

BACKDOOR LISTINGS

in Australia

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We study a large sample of Australian backdoor listings (BDLs) over the period from 1994 to 2014. BDLs account for roughly 13 per cent of all firms going public on the Australian Securities Exchange and are popular among hi-tech firms and those with foreign-domiciled assets. We find that the BDL market is likely influenced by the sentiment in the initial public offering (IPO) market, with the number of BDLs announced in a year being negatively (positively) correlated with the number of IPOs lodged (the percentage of IPOs withdrawn) in the prior year. Contrary to common belief, BDL transactions take longer to complete than IPOs, since they typically combine both a reverse takeover and the public listing process. Roughly three-quarters of our sample raised equity capital as part of the BDL process.

Backdoor listings (BDLs) have long been considered a viable alternative to IPOs for private firms seeking to list on the Australian Securities Exchange (ASX). In 2014, Australia witnessed a record number of BDLs, with these transactions being widely reported in the financial media.¹ This recent 'mining to tech' backdoor listing trend led Australian Securities and Investments Commission (ASIC) Commissioner John Price to raise a number of regulatory concerns about the BDL process.² Despite the popularity of BDLs on the ASX, Brown et al. (2013) is the only empirical Australian work that has been published in this area. While Kuo and Humphrey (2002) consider some of the key commercial, structural and regulatory issues surrounding BDLs, their discussion is largely qualitative in nature, relying mostly on anecdotal evidence. In view of this, the objective of this paper is to provide large sample evidence on various facets of BDL transactions, including their clustering across time and industry, origin of the private target, transaction format, deal size and consideration, regulatory approvals, related-party transactions, change of control, capital raisings, and transaction duration.

Backdoor listing defined

Backdoor listing is a loosely defined term that generally refers to a sequence of structured intercompany events whereby a private/unlisted firm or asset (target) achieves a listing status through a reverse takeover (RTO) of a publicly listed firm (shell), using the corporate shell of the latter as a vehicle for going public. Some confusion exists as to what constitutes a BDL and this has been reflected in various media reports.

It is important to note that a change of control in the listed entity is critical to the BDL process. Without a change of control, the transaction is simply a change in the direction and/or scale of a listed entity's business, with target shareholders having no significant role in the merged firm after the takeover.³ We assume a change of control has occurred if target shareholders collectively own a majority of the voting rights in the merged entity at the conclusion of the RTO prior to any capital raisings. In cases where a majority shareholding is not achieved, it is sufficient for target shareholders to have effective control if they, collectively, become the largest equity blockholder⁴ and either dominate the board of directors or occupy the position of CEO/managing director of the combined firm.

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Data

Our sample consists of 302 BDLs completed on the ASX between January 1994 and December 2014. The sample is identified through media search on Factiva. Each case is verified as a genuine BDL according to our definition by manual examination of the relevant public announcements disclosed by listed shells on Morningstar's *DatAnalysis Premium* database. For comparison purposes, we obtain a sample of initial public offerings (IPOs) spanning the same time period from the Connect4 database.

Distribution of BDLs across years and industries

Figure 1 depicts the distribution of BDLs over the 1994–2014 period together with a breakdown by industry. Table 1 presents additional information on both BDL and IPO activity over the same time period. It is evident that BDL completion frequency is relatively low before 1999 and peaks in 2000 (coinciding with the dotcom bubble with 31 transactions completed). They remain active over the ensuing period (2001–04) before tapering off in the lead-up to the global financial crisis (GFC) when the IPO market was booming. BDL activity picks up again after the GFC, cumulating in another record year in 2014. Overall, BDLs account for 13 per cent of all firms going public during the 1994–2014 period.

