



Law Council  
OF AUSTRALIA

*Business Law Section*

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Dear Messrs,

### **ASIC proposal for amendments to the ASX class waiver**

The Corporations Committee of the Business Law Section of the Law Council of Australia (the **Committee**) welcomes the opportunity to comment on ASX Limited's recent class waiver to enhance capital raising flexibility, and is writing to suggest a potential enhancement.

#### **1. ASX class waiver of, or case by case relief from, listing rule 10.11**

As recently discussed, the Committee submits that ASX should consider either:

- granting a temporary class waiver from Listing Rule 10.11; or
- indicating that in appropriate cases it would consider case by case relief,

to permit the issue of securities under an institutional placement to a person to whom ASX Listing Rule 10.11 applies (**Person of Influence** or **10.11 parties**), without obtaining security holder approval, *but only to the extent necessary for them to maintain their existing percentage interest* in the listed entity (as determined on a reasonable endeavours basis as discussed in section 3.2).

We think that the arguments for this are particularly strong where Listing Rule 10.11 applies solely because the person is a person within Listing Rule 10.11.3 (10+% holder with board representation rights) or an associate of such a person, although there are good arguments that the principle should also apply in relation to persons within Listing Rule 10.11.2 (30+% holder) and indeed to all Persons of Influence.

The relief would facilitate urgent and critical fundraisings by listed entities in response to the SARS-CoV-2 pandemic and lockdown measures implemented to combat it, and could be further conditional on:

- any nominee director of a Person of Influence not voting on board resolutions on whether or not to conduct the offer and its terms (including size and pricing), and not participating in allocation decisions; and
- the listed entity being required to conduct a security purchase plan (**SPP**) in conjunction with the placement at an offer price no higher than the placement price (the requirement could be framed in a similar manner to the requirements under the recent Class Waiver applying to SPPs associated with 25% placements).

The policy rationale underlying Listing Rule 10.11 is that a 10.11 party is likely to be in a position of influence whether the entity issues, or agrees to issue, equity securities to it, as

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well as the terms on which the issue is made. ASX Guidance Note 25 states that the harm that Listing Rule 10.11 seeks to protect against is that the 10.11 party will exercise that influence to favour itself at the expense of the listed entity. Guidance Note 25 states that ASX will only waive the central requirement for security holders to approve an issue of equity securities to a 10.11 party, where it is clear to ASX that the harm Listing Rule 10.11 seeks to protect against is not present.

The harm that Listing Rule 10.11 seeks to protect against would not be present on the terms of the proposed relief.

## 2. Listing Rule 10.11

Listing Rule 10.11 states:

Unless one of the exceptions in rule 10.12 applies, an entity must not issue or agree to issue equity securities to any of the following persons without the approval of the holders of its ordinary securities.

10.11.1 A related party.

10.11.2 A person who is, or was at any time in the 6 months before the issue or agreement, a substantial (30%+) holder in the entity.

10.11.3 A person who is, or was at any time in the 6 months before the issue or agreement, a substantial (10%+) holder in the entity and who has nominated a director to the board of the entity (in the case of a trust, to the board of the responsible entity of the trust) pursuant to a relevant agreement which gives them a right or expectation to do so.

10.11.4 An associate of a person referred to in rules 10.11.1 to 10.11.3.

10.11.5 A person whose relationship with the entity or a person referred to in rules 10.11.1 to 10.11.4 is such that, in ASX's opinion, the issue or agreement should be approved by security holders.

The notice of meeting to obtain approval must comply with rule 10.13.

The policy underpinning this rule is stated in paragraph 2.2 of ASX Guidance Note 25:

The policy that underpins Listing Rule 10.11 starts from the premise that a 10.11 party is likely to be in a position to influence whether the entity issues, or agrees to issue, equity securities to them, as well as the terms on which the issue or agreement is made. The harm it seeks to protect against is that the 10.11 party will exercise that influence to favour themselves at the expense of the entity.

