



The Allens
handbook on
takeovers in
Australia

Overview of Allens

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From playing a pioneering role in the development of legislation and regulatory frameworks in the Asia region for almost 200 years, to acting on numerous 'firsts' across a range of industry and community issues, it is in our DNA to make a difference and help shape what our world looks like.

Over this time, we've grown in scale and reach, today offering clients a global network of 41 offices in 26 countries through our global alliance with Linklaters.

We are privileged to have some of the world's longest ongoing client relationships, stretching back more than 170 years, and we're committed to bringing our talent, expertise and insights to continue solving their toughest problems and creating ways forward to help them thrive. New and exciting market entrants sit alongside these established companies in our client base, drawn to working with us through the innovative repackaging of our services for the growing and fast-paced start-up market.

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- Livent on its proposed merger with Allkem to form a A\$15.7 billion global lithium chemicals producer;
- Sydney Airport in responding to the A\$23.6 billion takeover by the Sydney Aviation Alliance;
- AusNet on its A\$10.2 billion acquisition by Brookfield by scheme of arrangement;
- Morrison & Co and Brookfield led consortium on the A\$3.7 billion acquisition of Uniti Group;
- KKR Infrastructure, OTPP and PSP Investments on the A\$5.2 billion acquisition of Spark Infrastructure by way of inter-conditional creditor and trust schemes;
- Crown Resorts on its response to the A\$9 billion takeover proposal from Blackstone, the merger proposal from The Star and the US\$3 billion funding proposal from Oaktree Capital;
- CKHH as a shareholder in Vodafone Hutchison Australia in relation to the A\$15 billion merger with TPG Telecom;
- Investa Office Fund on its response to the competing A\$3.3 billion proposals from Oxford Properties and Blackstone Real Estate;
- Unibail-Rodamco's A\$32 billion acquisition of Westfield Corporation;
- DUET Group's A\$7.3 billion acquisition by the CKI consortium;
- the A\$9.05 billion acquisition of Asciano Limited;
- M2's A\$3 billion merger with Vocus to create the 4th largest telecommunications company in Australia;
- Novion's A\$10.5 billion acquisition by Vicinity Centres (formerly Federation Centres);
- Oil Search's successful defence against Woodside's A\$11.7 billion acquisition proposal;
- Foster's Group's response to the takeover by SABMiller for A\$12.3 billion;
- Rio Tinto's response to BHP Billiton's US\$192 billion takeover offer and its strategic alliance with Chinalco;
- St.George Bank's A\$67 billion merger with Westpac Banking Corporation; and
- Wesfarmers' A\$20 billion acquisition of Coles.

An aerial, high-angle photograph of a city street intersection at night. The scene is illuminated by streetlights, creating a blue and white color palette. A white text box is overlaid on the left side of the image, containing the title 'About this handbook' and a list of topics. The background shows a crosswalk with white stripes, a traffic light, and a person walking on the sidewalk. The numbers '222' and '60' are visible on the road surface.

About this handbook

This handbook provides an overview of:

- the rules which govern takeovers of, and acquisitions of voting securities in, Australian publicly listed companies and trusts;
- how to undertake or respond to a takeover proposal for an Australian publicly listed company or trust; and
- the legal issues which commonly arise in Australian takeover transactions.

This handbook should not be relied on as a substitute for obtaining legal or other professional advice. Should you require legal advice, please contact us.

This handbook is current as at February 2024.

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Australian takeovers in brief

1. Introduction

- Takeovers in Australia are regulated by a combination of legislation and regulatory policy.
- The takeovers rules apply to acquisitions of listed Australian companies, listed Australian managed investment schemes (being investment trusts), and unlisted Australian companies with more than 50 shareholders.
- The takeovers rules reflect policies that:
 - the acquisition of control of an entity which is subject to the takeovers rules takes place in an efficient, competitive and informed market;
 - target shareholders have a reasonable time to consider a proposed acquisition and are given enough information to enable them to assess the merits of the proposal; and
 - target shareholders have an equal opportunity to participate in the benefits of a change of control of a company (referred to as a control transaction).
- The most common takeover structures in Australia are: an off-market takeover bid (for either a friendly or hostile deal) and a scheme of arrangement (for a friendly deal only).

2. The 20% rule and key concepts

- A person cannot acquire a 'relevant interest' in voting securities of an entity that is subject to the takeovers rules if that would result in any person's 'voting power' exceeding 20%, except via a specified exception (such as a takeover bid or scheme of arrangement).
- The concept of 'relevant interest' is extremely broad, covering almost all situations where a person has direct or indirect control over the voting or disposal of a security.
- A person's 'voting power' in an entity is the aggregate of that person's 'relevant interests' in voting securities and the 'relevant interests' of that person's associates, expressed as a percentage of all issued voting securities.
- The concept of 'association' seeks to ascertain all persons who should be considered as belonging to a single securityholding bloc in relation to an entity. It covers all entities within the same corporate group, and persons who are deemed to be working together for the purpose of influencing the composition of the relevant entity's board of directors or its management, or working together in relation to the relevant entity's affairs.

3. Exceptions to the 20% rule

- There are various exceptions to the 20% rule.
- These exceptions include acquisitions of relevant interests: under a takeover bid, under a scheme of arrangement, with target securityholder approval, under a creep acquisition (ie. 3% every 6 months), under a downstream acquisition (ie. acquisitions of shares in listed entities which hold securities in a target), under a rights issue, or as a result of exercising a security interest.

4. Takeovers regulators

- The key takeovers regulators are the Australian Securities and Investments Commission (ASIC) and the Takeovers Panel.
- ASIC has general supervision of the Corporations Act including the takeovers rules, and has the power to modify and grant relief from the takeovers rules.
- The Takeovers Panel is the primary forum for resolving takeover disputes. It has the power to declare circumstances unacceptable (even if they do not involve a breach of law) and to make remedial orders.
- Neither ASIC nor the Takeovers Panel has the power to make upfront binding rulings on a proposed structure or proposed course of action.
- Courts play a very limited role in takeover transactions conducted via a takeover bid structure. However, courts play a vital role in takeover transactions conducted via a scheme of arrangement, in that a scheme requires court approval.

5. Shareholding thresholds

- The key shareholding thresholds in an ASX-listed Australian company from a Corporations Act perspective are: $\geq 5\%$ (obligation to file substantial holding notice), $> 10\%$ (ability to block compulsory acquisition), $> 20\%$ (takeovers threshold), $> 25\%$ (ability to block scheme of arrangement and special resolution), $> 50\%$ (ability to pass ordinary resolution), $\geq 75\%$ (ability to pass special resolution) and $\geq 90\%$ (entitlement to compulsory acquisition).

6. Transaction structures

- The most commonly used takeover structures are: an off-market takeover bid (for either a company or trust), a scheme of arrangement (for a company) and a trust scheme (for a trust).
- The majority of friendly deals are effected via a scheme of arrangement or trust scheme, largely because of their 'all-or-nothing' outcomes.
- Other, less commonly used takeover structures include: a selective capital reduction (for a company) and a securityholder-approved transaction (for a company or trust).

7. Takeover bids (for companies and trusts)

- A takeover bid can be used for either a friendly or hostile acquisition of a company or trust.
- A takeover bid involves the making of individual offers to purchase target securities at a specified bid price.
- There are 2 types of takeover bid: an off market bid and a market bid.
- Virtually all takeover bids are off-market bids because of the ability to include conditions.
- Takeover bids are subject to the following key rules that:
 - all offers must be the same;
 - the bid price cannot be lower than price which the bidder paid for a target security within the previous 4 months;
 - the offer period to be no less than 1 month and no more than 12 months;
 - there are no special deals for individual target securityholders;
 - there are no self-triggering bid conditions (for off-market bids);
 - the bidder must issue a 'bidder's statement' containing the offer terms and other information;
 - the target must issue a 'target's statement' containing the target board's recommendation; and
 - the bidder is entitled to compulsory acquisition if it obtains a relevant interest in at least 90% of the target securities (and has acquired at least 75% of the securities it offered to acquire).

8. Schemes of arrangement (for companies)

- A scheme of arrangement can be used only for a friendly acquisition of a company, and is frequently used to effect 100% acquisitions.
- A scheme of arrangement is a shareholder and court-approved statutory arrangement between a company and its shareholders that becomes binding on all shareholders by operation of law.
- Schemes are subject to fewer prescriptive rules than takeover bids and therefore can be more flexible, but are supervised by ASIC and the courts.
- A standard scheme involves:
 - a scheme implementation agreement between the bidder and the target;
 - the preparation by the target, with input from the bidder, of a draft 'scheme booklet' which is given to ASIC for review;
 - the target seeking court approval for the despatch of the scheme booklet to target shareholders and court orders for the convening of the shareholders' meeting to vote on the scheme (ie. the scheme meeting);
 - holding the scheme meeting;
 - the target seeking court approval for the implementation of the scheme;
 - implementing the scheme; and
 - de-listing the target from ASX.

9. Trust schemes (for trusts)

- A 'trust scheme' can be used only for a friendly acquisition of a trust, and is frequently used to effect 100% acquisitions.
 - A trust scheme resembles a company scheme of arrangement, but without the requirement for court approval.
 - Trust schemes are subject to fewer specific rules than takeover bids and are therefore more flexible, but the Takeovers Panel has oversight.
- A standard trust scheme involves:
 - an implementation agreement between the bidder and the target;
 - the preparation by the target, with input from the bidder, of a draft explanatory memorandum which is sent to ASIC for review before sending to unitholders in advance of the unitholders' meeting;
 - holding the unitholders' meeting;
 - lodging the amended trust constitution with ASIC;
 - implementing the trust scheme; and
 - de-listing the target from ASX.

10. Strategic considerations for a prospective acquirer

- Threshold matters for a prospective acquirer to consider include: transaction structure; whether it is seeking 100% or just control; form of offer consideration; due diligence requirements; friendly or hostile deal; and the potential acquisition of a pre-bid stake.
 - The initial approach to the target is usually conducted verbally, and followed by a written confidential, non-binding and indicative proposal. The target generally has no obligation to announce such a proposal - unless it ceases to become confidential – but could decide to do so for strategic reasons.
 - If a target grants due diligence access it will usually only do so on the basis of a confidentiality agreement, which restricts the use of that information to implement a friendly transaction.
- The target may also require a 'standstill agreement' whereby the prospective acquirer cannot acquire target securities for a specified period except under a friendly transaction.
- A prospective acquirer can seek to bolster its position by acquiring a pre-bid stake (subject to the 20% takeovers rule, insider trading rules, any need for secrecy and other considerations).
 - If the target is not receptive to an approach, a prospective acquirer can launch a hostile takeover bid, make a 'bear hug' announcement or initiate a board spill.

11. Strategic considerations for a target

- The directors of an Australian company (or responsible entity of an Australian trust) will, given their fiduciary duties, usually seek to maximise shareholder value and, to that end, will usually consider the reasonableness of any takeover proposal.
- The overriding principles are that: (i) the directors of an ASX-listed Australian company (and responsible entity of a trust) must at all times act bona fide in the interests of the company (or trust unitholders), and for a proper purpose; and (ii) in respect of a takeover bid, target directors should not take actions, without securityholder approval, which causes the defeat of a control proposal.
- A board can prepare for a possible takeover approach by: preparing a takeover defence manual and undertaking other pre-approach tasks, such as monitoring the share register, maintaining a valuation of itself, preparing for the grant of due diligence to a bidder, and preparing draft ASX announcements.
- Key immediate decisions for a target following receipt of a takeover proposal are whether to: make an ASX announcement and engage with the bidder.
- If the target board concludes a takeover proposal to not be in the interests of shareholders, it should consider an appropriate defence strategy. This could involve seeking counter-bidders or establishing the inadequacy of the bidder's proposal.

12. Other takeovers issues

Other takeovers issues which commonly arise or need consideration include:

- whether foreign investment approval is required;
- whether competition clearance is required;
- ASIC's truth in takeovers policy which requires persons to be bound by their public statements in relation to a takeover; and
- the acquisition or cancellation of target options and other convertible securities.



Introduction

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- The takeovers rules reflect policies that:
 - the acquisition of control of an entity which is subject to the takeovers rules takes place in an efficient, competitive and informed market;
 - target shareholders have a reasonable time to consider a proposed acquisition and are given enough information to enable them to assess the merits of the proposal; and
 - target shareholders have an equal opportunity to participate in the benefits of a change of control of a company (referred to as a control transaction).
- The most common takeover structures in Australia are: an off-market takeover bid (for either a friendly or hostile deal) and a scheme of arrangement (for a friendly deal only).

1.1 What is a takeover?

In Australia, the term 'takeover' is often used to refer generically to the acquisition of control of a publicly listed company. Usually that control is obtained upon ownership of more than half of a company's voting shares. However, in some cases, control can be obtained at a lower shareholding interest if, as a practical matter, a person can determine the composition of a company's board of directors.

Sometimes, the term 'merger' is used in lieu of 'takeover'. In Australia the term 'merger' is more a commercial concept than a legal one, often to describe an agreed acquisition of one company by another where the two companies are of similar sizes. Unlike other jurisdictions (such as the United States), there is no practice in Australia to effect control transactions via a true merger which results in the target company being subsumed into the bidder company and the target company ceasing to exist.

Control transactions in Australia most commonly involve a bidder acquiring all (or at least a majority) of the voting securities in the target, and the target becoming a subsidiary of the bidder.

1.2 Regulatory framework

Takeovers in Australia are regulated by a combination of:

- **legislation:** Part 5.1 and Chapter 6 of the *Corporations Act 2001* (Cth);
- **governmental policy:** policy developed by the Australian Securities and Investments Commission (ASIC) (the national companies regulator) and the Takeovers Panel (a specialist tribunal which resolves takeover disputes); and
- **stock exchange rules:** to a lesser extent, the listing rules of the ASX.

In addition, Australia has:

- anti-trust rules set out in the *Competition and Consumer Act 2010* (Cth) which are administered by the Australian Competition and Consumer Commission;

- foreign investment rules set out in the *Foreign Acquisitions and Takeovers Act 1975* (Cth) and the accompanying regulations, where proposed acquisitions requiring approval are examined by the Australian Foreign Investment Review Board (FIRB); and
- other rules specific to an industry (such as banking, broadcasting, aviation and gaming) which may regulate control transactions.

The focus of this handbook, however, is on the takeovers rules in the Corporations Act.

1.3 What entities are governed by the takeovers rules?

The acquisition of interests in voting securities issued by the following types of entities need to comply with the Australian takeovers rules:

- all Australian-incorporated companies listed on the ASX or on another prescribed financial market operated in Australia;
- all unlisted Australian-incorporated companies with more than 50 shareholders; and
- all Australian-registered managed investment schemes listed on the ASX or on another prescribed financial market operated in Australia (these are normally listed unit trusts).

The other prescribed financial markets are Chi-X, SSX and NSX. The overwhelming majority of entities listed in Australia are listed on the ASX. For this reason, and for simplicity, the remainder of this handbook refers only to ASX-listed entities.

The takeovers rules can also regulate the acquisition of voting securities in entities (whether incorporated in Australia or elsewhere) that hold or have interests in the voting securities of an entity of a type mentioned above.

All persons, whether or not resident in Australia, must comply with the takeovers rules.

1.4 Fundamental principles

The takeovers rules and policies are founded on the following fundamental principles (set out at the beginning of Chapter 6 of the Corporations Act):

- the acquisition of control of a relevant entity (being one of the types of entities described above) takes place in an efficient, competitive and informed market;
- the security holders and directors of a relevant entity:
 - know the identity of any person who proposes to acquire a substantial interest in entity;
 - have a reasonable time to consider the proposal; and
 - are given enough information to assess the merits of the proposal;
- as far as practicable, the entity's securityholders should all have a reasonable and equal opportunity to participate in any benefits accruing to the entity's securityholders through the proposal; and
- an appropriate procedure is followed as a preliminary to compulsory acquisition of the entity's securities under the Corporations Act.

1.5 Transaction structures

A control transaction for an ASX-listed Australian company or trust can be effected through one of various takeover structures, either on a friendly or hostile basis. A friendly deal is one that is supported by the target board of directors.

The most common takeover structures are the **off-market takeover bid** (for either a friendly or hostile deal) and the **scheme of arrangement** (for a friendly deal only). These structures are discussed in this handbook.

The 20% rule and key concepts

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- A person cannot acquire a 'relevant interest' in voting securities of an entity that is subject to the takeovers rules if that would result in any person's 'voting power' exceeding 20%, except via a specified exception (such as a takeover bid or scheme of arrangement).
- The concept of 'relevant interest' is extremely broad, covering almost all situations where a person has direct or indirect control over the voting or disposal of a security.
- A person's 'voting power' in an entity is the aggregate of that person's 'relevant interests' in voting securities and the 'relevant interests' of that person's associates, expressed as a percentage of all issued voting securities.
- The concept of 'association' seeks to ascertain all persons who should be considered as belonging to a single security holding bloc in relation to an entity. It covers all entities within the same corporate group, and persons who are deemed to be working together for the purpose of influencing the composition of the relevant entity's board of directors or its management, or working together in relation to the relevant entity's affairs.

2.1 The 20% rule

The basic takeover rule is that a person cannot acquire a 'relevant interest' in issued voting shares of an Australian-incorporated company listed on the ASX (or issued voting shares of an unlisted Australian-incorporated company with more than 50 shareholders, or issued voting interests in an Australian-registered managed investment scheme listed on the ASX) through a transaction in relation to securities entered into by or on behalf of the person if, because of that acquisition, that person's or someone else's 'voting power' in the relevant entity:

- increases from 20% or below to more than 20%; or
- increases from a starting point that is above 20% and below 90%, unless the acquisition occurs via a specified exception (such as a takeover bid, scheme of arrangement or with target shareholder approval).

This is commonly known as the '20% rule' or '20% takeovers threshold'. At a basic level, the 20% rule means that a person is limited to holding a 20% shareholding interest in an ASX-listed company and cannot move beyond that except via a specified exception.

2.2 Key concepts

The key concepts for the purposes of the 20% rule and the takeovers regime generally are:

- relevant interest;
- association; and
- voting power.

2.3 Relevant interest

As explained below, there are five different ways in which a person will have a relevant interest in voting shares in a company or voting interests in a managed investment scheme (ie. trust). More than one person can have a relevant interest in the same parcel of shares at the same time. For simplicity, the term 'shares' rather than voting shares or managed investment scheme interests is used below.

(a) Registered holder

A person who is the registered holder of shares will have a relevant interest in those shares, unless the person holds the shares as a 'bare trustee' for the beneficial holder (ie. the person can only deal with or vote the shares upon the beneficial holder's instructions). Often a professional custodian or nominee holder will be considered a 'bare trustee'.

