

# A practical guide to IPOs, RTOs & ICOs



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## OVERVIEW OF IPO'S

An IPO is the process of transitioning a private company to a public company that is listed on the Australian Securities Exchange (ASX) with shares that can be publicly traded. Listing a company is an undertaking that is costly in time and money, and requires plenty of planning and preparation.

### ADVANTAGES

- **Capital:** the company's capital raising ability can be improved by exposing the company to a broad network of investors
- **Liquidity:** greater liquidity in the company's securities allows shares to be traded
- **Acquisitions:** the company's securities can be used as currency for acquiring other businesses
- **Exit Strategy:** a listing can create an exit for private investors or founders
- **Staff retention:** employees may have access to employee share/option schemes
- **Profile:** greater awareness of the company and its businesses, enhanced public profile, and more attractive to international investors.

### DISADVANTAGES

- **Loss of control:** founders / former owners may lose control, and the interests of shareholders may differ from the founders' objectives
- **Cost:** initial listing fees, annual listing fees, professional fees, compliance costs, increased costs of convening shareholder meetings
- **Accountability:** greater accountability to shareholders, and increased disclosure and reporting obligations
- **Privacy:** loss of privacy arising from greater public interest

- **Risk:** market conditions that are outside your control may affect the company's securities

- **Escrow periods:** the ASX can restrict the transfer of shares issued before the listing for up to two years after the listing, which can impact a founder's proposed exit strategy

### ADVISERS

You will need a team of professional advisers to guide you through the listing process.

- **Investment bank/lead manager:** coordinates, structures, markets the IPO and manages the offer
- **Lawyer:** prepares for the listing, coordinates the due diligence process, conducts legal due diligence, prepares the prospectus, advises on underwriting and is involved with offer management arrangements
- **Investigating accountant:** conducts financial and accounting due diligence and assists with the financial disclosures in the prospectus
- **Public relations consultant:** ensures the media coverage of the IPO is appropriately managed
- **Tax adviser:** advises on the tax implications of the listing process
- **Share registrar:** assists with maintaining the share register and processing applications

### LISTING PROCESS

The following timeline provides an indication of the listing process. The ASX divides the listing process into seven steps within an indicative time frame of 19 weeks for a relatively smooth transaction with diligent advisers and no material complications:

- **Step 1 (week 1):** Appointment of advisers and formation of a due

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diligence committee

- **Step 2 (weeks 2-10):** Preparing the prospectus and carrying out due diligence and verification
- **Step 3 (weeks 10-12):** Institutional marketing program commences
- **Step 4 (weeks 11-12):** Lodge prospectus with ASIC
- **Step 5 (weeks 11-16):** Lodge listing application with ASX
- **Step 6 (weeks 13-17):** Marketing and Offer period
- **Step 7 (weeks 18-19):** Offer closes, shares allocated, trading commences.

## ADMISSION TESTS

For a company to be admitted to the Official List of listed companies, the ASX must be satisfied that the following requirements are met:

### • Profit test requirements:

- the company must be a going concern
- its main business activity must have remained the same as it was during the last 3 full financial years
- it must provide audited accounts for the last 3 full financial years
- it must provide directors' statements confirming there is nothing suggesting the company is not continuing to earn profit from continuing operations up to the date of application
- it must have A\$1 million aggregated profit from continuing operations over the past 3 years and A\$500,000 consolidated profit from continuing operations over the last 12 months

OR

### • Asset test requirements:

- the company must have A\$4 million net tangible assets or A\$15 million market capitalisation
- it must have working capital of at least \$1.5 million and a statement must be included in the prospectus that the company has enough working capital to carry out its stated business objectives

## OTHER CONSIDERATIONS

- **Spread:** there is a requirement for shareholder spread, which comprises a minimum of 300 non-affiliated security holders who each hold shares with value of at least \$2,000
- **Free float:** there is a requirement for a minimum free float of 20% (the percentage of securities which are held by 'non-affiliated' security holders)
- **Structure:** the structure of offer must be considered (whether it takes the form of a subscription or sale or it is simply a compliance listing without any capital raise)
- **Governance:** there may need to be Board and governance changes, including the adoption of a board charter, remuneration committee charter, audit and risk committee charter, code of conduct, and policies on risk management, diversity, shareholder communications, and securities trading)
- **Material contracts:** the company must ensure that its material contracts are in writing and on foot

- **Assets:** the company must ensure that its assets are legally protected
- **Public company:** the company will need to convert to a public company if it does not already have that status
- **Prospectus liability:** the directors should take all steps to ensure that they are protected against liability for making misleading statements
- **Insurance:** the directors may consider IPO insurance to protect themselves from prospectus liability as this is generally not covered in D&O insurance
- **Regulators:** the company must liaise with ASIC and the ASX. ASIC regulates the offers of securities, and the ASX regulates admission to trading on the ASX and compliance with the ASX Listing Rules
- **Costs and timing:** the work and time involved in the listing process should not be underestimated. Typically the whole process will take about six months as there is usually a significant preparatory period as well as the listing work. This can take management focus away from the operation of the business. In addition to the advisers' fees, the company must also pay the ASX's initial listing fee (\$73,500 for a company with \$10 million market capitalisation up to \$152,250 for a company with more than \$100 million market capitalisation) and ongoing annual fees (\$25,732 for a company with \$10 million market capitalisation up to \$43,903 for a company with more than \$100 million market capitalisation)

## KEY DOCUMENTS

The following are the primary documents required during a listing process:

- **Prospectus:** a document which contains all the information reasonably required by investors and their professional advisers to make an informed assessment about the rights and liabilities attached to the offered shares and the company's assets and liabilities, financial position, performance, their profits and losses and prospects
- **Appendix 1A ASX Listing Application and Agreement:** a form that must be completed and submitted to the ASX.
- **Audited financial statements** for the 3 previous years
- **Corporate governance statement** confirming the adoption of relevant policies
- **Criminal history checks** for each director
- **Copy of employee incentive plan** if applicable
- **Copies of all material contracts**
- **Copies of all voluntary and mandatory escrow agreements with shareholders**
- **Supporting documentation** to Listing Application: other documents referred to in the Information Form and Checklist (ASX Listing) on the ASX website

## CONTINUING OBLIGATIONS

After a company's securities are listed on the ASX, the company will be required to comply with various additional obligations under the ASX Listing Rules. These include:

- continuous disclosure obligations
- full and half yearly financial reporting
- limitations on issues of new shares without shareholder approval
- restrictions on transactions with related parties without shareholder approval
- restrictions on significant transactions without shareholder approval
- the adoption of best practice recommendations for corporate governance, and the “if not, why not” approach to reporting on these practices

## OVERVIEW OF RTO'S

A reverse takeover, also known as a 'backdoor listing', is the acquisition of a listed company by shareholders in a (usually smaller) private company. It is typically more suitable for companies where capital is either already available or not needed.

### KEY STEPS

- Finding a listed shell company and either buying control or taking control of the listed shell company
- Seeking 'buy-in' from the board and major shareholders of the private company
- Signing a heads of agreement
- 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 the issue of shares under ASX Listing Rule 7.1 and changes in the nature and scale of the company as a result of the RTO under ASX Listing Rule 11.1
- Raising capital to grow the business and issuing a full prospectus (if necessary)
- Formally reinstating the company's securities to quotation on the ASX.

## ADVANTAGES

- It may result in less share dilution (and therefore greater control) in the company for the original shareholders (compared to a typical IPO)
- It can avoid triggering a change of control clause in a key contract
- The listed company will already likely satisfy certain conditions for listing that the private company may struggle to achieve through an IPO (particularly the preexisting 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)

## DISADVANTAGES

- There is likely to be a premium on the price of the listed company
- There is exposure to pre-existing contingent liabilities of the listed company
- The ASX may require that shares issued to some or all incoming shareholders are subject to mandatory escrow
- The RTO approval process may result in a public valuation placed on the business that may not reflect the value attributed to the transaction

## OTHER CONSIDERATIONS

Historically RTOs were often considered to be a cheaper, easier and a quicker way to list a company on a stock exchange, however, this is not necessarily still the case. Recent changes to the ASX Listing Rules now require an RTO to be approved by the listed entity's shareholders (as well as the target entity's shareholders), and there was also a change to the voting requirements with excluded persons now only prevented from voting in favour of a resolution, but being entitled to vote against it. Also the shares of the listed entity will be suspended when shareholder approval is obtained (until re-admission) which prevents shareholders from taking advantage of any spike in the price when the RTO is announced. These changes have made it more expensive and time-consuming in practice to implement an RTO.

## OVERVIEW OF ICO'S

ICOs are a relatively new way to raise capital. Investors transfer cryptocurrencies, which are digital or virtual currencies that are encrypted (secured), in exchange for digital coins/tokens (Tokens) for a set period of time. Companies usually sell Tokens in order to fund projects and operations and to meet other business objectives.

## REGULATORY ENVIRONMENT

The regulatory environment for ICOs remains uncertain and differs in each jurisdiction globally. In Australia, the structure, operation and the rights attaching to Tokens offered through an ICO help to determine the legal status of an ICO. If the ICO can be classified as a managed investment scheme, or the Tokens which form part of an ICO, can be classified as shares, derivatives or other financial products, then the laws which apply to these products (for example in the Corporations Act 2001 (Cth)) will apply.

## PROCESS

As there are few rules specifically for ICOs, there are only few key steps or requirements, which include:

- the preparation of an ICO whitepaper, which is created by the project team to detail the key information of the project
- an ICO must be conducted in a manner that promotes investor trust and confidence
- an ICO must comply with relevant laws, including the rules against providing misleading information.

## ADVANTAGES

- **Lack of regulation:** there is currently very little regulatory oversight, although this is expected to change as regulatory authorities around the world start to impose new rules
- **Open access:** the access to offerings is open to everyone
- **Time:** the time to implement an ICO is shorter than for an IPO.

## DISADVANTAGES

- **Lack of transparency:** most projects only have a conceptual framework set out in the white paper which makes assessing the fundamentals of an offer difficult, and due diligence tends to be focused towards the project's future expectations rather than its past history (since there usually is none)

- **Scam coins:** it is relatively easy for anyone to use blockchain technology to create an impressive looking ICO. Virtual currency exchanges and other entities holding virtual currencies, virtual tokens or coins may be susceptible to fraud, technical glitches, hacks, or malware. Virtual tokens or virtual currency can be easily stolen by hackers and the ability to recover them is significantly limited. Third-party wallet services, payment processors, and virtual currency exchanges that play important roles in the use of virtual currencies may be located overseas or may operate unlawfully. As a result, there can be challenges when investigating ICOs and investor remedies can become very limited.

- **No ownership:** the acquisition of Tokens does not grant ownership of the project.

## CONTACT US

The corporate team at Swaab 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 Angela Harvey.



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