cases, do not require shareholder approval at all
- Some exchanges that require shareholder approval at a lower threshold have exceptions for public offerings of securities to fund a takeover (e.g. TSX, NYSE and Nasdaq) which are not available in Australia. Some of these jurisdictions also have an established public market for contingent forms of funding that convert to securities if the acquisition completes but are otherwise cancelled (similar structures are rare in Australia)
- In a number of jurisdictions, "control transactions" are not separately regulated by a corporate regulator similar to ASIC, leaving the exchange as the primary regulator of control transactions.

While ASX acknowledges the approach adopted by other major exchanges, ASX considers that the proposed amendments will ensure that ASX is appropriately positioned amongst other international exchanges having regard to:

- The diverse practice across international exchanges, particularly amongst second boards
- The particular nature of the Australian market, a significant portion of which is formed by small cap companies who may be disproportionately affected by a lower threshold
- The broader regulatory settings in other jurisdictions, which do not have equivalent protections for control transactions to those in Australia and also reduce the potential impact of a shareholder approval requirement by providing exceptions to that requirement.

ASX also considers that the Corporations Act, ASIC and the Takeovers Panel are, and should remain, the primary source of regulation for takeovers in Australia. ASX should be cautious about adopting a shareholder approval requirement that would significantly reduce the flexibility provided by the Corporations Act and that may entrench existing substantial shareholdings in a bidder.

For similar reasons, ASX has formed the view that it should not depart from its longstanding policy in relation to significant transactions by listed entities, by extending the shareholder approval requirement to wholly cash transactions by adopting a threshold based on net assets or other criteria apart from dilution.

ASX acknowledges the views of respondents that a threshold based on increase in share capital could result in transactions being restructured to avoid the shareholder approval requirement. ASX notes that it will closely monitor transactions that appear to be deliberately structured to avoid the shareholder approval requirement for reverse takeovers and reserves the right to exercise its discretionary powers under the Listing Rules in these circumstances.

5. Proposed Listing Rule amendments

5.1. Proposed Listing Rule amendments

ASX intends to amend the Listing Rules to require a bidder to obtain shareholder approval under Listing Rule 7.1 for a reverse takeover. The proposed amendments are set out in the Exposure Draft Rule Amendments on the public consultations page of the ASX website at <http://www.asx.com.au/regulation/public-consultations.htm>.

5.2. Amendments to Listing Rule 7.2 and associated definitions.

Listing Rule 7.2, exceptions 5 and 6

ASX Listing Rule 7.2, exception 5 currently provides an exception from Listing Rule 7.1 for securities issued under an off-market bid or scheme of arrangement.

Similarly, ASX Listing Rule 7.2, exception 6 currently provides an exception from Listing Rule 7.1 for an issue of securities to fund the cash consideration for a takeover bid or scheme of arrangement if the terms of the issue are disclosed in the bid/merger documents.

ASX proposes to amend Listing Rule 7.2, exceptions 5 and 6 so that those exceptions do not apply to issues under, or to fund, a reverse takeover. This has the effect that an issue of shares under, or to fund, a reverse takeover will require approval under Listing Rule 7.1.

ASX also proposes ancillary amendments to Listing Rule 7.2, exceptions 5 and 6 and the definition of takeover to simplify the drafting of those sections. These changes are drafting changes only and do not affect the substance of those provisions.

Definition of reverse takeover and reverse takeover target

ASX proposes to introduce into Listing Rule 19.12 a definition of “reverse takeover”. This will be defined as “a takeover bid or a merger by way of scheme of arrangement under Part 5.1 of the Corporations Act where an entity is proposing to acquire securities of another body and the aggregate number of equity securities issued or to be issued by the entity:

- Under the takeover bid or scheme; and/or
- To fund the cash consideration payable under the takeover bid or scheme,

is equal to or greater than the number of fully paid ordinary securities on issue in the entity at the date of announcement of the takeover bid or scheme. Separate issues may be aggregated if, in ASX’s opinion, they form part of the same commercial transaction”.

