



## **GUIDANCE NOTE 17: RIGHTS ISSUES**

### **Overview**

This Guidance Note provides takeovers market participants with guidance on:

- (a) circumstances that the Panel is likely to declare to be unacceptable in relation to rights issues which have, or are likely to have, an effect on:
  - (i) control, or potential control, of a company<sup>1</sup>; or
  - (ii) the acquisition, or proposed acquisition, of a substantial interest in the company; and
- (b) what actions the Panel may take to remedy unacceptable circumstances in relation to such rights issues.

This Guidance Note generally relates to rights issues that seek to rely on the exceptions in item 10 or item 13 of section 611 of the Corporations Act 2001 (**Act**) from the 20% takeovers threshold in section 606(1) of the Act.

The exceptions in item 10 and item 13 of section 611 are two of the gateways through the takeovers regulation of Chapter 6. The applications which have come to the Panel are representative of long standing concerns that these exceptions may be open to abuse. Since the days of the NCSC and the Companies Code, regulators and the market have been concerned about the potential for rights issues being structured and used as a way of effecting a control change without having to comply with the provisions which would normally regulate control transactions.

In some cases which have come before the Panel, it has found that rights issues which fell within the exceptions in item 10 or item 13 gave rise to unacceptable circumstances. A very wide range of issues have been raised as contributing to those specific rights issues giving rise to unacceptable circumstances.

The Panel is concerned to ensure that any guidance it publishes does not interfere inappropriately with the very large number of rights issues which companies conduct which have very little potential effect on control. Similarly, the Panel does not wish to harm the shareholders of small cap companies for whom rights issues, often with potential control effects, may be essential elements of their funding and survival, by eliminating rights issues from the capital management tools of their directors.

---

<sup>1</sup> This Guidance Note applies equally to rights issues undertaken by managed investment schemes. In such instances references to shares include interests and references to shareholders include interest holders.

Distinguishing which rights issues will and will not give rise to unacceptable circumstances is dependant on the individual circumstances of the company and the rights issue. It is not possible to set out a safe harbour for structuring a rights issue which will not give rise to unacceptable circumstances.

In this Guidance Note, unless the context otherwise requires:

- (a) references to companies should be taken to be references to listed companies, unlisted companies with more than 50 shareholders and listed managed investment schemes; and
- (b) references to sections should be taken to be references to sections of the Corporations Act (*Cth*) 2001.

### **Background**

1. A “rights issue” is an issue of new shares offered to existing shareholders<sup>2</sup> of a company in proportion to their existing holdings. A rights issue is offered to all existing shareholders individually and may be rejected, accepted in full or (in a typical rights issue) accepted in part by each shareholder. Rights issues may be renounceable or non-renounceable. In a renounceable rights issue the rights can be traded if there is a market for them (renounceability is discussed in more detail below).
2. Rights issues may be underwritten. The role of the underwriter is to guarantee that the funds sought by the company will be raised. The agreement between the underwriter and the company is set out in a formal underwriting agreement. Typical terms of an underwriting require the underwriter to subscribe for any shares offered but not taken up by shareholders. The underwriting agreement will normally enable the underwriter to terminate its obligations in defined circumstances. A sub-underwriter in turn sub-underwrites some or all of the obligations of the main underwriter; the underwriter passes its risk to the sub-underwriter by requiring the sub-underwriter to subscribe for or purchase a portion of the shares for which the underwriter is obliged to subscribe in the event of a shortfall. Underwriters and sub-underwriters may be financial institutions, stock-brokers, major shareholders of the company or other related or unrelated parties. The Panel’s guidance covers both non-underwritten and underwritten rights issues.
3. A rights issue may result in a shareholder<sup>3</sup> or underwriter acquiring or increasing control in the company.
4. Section 611, item 10 provides an exception from the prohibition in section 606 on persons acquiring control of a company for persons who would otherwise breach that prohibition as a result of participating in a rights issue. Item 10 excepts:

---

<sup>2</sup> Certain shareholders with overseas addresses may be excluded: section 615.

