SWAAB

A PRACTICAL GUIDE TO REVERSE TAKEOVERS UNDER AUSTRALIAN LAW

A COURTESY GUIDE PREPARED BY SWAAB ATTORNEYS

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Overview of Reverse Takeovers

To put it simply, a reverse takeover (RTO) is the acquisition of a public company by shareholders in a (usually smaller) private company.

An RTO can be effected by the private company's shareholders selling their shares in the private company to the public company in exchange for the issue of shares in the public company. Alternatively the private company can sell its business to the public company in exchange for the issue of shares in the public company to the private company.

An RTO is often considered as an alternative to an initial public offering (IPO), and where the target public company is listed, an RTO can also be known as a 'backdoor listing'.

A 'backdoor listing' is generally considered to be a cheaper, easier and quicker way to list a company on a stock exchange. There are also a number of other reasons for using an RTO, including:

- it may result in less share dilution (and therefore greater control) in the company for the original shareholders, than in a typical IPO;
- to avoid triggering a change of control clause in a key contract;
- to circumvent the blocking power of a dissenting shareholder;
- to minimise exposure to market conditions in listing;
- the listed company will already likely satisfy certain conditions for listing that the private company may struggle to achieve through an IPO (particularly the pre-existing spread of the listed company's shareholder base);
- shareholders of the private company are usually eligible for capital gains tax rollover relief if certain conditions are satisfied;
- the funds expended to purchase the listed company will provide a tangible asset (in contrast to an IPO where the major costs of listing go to third parties and are lost).

An RTO does have some disadvantages relative to an IPO. These include:

- a potential premium on the price of the listed company (the price of the listed company is often greater than the value of its net tangible assets);
- exposure to pre-existing contingent liabilities of the listed company, such as unpaid creditors, employee liabilities and ongoing contractual obligations;
- the possibility of the Australian Securities Exchange (ASX) requiring that shares issued to some or all incoming shareholders be subject to mandatory escrow.

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Overview of the reverse takeover process

KEY STEPS

Some key steps that may be required before acquiring a public listed company include:

- a potential premium on the price of the listed company (the price of the listed company is often greater than the value of its net tangible assets);
- finding a listed shell company and either buying control of the listed shell company for cash or taking control of the listed shell company by vending in the business of the private company;
- seeking 'buy-in' from the board and major shareholders of the private company;
- signing a heads of agreement outlining the key terms of the acquisition;
- completing due diligence on the listed company;
- executing a formal legal agreement relating to the takeover;
- following the re-compliance requirements under the ASX Listing Rules;
- holding a general meeting of shareholders to approve changes in the nature and scale of the company as a result of the RTO under ASX Listing Rule 11.1 (or in relation to other approvals required under the ASX Listing Rules);
- raising capital to grow the business and issuing a full prospectus (if necessary);
- formally reinstating the company's securities to quotation on the ASX.

SHAREHOLDER APPROVAL

Whilst RTOs are not prohibited by the Corporations Act 2001 (Act), the Takeovers Panel (Panel) may declare 'unacceptable circumstances' have occurred in relation to an RTO, where the shareholders of the bidding company are not given the chance to approve it, particularly where the RTO has a material effect on 'control', or prevents rival bids.

ASIC strongly suggests that it is informed if an RTO is being contemplated in order to consider whether shareholder approval is required.

DIRECTOR DUTIES

In an RTO directors are bound by the same fiduciary and statutory obligations that regulate their conduct generally.

Directors' duties are particularly relevant where board action prevents alternative bids for the company and that action is not approved by shareholders.

REGULATIONS

The ASX Listing Rules impose a requirement for shareholder approval on listed companies in certain circumstances.

Under Listing Rule 7.1, a listed company is prohibited from issuing, in any 12 month period, ordinary securities which represent more than 15% of the issued ordinary share capital of the company (subject to various exemptions).

In relation to RTOs, Exception 5 in Listing Rule 7.2 exempts issues under an off-market bid or scheme of arrangement.

CONTACT US

The corporate team at Swaab Attorneys is committed to working with companies to help them meet their ambitions. If we can help you with any of the issues raised in this Guide, please contact Alistair Jaque. We would be very pleased to discuss any issues with you.

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This Guide is only intended to give an overview of the issues involved. It is not intended to be fully comprehensive or to be a substitute for legal advice.

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