



Philippa Stone, partner and joint global head of capital markets, and Nicole Pedler, senior associate, Herbert Smith Freehills

TAKING STOCK

What issuers need to know about ASIC's report on equity raising allocations.

A new report by regulator the Australian Securities and Investments Commission (ASIC) has identified better practices for issuers and financial services licensees assisting companies to execute transactions.

ASIC's Report 605, *Allocations in equity raising transactions*, released in December 2018, identified a spectrum of conduct ranging from good to well below required standards during equity raisings by ASX companies.

ASIC's overall message was not to change the standard approach. But it expressed concerns about issuers appearing not to obtain the best price for equity raising transactions. Its statements were based on a comparison of the issue price to the volume-weighted average price for the first day of trading following listing. This revealed the median security price increase was 5.6 per cent for initial public offerings (IPOs) and 4.1 per cent for placements.

This focus on price does not sufficiently acknowledge issuers have a range of objectives in addition to obtaining best price, which ASIC acknowledges in the report. These include ensuring long-term investors receive allocations and supporting a healthy aftermarket. Nonetheless, ASIC expects improvements in this area.

Context and scope

The way equity raisings are conducted is important given issuers' and licensees' obligations regarding market manipulation, making false or misleading representations, misleading or deceptive conduct and insider trading. Overstating investor demand in a capital raising is one example of this type of activity. ASIC's practice point suggestions provide guidance for companies.

A licensee's role when assisting an issuer with a capital raising is to identify investors to subscribe for new securities

and provide recommendations around securities' allocations. The issuer approves the allocation recommendation provided by the licensee and issues the new securities. Although in some cases the issuer will only be consulted about allocations, rather than having a veto or approval right. This does not preclude it from expressing its views.

Issuers should advise licensees about what they want to achieve from transactions, for example obtaining funds for a new acquisition. They should ensure existing shareholders receive a fair allocation, at the same time enhancing the shareholder base with additional supportive investors. ASIC recommends issuers discuss the approach to allocations with the licensee at various stages during a transaction such as when pitching, marketing and when the allocation recommendation is provided by the licensee.

It's also important for issuers to disclose their other objectives. These might include the issue price, who the recipients of new securities should be, the preferred register composition, the likely security price performance after the issue and geographic spread preferences.

Negotiate terms of engagement with the licensee, including a provision about

“Licensees generally provide feedback to issuers after they have marketed a transaction, at the same time preparing an allocation recommendation.”

how allocation decisions are made and approved and a clear statement of the issuer's role in the allocation process. As ASIC noted, the allocation decision is often a matter of negotiation between the issuer and the licensee.

Allocation recommendations

Licensees generally provide feedback to issuers after they have marketed a transaction, at the same time preparing an allocation recommendation. As ASIC observed, while issuers were generally interested in the outcome of allocations, their levels of engagement in the allocation process were variable.

ASIC has recommend it is better practice for issuers to understand and engage with the allocation process. For secondary capital raisings, consider the treatment of existing security holders, including passive investment funds, in allocation decisions.

For rights issues, consider the potential control implications of the offer structure, shortfall mitigation strategy and underwriting arrangements. Ask the licensee to provide a copy of their allocation policy and explain how the allocation recommendation is consistent with the policy and the issuer's objectives.

Messages to investors

Poor conduct around messages provided to investors during an equity raising may breach the prohibitions in the *Corporations Act* and the *ASIC Act* relating to misleading and deceptive conduct. Issuers also need to be mindful of their continuous disclosure obligations when making statements in market announcements about the level of demand for a transaction.

As such, issuers should scrutinise and question the basis for any advice or statements in draft ASX announcements about the transaction, in particular about the nature and level of demand from investors. It's also important to avoid the use of overly-expressive language and ensure statements are accurate and not misleading. ASX companies are encouraged to consider these issues to ensure they remain compliant.