<sup>3</sup> A shareholder who subscribes for shares under the rights issue may increase its voting power if the issue is not fully subscribed for and it is not fully underwritten, or where that shareholder is also an underwriter or sub-underwriter.

*An acquisition that results from an issue of securities that satisfies all of the following conditions:*

- (a) *a company offers to issue securities in a particular class;*
- (b) *offers are made to every person who holds securities in that class to issue them with the percentage of the securities to be issued that is the same as the percentage of the securities in that class that they hold before the issue;*
- (c) *all of those persons have a reasonable opportunity to accept the offers made to them;*
- (d) *agreements to issue are not entered into until a specified time for acceptances of offers has closed;*
- (e) *the terms of all the offers are the same.*

*This extends to an acquisition by a person as underwriter to the issue or sub-underwriter.*

5. For underwriters of rights issues, item 13 of section 611 provides an additional and similar exception where the rights issue is offered under a prospectus. Item 13 excepts:

*An acquisition that results from an issue under a disclosure document of securities in the company in which the acquisition is made if:*

- (a) *the issue is to a person as underwriter to the issue or sub-underwriter; and*
- (b) *the disclosure document disclosed the effect that the acquisition would have on the person's voting power in the company.*

6. By relying on these exceptions, shareholders who subscribe for shares under a non-underwritten rights issue and a person who subscribes for shares as underwriter or sub-underwriter to the rights issue, may acquire voting power beyond the takeover threshold and may therefore acquire, or consolidate, control of a company without breaching section 606.

### **Central proposition – presumption in favour of acceptability**

7. The Panel commences from the following propositions:
- (a) *companies are entitled to manage their capital in a range of ways;*
  - (b) *most rights issues will not have any control issues and this Guidance Note is likely to have little relevance to them;*
  - (c) *the fact that control of a company is affected by a rights issue does not of itself give rise to unacceptable circumstances;*
  - (d) *informed, rational shareholders who have reasonable and equal opportunities to participate in any benefits which flow from a rights issue may choose not to participate in a rights issue, with consequent control effects on their company;*

- (e) *shareholders* who invest in a company do so in the knowledge they may be diluted in the event of non-participation in a capital raising; and
  - (f) where there is a potential for a rights issue to affect control of a company, its directors should carefully consider all reasonably available options to mitigate the *control* effect of the issue, and consider taking professional advice on these options.
8. The Panel does not wish to narrow inappropriately the scope of an exception inserted by the legislature. Therefore, if a rights issue is structured so as to fall within the exceptions in item 10 or item 13 of section 611 of the Act, there will be a rebuttable presumption that it is not unacceptable.
9. However, where the circumstances and terms of a rights issue suggest that the rights issue may affect control of the company in an unacceptable manner, the Panel may declare unacceptable circumstances to exist. This Guidance Note indicates those factors which are likely to increase the risk of scrutiny of a rights issue and which may tend to make the Panel scrutinise the actions and arguments of the proponents of the rights issue more critically.

*Purpose and Outcome*

10. The Panel is not primarily concerned with the motive of the company (or underwriter) in undertaking (or underwriting) the rights issue, but whether the result, or likely result meets the principles set out in section 602. Where the Panel is asked to consider whether a proposed rights issue gives rise to unacceptable circumstances it will be concerned with whether the rights issue affects, or is likely to affect, control, or potential control, of the company more than is reasonably necessary for fundraising purposes, or an acquisition of a substantial interest in the company gives rise to unacceptable circumstances.
11. However, where the Panel finds (from direct or circumstantial evidence, including the structure of the offer) that the rights issue has been structured for the purpose of affecting control of the company, it will be less ready to accept the company's judgement that a rights issue was an appropriate method of raising the required funds or that aspects of the structure of the issue such as price, timing and renounceability were in fact reasonably necessary for fundraising purposes. This will increase the likelihood that the rights issue will appear to the Panel to give rise to unacceptable circumstances.