ASX also proposes to add to Listing Rule 19.12 a definition of “reverse takeover target”, meaning the body in which an entity is proposing to acquire securities in a reverse takeover.

ASX notes that a transaction is a reverse takeover where the number of equity securities issued or to be issued is **equal to** or greater than 100% of existing capital. This minor variation to the consultation proposal has been made to address feedback that shareholder approval should be required for a merger of equals, where shareholders of the bidder and target each hold 50% of the shares in the entity after the merger.

Whether a transaction is a reverse takeover will be assessed on a transaction by transaction basis, not over a specified time period as is typically the case for Listing Rule 7.1. However, ASX has the power to aggregate separate transactions if, in ASX's opinion, they form part of the same commercial transaction.

In addition, ASX also notes that entities are required to comply with the Listing Rules in accordance with their spirit, intent and purpose, by looking beyond form and substance and in a way that best promotes the principles on which the Listing Rules are based (Listing Rule 19.2). ASX will closely monitor transactions that appear to be deliberately structured to avoid the shareholder approval requirement for reverse takeovers and reserves the right to exercise its discretionary powers under the Listing Rules in these circumstances.

Equity securities

Whether a transaction is a reverse takeover will depend on the number of equity securities being issued. ASX will amend Listing Rule 7.1B to clarify that the number of equity securities to be issued for the purposes of determining whether a transaction is a reverse takeover should be calculated in the same way as for other Listing Rule 7.1 calculations.

ASX is proposing to introduce into Listing Rule 7.1B.1 a specific provision stating that, for these purposes, options or other convertible securities being issued will be counted based on the maximum number of ordinary securities into which they may convert. This position is currently outlined in the notes to Listing Rule 7.1B.1. As part of its broader review of Chapter 7, ASX has formed the view that this issue is more properly addressed in the body of the rule rather than in the notes. This change is therefore a drafting change only and does not reflect a change in ASX's policy on this issue.

Application to trust schemes and foreign takeovers

On their face, Listing Rule 7.2, exceptions 5 and 6 only apply to takeover bids or schemes of arrangement under the Corporations Act. ASX has in the past, in appropriate cases, granted a waiver to extend exceptions 5 and 6 to a merger with an Australian trust by way of a "trust scheme of arrangement" or to an entity making a takeover offer for, or merging with, a foreign company or trust where the takeover or merger is subject to an equivalent regulatory regime to the Corporations Act. In future, this waiver will not be granted if the entity is, in substance, engaging in a reverse takeover of the foreign company or trust.

Application to pro-rata issues

Listing Rule 7.2 contains a separate exception for pro rata issues to ordinary shareholders (exception 1). This exception could also be utilised to raise funding for a reverse takeover.

ASX sought submissions on whether shareholder approval should be required if a reverse takeover is funded by a pro rata issue. Divergent views were expressed on this issue. Those who did not support shareholder approval extending to pro-rata issues to fund reverse takeovers noted that pro rata offers give shareholders the right to participate to avoid dilution and would not necessarily result in target shareholders holding more than 50% of the bidder after the transaction, depending on the amount of any shortfall and how it is taken up by outside investors.

Some of those supporting a requirement for shareholder approval noted that shareholders may not always be able to participate to avoid dilution and that the right to participate was not the same as the right to vote on the proposal. There was also a strong correlation between those who supported shareholder approval for pro rata issues to fund a reverse takeover and those who supported imposing shareholder approval requirements for "major transactions" based on broader criteria, such as an increase in net assets, rather than being based solely on dilution.

Having considered the feedback from consultation, ASX has formed the view that shareholder approval should not be required for a pro rata issue to fund a reverse takeover because the pro-rata offers give shareholders the opportunity to participate in the capital raising to avoid dilution.

5.3. Amendments to disclosure requirements

Content of notice of meeting

ASX Listing Rule 7.3.8 sets out the information required to be disclosed in a notice of meeting seeking approval under Listing Rule 7.1.