(b) Control over voting

A person who is not the registered holder of shares but nevertheless has the power to exercise, or control the exercise of, a right to vote attached to the shares will also have a relevant interest in those shares. The references to power and control are to be read broadly, and include power or control that: is indirect, or is express or implied, or is formal or informal, or can be exercised as a result of an agreement or practice (whether or not legally enforceable), or can be made subject to restraint or restriction.

For instance, where a registered holder of shares has conferred on another person the right to decide how to vote the shares, whether on a single resolution or for a specified period or otherwise, the other person will have a relevant interest in the shares for so long as that right exists. Also, an arrangement or practice whereby a person other than the registered holder of shares can determine how the shares are voted will give that person a relevant interest in the shares.

However, there is an exception for proxy appointees – a person who is appointed by a registered holder of shares to vote as a proxy at a single meeting of shareholders and has not been provided any valuable consideration for that appointment will not be taken to have a relevant interest in the shares.

(c) Control over disposal

A person who is not the registered holder of shares but has the power to dispose, or control the exercise of, a power to dispose of the shares will have a relevant interest in those shares. The references to power and control are to be read broadly, and includes power or control that: is indirect, or is express or implied, or is formal or informal, or can

be exercised as a result of an agreement or practice (whether or not legally enforceable), or can be made subject to restraint or restriction.

There are various situations in which a person other than the registered holder will be taken to have control over the disposal of shares. These include, for instance:

- where the person has contracted to purchase shares but completion has yet to occur;
- where the person's consent is required for disposal of the shares; and
- where the person has a pre-emptive or other right to purchase the shares before they can be offered for sale to a third party.

There are various situations in which a person who is taken to have control over the disposal of shares will *not* be treated as having a relevant interest in the shares. These include:

- where a person has taken security interests over the shares in the ordinary course of the person's business of the provision of financial accommodation (commonly known as the 'moneylender exemption');
- where the person holds exchange-traded derivatives over shares (prior to the obligation to make or take delivery of the shares arising);
- where the person has the benefit of pre-emptive rights on the transfer of shares and those rights are contained in a company constitution where all shareholders have pre-emptive rights on the same terms; and
- where the person has entered into an agreement (eg to purchase shares) that is conditional upon target shareholder approval or an ASIC exemption.

(d) Accelerated relevant interests

A person will be taken to have a relevant interest in issued shares if:

- the person has entered into an agreement with another person with respect to the shares and would have a relevant interest in the shares if the agreement were performed (eg entry into a share purchase agreement confers on the purchaser a

relevant interest in the shares even if completion occurs at a later date);

- another person has given or gives the person an enforceable right in relation to the shares – whether the right is enforceable now or in the future and whether or not on the fulfilment of a condition – and the person would have a relevant interest in the shares if the right is enforced (eg if a person is given a right to exercise votes attached to shares but that right only arises upon the satisfaction of a certain condition, the person immediately obtains a relevant interest in the shares and not only if and when the voting right actually arises); or
- another person has granted or grants an option to, or has been or is granted an option by, the person with respect to shares (in other words all parties to a call option or put option arrangement in respect of shares are taken to immediately have a relevant interest in the shares, to the extent they do not have a pre-existing relevant interest, upon the creation of the option).

(e) Deemed relevant interests through corporate groups

There are broad tracing provisions whereby each entity within a corporate group (ie. the parent and all of its controlled entities) is deemed to have a relevant interest in any shares in which any group entity has a relevant interest.

Specifically, a person is deemed to have a relevant interest in any shares that any of the following has:

- a body corporate, or managed investment scheme, in which the person's 'voting power' is above 20% (the '20% deeming rule'); and
- a body corporate, or managed investment scheme, that the person controls (the 'control deeming rule').

The 20% deeming rule can apply only once in a chain of entities, whereas the control deeming rule can be applied multiple times in a chain. The rules can result in a person breaching the basic 20% threshold with respect to an ASX-listed company via upstream acquisitions (eg acquisitions of shares in a company which either holds shares in the ASX-listed company or which holds shares in a company which holds shares in the ASX-listed company).

2.4 Voting power

A person's 'voting power' in a company or managed investment scheme is calculated by aggregating:

- the relevant interests which the person holds in the entity's voting shares or voting interests; and
- the relevant interests which the person's 'associates' hold in the entity's voting shares or voting interests,

and expressing the result as a percentage of all voting shares or voting interests on issue.

2.5 Association

The concept of 'association' in the Corporations Act seeks to ascertain all persons who should be considered as belonging to a single securityholding bloc in relation to a company or managed investment scheme. It is possible for a person to be associated with another person even if they do not also acquire a relevant interest in each other's shares.

Two or more persons will be considered 'associates' in relation to a company or managed investment scheme where:

- they are companies belonging to the same corporate group;
- they have entered into a 'relevant agreement' (being an agreement, arrangement or understanding) for the purpose of controlling or influencing the composition of the board of the company or of the entity which is the responsible entity of the managed investment scheme or the conduct of the company's or managed investment scheme's affairs (where 'affairs' is broadly defined to include an entity's business operations, internal management and the exercise of voting rights attached to its securities) – this is known as the 'relevant agreement' test; or
- they are 'acting or proposing to act in concert' (ie. with a common purpose and a meeting of the minds) in relation to the company's or managed investment scheme's affairs (where 'affairs' is broadly defined to include an entity's business operations, internal management and the exercise of voting rights attached to its securities) – this is known as the 'acting in concert' test.

There is significant overlap between the 'relevant agreement' and 'acting in concert' tests.

2.6 Practical application of the 20% rule

The 20% rule is not breached merely because a person's voting power has exceeded 20%. For instance, if person A holds 18% of a company's voting shares and becomes associated with person B (otherwise unrelated to and not associated with person A) who holds 10%, each of person A and person B will have voting power of 28% in the company. However, if neither A nor B has a relevant interest in each other's shares, there is no breach of the 20% rule. This is because the rule only applies where there is an acquisition of a relevant interest which results in a person's voting power exceeding 20%.

This means that merely forming an association which results in a person's voting power increasing beyond the 20% threshold is itself not unlawful. However, in practice, there is a fine line between association and relevant interest. Also, any person who has voting power of 5% or more needs to publicly disclose that fact within two business days via the filing of a substantial holding with the ASX and the relevant entity, which must disclose how the voting power (relevant interest and/or association) arose.

As a final point, the 20% rule will apply to the acquisitions of relevant interests between associates. Using the above example, each of persons A and B will have voting power of 28% as a result of their association. If A sought to acquire B's 10% stake its voting power will not increase but in that circumstance the takeovers rules operate to disregard the association for the purposes of the 20% rule. Therefore A could not acquire B's stake except via a specified exception to the 20% rule.

Exceptions to the 20% rule

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- There are various exceptions to the 20% rule.
- These exceptions include acquisitions of relevant interests: under a takeover bid, under a scheme of arrangement, with target securityholder approval, under a creep acquisition (ie. 3% every 6 months), under a downstream acquisition (ie. acquisitions of shares in listed entities which hold securities in a target), under a rights issue, or as a result of exercising a security interest.

The 20% rule operates as a limit on how much a person can acquire in an ASX-listed company or trust. Moving beyond that threshold can only be done through one of a number of specified exceptions. Unlike other jurisdictions, there is no 'mandatory bid' concept in the Australian rules that allows a person to acquire a securityholding

or other relevant interest of more than 20% on the basis that a follow-on general offer is made to all target securityholders.

The following acquisitions of relevant interests in voting securities are exempted from the 20% rule.

Takeover bid

Acquisition arising from acceptance of a takeover bid in accordance with Chapter 6 of the Corporations Act. This is discussed further in section 7. (Acquisitions on-market during a takeover bid are also permitted in limited circumstances.)

Scheme of arrangement

Acquisition arising from a court-approved scheme of arrangement. This is discussed further in section 8.

Securityholder approval

Acquisition approved by an ordinary resolution of securityholders of the relevant entity. The following persons cannot vote in favour of the resolution: the acquirer, the acquirer's associates, the 'sellers' and the sellers' associates. This exception cannot (without ASIC relief) be used to acquire 100% of an entity because all target securityholders would be excluded from voting in favour of the resolution. The exception is more commonly used for new security issuances (ie. where new funds are injected into the entity), rather than to transfer existing securities which normally does not provide any direct benefit to securityholders other than the seller.

Creep acquisition

Acquisitions of up to 3% every 6 months from a starting point above 19%. Note that a person who has acquired more than 20% under another exception must wait 6 months before it can make acquisitions under this exception.

Downstream acquisition

Acquisition resulting from the acquisition of securities in an 'upstream' entity (ie. one which is listed on the ASX or on a specified foreign exchange) which itself has a relevant interest in a 'downstream' ASX-listed company or trust.

However, a downstream acquisition may be considered unacceptable by the Takeovers Panel where control of the downstream company appears to be a significant purpose of the upstream acquisition (eg if the shares in the downstream company comprise over 50% of the upstream company's assets).

Rights issue

Acquisition resulting from pro-rata rights issues to securityholders. This exception extends to underwriters of such rights issues. However, a purported reliance on the rights issue exception may be found unacceptable by the Takeovers Panel where the control effect of a rights issue exceeds what is reasonably necessary to raise funds.

Security interest

Acquisition resulting from enforcement of security interest taken over securities in the ordinary course of the acquirer's ordinary course of business of the provision of financial accommodation.

An aerial photograph of a valley. The top half shows a dense green forest on a hillside. Below the forest is a wide, green grassy field. A river with clear, turquoise water flows through the valley, winding between sandy banks. The bottom half of the image shows more of the river and its meandering path through the valley.

Takeovers regulators

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- The key takeovers regulators are the Australian Securities and Investments Commission (ASIC) and the Takeovers Panel.
- ASIC has general supervision of the Corporations Act including the takeovers rules, and has the power to modify and grant relief from the takeovers rules.
- The Takeovers Panel is the forum for resolving takeover disputes. It has the power to declare circumstances unacceptable (even if they do not involve a breach of law) and to make remedial orders.
- Neither ASIC nor the Takeovers Panel has the power to make upfront binding rulings on a proposed structure or proposed course of action.
- Courts play a very limited role in takeover transactions conducted via a takeover bid structure. However, courts play a vital role in takeover transactions conducted via a scheme of arrangement, in that a scheme requires court approval.

4.1 Introduction

The takeovers rules in the Corporations Act are administered by ASIC, with takeover disputes largely being determined by the Takeovers Panel (other than in the context of schemes of arrangement once they become subject to the court's scrutiny). In the case of acquisitions of an ASX-listed entity, the rules of the ASX also become relevant. The court has a central role in considering and approving schemes of arrangement, but otherwise has a limited role in takeovers.

Other bodies also have a role in regulating control transactions, depending on the circumstances. These include the Australian Competition and Consumer Commission in respect of competition matters, and the Foreign Investment Review Board in respect of foreign investment approval matters.

4.2 ASIC

ASIC is a government body which has general supervision of all aspects of the Corporations Act including takeovers. ASIC is invested with broad facilitative, regulatory and enforcement powers including (insofar as they relate to takeovers):

- to modify and grant relief from provisions of the takeovers rules in the Corporations Act, which ASIC can do (and has previously done) through legislative instruments (previously called 'class orders') which apply widely or through transaction-specific modification and relief instruments;
- to review 'scheme booklets' to be sent to target shareholders in a company scheme of arrangement before such booklets can be submitted to the court for approval to despatch to shareholders;
- to make submissions to the court in respect of a scheme of arrangement and, where it considers it appropriate, to issue a no-objection statement;
- to apply to the Takeovers Panel for declarations of unacceptable circumstances and remedial orders, and to make submissions on applications made by others;
- to investigate suspected breaches of the law and in so doing require people to produce books or answer questions; and

- to seek civil penalties from the courts and to commence certain prosecutions.

As part of its supervisory role ASIC has a practice of reviewing takeover and takeover-related documents (such as ASX announcements, bidder's statements and target's statements) and, if a document appears to raise a legal or policy issue, making informal enquiries of the relevant persons. These enquiries can be a precursor to a formal investigation.

It must be noted that, other than making decisions about applications for modifications of or relief from the takeovers rules, ASIC does not (and does not have the power to) provide upfront binding rulings on whether a proposed course of action will comply the takeovers rules. Nor is ASIC a forum for resolving takeover disputes – that role is performed by the Takeovers Panel.

4.3 Takeovers Panel

The Takeovers Panel is a specialist tribunal for resolving takeover disputes. It has near-exclusive jurisdiction to hear disputes in relation to a takeover bid, and broad non-exclusive jurisdiction in relation to control transactions and acquisitions of voting securities that do not involve a takeover bid. It also has jurisdiction to hear matters relating to a proposed scheme of arrangement before the courts are involved.

The Panel's objective is to determine takeover disputes in an efficient manner by focusing on commercial and policy issues rather than technical legal points. To this end, the Panel comprises part-time members appointed by the government from the ranks of public company directors, senior investment bankers, academics and lawyers. Each application to the Panel is heard by a sitting Panel of three of those members. The Panel is supported by a full-time executive team.

The Panel's primary power is to declare circumstances unacceptable in relation to a takeover bid for, or the control of, an Australian publicly listed company or trust. The Panel can make such a declaration if it appears to the Panel that the circumstances:

- are unacceptable having regard to the effect that the Panel is satisfied that the circumstances have had, are having, will have or are likely to have on:

- the control or potential control of a listed company or listed managed investment scheme; or
- the acquisition or proposed acquisition of a substantial interest in a listed company;
- are otherwise unacceptable having regard to the purposes of the takeovers rules (ie. the fundamental principles in section 1.4); or
- are unacceptable because they constitute or are likely to constitute a breach of the black letter takeover rules or the provisions relating to substantial shareholding notices or tracing provisions,

and after having regard to the public interest.

If the Panel makes a declaration of unacceptable circumstances, it has very broad powers to make orders to protect the rights of persons (especially target security holders) and to ensure that a takeover bid proceeds (as far as possible) in a way that it would have proceeded if the unacceptable circumstances had not occurred. This includes divestment orders and orders affecting the rights of third parties.

As with a court, the Panel cannot act of its own accord. It can only make a declaration of unacceptable circumstances in response to an application brought by ASIC or an interested party (eg a target entity, target securityholder, or a competing bidder).

However, the similarities to a court end there. Unlike a court, the Panel does not make decisions on the basis of black letter takeovers rules. The Panel is required to, and in practice does, take a purposive approach to the takeovers rules – the upshot being that structures and courses of action which technically avoid the operation of any takeover rule but which may be inconsistent with the fundamental takeovers principles are at risk of being struck down by the Panel. Also, unlike a court the Panel is not bound by rules of evidence, thereby giving the Panel greater flexibility in determining what information it can take into consideration when ruling on an application. Further, unlike a court, virtually all Panel cases are conducted by written submissions and involve a fairly short timetable.

The Panel also has the power to review ASIC decisions whether to grant modifications of or relief from the takeovers rules. This power is not commonly exercised,

as relatively few applications for such review have been made to date.

The Panel has published a number of guidance notes which discuss the policy the Panel considers relevant in control transactions. Prior Panel decisions (roughly 15-35 each year since the Panel was established in 2000) are also a useful source of guidance. However, it must be noted that, unlike the London Takeover Panel, the Australian Takeovers Panel does not (and does not have the power to) provide upfront binding rulings on whether a proposed course of action complies with the takeovers rules or is immune from a declaration of unacceptable circumstances.

4.4 ASX

The ASX does not specifically regulate the manner in which takeovers are conducted, aside from settlement rules regarding the electronic processing of takeover bid acceptances and other rules relating to reporting of information and restrictions on security issuances by a target entity following a takeover bid being announced. In addition, the ASX is normally involved in approving securities trading arrangements to facilitate the implementation of a scheme of arrangement.

In respect of a takeover, the ASX's focus is to ensure that ASX-listed entities comply with the ASX Listing Rules, particularly the continuous disclosure obligations. In short, each ASX-listed entity is obliged to disclose all price-sensitive information once it becomes aware of that information, unless the information falls within a limited exception. ASX-listed entities who are the subject of a confidential takeover approach need to be particularly mindful of their continuous disclosure obligations.

4.5 The courts

Given the Takeovers Panel's near-exclusive jurisdiction to hear disputes in relation to takeover bids, courts play a very limited role in takeover transactions conducted via a takeover bid structure. In contrast, courts play a vital role in takeover transactions conducted via a scheme of arrangement structure – namely to order the convening of the scheme meeting and to confirm the scheme once approved by target shareholders (which is required for implementation of the scheme).

Shareholding thresholds

5

- The key shareholding thresholds in an ASX-listed Australian company from a Corporations Act perspective are: $\geq 5\%$ (obligation to file substantial holding notice), $> 10\%$ (ability to block compulsory acquisition), $> 20\%$ (takeovers threshold), $> 25\%$ (ability to block scheme of arrangement and special resolution), $> 50\%$ (ability to pass ordinary resolution), $\geq 75\%$ (ability to pass special resolution) and $\geq 90\%$ (entitlement to compulsory acquisition).

Below is a sample of other takeovers issues which commonly arise or need to be considered. This is by no means an exhaustive list.

The following table identifies the key shareholding thresholds in an ASX-listed company from a Corporations Act perspective¹. For simplicity the table focuses on companies only (but the same principles apply to the acquisition of interests in listed managed investment schemes).

Percentage (%) of issued shares	Implications
≥5%	<p>Substantial holding notice</p> <p>A person who obtains voting power in 5% or more of an ASX-listed company is required to publicly disclose that fact within 2 business days via the filing of a substantial holding notice. A person's voting power consists of their own 'relevant interest' in shares plus the relevant interests of their associates. A further notice needs to be filed within 2 business days after each subsequent voting power change of 1 percentage point or more, and after the person ceases to have voting power of 5% or more.</p> <p>The notice must attach all documents which contributed to the voting power the person obtained, or provide a written description of arrangements which are not in writing.</p>
>10%	<p>Blocking of compulsory acquisition</p> <p>A person who has a greater than 10% shareholding interest in an ASX-listed company will be able to prevent a majority shareholder from moving to 100% ownership through compulsory acquisition, because the compulsory acquisition threshold is set at 90%.</p>
>20%	<p>Takeovers threshold</p> <p>A person cannot acquire a 'relevant interest' in a company's shares if it would result in that person's or someone else's 'voting power' in the company increasing from 20% or below to more than 20%, or increasing from a starting point that is above 20% and below 90%, unless the acquisition occurs via a specified exception (such as a takeover bid, scheme of arrangement or with target shareholder approval).</p>
>25%	<p>Blocking of scheme of arrangement</p> <p>A person who owns or has voting control over 25% or more of a company's shares can unilaterally block the approval of a takeover conducted by a scheme of arrangement, because one of the scheme voting thresholds is approval by at least 75% of the votes cast on the scheme resolution. (In practice, a person can normally block a scheme with less than a 25% interest given voter turnout at scheme meetings is often substantially lower than 100%.)</p> <p>Blocking of special resolutions</p> <p>A person who owns or has voting control over 25% or more of a company's shares can unilaterally block the approval of a special resolution (see below regarding 'special resolution'), because it requires approval by at least 75% of the votes cast on the resolution. (In practice, a person can normally block a special resolution with less than a 25% interest given voter turnout at company meetings is often substantially lower than 100%.)</p>

¹ Shareholding thresholds which trigger foreign investment approvals are outlined in section 12.1. There are also various industry and entity-specific laws which impose separate ownership rules, eg *Financial Sector (Shareholdings) Act 1998* (Cth), *Air Navigation Act 1920* (Cth), *Qantas Sale Act 1992* (Cth), *Airports Act 1996* (Cth) and *Telstra Corporation Act 1991* (Cth).