*Onus on Board*

12. Where a rights issue may affect control of the company, the Panel expects that the board of a company will take the steps it reasonably can to minimise the potential for that to occur. A board's failure to do so, and to demonstrate that it has done so, may make the Panel less ready to accept the board's judgement as to the matters set out in paragraph 10 above.
13. The Panel is concerned to ensure that rights issues are not used to avoid the prohibition in section 606 by abuse of the exceptions in item 10 and item 13 of section 611. Therefore, any steps which a company takes to reduce the likelihood of control being affected by a rights issue will limit the opportunities

for complainants to present a case that the rights issue gives rise to unacceptable circumstances and therefore reduce the likelihood of scrutiny by the Panel.

*Safe Harbours*

14. There is no single test to determine whether a rights issue will give rise to unacceptable circumstances and this question will always depend to a significant degree on the facts of the matter before the Panel. Similarly, there is no “safe harbour” within which a rights issue is, by definition, acceptable.

**Factors bearing upon unacceptability**

*Need for funding and form of fundraising*

15. A rights issue which is brought before the Panel will be liable to a higher level of scrutiny by the Panel and carry an increased risk of a declaration of unacceptable circumstances if:
  - (a) it results, or is likely to result, in no readily discernible benefit to the company;
  - (b) the company has no compelling need for funds; and
  - (c) it leads to an effect on control of the company<sup>4</sup>.
16. The exception from the takeover prohibition in item 10 of section 611 was included as a necessary paring back of the regulation of control transactions to allow a company in need of funding to raise capital by way of a rights issue.
17. The Panel considers that the short time frame within which it is required to conduct proceedings, and the detailed forensic accounting required in many cases, mean it may be difficult to establish definitively the financial need of a company or the board’s motives in promoting the issue. Therefore, the Panel considers that it should not normally second guess the judgement of directors based on grounds and evidence that appear on their face to be reasonable, that their company requires the funds sought in the rights issue, the raising of those funds will be of benefit to shareholders and that the rights issue was an appropriate mechanism.
18. The Panel proposes that the onus for demonstrating that there is, or was, no need for funds or that a rights issue was not an appropriate mechanism for raising those funds should generally, therefore, fall on the party seeking to challenge the rights issue. However, that onus is likely to shift onto the directors if:
  - (a) the directors’ assessment of the need for funds or that the rights issue was an appropriate mechanism is not supported by rational reasons (which would include advice received by directors from the company’s professional advisers); or

---

<sup>4</sup> However, as discussed at paragraph 67, the Panel is likely to expect fuller disclosure in relation to a rights issue that may have a material effect on control than one which may only slightly increase the voting power of an existing controller.

- (b) there are reasonable arguments against the purported purpose which the directors fail to rebut.
19. While the onus initially lies with the complainant, the Panel recognises that complainants will frequently have far less access to relevant information than the directors of a company. The Panel will take this into account when assessing whether or not the complainant has established a basis for its assertions.
20. Factors that the Panel will likely consider when assessing the need for funds and the appropriateness of a rights issue include:
- (a) the relative amount sought to be raised (bearing in mind the prevailing market prices and the 15% placement limit without shareholder approval that applies to listed companies under ASX Listing Rule 7.1);
  - (b) whether the company has explored other capital-raising alternatives;
  - (c) whether the company received advice from financial advisers;
  - (d) the financial situation and solvency of the company;
  - (e) the response, or likely response of the shareholders, and particularly any substantial shareholders, to the rights issue;
  - (f) whether the rights issue is underwritten by professional underwriters / sub-underwriters; and
  - (g) market factors leading up to the rights issue and those reasonably likely to occur during the rights issue.

