



GUIDANCE NOTE 19: INSIDER PARTICIPATION IN CONTROL TRANSACTIONS

Overview

1. This Guidance Note provides takeover market participants with guidance on situations where there is involvement or potential involvement by the management, directors or external advisers of a target company¹ with the bidder² (**insiders** or **participating insiders** (see paragraphs 10 to 13 below)) in a takeover bid or potential bid for the target company (**bid**)³.
2. The Panel's primary concerns in those situations are to ensure that:
 - (a) consideration by the target board and management of the bid, and any competing proposal, is undertaken free from any actual influence, or appearance of influence, from participating insiders; and
 - (b) any disclosure of target company confidential information to the bidder or potential bidder is subject to appropriate controls.
3. This Guidance Note sets out when the Panel may declare circumstances arising from such situations to be unacceptable having regard to the purposes of Chapter 6 of the *Corporations Act 2001 (Act)*, set out in section 602 of the Act.

Panel's jurisdiction - directors' duties etc

4. There is considerable overlap between the issues which are discussed in this Guidance Note and directors' and employees' duties, employment law and the duties and terms of engagement of advisers. This guidance applies to these issues where they affect the principles set out in section 602 of the Act, including the maintenance of an efficient, competitive and informed market for a company's securities where the company is subject to a takeover bid.
5. The Panel expects that all relevant parties will comply with their legal, fiduciary and statutory duties (and seek advice on these as required), but its primary concern is to determine whether unacceptable circumstances exist in the context of a takeover bid, not to determine whether there has been a breach of directors' or employees' duties or other obligations under the law. The Panel does not regard it as being its role to determine and enforce such duties and obligations.
6. Market participants need to take care to consider and address all of the legal consequences and obligations that flow from control transactions with insider

¹ "Companies" include listed managed investment schemes and listed bodies.

² Bidder includes the bidder and its associates.

³In this Guidance Note, the term "bid" may include takeover bids, schemes of arrangements and other control transactions. The Panel recognises that the courts regulate schemes of arrangement. However, the issues discussed in this Guidance Note may arise in circumstances where the issues are not supervised by the court.

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participation. The circumstances discussed in this Guidance Note may also raise issues which extend beyond the scope of this Guidance Note. Merely because a person adheres to the policy discussed in this Guidance Note does not mean that their actions will be sufficient to comply with the person's broader legal obligations.

7. The discussion in this Guidance Note is not an exhaustive discussion on conflicts of interests and directors' duties generally and only addresses the topic in the context of the principles set out in section 602.

Private Equity and other buy-outs

8. The issues discussed in this Guidance Note are applicable to all takeover bids (irrespective of the source of funding). However, some of the issues have recently been brought to prominence by the increase in the number of private equity bids or other buy-outs which frequently have features which make this Guidance Note particularly relevant for such bids.
9. The Panel is concerned not to discriminate between private equity bidders and other types of bidders in its application of the principles set out in section 602 of the Act.

Participating Insiders

10. For the purposes of this Guidance Note, the term "**insider**" means either or both of:
 - (a) any officer or adviser of the target company who is in a position to influence the target's consideration of the bid;
 - (b) any person with significant non-public information in relation to the target or its business obtained through that person's role as an officer or adviser, or former officer or adviser, of the target company.
11. An entity which has such information through its role as an adviser to the target will not be regarded as an "insider" for the purposes of this Guidance Note where it is acting in a different capacity in relation to a bid or potential bid, if there are appropriate and effective Chinese walls in place and the significant non-public information is quarantined from that part of the entity which is so acting.
12. The term "**participating insider**" means insiders (as defined above) who are given an understanding by, or enter or propose to enter into an agreement with, a potential bidder that they will gain or benefit⁴ from the bidder making a successful bid, for example, by:
 - (a) acquiring equity in, or options or other derivatives or like interests over such equity in:
 - (i) the target;
 - (ii) the bid vehicle or a related entity;

⁴ Including obtaining a "financial benefit".

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- (iii) the bidder or a related entity;
 - (iv) another entity whose performance is related to the performance of the target; or
 - (v) funds managed by the bidder or related entities; or
- (b) agreeing to enter into, or forming an understanding about entering into, employment or other agreements that will apply if the target is acquired by the bidder and are reasonably likely to cause a real or perceived conflict of interest for the insider because of their value, for example significant levels of compensation, or cash or fee incentives, based on the performance of the target or elements of the target.⁵
13. The Panel intends that the description of participation should not include:
- (a) an offer by a potential bidder to continue the person's existing equity, compensation or other arrangements with the target or enter into new arrangements on similar terms to the existing arrangements⁶;
 - (b) fees or other arrangements entered into between the target and an adviser under which the adviser would gain or benefit from the bidder making a successful bid; or
 - (c) any participation in a control transaction which is on the same terms as afforded to all other shareholders in the target.

