

Equity Capital Markets Update

ASX gives mid to small caps a boost

In brief

- ASX has released a new proposals and consultation paper, *Strengthening Australia's equity capital markets*, detailing the first of several initiatives it plans to introduce in 2012 to maintain the attractiveness of Australia's equity capital markets.
- The proposed changes present significant opportunities for junior mining companies to access the additional capital that it is so important in funding their growth.

Introduction

In April 2012, ASX released a new proposals and consultation paper, *Strengthening Australia's equity capital markets* ("ASX Proposals"), detailing the first of several initiatives it plans to introduce in 2012 to maintain the attractiveness of Australia's equity capital markets.

The ASX Proposals follow on from the ASX review carried out last year, *SME, Mid-Cap and Micro-Cap Equity Market Review* (March 2011) which confirmed that the existing "one size fits all" market structure is strongly backed by market participants with reform of admission criteria and secondary capital raising rules preferred as methods of boosting the competitiveness of smaller companies.

Accordingly ASX is proposing to amend the ASX Listing Rules to facilitate capital raising for mid to small caps and to update its admission requirements.

ASX also released a summary of the feedback received in ASX's consultation on *Reserves and Resources Disclosure Rules for Mining & Oil and Gas Companies* (October 2011). The consultation process confirmed broad support for ASX's proposals to facilitate greater transparency and consistency in reserves and resources reporting.

Facilitating capital raising for mid to small caps

Background

Throughout 2011, ASX consulted widely to identify how to address the needs of listed mid to small caps, while maintaining strong levels of investor protection. Australia has more than 1,600 mid to small caps, accounting for over three quarters of the total number of ASX listed companies with over half of these in the resources sector.

Many mid to small caps are constrained in their ability to raise funds because they have a narrow range of shareholders and are often more speculative in nature. Placements to institutional investors are a vital source of capital for these companies. Analysis of capital raising in 2011 showed that placements provided close to 70% of the secondary capital needs for small to mid caps.

Proposal

Currently, under listing rule 7.1, an entity cannot issue or agree to issue a number of equity securities if that number would exceed 15% of the number of ordinary securities on issue 12 months before the date of issue or agreement, unless the entity has obtained shareholder approval or an exemption applies. The existing rule is seen as imposing unnecessary capital raising costs and impeding flexibility particularly for those companies with frequent needs to raise capital to fund long term projects.

New listing rule 7.1A will permit mid to small caps to seek approval from shareholders (valid for 12 months) to issue a number of equity securities equal to 10% of the number of ordinary securities on issue 12 months before the date of issue (in addition to the 15% currently permitted under listing rule 7.1 without shareholder approval). An entity undertaking a placement of up to 25% of the entity's issued capital under listing rules 7.1 and 7.1A will still need to consider the prohibition in Chapter 6 of the *Corporations Act* on a person increasing voting power in a listed entity to above 20% (or from a level above to 20% and below 90%).

The issue price of securities issued under listing rule 7.1A must be no less than 75% of the average market price for securities in that class calculated over the 15 trading days on which trades in that class were recorded immediately before the date on which the securities are "issued". Generally securities are priced at least three trading days before they are issued so this may give rise to some practical difficulties.

ASX proposes to define mid to small caps as listed entities with a market capitalisation of A\$300 million or less. A list of these entities will be published on the ASX website twice a year, on the last trading day in May and November. ASX will determine an entity's market capitalisation by reference to quoted securities in the entity's main class (other than restricted securities and securities quoted on a deferred settlement basis) and the last traded price for those securities.

If shareholder approval is obtained under listing rule 7.1A it will continue to operate even if the entity's market capitalisation goes over A\$300 million during the 12 month period.

The proposal aims to bring the ASX's capital raising framework for mid to small caps in line with comparable jurisdictions like Toronto, London, Hong Kong and Singapore.

Information Requirements

The notice of the meeting at which a mid to small cap seeks shareholder approval under listing rule 7.1A will need to disclose certain information, including:

- the minimum price at which equity securities may be issued under listing rule 7.1A;

- the risks of economic and voting dilution of existing security holders that may result from an issue under listing rule 7.1A, including a table describing the potential dilution on the basis of at least three different assumed issue prices and three different values for the number of existing ordinary securities (ie the base number that is multiplied by 10%);
- the date by which the new securities may be issued;
- the purposes for which the equity securities may be issued, including whether the entity may issue any of them for non-cash consideration; and
- details of securities issued in the previous 12 months under an earlier approval under listing rule 7.1A.