#### *Structure of Rights Issue*

21. In undertaking a rights issue, a company and, if the rights issue is underwritten, the underwriter will, in practice, usually decide on structural matters, such as the price at which new shares are offered, the number of shares offered and whether the issue will be renounceable. These factors cannot be considered in isolation from each other and the Panel will look at the structure of the rights issue as a whole in deciding whether that structure may give rise to unacceptable circumstances.
22. When it looks at the structure of a rights issue the Panel will look at whether the rights issue has been structured, as a whole, to minimise as far as possible any unnecessary effect on control of the company. Set out below is a discussion of the most important structural issues – pricing and renounceability – the Panel will look to in determining whether unacceptable circumstances exist in relation to the structure of the rights issue, and how they relate to each other and other elements of a rights issue.

#### *Pricing*

23. The price at which new shares are offered under a rights issue is likely to be a relevant factor in determining whether the control effects of the rights issue are unnecessary and give rise to unacceptable circumstances. However, the effect of the price on the decisions to be made by shareholders whether to take up the

rights offer depends on other factors, such as the size of the rights issue compared to the company's existing share capital, whether or not the rights issue is renounceable and the effect on the prospects of the company if the rights issue succeeds.

24. The Panel will expect directors to consider the issues carefully and choose a level of pricing that they consider most likely to minimise unnecessary potential effects of the rights issue on control of the company.

Low discount

25. A rights issue which is priced more closely to the market price of the securities (or even at a premium) provides less incentive for the rights issue to be taken up by all shareholders and, therefore, may increase the likelihood of control becoming concentrated with an underwriter or other participating major shareholder.<sup>5</sup> The price may be set at a level which makes the issue attractive only to a shareholder or underwriter who wishes to acquire control.

High discount

26. A rights issue which is offered at a high discount will have the advantage, from a control perspective, of being attractive to shareholders to take up (in order to gain the benefit of the discount) and thus is likely to reduce a shortfall flowing to an underwriter. In a renounceable rights issue, a higher discount is likely to facilitate an active market for the rights, also reducing the control effects of the issue.
27. On the other hand, a rights issue priced at a large discount may result in:
- (a) value being transferred from pre-existing shares to the newly issued shares;
  - (b) greater dilution of shareholders who do not participate in the rights issue; and
  - (c) greater flow through to an underwriter in a non-renounceable rights issue, and thus have an adverse effect on shareholders who elect not to participate.
28. The value transfer from existing shares to new shares referred to in paragraph 27(a) above will occur whenever rights are offered at a discount to the current market price and occurs regardless of whether the issue is renounceable or not and regardless of whether it is underwritten or not. The size of the value transfer is a function of the rights issue ratio and the size of the discount. Existing shareholders can:
- (a) gather all of that value transfer by exercising all of their rights (in a renounceable or non-renounceable rights issue); or

---

<sup>5</sup> In *InvestorInfo* [2004] ATP 06 at paragraph [38(c)], it was stated that the attractiveness of the pricing of the rights issue was a relevant factor because a significant discount to market will indicate that the issuer is seeking to attract shareholders to exercise their rights (in the *InvestorInfo* case the securities were to be listed and the rights issue was renounceable).

- (b) assuming there is a market for the rights, gather/recoup some of that value transfer by selling their rights (in a renounceable rights issue); or
  - (c) gather/recoup some of that value by selling some of their existing shares and using the proceeds to take up the discounted rights (in a renounceable or non-renounceable rights issue).
29. Generally, the Panel will consider that a larger discount is more likely to encourage existing shareholders (or new investors in a renounceable rights issue) to take up the rights offered. Therefore, a larger discount is less likely to cause a rights issue to have an effect on control, or potential control, of a company, or the acquisition of a substantial interest in the company.
30. However, this indication may not apply where the rights issue is non-renounceable, or where the rights issue is underwritten or sub-underwritten by a related party. Similarly, a larger discount may not reduce, and may exacerbate, the likely effect on control of a rights issue in an unlisted company.

#### Listed vs unlisted

31. The question of pricing is more easily considered in relation to liquid, listed securities, because there will be a market price against which to compare the issue price for the rights. For unlisted securities, illiquid listed securities and listed securities with a volatile market price, there may not be a readily accessible price comparison.

