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CORPORATE UPDATE

**MINING COMPANY ONE DAY, TECHNOLOGY COMPANY THE NEXT:
EXPLAINING THE HYPE AROUND REVERSE TAKEOVERS/BACKDOOR LISTINGS**

This year has seen a sharp increase in backdoor listings (also known as reverse takeovers) on the Australian Securities Exchange (ASX), to a level that has not been experienced since the peak of the dotcom boom. There has been a great deal of media attention dedicated to backdoor listings in recent times, and this article aims to give a broad overview of what is involved in undertaking a backdoor listing. This article also includes some of our top tips in navigating a backdoor listing, to ensure that the process runs as smoothly and efficiently as possible.

WHAT IS A BACKDOOR LISTING?

ASX Guidance Note 12, which deals with significant changes to activities, defines the backdoor listing process in contrast to the "front door" listing process. A backdoor listing involves an undertaking becoming listed on the ASX by being "injected" into an existing listed entity, rather than undertaking the more conventional process of being listed in accordance with the application process under the ASX Listing Rules. A backdoor listing usually takes the form of the existing listed entity purchasing the undertaking, in exchange for an issue of securities to the vendors of the undertaking, and/or a payment of cash to the vendors.

The backdoor listing process usually involves a requirement to obtain approval of shareholders of the listed entity, including for one or more of the following reasons:

- As mentioned above, the process often involves the issue of securities to the vendors of the undertaking being backdoor listed, as consideration for the sale. Depending on the percentage ownership that the vendors will obtain, shareholder approval may be required under the *Corporations Act 2001* (Cth) (if the percentage is 20% or greater) and the ASX Listing Rules (if the percentage exceeds the listed entity's existing placement capacity).

- The listed entity may be required to obtain shareholder approval in connection with any proposed change in the nature or scale of its activities, in connection with the backdoor listing (explained in greater detail below).
- If the process involves any related party transactions, then these may also require shareholder approval under the *Corporations Act 2001* (Cth) and the ASX Listing Rules.

The end result of a successful backdoor listing process is that the listed entity maintains its listing on the ASX, but has a different ownership structure, different board of directors and senior management, and (in many cases) different nature and scale of activities.

WHY UNDERTAKE A BACKDOOR LISTING?

Obtaining a listing on the ASX can provide many advantages. For example, a company listed on the ASX has access to a wider pool of investors and potential investors, which can be useful when the company needs to raise further capital. In addition, an ASX-listed status may have advantages in dealing with customers in certain industries. A backdoor listing process may also revitalise an already listed entity, resulting in it undertaking more profitable and viable activities, which in turn may create greater value for shareholders.

The sudden and recent surge in backdoor listings has come about for a number of reasons. According to some sources, the recent downturn in the resources sector has left a surplus of small exploration companies on the ASX that are (sometimes) short on cash. Given the reduced levels of operations, some of these companies consider that there would be a low likelihood of successfully raising required levels of further working capital by way of a capital raising.

While some consider that a backdoor listing is a quicker, cheaper and easier way of gaining an ASX listing, opinions remain divided on this issue. Interestingly, Australian Securities and Investments Commission (ASIC) commissioner John Price has recently issued a word of caution to investors and directors in the context of backdoor listings, especially where there has been insufficient disclosure of proposed changes of activities, how this will affect a company's business plan, and how

this will affect working capital requirements. In addition, ASIC has raised concerns about the independence of some independent experts providing reports in the context of proposed backdoor listings.

ASX has also responded to the recent increase in backdoor listings by releasing revised Guidance Note 12, which provides further detailed guidance on backdoor listings (and which is explored in greater detail below).

WHERE THINGS CAN GO WRONG

Backdoor listings usually involve a considerable degree of complexity over and above that which is normally associated with a "front door" listing. As such, it is important to be prepared, and to consider all relevant factors in determining whether (and how) to proceed with a backdoor listing. Outlined below are our top tips to keep in mind:

- **Review the proposed business plan:** Both the listed entity and the undertaking it proposes to acquire will need to be satisfied that there are commercially justifiable reasons for proceeding with a backdoor listing. In addition, the parties will need to ensure a smooth transition to the new business plan, so as to maximise value for shareholders.
- **Engage with the ASX early:** The ASX Listing Rules confer wide-ranging discretion on the ASX in considering proposed backdoor listings. Engaging with the ASX sooner rather than later increases the likelihood that any issues will be dealt with promptly, so as to avoid the transaction timetable being subject to lengthy delays. This is consistent with Guidance Note 12, which notes that ASX will be able to provide general advice on the application of relevant ASX Listing Rules, including any steps the entity will need to take to re-comply with admission requirements.
- **Have a clear and realistic timetable for the proposed backdoor listing:** Backdoor listings can be complex and time-consuming, and there are many factors that can contribute to delays in the process. The following are some of the important aspects to keep in mind:
 - **Consider what level of due diligence will be required:** Both the listed entity and the undertaking it proposes to acquire will need

to undertake due diligence on each other. The listed entity will need to ensure that the other undertaking has a sound business plan, and can deliver value to shareholders. On the other hand, the undertaking proposed to be acquired will need to ensure that it will not encounter any unanticipated (and unwanted) liabilities after the backdoor listing is completed. There are a number of strategies which can be considered to mitigate such risks.

- **Factor in time required to obtain shareholder approvals:** Remember that a notice of meeting needs to be prepared, which will require engaging with lawyers and other advisors. Preparation of the notice of meeting may also require engaging with an independent expert and obtaining a report from such expert, which can be a lengthy process. The notice of meeting needs to be reviewed and approved by the ASX, which adds to the timeline. Finally, the 28 day notice period (plus time for the notice to be despatched to shareholders) needs to be factored into the timeline.
- **Consider whether a prospectus (or similar document) will be required for the proposed backdoor listing:** While backdoor listings are often considered to be a convenient means of bypassing the need to issue a prospectus, this is most often not the case. Unless the listed entity and the undertaking it proposes to acquire have similar businesses of a similar scale, it is likely that a prospectus (or other disclosure document) will need to be issued. Preparing a document such as a prospectus (and ensuring its contents have been verified) can be a costly and time-consuming process, and this should be factored in to the transaction timetable.
- **Consider what other transaction documents will be required:** The parties will likely agree an outline of the process, including its proposed timing, the circumstances in which the process can be terminated, and so on. This often takes the form of an implementation agreement. In addition, the transaction will involve a change in ownership of the undertaking

proposed to be listed, in exchange for which the vendors will be issued shares and/or paid cash. This transaction will be documented in a share sale agreement. Depending on the precise circumstances of the transaction, other transaction documents may be required.

- **Consider whether further funding is required in connection with the backdoor listing:** Depending on the current cash reserves of the listed entity, execution of the business plan may require it to undertake a capital raising at the same time as or shortly after the backdoor listing is finalised. Similarly, any cash required to be paid to the vendors might be sourced through a capital raising. Depending on the precise form of capital raising, this may involve lodgement of another disclosure document and/or shareholder approval. Any such factors need to be factored into the proposed timing by which the overall transaction will occur.
- **Pay careful attention to continuous disclosure obligations:** The listed entity will need to ensure that it has adequate procedures and protocols in place to allow it to continue to rely on any relevant exceptions to its continuous disclosure obligations under the ASX Listing Rules. Of paramount importance in this regard will be ensuring that relevant information remains confidential throughout the process of negotiations with the vendors of the undertaking proposed to be acquired. Again, continuous disclosure obligations will be relevant at the time agreements are executed by the parties.
- **Consider whether any conditions of admission or quotation will need to be re-complied with:** If ASX requires the conditions for admission and quotation of the entity's securities to be re-complied with, this could give rise to a requirement for extra transaction steps to be undertaken. For example, if the entity's shares are trading at less than 20 cents each, then a share consolidation may be required.

WHAT ASX GUIDANCE IS AVAILABLE?

As mentioned above, ASX Guidance Note 12 deals with significant changes to activities. Guidance Note 12 provides guidance to assist listed entities and their advisors to understand how ASX applies the ASX Listing Rules dealing with significant changes to a listed entity's nature or scale of activities. These provisions are outlined in Chapter 11 of the ASX Listing Rules, which is relevant to backdoor listings as follows:

- ASX Listing Rule 11.1 provides that if an entity proposes to make a significant change, either directly or indirectly, to the nature or scale of its activities, it must provide full details to ASX as soon as practicable, and must do so before making the relevant change.
- Under ASX Listing Rule 11.1.2, ASX may require the listed entity to seek the approval of holders of ordinary securities. In these circumstances, the entity must comply with any requirements of ASX in relation to the notice of meeting.
- Under ASX Listing Rule 11.1.3, ASX may require the listed entity to again meet the requirements in Chapters 1 and 2 of the ASX Listing Rules (dealing with admission to the official list of ASX and quotation of securities) as if the entity were applying for admission to the official list of the ASX.