ASX sought submissions on whether any changes to the usual Listing Rule 7.1 disclosure requirements should be imposed if shareholder approval is required for reverse takeovers and, in particular, whether an independent expert's report should be required.

Of those who responded on this issue, the vast majority (including investors and governance groups) did not support a mandatory requirement for an independent expert's report, instead suggesting this be left to the discretion of the directors as is currently the case for other control transactions. Some respondents noted that any requirement to prepare an independent expert's report could result in unnecessary costs and delays. Two respondents suggested that an independent expert's report should be required because it will provide bidder shareholders with information to assist in determining how to vote on the proposal. One respondent suggested that ASX could adopt an "if not, why not" approach to independent expert's report.

No other changes to the disclosure requirements in Listing Rule 7.3.8 were suggested.

ASX notes that in the context of a takeover bid or scheme of arrangement, the bidder and target must prepare substantial disclosure for the bidder's and target's statements or for inclusion in the scheme booklet. ASX considers that bidder shareholders would typically benefit from access to a similar level of disclosure as is provided to target shareholders under the regulated documents.

To address concerns in relation to the disclosure provided to bidder shareholders, ASX proposes to amend Listing Rule 7.3.8 to require bidders to disclose information "in relation to the reverse takeover". Consistent with the majority of feedback, ASX does not intend to impose a requirement for the bidder to prepare an independent expert's report.

As noted, above ASX proposes to issue a new Guidance Note 21 *The Restrictions on Issuing Equity Securities in Chapter 7 of the Listing Rules*. This guidance will outline the information ASX expects to be disclosed in relation to a reverse takeover. The guidance will note that, over and above the specific requirements set out in the Listing Rules, a notice of meeting must also include such other material as will fully and fairly inform security holders of the matters to be considered at the meeting and enable them to make a properly informed judgment on those matters. In some cases, this may require the entity to disclose more than just the information specifically required under the Listing Rules.

Guidance Note 21 will state that, in the context of a reverse takeover, ASX would expect the notice to include a reasonable level of information about the reverse takeover, including:

- The identity of the reverse takeover target
- A summary of the reverse takeover target's principal activities and the jurisdictions in which it operates
- A description of the reverse takeover target's business model, including any key dependencies and key risks

- A copy of the reverse takeover target’s most recent audited accounts or a link to where they can be viewed and downloaded
- The consideration payable by the entity to security holders of the reverse takeover target
- Details of any regulatory approvals or waivers required or other material conditions that must be satisfied for the reverse takeover to proceed
- 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
- A capital table showing the issued capital of the entity before and after the reverse takeover
- If the entity is proposing to issue securities to raise funds in connection with the reverse takeover, the following information about the issue:
 - The nature of the issue (e.g. placement, pro rata offer or public offer pursuant to a prospectus, PDS or information memorandum)
 - Any minimum subscription proposed
 - Whether the issue will be underwritten and, if so, by whom
 - The amount proposed to be raised by the issue
- Details of any person who will acquire control of, or voting power of 20% or more in, the entity as a result of the reverse takeover
- If there are any changes proposed to the entity’s board or senior management, details of those changes
- The timetable for implementing the transaction including, if it has not already occurred, the timing for dispatch of the bidder’s statement or scheme booklet to target security holders.

ASX notes that the bid or scheme documents provided to target security holders in a reverse takeover would typically include disclosures substantially equivalent to those set out above. Where the notice of meeting seeking bidder security holder approval under Listing Rule 7.1 is sent at the same time as, or after, the bid or scheme documents are sent to target security holders, the notice of meeting can, and should, include substantially equivalent disclosures to those made to the target security holders.

In some cases, bidder security holder approval may need to be sought before the bid or scheme documents for target security holders are finalised. In these cases, ASX will carefully monitor the disclosures made in the notice of meeting to ensure they satisfy the requirements above. If subsequently the bid or scheme documents provided to target security holders disclose materially new or different information that would have been relevant to a decision on how to vote on the Listing Rule 7.1 approval, ASX may require a fresh security holder approval to be obtained.