#### Large issue

32. If the amount of funds required by the company to be raised is large in comparison to the value of the company (requiring a very large issue ratio), the price at which new shares are offered will be less relevant. This follows from the fact that the existing assets of the company (which would form the basis of the value of the existing shares, and hence the reference value against which a discount would be measured) will comprise a smaller proportion of the value of the company following the completion of the rights issue. However, a company undertaking such a large rights issue may have a greater hurdle to overcome in demonstrating its need for those funds and may require shareholder approval, for example under the Listing Rules.

#### Managed investment schemes

33. Managed investment schemes are subject to a requirement to have set out in their constitution “adequate provision for the consideration that is to be paid to acquire an interest in the scheme” (section 601GA(1)). This is effectively a restriction on the discretion of the responsible entity to set an issue price at the time of an issue of interests. ASIC Class Order CO 05/26 provides<sup>6</sup> an exception from this rule, allowing:

---

<sup>6</sup> At the time of publishing of this Guidance Note ASIC Class Order CO 05/26 had not been amended to incorporate the matters set out in sub-paragraph (b)(i). The amendments are proposed to be effected early in 2006.



- (a) responsible entities to independently set the issue price in certain cases, including a rights issue; and
- (b) underwriting of rights issues by:
  - (i) associates of responsible entities of listed schemes conditional on:
    - (A) the underwriter holding an Australian financial services licence;
    - (B) the AFS licence containing conditions prohibiting the underwriter voting the shortfall interests or selling those interests to a person it knows is its associate; and
    - (C) the underwriting agreement being on arm's length terms, with its sole purpose the assumption of risk of the shortfall and distribution of managed investment products; and
  - (ii) persons who are not associated with responsible entities of listed schemes.

#### *Renounceability*

- 34. A rights issue is “renounceable” if the right of each shareholder to subscribe for their entitlement may be transferred to a third party (who need not be another shareholder). Due to the limited market for rights in unlisted companies, renounceable rights issues are generally only undertaken by listed companies. Acquirers of these rights may subsequently exercise them to acquire shares in the company. On-market trading of rights may occur under a renounceable rights issue if the rights are quoted. The entitlements of shareholders under a non-renounceable rights issue cannot be transferred.
- 35. Subject to the rights having a value and demand existing for the rights, renounceability should lead to a higher likelihood of the rights being exercised. This in turn would reduce the flow-through to an underwriter of those shares not taken up by the original shareholders. A shortfall facility or similar dispersion facility, such as a back-end bookbuild, may also reduce the flow-through to the underwriter or sub-underwriters (these are discussed in more detail below).
- 36. A rights issue which is non-renounceable is likely to limit the pool of potential applicants. This is likely to increase the likelihood of control becoming concentrated with an underwriter or other participating major shareholder and increase the likelihood of the rights issue giving rise to unacceptable circumstances.
- 37. In addition, given that there is no relevant exception from section 606 for the buyers of rights who then exercise them, those buyers are less likely to acquire or increase control of the company by buying and exercising renounceable rights, therefore a renounceable rights issue is less likely to give rise to unacceptable circumstances.
- 38. The ability to sell renounceable rights makes it easier for shareholders to access the benefits of a rights issue and assist in ensuring equality and reasonableness of opportunity per section 602(c) of the Act. Where a market for rights is

unlikely (for example, because the company is not listed, or the stock is illiquid) or making the rights issue renounceable is unreasonably costly, it may be appropriate for the Panel to consider non-renounceability of a rights issue not to be significant.

39. On the basis of the above issues, a rights issue by a listed company which is renounceable may be less likely to give rise to unacceptable circumstances. However, renounceability is not a safe harbour and is only one of the factors which the Panel will consider when determining whether or not a rights issue gives rise to unacceptable circumstances.
40. If a rights issue is priced so that the rights have an insignificant value, there will be little incentive for shareholders or investors to acquire them. Therefore, renounceability is less likely to be an ameliorating factor in rights issues which affect control and the rights have an insignificant value.