Addressing Potential Conflicts of Interests

14. The Panel considers that insiders should promptly inform the relevant sub-committee or the board of the target company of any approaches that might lead to a change of control proposal being tabled and obtain the relevant sub-committee or the board's consent before they provide any non-public information.
15. The Panel considers that it would be prudent for companies to make such requirements clear to their management and boards, and that bidders seeking to gain the support of insiders should also make any proposed discussions subject to such requirements.
16. As soon as the board of a company becomes aware or informed of a bid or potential bid for the company, in which there is, or is likely to be, participation by insiders, it should establish appropriate protocols. Normally this will involve appointing an independent board committee (**IBC**) consisting of those directors who are not participating insiders to oversee the application of these protocols and the process in the interests of target shareholders. Any directors

⁵ The Panel would be concerned if the spirit and intention of this Guidance Note were sought to be avoided by the timing of any understanding or agreement, or by making any agreement or understanding tacit.

⁶ The Panel would not consider new arrangements to be equivalent to the continuation of existing arrangements if the management receive cash or other benefits on termination of the existing arrangements i.e. new arrangements would not be viewed as "rolled over" if the management cash-out the old arrangements prior to entering the new ones with the bidder.

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who are participating insiders should not be present at, or participate in or vote on, any consideration by the board of the bid or any competing bid.

17. When considering what processes and protocols to adopt to manage the bidding and negotiation process and potential conflicts of interests of participating insiders, the IBC should have regard to the effect that any such processes and protocols could have on the interests of shareholders in order to ensure that the principles set out in section 602 of the Act are upheld. These include ensuring that:
 - (a) the acquisition of control over voting shares of listed companies takes place in an efficient, competitive and informed market; and
 - (b) the holders of shares in a company:
 - (i) know the identity of the person who proposes to acquire a substantial interest in the company;
 - (ii) have reasonable time to consider the proposal; and
 - (iii) have enough information to assess the merits of the proposal.
18. The protocols should seek to:
 - (a) establish rules concerning information disclosure and access, confidentiality and related matters;
 - (b) preclude influence by participating insiders on the target's response to any proposal (recognising that the IBC may need to obtain information from participating insiders, including to assist with the preparation of the target's statement and to comply with section 638 of the Act);
 - (c) ensure that the IBC has appropriate advice; and
 - (d) ensure that shareholders' best interests are advanced in the face of any proposal involving participating insiders, including through the IBC's approach or attitude to potential rival bidders and the proper ongoing conduct of the company's business during the period.
19. Because each situation is different, the Panel does not wish to prescribe what processes or protocols an IBC should adopt to manage potential conflicts of interests of participating insiders in order to ensure that the principles in section 602 of the Act are upheld. Where it receives an application, the Panel will examine the protocols adopted in each matter on a case-by-case basis. However, as an illustrative example, the Panel sets out some protocols that an IBC may adopt, where appropriate to a company's circumstances. Each IBC will need to consider and adopt protocols appropriate to its company's circumstances. Examples of protocols that an IBC may consider adopting include:
 - (a) informing participating insiders and bidders that the IBC will control any process and the degree of any involvement by participating insiders. To assist compliance with this, the IBC may require a representative of the target company to be present at all meetings between participating insiders and the bidder or potential bidder;