Percentage (%) of issued shares	Implications
>50%	<p>Passage of ordinary resolutions</p> <p>A person who owns or has voting control over more than 50% of a company's shares can unilaterally pass an ordinary resolution, because it requires approval by a majority of votes cast. Importantly, directors can be appointed and removed by shareholders by ordinary resolution. (In practice, a person can normally pass an ordinary resolution on their own with less than a 50% interest given voter turnout at company meetings is often substantially lower than 100%.)</p> <p>(Note: where there remain minority shareholders in a company, the company's directors cannot favour the controlling shareholder over the others because the directors have a duty to consider the interests of the company as a whole. Further, related party dealings that require shareholder approval will likely need to be approved by the minority shareholders alone, with the controlling shareholder(s) excluded from voting.)</p>
≥75%	<p>Passage of special resolutions</p> <p>A person who owns or has voting control over 75% or more of a company's shares can unilaterally pass a special resolution, because it requires approval by at least 75% of the votes cast. Under the Corporations Act, certain matters need to be passed by a special resolution of shareholders, eg amendments to the constitution, change of company name, change of company type, selective reduction of capital, selective buy-back of shares and winding-up. (In practice, a person can normally pass a special resolution on their own with less than a 75% interest given voter turnout at company meetings is often substantially lower than 100%.)</p> <p>(Note: where there remain minority shareholders in a company, the company's directors cannot favour the controlling shareholder over the others because the directors have a duty to consider the interests of the company as a whole. Further, related party dealings that require shareholder approval will likely need to be approved by the minority shareholders alone, with the controlling shareholder(s) excluded from voting.)</p>
≥90%	<p>Entitlement to compulsory acquisition</p> <p>Generally speaking, where a person owns 90% or more of a company's shares they can compulsorily acquire the remainder.</p>

An aerial topographic map of a mountainous region, showing a winding river and various terrain features. The colors range from dark blue in the valleys to brown and tan on the higher elevations.

Transaction structures

6

- The most commonly used takeover structures are: an off-market takeover bid (for either a company or trust), a scheme of arrangement (for a company) and a trust scheme (for a trust).
- The majority of friendly deals are effected via a scheme of arrangement or trust scheme, largely because of their 'all-or-nothing' outcomes.
- Other, less commonly used takeover structures include: a selective capital reduction (for a company) and a securityholder-approved transaction (for a company or trust).

6.1 Commonly used structures

By far the most common structures which are used to acquire control of an ASX-listed company or trust are:

- an **off-market takeover bid**, in the case of either a company or trust (discussed in section 7);
- a **scheme of arrangement**, in the case of a company (discussed in section 8); and
- a **trust scheme**, in the case of a trust (discussed in section 9).

An off-market takeover bid can be used for either a friendly or hostile deal, whereas a scheme of arrangement and trust scheme can only be used in a friendly deal. A friendly deal is one that has the support of the target's board of directors. In Australia the majority of friendly deals are effected via a scheme of arrangement or trust scheme, rather than a takeover bid, largely because of its 'all-or-nothing' outcome. If the relevant scheme is approved, the bidder will acquire 100% of the target but, if it is not approved, the bidder will not acquire any target securities. In contrast, under a takeover bid, the bidder can only be certain of obtaining 100% if it reaches the 90% compulsory acquisition threshold, but to get to that stage it is usually necessary to declare the bid unconditional first.

A number of ASX-listed entities (predominantly in the property trust sector) trade as stapled entity structures. These structures comprise one or more entities which are run as a combined economic unit and the securities of which are quoted jointly. Such securities are known as 'stapled securities'. The common form of stapled entity structure consists of a company and a unit trust, where each share issued by the company is stapled to each unit issued by the trust such that they cannot be traded separately – hence the term stapled security. Other forms of stapled structures which are currently (or have previously been) listed on the ASX include two or more unit trusts, and two or more unit trusts plus a company.

A person seeking to acquire control of a stapled entity structure needs to acquire all entities within the structure. This can be achieved via simultaneous and inter-conditional takeover bids for all entities within the stapled structure, or simultaneous and inter-conditional scheme(s) of arrangement and/or trust scheme(s). It is not feasible to make a simultaneous takeover bid for one entity within a structure, and to propose a scheme of arrangement or trust scheme for another.

6.2 Bid vs scheme structure

The following table contains an overview of the differences between an off-market takeover bid and a scheme of arrangement as the structure for acquiring 100% of the shares in an ASX-listed Australian company. For simplicity, the table looks only at company targets (rather than trust targets as well). The table does not canvass all the differences between the bid and scheme structures, but focuses on those which are likely to be decisive in choosing between the two approaches. It does not address taxation or accounting differences.

	Off-market takeover bid	Scheme of arrangement
Character	<p>Bidder's initiative and control, subject to the terms of any bid implementation agreement with the target.</p> <p>Written offer by bidder to purchase all shares held by target shareholders.</p> <p>Can be conditional (ie. to produce an ALL OR NOTHING result), or unconditional to get as many target shares as bidder can, then subsequently seek to move to compulsory acquisition thresholds.</p>	<p>Target's initiative and control, subject to the terms of a scheme implementation agreement with the bidder.</p> <p>Target shareholder-approved and court-approved arrangement between target and its shareholders to either transfer shares to bidder in exchange for specified consideration or have their shares cancelled in exchange for specified consideration.</p> <p>ALL OR NOTHING proposition: compulsory acquisition irrelevant.</p>
Threshold	<p>Compulsory acquisition requires:</p> <ul style="list-style-type: none"> • 90% relevant interest in target shares; <u>and</u> • acquisitions of 75% of non bidder-held shares by close of bid. <p>Assuming that bidder commences with no target shares, 90% relevant interest test is the only relevant threshold.</p> <p>Inaction (eg dead and lost shareholders) = Rejection</p>	<p>Approval by a vote of shareholders by at least:</p> <ul style="list-style-type: none"> • 75% of votes cast; <u>and</u> • a majority by number of all target shareholders present and voting (in person or by proxy). <p>Bidder is usually treated as a separate class, assuming it owns target shares. Court has discretion to waive the majority by number test.</p> <p>Inaction = Acquiescence (ie less support required at shareholder meeting)</p> <p>A scheme involves a lower target shareholder 'approval' threshold than a takeover bid, because of the 75% voting requirement versus the 90% compulsory acquisition threshold plus the fact that voter turnout at a scheme meeting is often substantially less than 100%.</p>
Role of regulators and court	<p>No court involvement unless a challenge to bid by ASIC. All other challenges to Takeovers Panel, not courts. ASIC has no formal review role.</p>	<p>Two court hearings: first, to order the convening of the target shareholder meeting and to approve despatch of the scheme booklet; and second, to approve the scheme itself after the shareholder meeting.</p> <p>ASIC has formal review role and is required to confirm to court whether it has any objections to scheme.</p>

	Off-market takeover bid	Scheme of arrangement
Disclosure	<p>Bidder prepares the offer document called a Bidder's Statement, which includes offer terms, funding sources, intentions for target and all other information known to bidder which is material to target shareholders.</p> <p>Target responds with a Target's Statement which contains the target directors' recommendation and all information known to the directors which target shareholders would reasonably require to make an informed assessment whether or not to accept the takeover offer.</p>	<p>Target prepares scheme booklet (with notice of court-ordered meeting): must contain certain prescribed information. ASIC demands same level of disclosure as a Bidder's Statement and Target's Statement combined.</p>
Conditions	<p>Bid may be subject to conditions, though there are restrictions on what conditions can be imposed (eg a condition cannot be within bidder's control). Typical conditions include minimum acceptance condition (eg 90% compulsory acquisition threshold), no material target transactions, no 'prescribed occurrences' in relation to the target, and receipt of regulatory approvals.</p>	<p>Courts are reluctant to approve schemes that are conditional. However, it is permissible and usual for a scheme implementation agreement between a bidder and target to be subject to conditions that must be satisfied or waived before the scheme is approved by the court.</p>
Expert's report	<p>Target's Statement only required to include independent expert's report if bidder has 30% or more of target shares, or bidder and target have one or more common directors.</p>	<p>Independent expert's report practically always included in scheme booklet, and ASIC and the court expects inclusion of report.</p>
Different treatment among holders	<p>All target shareholders must be treated equally.</p>	<p>Target shareholders can be treated differently if this is disclosed, though this could create separate shareholder classes requiring separate votes.</p>
Flexibility of structure	<p>Less flexible than a scheme in that related transactions cannot be incorporated, and that the offer can be varied only to increase offer price and/or extend offer period. However, increase to offer price or extension of offer period is a straightforward process.</p>	<p>More flexible than a takeover bid in that related transactions can be incorporated, and deal can be varied in any manner. However, any variation following despatch of shareholder documents normally requires court approval.</p>
Timing	<p>Minimum of about two to three months.</p>	<p>Minimum of about two to three months.</p>

6.3 Other structures

There are a number of alternative structures by which a person can obtain control of an ASX-listed Australian company or trust. These include the following.

(a) Selective capital reduction (for a company only)

This structure can be used to enable a person to acquire 100% of a company's shares. It involves a reduction of the target company's share capital through the cancellation of all issued shares other than those held by the 'bidder', in exchange for consideration from the company that is usually funded by the bidder. The transaction requires target shareholder approval under the capital reduction provisions of the Corporations Act.

As with a scheme of arrangement, this structure provides the benefit of an all-or-nothing outcome, but without the requirement for ASIC sign-off and court approval. However, the structure is not frequently used as it has certain limitations and risks, such as the following.

- **(Shareholder approval thresholds)** A selective capital reduction must be approved by two shareholder resolutions:
 - first, a special resolution at a meeting of all shareholders (ie. at least 75% of votes cast voting in favour), with no votes being cast in favour of the resolution by any shareholder who is to receive consideration as part of the reduction; and
 - second, a special resolution at a meeting of only those shareholders whose shares will be cancelled (ie. at least 75% of votes cast voting in favour).

None of the 'minority' shareholders can vote in favour of the first resolution but they can vote against. This means that the bidder needs to ensure it holds a sufficient number of shares to overcome any 'no' votes by minority shareholders. For instance, if the bidder holds 15% of the shares, shareholders who hold only 5% in total can block the proposal (assuming no other shareholders vote in favour).

(Requirement for capital) A selective capital reduction can only occur to the extent that the target company has sufficient share capital. Often the proposed aggregate consideration is higher than the share capital recorded in the target's accounts.

- **(Form of consideration)** In most cases the form of consideration for the reduction can only be cash. This is because a person cannot be compelled to accept shares – under Australian law there is a requirement that a person must consent to becoming a member of a company. Where the bidder proposes to offer its own shares as consideration, a scheme of arrangement will be required because only under a scheme structure will all target shareholders be deemed to have consented to acquiring bidder shares (except in certain circumstances where the target company's constitution contains a deemed consent provision).
- **(Additional requirements imposed on targets)** A company can only reduce its share capital if it is fair and reasonable to the shareholders as a whole, and if it does not materially prejudice the company's ability to pay its creditors. If challenged in a court, the company bears the onus of establishing that the requirements have been complied with. These requirements are not imposed on targets in the bid or scheme structures. There is some support, but no definitive law, for the view that the fair and reasonableness requirement is satisfied if the consideration falls within an independent expert's valuation range.

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- **(Tax consequences)** There is always a question of whether the payment of consideration to minority shareholders is treated as capital (such that shareholders will pay capital gains tax on any gain, as with the consideration received under a bid or scheme), or whether the Australian Taxation Office (the ATO) will determine that part or all of the consideration should be treated as an unfranked dividend. For a minority shareholder it is usually preferable for the consideration to be treated as capital (as any capital gain can be offset by capital losses, or the shareholder can take advantage of the capital gains tax discounting rules) rather than as an unfranked dividend (as that will be treated as income which is taxed at the shareholder's marginal income tax rate). An ATO ruling is usually necessary to confirm the position.

(b) Securityholder-approved transaction
(for a company or trust)

This structure can be used to enable a person to acquire a majority, but not 100%, of the issued securities in a company or trust. It involves the bidder being issued with, or acquiring from an existing securityholder, such number of target securities so as to result in the bidder obtaining a majority interest. The transaction must be approved by target securityholders under section 611 item 7 of the Corporations Act (which is an exception to the 20% rule).

The reason why a person cannot use the s611 item 7 structure to acquire 100% ownership is because of the voting restrictions on the transaction. A s611 item 7 transaction must be approved by an ordinary resolution of securityholders, with no votes being cast by the bidder or any person whose securities are to be acquired, or by any of their respective associates. So if the bidder sought to purchase 100% of the target securities there would no securityholders qualified to vote in favour of the resolution. ASIC policy is generally not to grant relief from these voting restrictions.

The s611 item 7 structure is rarely used for transactions involving the transfer of existing securities as securityholders are usually unlikely to approve a change of control where they receive no direct benefit. The structure is more commonly used for significant equity injections which result in the issue of new securities.

Takeover bids

(for companies and trusts)

7

- A takeover bid can be used for either a friendly or hostile acquisition of a company or trust.
- A takeover bid involves the making of individual offers to purchase target securities at a specified bid price.
- There are two types of takeover bid: an off market bid and a market bid.
- Virtually all takeover bids are off-market bids because of the ability to include conditions.
- Takeover bids are subject to the following key rules that:
 - all offers must be the same;
 - the bid price cannot be lower than the price which the bidder paid for a target security within the previous 4 months;
 - the offer period to be no less than 1 month and no more than 12 months;
 - there are no special deals for individual target securityholders;
 - there are no self-triggering bid conditions (for off-market bids);
 - the bidder must issue a 'bidder's statement' containing the offer terms and other information;
 - the target must issue a 'target's statement' containing the target board's recommendation; and
 - the bidder is entitled to compulsory acquisition if it obtains a relevant interest in at least 90% of the target securities (and has acquired at least 75% of the securities it offered to acquire).

7.1 What is a takeover bid?

In general terms, a takeover bid involves a bidder making individual purchase offers at a specified bid price to all holders of securities in an ASX-listed Australian company or trust. If, by the end of the offer period, the bidder has received acceptances of the offers sufficient to give it a relevant interest in at least 90% of the target securities (and has also acquired at least 75% of the securities it offered to acquire), the bidder can proceed to compulsorily acquire the remaining target securities at the bid price.

There are two types of takeover bid:

- an off market bid (which may offer cash or other consideration, may be subject to conditions, and may be for 100% of the target securities or a specified proportion of each target securityholder's securities); and
- a market bid (which must be an unconditional cash offer).

In an off-market bid, the bidder must make its offers to target securityholders in writing in a document called a bidder's statement. The target must respond to that by preparing and despatching to its securityholders a document called a target's statement which contains the target directors' recommendation. In contrast, a market bid (often called an on-market bid) involves the bidder appointing a broker to stand in the ASX market and make offers to acquire target securities at the specified bid price, with acceptances being effected by the execution of on-market trades rather than off-market acceptances. Despite the offers being made on-market, a bidder's statement and target's statement still needs to be prepared in a market bid.

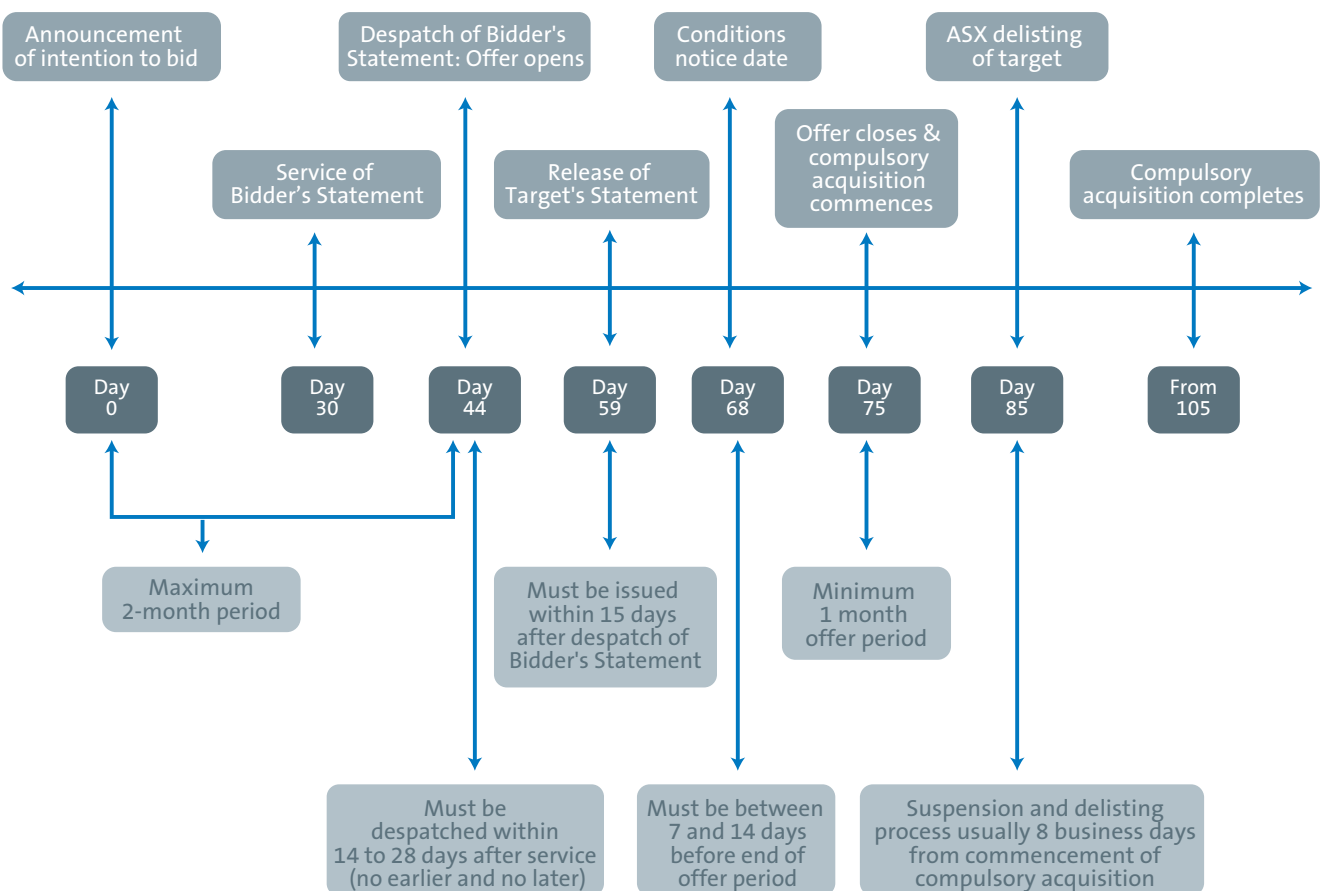
A takeover bid, whether an off-market or market bid, can be used for either a friendly or hostile acquisition. In a friendly deal, it is common for the bidder and target to enter into a bid implementation agreement which contains: the agreed key terms and conditions of the offer, the target's obligations to recommend the bid, and various other provisions dealing with the operation of the target prior to the bidder obtaining control of the target. It is also common for a bid implementation agreement to contain deal protection mechanisms such as exclusivity provisions (including 'no-shop' and 'no-talk' restrictions), rights to match rival bidders and a break fee payable by the target to the bidder in certain circumstances if the bid is not successful. A bid implementation agreement is binding only on the target and not on target shareholders.

