Australian Government
Takeovers Panel

Attachment: Comparisons

Guidance Note 7 – Lock up devices

Introduction

1. This guidance note has been prepared to assist market participants understand the Panel's approach to lock-up devices.[1] It applies in control transactions, including takeovers. For convenience, the terms 'bid', 'bidder' and 'target' are used. The types of lock-up devices addressed might also be referred to as 'deal protection' measures.

   Examples: asset lock-ups, break fees, no-shop agreements, no-talk agreements

[1] Considered by the Panel in many matters, for example: *Normandy Mining Limited (No. 3)* [2001] ATP 30, 20 ACLC 471; *Ballarat Goldfields NL* [2002] ATP 7, 41 ACSR 691; *Ausdoc Group Limited* [2002] ATP 9, 42 ACSR 629; *Sirtex Medical Limited* [2003] ATP 22; *National Can Industries Limited* [2003] ATP 35, 48 ACSR 409; *National Can Industries Limited 01R* [2003] ATP 40, 48 ACSR 427; *Axiom Properties Limited 01* [2006] ATP 1; *Wattyl Limited* [2006] ATP 11; *Magna Pacific (Holdings) Limited 02* [2007] ATP 03; *Queensland Cotton Holdings Limited* [2007] ATP 05

2. The ~~discussion is~~principles discussed in the note are of general application and can be applied to any arrangement which has the effect of fettering the actions of a target, a bidder or a substantial shareholder.

3. The examples are illustrative only and nothing in the note binds the Panel in a particular case.

4. ~~3.~~ The policy bases for this note are that lock up devices may:

   - inhibit the acquisition of control over voting shares taking place in an efficient, competitive and informed market or
   - deny holders of the relevant class of shares a reasonable and equal opportunity to participate in the benefits of a proposal under which a person may acquire a substantial interest.

~~Devices generally~~

5. ~~4.~~ In this note the following definitions apply:

Term	Meaning
asset lock-up	an arrangement between a bidder and target for the sale, purchase or encumbrance of ~~a target~~an asset in exchange for • proposing a bid or other control transaction or • a period of exclusivity or the opportunity to undertake due diligence for a control transaction
break fee	consideration however payable by a target if specified events occur which prevent a bid from proceeding or cause it to fail[2]
'fiduciary' out	a provision which allows the directors of ~~one~~a party to ~~terminate~~be relieved of a lock up obligation (or aspects of it) if their ~~fiduciary~~ duties require them to do so
lock-up device	an arrangement that encourages or facilitates a ~~bid, scheme of arrangement or other~~

[2] Generally, this is because the target shareholders decline the offer or fail to approve the merger, or the target receives a superior proposal from a rival bidder. These events will typically be outside the control of the bidder, but not necessarily of the target or its shareholders. See also paragraph 12

Term	Meaning
	~~shareholder-approved~~control transaction[3] ~~by~~and potentially hinders another actual or potential control transaction *Example: 1 By* ***imposing a restriction on actions of the target (or a shareholder), as in a no shop agreement or no talk agreement*** ***2. By providing for compensation if the control transaction does not proceed, as in a break fee***
~~no-due-diligence agreement~~	~~an arrangement under which a target will not allow a rival bidder, or potential bidder, to conduct due diligence on it without the initial bidder's consent~~
~~no-shop agreement~~	~~an arrangement under which a target (or a shareholder) will not solicit a bid or other control transaction from a third party~~
~~no-talk agreement~~	~~an arrangement under which a target will not negotiate with another bidder or potential bidder, even if the approach is unsolicited~~

Devices generally

6. ~~5.~~ Lock-up devices are ~~sometimes referred to as deal protection measures~~not unacceptable as such. They may help secure a proposal[4] by protecting against costs (opportunity and expended) ~~costs~~ that would not be recoverable if the transaction did not complete. They may reduce the bidder's risk that the target will not complete the ~~control transaction. They~~proposal. However, they may also deter rival bidders.

7. ~~6. Lock-up devices are not unacceptable as such.~~ Whether any lock-up device gives rise to unacceptable circumstances will depend on its effect or likely effect, having regard to s602 ~~(particularly s602(a))~~ and

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~~3 See item 7 of s611~~

3 Including shareholder approved transactions under item 7 of s611

4 For example, induce the first bidder to bid or a subsequent bidder to compete

s657A.[5] The Panel will look at the effect or likely effect of the device on:

(a) competition involving current or potential bidders, and whether it is significant and

(b) ~~coercion of~~ shareholders~~. This is~~ and whether they may be substantially coerced into accepting the bid (ie, the tendency to ~~adversely affect~~diminish the value ~~or nature~~ of the company if shareholders~~' investment (via their shares) if they~~ do not accept).[6] ~~A fee payable on control passing to a counter-bidder is unlikely to be coercive because the counter-bid supplants the original proposal.~~

~~7. The Panel expects that the target's directors will be able to explain the process they undertook in considering the lock-up device, including any advice taken. Relevant factors include:~~

~~(a) the stage the transaction had reached when the device was negotiated~~

~~(b) whether other interest had been canvassed~~

~~(c) the bargaining power of each party~~

~~(d) the size and complexity of the transaction~~

~~(e) the likely (opportunity and expended) costs involved and~~

8. ~~(f) ancillary provisions in the agreement.~~ The Panel looks at the substance of the ~~agreement~~lock-up device over its form.

