



Insider Participation In Control Transactions – Public Consultation Response Statement Dated 7 June 2007

INTRODUCTION

On 21 February 2007, the Takeovers Panel released a draft Guidance Note on Insider Participation in Control Transactions (GN) and an accompanying Issues Paper for public comment. Comments on the draft GN and the Issues Paper were due by 6 April 2007.

The Panel received fifteen submissions in response to the GN. The Panel thanks the authors of these helpful submissions for their interest and valuable feedback.

Consistent with the Panel's published policy on responding to submissions, this paper sets out the Panel's response to the public consultation process and its conclusions on the material comments received from respondents. Due to the large number of comments received, the Panel has not sought to address each individual comment.

MATERIAL COMMENTS RECEIVED AND PANEL'S CONCLUSIONS

General comments

Comment

The large majority of the submissions supported the issue of the GN and thought that it would assist market participants and advisers in addressing insider participation issues.

Two respondents expressly did not support the issue of the GN for reasons including that existing statutory and case laws dealing with the duties of officers, employees and advisers and evolving market norms are sufficient to ensure that insider bids take place in an efficient, informed and competitive market.

However, one of these respondents acknowledged that the issue of the GN may assist a sitting Panel to deal with similar issues that may arise in an application and may be of some assistance to companies and their advisers dealing with these issues.

Panel Response

The Panel acknowledges that circumstances described in the GN may raise issues under existing statutory provisions and directors' duties at the same time as raising control issues for the Panel. However, the focus of the GN is solely on the application of the principles in section 602 to insider participation in control transactions and general market response is that the Panel's guidance in this area would be useful.

Comments

Two respondents thought that the GN should include a clear statement upfront regarding the obligations under common law and statute for directors and officers and prominent warnings that the GN only deals with policy considerations under section 602.

Panel Response

The Panel has expanded its existing statement in the published GN to emphasise that the circumstances discussed in the GN may also raise issues under other parts of the Corporations Act or other areas of the law, and market participants need to take care to consider and address all of the legal consequences and obligations that flow from control transactions with insider participation.

Panel's Jurisdiction

Generally, respondents agreed with the approach taken by the Panel in relation to its jurisdiction.

Private equity and other buy-outs*Comment*

One respondent thought that paragraph 8 of the draft GN indicated potential for the Panel to adopt a differential or discriminatory approach to PE bids where warranted for policy reasons.

Panel Response

The Panel has deleted the reference in this paragraph.

Definition of "insiders"*Comment*

Some respondents submitted that "insiders" should only include those people who may be able to influence the target's consideration of the bid rather than those who only have access to confidential information about the target.

Others submitted that the definition should apply only to insiders who have a significant financial stake in the bidder or will otherwise gain a financial benefit from the success of the bid.

Panel response

The Panel did not consider that it is appropriate to limit the guidance only to those who are able to influence the target's consideration of the bid. The Panel considered that participation by people who have access to confidential information about the target company may also give rise to unacceptable circumstances. For example, key employees of a target company, who may not in a position of influence with the target board, may still have useful non-public information about the target which can be passed to potential bidders in the event that those employees decide to participate with the bidders.

Comment

Some respondents were concerned that the definition of "insider" included "financial and other advisers of the company". Some thought that advisers should not be included in the definition as they will not, simply by virtue of their advisory role, have an ability to influence decision-making.

One respondent submitted that the Panel should be careful to ensure its guidance does not disqualify advisers from subsequently participating in a bid for a former

client when it is not strictly necessary for an efficient, competitive and informed market that they should be excluded.

Panel response

The Panel has included an exception for former advisors in the published GN which should address the concern about their inclusion in the definition.

However, the Panel considered that advisors are quite likely to have the types of influence or knowledge that the GN is concerned to ensure does not affect an efficient competitive and informed market for securities. While accepting that advisors are not decision makers themselves, the Panel thinks that advisers do have influence on decisions made by target companies in takeovers. The Panel considers that directors are best equipped to assess whether advisors to the company have information or influence which may adversely affect the efficient competitive and informed market for the securities of their companies, and will be best able to manage those issues by the protocols they put in place for their specific circumstances.

Comment

One respondent was concerned that in the absence of an express exception, it is not clear that the definition would exclude retail banking services (including funding) or general advisory services that are provided by a bank in its usual course of business. It is not clear that the bank could provide banking or other advisory services to a bidder on a commercial arms' length basis.

Panel response

Although the Panel considered that the type of service described by the respondent was not within the definition of insider in the draft GN, the Panel has included a carve-out in the published GN to address this concern.

Definition of "participating insider"

Comment

A few respondents submitted that the definition of 'participating insider' should be limited to insiders with a material financial stake in the bidder or in the outcome of the bid.

Response

While the Panel considered that only interests that are material will be likely to give rise to unacceptable circumstances, the Panel considered that initially it would be wise to include in the definition all insiders who would benefit from the bidder making a successful bid and, if later experience indicates it would be appropriate, the Panel may amend the definition of participating insiders to limit it to those insiders who have material interests in the outcome.

Comment

One respondent submitted that the following scenarios should not, of themselves, lead to a person becoming a "participating insider":

- where an insider has employment arrangements with a bidder (unless they involve materially different equity participation rights);

- an invitation to target directors to join the bidder's board.

Response

The Panel considers that the first point is addressed in the final GN paragraph 13(a). The Panel considers that the second point could raise the types of issues which the GN seeks to address and should not be excluded.