TABLE 1: Distribution of BDLs and IPOs by year

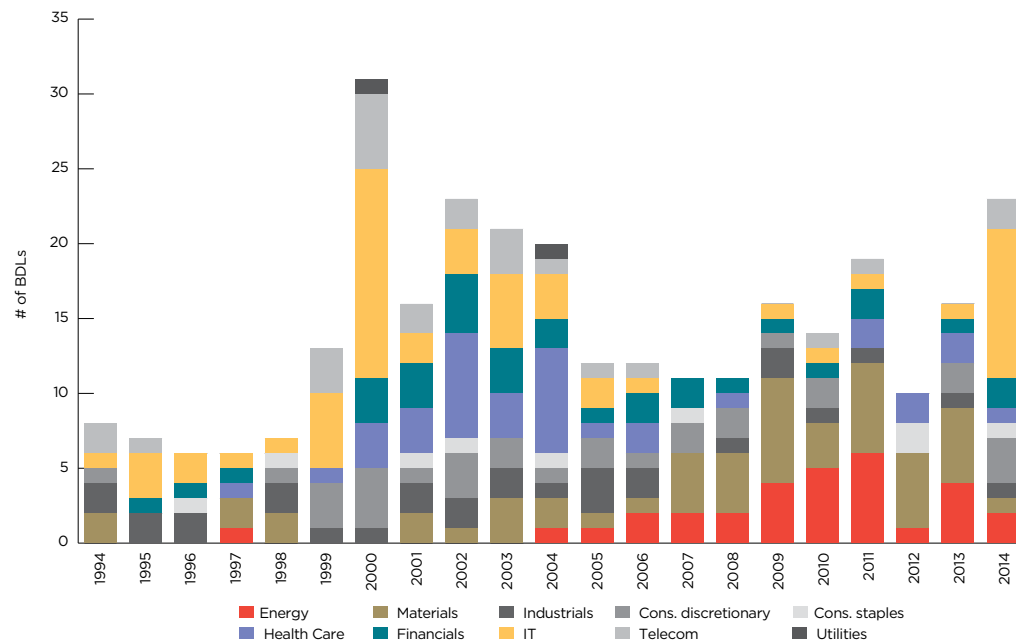
Year	BDL				IPO						All going-public Transactions		
	Announced		Completed		Lodged		Listed		Withdrawn		All	% BDL	% IPO
	No.	%	No.	%	No.	%	No.	%	No.	% of lodged			
1994	11	3.5	8	2.6	114	4.9	90	4.5	18	15.8	98	8.2	91.8
1995	7	2.2	7	2.3	44	1.9	37	1.8	4	9.1	44	15.9	84.1
1996	5	1.6	6	2.0	78	3.3	68	3.4	6	7.7	74	8.1	91.9
1997	7	2.2	6	2.0	79	3.4	76	3.8	9	11.4	82	7.3	92.7
1998	4	1.3	7	2.3	45	1.9	47	2.3	1	2.2	54	13.0	87.0
1999	26	8.2	13	4.3	112	4.8	106	5.2	1	0.9	119	10.9	89.1
2000	24	7.6	31	10.3	195	8.4	149	7.4	37	19.0	180	17.2	82.8
2001	21	6.6	16	5.3	70	3.0	59	2.9	20	28.6	75	21.3	78.7
2002	25	7.9	23	7.6	75	3.2	66	3.3	15	20.0	89	25.8	74.2
2003	19	6.0	21	7.0	110	4.7	91	4.5	8	7.3	112	18.8	81.3
2004	13	4.1	20	6.6	182	7.8	161	8.0	16	8.8	181	11.0	89.0
2005	16	5.0	12	4.0	191	8.2	172	8.5	20	10.5	184	6.5	93.5
2006	8	2.5	12	4.0	203	8.7	181	9.0	18	8.9	193	6.2	93.8
2007	9	2.8	11	3.6	250	10.7	247	12.2	22	8.8	258	4.3	95.7
2008	13	4.1	11	3.6	59	2.5	42	2.1	16	27.1	53	20.8	79.2
2009	17	5.4	16	5.3	48	2.1	38	1.9	5	10.4	54	29.6	70.4
2010	24	7.6	14	4.6	138	5.9	100	4.9	16	11.6	114	12.3	87.7
2011	9	2.8	19	6.3	114	4.9	106	5.2	28	24.6	125	15.2	84.8
2012	15	4.7	10	3.3	69	3.0	49	2.4	20	29.0	59	16.9	83.1
2013	16	5.0	16	5.3	62	2.7	59	2.9	13	21.0	75	21.3	78.7
2014	28*	8.8	23	7.6	94#	4.0	78	3.9	4	4.3	101	22.8	77.2
Total	317	100.0	302	100.0	2332	100.0	2022	100.0	297	12.7	2324	13.0	87.0

Notes: *Includes 16 BDLs that are still ongoing. #Includes 14 IPOs that are upcoming floats.