If the securities are issued for non-cash consideration, ASX has indicated that the entity must issue a valuation to the market that demonstrates that the non-cash consideration satisfies the "at least 75% of market value" requirement. The valuation may be provided by an independent expert or by the directors, provided that the directors have appropriate expertise to value the relevant kind of non-cash consideration and the directors' valuation report contains a similar level of analysis and is of a similar standard as an independent expert's report. Practically, issuing securities under listing rule 7.1A for non-cash consideration will give rise to some additional matters for boards to consider.

Once shares have been issued under the new rule 7.1A, the entity must provide the ASX with details of, amongst other things, the dilution that has occurred for existing shareholders, why a placement was used and not a pro rata issue available to all shareholders, and details of the allocation policy for the issue (including the involvement of directors in determining the policy and any consideration given to making the issue of securities to existing shareholders).

Updating admission requirements

ASX is also proposing to update admission requirements by lowering the threshold for the number of security holders that an entity needs to be admitted to the official list and increasing the net tangible assets test.

ASX Listing Rule	Existing	Proposed
	Spread requirements	
LR 1.1 Condition 7	500 holders with a minimum holding of A\$2000 or 400 holders with a minimum holding of A\$2000 and at least 25% held by non-related parties or	400 holders with a minimum holding of A\$2,000 350 holders with a minimum holding of A\$2,000
	No current equivalent	300 holders with a minimum holding of A\$2000 and at least 50% held by non-related parties
	Net tangible assets	
LR 1.3	Net tangible assets that an entity is required to have at the time of admission is at least A\$2 million	Net tangible assets that an entity is required to have at the time of admission is at least A\$4 million

Although strong support was received during the consultation process for changing the minimum issue price requirement to less than \$0.20 per share, this change has not been proposed (with no explanation provided as to why).

Other initiatives

ASX has foreshadowed other market initiatives to support mid to small caps by promoting liquidity and boosting the profile of smaller companies generally. The initiatives include:

- supporting price formation for mid to small caps through additional intra-day auctions, market makers, and re-introduction of broker IDs;
- extending trading hours to attract more Asian investors towards cash-poor junior mining companies;
- trialling a new Equity Research Scheme to fund the production of high-quality, independent research for listed entities with a market capitalisation below \$1 billion, to improve the ability of smaller companies to communicate to, and raise capital from, a broader set of investors; and
- launching the Australian Resources Conference and Trade Show, to be held in Perth in November 2012, to bring together international and domestic providers of capital and Australian resource entities in one location.

Conclusion

- The ASX Proposals signal ASX's response to the need to identify ways to attract investors and enhance the global competitiveness of Australia's financial markets.
- The proposed changes present significant opportunities for junior mining companies to access the additional capital that it is so important in funding their growth.
- Draft rules for the mid to small cap proposals were lodged with ASIC in March 2012 to begin the process of regulatory approval. ASX is seeking feedback on its proposed rule changes by 14 May 2012.

Contacts



Sarah Dulhunty
Partner
Sydney
T: +61 2 9258 6643
E: sarah.dulhunty@ashurst.com



Corey Lewis
Senior Associate
Melbourne
T: +61 3 9679 3506
E: corey.lewis@ashurst.com



Elizabeth Hourigan
Lawyer
Perth
T: +61 8 9366 8078
E: elizabeth.hourigan@ashurst.com



Shae Francis
Graduate
Perth
T: +61 8 9366 8042
E: shae.francis@ashurst.com

ASX reports on its consultation on disclosure rules for mining companies

In brief

- ASX released the ASX Listing Rules Review Issues Paper: Reserves and Resources Disclosure Rules for Mining and Oil & Gas Companies dated 5 October 2011.
- In April 2012 ASX released a Report on Consultation Feedback for the issues paper ("report").
- This article summarises the consultation outcomes of the report and some of the commentary.

