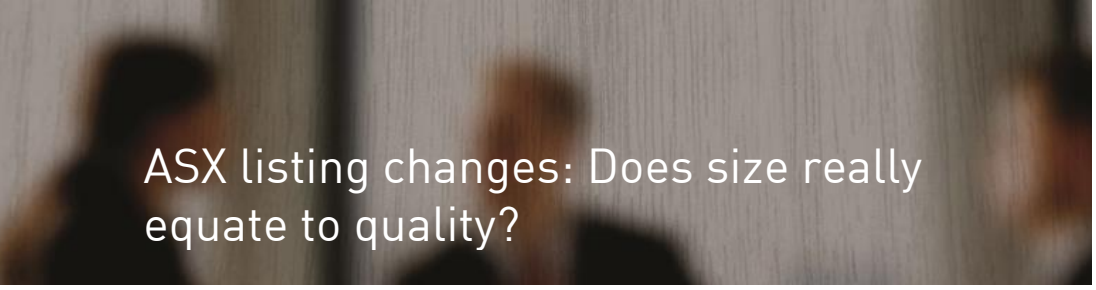

ASX listing changes: Does size really equate to quality?

HopgoodGanim LAWYERS

Immediate Changes

Suspension for back door listings

ASX currently allows the securities of a company that announces a backdoor listing to continue to trade up to the date on which its security holders are asked to approve the transaction. ASX then suspends trading until the entity has re-complied with the admission and quotation requirements.

ASX has changed this policy with immediate effect so that a company's securities will be suspended from the moment it announces the proposed transaction, until it has re-complied with ASX's admission and quotation requirements.

This is likely to put at least some pressure on backdoor listings as a path to the market – with an immediate suspension, the market will not have the opportunity to factor into the share price the perceived value of the transaction. The fundraising process that generally comes with a backdoor listing will similarly not have the benefit of any increase in value which is perceived from the transaction.

ASX discretion to refuse admission

The ASX has absolute discretion in deciding whether or not to admit an entity to the official list and to quote its securities.

The ASX has amended Guidance Note 1 to provide non-exhaustive examples of when ASX may exercise its discretion not to admit an entity to the official list. The examples reinforce the broad discretion of the ASX. Key examples include:

- ASX is not satisfied that the applicant has an appropriate structure and operations for a listed entity;
- ASIC or another corporate regulator has expressed concerns to ASX about the admission of the applicant to the official list; and
- ASX otherwise has concerns that admitting the applicant to the official list may put at risk the reputation of the ASX market as one of quality and integrity.

The ASX has also amended Guidance Note 1 to provide additional examples that may indicate that an applicant does not have an acceptable structure and operations for a listed entity, including:

- where the applicant has a vague or ill-defined business model or its business operations do not appear to ASX to have any substance;
- where the 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; and
- where the applicant's board has no directors with experience directing or managing a listed entity.

These aspects will need to be considered carefully as part of any IPO or backdoor listing planning process at an early stage.

Minimum free float of 20%

Currently there is no minimum free float rule imposed on companies seeking admission. Guidance Note 1 provides that ASX generally expects that entities will list with a free float of at least 10%.

The ASX has proposed the introduction of a specific rule requiring all applicants to have a minimum free float at the time of admission of 20%. The "free float" is the percentage of the entity's main class of securities that are not restricted securities or subject to voluntary escrow, and that are held by non-affiliated shareholders.

While the rule change will not have immediate effect, the ASX have stated that it is currently exercising its discretion to require all applicants to have a minimum free float at the time of listing of 20%. The rule change proposed will then formalise this position when it comes into effect. The ASX has stated that the requirement is aimed at "*striking an appropriate balance between supporting liquidity in the secondary market and supporting innovation and emerging growth industries*".

Proposed changes

Profit test - increased consolidated profit

For companies seeking to be admitted under the profit test, ASX is looking to increase the consolidated profit requirement in the year prior to admission from $400,000 to $500,000.

Assets test – increased NTA and market capitalisation

Currently, the minimum requirements for companies to meet the assets test are an NTA of at least $3 million, or a market capitalisation of at least $10 million.