TABLE 2: Correlations between BDL and IPO markets

	(t)	(t-1)	(t-2)
	# IPOs lodged		
# BDLs announced (t)	0.043	-0.265	-0.106
	% IPO withdrawn		
# BDLs announced (t)	0.081	0.208	0.322

The correlation coefficient (Table 2) between the number of BDLs announced in year t and the lagged (year $t-1$) number of IPOs lodged is -0.265 . This seems to suggest that when the IPO market is booming, there is less demand for BDLs. In addition, the number of BDLs announced in year t is positively correlated with the percentage of IPOs withdrawn in year $t-1$ ($\rho=0.208$) and year $t-2$ ($\rho=0.322$). If a high percentage of IPOs withdrawn is a proxy for unfavourable IPO market conditions, the positive correlation indicates a higher subsequent demand for BDLs as an alternative route to public listing (i.e. a substitution effect).

FIGURE 1: Distribution of backdoor listings across years and industries

In terms of industry breakdown, Figure 1 shows technology firms (IT and telecommunications) dominate the two BDL peak years of 2000 and 2014, whereas the 2001–04 period has seen increased participation from the healthcare sector (biotechnology and life science firms). BDLs from the energy and materials sectors played a greater role during the 2007–13 period, coinciding with the later stages of the mining boom and subsequent downturn.

TABLE 3: Breakdown of BDLs and IPOs by industry sector, 1994–2014

Transaction type	Global Industry Classification Standard										
	10	15	20	25	30	35	40	45	50	55	Total
BDL	10.3%	16.9%	9.6%	10.3%	3.0%	11.9%	10.3%	18.5%	8.6%	0.7%	100.0%
IPO	10.2%	35.4%	9.4%	9.6%	2.4%	7.3%	14.7%	7.6%	2.1%	1.5%	100.0%

Note: The Global Industry Classification Standard (GICS) sectors are: energy (10), materials (15), industrials (20), consumer discretionary (25), consumer staples (30), health care (35), financials (40), information technology (45), telecommunication services (50), and utilities (55).

In aggregate, Table 3 shows IPOs are more concentrated than BDLs in the materials (35.4 per cent vs 16.9 per cent) and financial (14.7 per cent vs 10.3 per cent) sectors, whereas BDLs are more concentrated than IPOs in the health care (11.9 per cent vs 7.3 per cent), information technology (18.5 per cent vs 7.6 per cent) and telecommunications (8.6 per cent vs 2.1 per cent) sectors.

Target domicile

TABLE 4: Target domicile by region

Region	No.	%
Australia	203	67.2
<i>Foreign</i>		
North Asia	21	7.0
Southeast Asia	20	6.6
North America	15	5.0
Africa	13	4.3
South Pacific	11	3.6
Europe	9	3.0
South America	5	1.7
Other	5	1.7
Total	302	100.0

The ASX is a popular destination for BDL by foreign firms (Table 4). Of the 302 BDLs sampled, close to one-third (99 cases or 32.8 per cent) of the targets are foreign (either their operations or assets are located outside of Australia). Asia is the leading source of foreign targets, with 21 and 20 of them originating from North Asia (predominately, China) and Southeast Asia (predominately, Singapore and Indonesia), respectively. Other significant sources of foreign targets include North America (15), Africa (13) and South Pacific (11, including New Zealand). By industry, the majority (51 cases or 51.5 per cent) of foreign targets are in the extractive industries (energy and materials). Indeed, 66.2 per cent of all extractive industry targets have their tenements/projects overseas.