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- (b) requiring participating insiders to:
 - (i) cease communications or involvement with any bidder or potential bidder, except as permitted under the protocols established by the IBC; or
 - (ii) in appropriate circumstances, stand aside or resign from their management/board positions in order to pursue the proposed bid (recognising that certain legal and equitable obligations, including with respect to confidentiality and use of information may continue notwithstanding such resignation and subject to the board's ongoing right to require assistance from those insiders during any leave of absence);
 - (c) advising participating insiders that they must not provide any corporate information⁷ to anyone⁸ without the express approval of the IBC and following entry into an appropriate confidentiality agreement between the target company (represented by the IBC) and the person;
 - (d) requiring that none of the participating insiders discusses the bid or any competing proposal with customers, suppliers or other employees of the target company unless specifically requested to do so by the IBC, and only on terms and conditions approved by the IBC; and
 - (e) requiring participating insiders to disclose to the target company any material "non public" information about the target company which they have provided to the bidder or potential bidder with whom they are or may be involved.
20. In addition, the Panel would normally expect that an IBC would adopt processes and protocols to monitor, manage and control the flow of information to all actual and potential bidders, including those that are involved with participating insiders.
21. The Panel is more likely to find that unacceptable circumstances exist where appropriate protocols have not been established and followed to ensure that:
- (a) potential conflicts of interest are adequately addressed; and
 - (b) an efficient, competitive and informed market for control of securities of the target, and the principles set out in section 602, are upheld.
22. The Panel notes that the above discussion is not an exhaustive discussion on conflicts of interests generally and only addresses the topic in the context of the principles set out in section 602. Market participants should note that solely complying with the example protocols discussed above may not necessarily be adequate or sufficient in terms of their duties and responsibilities to manage all conflicts of interests faced by participating insiders. Market participants should also note that, in certain instances, ratification of a participating insider's conflicts of duties by a target board, for example through the participating

⁷ including the existence of any potential bidder or the details of any potential bid.

⁸ including any employee, customer or supplier of the target.

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insider obtaining the board's consent or following the IBC's protocols, may not be adequate or sufficient to cure a breach of that insider's duties.

Provision of Information to Potential Rival Bidders

23. There is currently no general requirement that a target company must provide equal access to information about the target company to rival bidders. In *Goodman Fielder 02* [2003] ATP 5, the sitting Panel considered that Goodman Fielder directors needed to explain to their shareholders why they had given access to rival bidders but not Burns Philp, "both to resolve the apparent anomaly and to provide additional information about the bid process" [para 96]. The Panel considers that the principles enunciated in *Goodman Fielder 02* continue to be appropriate principles.
24. The Panel would normally expect that, in circumstances where target directors have not provided equal access to information to potential rival bidders, they would have sound reasons for their decision⁹, given the effect or potential effect of their decision on an efficient competitive and informed market for the target company and its securities that a selective release of such information to some (but not all potential bidders) by the target company may cause¹⁰.
25. If participating insiders are involved in a takeover bid or potential takeover bid, and other potential bidders are given less information than that given to the bid involving participating insiders, the Panel, if it receives an application, would likely scrutinise closely the circumstances, and reasons given by target directors in support of their decision to withhold that same information from the other potential bidders (and especially where the bid involving participating insiders is recommended by the target board). This is to ensure that the reasons and the outcome are consistent with the purposes of Chapter 6, and in particular, with the existence of an efficient, competitive and informed market for the securities in the target company.

Disclosure to Shareholders

26. The IBC should carefully consider all information provided to any potential bidder to determine whether such information should be included in the target's statement so as to give target shareholders enough information to enable them to assess the merits of the proposal. The Panel considers that, as a general principle, the target should seek to ensure that a bidder who is involved with participating insiders does not have an advantage over shareholders in relation to material information about the target company¹¹. For example, a target should carefully compare the level and detail of information which was provided to the bidder against the level of information disclosed in the target's statement.

⁹ *Goodman Fielder 02* [2003] ATP 5 at [96].

¹⁰ An effect on the efficient, competitive and informed market for securities of the company will, necessarily, have some effect on the interests of shareholders of the company.

¹¹ Such information advantage may include forward looking information.

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27. Similar requirements clearly also apply to a bidder who receives information from the target or from participating insiders. A bidder should consider the information to be disclosed in its bidder's statement very carefully. For example, a bidder should carefully compare the level and detail of information which was provided to the financiers to the bid against the level of information disclosed in the bidder's statement.
 28. The bidder and the IBC should ensure that there is adequate disclosure to target shareholders, whether in the bidder's statement or target's statement, including information as to:
 - (a) the identity of any participating insiders;
 - (b) details of any incentive, participation and fees offered to participating insiders;
 - (c) the process, and the protocols adopted by the IBC to address potential conflicts of interest; and
 - (d) the identity of the persons behind a bidder to the extent required by sections 602.
 29. The Panel is more likely to find that unacceptable circumstances exist where target shareholders have not been given adequate information or where a bidder that is involved with participating insiders has an advantage over shareholders in relation to material information about the target company, because of the information that it has received from the target company or from participating insiders.
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