To address the potential conflicts involved and to minimise the risk of this harm occurring, Listing Rule 10.11 displaces the general rule that the board of directors (or, in the case of a listed trust, the responsible entity (**RE**) of the trust) is responsible for managing the business of the entity to the exclusion of its security holders and requires the issue or agreement to be approved by the holders of ordinary securities in the entity. 10.11 parties who will participate in the issue and their associates are precluded from voting on the resolution to approve it.

Listing Rule 10.11 was substantially broadened in its application with effect from 1 December 2019, as part of a range of changes to the Listing Rules and supporting guidance notes initiated by the ASX consultation paper *Simplifying, clarifying and enhancing the integrity and efficiency of the ASX listing rules* released on 28 November 2018. The previous application of Listing Rule 10.11 is explained in footnote 25 of ASX Guidance note 25:

Listing Rule 10.11.3 was introduced on 1 December 2019. Prior to that date ASX had a general practice of applying Listing Rule 10.11 to issues of equity securities to substantial holders with board representation and with approximately 25%+ shareholdings. It did so by exercising its discretion in that regard under Listing Rule

10.11.5 (then Listing Rule 10.11.2). ASX deemed it appropriate to change this practice to a rule in 2019 for better transparency and to extend it to substantial (10%+) holders with board representation. ASX considered that a substantial (10%+) holding along with board representation was sufficient to give a person influence over any equity raisings the entity may undertake. This change also aligned Listing Rule 10.11.3 more closely with Listing Rule 10.1.3.

The insertion of current Listing Rule 10.11.3 was not part of the changes in the initial consultation package, but its subsequent introduction is explained in the ASX paper *Simplifying, clarifying and enhancing the integrity and efficiency of the ASX listing rules – consultation response* released on 10 October 2019:

One respondent noted in relation to section 3.13 of GN 25 that ASX has previously indicated a holding of over 30% of an entity's ordinary securities or holding a lesser percentage of an entity's ordinary securities but with an attendant right to appoint a director is likely to mean the entity will be considered a related party by ASX. The respondent submitted that it would be helpful if ASX could clarify its position and specify these percentages in GN 25. ASX sees the merit in this suggestion but, on further reflection and for greater market certainty, ASX considers that this should be addressed in the LR rather than in guidance. ASX has therefore added to LR 10.11:

- a new LR 10.11.2 to extend LR 10.11 to “a person who is, or was at any time in the 6 months before the issue or agreement, a substantial (30%+) holder in the entity”;
- a new LR 10.11.3 to extend LR 10.11 to “a person who is, or was at any time in the 6 months before the issue or agreement, a substantial (10%+) holder in the entity and who has nominated a director to the board of the entity (in the case of a trust, to the board of the responsible entity of the trust) pursuant to a relevant agreement which gives them a right or expectation to do so; and
- a new LR 10.11.4 to extend LR 10.11 to an associate of a person referred to in rules 10.11.1 to 10.11.3,

and renumbered existing LR 10.11.2 to 10.11.5. It has also inserted new definitions of “substantial (30%+) holder” and “substantial (10%+) holder” in LR 19.12 and added new sections 2.4, 2.5 and 2.6 to GN 25 with guidance on these new provisions.

There are a number of exceptions to Listing Rule 10.11 in Listing Rule 10.12, including in relation to an entitlement offer taking up an entitlement, underwriting the offer and sub-underwriting the offer, and including an SPP. The policy basis for these exceptions is that participation by 10.11 parties is fair (and not likely to be subject to “exercise [of] influence to favour themselves”) where they have the opportunity to participate alongside and on the same basis as other security holders.

### **3. Reasons for the class waiver or case by case relief**

#### ***3.1 The Person of Influence would not be in a position to influence the offer***

The decision whether or not to conduct the placement and SPP, the amount to be raised, the price at which the securities would be offered, and any allocation to the Person of Influence would be decisions approved by the board of the listed entity in meetings at which any nominee of the Person of Influence would be required to excuse themselves from voting to comply with the conditions of the ASX relief.

