COVID-19: PRESSURE POINTS: EQUITY RAISING IN THE FACE OF COVID-19 (AUSTRALIA)

24 March 2020 | Australia
Legal Briefings – By **Tim McEwen**

In this current environment of uncertainty, we have set out a refresher on the three main capital raising alternatives available to ASX listed entities that may be seeking to bolster their balance sheets.

For many listed entities it will be a complicated question whether to raise or not and, if so, how, particularly given the current volatility of global stock markets and the uncertainty as to how things will develop.

While the Australian securities market and the economy roil, the equity raising rules still apply and need to be complied with. We have seen regulatory intervention for the temporary relaxation of insolvency laws and ASIC's relaxation of rules around the timing and procedures for AGMs. There is now consideration being given to whether ASX and ASIC should follow the lead of the NZX and temporarily increase the placement capacity of listed companies from 15% (NZX has moved from 15% to 25% until 31 October 2020) and the security purchase plan (**SPP**) limit from $30,000 (NZX has increased the limit to NZ$50,000 until 31 October 2020) and shorten the timetables for rights issues. Consideration is also being given to whether ASIC may allow greater latitude for trading suspensions to extend beyond the current five business day limit without leading to the need for a prospectus for an equity raising.

However, at the moment the equity raising rules and related aspects such as the Takeovers Panel's guidance on related party underwriting of rights issues (Takeovers Panel Guidance Note 17 Rights Issues) continue.

An ASX listed entity is faced with three main options to raise equity.

A RIGHTS ISSUE MADE PRO RATA TO EXISTING SHAREHOLDERS

A rights issue can be renounceable (with or without rights trading on ASX) or non-renounceable in which case it is limited to being no greater than 1:1 without security holder approval.

Unless the listed entity has been suspended for more than five trading days in the previous 12 months, is not in compliance with its financial reporting or continuous disclosure obligations or has been banned by ASIC from doing so, the rights issue can be made through the issue of a cleansing statement and without a prospectus.

The key disclosure obligation of a listed entity in relation to a rights issue is to disclose all ‘excluded information’, being information which is being withheld from disclosure under Listing Rule 3.1 and which information is reasonably required for making an informed assessment of the listed entity’s financial position and performance and prospects.

Despite the reference to ‘prospects’, the disclosure for a rights issue is not required to include a financial forecast. Consideration will need to be given to what prospective information can be provided.

The rights issue can be made on an accelerated or non-accelerated timetable as set out in the Listing Rules. An accelerated offer will have funds from the institutional component of the offer received by approximately business day 5 and the offer completed by approximately business day 17 to 21. A non-accelerated offer will have funds received by approximately business day 18.

A rights issue can be combined with a placement.

Any underwriting of a rights issue, in particular by a related party, will need to be appropriately structured having regard to the Takeovers Panel’s guidance on control. See Takeovers Panel Guidance Note 17.

A PLACEMENT OF SHARES TO INSTITUTIONAL INVESTORS, POTENTIALLY FOLLOWED BY A SECURITY PURCHASE PLAN

A listed entity is generally limited to issuing no more than 15% of its issued shares in a 12 month period subject to particular exceptions (including a rights issue). The shares offered in a placement can be issued to institutional investors who do not require a prospectus and the offer is not limited to existing security holders. A related party of the listed entity, including a director cannot participate in a placement (related parties can participate in a rights issue).

On a similar basis to when a rights issue can be made with a cleansing statement, to allow the placement securities to trade on ASX, the listed entity needs to issue a cleansing statement and ensure that all excluded information is disclosed.

A placement can be completed within five business days of announcement.

While not a pro rata offer, our experience is that existing institutional security holders are generally offered their pro rata amount of the placement.

A placement is generally limited to investors who do not require the issue of a prospectus. To enable retail shareholders to participate in the overall equity raising, it is common for the listed entity to also offer securities under a security purchase plan (**SPP**). *ASIC Corporations (Share and Interest Purchase Plans) Instrument 2019/547* enables the SPP offer to be made to shareholders without a prospectus and in reliance on the cleansing statement used for the placement. Under the SPP security holders can apply for up to $30,000 of new securities each. The SPP amount can be capped.

We identified the combination of placements and SPPs as a trend for 2020 in our 2019 Australian IPO Review: 2020 Predictions. We expect that this offer structure will now be even more common in the current circumstances and in particular if ASIC and ASX increase listed entities' placement capacity beyond 15%.

Appropriately structured, a placement and SPP can effectively ensure that most retail shareholders are able to access at least their pro rata amount of the overall placement and SPP offer (therefore almost equivalent to a rights issue). The pricing of the SPP can take account of falls in the listed entity's market price after the placement with shareholders able to apply at the lesser of the placement price and a specified discount to the five day VWAP up to the close of the SPP offer. This provides a protection to retail shareholders that is not available in a rights issue, which requires a fixed price across the whole offer period.

A CONVERTIBLE NOTE, CONVERTIBLE INTO ORDINARY SECURITIES IN ACCORDANCE WITH ITS TERMS

While not an immediate equity raising, the convertible note structure allows a new (or existing investor(s), but not a related party, unless shareholder approval is obtained) to invest into a listed entity with a security that ranks above ordinary securities and potentially alongside or behind existing debt arrangements.

Convertible notes are popular with institutional investors such as private equity investors or special situation funds. The convertible notes will not usually trade on ASX.

The notes (including in many cases, capitalised interest) can be converted, usually at the option of the holder, up to a maturity date. The note terms can include anti-dilution adjustments, for example, for rights issues or placements, and various other protections for the holder(s).

To be able to issue convertible notes, the listed entity needs to have sufficient available placement capacity taking account of the then expected number of securities to be issued on conversion.

CONCLUSION

The potential for a listed entity to raise equity continues to exist in the current markets and circumstances. Such an equity raising will give rise to various structural and disclosure issues, however, these can be navigated. We have experience in each of these equity raising options. If we can be of any assistance, please phone, or email any of these key contacts:

More on navigating the COVID-19 outbreak

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.

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