Our articles:

- *Disclosure – driving transparency in the mining and oil & gas sectors* of 13 October 2011; and
- *ASIC responds to ASX consultation paper on disclosure rules of mining companies* of 14 December 2011,

discussed aspects of this ASX consultation process for the reporting regime for reserves and resources. This article summarises the latest report which compiles responses from consultation sessions held in December 2011 and January 2012 as well as the submissions received on the issues paper.

The rule changes arising from this process will be important for Australian listed entities in the mining and petroleum sector as they will impact on their continuous disclosure and reporting obligations. The current obligations are set out, in the main, under listing rule 3.1 and chapter 5 of the Listing Rules and in Guidance Note 8.

The report's commentary includes proposed changes to the Listing Rules as well as some suggested changes to the JORC Code in relation to mining resources estimation. The report contemplates adapting the SPE- PRMS to turn it into a set of reporting requirements for the petroleum sector.

The consultation report raises an issue of the ability of ASX to evaluate the competence of "competent persons" who give opinions on evaluation and estimation of mineral resources and ore reserves. It indicates that the ASX is considering forming a panel of experts to call upon for advice in this area, for example in response to a legitimate complaint.

A major theme emerging from the consultations was that mining and oil & gas companies have a commercial sensitivity towards and guard the confidentiality of pricing information and economic assumptions in relation to commodities and production. This sensitivity needs to be balance against the need to disclose pricing information and assumptions, as these are clearly matters which are fundamental to valuing mining and oil and gas companies and allowing comparisons between them.

The report discusses responses to each of 6 key issues for mining and 7 key issues in relation to petroleum reporting and transparency raised by ASX in the issues paper. These are summarised in the tables below.

Mining

Two new issues identified during the consultations as having merit were:

- streamlining the competent person sign off requirements for subsequent public reporting of mineral resource and ore reserve estimates; and
- removing the requirement to obtain a listing rule waiver to report historical estimates of mineralisation (where outside the JORC Code).

ASX Reporting Issue	Outcome of consultation
<p>1. The proposed introduction of a mandatory requirement of disclosure of specific drill hole and intercept information – the easting, northing, elevation, dip, azimuth, down hole width, depth, and the end of hole - in reporting the results of drilling to the market.</p>	<p>The proposed mandatory disclosure of exploration results requirement was referred to as having a "mixed result" with nearly half of the respondents in support. Most considered that the present flexibility was appropriate.</p> <p>In addition, some respondents sought specific guidance if such mandatory reporting was required where the drilling data for exploration did not disclose mineralisation.</p>
<p>2. A mandatory requirement for inclusion of a cautionary statement for exploration target statements in a public report.</p> <p>The proposed cautionary statement is to be proximate to the exploration target statement and be given similar prominence</p>	<p>The ability to report on exploration targets was supported by respondents as providing the basis for justifying exploration expenditure.</p> <p>The use of cautionary statements received support with a qualification that in cases where there is more than one reference to an exploration target in a report, cross reference to the initial cautionary statement should suffice.</p> <p>There was also a proposition that headline statements about the quantity of exploration targets were problematic in qualifying and respondents supported a prohibition on including quantities in headline statements.</p>
<p>3. Disclosure of assumptions underpinning mineral resources and ore reserve estimates, including consideration of a requirement for a technical report, as is required in Canada</p>	<p>A technical report was opposed by respondents, with considerable misgivings about increased compliance costs.</p> <p>There was debate concerning the need for change given the JORC Code seems to cover the area. The report canvasses debated points without arriving at a conclusion.</p>
<p>4. Defining a level of study for a maiden ore reserve declaration</p>	<p>There was debate about if a requirement should be mandated even though the body of comments appears to support use of a preliminary feasibility study for consistency in reporting, with defined levels of accuracy.</p>
<p>5. ASX preferred option is that disclosure of production targets be prohibited when based solely on an exploration target</p>	<p>The consultation process gave rise to a diverse range of views and concerns, with confidentiality and commercial sensitivity of the information and assumptions as to economic elements including commodity prices being raised. Concerns were raised about a blanket prohibition for certain types of inferred resources.</p>
<p>6. Annual report and reconciliation of mineral resource and ore reserve estimates</p>	<p>The reconciliation requirement is broadly supported however the potential confusion with the term "production reconciliation" lead to some definitional debate on the term to adopt.</p>

Petroleum

A consistent approach to the reporting of unconventional resources in the petroleum sector arose as an issue in the consultation process and it was suggested by respondents that ASX address this issue.