Virtually all takeover bids are off-market bids because of the ability to include conditions. For simplicity this handbook focuses on the off market bid structure involving an offer for 100% of a target's securities. This section 7 focuses on the key takeover rules and features. See sections 10 and 11 for a discussion of the strategic considerations involved in planning or responding to a takeover proposal.

7.2 Indicative timetable

Below is an indicative timetable for a basic off-market takeover bid, which assumes that the bid becomes unconditional, does not require any extensions and

proceeds to compulsory acquisition. It is also assumed that there is no rival bidder and no regulatory action which affects timing.



7.3 Key takeover bid rules and features

The rules governing an off-market takeover bid are detailed in Chapter 6 of the Corporations Act, and supplemented by ASIC and Takeovers Panel policies. Below is a summary of the key takeover bid rules and features.

(a) Bid announcement and 2-month rule

It is standard practice for a bidder to first announce an intention to make a takeover bid for a target before lodging and despatching its bidder's statement. The making of a bid announcement triggers an obligation on the bidder to despatch its bidder's statements (which contain the takeover offers) within 2 months. This is commonly known as the '2-month rule'. The terms and conditions of the takeover offers must be the same or not substantially less favourable (to target securityholders) than

those in the announcement. Because of this the proposed offer conditions (see paragraph (h) below) need to be set out in full or described in detail in the announcement.

There are limited circumstances in which a bidder need not follow through. These include where a bidder could not reasonably be expected to proceed with the takeover bid as a result of a change in circumstances, eg an offer condition being breached or the bidder has been clearly overbid.

(b) Offers must be the same

All the offers made under the bid must be the same, subject to certain statutory exceptions.

(c) Offer consideration

There are no restrictions on what can comprise offer consideration. It can be in the form of cash (in any currency), securities (whether quoted or unquoted) or other non-cash assets, or a combination of those, provided that all target securityholders are offered the same thing. A bidder can offer consideration alternatives (eg cash or shares), again provided that all target securityholders are offered the same alternatives.

If the offer consideration comprises cash, the bidder's statement must contain details of the source of that cash consideration (eg cash at bank, funding from parent entity, external debt financing or equity raising). A bidder should not announce a bid without either adequate funding arrangements already in place or reasonable grounds to expect that it will have sufficient unconditional funding in place to satisfy acceptances when its offers become unconditional. Reasonable grounds may still exist even if any debt financing has not been formally documented or remains subject to conditions to drawdown at the time of announcement, but there must be an enforceable commitment.

If the offer consideration comprises securities, the bidder's statement must contain prospectus-level disclosure regarding the assets, liabilities, profits and prospects of the issuing entity and particulars of the securities being offered.

The offer consideration can be increased, but not reduced, during the course of a bid. All target securityholders who have already accepted the bid are entitled to receive any increase. If the bidder acquires target securities on-market or otherwise outside the takeover bid during the offer period at a price higher than the bid price, the offer is deemed to be increased to that price. If the original offer did not include a cash-only consideration and the bidder purchases target securities outside the bid for cash, the bidder must give offerees who have accepted the opportunity to elect to receive cash.

(d) Minimum bid price rule

The consideration offered for target securities must equal or exceed the maximum consideration that the bidder or an associate provided, or agreed to provide, for a target security under any purchase or agreement during the 4 months before the date of the bid. There are particular rules for determining the value of pre-bid non-cash consideration, and for applying this rule where the consideration under the bid is or includes scrip.

(e) Time limits for payment of consideration

In general terms, the offer consideration must be paid or provided by the earlier of 1 month after the offer is accepted (or if the offer is subject to a defeating condition, within 1 month after the contract becomes unconditional) and 21 days after the end of the offer period. It is common for bidders to accelerate payment timeframes to attract acceptances, once the offer is unconditional.

(f) Length of offer period

The offers must remain open for at least one month. The offer period can be extended by a further period, subject to an aggregate offer period of not more than 12 months. Most bids are made for the minimum period of one month and then extended as necessary to secure sufficient acceptances. If the offer is conditional, any extension must be effected before the 'status of conditions' notice is filed (see paragraph (h) below for a description of this notice). The only exception to this is where a rival takeover bid is announced or improved during that last

7-day period. The offer period will be automatically extended if within the last 7 days the consideration is improved or the bidder's voting power increases to more than 50%. In that case, the offer period is extended by 14 days from the relevant event.

If the offer period is extended by more than 1 month (or by a cumulative period of more than 1 month) while the offer remains conditional, every target securityholder who accepted the offer before the extension is entitled to withdraw their acceptance.

(g) Collateral benefits rule

The bidder cannot give or agree to give a benefit to a person outside the benefits offered to all target securityholders under the bid if it is likely to induce the person to dispose of their securities or accept the offer under the bid. Technically speaking, such benefits (known as collateral benefits) are only prohibited where given or offered during the offer period, however, the Takeovers Panel's application of the fundamental takeover principle of 'equality of opportunity' means that there is a risk of the Panel making a declaration of unacceptable circumstances in relation to a benefit given prior to, or agreed to be given after, the offer period. As a general rule, a benefit is less likely to constitute unacceptable circumstances if it is given on arm's-length terms (eg the bidder acquiring an asset from a target securityholder for no more than market value), but would still constitute a collateral benefit if given during the offer period and is likely to induce the target securityholder to dispose of their shares or accept the takeover bid.

(h) Conditions to the offers

An off-market bid can be made subject to conditions which, if triggered, will enable the bidder to let its bid lapse and all acceptances will be voided. There are restrictions on what conditions can be imposed. In particular, a condition cannot be 'self-triggering', ie. dependent on the bidder's opinion, events within its control or events which are a direct result of the bidder's actions. This means that a general due diligence condition is not possible, though it is possible to craft due diligence-type conditions linked to objectively determinable outcomes (eg that the

target maintain a specified minimum cash position or publicly confirm that a certain state of affairs exists or does not exist). Also, there cannot be any maximum acceptance condition (one triggered if acceptances exceed a specified level). A bidder can waive conditions of its offers, but must do so at least 7 days before the offers close (the exception to this is what are called prescribed occurrence conditions which are a very narrow category of circumstances in relation to the target – see below).

Common bid conditions include: minimum relevant interest threshold (often 90% to tie in with the compulsory acquisition threshold), regulatory approvals (eg foreign investment approval or anti-trust approval), no material adverse change in relation to the target, no material transactions by the target, and no 'prescribed occurrences' in relation to the target (eg no new equity issues, no insolvency events, and no sale of the main undertaking).

The bidder must nominate a date, which must be between 7 and 14 days before the end of the offer period, on which it will notify the market on the status of its bid conditions. This date will usually be extended by the same period as any offer period extension.

(i) Bidder's statement

The offers despatched to target securityholders must be accompanied by or contained in a bidder's statement. This document requires a considerable amount of preparation on the part of the bidder and its advisers. It is required to contain all information known to the bidder which is material to a decision by a target securityholder whether or not to accept the offer. It is also required to contain a range of statutory disclosures, including:

- a statement of the bidder's intentions regarding the continuation of and any major changes to be made to the target's business, and the future employment of present employees;
- where cash is offered as consideration, the funding sources of that cash; and
- where securities are offered as consideration, information to prospectus disclosure standard regarding the assets, liabilities, profits and prospects

of the issuer and particulars of the securities being offered.

The bidder cannot despatch its bidder's statement and offers to target securityholders earlier than 14 days after service of the bidder's statement on the target (unless the target directors consent to early despatch, which often occurs in a friendly takeover bid). A bidder's statement must be despatched no later than 28 days after service on the target, and within 2 months after the bidder has announced its intention to make a takeover bid.

In a hostile bid situation, the target board will normally use the 14-day waiting period to review the bidder's statement to determine whether there are any aspects which require clarification for securityholders. If the bidder's statement is considered to be defective in any way, or appears to contain material misstatements or omissions, the target board can make an application to the Takeovers Panel for a declaration of unacceptable circumstances and orders for corrective disclosure. In practical terms, any such application should be brought no later than the end of the first 7 days of that 14-day period.

(j) Target's statement

After receipt of the bidder's statement, the target must prepare and despatch to its securityholders a target's statement responding to the bid. The target's statement must contain a statement by each target director recommending that the bid be accepted, or not accepted, and giving reasons for the recommendations, or reasons why a recommendation has not been made. It must include all information known to any target director that target securityholders and their professional advisers would reasonably require to make an informed assessment whether to accept the bid.

Once the 14-day waiting period expires and the bidder despatches the bidder's statement to target securityholders, the target then only has 15 days to finalise preparation of its target's statement and print and commence despatch of that target's statement to its securityholders. This can place

considerable pressure on a target which is subject to a hostile bid.

If the bidder's voting power in the target is 30% or more, or a director of the bidder is also a director of the target, then the target's statement must be accompanied by an independent expert's report. That report must state whether, in the expert's opinion, the offer is fair and reasonable. It is also possible that the target will wish to obtain an independent expert's report as part of its defence, which would accompany the target's statement. The independent expert's report will be a long-form report, giving a detailed assessment of the value of the target and its securities, as well as a (usually less detailed) assessment of the value of the bidder's offer consideration, if for example it includes scrip.

(k) Getting to 90% - the 'chicken and egg'

A key issue for a bidder looking to acquire 100% under a takeover bid is that, while the bid will be subject to a 90% minimum acceptance condition, institutional investors often will not accept while the bid remains conditional. This means that bidders will generally need to waive the offer conditions in order to reach the 90% compulsory acquisition threshold – though this exposes the bidder to the risk of ending up with less than 90% or even with a minority interest. It is largely because of this risk that the scheme structure, which provides an 'all-or-nothing' outcome, is frequently used to effect a 'friendly' 100% acquisition of a target.

One tool which has been developed to attempt to deal with this issue in a takeover bid is the institutional acceptance facility, which has been used in numerous takeover bids. The concept is simple. Rather than accepting the bid at the outset, certain institutional target securityholders are given the option of initially just indicating their intention to do so. That is achieved by the institution providing 'acceptance instructions' to a third-party trustee. The instructions either take the form of a completed acceptance form or (if the securities are held through a custodian) written directions to the custodian. The trustee holds the instructions until a specified trigger event occurs – most commonly the delivery of a notice by the bidder confirming that, when combined

with the actual acceptances already received by the bidder, the instructions will (when processed) result in the bidder achieving acceptances for more than a specified percentage of the target (such as 50% or 90%) and the bid will then become unconditional.

Upon the trigger event occurring, the trustee acts on the instructions by delivering the acceptance forms to the bidder and providing the directions to the custodians. Hence, it is only at that point that the institutional securityholders' intentions to accept are converted into actual acceptances of the bid. Up until the trigger event occurring, the securityholders have the ability to retract their instructions, and retain full control over the voting and disposal of their securities.

Such facilities have an in-built flexibility which makes them attractive to bidders: they can be introduced at any time during a bid and (within limits) the bidder has a broad discretion as to what trigger event applies. This flexibility is particularly useful. A bidder has the opportunity of first assessing the bid's progress before having to commit to withdrawal rights. If such rights become necessary, they can then be tailored to the particular circumstances prevailing – the facility can be directed at the specific securityholders that have concerns, and can be structured with a trigger event that achieves the precise outcome desired by the bidder.

(l) Compulsory acquisition

If at the end of the offer period the bidder has received acceptances sufficient to give it relevant interests in 90% or more of the target's voting securities, the bidder can proceed to compulsorily acquire the remainder at the bid price. This process usually takes about 1 to 2 months to complete. In theory the bidder can commence the compulsory acquisition process during the offer period provided the 90% threshold is met, but it is usual to wait until the offer period has ended.

(m) Liability regime

The Corporations Act contains a detailed liability regime for misleading or deceptive statements or conducts in relation to takeover transactions.

There is a specific regime covering bidder's statements and target's statements. Broadly, the inclusion of a misleading or deceptive statement in such a document, or an omission of required information from such a document, is prohibited and gives rise to a requirement to compensate any person who suffered loss as a result, and can also give rise to criminal liability. Each director of the bidder or target automatically bears liability if the bidder or target (as applicable) has issued a defective bidder's statement or target's statement (as applicable).

Defences against criminal and civil liability for a defective bidder's statement or target's statement include: that the relevant person proves they did not know the statement was misleading or deceptive or that there was a relevant omission; or the relevant person (if a director) proves that they placed reasonable reliance on the company's management; or the relevant person (if a company) proves that they placed reasonable reliance on an external adviser. It is common practice for bidders and targets to establish due diligence processes to assist in establishing these defences if required, in addition to minimising the risk of including a misleading or deceptive statement in a bidder's statement or target's statement in the first place.



Schemes of arrangement (for companies)

8

- A scheme of arrangement can be used only for a friendly acquisition of a company, and is frequently used to effect 100% acquisitions.
- A scheme of arrangement is a shareholder and court-approved statutory arrangement between a company and its shareholders that becomes binding on all shareholders by operation of law.
- Schemes are subject to fewer prescriptive rules than takeover bids and therefore can be more flexible, but are supervised by ASIC and the courts.
- A standard scheme involves:
 - a scheme implementation agreement between the bidder and the target;
 - the preparation by the target, with input from the bidder, of a draft 'scheme booklet' which is given to ASIC for review;
 - the target seeking court approval for the despatch of the scheme booklet to target shareholders and court orders for the convening of the shareholders' meeting to vote on the scheme (ie. the scheme meeting);
 - holding the scheme meeting;
 - the target seeking court approval for the implementation of the scheme;
 - implementing the scheme; and
 - de-listing the target from ASX.

8.1 What is a scheme of arrangement?

In general terms, a scheme of arrangement is a shareholder and court-approved statutory arrangement between a company and its shareholders that becomes binding on all shareholders by operation of Part 5.1 of the Corporations Act. The scheme structure can be used to reconstruct a company's share capital, assets or liabilities. The structure can also be used to effect a compromise between a company and its creditors (which includes option holders).

The scheme structure is frequently used to effect an acquisition of 100% of the shares in a target company. In fact, in a friendly deal the scheme structure is more often used than the takeover bid structure. This is largely because of its 'all-or-nothing' outcome and the potentially lower target shareholder approval threshold (see section 6.2). A scheme acquisition may be done by way of a cancellation scheme (ie. all shares not held by the bidder are cancelled in exchange for the scheme consideration) or a transfer scheme (ie. all shares not held by the bidder are transferred to the bidder in exchange for the scheme consideration). The transfer scheme is the more commonly used type. As the bidder is not a party to the

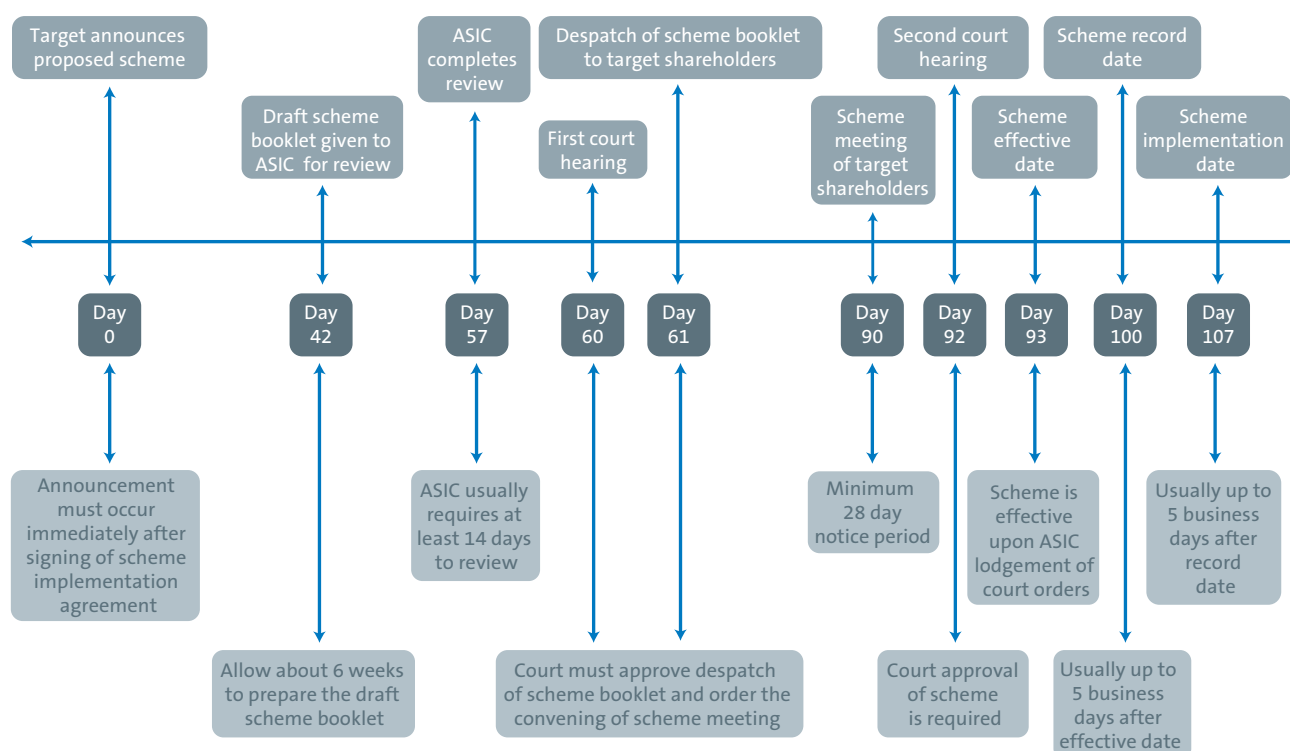
scheme, the court will usually require or expect the bidder to execute a deed poll in favour of target shareholders undertaking to pay the scheme consideration (ie. the purchase consideration) to them upon implementation.