As is customary, all existing institutional security holders would be expected to be offered their proportionate share in the placement to the extent practicable, having regard to the ability of the underwriters to contact and on-board them (contact is commonly via Bloomberg emails which secure a wide response, and the on-boarding process generally involves verification of investors' institutional status, as well as normal KYC and credit

checks), the existence of cornerstone support for the offer and legal constraints in investors' home jurisdictions. Under the proposed terms of the relief, the Person of Influence would not be eligible to subscribe for securities under the placement greater than its pro-rata share. Security holders that did not participate in the placement who have a registered address in Australia or New Zealand would be able to apply for up to \$30,000 of new securities under SPP. ASX could also require, consistent with the recent Class Waiver, that any scale back arrangements be applied on a pro rata basis to all participants.

Such an offer would be structured in a manner broadly consistent with the policy principles underlying certain exceptions to Listing Rule 10.11. Exception 1 (pro-rata offer) and Exception 4 (security purchase plan) are exceptions to Listing Rule 10.11 that ensure that all security holders have an equal opportunity to participate in the issue on the same terms and do not present an opportunity for 10.11 parties to acquire securities on more favourable terms than other security holders. Such an offer structure would allow most security holders to take up an allocation that is at least as large as the pro rata allocation they would receive in an entitlement offer of the same size as the placement. Many smaller security holders would be offered well in excess of a pro rata participation in the offer, and larger non-institutional security holders may be able to participate in the placement through a broker firm bid.

The Person of Influence would not subscribe for new securities under the placement at an offer price more favourable than other security holders. Security holders under the SPP would subscribe for securities at a price no higher than the placement price.

The Committee submits that the proposed arrangements for the terms, allocation and pricing of such an offer would allow security holders to have a substantially equal opportunity to participate in the offer (and in the case of retail security holders under the SPP, potentially at an offer price more favourable than the placement) and would not present an opportunity for the Person of Influence to exercise any influence it has with the listed entity to favour itself at the expense of the listed entity.

The Committee understands from discussions with ASX that ASX is concerned, if it were to give relief, that failure to offer the placement on a substantially pro rata basis to some institutions (for example because of foreign status), combined with scale back arrangements for the SPP, might make an offer unfair to some holders despite the fact that 10.11 parties could not increase their existing percentage interest.

In practice, in our experience, in most registers the net total effect of:

- exclusion of some institutions arising from inability of the underwriters to contact and on-board them in the available time, or unwillingness to accept credit risk on them, or legal constraints in their home jurisdictions; and
- other shareholders not receiving an opportunity to apply for, and (if they apply) be allocated, their full theoretical pro rata share of the offer under the SPP,

is very minor.

We do not believe that ASX should impose a rigid condition on the proposed relief requiring pro rata treatment of shareholders, given that there will always be some imperfections even where pro rata treatment is sought to be maximised (including because of imperfection of information about existing holdings).

However, if ASX is concerned about this aspect, we suggest it consider an approach involving case by case relief (we understand that this is ASX's preference in any case), and stating, in any public statement or internal policy regarding the potential availability of such relief, that it would expect applicants for the relief to be able to demonstrate to ASX's satisfaction that the structure of the placement and SPP is fair to shareholders and does not improperly advantage the Person of Influence. ASX would then be free to substantively consider the offer structure proposed by an applicant, and grant relief where satisfied it was fair – this could include consideration of factors such as:

- SPP structure, including absence of a cap or adequacy of the cap to accommodate pro rata demand by shareholders, based on reasonably expected levels of take-up;

- expectation of substantial pro rata opportunities for institutional shareholders having regard to all factors including any jurisdictional exclusions.

A further matter which could be considered as part of a more general discretion, would be variants where a waiver is only sought to permit a Person of Influence to take up *part* of what would otherwise be its pro rata share of a raising. In that case, we expect that ensuring fair treatment for other shareholders would be likely to involve an expectation they would have the opportunity to participate up to a substantially similar proportional level.

Further, where 'pro-rata' demand or participation is referred to in any relief, the concept should be framed as a 'reasonable endeavours' standard for the applicant, with the ability to rely on information provided by shareholders and the most recently available registry analytics, without the need to reconcile assumed holdings.