Supplementary disclosures

The proposed new Guidance Note 21 will also outline ASX’s policy in relation to supplementary disclosures. Where materially new or different information emerges after a notice of meeting proposing a resolution to approve an issue under, or to fund, a reverse takeover has been sent to security holders but before the vote on the resolution, the entity may need to make supplementary disclosure to members. This should be done in

sufficient time ahead of the meeting to allow security holders to consider, and if necessary take advice on, how the new or different information should affect their vote on the resolution.

In line with ASIC guidance on similar matters, ASX generally considers that members should receive the supplementary information at least 10 days before they are required to vote. Anything less is likely to warrant an adjournment of the meeting or the calling of a new meeting.

Where materially new or different information emerges after security holders have voted on such a resolution, the entity may need to seek a fresh security holder approval. This may occur, for example, if there is a material increase in the consideration being offered in a reverse takeover, compared to what was approved by security holders.

Time within which securities must be issued

Listing Rule 7.3.2 currently requires a notice of meeting proposing a resolution to approve an issue of securities under Listing Rule 7.1 to disclose that the securities will be issued within 3 months of the approval being given.

ASX proposes to amend this rule to include a new provision for issues being made under, or to fund, a reverse takeover that extends the period within which the securities must be issued from 3 months to 6 months. This requirement is designed to strike a balance between giving entities the time practically necessary to complete an issue of equity securities under a reverse takeover, and ensuring that the securities are issued within a reasonable time frame after security holder approval so that the approval can still be considered to be current and not rendered stale by subsequent events.

5.4. Amendments to voting exclusion statements and ancillary definitions

Listing Rule 7.3.8 currently requires a notice of meeting proposing a resolution to approve an issue of securities under Listing Rule 7.1 to include a voting exclusion statement setting out those who are excluded from voting on the resolution.

The current voting exclusion statement for Listing Rule 7.1 precludes the following people and their associates from voting on the resolution:

- A person who may participate in the proposed issue and
- A person who might obtain a benefit, except a benefit solely in the capacity of a holder of ordinary securities, if the resolution is passed.

ASX sought submissions on whether any changes to the standard voting exclusions would be necessary if a shareholder approval requirement for reverse takeovers was implemented. In particular, ASX asked whether common shareholders (i.e. bidder shareholders who also hold shares in the target) should be permitted to vote, subject to the usual exclusions for related and interested parties.

Of those who responded on this issue, all considered that bidder shareholders who also hold shares in the target should still be permitted to vote on the resolution by the bidder. No other changes to the voting exclusions were proposed by respondents.

ASX agrees that common shareholders should be entitled to vote, unless the shareholder has an additional interest that is materially different to other bidder or target shareholders. ASX considers that this is consistent with the approach adopted more broadly in control transactions, including in relation to the determination of voting classes for schemes of arrangement.

However, both limbs of the current voting exclusion for Listing Rule 7.1 approvals would preclude common shareholders from voting on a proposed issue under, or to fund, a reverse takeover.

In determining the appropriate voting exclusion for reverse takeovers (with particular reference to common shareholders), ASX considers it important to distinguish between:

- Shares issued to target shareholders under the takeover or scheme, since all target shareholders (including those who also hold shares in the bidder) would be permitted to participate on the same terms in the issue
- Shares issued to target shareholders under a separate issue made to raise cash to fund a takeover or scheme (for example, a private placement), in which case all target shareholders are not likely to participate on the same terms.

Consistent with the position adopted for schemes of arrangement, where the bidder would typically not be entitled to vote in the same class as other target shareholders, ASX proposes to amend the voting exclusion so that the reverse takeover target and its associates would not be entitled to vote in favour of the resolution to approve the proposed issue under, or to fund, the reverse takeover. As noted further below, the reverse takeover target would be permitted to vote against the resolution.