The ASX has proposed to increase these thresholds to an NTA of at least $5 million or a market capitalisation of at least $20 million.

In the report, the ASX acknowledges that the current assets test provided a pathway for resource entities and tech start-ups to list and raise funds when other sources of funds were not available. It further stated that in 2015, there were 25 technology company IPOs undertaken, raising in excess of $1 billion. Twenty of these technology company IPOs were admitted under the assets tests, with 15 companies admitted under the NTA test and 5 companies admitted under the market capitalisation test.

Assets test – amended working capital requirement

All companies admitted under the assets test are currently required to have at least $1.5 million in working capital, after taking into account any budgeted revenue for the first full financial year after listing. For mining and oil and gas exploration entities, this $1.5 million in working capital must be available after allowing for budgeted administration costs, and the costs of acquiring plant, equipment and/or tenements.

Under the amended rule, all companies admitted under the assets test must have at least $1.5 million in working capital available after:

- taking into account the company's budgeted revenue for the first full financial year after listing; and
- allowing for the first full financial year's budgeted administration costs and the cost of acquiring any assets referred to in the prospectus, PDS or information memorandum (to the extent that those costs will be met out of working capital).

Assets test – new audited accounts requirement

The ASX has proposed that all companies seeking admission under the assets test must produce audited accounts for the last three years. However, if a company has been in operation for less than 3 full years, ASX will have a discretion under the proposed new rules to accept less than three full years of audited accounts.

Change to minimum spread requirements

The ASX is also looking at changes to the spread of the shareholder register which would mean companies could list with fewer shareholders, but the necessary dollar value of each security holder counted toward the spread is higher.

Currently, ASX's spread test can be satisfied in one of three ways:

- 400 security holders who hold a parcel of securities with a value of at least $2,000;
- 350 security holders who hold a parcel of securities with a value of at least $2,000, where there is a free float of at least 25%; or
- 300 security holders who hold a parcel of securities with a value of at least $2,000, where there is a free float of at least 50%.

The proposed change is that ASX requires:

- 200 security holders if the company has a free float of less than $50 million or 100 security holders if the company has a free float of $50 million or more; and
- each security holder counted towards spread must hold a parcel of securities with a value of at least $5,000.

Comments and implications

- It is interesting to see that while ASX was happy to allow the listing of junior exploration companies with no revenue and no certainty of success, given the current market conditions, they now appear to be taking a hard stance on start-ups seemingly because the business model is "ideas based".
- The new rules will make it harder for or prevent many innovative technologies from getting the early stage funding they seek by way of an ASX listing. As a result, alternative funding such as crowd-funding campaigns may become crucial to allow starts-ups to obtain the necessary funding to enable expansion. Unfortunately, the Federal Election has resulted in the Corporations Amendment (Crowd-sourced Funding) Bill 2015 (the new legislative regime to facilitate equity based crowd-funding) lapsing. This means that companies are limited to rewards based crowd-funding or wholesale investor equity crowd-funding until the Bill is reintroduced and passed by Parliament.
- NSX has offered for some time now lower qualifying hurdles for a company to be listed than ASX. The natural "knock-on" effect of these changes may well be that there is an influx of companies who will be seeking to list on the NSX. We expect that the NSX will be watching this consultation process with great interest. Similarly, there may be increased interest in other markets, including overseas markets such as TSX.

In the current political environment where the "innovation boom" is being touted as the answer to sustaining Australia's economic growth, a move which would inhibit the expansion of start-ups comes as a surprise. While the ASX believes that the changes will only concern a very small number of companies who are "too small to list", there is a possibility of wide reaching effects on the Australian economy.

It also remains to be seen whether ASX's apparent policy of "bigger equals better" is well placed. There are countless examples of both "big" and "small" companies which have not displayed quality and integrity. It may well be better to focus on the disclosure of all companies so that investors are equipped with all of the information they need to make an informed decision about their investments – rather than simply removing an entire slice of the market.

HopgoodGanim Lawyers will be making a submission in response to the ASX Consultation Paper, and welcomes feedback from any interested parties. For more information on the proposed changes or to contribute to HopgoodGanim Lawyers' submission on, please contact our Corporate Advisory and Governance team.