FINANCIAL REVIEW

SE News - Opinion

HD **ASX loopholes crush shareholders**

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WC 654 words
PD 1 May 2014
SN The Australian Financial Review
SC AFNR
ED First
PG 54
LA English


LP

Scrip takeovers Holes in the ASX listing rules, almost unknown anywhere else, allow management teams to undertake expensive flights of fancy. Martin Lawrence

The "merger of equals" between **oil** and gas explorers and producers Roc **Oil** and Horizon **Oil** illustrates the bizarre hole in the ASX listing rules that allows shareholders of bidders to be infinitely diluted without protection. The risk of this regulatory oversight is now starkly apparent for Roc shareholders, who have no say over the transaction, regardless of their view on its merits.

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As pointed out by The Australian Financial Review columnist Trevor Sykes, among others over the years, the current listing rules allow a **company** to "acquire" another **company** through a scrip takeover offer with no bidder shareholder approval required – even if, as is the case with the ROC-Horizon deal, Roc shareholders will hold only 42 per cent of the merged **company**.

The general rule is that shareholder approval is required when an issue (without pre-emptive rights) would expand the capital base of an ASX-listed **company** by more than 15 per cent in any 12-month period. Listing rule 7.2 explicitly exempts shareholder approval for an issue of securities that is consideration for a takeover offer or which would fund one.

Lest shareholders think that this loophole is exploited only by smaller companies, it is the reason why shareholders of Oxiana had no say in the ill-fated "merger of equals" with Zinifex. It was also exploited by Alinta when it selected the structure for its audacious attempt to acquire AGL in 2006. That deal would have diluted Alinta shareholders by 75 per cent without any Alinta shareholder approval whatsoever.

The existence of the loophole in listing rule 7, combined with the reluctance of the ASX to apply listing rule 11 to give shareholders veto rights over significant transactions, puts Australia at odds with most comparable jurisdictions. Few other wealthy countries give so much latitude to boards to dilute shareholders in the context of a takeover offer.Inconsistency in rules

Shareholders of UK companies can veto very large transactions; an opportunity that Rio Tinto shareholders now wish they had taken up when reflecting on their endorsement of the $40 **billion acquisition** of Alcan in 2007. Even the normally oppressed shareholders in US companies have the right to approve dilutive takeovers above a certain threshold, as do shareholders investing in **Hong Kong**- and Singapore-listed entities. Even in South Africa, shareholders of Woolworths, now bidding for David Jones, will have an opportunity to veto the deal.

The glaring inconsistency in the ASX rules, which allows bidder shareholder private property rights to be trampled on by the transaction industry, cries out for intervention. The Council of Financial Regulators reform agenda put forward late last year would empower ASIC (subject to ministerial approval) to direct a market operator such as ASX to adopt a listing rule with specified content.

The present regime allows management teams to embark on costly and risky flights of fancy without shareholder limitation. Owners are left only with the imperfect remedies of a meeting to eject a board while the transaction timetable is ticking, selling their shares or punishing management long after the event. Worse, the discretionary application of listing rule 11 creates the worst kind of rule, enforced only when those tasked with enforcement deem it expedient to do so.

The existence of these lax rules benefits nobody outside of the transaction industry. If the ASX wished to demonstrate to investors that it had their best interests at heart, it would immediately remove the inconsistency that requires shareholder approval for a placement representing 16 per cent of shares on issue to fund the **purchase** of an asset but exempts from approval a share issue diluting shareholders by 75 per cent to fund a takeover.

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**CO** rocoil : Roc Oil Company Ltd

**IN** i1 : Energy | i13 : Crude Oil/Natural Gas

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**AN** Document AFNR000020140430ea510002j