In light of the above, ASX proposed to amend the voting exclusion for Listing Rule 7.1 so that the excluded persons are as follows:

- Where the resolution relates to a proposed issue under a reverse takeover – the reverse takeover target and any person who will obtain a material benefit as a result of the reverse takeover or the proposed issue (except a benefit solely by reason of being the holder of ordinary securities in the entity or the reverse takeover target)
- Where the resolution relates to a proposed issue to fund a reverse takeover – the reverse takeover target, any person who is expected to participate in the proposed issue, and any person who will obtain a material benefit as a result of the reverse takeover or the proposed issue (except a benefit solely by reason of being the holder of ordinary securities in the entity or the reverse takeover target)
- In any other case – any person who is expected to participate in, or who will obtain a material benefit as a result of, the proposed issue (except a benefit solely by reason of being the holder of ordinary securities in the entity).

ASX notes that the proposed amendments do not impose a cap on the size of common security holdings in respect of which a shareholder would be entitled to vote (other than where the security holder is a controlling security holder, and therefore an associate, of the reverse takeover target). This means that a security holder whose stake in the bidder may increase significantly after the reverse takeover as a result of its holding in the target would still be entitled to vote on the resolution.

ASX also notes, that even if a person is not excluded from voting in relation to a proposed issue under or to fund a reverse takeover, ASIC and the Takeovers Panel retain their regulatory powers and functions under the Corporations Act, including to the Takeovers Panel's power to determine that circumstances in relation to an acquisition of securities in the bidder are unacceptable.

Ancillary amendments

The amendments to the voting exclusion statement set out above reflect some additional amendments identified as part of the broader review of Chapter 7 which are set out in further detail below.

Material benefit

The existing reference in the voting exclusions for rule 7.1 to “a person who might obtain a benefit, except a benefit solely in the capacity of a holder of ordinary securities, if the resolution is passed” is considered too broad and uncertain. To give greater certainty as to which parties must have their votes excluded on this score, ASX proposes to replace this reference with a reference to a person who will obtain a material benefit as a result of the reverse takeover (where applicable) or the proposed issue.

ASX will give guidance in new Guidance Note 21 on what types of benefits would be considered material, or not material, for the purposes of these voting exclusions. The guidance will state that ASX considers a material benefit to be one that is likely to incline the recipient of the benefit to vote differently to other ordinary security holders of the entity on the resolution in question. Examples include:

- A professional adviser who will be paid a success fee if the issue (or where the issue is being made under, or to fund, a reverse takeover, if the reverse takeover) proceeds
- An underwriter or sub-underwriter of the issue who will be paid an underwriting or sub-underwriting fee in relation to the issue
- A lead manager of, or broker to, the issue who will be paid a fee or commission on the proceeds of the issue.

The guidance will further state that, in the context of reverse takeovers, ASX would not typically consider any one of the following, of itself, to be a material benefit resulting from the reverse takeover:

- Being a director of the entity or the reverse takeover target
- Consideration payable to a holder of another class of securities under or in connection with the reverse takeover on the same terms as all other holders of securities in that class (unless it appears to ASX that the consideration materially exceeds the fair value of those securities and is, in effect, a disguised material benefit)
- Redundancy or termination benefits payable to an officer or an employee of the bidder or the reverse takeover target if the transaction proceeds, provided the benefit is a bona fide payment made in accordance with contractual entitlements or established policy and generally available to all officers and employees whose office or employment may be terminated.

The guidance will note that the material benefit must be obtained as a result of the reverse takeover. This would not capture payments made in the ordinary course of business that are not commercially connected with the proposed issue.

In formulating its views above on material benefits in the context of reverse takeovers, ASX has had regard to ASIC and Takeovers Panel guidance⁹ and applicable case law on collateral benefits and the determination of classes for the purpose of voting on a scheme of arrangement. This is to ensure, to the extent possible, consistency of treatment across control transactions.

ASX also notes that it has the residual power under the final row in the table in rule 14.11.1 and also under rule 14.11.2 to exclude the votes of any person on a resolution required under the Listing Rules if, in ASX’s opinion, the votes of those persons should be disregarded.