~~8. Regardless of whether a lock-up device is unacceptable it may be void or unenforceable, for example because it contravenes the law relating to directors' duties, reductions of capital, or financial assistance.~~

Break Fees

The 1% guideline

9. ~~A break fee might be viewed as an option fee paid to secure a proposal for a target (or shareholders) to consider.~~ In the absence of other factors, a break fee not exceeding 1% of the equity value of the target[7]

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[5] Unless otherwise indicated, references are to the *Corporations Act 2001 (Cth) 2001*

[6] For example, ***Ausdoc Group Limited*** [2002] ATP 9 at [44] and ***Ballarat Goldfields NL*** [2001] ATP 7 at [14]-[16]

[7] The aggregate of the value of all classes of equity securities issued by the target having regard to the value of the bid consideration when announced. In limited cases, it may be appropriate for the 1% guideline to apply to a company's enterprise value, for instance because the target is highly geared

is generally not unacceptable.[8] There may be facts which make a break fee within the 1% guideline unacceptable - for example if triggers for payment of the fee are not reasonable (from the point of view of coercion).[9] In the absence of other factors, reasonable triggers might include:

~~10. If excessive, a break fee risks being anti-competitive (to an alternate proposal) or coercive (to shareholders minded to reject the proposal).~~

- a change of directors' recommendation (but it might be unreasonable for the trigger to be a change of recommendation because of a breach of the implementation agreement by the bidder, or a condition precedent outside the target's control not being satisfied, or an expert opining that the transaction is not fair and reasonable)
- a competing transaction that successfully completes
- a material condition precedent within the target's control not being satisfied or
- a material breach within the target's control
- other events affecting the bid (eg, a major asset of the target is destroyed).

10. ~~11.~~ In considering whether a break fee gives rise to unacceptable circumstances, the Panel is guided by the following (among other things):

~~(a) whether the fee is demonstrably not anti-competitive because, for example, another bidder has increased its bid or a new bid has been proposed since it was announced[7]~~

~~(b) whether the fee exceeds 1% of the equity value of the target.[8] In the absence of other factors, a 1% fee is generally not~~

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[8] ***National Can Industries 01(R)*** [2003] ATP 40 at [33]. Note however that an applicant may be able to establish that the fee is anti-competitive or coercive despite being less than 1%

[9] "Naked no vote" break fees (ie fees payable by a target to a bidder if the takeover is rejected by the target's shareholders even though there is no competing bid) may fall into this category. See *Ausdoc Group Ltd* [2002] ATP 9 at [43]

~~[7] In ***Normandy Mining Limited (No. 3)*** [2001] ATP 30, the break fee was approximately 1% of equity value, which might have been excessive because of the large size of the bid, but for a counter-bid~~

~~[8] The aggregate of the value of all classes of equity securities issued by the target having regard to the value of the bid consideration when announced. In limited cases, it may be appropriate for the 1% guideline to apply to a company's enterprise value, for instance because the target is highly geared~~

~~unacceptable[9] If the fee exceeds 1%, the Panel must be satisfied that it is not anti-competitive or coercive~~

(a) ~~(c)~~ whether the fee was agreed after a public, transparent process designed to elicit proposals[10]

(b) ~~(d)~~ whether the proposal was solicited by the target

(c) whether the fee is fixed or capped (either in dollar or percentage terms) ~~and~~

(d) whether the fee (on a cost per share basis) is less than the premium under the bid[11]

(e) the cost, effort or risk involved in making the proposal

(f) whether the fee reimburses actual expenses

(g) whether another bidder has increased its bid or made a bid and whether the fee was material in determining the price that the competing bidder was prepared to pay.[12] In this case the fee may not be anti-competitive.

(h) any other relevant factors, such as whether the obligation is limited to a reasonable period.

11. ~~12.~~ Multiple fees (with a party and its associates in respect of the same or related transactions) ~~may~~are likely to be aggregated for the purpose of the 1% guideline.~~11~~[13]

~~Fiduciary out~~

Timing

12. ~~13. A fiduciary carve out for a break fee is usually unworkable, so not required. However, target directors must make decisions in the best interests of the company on the basis of the information available after reasonable enquiry.[12] They should consider whether it is~~It may be appropriate to delay entry into a break fee agreement, or incorporate a 'fiduciary' out, if an event ~~beyond their control~~ that might trigger payment of the fee is ~~outstanding.[13]~~imminent.

