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WHITE PAPER

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# ASX Releases Continuous Disclosure Guidance on the Insolvent Trading Safe Harbour

On 9 March 2018, an updated version of ASX's Guidance Note 8 came into effect to include guidance on a listed entity's continuous disclosure obligations in the context of the new insolvent trading safe harbour for directors contained in section 588GA of the Corporations Act. ASX has made it clear that the safe harbour laws do not affect an entity's continuous disclosure obligations or reduce the entity's obligation to disclose the extent of its financial difficulties. This will place a listed entity under a heightened disclosure risk during the period of a safe harbour.

This Jones Day *White Paper* includes an overview of the continuous disclosure regime, explains ASX's guidance on the insolvent trading safe harbour, and provides recommendations for continuous disclosure management in the safe harbour period

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## BACKGROUND

The safe harbour protections in section 588GA of the *Corporations Act 2001* (Cth) ("Corporations Act"), which came into force on 19 September 2017, provide a conditional carve-out from a director's potential liability for insolvent trading provided certain conditions are satisfied. The safe harbour will protect directors from insolvent trading liability for debts incurred by a company if, after a director starts to suspect that the company may become or is insolvent, the director starts developing one or more courses of action that are reasonably likely to lead to a better outcome for the entity than the immediate appointment of an administrator or liquidator to the company. There are a number of other conditions that must be satisfied to rely on the safe harbour protections, and the protections will only apply to debts incurred directly or indirectly in connection with any such course of action.

Since the safe harbour laws came into force, there has been uncertainty as to whether a listed entity is required to make an immediate disclosure to ASX if its directors decide to rely on the insolvent trading safe harbour, and the extent to which the safe harbour reduces or otherwise alters the entity's disclosure obligations regarding its financial position and the courses of action being developed by the directors. The updated guidance from ASX provides some helpful clarifications in this regard, as discussed below.

## OVERVIEW OF CONTINUOUS DISCLOSURE REGIME

Once a listed entity is or becomes aware of any information concerning the entity that a reasonable person would expect to have a material effect on the price or value of the entity's securities, Listing Rule 3.1 requires the entity to immediately tell ASX that information.

Listing Rule 3.1A sets out the carve-outs to the general disclosure requirement. The carve-outs provide that an entity will not be required to disclose information while *all* of the following are satisfied:

- The information falls within one of a number of additional criteria (for example, the information comprises matters of supposition, is insufficiently definite to warrant disclosure or concerns an incomplete proposal or negotiation);
- The information is confidential and ASX has not formed the view that the information has ceased to be confidential; *and*
- A reasonable person would not expect the information to be disclosed.

The Corporations Act creates civil and criminal liability for noncompliance with the continuous disclosure requirements. Liability can extend not just to the listed entity, but also to individual directors and officers who are involved in the contravention.

## ASX GUIDANCE ON THE INSOLVENT TRADING SAFE HARBOUR

The updated guidance issued by ASX provides some useful clarifications for directors of listed entities who are relying on the insolvent trading safe harbour.

ASX has confirmed that the fact an entity's directors are relying on the insolvent trading safe harbour is unlikely to constitute information that (in isolation) requires disclosure to the market, as it is likely to fall within the carve-outs to immediate disclosure under Listing Rule 3.1A. This is on the basis that information about possible alternatives to an insolvent administration being pursued by directors concern an incomplete proposal or negotiation or is insufficiently definite to warrant disclosure. However, as soon as the information ceases to be confidential or the directors determine a definitive course of action, the entity will be required to make an immediate disclosure to ASX of the information under Listing Rule 3.1.

It is important to note that the safe harbour does not affect an entity's continuous disclosure obligations or reduce the entity's obligation to disclose the extent of its financial difficulties. This was made clear in the Explanatory Memorandum for the Treasury Laws Amendment (2017 Enterprise Incentives No. 2) Bill, which introduced section 588GA, and this point has been specifically restated by ASX in its guidance on the issue. This means that directors will need to carefully consider the financial and other information underpinning their suspicions regarding an entity's insolvency to determine whether that information includes market sensitive information. This should include an analysis of previous earnings guidance or financial statements regarding the entity's financial position (including analyst commentary) that may require correction or updating by way of announcement under Listing Rule 3.1.

It is also worth noting that an entity cannot rely on the disclosure carve-out for information that is insufficiently definite to warrant disclosure if the entity is aware of information about a known event or circumstance that will have a material effect on the price or value of its securities, but has not yet been able put a figure or estimate on the financial impact on the event or circumstance. In other words, an entity could not delay announcing a material impairment to its assets exists (which in turn underpins the directors' suspicions regarding insolvency) just because the entity is not yet in a position to quantify the magnitude of that material impairment for the purposes of announcement.

Any entity that seeks to rely on the safe harbour will be under tremendous pressure to develop, negotiate and complete a definitive course of action as soon as possible and within a reasonable period. If the listed entity becomes aware that it is required to immediately announce materially negative market sensitive information regarding the financial position of the entity and that disclosure may pose a significant impediment to successfully executing a particular turnaround transaction, ASX has stated that the proper course is for the listed entity to approach ASX to discuss the possibility of a voluntary suspension (or a trading halt if appropriate) to manage the entity's disclosure obligations while it completes the transaction.

An entity seeking a voluntary suspension will need to make a written request to ASX for release to the market that meets the requirements of Listing Rule 17.2, including by containing the reasons for the suspension (or continued suspension) and a proposed timetable for trading in its securities to resume. ASX has specifically stated that the request must include a forthright account of the entity's current financial situation, details of the turnaround transaction that the entity says is critical to its continued financial viability, and an affirmation that, in the entity's opinion, continued trading of its securities is likely to be materially prejudicial to its ability to complete that transaction.

## RECOMMENDATIONS FOR CONTINUOUS DISCLOSURE MANAGEMENT IN THE SAFE HARBOUR PERIOD

Listed entities relying on the safe harbour should adopt a disclosure strategy on a case by case basis to ensure that the entity's interests in completing a turnaround transaction under the safe harbour on a confidential basis are balanced with the overriding duty of the directors to comply at all times with the entity's continuous disclosure and financial reporting obligations. It will be particularly important that the entity has systems in place to protect against leaks during the safe harbour period. This strategy should be prepared with the benefit of specialist advice and oversight from a deal team including insolvency and public M&A practitioners.

An entity that is relying on the insolvent trading safe harbour will be subject to a heightened level of continuous disclosure risk as it attempts to develop, negotiate and execute a financial restructure, reorganisation or other turnaround transaction in the safe harbour period. The entity's financial reporting obligations will also remain unaffected during the safe harbour, and so the

timing for preparation and lodgement for an entity's financial reports (which includes the directors' statement of solvency) will also need to be factored into the disclosure strategy for implementing any turnaround transaction on a confidential basis.

Generally speaking, the disclosure risks will likely be much greater if the directors suspect that the entity is insolvent, as opposed to merely suspecting that the entity may become insolvent. In any case, if an entity that relies on the safe harbour ends up in an insolvent administration, continuous disclosure compliance will often be judged in hindsight. This poses a significant class action and litigation risk for directors, as securityholders and other stakeholders will look carefully to identify any potential disclosure breaches (including by omission or delay) regarding the entity's financial difficulties in the period leading up the appointment of an administrator. It is also important to note that although an entity may be able to rely on a disclosure exception to Listing Rule 3.1, the entity (and its officers) may still be liable for other contraventions such as engaging in misleading and deceptive conduct. A disclosure strategy should also seek to protect against the risks of any action for misleading and deceptive conduct.

## LAWYER CONTACTS

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