⁹ Takeovers Panel Guidance Note 21: Collateral benefits and ASIC Regulatory Guide 9: Takeover bids

Participation in the issue

The existing reference currently in the voting exclusion for rule 7.1 to a person who “may participate” in the proposed issue is considered too broad and potentially confusing, particularly where the issue is being conducted by way of public offer. The existing note to that voting exclusion explains that this requires more than a mere possibility that a person could participate in the issue. Rather than address this issue by way of a note, ASX is proposing to replace this reference in the voting exclusion for rule 7.1 with a reference to a person who “is expected to participate” in the proposed issue.

Voting against a proposal

ASX also proposes to amend Listing Rule 14.11 to provide that the persons who are excluded from voting are only precluded from voting *in favour* of the resolution. Those persons will be permitted to vote *against* the resolution. ASX has seen instances where parties have structured a transaction in such a way to attract a voting exclusion for persons who are opposed to the transaction. The intent of the voting exclusion requirement is to ensure that a transaction can only proceed if it is approved by security holders who do not have a personal interest in the transaction. It is not to deny security holders who are opposed to a transaction an opportunity to vote against it.

This change will apply to all voting exclusions under the Listing Rules, not just those related to security holder resolutions approving an issue of securities under Listing Rule 7.1.

Definition of associate

The Listing Rules currently provide that the term associate has the meaning given in sections 12 and 16 of the Corporations Act. Section 12(2)(a) of the Corporations Act provides that a person (the second person) is an associate of the primary person if the primary person is a body corporate and the second person is:

- A body corporate that the primary person controls; or
- A body corporate that controls the primary person; or
- A body corporate that is controlled by an entity that controls the primary person.

This definition only applies to bodies corporate that control or are controlled by the primary persons and not to other entities (in particular, natural persons). ASX is of the view that, for the purposes of the Listing Rules, the definition should apply to controlling security holders regardless of their legal status. ASX proposes to amend the definition of associate to:

- Incorporate directly the relevant language from sections 12 and 16 of the Corporations Act
- Amend the language incorporated from section 12(2)(a) so that it applies to entities (including natural persons) as well as bodies corporate
- Amend the deeming provision in the definition of associate in the Listing Rules so that related parties of all natural persons who are excluded from voting will be deemed to be their associates unless the contrary is established.

This change will apply to all references to associate in the Listing Rules, not just those relevant to reverse takeovers.

Annexure A – International comparison of shareholder approval requirements for scrip issues

Jurisdiction/exchange	% at which approval required
Canada <ul style="list-style-type: none"> • TSX • TSX-V 	<ul style="list-style-type: none"> • 25% (subject to public offer exception) • N/A if target listed on TSX or other senior exchange. Otherwise, 100%
Hong Kong <ul style="list-style-type: none"> • HKEx Main Board • HKEx GEM 	<ul style="list-style-type: none"> • 25% • 25%
JSE	30%
New Zealand	N/A
Singapore <ul style="list-style-type: none"> • SGX (Main Board) • SGX Catalist 	<ul style="list-style-type: none"> • 100% (or 20% if not an expansion of issuer’s core business) • 100% (or 75% if not an expansion of issuer’s core business)
UK ¹⁰ <ul style="list-style-type: none"> • LSE (premium listing) • LSE (standard listing) • AIM 	<p>25%</p> <p>N/A for takeovers of entities in the same listing category. Otherwise, 100% or if it results in fundamental change in business, board or voting control</p> <p>100% or results in fundamental change in business, board or voting control</p>
US <ul style="list-style-type: none"> • NYSE • Nasdaq 	<ul style="list-style-type: none"> • 20% (subject to public offer exception) • 20% (subject to public offer exception)

