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PUBLIC-LISTED COMPANIES

UNDERSTANDING PN17 STATUS

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THE Practice Note 17 (PN17) rules of the Main Market Listing Requirements are part of the fabric of the Listing Requirements (LR) which are meant to highlight that a public-listed company (PLC) is in financial distress.

(The ACE Market Listing Requirements has the Guidance Note 3 which highlights that a PLC is in financial distress).

The LRs are part of the contractual obligations that a PLC undertakes in return for being listed. Since a PLC takes money from the public (and shareholders), the company should be accountable to them when it finds itself in financial distress — this is only equitable.

Thus, PN17 is a rule that seeks to keep all informed of financial distress — it is a public announcement made by the PLC when it finds that it has triggered a PN17 criteria.

When a PLC is tagged as a PN17 company, the market generally reacts negatively by sending the share prices lower, and rightly so, as the company is deemed to be in financial distress.

As we all know, a PN17 status is not necessarily a point of no return. PLCs which have successfully got out of the PN 17 status find that the market rewards such outcome with an uptick in their share prices.

There is a pocket of investors who "specialises" in investing in PN17 companies, hoping to ride on this uptick in share prices.

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Such investors place great reliance on the perceived ability of the board leadership to steer the company out of the PN17 status.

To think of the PN17 status and the underlying criteria as meaningless or irrelevant would be arrogant as the PN17 rules are codified by Bursa Malaysia, and as a check-and-balance, with the tacit approval of the Securities Commission.

There would have been public and industry consultations too.

To better understand the relevance of PN17, one must go to the rule itself — para 2.1 of PN17.

What triggers the PN17 status

There are six conditions under which a PLC would trigger the PN17 status.

Firstly, it is triggered when the shareholders' equity on a consolidated basis is 25 per cent or less of the share capital (excluding treasury shares) and is less than RM40 million.

In layman's terms, this mean the share capital has eroded by 75 per cent or more to a low of RM40 million.

Losses have eaten into the share capital and in these instances, the losses are of such magnitude that they have wiped out more than 75 per cent of the share capital.

The second trigger is when receivers or managers have been appointed to a PLC, its subsidiary or associated company which accounts for at least 50 per cent of the total assets employed on a consolidated basis.

The appointment of receivers or managers indicate that the company is being managed by them and not the board.

Such appointments may result in the companies being wound up if the receivers and managers do not see a future for the company.

The third trigger is the winding-up of a PLC's subsidiary or associated company which accounts for at least 50 per cent of the total assets employed on a consolidated basis.

This is not the end of the PLC as the PLC may choose to "chop off" or rehabilitate the subsidiary or associated company.

The fourth trigger is when the auditors have expressed an adverse or disclaimer opinion in the PLC's latest audited financial statements.

A rule of thumb for investors is that an unqualified opinion is the safest. All other types of opinion indicate different degrees of concern and risk.

The words used in these opinions betray the concern — "adverse" and "disclaimer".

The fifth trigger is when auditors highlight a material uncertainty related to a going concern or express a qualification on the company's ability to continue as a going concern in the company's latest audited financial statements and the shareholders' equity is 50 per cent or less of the share capital (excluding treasury shares) of the company.

A "going concern" simply means what it states — a concern as to whether the company can go on — whether the company can continue to settle its obligations as and when they fall due in the future.

The final trigger is a default in payment by a PLC, its major subsidiary, or major associated company and the PLC is unable to provide a solvency declaration to the exchange.

A default is a serious thing. It is prima facie evidence that you cannot pay your debts.

An inability to declare that you are solvent is equally serious.

As can be noted, there are very cogent reasons why the various triggers have been included as an indication of financial distress.

Minority shareholders should be aware of the implications of a PLC being classified as a PN17 company and the reason why.

Warning bells

When a company is classified as a PN17 company, all is not well. The company is in ill health, and it becomes the responsibility of the board to steer the company back to health (unless receivers or managers have been appointed).

Sometimes, the ill patient recovers to be healthy. Sometimes there is no recovery. Delisting then becomes the demise from the exchange.

Minority shareholders should monitor the regular announcements in relation to the regularisation plans of the PN17 company which are announced to the exchange. They should also monitor the impending deadlines imposed by the exchange.

If you have confidence in the board, you may wish to invest in the PN17 company. But if you are risk-averse, you may wish to avoid PN17 companies. After all, there are more than 900 PLCs which are not PN17 companies on Bursa Malaysia.

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