Unlike a takeover bid, a scheme can only be used for a friendly transaction, because it is the target (not the bidder) that is required to produce and send to target shareholders a document containing the scheme proposal and certain other statutory information. Also, it is the target which applies to the court for orders convening the meeting(s) of its shareholders to vote on the scheme. Following shareholder and court approvals, the scheme will be implemented, resulting in the bidder owning 100% of the shares in the target.

This section 8 focuses on the key scheme of arrangement rules and features. See sections 10 and 11 for a discussion of the strategic considerations involved in planning or responding to a takeover proposal.

8.2 Indicative timetable

Below is an indicative timetable for a basic scheme of arrangement, which assumes that the scheme is successful, that there is no rival bidder and there are no regulatory actions that will affect timing.



8.3 Key scheme rules and features

The rules in Part 5.1 of the Corporations Act governing a scheme of arrangement are not as prescriptive as those contained in Chapter 6 for a takeover bid. Many of the rules applying to a takeover bid do not apply to a scheme. However, the Part 5.1 scheme rules need to be read in light of the numerous court decisions regarding schemes, as well as ASIC policies, which more or less seek to reflect the fundamental takeovers principles (see section 1.4).

Below is a summary of the key features of a scheme transaction, having regard to the scheme rules.

(a) Scheme implementation agreement

While not required by law, it is universal practice for a bidder and target to enter into an implementation agreement in respect of a scheme. This is because the proposal and implementation of a scheme requires a joint bidder-target effort. In contrast, a takeover bid involves the bidder and target undertaking discrete roles with specific areas of responsibility.

A scheme implementation agreement will usually contain: the target board's obligations to pursue and recommend the scheme, the target's obligations to apply to the court for an order convening a shareholders' meeting to vote on the scheme, the scheme purchase consideration, the bidder's obligations to provide the scheme consideration and assist with the preparation of the scheme booklet to target shareholders, the conditions to the scheme, and various other provisions dealing with operation of the target prior to scheme implementation. It is also common for a scheme implementation agreement to contain deal protection mechanisms such as exclusivity provisions (including 'no-shop' and 'no-talk' restrictions), rights to match rival bidders and a break fee payable by the target to the bidder in certain circumstances if the scheme is not successful.

For the most part, scheme implementation agreements and schemes can contain whatever provisions are agreed between the parties. However, there are certain matters which ASIC and the court

will have regard to when giving their approvals. For instance, deal protection mechanisms generally need to comply with Takeovers Panel policy (eg no-talk restrictions need to be subject to an exclusion to enable superior proposals to be considered and recommended, and a break fee cannot normally exceed 1% of the target's equity value).

In respect of a scheme implementation agreement, the regulatory focus is on disclosure. For instance, there needs to be adequate disclosure of any conditions to a scheme and of any matter known to the bidder or target that can affect the likelihood of implementation of the scheme. Note, though, that unlike for takeover bids, scheme conditions can be self-triggering (eg a due diligence condition is permitted). However, it is uncommon for targets to agree to such conditions.

The signing of a scheme implementation agreement triggers an obligation on an ASX-listed target to make a market announcement. The form of announcement should be agreed in advance between the bidder and target. Normally, a scheme announcement will contain the key terms and conditions of the proposed scheme, the target board's recommendation that shareholders vote in favour of the scheme in the absence of a superior proposal (and sometimes also subject to an independent expert concluding that the scheme is in the best interests of target shareholders), and an indicative timetable. It is also common for the scheme implementation agreement to be publicly released in its entirety.

(Note: a scheme implementation agreement is binding only on the target and not on target shareholders. Only if and when a scheme is approved by shareholders and then the court does the scheme become binding on target shareholders.)

(b) Scheme booklet

After the scheme implementation agreement is signed, the parties complete preparation of the explanatory memorandum (usually referred to as a scheme booklet) which the target is required by law to send to its shareholders in advance of the scheme vote. A scheme booklet must contain information about the scheme, the target directors' recommendation and other disclosures – effectively it must contain the same information that would be in a bidder's statement and a target's statement if the transaction were effected via a takeover bid instead. The scheme booklet must contain information supplied by both the bidder and target – hence the need for the target to ensure the scheme implementation agreement obliges the bidder to provide the requisite information.

It is also common practice, and expected by ASIC and the court, for a scheme booklet to include or be accompanied by an independent expert's report commissioned by the target which states whether, in the expert's opinion, the scheme is in the best interests of target shareholders. There is a statutory requirement for the target to commission an independent expert's report where the bidder's voting power in the target is 30% or more, or a director of the bidder is also a director of the target.

ASIC must be given a reasonable opportunity to review and effectively approve the scheme booklet – it usually requires a review period of at least 14 days.

(c) First court hearing

Following ASIC's review of the scheme booklet, the target must apply to the court for orders to approve the despatch of the scheme booklet and the convening of the scheme shareholders' meeting(s). If there is more than one class of target shareholders for the purposes of the scheme, each class must vote separately on the scheme (see paragraph (e) below on scheme classes).

The court cannot make those orders unless ASIC has been given at least 14 days' notice of the court hearing and the court is satisfied that ASIC has had a reasonable opportunity to examine the proposed scheme and scheme booklet, and to make submissions on those.

(d) Scheme meeting

The meeting of target shareholders to vote on the scheme (ie. the scheme meeting) is usually held about 28 days after the despatch of the scheme booklet. For the scheme to be approved by shareholders, it must be approved at meetings of each 'class' of shareholders as follows:

- the scheme must be approved by a majority in number of the target shareholders in the relevant class who have cast votes on the resolution (but note that the court has the power to waive this requirement); and
- the scheme must also be approved by 75% or more of the votes cast on the resolution by target shareholders in the relevant class.

If the bidder or its associates hold any target shares, they must usually either refrain from voting or vote in a separate class. The practice is for the bidder and its associates to refrain from voting.

See paragraph (e) below on scheme classes.

(e) Scheme classes

The requirement for a scheme to be approved by each class of shareholders makes the formation of classes of utmost importance.

The rule is that, for the purposes of a scheme, a class of shareholders are those 'whose rights are not so dissimilar as to make it impossible for them to consult together with a view to a common interest.' This involves an analysis of: the rights against the company which are to be affected by the scheme; and the new rights (if any) which the scheme gives, by way of compromise or arrangement, to those whose rights are to be so affected.

The concept of scheme classes should not be confused with classes of shares. In a scheme context, different classes can arise as between shareholders who hold the same type of share (eg ordinary share). This is because a scheme can potentially confer different benefits on different shareholders. A clear-cut example of the creation of scheme classes is where one set of target shareholders is offered a specific type of scheme consideration (say, shares in the bidder) whereas all other shareholders are offered cash only. This is allowed in a scheme as the collateral benefits rule in takeover bids does not apply to schemes. Differential consideration is not possible in a takeover bid given the collateral benefits rule plus the requirement that all offers must be the same.

But it is rarely this straightforward. There are often complex questions of whether scheme classes arise where one target shareholder has entered into an arrangement with the bidder that is separate from, but conditional upon, the scheme (eg an asset sale). The general principle ought to be that where the separate arrangement is struck on demonstrably arm's-length terms there is unlikely to be a class issue, though this has yet to be properly tested as the practice has been for target shareholders who are party to a 'side deal' with the bidder to abstain from voting on the scheme.

The creation of separate classes can be problematic because it gives each class of shareholders an effective veto right over the scheme.

Even where there are no separate classes, a Court may take into account the fact that particular target shareholders have extraneous commercial interests when exercising the court's discretion in deciding whether to approve a scheme. The Court can, as part of its fairness discretion, disregard the votes of target shareholders with extraneous interests.

(f) Second court hearing

If the scheme is approved by target shareholders and all scheme conditions have been satisfied or waived, the target returns to court for an order approving the scheme. The court hearing usually occurs within a day or two after the scheme meeting.

At that second court hearing the court does have a discretion to refuse to approve the scheme. The courts are normally reluctant to impose their own commercial judgment in relation to a scheme that has been approved by shareholders, except in very limited circumstances such as where the relevant scheme offends public policy. However, courts are not permitted to approve a scheme unless: it is satisfied that the scheme has not been proposed for the purpose of avoiding the requirements of Chapter 6 (ie. to avoid using the takeover bid structure), or ASIC issues a no-objection statement.

(g) Effective date and implementation

If the scheme is approved by the court, it takes effect upon lodgement of the court order with ASIC. There is normally a period of up to 2 weeks between the day the scheme becomes effective and the date it is implemented. This is to allow time for the target to close its register, ascertain which persons are registered shareholders as at the record date (usually up to 1 week before the implementation date) and prepare for the provision of scheme consideration. On the implementation date:

- all of the target shares other than those held by the bidder are transferred to the bidder (in a transfer scheme) or cancelled (in a cancellation scheme); and
- the scheme consideration is provided to target shareholders – if it comprises cash this occurs via the despatch of cheques or the electronic transfer of funds into nominated bank accounts, and if it comprises securities this occurs via the issue of those securities.

(h) De-listing

Following scheme implementation the target is then delisted on a date determined by the ASX upon application by the target – normally no more than a few days after the implementation date.

(i) Liability regime

Unlike for takeover bids there is no specific liability regime for scheme booklet disclosures. Rather, a scheme booklet is subject to the general misleading or deceptive conduct provisions in the Corporations Act.

Under those provisions, if there is a statement or omission in the scheme booklet that is misleading or deceptive, any person who suffers loss or damage as a result can recover the loss or damage from the person who breached the obligation. There is no specific defence to liability but a person can seek relief from the court from liability to pay compensation on the basis that the person acted honestly and, having regard to all the circumstances, ought fairly to be excused for the breach.

The target company has primary liability for a scheme booklet, though any person who was involved in a breach of the misleading and deceptive conduct provisions will bear liability (eg the bidder will usually bear liability for bidder-provided information). Despite the absence of statutory defences, the directors of a target company and bidder company can, in practice, substantially reduce their liability exposure by establishing a due diligence and verification system similar to that devised for takeover bid documents. Courts expect that target companies, as well as bidder entities, will have established and implemented such systems.

Trust schemes

(for trusts)

9

- A 'trust scheme' can be used only for a friendly acquisition of a trust, and is frequently used to effect 100% acquisitions.
- A trust scheme resembles a company scheme of arrangement, but without the requirement for court approval.
- Trust schemes are subject to fewer specific rules than takeover bids and are therefore more flexible, but the Takeovers Panel has oversight.
- A standard trust scheme involves:
 - an implementation agreement between the bidder and the target;
 - the preparation by the target, with input from the bidder, of a draft explanatory memorandum which is sent to ASIC for review before sending to unitholders in advance of the unitholders' meeting;
 - holding the unitholders' meeting;
 - lodging the amended trust constitution with ASIC;
 - implementing the trust scheme; and
 - de-listing the target from ASX.

9.1 What is a trust scheme?

A 'trust scheme' is a transaction structure which has been developed by the market over the past 15 or so years to effect a friendly acquisition of an ASX-listed trust - as an alternative to a takeover bid. The structure is called a 'trust scheme' because in some ways it resembles a scheme of arrangement for a company. However, ASX-listed trusts (formally known as listed managed investment schemes) cannot be the subject of a scheme of arrangement under Part 5.1 of the Corporations Act.

In general terms, a trust scheme involves unitholders of the target trust being asked to approve the transaction and also amendments to the trust constitution that will authorise the trustee (or responsible entity) to take steps, the end result of which will be that the bidder owns all of the units in the trust. Each ASX-listed trust must have a 'responsible entity' which is a company that under the Corporations Act performs the dual role of trustee and trust manager (though it is not uncommon for a responsible entity to appoint a custodian to hold trust property). In a takeover context, the directors of the responsible entity of a target trust are commonly referred to as the 'target directors'. In this section 9, the terms 'target', 'target directors' and 'target's responsible entity' will be used interchangeably.

Generally, there are two kinds of trust schemes: 'transfer schemes' and 'redemption schemes'.

- A **transfer scheme** involves transferring all of the issued units to the bidder (except units already held by the bidder). The transfer price paid (or scrip issued) by the bidder is passed on to the target unitholders.
- A **redemption scheme** involves redeeming (cancelling) all of the issued target units (except units held by the bidder). A key issue is to determine how best to ensure that the trust has the cash (or scrip) needed to pay for the redemptions.

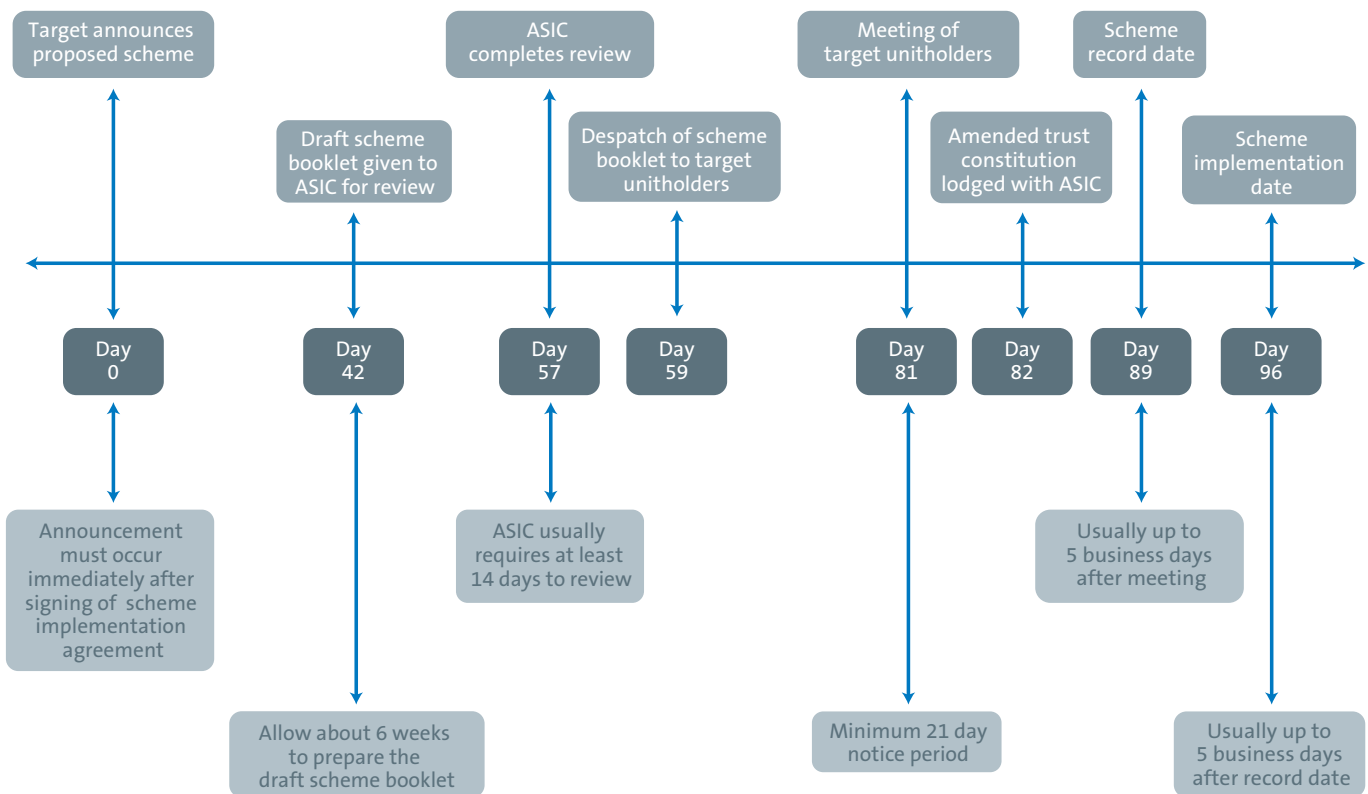
From a practical perspective, the two types of schemes follow similar procedures and have substantially the same effect for the bidder and for target unitholders. Which approach is used in a particular transaction will be determined by a range of factors, including tax (for both investors and the bidder), stamp duty and whether there are any pre-emptive rights over the target's assets.

The trust scheme structure is frequently used to effect an acquisition of 100% of the units in a target trust. In fact, in a friendly deal the trust scheme structure is much more often used than the takeover bid structure. This is largely because of its 'all-or-nothing' outcome and the lower target unitholder approval threshold (similar to a company scheme of arrangement - see section 6.2). As the bidder is not a party to the trust scheme, the target should require the bidder to execute a deed poll in favour of target unitholders undertaking to pay the trust scheme consideration (ie. the purchase consideration) to them upon implementation.

This section 9 focuses on the key trust scheme rules and features. It is prepared on the assumption that the target is a stand-alone trust, not part of a stapled entity structure. Where the trust is part of a stapled entity structure (eg trust stapled to a company), a trust scheme would need to be inter-conditional with a scheme of arrangement for the company side of the structure. See sections 10 and 11 for a discussion of the strategic considerations involved in planning or responding to a takeover proposal.

9.2 Indicative timetable

Below is an indicative timetable for a basic trust scheme, which assumes that the trust scheme proceeds as a transfer scheme, the trust scheme is successful, there is no rival bidder, judicial review is not sought and there are no regulatory actions which affect timing.



Takeovers Panel policy and general trust law. The Takeovers Panel has assumed jurisdiction of disputes regarding a trust scheme.

Below is a summary of the key features of a trust scheme transaction, having regard to the relevant rules.

9.3 Key trust scheme rules and features

In contrast to a takeover and scheme of arrangement, there is no specific statutory mechanism for a trust scheme. It is based on a combination of s611 item 7 of the Corporations Act (securityholder-approved transactions),

(a) Implementation agreement

While not specifically required by law, it is universal practice for a bidder and target (specifically, the target's responsible entity) to enter into an implementation agreement in respect of a trust scheme. This is because the proposal and implementation of a trust scheme requires a joint bidder-target effort. In contrast, a takeover bid involves the bidder and target undertaking discrete roles with specific areas of responsibility.

An implementation agreement will usually contain: the target's obligations to pursue and recommend the trust scheme, the target's obligation to convene a meeting of unitholders to vote on the trust

scheme, the trust scheme purchase consideration, the bidder's obligations to provide the trust scheme consideration and assist with the preparation of the trust scheme booklet to target unitholders, the conditions to the trust scheme, and various other provisions dealing with operation of the target prior to trust scheme implementation. It is also common for an implementation agreement to contain deal protection mechanisms such as exclusivity provisions (including 'no-shop' and 'no-talk' restrictions), rights to match rival bidders and a break fee payable by the target to the bidder in certain circumstances if the trust scheme is not successful.