On 30 September 2014, ASX released an updated version of Guidance Note 12, which can be accessed by clicking [here](#). Further detail is set out below.

The main circumstances in which ASX will apply ASX Listing Rules 11.1.2 and 11.1.3

In the context of potential backdoor listings, Guidance Note 12 provides that ASX will carefully examine any proposed transaction, notified to it under ASX Listing Rule 11.1, that involves a listed entity acquiring a business from, or merging or amalgamating with, a non-ASX listed entity, and which is likely to result in a **doubling** or more of any of the listed entity's:

- consolidated total assets;
- consolidated total equity interests;
- consolidated annual revenue (or in some cases, consolidated annual expenditure);

- consolidated annual profit before tax and extraordinary items; or
- total securities on issue (on a fully diluted basis).

Guidance Note 12 now expressly states that a transaction that does not result in a doubling (or more) of any of the above measures will not be regarded by ASX as a backdoor listing. On the other hand, Guidance Note 12 also provides that a transaction resulting in a doubling (or more) of any of the above measures does not necessarily mean that ASX will regard the transaction as a backdoor listing (but ASX will examine any such transactions more closely to determine whether they are backdoor listings).

Guidance Note 12 provides that ASX will usually use the entity's most recent published financial statements, or its Appendix 3B filings with ASX, to determine whether the entity has 'doubled up' in any of the measures mentioned above.

Circumstances in which an information memorandum can be lodged

Guidance Note 12 now states that where ASX exercises its discretion under ASX Listing Rule 11.1.3 to require an entity to re-comply with ASX Listing Rule requirements, ASX may agree to accept an information memorandum in lieu of a prospectus or product disclosure statement.

This is only relevant where the entity is not making an offer of securities in connection with the significant change in activities, and the information memorandum must comply with minimum content requirements as set out in Guidance Note 12 (including that it contains a statement that the entity has not raised any capital during the previous three months, and will not need to raise any capital during the next three months).

Minimum requirements to maintain an ASX listing, and documents to be provided to ASX.

Revised Guidance Note 12 provides restated guidance as to how ASX will apply minimum requirements in the context of an entity re-complying with Chapters 1 and 2 of the ASX Listing Rules. In particular, revised Guidance Note 12 includes restated guidance on meeting minimum spread requirements, meeting the profits test or assets test (and the circumstances in which each

will be applied), how ASX will apply the escrow requirements for restricted securities (including in connection with capital raisings undertaken to achieve re-compliance), how ASX will apply the "20 cent rule" (which may require a listed entity to undertake a consolidation of securities in order to boost the value of securities to 20 cents or more) and how ASX will apply the rule regarding minimum option exercise price.

Revised Guidance Note 12 also sets out the circumstances in which a listed entity will be required to cure past breaches of the ASX Listing Rules (for example, where financial statements have not been audited, reviewed and/or lodged), and also sets out other documents that are required to be provided to ASX (for example, a reviewed pro forma statement of financial position, together with the review, as if the listed entity were being admitted to the official list of the ASX for the first time).

Guidance Note 12 also provides that ASX may require an entity to disclose information over and above what would otherwise be required to be lodged on an application for admission to the official list of the ASX (including the non-listed entity's financial statements).

Contents of notices of meeting

Guidance Note 12 provides further guidance on the information that ASX considers should be included in a notice of meeting seeking shareholder approval for a transaction in connection with ASX Listing Rule 11.1.2, including details as to the material terms of the transaction, proposed capital raising requirements in connection with the transaction, proposed changes to the board or senior management of the entity in connection with the transaction, and the proposed timetable for implementing the transaction.

CONCLUSION

There has been a great deal of recent media attention dedicated to backdoor listings, with a significant amount of commentary to the effect that they are a quicker, cheaper and easier way of obtaining a listing on the ASX. While opinion on this issue remains divided, companies considering a backdoor listing should be aware of the complexity associated with backdoor listings and should be aware of the importance of seeking advice from an

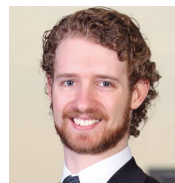
early stage. Planning and preparation in the early stage (especially in the context of the timetable by which the transaction is proposed to proceed) should assist in ensuring that the transaction proceeds as smoothly and efficiently as possible.

MORE INFORMATION

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