	ASX Reporting Issue	Outcome of consultation
1.	Adoption of standardised petroleum resources definitions and comprehensive classification system	Support was present for adoption of the SPE PRMS classification system. It was noted that many industry companies already use this internally, which reduces potential compliance costs if adopted.
2.	General reporting requirements for reserves and resources	As the SPE PRMS is a management system rather than a set of reporting requirements, ASX acknowledged some adaptation is required to apply it to a reporting task. A number of detailed reserves and resources reporting requirements and qualifications were canvassed, including the use of cautionary statements.
3.	Annual reserves and mandatory reporting requirements	<p>A majority of respondents supported mandatory annual reporting requirements of:</p> <ul style="list-style-type: none"> • company level 1P and 2P reserves by product; • aggregated 1P and 2P reserves by product and location, subject to materiality criteria; • company level 1P and 2P reserves of unconventional resources; and • a reconciliation against the previous year's reporting of company level 1P and 2P reserves by product, subject to materiality criteria.
4.	<p>Reporting exploration and drilling results and the extent to which this should apply to:</p> <ul style="list-style-type: none"> • unconventional resources; or • seismic survey exploration 	<p>Almost all respondents indicated support for making it clearer that drilling program reporting is required when the information is expected to have a material effect on the price or value of an entity's securities.</p> <p>Unconventional resources were in the main considered by respondents to be validly reported on by these reporting requirements.</p> <p>Certain forms of data and interpretations, including seismic material, were considered to be confidential and unhelpful to investors.</p>
5.	Disclosure of key assumptions underpinning reserves and resources estimates	<p>The reaction of respondents was to emphasise that a number of economic assumptions, commodity price assumptions and price data is considered confidential by companies. However, support was present for providing a brief statement of the methodology used to arrive at such assumptions.</p> <p>Disclosure by respondents in relation to a material project/asset was supported in making announcements including:</p> <ul style="list-style-type: none"> • operator/non-operator status for the project; • the type of permits/licences; • a brief description of the basis for confirming commercial production from the project and assigning reserves;

		<ul style="list-style-type: none"> • a brief description of the analytical procedures for estimating reserves; • the estimated aggregate recovery from existing wells and facilities and from significant future investments; • a brief description of the proposed production method; and • a brief description of applicable specialised processing following extraction.
6.	Disclosure of production targets	<p>ASX concluded that listing rule requirements were not required at present.</p> <p>Respondents again emphasised the commercial sensitivity of underlying economic assumptions as a concern.</p>
7.	Qualified reserves and resources evaluator requirements	The qualification requirement is broadly supported by respondents, however the specifics are debated in terms of the precise standards to adopt for evaluators.

Contacts



David McManus
Partner
Sydney
T: +61 2 9258 6094
E: david.mcmanus@ashurst.com



Martin Kudnig
Partner
Melbourne
T: +61 3 9679 3222
E: martin.kudnig@ashurst.com



Sam Golding
Special Counsel
Melbourne
T: +61 3 9679 3314
E: sam.golding@ashurst.com

Abu Dhabi

Suite 101, Tower C2
Al Bateen Towers
Bainunah (34th) Street
Al Bateen
PO Box 93529
Abu Dhabi
United Arab Emirates
T: +971 (0)2 406 7200
F: +971 (0)2 406 7250

Adelaide

Level 4
151 Pirie Street
Adelaide SA 5000
Australia
T: +61 8 8112 1000
F: +61 8 8112 1099

Brisbane

Level 38, Riverside Centre
123 Eagle Street
Brisbane QLD 4000
Australia
T: +61 7 3259 7000
F: +61 7 3259 7111

Brussels

Avenue Louise 489
1050 Brussels
Belgium
T: +32 (0)2 626 1900
F: +32 (0)2 626 1901

Canberra

Level 11
12 Moore Street
Canberra ACT 2601
Australia
T: +61 2 6234 4000
F: +61 2 6234 4111