For the most part, implementation agreements can contain whatever provisions are agreed between the parties. However, the Takeovers Panel's view is that the takeover bid rules in Chapter 6 of the Corporations Act should apply to trust schemes (eg no collateral benefits, minimum bid price rule and no self-triggering conditions). In practice, though, any departures from the takeover bid rules can largely be addressed through disclosure to target unitholders (eg disclosure of any self-triggering conditions such as bidder due diligence) or the creation of separate classes of target unitholders for voting purposes (eg in situations where certain unitholders will or may receive a benefit from the bidder which is not available to other unitholders). In addition, deal protection mechanisms in an implementation agreement generally need to comply with Takeovers Panel policy (eg no-talk restrictions need to be subject to an exclusion to enable superior proposals to be considered and recommended, and a break fee can usually not exceed 1% of the target's equity value).

The signing of an implementation agreement triggers an obligation on an ASX-listed target to make a market announcement. The form of announcement should be agreed in advance between the bidder and target. Normally a scheme announcement will contain the key terms and conditions of the deal, the target board's recommendation that unitholders vote in favour of the trust scheme in the absence of a superior proposal (and sometimes also subject to an independent expert concluding that the terms of

the trust scheme are fair and reasonable for target unitholders), and an indicative timetable. It is also common for the implementation agreement to be publicly released in its entirety.

(Note: an implementation agreement is binding only on the target and not on target unitholders. Only if and when a trust scheme is approved by unitholders and the amended target constitution is lodged with ASIC does the trust scheme become binding on target unitholders.)

(b) Explanatory memorandum

After the implementation agreement is signed, the parties complete preparation of the explanatory memorandum which the target responsible entity is required, by law, to send to its unitholders in advance of the scheme vote. An explanatory memorandum must contain information about the trust scheme (including the proposed amendments to the trust constitution to enable the responsible entity to implement the scheme), the target directors' recommendation and other disclosures – effectively it must contain the same information that would be in a bidder's statement and a target's statement if the transaction were effected via a takeover bid instead. The scheme booklet must contain information supplied by both the bidder and target – hence the need for the target to ensure the implementation agreement obliges the bidder to provide the requisite information. If the consideration for the scheme is a security, then the content requirements for offering that type of security must also generally be met.

It is also common practice, and expected by the Takeovers Panel, for an explanatory memorandum to include, or be accompanied by, an independent expert's report commissioned by the target which states whether, in the expert's opinion, the terms of the scheme are fair and reasonable to target unitholders.

Where the trust scheme requires unitholder approval under s611 item 7 of the Corporations Act (see paragraph (c) below), a draft of the explanatory memorandum should be given to ASIC for its review at least 14 days before despatch.

(c) Unitholders' meeting

The meeting of target unitholders to vote on the trust scheme is usually held about 21 to 28 days (depending on the target's notice of meeting requirements) after the despatch of the explanatory memorandum.

Under a trust scheme that proceeds as a transfer scheme, the target's unitholders will be required to pass the following two resolutions:

- an ordinary resolution (ie. a majority of votes cast) to approve, for the purposes of s611 item 7 of the Corporations Act, the bidder increasing its voting power in the target above 20%; and
- a special resolution (ie. at least 75% of votes cast) under s601GC of the Corporations Act to amend the target's constitution to enable the target's responsible entity to implement the trust scheme.

An ASIC modification is required, and usually given, to enable the unitholders not associated with the bidder to vote in favour of the first resolution (because s611 item 7 would otherwise prohibit any unitholder who is to receive trust scheme consideration to vote in favour of the trust scheme). The bidder and its associates cannot vote in favour of the first resolution.

The target's responsible entity and its associates are not entitled to vote their interest on either resolution (or on any unitholder resolution) if they have an interest in the resolution or matter other than as a unitholder.

It is the Takeovers Panel's expectation that, where a target unitholder is treated differently to others (eg receives a benefit from the bidder not available to others), that target unitholder should not vote in favour of the trust scheme or have their votes disregarded.

(d) Effective date and implementation

If the trust scheme is approved by target unitholders and becomes unconditional, the target's amended constitution is lodged with ASIC and comes into effect on lodgement. There is normally a period of up to 2 weeks between the day the amended

constitution becomes effective and the date of implementation of the trust scheme. This is to allow time for the target to close its register, ascertain which persons are registered unitholders as at the record date (usually up to 1 week before the implementation date) and prepare for the provision of trust scheme consideration.

On the implementation date:

- in a transfer scheme, all of the units other than those already held by the bidder are transferred to the bidder and unitholders receive the transfer price paid by the bidder for those units (or, if applicable, securities instead of cash); and
- in a redemption scheme, all of the units other than those held by the bidder are redeemed in exchange for cash (or, if applicable, securities) – in a cash-only transaction the bidder might subscribe for and be issued new units immediately before redemption so as to fund the redemptions.

(e) Post-implementation

Following trust scheme implementation, the target is delisted on a date determined by the ASX upon application by the target – normally no more than a few days after the implementation date. The bidder then arranges for the target to be removed as a managed investment scheme. In addition, a bidder will want to replace the target's responsible entity if the bidder has not separately purchased that entity.

(f) Liability regime

Unlike for takeover bids, there is no specific liability regime for trust scheme explanatory memorandum disclosures, at least where the consideration is just cash. Rather, an explanatory memorandum is subject to the general misleading or deceptive conduct provisions in the Corporations Act.

Under those provisions, if there is a statement or omission in the explanatory memorandum which is misleading or deceptive, any person who suffers loss of damage as a result can recover the loss or damage from the person who breached the obligation. There is no specific defence to liability, but, a person can seek relief from the court from liability to pay

compensation on the basis that the person acted honestly and, having regard to all the circumstances, ought fairly to be excused for the breach.

The target has primary liability for a trust scheme explanatory memorandum, though any person who was involved in a breach of the misleading and deceptive conduct provisions will bear liability (eg the bidder will usually bear liability for bidder-provided information). Despite the absence of statutory defences, the directors of a target responsible entity and bidder company can, in practice, substantially reduce their liability exposure by establishing a due diligence and verification system similar to that devised for takeover bid documents.

If securities are included as consideration then the liability regime applicable to the type or types of security will apply to the explanatory memorandum disclosures.

(g) Judicial advice

A target responsible entity can, but is not obliged to, apply to a court for 'judicial advice' in relation to the trust scheme. The court is asked to confirm that the responsible entity is justified in convening a meeting of unitholders for the purpose of considering resolutions to approve the trust scheme.

A key advantage to obtaining judicial advice is that it largely removes any practical risk of the responsible entity being liable for breach of trust in proposing and giving effect to the trust scheme (though it does not shield against claims based on other grounds such as breach of duty under the Corporations Act). The principal drawbacks of seeking judicial advice are time and cost, though the court process usually adds at most an extra 1 to 2 weeks to the process.

For trust schemes the customary approach is to first seek confirmation by the court that the responsible entity can call the meetings of unitholders and, if the unitholders pass the required resolutions, then seek confirmation that implementation of the transaction can proceed.

Without judicial advice, in theory, disaffected unitholders would have up to 12 years to attack the transaction. In practice, the chances of a successful challenge should decline steeply if unitholders failed to act promptly.

There is no standard practice regarding seeking judicial advice and trust schemes. However, judicial advice will always be sought if the transaction also involves a company scheme of arrangement to be considered by the same court (eg in relation to a scheme for a stapled group involving a trust and a company). This is because the judge will want to be told about the whole transaction and have all the participants before them.

In the past, judicial advice was not generally sought for a trust scheme where a company scheme of arrangement was not also required. However, it is becoming more common.

Strategic considerations for a prospective acquirer

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- Threshold matters for a prospective acquirer to consider include: transaction structure; whether it is seeking 100% or just control; form of offer consideration; due diligence requirements; friendly or hostile deal; and the potential acquisition of a pre-bid stake.
- The initial approach to the target is usually conducted verbally, and followed by a written confidential, non-binding and indicative proposal. The target generally has no obligation to announce such a proposal - unless it ceases to become confidential – but could decide to do so for strategic reasons.
- If a target grants due diligence access it will usually only do so on the basis of a confidentiality agreement, which restricts the use of that information to implement a friendly transaction. The target may also require a 'standstill agreement' whereby the prospective acquirer cannot acquire target securities for a specified period except under a friendly transaction.
- A prospective acquirer can seek to bolster its position by acquiring a pre-bid stake (subject to the 20% takeovers rule, insider trading rules, any need for secrecy and other considerations).
- If the target is not receptive to an approach, a prospective acquirer can launch a hostile takeover bid, make a 'bear hug' announcement or initiate a board spill.

10.1 Threshold matters

In Australia, it has traditionally been difficult to successfully conclude a control transaction without the co-operation and favourable recommendation of the target's board of directors at some point in the process.

It is therefore not surprising that a prospective acquirer will almost always seek the upfront recommendation of the target board. In a scheme of arrangement or trust scheme transaction, the target board's recommendation is a pre-requisite.

In a control context, the prospective acquirer's first contact with the target is customarily a verbal, informal sounding-

out (by the chairman or a senior executive of the acquirer or by the acquirer's external financial adviser) of the target's appetite for a control transaction. Depending on the outcome of that discussion, the prospective acquirer would commonly submit to the target a written, confidential, indicative and non-binding proposal and seek due diligence.

But before any contact is made with the target, there are some threshold matters that a prospective acquirer will have considered with the assistance of its external financial, legal and accounting advisers. These include the following. (For simplicity the table looks only at company targets (rather than trust targets as well).)

Transaction structure

Does the prospective acquirer have a preferred transaction structure – takeover bid or scheme of arrangement? See section 6.2.

Control or 100%?

Is the prospective acquirer seeking to acquire 100% of the target, or would it be satisfied with simply obtaining a controlling interest and maintaining the target's ASX listing? This will inform the decision on transaction structure – a scheme of arrangement is often ideal for a 100% acquisition, whereas a proportional takeover bid is the only way to guarantee an acquisition of less than 100%. See sections 6, 7 and 8.

Offer consideration

How much is the prospective acquirer prepared to offer? Is the prospective acquirer prepared to engage in a bidding war if a rival bidder emerges? If the offer/purchase consideration is or comprises cash, how will that be funded – through existing cash reserves, existing or new debt facilities, new equity raising or otherwise? If the consideration is or comprises equity securities issued by the prospective acquirer, the prospective acquirer will need to be prepared to provide detailed information about itself to target securityholders. If the prospective acquirer is a non-Australian company but the target largely comprises Australian investors, is the prospective acquirer prepared to undertake a secondary listing on ASX to attract target securityholder acceptances or approval?

Due diligence

How much due diligence on the target does the prospective acquirer need? It is normal to seek due diligence access at the time of submitting a written proposal. Ideally, the prospective acquirer will have a broad understanding of the target and what are likely to be 'dealbreaker' issues, based on publicly available information and industry knowledge and experience.

Friendly or hostile

Will the prospective acquirer be prepared to undertake a hostile takeover bid if the target is not receptive to a deal, or is the prospective acquirer only willing to undertake a friendly transaction? To a large degree this will depend on whether the prospective acquirer is prepared to undertake a transaction without the benefit of detailed due diligence.

Pre-bid stake

Is the prospective acquirer interested in acquiring an initial stake in the target to increase the chances of a successful deal, or to use as the platform for a hostile bid, or to exert pressure on the target or to act as a blocking stake against rival bidders? The prospective acquirer's ability to acquire a pre-bid stake will be impacted by insider trading rules to the extent it is granted due diligence or otherwise acquires information that is confidential and price-sensitive. Also, a bidder should be aware that it will be unable to vote any target shares it holds on the scheme of arrangement.

Regulatory approvals and conditions

What, if any, regulatory approvals does the prospective acquirer need in Australia and elsewhere in order to undertake the deal, and what is the likelihood of obtaining those approvals? Common regulatory approvals are Australian foreign investment approval and competition approvals.

Public disclosures

Is the prospective acquirer comfortable with the risk of being 'outed' as a potential bidder for target, notwithstanding that it has submitted a confidential and non-binding proposal? The target could voluntarily announce the indicative proposal or be forced to do so under its continuous disclosure obligations.

Some of these matters are examined in more detail below.

10.2 The initial approach

A prospective acquirer's initial approach to the target is usually an informal, verbal one conducted between the chairman or senior executives of the two entities (or between respective external financial advisers). The purpose of such approach is to sound-out the target's appetite for a friendly control transaction. If it transpires that the parties have fundamentally different views on value which are unlikely to be bridged, then the prospective acquirer might decide to leave things at that. But if preliminary discussions indicate that a deal is possible, the prospective acquirer might be encouraged to submit a written proposal.

Written proposals are normally submitted on a confidential, indicative and non-binding basis. There are two key reasons for this.

(a) Confidentiality

First, there are strategic benefits for the prospective acquirer in maintaining the confidentiality of an approach. The submission of a confidential takeover proposal will usually not trigger an ASX announcement obligation on the target's part. This is because, while a takeover proposal will qualify as price-sensitive information that an ASX-listed target is prima facie obliged to disclose under its ASX continuous disclosure obligations, there is an

exception for information that is confidential and concerns an incomplete proposal or negotiation. A confidential, indicative and non-binding proposal falls within the exception.

Notwithstanding that, some companies have in the past voluntarily announced the receipt of a confidential proposal – whether to seek to generate a bidding auction or due to a conservative approach to disclosure, or otherwise. Unfortunately, there is little that a prospective acquirer can do to prevent this. Note that a target's announcement that it has received an indicative proposal does not usually impose on the prospective acquirer any obligation to proceed with a takeover. Note also that an ASX-listed target is not required, under its continuous disclosure obligations, to announce the receipt of an incomplete and confidential proposal for so long as it remains confidential.

Where the proposal is 'leaked' in the media or to the market, confidentiality may be lost and the target will then be obliged to announce the receipt of the proposal.

(b) Due diligence and board recommendation

Secondly, a prospective acquirer is often not willing to be bound to proceed with a takeover unless and until it has had an opportunity to conduct due diligence

on the target and has secured the target board's recommendation, and will be unable to proceed with a scheme of arrangement unless it has secured the target board's recommendation. As a takeover bid cannot be made subject to a general due diligence condition (see section 7.3(h) above), if there are due diligence issues to be addressed that will need to be done ahead of the offer being announced. There may be other pre-conditions which need to be satisfied, such as the prospective acquirer obtaining indicative financing commitments.

10.3 Due diligence and confidentiality agreement

Given that ASX-listed entities in Australia are subject to fairly extensive reporting requirements and have an obligation to publicly release all price-sensitive information (otherwise known as 'continuous disclosure obligations'), a preliminary due diligence exercise based solely on publicly available information should give a prospective acquirer a reasonable understanding of the target and of what matters it should probe.

Obviously there are limits to relying on publicly available information. Much information relating to a company's business is not disclosed either because it is not price-sensitive or is price-sensitive but need not be disclosed due to an exception to the continuous disclosure rules (eg the information is confidential and is generated for internal management purposes or is a trade secret). Information which may not be price-sensitive to an investor and not publicly available can nonetheless be commercially sensitive and of interest to a prospective acquirer. For instance, internal management budgets and forecasts are likely to affect value, as will the existence of change of control provisions in contracts.

A target in most circumstances has no obligation to provide due diligence access to any person, nor to provide a particular level of access once granted. However, it would be consistent with a board's duty to act in the best interests of shareholders to take reasonable steps to facilitate a proposal that, if implemented, would maximise value for shareholders.

A target will almost always require a prospective acquirer to sign a confidentiality agreement before granting due diligence access. Under a standard confidentiality agreement, the prospective acquirer agrees to keep due diligence information confidential and to use it only for the purposes of a target-recommended transaction.

10.4 Standstill agreement

Under a standstill agreement, the prospective acquirer agrees not to acquire any interest in any securities in the target for a specified period. From the target's perspective, the standstill agreement serves a number of purposes:

- it enables a target board to enter into discussions knowing that the other party will not then turn hostile on the target, or acquire a stake to attempt to block a competing transaction subsequently recommended by the target board;
- it means that if that other party does then acquire target securities (assuming it can do so without contravening insider trading laws), the target does not have to prove that that party used confidential information in acquiring the shares in breach of the agreement – only that the standstill agreement has been triggered; and
- it provides some protection for the target from potential liability for 'tipping' under the insider trading provisions of the Corporations Act - 'tipping' is where a person discloses non-public, price-sensitive information to a person who the first person believes would be likely to acquire target shares.

10.5 Pre-bid acquisitions

A prospective acquirer may seek to acquire a 'pre-bid' stake in the target (ie. a relevant interest in target securities in advance of acquiring securities under a control transaction). A pre-bid stake can be used as a platform for a hostile takeover bid, or to exert pressure on the target to agree to a deal or to act as a blocking stake against rival bidders. A pre-bid stake can take various forms, ranging from conditional or unconditional security acquisitions to put and call option arrangements to agreements to accept a takeover bid or vote in favour of a scheme.

The key constraints and considerations relevant to a pre-bid acquisition are as follows.

- **(20% takeovers rule)** The prospective acquirer must ensure that it does not have a relevant interest in more than 20% of the target securities, or otherwise voting power of more than 20% in the target, as a result of any pre-bid acquisitions. Otherwise it will breach the 20% rule (see section 2). Negotiations for the acquisition of a pre-bid stake from an existing target shareholder need to be managed to avoid forming any agreement, arrangement or understanding as to how the target shareholder will vote or dispose of the balance of their shares – otherwise the prospective acquirer will become an associate of the target shareholder and the prospective acquirer’s voting power in the target will increase by reference to the target shareholder’s total holding.
- **(Foreign investment approval requirements)** If the prospective acquirer is a ‘foreign person’ it may need to obtain Australian foreign investment approval (FIRB approval) to acquire securities in the target (see section 12.1).
- **(Insider trading)** If non-public price sensitive information is provided by the target to the prospective acquirer in the due diligence material, technically this would prevent the prospective acquirer from acquiring any target securities. This is because such acquisitions would constitute unlawful insider trading. (Note, though, that the insider trading rules do not prohibit a prospective acquirer from trading in target securities merely because the prospective acquirer intends to make a takeover bid – this is because there is an ‘own intentions’ exception).
- **(Substantial holding disclosures)** Where the prospective acquirer holds a relevant interest in 5% or more of the target’s voting securities, or otherwise voting power of 5% or more in the target, as a result of any pre-bid acquisitions, the prospective acquirer will need to disclose its interest via the filing of a substantial holding notice (see section 5). Importantly, a substantial holding notice must have attached to it a copy of all relevant agreements, such as the share purchase agreement or pre-bid acceptance agreement (as applicable). Therefore,

where a prospective acquirer seeks to acquire a secret pre-bid stake it should limit itself to less than a 5% interest – however, note that a prospective acquirer’s relevant interests will need to be revealed if the target issues tracing notices on the registered holder of the relevant shares.