Comment

One respondent submitted that the definition should not include insiders who receive a benefit from the transaction if they are not actively participating, for example, directors may have pre-existing options that are triggered as a consequence of the transaction.

Panel's response

The Panel looked at the situation where options become exercisable in the event of a bid. This would not be caught by the definition since nothing is acquired from the bidder. The Panel also looked at the situation where the bidder provides options to the director. That situation could raise the type of issues which the GN seeks to address. The Panel has included a new paragraph in the published GN (paragraph 13(c)) which addresses 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

Comment

One respondent submitted that the section might cause insiders to conclude mistakenly that the GN deals with conflicts generally, rather than being limited to Chapter 6 considerations. They were concerned that this section might create the impression that conflicts can be satisfactorily dealt with by getting the board's consent and following the procedures established by the IBC.

Panel's response

The Panel has clarified that:

- the GN does not set out 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 will need to consider all of the legal consequences that flow from a takeover bid with insider participation, not just Chapter 6 issues; and
- ratification by the target board will not be sufficient to cure all breaches of duties.

Comment

A number of respondents submitted that paragraph 12 in the draft GN was too restrictive or prescriptive. They submitted that, in reality, many companies often receive high level, informal enquiries from potential strategic or financial acquirers that may not eventuate into any firm proposal. They submitted that over-regulation in relation to initial approaches may diminish competition and the number of potential takeover bids.

Panel response

The Panel has deleted the reference to insiders informing the board as soon as they are approached by a potential bidder. The Panel confirms that it considers that insiders should promptly inform the board or relevant sub-committee 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. =

Protocols*Comment*

A number of parties stated the view that it is not possible to have a 'one size fits all' approach in dealing with potential conflicts and that boards should be free to exercise judgement as to what is the appropriate response for the company. Some respondents submitted that it would be preferable that the issues be dealt with on a case by case basis, having regard to a number of key principles.

Panel response

The Panel considered that it had clearly stated that the protocols discussed in the draft GN were only examples and that decisions as to what protocols were appropriate for individual companies were for the boards of those companies in the particular circumstances in which they found themselves. However, the Panel has clarified that directors should adopt protocols which the directors consider are appropriate for their companies on a case by case basis and that the Panel, where it receives an application, will adopt a similar case-by-case approach.

Comment

A number of parties were concerned that the illustrative examples of protocols (paragraph 18 of the draft GN) may be viewed as best practice or that they will become a de-facto standard, the departure from which a target company must justify.

Panel response

The Panel does not intend that parties need to justify departures from the example protocols. The Panel has emphasised its original guidance that each target board will need to consider and adopt protocols appropriate to its company's circumstances and that the examples are not intended to be any form of de facto standard.

Comment

Some respondents were concerned about the example protocol that management should "stand aside or resign".

Panel response

The Panel has emphasised that the example protocol, like the others, was for directors of the IBC to consider in light of their company's particular circumstances.

Comment

One respondent submitted that the example in paragraph 18(e) of the draft GN was too prescriptive. It should require participating insiders to disclose to the IBC what

material non-public information, if any, the participating insider has provided to the bidder.

Panel response

The Panel has adopted this suggestion.

Comment

In response to question 18(c) in the Issues Paper, a number of respondents submitted that there should be no requirement to conduct an actively managed auction or other form of competitive process.

Panel response

The Panel considers that the responses are consistent with its initial views on the matter and therefore does not propose to include any such requirement in the published Guidance Note.

Information to potential rival bidders

Comment

Some respondents expressed uncertainty as to whether the principles in Goodman Fielder 02 in relation to access to information about the target company to potential rival bidders, continue to apply.

Panel response

The Panel has clarified that it considers the principles in Goodman Fielder 02 continue to be appropriate.

Disclosure to shareholders

Comment

A number of respondents submitted that section 638 is adequate to address disclosure issues and that the overriding principle should remain whether or not that information is material to a shareholder's decision. A number of respondents were concerned that there may have been an implication in paragraph 23 of the draft GN that a target company be required to release the same information to shareholders as provided to bidders with insider participation.

Panel's response

The Panel does not consider that the draft Guidance Note stated or implied that a target company be required to release the same information to shareholders as provided to bidders with insider participation. However, the Panel has clarified that a 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 company but that this does not require that target shareholders be provided exactly the same data as provided by the target to a bidder.

Comment

Some respondents submitted that whilst a target may decide to provide, on a confidential and no-reliance basis, an indicative, qualified set of management projections to a potential bidder who is associated with a participating insider, it may

be misleading to disclose the same information to shareholders or the information may need to be so qualified as to be confusing or immaterial.

Panel response

The Panel considers that the concerns expressed (i.e. that the appropriate qualifications to such information would make it confusing or immaterial to target shareholders) are unfounded.

The Panel considers that where a potential bidder requires particular information such as management projections prior to finalising the terms of an offer, the information is likely to be material to target shareholders.

The Panel acknowledges the concerns of some respondents that requiring such information to be provided to target shareholders might chill the flow of information from targets to bidders, and that this may reduce the number of takeovers that are made. However, the Panel does not accept that bidders should be given more material information than target shareholders.

The Panel's view on such information is similar to that discussed above i.e. target shareholders are likely to reasonably expect to be provided with the material information provided to potential bidders but there is no requirement for the target to replicate exactly in the target's statement all of the information provided to a potential bidder.