#### *Non-Renounceability*

41. The reasons commonly put forward for not making a rights issue renounceable include:
  - (a) there is unlikely to be a market for rights because the company is not listed;
  - (b) there is unlikely to be a market for rights because the market for the securities of the company is very illiquid; and
  - (c) making the rights issue renounceable will be unreasonably costly.
42. A company considering a non-renounceable rights issue may wish to consider structuring a rights issue to avoid other factors which would tend to increase the risk of the rights issue having an effect on control or potential control of the company, in order to reduce the likelihood of the Panel considering that the rights issue gave rise to unacceptable circumstances. This may be especially relevant because the same factors which make renounceability less attractive are factors which are likely to increase the risk of the rights issue having an effect on the control or potential control of the company.

#### *Underwritten rights issues*

43. The second limb of the exception in item 10 of section 611 relates to “*an acquisition by a person as underwriter to the issue or sub-underwriter*”. An underwriter or sub-underwriter to a rights issue may acquire control of the company by relying on this exception. Where a prospectus has been lodged in relation to the rights issue, an underwriter may also rely on the exception in item 13 of section 611. In the case of a fully underwritten rights issue, the only person whose voting power can increase is the underwriter’s.<sup>7</sup>

---

<sup>7</sup> However, where there is a shortfall facility, applicants under that facility, or where the rights issue is renounceable, purchasers of those rights who exercise their rights, may also increase their voting power, subject to section 606.

44. A company may engage a professional underwriter (that is, a person who underwrites in the normal course of their business), or a major shareholder, related party or some other party, to underwrite its rights issue.
45. In general, a professional underwriter seeks to earn fees from underwriting, or profit from the on-sale of shortfall shares, and not to hold shares in the company it has underwritten to control or run that company. The Panel accepts that because of the nature of the risk which underwriters bear, there will be circumstances where underwriters (or sub-underwriters) are required to subscribe for shares pursuant to an underwriting agreement and cannot readily on-sell those shares. Therefore, blanket statements or rules in relation to the acceptability of all underwriting situations are very difficult.
46. The Panel accepts that for many companies whose nature, size and market following are likely to necessitate rights issues which may have control effects, a related party or major shareholder is likely to be the only realistic source of underwriting. While underwriting by a related party is not, of itself unacceptable, a company using a related party underwriter should recognise that this will likely cause greater scrutiny of the acceptability of the rights issue if control of the company is, or may be, affected and increased risk of a declaration of unacceptable circumstances.
47. The Panel also considers that a professional underwriter is unlikely to have any interest in obtaining control of the company. Therefore, the failure by directors to properly canvass professional underwriters, or seek out alternatives to a related party underwriter, may increase the likelihood of a rights issue and associated underwriting giving rise to unacceptable circumstances.
48. Sub-underwriting may have the same effect as underwriting in regard to control of the company and will receive the same level of scrutiny. On that basis, the concerns raised in relation to underwriters (especially related party underwriters) will also apply to sub-underwriters. Using several non-associated professional sub-underwriters (and hence decreasing the likelihood of control passing to any one of them) is likely to reduce the force of any inference that the rights issue is likely to affect control.
49. Informed approval by non-associated shareholders of the rights issue and underwriting or sub-underwriting by related parties would safeguard any consequent share acquisitions.

### **Shortfall facilities and other methods of dispersing a shortfall**

#### *Effect on dispersing control*

50. Recently, companies have adopted a number of strategies to deal with a shortfall in a rights issue rather than solely requiring the underwriter to subscribe for the initial shortfall. This may reduce the risk for the underwriter, and thus the fee payable by the company to the underwriter. Relevantly to the Panel's consideration, adopting such a strategy may also reduce the risk of the underwriter, or a major shareholder, acquiring or increasing control of the company. Two of the currently used strategies "shortfall facilities" and "back

end book builds” are described below. The Panel considers that acquisitions under a dispersion strategy, whether by existing shareholders or other persons, would not attract the benefit of the item 10 or item 13 exception.