- **(Minimum bid price)** The price which a prospective bidder or an associate agrees to pay for target securities within the 4 month period before a takeover bid sets a floor price for the bid price (see section 7.3(d)).

10.6 Going on the offensive

For a prospective acquirer’s perspective, the ideal sequence of events is that the target responds favourably to an approach, quickly grants due diligence access and works co-operatively with the prospective acquirer in negotiating and settling a bid or scheme implementation agreement. However, a prospective acquirer should consider its strategic options should the target reject an indicative proposal and the prospective acquirer does not wish to walk away. There are a number of options, including as follows.

(a) Hostile takeover bid

The prospective acquirer can launch a hostile takeover bid and thereby put its proposal directly to target securityholders. The hostile bid option is not suitable for everyone. Certain companies may have a policy or practice of only undertaking friendly deals – hostile deals in Australia can be unpleasant and protracted, and often involve Takeovers Panel proceedings and public relations battles. Also, a hostile bidder needs to be prepared to buy the target without having undertaken detailed due diligence. It is not permissible to make a bid subject to a general due diligence condition, though it is possible to craft due diligence-type conditions linked to objectively determinable outcomes (eg that the target maintain a specified minimum cash position) (see section 7.3(h)). Further, a prospective acquirer that had sought to acquire 100% of the target under a scheme of arrangement will need to be comfortable with the possibility of acquiring less

than 100% under a takeover bid if it does not have a 90% minimum acceptance condition or waives such a condition to encourage acceptances (see section 7.3(k)).

(b) Bear hug announcement

The prospective acquirer could unilaterally announce that it has submitted an indicative and non-binding proposal to the target, but stop short of announcing a hostile takeover bid. The announcement would set out the indicative terms and conditions of the proposal, and outline why the prospective acquirer believes it would be favourable for target securityholders. This is known as a 'bear hug'. The aim is to pressure a target board to engage in negotiations lest it be criticised by its securityholders for failing to do so. The prospective acquirer's announcement needs to be carefully worded so that it is not considered to trigger the 2-month rule for a takeover bid (see section 7.3(a)).

(c) Board spill

If a prospective acquirer holds 5% or more of a target's shares it can requisition a general meeting of target shareholders to vote on changes to the target's board of directors. Obviously, the larger the shareholding, the more likelihood of success at the general meeting.

Strategic considerations for a target

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- The directors of an Australian company (or responsible entity of an Australian trust) will, given their fiduciary duties, usually seek to maximise shareholder value and, to that end, will usually consider the reasonableness of any takeover proposal.
- The overriding principles are that: (i) the directors of an ASX-listed Australian company (and responsible entity of a trust) must at all times act bona fide in the interests of the company (or trust unitholders), and for a proper purpose; and (ii) in respect of a takeover bid, target directors should not take actions, without securityholder approval, which causes the defeat of a control proposal.
- A board can prepare for a possible takeover approach by: preparing a takeover defence manual and undertaking other pre-approach tasks, such as monitoring the share register, maintaining a valuation of itself, preparing for the grant of due diligence to a bidder, and preparing draft ASX announcements.
- Key immediate decisions for a target following receipt of a takeover proposal are whether to: make an ASX announcement and engage with the bidder.
- If the target board concludes a takeover proposal to not be in the interests of shareholders, it should consider an appropriate defence strategy. This could involve seeking counter-bidders or establishing the inadequacy of the bidder's proposal.

11.1 Threshold matters

In planning and executing any takeover response strategy, the directors of an ASX-listed Australian company need to have regard to the following fundamental principles. (For simplicity this section 11 refers to ASX-listed Australian ‘companies’ only but it is equally applicable to ASX-listed Australian trusts.)

(a) Directors’ duties

Directors are at all times subject to fiduciary and statutory obligations, including to act bona fide in the interests of the company as a whole, and for a proper purpose. Depending on the circumstances, the directors can seek to discharge their duties in a takeover proposal context by (among other things):

- recommending or supporting a takeover proposal which the directors reasonably consider to be in shareholders’ interests, in the absence of a superior proposal;
- rejecting, or refusing to recommend or support, a takeover proposal which the directors reasonably consider to be at an undervalue;
- engaging in discussions with a prospective acquirer with a view to extracting a higher price;
- seeking alternative superior proposals; or
- investigating alternative transactions that do not involve a change of control by a third party.

(b) Frustrating actions

The Takeovers Panel has developed a policy regarding actions by a target which could cause a takeover bid or genuine potential takeover bid to be withdrawn or not proceeded with. (However, note that the policy only applies to takeover bids, and not to takeover proposals that specify that a transaction is to be conducted only via a scheme of arrangement dependent on the target board of directors recommending it.)

These actions are known as ‘frustrating actions’. In general terms, it is unacceptable from a takeovers policy perspective for target directors to take any action which causes the defeat of a control proposal, without having given the shareholders a choice (eg seeking prior shareholder approval for the frustrating action). The underlying principle is that transactions that have an effect on the company’s control should be left to shareholders, not directors.

An action can constitute a frustrating action even if it is consistent with a director’s fiduciary duties. For instance, if a takeover bid contains a condition that the target not acquire any major assets and the target nonetheless does so in breach of the condition, the bidder can rely on the breach and walk away. The target directors’ actions could constitute frustrating actions.

Frustrating actions are not unlawful. However, the Takeovers Panel has the power to make orders if it declares actions to be unacceptable, eg orders to unwind a transaction or require it to be put to target shareholders for approval.

Note that the frustrating actions policy does not prevent a target from seeking alternatives to a bid or recommending the rejection of a bid. Nor is it intended to interfere with a target’s ordinary course of business.

11.2 Pre-approach planning

While the circumstances of every takeover proposal are different and require decisions to be made at the time, there are certain things that a company's board can do to prepare for a possible takeover approach. A common approach is for a company to prepare, in conjunction

with its legal and financial advisers, a takeover defence manual which sets out some pre-approach work that can be undertaken as well as the immediate actions to be undertaken if a proposal is received.

A typical pre-approach defence plan would deal with the following matters.

Subject matter	Description
Takeover defence team	The company should identify who is to be centrally involved in responding to a takeover proposal. A defence team will usually include: company executives, directors, financial advisers, legal advisers, accounting advisers and a public relations firm.
Monitoring of register	The company should regularly monitor who holds its shares, by examining the share register (which will disclose registered holders) and substantial holding notices (which will disclose persons who have voting power of more than 5%) and issuing 'tracing notices' to registered shareholders (usually in order to obtain details of persons who have relevant interests of less than 5%). This exercise should reveal whether any potential bidders have acquired interests in the company's shares.
Identify potential bidders	The company should compile a comprehensive list of potential bidders, and identify potential alternatives to a takeover proposal, including internal proposals and 'break up' models. Integral to that process is an understanding of the synergy opportunities open to potential bidders and understanding the particular characteristics of the likely bidders.
Valuation	The company should commence and maintain a program of valuing itself and its businesses according to various takeover scenarios. The analysis should include a census of existing broker/analyst valuations.
Due diligence preparation	The company could establish an online data room containing material documents to enable the prompt granting of due diligence access to a potential bidder. In conjunction with this, a draft confidentiality and standstill agreement could be drafted by the company's legal advisers (see sections 10.3 and 10.4). In addition, the company could undertake a due diligence exercise on its material contracts, to confirm the impact of a change of control transaction.
Communications protocol	There should be a protocol regulating who is authorised to speak on behalf of the company to the media, shareholders, employees, customers, suppliers and other persons in relation to takeover matters.
Draft announcements	The company should have ready a handful of draft ASX announcements that it can quickly complete and release as immediate responses to a takeover proposal. It is advisable to at least prepare a draft 'holding response' which notes that a takeover proposal has been received and that the board will consider it.

11.3 Immediate response to an approach

As discussed in section 10.2, a prospective acquirer will usually initiate contact verbally at a senior executive or chairman level, and then follow that with a written, confidential, indicative and non-binding proposal to undertake a recommended takeover transaction.

In the event a company receives such a proposal, the key immediate steps are normally as follows.

- Inform the board and external advisers.
- Consider whether an ASX announcement and/or trading halt are necessary.
- Commence various workstreams where applicable:
 - valuation stream – this is focused on analysing the value of the specific proposal compared with potential counter-proposals and internally generated alternatives (such as demerger, asset sales and capital returns);
 - contestability stream - focusing on analysing alternatives to the proposal, particularly if at an undervalue;
 - communications stream – responsible for communicating and liaising with the company's key stakeholders should the proposal cease to be confidential; and
 - regulatory and legal stream - responsible for ensuring compliance by the company with legal and regulatory requirements, and monitoring compliance by the prospective acquirer.

- Having regard to the outputs of the valuation and contestability streams, the board needs to decide whether to engage with the prospective acquirer. The board should not feel compelled to make an immediate decision on whether to recommend the proposal, and in most cases is not in a position to do so where the proposal is indicative only. Normally the threshold decision is whether to grant due diligence to the prospective acquirer. It may be that the board believes the proposal is at an undervalue, but is nonetheless prepared to grant due diligence to facilitate discussions on a possible price increase.

11.4 Defensive tactics

A target's course of action following the initial response will depend on whether it decides to engage with the bidder. A decision to engage can mark the first step in an ultimately successful transaction. A decision to reject a proposal can result in the bidder walking away and the target continuing with its business as normal, or alternatively can result in the bidder going on the offensive, eg making a hostile takeover bid (see section 10.6). If a takeover bid is made, the target board has statutory obligations to respond to the bid (see section 7.2).

A target which is faced with a public takeover proposal at what the target board considers to be at an undervalue will obviously want to understand the constraints on the range of defensive tactics at its disposal. As noted earlier, all target director actions need to comply with fiduciary duties and (where it applies) not fall foul of the Takeovers Panel's policy on frustrating actions. Given their fiduciary duties, the directors of an Australian company (or responsible entity of an Australian trust) will usually seek to maximise shareholder value and, to that end, will usually consider the reasonableness of any takeover proposal.

The table below contains a selection of possible defensive actions, divided into those which are likely to be acceptable from a fiduciary duties, Takeovers Panel and regulatory perspective, and those which are unlikely to be acceptable from that same perspective. It covers actions which could be undertaken prior to or after receipt of a takeover proposal, and it is assumed that the

target board has reached an informed, reasonable view that the relevant takeover proposal is at an undervalue and not in the interests of shareholders. (Note that the acceptability or otherwise of an action will depend on the circumstances, so the below should not be taken as a fixed checklist.)

Target actions <u>LIKELY</u> to be acceptable from a fiduciary duties, Takeovers Panel and regulatory perspective	Target actions <u>UNLIKELY</u> to be acceptable from a fiduciary duties, Takeovers Panel and regulatory perspective
<ul style="list-style-type: none"> ✓ Seeking or facilitating a higher rival proposal. ✓ Publicly criticising the commercial merits of the proposal, such as its value, conditionality and execution risk, vis-à-vis the prospects of the target as a stand-alone entity. ✓ Taking action in the Takeovers Panel or the court against what the target reasonably considers to be unlawful or unacceptable conduct on the bidder's part (eg alleged misleading statements by the bidder). ✓ Commissioning an independent expert to undertake a valuation of the company, which can support a board recommendation to reject the proposal. ✓ Investigating alternative proposals (which may ultimately need to be made subject to shareholder approval) eg demerger or sale of key assets and subsequent capital return. 	<ul style="list-style-type: none"> ✗ Establishing a US-style shareholder rights plan which gives all shareholders, other than the bidder, a right to subscribe for additional shares at a discount. ✗ Issue of shares to a friendly party where there is no pressing need for the funds raised. ✗ Entering into pre-emptive rights arrangements with third parties (such as joint venture counterparties) over significant company assets after a takeover bid has been announced, or before a bid has been announced and that is not immediately disclosed to the market. ✗ Announcing or undertaking any action or transaction that would breach a takeover bid condition, and such action is not subject to shareholder approval or not in the company's ordinary course of business or was not disclosed to the market prior to the receipt of a takeover proposal. ✗ Incurring significant liabilities or materially changing the terms of the company's debt arrangements, which the company would not otherwise have done.

An aerial view of Earth from space, showing a vast expanse of blue oceans and white, swirling clouds. The perspective is from a high altitude, looking down at the planet's surface.

Other takeovers issues

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- Other takeovers issues which commonly arise or need consideration include:
 - whether foreign investment approval is required;
 - whether competition clearance is required;
 - ASIC's truth in takeovers policy which requires persons to be bound by their public statements in relation to a takeover; and
 - the acquisition or cancellation of target options and other convertible securities.

Below is a sample of other takeovers issues which commonly arise or need to be considered. This is by no means an exhaustive list.

12.1 Foreign investment approval

Australia has a foreign investment approval regime that regulates acquisitions by foreign persons of equity securities in Australian companies and unit trusts, and of Australian businesses and Australian real property assets. The regime is set out in the *Foreign Acquisitions and Takeovers Act 1975 (Cth)* and accompanying regulations. This section contains a brief overview of the regime. A more detailed overview is available on Allens' website.

A foreign person is generally:

- an individual that is not ordinarily resident in Australia;
- a foreign government or foreign government investor;
- a corporation, trustee of a trust or general partner of a limited partnership where an individual not ordinarily resident in Australia, foreign corporation or foreign government holds an equity interest of at least 20%; or
- a corporation, trustee of a trust or general partner of a limited partnership in which two or more persons, each of which is an individual not ordinarily resident in Australia, a foreign corporation or a foreign government, hold an aggregate equity interest of at least 40%.

A transaction that is subject to the mandatory approval requirements in the foreign investment approval regime should not be implemented unless the Australian Treasurer has 'approved' the transaction via the issuance of a no-objection notice. Therefore, a transaction that needs approval should be conditional upon the receipt of that approval.

In deciding whether to approve a proposed transaction, the Treasurer has the benefit of advice from the Foreign Investment Review Board (FIRB). The Treasurer can block proposals by foreign persons that are contrary to the national interest or to national security (depending on the type of proposal), or alternatively approve proposals on an unconditional basis or subject to conditions. Whether a

proposed transaction is contrary to the national interest or national security (as applicable) is assessed on a case-by-case basis. There are no fixed national interest rules but the Australian Government typically considers these factors: national security, competition, other Australian Government policies (including tax), impact on the economy and community, and character of the investor. Additional factors are taken into account where the target entity is in the agricultural sector or the proposed acquisition is of residential land or the acquirer is a foreign government investor.

Applications for foreign investment approval (commonly referred to as 'FIRB approval') to acquire an entity's securities are submitted to FIRB. Once a FIRB application has been lodged (and FIRB confirms that the relevant application fee has been paid) there is a statutory time period for the Treasurer to make a decision and, if no decision is made, then no further orders can be made (that is, the Treasurer cannot prohibit or unwind a transaction if a decision is not made in time). The general rule is that the Treasurer has 30 calendar days to make a decision and a further 10 days to notify the applicant. However, there are several ways that this timeframe can be extended:

- if the Treasurer requests information and documents from a person in relation to the application, the clock stops until the request has been satisfied;
- the Treasurer may also make an interim order (which is publicly available) which has the effect of prohibiting a transaction on a temporary basis (up to 90 days), effectively extending the time for the Treasurer to make a final decision;
- the Treasurer can unilaterally extend the timeframe by up to 90 calendar days (and this is in addition to the power to make an interim order); or
- an applicant can request that the timeframe be extended. The usual circumstances in which an applicant will request an extension is where FIRB indicates that it requires further time to assess an application and asks that the applicant consider requesting an extension – this is a common occurrence. In that situation, an applicant will usually agree to make an extension request, to avoid a public interim order being made or the application being rejected.

Despite the statutory time period there is no certainty that FIRB approval will be given by a particular time given that either the Treasurer or the applicant may take steps that extend that timeframe.

In the vast majority of cases, FIRB approval is not a takeover completion risk – approval is granted for the overwhelming majority of applications. However, conditions, such as standard tax conditions, can be imposed in FIRB approvals.

The rules regarding when ‘FIRB approval’ is required are complex. There is a layered system of categories, exceptions and multiple thresholds.

In the context of an acquisition of securities in an entity, and where no special rules apply (there are many – see further below):

- (a) a foreign person needs FIRB approval to acquire a direct interest (generally 10% plus equity interest)

if the target operates a ‘national security business’ (generally one involved in or connected with a ‘critical infrastructure asset’, telecommunications, defence or a national intelligence community (of either Australia or a foreign country), or their supply chains) and in such cases a nil FIRB approval monetary threshold applies; and

- (b) a foreign person needs FIRB approval to acquire a substantial interest (20% plus equity interest) if the target is:
 - (i) an Australian company carrying on an Australian business;
 - (ii) an Australian unit trust; or
 - (iii) a holding entity of either of them,

where the target is valued above the following thresholds:

Investor	Threshold	How calculated
<p><i>Agreement country investors</i> – An entity that is an enterprise or national of an ‘FTA Country’ (Canada, Chile, China, Hong Kong, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, South Korea, United Kingdom, USA and Vietnam) but excluding:</p> <ul style="list-style-type: none"> • acquisitions by their subsidiaries incorporated elsewhere, including an Australian subsidiary; • foreign government investors (who are subject to more stringent rules – see below); and • acquisitions of targets that operate a national security business or operate in sensitive sectors (which include media, telecommunications, transport and various military applications). 	A\$1,427 million, indexed annually	<p>The higher of:</p> <ul style="list-style-type: none"> • the total asset value for the entity; and • the total value of the issued securities of the entity
<p><i>Agreement country investors</i> – where the target is carrying on a sensitive business (which includes media, telecommunications, transport and various military applications) but excluding:</p> <ul style="list-style-type: none"> • acquisitions by their subsidiaries incorporated elsewhere, including an Australian subsidiary; and • foreign government investors (who are subject to more stringent rules – see below). 	A\$330 million, indexed annually	
<p>Foreign persons who are not agreement country investors or foreign government investors (the latter being subject to more stringent rules – see below).</p>	A\$330 million, indexed annually	

Special rules apply in a number of situations, including as follows.