### **3.2 A lower threshold for influence means a lower threshold for waivers**

The Committee does not question generally the tightening of ASX's rules in relation to issues of equity securities to persons of influence. However, the Committee does note that ASX has now set this threshold at a relatively low 10%. By way of comparison, the takeover threshold in the *Corporations Act 2001 (Cth)* for a stake which may give control or influence and the threshold in the *Foreign Acquisitions and Takeovers Act 1975 (Cth)* for a significant action to be deemed a change of control involving the acquisition of securities by a foreign person who is not a foreign government investor are set at 20%.

As noted above, the Committee considers that there are good arguments to apply the relief to all Persons of Influence.

However, even if ASX disagrees, the Committee submits that the relatively low "substantial (10%) holder" threshold (and indeed the "substantial (30%+) holder" threshold, given such a person may also have no real control) means ASX should be open to exercising its discretion to provide a waiver in appropriate cases.

### **3.3 Impact of SARS-CoV-2 and lockdown measures to combat it on equity offers**

The COVID-19 pandemic and the efforts of governments to mitigate its impact, are having material impacts on the capital position of many entities listed on ASX. ASX has already provided class waivers in response.

In this market, there is no assurance an equity raising will succeed, and there are several examples of equity raisings that have not succeeded or have struggled.

A placement structure is generally the most executable offer structure, does not require sub-underwriting and achieves the tightest pricing, and these considerations are particularly important at a time of heightened volatility. The ability to conduct the placement in the present market, and the ability to procure underwriting, may be prejudiced should a Person of Influence not be permitted to subscribe for securities. Participation by a Person of Influence can also be positive in terms of securing better pricing and investor support for the capital raising, given it demonstrates confidence by the Person of Influence and tightens demand.

As noted above, placements by listed entities are generally conducted on the basis that each eligible institutional security holder will be offered substantially a pro rata share in the placement, subject to some qualifications. This will generally be done on a best endeavours basis by reference to the listed entity's most recent registry analysis, but without undertaking exhaustive processes to reconcile assumed holdings (e.g. for recent trading or swap positions) when determining a security holder's 'pro rata' share of the placement. The absence of such reconciliation processes, necessary for an entitlement offer, also assists with timing of offer launch and the conduct of the bookbuild process, but in our experience does not prejudice the application of a substantially pro rata approach.

An ASX waiver to permit a Person of Influence to participate in a placement that is conducted in conjunction with an SPP would materially improve the prospects the offer is successful and provide listed entities with needed equity in a difficult market to raise capital.

### **3.4 Actions by other securities exchanges**

The Committee understands other regulators have relaxed their equivalent rules in the context of COVID-19. The Committee understands NYSE have provided a waiver until 30 June 2020 of Section 312.03(b) that permits issues and sales of securities to related parties, regardless of percentages issued, provided that:

- the sale is for cash at a price no less than the minimum price;
- the transaction is reviewed and approved by the company's audit committee or a comparable committee comprised solely of independent directors; and
- proceeds from the sale of securities to the related party will not be used to fund an acquisition of stock or assets of another company in which the related person has a direct or indirect interest or assets to be acquired or in the consideration to be paid for such acquisition.

As a result of the NYSE waiver, the NYSE's shareholder approval rule for related party transactions will temporarily be consistent with Nasdaq's Marketplace Rule 5635(a)(2). The Committee notes the waiver does not apply to transactions that implicate a change of control and, as a result, shareholder approval would still be required under that rule if the issuance also constitutes a change of control. No change of control or influence is proposed in the present case.

The Committee also understands NZX has given class relief to permit insiders to take up to 10% of securities on issue without regulatory or member approvals and this is not subject to any additional conditions.

The Committee notes that the relief requested here (whether granted on a class waiver or a case by case waver basis) does not go as far as the NYSE example, as it would only apply to allow the 10.11 party to maintain its pro rata holding. In this regard it would be consistent with the policy considerations underlying a number of the existing exceptions to Listing Rule 10.11.

If you have any questions please contact the Chair of the Corporations Committee Shannon Finch ([shannonfinch@jonesday.com](mailto:shannonfinch@jonesday.com) or +61 428 894 002) in the first instance.

Yours sincerely,



**Greg Rodgers**  
**Chair, Business Law Section**