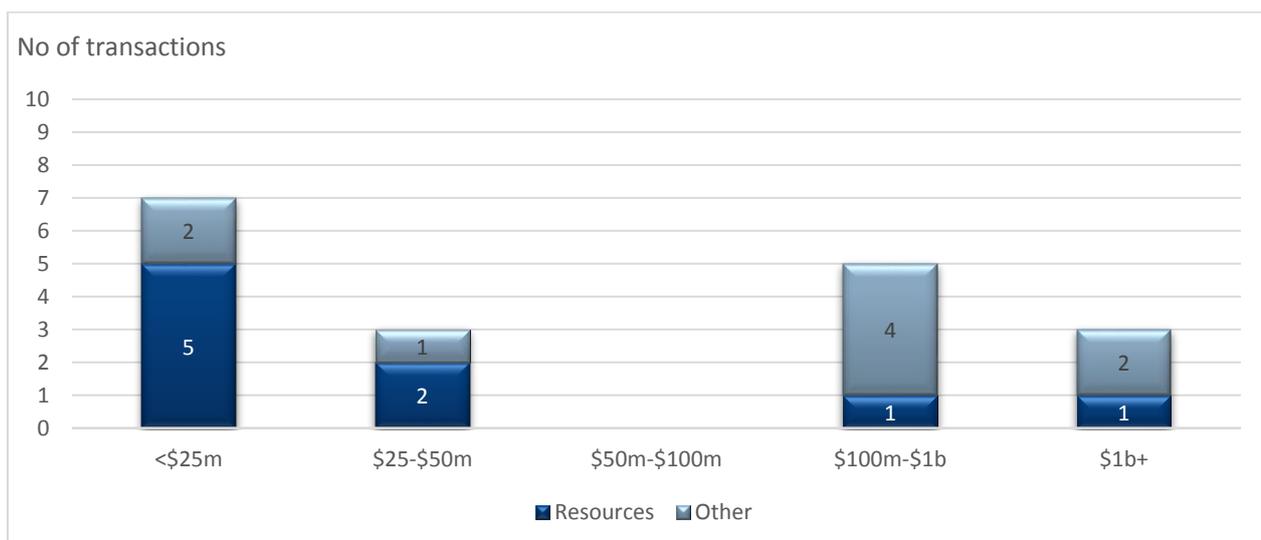
¹⁰ LSE Premium Listings represent less than 40% of listed entities in the UK.

Annexure B – Analysis of Australian market for takeovers¹¹

Reverse Takeovers

- There were 18 proposed reverse takeovers by Australian listed bidders that would have required shareholder approval under the consultation proposal
- These transactions, if completed, would have resulted in share issues from 100% up to approximately 580% of existing capital
- These transactions represent approximately 20% of all scrip bids by Australian listed bidders¹²
- These reverse takeovers are spread across all segments of the market, with some at the small cap end (targets with a market cap of less than \$50m) and some at the mid to large cap end (targets with a market cap in excess of \$400m)
- 50% of reverse takeovers were in the resources sector

Table 1 - Reverse Takeovers – By Target Market Capitalisation and Industry Sector



Overall market for control of ASX listed companies

- There were approximately 308 proposed bids for ASX listed companies
- Australian listed bidders made approximately 40% of bids and Australian unlisted or foreign bidders approximately 60%
- Cash bids represented approximately 60% of all transactions and scrip approximately 40%
- For Australian listed bidders, scrip bids represent about 70% of all bids

¹¹ Takeovers and schemes of arrangement of Australian listed companies from 1 January 2012 to 31 August 2016¹¹

¹² References to scrip bids also includes bids offering a combination of cash and scrip.

Scrip bids by Australian listed bidders for ASX listed companies

- Approximately 87 proposed scrip bids by Australian listed bidders
- The resources sector accounted for more than 50% of all scrip bids by Australian listed bidders
- Table 2 shows the approximate number of scrip transactions at different dilution levels
- Reverse takeovers represented approximately 20% of scrip bids by Australian listed companies
- Approximately 40% of scrip bids (or about 36 transactions) could have resulted in shares issues of 50% or more. This represents approximately 1/3 of all bids by Australian listed companies
- Approximately 70% of scrip bids (or about 60 transactions) could have resulted in shares issues of 25% or more. This represents nearly 1/2 of all bids by Australian listed companies
- Foreign bidders made approximately 30 scrip bids. Of those, about 1/3 appeared to require bidder shareholder approval

Table 2 - Scrip Takeovers – By Maximum Potential Share Issue/dilution level