Dubai

Level 5, Gate Precinct Building 3
Dubai International
Financial Centre
PO Box 119974
Dubai
United Arab Emirates
T: +971 (0)4 365 2000
F: +971 (0)4 365 2050

Frankfurt

OpernTurm
Bockenheimer Landstraße 2-4
60306 Frankfurt am Main
Germany
T: +49 (0)69 97 11 26
F: +49 (0)69 97 20 52 20

Hong Kong

11/F, Jardine House
1 Connaught Place
Central
Hong Kong
T: +852 2846 8989
F: +852 2868 0898

Jakarta (Associated Office)

Oentoeng Suria & Partners
Level 37, Equity Tower
Sudirman Centre
Business District
JI. Jend. Sudirman Kav. 52-53
Jakarta Selatan 12190
Indonesia
T: +62 21 2996 9200
F: +62 21 2903 5360

London

Broadwalk House
5 Appold Street
London EC2A 2HA
UK
T: +44 (0)20 7638 1111
F: +44 (0)20 7638 1112

Madrid

Alcalá, 44
28014 Madrid
Spain
T: +34 91 364 9800
F: +34 91 364 9801/02

Melbourne

Level 26
181 William Street
Melbourne VIC 3000
Australia
T: +61 3 9679 3000
F: +61 3 9679 3111

Milan

Via Sant'Orsola, 3
20123 Milan
Italy
T: +39 02 85 42 31
F: +39 02 85 42 34 44

Munich

Ludwigpalais
Ludwigstraße 8
80539 Munich
Germany
T: +49 (0)89 24 44 21 100
F: +49 (0)89 24 44 21 101

New York

Times Square Tower
7 Times Square
New York, NY 10036
USA
T: +1 212 205 7000
F: +1 212 205 7020

Paris

18, square Edouard VII
75009 Paris
France
T: +33 (0)1 53 53 53 53
F: +33 (0)1 53 53 53 54

Perth

Level 32, Exchange Plaza
2 The Esplanade
Perth WA 6000
Australia
T: +61 8 9366 8000
F: +61 8 9366 8111

Port Moresby

Level 4, Mogoru Moto Building
Champion Parade
PO Box 850
Port Moresby
Papua New Guinea
T: +675 309 2000
F: +675 309 2099

Rome

Via Sistina, 4
00187 Rome
Italy
T: +39 06 42 10 21
F: +39 06 42 10 22 22

Shanghai

Suite 3408-10
CITIC Square
1168 Nanjing Road West
Shanghai 200041
PRC
T: +86 21 6263 1888
F: +86 21 6263 1999

Singapore

55 Market Street
#07-01
Singapore 048941
T: +65 6221 2214
F: +65 6221 5484

Stockholm

Jakobsgatan 6
Box 7124
SE-103 87 Stockholm
Sweden
T: +46 (0)8 407 24 00
F: +46 (0)8 407 24 40

Sydney

Level 36, Grosvenor Place
225 George Street
Sydney NSW 2000
Australia
T: +61 2 9258 6000
F: +61 2 9258 6999

Tokyo

Shiroyama Trust Tower
30th Floor
4-3-1 Toranomom, Minato-Ku
Tokyo 105-6030
Japan
T: +81 3 5405 6200
F: +81 3 5405 6222

Washington DC

1875 K Street NW
Washington, DC 20006
USA
T: +1 202 912 8000
F: +1 202 912 8050

This publication is not intended to be a comprehensive review of all developments in the law and practice, or to cover all aspects of those referred to. Readers should take legal advice before applying the information contained in this publication to specific issues or transactions. For more information please contact us at aus.marketing@ashurst.com.

Ashurst Australia (ABN 75 304 286 095) is a general partnership constituted under the laws of the Australian Capital Territory carrying on practice under the name "Ashurst" under licence from Ashurst LLP, a limited liability partnership registered in England and Wales. Further details about the Ashurst group can be found at www.ashurst.com.

© Ashurst Australia 2012. No part of this publication may be reproduced by any process without prior written permission from Ashurst. Enquiries may be emailed to aus.marketing@ashurst.com. Ref: 652194360.01 10 May 2012