Transaction format

TABLE 5: Transaction format

Transaction format	No.	%
Share sale agreement	261	86.4
Public takeover	16	5.3
Scheme of arrangement	5	1.7
Acquisition of business and assets	20	6.6
Total	302	100.0

Table 5 shows the vast majority (261 cases or 86.4 per cent) of BDLs are structured by way of a share sale agreement. This is the case if the target is incorporated as a private company. If the target is an unlisted public company, the transaction has to be structured as a public, off-market takeover (16 cases or 5.3 per cent). In five BDL cases (1.7 per cent), the transaction is conducted as a scheme of arrangement, whereby shareholder approvals and formal court sanctions are required. The remaining 20 cases (6.6 per cent) are acquisitions of businesses and assets, popular if the private target is a real estate development asset.

Deal size and consideration paid

TABLE 6: Deal size, consideration and shareholding by target

Variable	No.	Mean	Median	SD	Min	Max
Deal size (\$m)	302	38.4	12.8	107.0	0.6	1168.1
Cash consideration (\$m)	302	1.8	0.0	7.9	0.0	94.8
Share consideration (\$m)	302	36.5	11.6	106.3	0.6	1168.1
Shareholding by target (%)	302	65.8	66.7	18.2	20.5	99.4

Note: All dollar values have been converted to 2014 dollar terms using the Consumer Price Index published by the Australian Bureau of Statistics.

BDLs are typically small deals (Table 6). In 2014 dollar terms, the average deal size in our sample is \$38.36 million, with a median of \$12.76 million, indicating skewness to the right tail. The smallest and largest deals are \$0.64 and \$1,168 million, respectively. This contrasts with a mean (median) deal value of \$821.44 (\$133.19) million for a sample of 912 other successful acquisitions (other than RTOs) announced during the 1997–2014 period.⁵ Note that our measure of deal size includes only consideration paid by the shells in the form of cash (average \$1.8 million) and shares (average \$36.5 million), suggesting shares account for 95.2 per cent of the total consideration paid. Contingent claims have also been used as a form of payment in BDL transactions. In total, 113 cases (37.4 per cent) involved options as part of the consideration and 60 cases (19.9 per cent) involved earn-outs or deferred payments that depend on certain pre-determined performance hurdles being achieved by the target. Earn-outs are common among BDL deals where the target is involved in technology or mining/exploration businesses and are seen as a way of protecting the shell shareholders from the inherent risk associated with the target.⁶

Regulatory approvals

In Australia, there is no formal regulation of BDLs *per se*. There are, however, provisions in the Corporations Act and the ASX Listing Rules that may become operative and applicable to certain aspects of a BDL. The Corporations Act s 606 generally prohibits a person, or parties acting in concert, from acquiring a relevant interest in the voting shares of a public company if, because of the transaction, that person's voting power in the company increases from 20 per cent or below to more than 20 per cent. Section 611(7) provides an exemption to the prohibition if an acquisition is approved previously by shareholders by a resolution passed at a general meeting. To assist shareholders in assessing the merits of the transaction, the law also requires that shareholders be given all information material to the decision on how to vote on the resolution. In practice, an independent expert's report will normally be required, expressing an opinion on the fairness and reasonableness of the transaction to shareholders. Table 7 reveals that of all 302 transactions in the sample, the takeovers provisions are invoked in 212 cases (70.2 per cent).

TABLE 7: Regulatory approvals

Approval type	No.	%
<i>Corporations Act – Section 606</i>		
Invoked	212	70.2
Not invoked	90	29.8
<i>ASX change of activity</i>		
No significant change	14	4.6
Change to nature	45	14.9
Change to scale	51	16.9
Change to both nature and scale	192	63.6
<i>ASX re-admission requirement</i>		
No re-admission requirement	32	10.6
Re-compliance with Chs. 1 and 2 of Listing Rules	229	75.8
Shareholder approval only	41	13.6
<i>Related-party transaction</i>		
Related	66	21.8
Not related	236	78.2
<i>Name change</i>		
No change	59	19.5
Changed	243	80.5
<i>Prospectus</i>		
Not required	78	25.8
Required	224	74.2

ASX Listing Rule 11.1 deals with any proposed significant change to the nature or scale of activities by listed entities. Depending on how significant the change of activity is, the ASX may, at their discretion, require the listed entity to obtain shareholders' approval at a general meeting and re-comply with the requirements of Chapters 1 and 2 of the Listing Rules again as if the entity is applying for admission to the ASX official list. As Table 7 suggests, only 14 BDL transactions (4.6 per cent) do not constitute a significant change of activity. The remaining 288 cases are classified as significant changes of activities in nature (45 cases or 14.9 per cent), scale (51 cases or 16.9 per cent) or both (192 cases or 63.6 per cent). In excess of 80 per cent of all BDLs are also associated with the shell changing its name. In most cases the name changes to that of the target.