- **(Foreign government investors)** There are different rules for investments by a foreign government investor compared with a private investor. Foreign government investors are subject to more rigorous screening than other investors – generally foreign government investors need FIRB approval to acquire a direct interest (which is generally a 10% or greater interest but may be less depending on the circumstances) in an Australian entity and there is no monetary threshold that applies. Many commercial investors that operate independently are counted as foreign government investors – not only sovereign wealth funds, public sector pension funds and state owned enterprises, but also many entities that have part government ownership upstream.
- **(Agribusiness)** All foreign persons making a direct investment (which is generally a 10% or greater interest but may be less depending on the circumstances) in an agribusiness for consideration of A\$71 million or more (including the value of any existing investment in that agribusiness) must obtain FIRB approval before proceeding. An agribusiness entity is one that:
 - derives earnings from carrying on one or more businesses in a prescribed class of agricultural businesses which represent more than 25% of the entity's EBIT; or
 - uses assets in carrying on one or more such businesses and the value of the assets exceeds 25% of the total asset value of the entity.
- **(Media sector)** Any acquisition by a foreign person of a direct interest (which is generally a 10% or greater interest but may be less depending on the circumstances) in an Australian media business requires FIRB approval.
- **(Land-rich entities)** Any acquisition by a foreign person of securities in an Australian land corporation or trust (being a corporation or trust where interests in Australian land account for more than 50% of the entity's total assets by value) requires FIRB approval where the value of the securities acquisition exceeds the applicable land monetary threshold. There is a nil

monetary threshold if the Australian land corporation or trust has 'national security land', which is generally land that is defence premises or where it is publicly known (or could be known upon the making of reasonable enquiries) that a national intelligence agency has an interest in the land. Other monetary thresholds could apply depending on the type of Australian land interests held. There are FIRB approval exceptions (in general terms) for acquisitions of less than 10% in an Australian land corporation or trust where there is no influence over management or policy.

Even where an acquisition of equity securities in an Australian company or unit trust does not trigger the mandatory FIRB approval requirements, the acquisition might still be considered a 'reviewable national security action' such that, if voluntary FIRB approval is not obtained, the acquirer is subject to the risk that at any time before the end of 10 years after the acquisition, the Treasurer exercises their call-in power to review the acquisition and make orders on national security grounds. If the acquirer decides to voluntarily seek FIRB approval, the receipt of FIRB approval should be a condition precedent to completion of the acquisition.

12.2 Competition clearance

Australia has a competition regime which is aimed at prohibiting anti-competitive trade practices and protecting consumers. The regime is set out in the *Competition and Consumer Act 2010 (Cth)* (the CCA) which is administered by a government regulator called the Australian Competition and Consumer Commission (the ACCC).

Section 50 of the CCA prohibits acquisitions of shares and/or assets that would have the effect or be likely to have the effect of substantially lessening competition in a market in Australia.² There are no minimum turnover or other thresholds, and acquisitions of any size (including of minority interests) could potentially be captured by the prohibition. Accordingly, section 50 applies to all acquisitions of shares or assets, regardless of whether they deliver 'control' of the target firm, if the acquisition leads to a substantial lessening of competition. Section

² The definition of 'market' includes a market for goods or services in Australia or in a region, territory or state of Australia, and can include local markets. The ACCC also recognises that markets can be global or regional in nature, and in such cases will examine the effect on competition in the global or regional market that exists within Australia.

50 may therefore apply to minority acquisitions where the acquisition gives rise to reduced competitive tension or the potential for coordination in the market by virtue of some overlap arising from the acquisition. The CCA contains a non-exhaustive list of factors that determine whether an acquisition may have the effect of substantially lessening competition. These include:

- potential constraints on the merged firm, such as the degree of import competition, the height of barriers to entry, and the degree of countervailing power; and
- the characteristics of the market – such as the nature and extent of vertical integration and the likelihood that the acquisition will result in the removal of a vigorous and effective competitor.

There is no compulsory notification requirement under the CCA. However, the ACCC expects to be notified of takeover and merger proposals in advance where the products or services of the relevant parties are either substitutes or complements and the merged group will have a post-merger market share greater than 20 per cent in a relevant market. In addition, where a takeover proposal will, or is likely to, raise competition concerns (eg. because it may raise horizontal, vertical or conglomerate effects concerns), the relevant parties should seek Australian competition clearance for the takeover. Foreign-to-foreign mergers can be captured by Australia's merger control regime, however, a local nexus or effects is required.³

The ACCC can investigate a merger even where a party has not notified it of the takeover or merger proposal. The ACCC has the power to apply for a court injunction to prevent a proposed transaction from proceeding. Where a transaction has been completed in breach of s50 of the CCA, the ACCC can also apply to the Federal Court for a range of remedies including a divestiture order, pecuniary penalties, director disqualification orders and/or an order declaring the transaction void. Third parties may also seek damages

There are two processes by which clearance can be sought from the ACCC:

- **(Informal clearance)** An informal clearance system has developed in Australia under which parties proposing to acquire shares or assets may approach the ACCC on an informal (and sometimes confidential) basis for clearance. It is the main method for obtaining

clearance in Australia. There is no set timeframe within which the ACCC must reach a decision but the ACCC has issued guidance on timing for informal reviews. As a general guide, if the ACCC decides that the takeover proposal does not raise any competition issues and does not require the ACCC to conduct market enquiries, the parties may be advised of this conclusion within about 2 to 8 weeks (depending on the complexity of the transaction). Reviews that require public market consultation and are subsequently found not to raise competition concerns will normally be completed within 6 to 12 weeks from the date the ACCC initiates the market consultation. When reviews require subsequent market inquiries to consult on a statement of issues (which outlines the basis and facts on which the ACCC has come to a preliminary view that a proposed merger raises competition concerns that require further investigation) or remedies, the total review process is likely to be completed within 6 to 12 weeks after the statement of issues is published, although may take longer in complex cases. Although informal clearance decisions are not legally binding on the ACCC, the ACCC will not, as a general rule, subsequently contest a merger which it has cleared, unless clearance was granted on the basis of false or misleading information or relevant information was withheld. The informal clearance process can be used for proposed as well as completed transactions.

- **(Merger authorisation)** There is a merger authorisation procedure that is also conducted by the ACCC. The ACCC may authorise a transaction if it determines that a merger is unlikely to substantially lessen competition, or where the public benefits of the transaction outweigh any public detriment (the latter test is not available in the informal clearance process described above). Where the ACCC authorises a merger and any conditions attached to the clearance are complied with, an action cannot be brought by the ACCC or third parties on the basis that the acquisition contravenes s50 of the CCA. If the ACCC makes a determination not to authorise the transaction, the parties may appeal to the Australian Competition Tribunal. The Tribunal can only review the ACCC's determination on the information that was originally before the ACCC, subject to limited

³ Foreign-to-foreign mergers can be captured under section 50 or section 50A of the CCA. Section 50 will apply to acquisitions that occur outside Australia if they involve bodies corporate incorporated in or carrying on business within Australia, or Australian citizens or persons ordinarily resident within Australia. It may be sufficient if the acquirer 'carries on a business in Australia' through a subsidiary or other representative, even though the acquirer itself has no direct operations in Australia. Section 50A will apply if a foreign-to-foreign merger results in a controlling interest being acquired in a corporation that carries on business in Australia. In both cases, there is a local effects test, which is whether the acquisition will have the effect or likely effect of substantially lessening competition in a market in Australia.

rights to introduce new material. The ACCC has a 90 calendar day time limit to deal with an application for formal clearance, with the option to extend this period multiple times with consent of the applicants. If no decision is made within this period, the ACCC is taken to have refused to grant the merger authorisation. The process involves the payment of a A\$25,000 application fee, and is more prescriptive, than the informal clearance process. For example, the application must include information and data as stipulated by the ACCC, as opposed to the informal process, which provides greater flexibility in the form of the submission. The merger authorisation process can only be used for anticipated transactions (as opposed to closed transactions). All papers

submitted to the ACCC by the applicants or third parties, including ACCC decisions, are published on the ACCC's website, subject to limited rights to redact commercially sensitive material. The merger authorisation regime may be attractive to parties content with such levels of transparency or where the parties consider they have strong public benefits arguments. A review directly to the Australian Competition Tribunal of a negative ACCC authorisation decision is another advantage of the authorisation regime (as this right is not available directly from an informal review where parties would need to apply to the Federal Court).

The following table contains an overview of key differences between the informal review and merger authorisation processes.

	Informal review	Merger authorisation
Effect of filing	Voluntary and non-suspensory	Voluntary and suspensory
Legal test	Substantial lessening of competition	Substantial lessening of competition or overwhelming public benefit
Timing	No statutory deadlines. ACCC provides its own indicative timelines: <ul style="list-style-type: none"> • Pre-assessment: 2-4 weeks • Phase 1: 6-12 weeks • Phase 2: 6-12 weeks 	30 calendar days (overseas mergers) or 90 calendar days (all other mergers) (both can be extended in limited circumstances)
Outcome	<ul style="list-style-type: none"> • Merger opposed • Merger not opposed • Merger not opposed subject to court enforceable undertakings 	<ul style="list-style-type: none"> • Authorisation application granted • Authorisation application dismissed (ie, not granted) • Authorisation application granted subject to court enforceable undertakings <p>The ACCC is required to publish reasons for its decision to dismiss a merger authorisation application.</p>
Publicity	<p>Transactions cleared in pre-assessment can be cleared confidentially.</p> <p>If there is a public review, a summary of the transaction will be published on the ACCC's website. The ACCC will consult with market participants for their views. Decisions to oppose or clear a merger are published (including conditions).</p>	The application, all third party submissions and the ACCC's decision are published, subject to some limited ability to request excisions for confidential / commercially sensitive information.

	Informal review	Merger authorisation
Effect of decision	No statutory immunity from third party challenges but ACCC is not likely to challenge if ACCC clears	Statutory immunity from ACCC and third party actions.
Appeal rights from refusal / opposition	No appeal from informal ACCC decision, but the parties may seek a Federal Court declaration that the transaction does not contravene s50 of the CCA or seek merger authorisation	Limited merits review of the ACCC's decision by application to the Australian Competition Tribunal

Parties involved in contentious mergers may be subject to additional scrutiny by the ACCC, which can issue s155 notices pursuant to compulsory information-gathering powers under the CCA. Section 155 notices issued during merger reviews could involve examinations under oath and/or significant information and/or document requests. Refusal or failure to comply with a section 155 notice (to the extent that the recipient is capable of complying with it) or knowingly providing information that is false or misleading to the ACCC, are criminal offences that may attract fines or even imprisonment for individuals.

Although there is no requirement for the parties not to complete a transaction when seeking informal clearance from the ACCC, parties generally do not proceed with transactions that are being considered by the ACCC until they obtain clearance. Takeover proposals which are the subject of an authorisation application cannot be completed until a decision has been made by the relevant authority. The authorisation application must be accompanied by a court-enforceable undertaking that the applicant will not complete the proposed acquisition until the ACCC's assessment is complete.

Even following the completion of the ACCC's assessment process, it remains important for the parties to the transaction to maintain their independence as separate competitors until transaction completion takes place. The prohibition on cartels in the CCA will continue to regulate conduct between purchaser and target until completion. Failing to act independently, or acting in a coordinated manner prior to closing, known colloquially as 'gun-jumping', may amount to a contravention of this prohibition.

Penalties for illegal conduct arising from gun-jumping increased five-fold in November 2022 and may now reach – for each contravention – a maximum of the greater

of A\$50 million (increased from A\$10 million) or three times the value derived from the relevant contravention, or, if the value derived from the breach cannot be determined, 30 per cent (increased from 10 per cent) of the company's turnover during the period it engaged in the conduct. Individuals face civil penalties of a maximum penalty of A\$2.5 million per contravention (increased from A\$500,000) or criminal penalties of a maximum of A\$500,000 (increased from A\$444,000) and/or a maximum of 10 years in jail (for cartel conduct).

This has implications for the permissible level (and kind) of coordination that parties to transaction agreements may engage in prior to completion in circumstances where the parties are competitors. In particular, this could include parties:

- agreeing to pre-closing guidelines between counterparties that commit each party to abide by their obligations under the CCA, and that clarify the purpose and scope of any pre-planning activities (including sharing of information);
- ensuring each transaction party maintains an independent 'face to market', preserving their own relationships with, and dealing independently with, their own customers and suppliers, especially regarding pricing;
- ensuring that each transaction party continues to make its own independent decisions about its strategy and conduct on the market. In particular, this means that pre-closing rights – giving a purchaser the ability to veto certain conduct of the target pre-closing - should be carefully reviewed;
- seeking competition law advice on any pre-closing conduct of business contractual obligations or notification requirements contained in transaction agreements to avoid illegally conferring control to the purchaser prior to completion; and

⁴ Statements of intention (eg that a shareholder will accept a takeover bid) can lead to a Takeovers Panel declaration of unacceptable circumstances for reasons independent of whether the statement is adhered to.

- ensuring there is no co-mingling of assets, transfer of employees, exchange of pricing information, sharing of customers or amalgamations of brands prior to closing.

Possible reforms to the competition clearance review process

In November 2023, the Competition Taskforce within the Australian Treasury issued a consultation paper (see [here](#)) outlining three possible options for change to Australia's merger laws.

- **Option 1, voluntary formal clearance:** businesses could choose to notify a merger (which would be suspended during the review) and the ACCC could grant immunity from court action if *satisfied* that the merger *would not* be likely to substantially lessen competition. Any review of the ACCC's decision would be by the Tribunal. This option reverses the burden of proof and requires the parties to show that the transaction *would not* be likely to substantially lessen competition, to the ACCC's satisfaction. Under the current merger regime the ACCC is required to show that the transaction *would* be likely to substantially lessen competition. Option 1 adopts aspects of the current merger regime in New Zealand and the United Kingdom.
- **Option 2, a mandatory suspensory regime:** businesses would be required to notify the ACCC of mergers above the threshold. The ACCC could also choose to investigate mergers below the threshold. The merger would be suspended for a period of time while the ACCC conducts its assessment. If the ACCC concludes that the transaction is likely to substantially lessen competition and the parties do not voluntarily abandon the merger, the ACCC would need to commence proceedings in the Federal Court to prohibit the merger. Option 2 is broadly based on the approach taken in the United States and Canada.
- **Option 3, a mandatory formal clearance regime:** businesses would be required to notify mergers above a certain threshold and the ACCC could 'call in' mergers below the threshold in certain circumstances. The merger would be suspended for a period of time while the ACCC conducts its assessment. The ACCC would grant clearance if it is *satisfied* that the merger *was not* likely to substantially lessen competition or with

consideration of the public benefits if a merger cannot be cleared on competition grounds. The ACCC decision would be reviewable by the Tribunal on the papers before the ACCC. Similar to option 1, option 3 shifts the burden of proof onto the parties, who are required to show the transaction is not likely to substantially lessen competition, to the ACCC's satisfaction. This is the reform option that the ACCC proposed.

The consultation on the merger reform proposals closed on 19 January 2024. A response by the Government is expected before June 2024. For Allens' coverage and analysis of the proposals, see [here](#).

12.3 Truth in takeovers policy

A feature unique to the Australian takeovers market is ASIC's 'truth in takeovers' policy. The policy is that where a market participant makes a public statement (known as a 'last and final statement') in the course of a takeover bid that they will or will not do something in relation to the bid, ASIC expects that the market participant will adhere to that statement unless they have clearly and expressly qualified it at the time of making it⁴. The Takeovers Panel generally expects likewise, although in practice it may grant alternative remedies to requiring strict adherence to a last and final statement (see below). A common example of a last and final statement is a statement by a takeover bidder that it will not increase its offer price or will not extend its bid. The policy only refers expressly to takeover bids, but ASIC and the Takeovers Panel regard it as extending to schemes of arrangement.

The truth in takeovers policy is unique because it is not founded on any specific rule that persons are bound by their public statements. Rather, the regulators consider that a person's departure from a last and final statement could be in breach of the misleading or deceptive conduct provisions of the Corporations Act. The rationale is that buyers and sellers of securities are entitled to rely on unqualified statements that a bidder, target or major shareholder will do or not do something in relation to the bid, and should not be exposed to loss if that party subsequently acts contrary to the statement. For example, if a bidder makes a statement that it will not increase its offer price and subsequently departs from that statement by announcing an increased offer price, a shareholder who

has sold on-market following the statement will have missed the opportunity to participate in the increase. Likewise, if a bidder makes a statement that it will not extend its bid and subsequently does so, a shareholder who has sold on-market may on the basis of the statement may lose the opportunity of an increased offer during the extended period.

The Takeovers Panel has shown a readiness to 'enforce' the policy and make declarations of unacceptable circumstances where a bidder has departed from a last and final statement. In particular, the Panel has in two cases declared unacceptable circumstances where a bidder has publicly stated that it would not increase its offer price but subsequently did so. In both cases, the Panel allowed the increased bid to proceed but ordered the bidder to compensate certain shareholders who traded in shares following the last and final statements. The Panel's decisions in those cases reflect a tension between upholding the truth in takeovers policy and ensuring that shareholders are not deprived of the best possible price for their shares.

The forum in which a last and final statement is made does not matter. An off-the-cuff comment by the CEO of a bidder to a journalist which is then published in a newspaper can attract the policy as much as a statement in an ASX announcement. Therefore, bidders, targets, major shareholders and other persons who play a significant role in a takeover proposal need to be careful in the public statements they make, and should seek legal advice before making any last and final statements.

12.4 Options and other convertible securities

Many ASX-listed Australian companies have employee incentive plans which involve the granting of share options or rights to executives. A person seeking to acquire ownership of all of a company's shares should make arrangements to acquire, or have cancelled, any options, rights and other securities convertible into shares. This is to avoid the highly undesirable situation where a bidder has acquired 100% of the company's shares but there remain options or rights on issue which, if exercised, would result in the issue of shares to the options or rights holders and the bidder ceasing to own 100% of the company. This is an issue because in that

situation the company's directors would need to take into the account the interests of the minority shareholders, and the company would be subject to the related party transactions restrictions in the Corporations Act. Furthermore, the exercise of the options or rights may, depending on the circumstances, cause the target to exit the bidder's Australian tax consolidated group.

The common methods for acquiring or cancelling options and rights (and other convertible securities) are as follows:

- if the control transaction proceeds via a takeover bid:
 - the bidder making a simultaneous takeover bid for each class of convertible securities; or
 - the bidder entering into contractual arrangements with each convertible securityholder and the target under which the convertible securities are to be transferred to the bidder or cancelled if the bidder obtains a relevant interest in more than 50% of the target's shares and the bid is unconditional; and
- if the control transaction proceeds via a scheme of arrangement:
 - the bidder proposing a simultaneous scheme of arrangement for each class of convertible securities; or
 - the bidder entering into contractual arrangements with each convertible securityholder and the target under which the convertible securities are to be transferred to the bidder or cancelled if the scheme becomes effective.

To avoid any collateral benefit or unequal treatment issues, the consideration provided for the acquisition or cancellation of convertible securities should be no greater than market value. For this purpose it is usual to undertake a Black-Scholes or other valuation of the convertible securities.

An alternative method of eliminating convertible securities is to compulsorily acquire them. In general terms, a person can compulsorily acquire a company's convertible securities if the person's voting power in the company is at least 90% and the person beneficially owns at least 90% by value of all the shares and convertible securities in the company. The consideration payable is normally the fair market value of the convertible securities.

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