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By email

Corporations Team
Australian Securities and Investments Commission
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Email: asic.takeovers.policy.submissions@asic.gov.au

Dear Sir / Madam

Submission on ASIC Consultation Paper 365: Remaking ASIC class orders on takeovers, compulsory acquisitions and relevant interests

Thank you for the opportunity to make comments in response to ASIC's Consultation Paper 365: *Remaking ASIC class orders on takeovers, compulsory acquisitions and relevant interests (CP 365)*.

We wish to make submissions in response to Question B3Q1 regarding ASIC's proposal to amend the money lending exception in section 609(1) of the *Corporations Act 2001* (Cth) (**Corporations Act**), as modified by [CO 13/520], to apply only where a lender does not have other relevant interests in securities of the entity.

For the reasons set out below, we do not agree with ASIC's proposal to amend the money lending exception in section 609(1) and submit that the current wording of the exception should be retained. In our view, the proposed amendment is inconsistent with the policy objectives of Chapter 6 and issues relating to misuse of the exception would be better addressed by way of updated guidance.

1 Purpose of ASIC's proposal in CP 365

- (a) As noted in paragraph 26 of CP 365, ASIC is considering whether the money lending exception in section 609(1), as currently modified by [CO 13/520], should be amended such that it will not apply where a financier has an equity interest in securities in the entity.
- (b) The amendment has been proposed because, where a financier otherwise has an equity interest in securities in the entity, this may imply that the arrangements are contrary to the ordinary provision of financial accommodation, and therefore may be a potential misuse of the exception and inconsistent with the policy basis of section 609(1). ASIC has noted that the matter is being raised following consideration of this issue in *Donaco International Limited* [2019] ATP 11 (**Donaco**).
- (c) For the reasons set out in this submission, we submit that ASIC's proposed amendment to the money lending exception in section 609(1), as currently modified by [CO 13/520], should not be adopted as it would be inconsistent with the policy objectives of Chapter 6 of the *Corporations Act* and would place an unreasonable and unnecessary restriction on lenders that would be at odds with their ordinary course business practices.
- (d) We note that the intended scope of operation of ASIC's proposed amendments to the money lending exception is not entirely clear to us from the proposal in B3 and the explanation in paragraph 26 of CP 365. We presume that ASIC's proposal is that, where a financier has any other equity interest in an entity, that financier may not rely on the money lending exception in

respect of (A) the relevant interests in securities that would arise from the taking by that financier of security interests in the ordinary course of providing financial accommodation, nor (B) that other equity interest, even where that other equity interest forms part of broader security arrangements entered into in the ordinary course of providing the financial accommodation.

- (e) We also note that, although our view is that the wording in section 609(1), as currently modified by [CO 13/520], should be retained and ASIC's proposed amendments should not be implemented, it is not clear from paragraph 7(a) of Attachment 3 to CP 365 how such changes are addressed in the revised instrument. If, notwithstanding our submissions, ASIC decides to proceed with implementing the amendments, the wording in paragraph 7(a) of the instrument will need to be refined to remove any ambiguity and to provide clarity on how the amendments are intended to operate.

2 Potential issues associated with the proposed amended money lending exception

Commercial investments

- (a) The overall objective of Chapter 6 of the Corporations Act is to ensure that, among other things, acquisitions of control take place in an efficient, competitive and informed market, and that the Eggleston principles are upheld.
- (b) Any amendment to the money lending exception in section 609(1) that results in a lender being restricted from acquiring a relevant interest in an entity under any circumstances, even as part of a separate commercial investment, if it wishes to rely on the exception would be inconsistent with the policy objectives of Chapter 6.
- (c) For example, under the proposed amendment, if an institutional bank holds a security interest over 5% of the shares in a listed entity through its banking arm in the ordinary course of its lending business, and separately, its business development arm holds an interest in 19% in the same listed entity, the bank would no longer be able to access the money lending exception and therefore would be deemed to hold a relevant interest in the entity of over 20%. This consequence is uncommercial and unreasonable, as:
 - (i) a commercial investment by one division of an institutional bank in an entity would ultimately bar the banking division of the same bank from lending money to that entity (or vice versa); and
 - (ii) in certain circumstances, the proposed amendment could potentially require lenders to either cease lending money to an entity or undertake a sell down of equity interests in an entity where the lender ceases to be able to rely on the money lending exemption (for example, to avoid a breach of section 606 of the Corporations Act).
- (d) Accordingly, the proposed amendment may negatively impact the availability of credit, impose material compliance burden on lenders and create significant inefficiency and increase volatility in the market (inconsistent with the Eggleston principles).