In terms of re-admission requirements (Table 7), 229 BDL cases (75.8 per cent) are required by the ASX to re-comply with Chapters 1 and 2 of the Listing Rules as if they are applying for a new listing while 41 cases (13.6 per cent) require shareholders' approval only. No shareholder approval or re-admission requirements are imposed on the remaining 32 cases (10.6 per cent). Close to three-quarters (74.2 per cent) of all BDLs issued some form of a prospectus or information memorandum for re-compliance and/or capital raising purposes.

Related-party transactions

Table 7 also reports that of all the 302 BDLs, 66 cases (21.8 per cent) are considered related-party transactions. These transactions involve one or more of the vendors of the target being a director and/or substantial shareholder of the shell at the time when the transaction was announced. This indicates vendors of the target might already have a toehold in the shell before the transaction. As a safeguard against conflict of interest, related-party transactions are regulated by Chapter 2E of the Corporations Act and Chapter 10 of the ASX Listing Rules, requiring shareholder approval at a general meeting.

Change of control

TABLE 8: Change of control

Control type	No.	%
Majority shareholding	238	78.8
Largest blockholder + BOD + CEO/MD	38	12.6
Largest blockholder + BOD	5	1.7
Largest blockholder + CEO/MD	21	7.0
Total	302	100.0

Target shareholders, on average, obtained 65.8 per cent of the shareholding in the merged entity at the conclusion of the RTO (prior to any concurrent capital raisings), with a range between 20.5 per cent and 99.4 per cent (Table 6). By control type, Table 8 reveals target shareholders gained control by acquiring a majority of the voting rights in the merged entity in 238 cases (78.8 per cent). Of the remaining 64 cases, target shareholders obtained control by becoming the largest blockholder of the merged entity (with a shareholding of between 20 per cent and 50 per cent) and dominating either the board of directors (5 cases or 1.7 per cent) or the CEO/managing director (21 cases or 7.0 per cent) or both (38 cases or 12.6 per cent).

Concurrent capital raisings

TABLE 9: Capital raisings

Raising type	No.	Mean	Median	SD	Min	Max	Sum
<i>BDLs</i>							
No capital raising	68	0.0	0.0	0.0	0.0	0.0	0.0
Public offer (\$m)	148	7.4	4.8	10.8	0.2	102.5	1098.4
Private placement (\$m)	46	8.7	3.5	14.4	0.1	72.9	401.4
Rights issue (\$m)	8	13.7	6.4	16.9	2.5	52.6	109.5
Mixed offer (\$m)	32	13.3	6.3	24.9	0.8	139.5	426.6
Total (\$m)	302	6.7	3.2	13.3	0.0	139.5	2035.9
<i>IPOs</i>							
Public offer (\$m)	2022	94.6	9.7	590.2	0.3	22404.0	191306.3

Note: All values are converted to 2014 dollar terms using the Consumer Price Index published by the Australian Bureau of Statistics.

Not all BDLs involve capital raisings. As Table 9 shows, 68 cases (22.5 per cent) did not raise any equity capital, suggesting the shell was essentially a cash box or market conditions were not favourable for raising capital at the time. For the remaining 234 cases where capital raisings are involved, the mean and median proceeds (in 2014 dollars) are \$8.7 million and \$4.8 million, respectively. The smallest amount of capital raised is a mere \$0.12 million while the largest raising is \$139.5 million. In terms of capital raisings by type, 148 cases are public offers, 46 cases are private placements, eight cases are rights issues and 32 cases involve mixed offers (more than one offer type).