51. A “shortfall facility” in the context of a rights issue is a facility which allows shareholders to subscribe for any shares not taken up by other shareholders under the rights issue. Where the rights issue is underwritten, this participation will usually be in advance of determining the shortfall available to the underwriter.
52. A “back-end bookbuild” is a bookbuild conducted in respect of the shortfall in a rights issue (a “bookbuild” being an offer of securities to investors - typically institutions - for which bids are sought from the investors and the allotments and issue price are determined based on those bids). A back-end bookbuild is another method of dispersing the rights not taken up under a rights issue widely and minimising the chance of the issue having a control effect.
53. A dispersion strategy, such as a shortfall facility or back-end bookbuild, is not a necessary element of a rights issue which seeks to rely on item 10 or item 13. However, given its potential to mitigate the control effects of a rights issue by facilitating take up by shareholders or other investors of any shortfall shares offered under a rights issue (rather than the shortfall flowing through to an underwriter or sub-underwriter), the inclusion of a dispersion strategy is likely to assist in avoiding an inference that may otherwise arise that the rights issue is being undertaken to allow an underwriter or major shareholder to acquire or consolidate control of the company.
54. A dispersion strategy will only mitigate control effects of a rights issue if it is structured to do so. Features which may assist a dispersion strategy achieve its stated goal include:
  - (a) an underwriter or sub-underwriter receiving entitlements under the dispersion facility after all other requests have been satisfied;
  - (b) sufficient time and disclosure being offered to shareholders and other investors to assess the rights or shares being offered;
  - (c) external investors are open to take up the rights or shares offered under the dispersion strategy.

*Ability to rely on the underwriting exception for acquisitions under a dispersion strategy*

55. The Panel considers that a person is *not* able to rely on the underwriting exception in item 10 or 13 to protect an acquisition under a shortfall facility which would otherwise cause them to breach section 606 – this turns on whether that person can be considered to be an underwriter and thereby rely on the second limb of item 10 or item 13.
56. It is the Panel’s view that such a person is *not* an underwriter. An “underwriter” is someone who facilitates the making of a capital raising by contractually committing to the company to subscribe for the shortfall *prior to the offer being made*.

## Disclosure

57. The Panel considers that a company raising capital by way of a rights issue must be conscious of the increased importance of disclosure in circumstances where shareholders are considering not merely the desirability of making a further investment in the company, but also the control implications of the rights issue and whether to take steps to protect against the dilution of their existing holding.<sup>8</sup>
58. Therefore, a rights issue undertaken without full and meaningful disclosure of the consequences of any potential effect on control will carry a heightened risk of a declaration of unacceptable circumstances.
59. Rights issue disclosure may be made in a variety of forms under Part 6D.2:
  - (a) a full prospectus (with or without a profile statement) under sections 709(1) and (2);
  - (b) a “transaction specific” prospectus under section 713,
  - (c) an Offer Information Statement under section 709(4), or
  - (d) a “cleansing notice” under section 708AA.
60. Exceptionally, a rights issue may also be made without disclosure as required under Part 6D.2, if it meets the requirements of section 708 (i.e., is a small scale offering, an offering to professional investors, etc).
61. The Panel considers it appropriate to take into account the legislative intention for the disclosure required, the type of document used, and the adequacy of disclosure in respect of the control effects of the rights issue in considering whether unacceptable circumstances exist.

### *Disclosure of control effects*

62. It is important that the reasons behind the choice and roles of any supporting shareholders, underwriters and sub-underwriters be disclosed to shareholders. If the possible control scenarios can be and are properly disclosed, including the identities of those who may end up owning any shortfall, and the future shareholding pattern of the issuer is frankly discussed, shareholders will be able to make informed decisions on participating, or not participating, in the rights issue and the potential control consequences. Such information would be expected to be found in a full prospectus or cleansing notice because of the specific requirements in the Act. The Panel thinks it is likely that such information would be required in a transaction specific prospectus. Because an Offer Information Statement is used for small capital raisings, there may be limited control implications. But that may not be so for a company with low