Equity component of financing arrangements

- (e) In the case of a non-traditional lenders, taking equity positions alongside debt positions is not uncommon, particularly in circumstances where the risk profile and nature of the borrower's business may mean that it is not able to service a higher interest rate required to access more traditional secured lending arrangements from major banks. For example, it is common practice for such lenders to take warrants or other equity-based instruments in connection with the provision of debt financing in recognition of the increased credit risk assumed by the lender. Such an equity position would not necessarily reflect the intention of a lender to influence control of the issuer of securities. Accordingly, the proposed amendment may have a material adverse impact on the willingness of non-bank and non-traditional lenders to provide finance and the availability of funding.

- (f) In *Donaco*, the Takeovers Panel decided not to conclude that the lender could not rely on the money lending exception for relevant interests in section 609(1) on the basis that a finding that the money lending exception did not apply could have a negative impact on non-traditional lending in Australia (see paragraph 95 of the *Donaco* reasons for decision).
- (g) The issue has also been discussed at length by Associate Professor Emma Armson of the University of New South Wales.¹ Assoc. Prof. Armson has noted the practice of financiers holding equity interests in entities to which they lend money, in support of the argument in *Donaco* that 'taking equity positions alongside its debt positions was in the ordinary course of its business of providing financial accommodation'.²
- (h) For reference, Assoc. Prof. Armson also argued that 'secured lending arrangements involving the lender obtaining an equity interest relating to the company's shares could satisfy the three legislative requirements in the money lending exceptions'.³
- (i) We are of the view it would be preferable for ASIC and the Panel to consider providing guidance clarifying circumstances that would be considered unacceptable for an equity interest to be taken alongside debt or otherwise (for example, where the combined interest exceeds the 20% limit) and also in respect of when disclosure of such interests should be provided.

Achieving policy objectives

- (j) We consider the proposed amendment would be likely to have unintended and undesirable consequences beyond the purposes of addressing arrangements that may misuse the exception and/or be inconsistent with policy and could have a disproportionate material adverse impact on market participants – inconsistent with promoting an efficient, competitive and informed market.
- (k) Further, we consider that the Takeovers Panel (supported by ASIC and its own guidance) provides the appropriate mechanism for regulating and preventing circumstances where market participants may seek rely on section 609(1) in a manner inconsistent with its policy basis.

3 Conclusion

- (a) For the reasons set out above, we submit that the money lending exception should not be amended as proposed by CP 365. Our view is that the proposed amendments made to the money lending exception are inconsistent with the broader policy objectives of Chapter 6 and will cause unreasonable and uncommercial consequences for lenders and borrowers.
- (b) We submit that, given the complexities associated with the money lending exception and the wide-ranging circumstances of individual lenders and borrowers, ASIC should take a nuanced approach to regulating the issue. In this respect, we generally agree with Assoc. Prof. Armson's suggestion that the most appropriate means of addressing relevant concerns arising out of the money lending exception would be for the Panel and ASIC to clarify the operation of the exemption through updated guidance.⁴ Following which, to the extent any instances of inappropriate utilisation of the money lending exception arise in the future, ASIC may make submissions to the Takeovers Panel to that effect and it will be open to the Takeovers Panel to declare unacceptable circumstances on a case-by-case basis if deemed necessary (including in circumstances where lenders may in fact comply with the exceptions set out in section 609(1) as currently modified by [CO 13/520]).

¹ Emma Armson, 'Reforming the Money Lending Exceptions for Takeover' (2022) 45(2) *Melbourne University Law Review* 385.

² *Ibid* 407

³ *Ibid* 407.

⁴ *Ibid* 415

Please do not hesitate to contact the below authors if you would like to discuss our submission with us.

Yours faithfully,

Gilbert + Tobin

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