Transaction duration

TABLE 10: Transaction duration (days)

	No.	Mean	Median	SD	Min	Max
All BDLs	302	174.3	139.5	122.8	36	1216
<i>ASX re-compliance requirement</i>						
Yes	229	189.1	155	131.1	41	1216
No	73	127.8	108	76.1	36	541
<i>Capital raisings</i>						
Yes	234	184.3	148.5	131.8	38	1216
No	68	139.5	126.5	76.2	36	541
<i>By capital raising type</i>						
Public offer	147	194.6	162	139.9	50	1216
Private placement	46	155.4	120.5	93.3	43	394
Rights issue	8	153.0	138	111.0	38	405
Mixed offer	32	190.5	135	142.8	41	618
<i>By transaction format</i>						
Share sale agreement	261	170.6	135	125.8	36	1216
Public takeover	16	182.6	162	77.4	93	390
Scheme of arrangement	5	212.0	180	95.8	134	363
Acquisition of business and assets	20	205.9	185	119.2	64	418
<i>All IPOs</i>						
From lodgement to listing	2022	60.2	51	34.7	12	414
From kickoff to listing	2022	102.2	93	34.7	54	456

Market folklore has it that it is quicker to complete a BDL than an IPO in the process of going public. Table 10 presents evidence on the duration (in days) of BDL transactions, measured from the first announcement date by the shell to the completion date, where the latter is taken as the date the merged entity is re-admitted to the ASX (if re-compliance with Chapter 1 and 2 of Listing Rules is required) or the official date the RTO is completed (if no re-admission to the ASX is required). For BDLs, the mean (median) duration is 174.3 (139.5) days, respectively. Due to an outlier (max = 1,216 days), we focus on the median rather than the mean.

Sub-sample results show BDL transactions with ASX re-admission requirements (155 days) generally take longer to complete than those without re-admission requirements (108 days). Cases with concurrent capital raisings (148.5 days) require more time to complete than those that raise no capital (126.5 days). By capital raising type, BDLs with public offers take the longest (162 days) while those with private placements take a median of 120.5 days, with rights issues and mixed offers lying in between. In terms of transaction type, BDLs structured as share sale agreements are the fastest to execute (135 days), followed by off-market public takeovers (162 days). Scheme of arrangement transactions tend to take longer to complete (180 days), probably due to the more formal procedures (e.g. court sanctions) involved. Interestingly, BDLs structured as acquisitions of business and assets have the longest transaction duration (185 days).

For comparison, we compute two measures of transaction duration for our IPO sample. The first measure captures the number of days from the prospectus lodgement date with ASIC to the listing date. The mean (median) IPO duration is 60.2 (51) days, respectively, which is shorter than that for BDL transactions. We obtain a second measure of IPO duration (from date of kick-off meeting between IPO firm and investment bankers/underwriters until listing date) by adding 42 days⁷ to our first measure. This results in a mean (median) IPO duration of 102.2 (93) days, which is still lower than that for BDLs. Note that the duration measure for BDLs does not take into consideration the initial planning and negotiation stages undertaken by the target prior to the formal deal announcement by the shell. Kuo and Humphrey (2002) estimate it typically takes a target up to four weeks from the initial appointment of advisers through to execution of the term sheet with the shell. Adding another four weeks to our BDL duration measure would render the difference between the two types of going-public transactions even greater.

Conclusion

Evidence from a sample of 302 Australian BDLs suggests they are not necessarily simpler or faster than the IPO process. BDLs are essentially a combination of a RTO and the public listing process. As a result, more regulatory approvals are required and they take longer to complete than IPOs. This finding has implications for entrepreneurs/owners of private firms contemplating a public listing via the backdoor route.

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Notes

1. See, for example, 'Record numbers queuing up for backdoor listings' by Nick Abrahams published in *The Australian Financial Review* on 30 September 2014.
2. 'ASIC raises red flag over "mining to tech" backdoor', by Tess Ingram published in *The Australian Financial Review* on 31 July 2014.
3. For example, the listed firm can acquire the private target by paying all (or majority of) the consideration in cash.
4. We require target shareholders to own at least 20 per cent of the shares in the merged entity.
5. This sample of other acquisitions is obtained from the Connect4 database.
6. The lack of information in assessing the value of these contingent payments means they are not included in our calculation of deal size.
7. Evidence from Floros and Shastri (2010) on US penny stock IPOs shows that the median duration between the kick-off meeting and prospectus registration date is approximately 42 days.

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