---

<sup>8</sup> While the disclosure being discussed here concerns control effects, it is important to bear in mind that, where relevant, shareholders also need an understanding of the issuer’s business, financial performance, plans and prospects.

capitalisation, and therefore the circumstances may suggest that such information should be disclosed.<sup>9</sup>

63. In addition, the intentions for the company of persons who may obtain control of it as a result of the rights issue should also be disclosed, to the extent that the information is able to be ascertained by the company. This information should be feasible for the company to obtain in relation to underwriters and sub-underwriters but not necessarily in relation to major shareholders whose voting power may increase simply by taking up their entitlement in a non-underwritten offer while other shareholders do not.
64. If the company proposes to institute a dispersion strategy to sell any shortfall of rights, it should include a discussion as part of its disclosure of the potential effects on control of the company which its proposed dispersion strategy might cause.
65. If a rights issue is undertaken without a document under Part 6D.2, it is highly likely to face increased scrutiny of the disclosure made to shareholders.
66. While in any application the Panel will advise what aspects of a rights issue disclosure it finds unacceptable, it will not provide detailed guidance to a company as to what will constitute complete disclosure. This is because it is not the Panel's role to be a primary regulator of the disclosure content of rights issues. Further, a Panel decision about disclosure should not be taken to be an approval of the documentation used for making the rights issue in respect of any item of disclosure other than those raised in the application or reasons.

*Disclosure of the extent of the control effect*

67. Rights issues which may cause effective control to pass to a shareholder, or an underwriter, will receive closer scrutiny than those which only slightly increase the voting power of an existing controller. For example, the Panel would expect fuller disclosure in relation to a rights issue which may increase a person's voting power from 10% to 40%, than in relation to a rights issue which may increase a person's voting power from 51% to 55%.

**Timing of Applications**

68. Potential applicants should ensure that any application to the Panel to consider the acceptability of a rights issue is made in a timely manner in order to minimise potential harm and disruption to companies and their shareholders.

**Submissions**

69. Applicants, and respondents, should expressly address, in evidence and reasoning, the effect which the aspects of the rights issue which are complained of, have had, would have, or are likely to have, on:
  - (a) control, or potential control, of a company; or

---

<sup>9</sup> [In the matter of Anaconda 02-05 \[2003\] ATP 04](#), [70], [72].

- (b) the acquisition or proposed acquisition, of a substantial interest in the company.

### Remedies

70. The Panel will consider making orders, or accepting undertakings, where it considers that the circumstances complained of constitute unacceptable circumstances. The Panel will seek submissions on the effect of the unacceptable circumstances, the appropriate remedies, and the nature of any prejudice caused by the proposed orders. The orders that the Panel may make to protect the interests of persons affected by the unacceptable circumstances are potentially very wide.
71. Orders which the Panel may make may require, inter alia:
- (a) further disclosure;
  - (b) withdrawal rights for persons who have acquired shares;
  - (c) reopening of the rights issue;
  - (d) divestiture of shares acquired under the rights issue;
  - (e) freezing of voting power of shares acquired under the rights issue;
  - (f) shareholder approval of the rights issue;
  - (g) different underwriting or sub-underwriting arrangements.
72. As discussed in paragraph 10 above, the Panel will not base its decisions as to whether or not unacceptable circumstances exist, on the intentions or purpose of the company in structuring the rights issue. However, consistent with the following paragraph, paragraph 11 above, where the Panel finds evidence of motive or intention to bring about the unacceptable circumstances by any person, it may take that into account when considering the orders which may be required to remedy the unacceptable circumstances. In doing so, the Panel considers that any prejudice which its preferred orders might cause is **less likely** to be **unfair** prejudice to that person (because of the motive/intention) than similar prejudice caused by orders where the Panel finds evidence that the person's motive or intention was **not** to bring about unacceptable circumstances.

---

### Publication History

First Issue: 10 January 2006

Second issue 18 December 2007