~~[9] *National Can Industries 01(R)* [2003] ATP 40 at [33]~~

[10] ***Ausdoc Group Ltd*** [2002] ATP 9

[11] ***Ausdoc Group Ltd*** [2002] ATP 9 at [35(f)]

[12] In ***Normandy Mining Limited (No. 3)*** [2001] ATP 30, the break fee was more than 1% of equity value, which might have been excessive because of the large size of the bid, but for a counter-bid

~~11~~[13] *National Can Industries 01 and 01R.* Contrast *Ausdoc Group Limited*

~~[12] *Normandy Mining Limited 03* [2001] ATP 30 at [40].~~

Example: Negotiating a break fee payable if a director changes his or her recommendation shortly before an expert's report on which the recommendation will be based is due, when the directors could have waited, may give rise to unacceptable circumstances.[14]

Restriction agreements

Agreements

13. Restriction agreements restrict the ability of the target (or shareholder) to act. The possible effect of one or more restrictions in a restriction agreement may be anti-competitive and give rise to unacceptable circumstances.

14. ~~There are different types of restriction~~Restriction agreements~~, which~~ may be coupled with notification obligations[15] or matching rights. [16] These may increase the anti-competitive~~, namely (in increasing order of restrictive~~ effect~~):~~.

    - ~~no-shop agreements~~
    - ~~no due diligence agreements and~~
    - ~~no-talk agreements.~~

15. A notification obligation reduces the likelihood that a competing bidder will want to make an approach, and may even act as a restriction agreement in its own right. It must be limited and reasonable in the circumstances. It may be subject to a fiduciary out so that details of the competing proposal need not be passed on. Limiting the disclosure reduces the anti-competitive effect. If it is simply the fact of an approach that is passed on, there may be little increase in effect.

16. Notification may also be coupled with a matching right. A matching right will be less anti-competitive if the competing bidder has a reasonable opportunity after the original bidder has matched its bid to increase its offer. A matching right will be more anti-competitive if the matching right includes an obligation to provide the original bidder with details of negotiations with the subsequent potential bidder.

~~13~~ [14] ***National Can Industries Limited 01*** [2003] ATP 35 at [41] and ***National Can Industries Limited 01(R)*** [2003] ATP 40 at [37]

[15] A provision that requires the target (shareholder) to disclose details of any potential competing proposal to the original bidder

[16] A provision that allows the bidder to match the third party deal proposed to the target

17. Restriction agreements may have a less anti-competitive effect if coupled with a window-shop provision,[17] go-shop provision[18] or market-check provision.[19] Such provisions should allow a reasonable period to 'shop' the target. They should not unreasonably constrain any 'fiduciary' out that might be coupled to a particular restriction.

18. In considering whether unacceptable circumstances arise, the Panel also considers the potential benefits to target shareholders of the agreement and the reasons why target directors are satisfied of the commercial and competitive benefits to shareholders of entering the agreement.

Types of restrictions

No-Shop ~~Agreements~~restriction

19. ~~15. No-shop agreements are less anti-competitive than no-talk agreements. They only prevent~~A no-shop restriction prevents the soliciting of alternatives, usually during a defined period of exclusivity. ~~Provided~~The longer the period ~~of restraint is limited and reasonable,[14] the Panel generally does not consider that a fiduciary out is needed.~~ the more anti-competitive is the effect of the restriction. Normally the period would not extend into the bid period but it may do so if justifiable having regard to the advantages the agreement offers target shareholders.

20. While a simple no-shop restriction does not prevent the target (or shareholder) dealing with unsolicited approaches (and therefore if it is limited and reasonable may not require a 'fiduciary' out), it is sometimes coupled with a notification obligation. This increases the anti-competitive effect (which may be reduced by limiting the information required to be passed on).

21. Whereas a limited and reasonable no-shop restriction generally does not require a 'fiduciary' out, being less anti-competitive than a no-talk

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[17] A provision that the target cannot actively solicit offers, but can consider unsolicited offers, give the potential offeror information and accept the offer if necessary to avoid a breach of fiduciary duty

[18] A provision that allows the target (or shareholder) a reasonable set time in which it can 'shop' the market

[19] A provision allowing the target to announce that it will entertain third-party interest for a reasonable set period, after which it proposes to deal with the bidder. Used, for example, in management buy-outs as a way of testing the fairness of the proposal by proving the market for other offers. A fiduciary out should still allow alternative proposals.

~~[14] It may extend into the bid period if justifiable having regard to the advantages the agreement offers target shareholders~~

restriction, the Panel is likely to treat it like a no-talk restriction if, for example:

(a) ~~16. The Panel will look at the substance of the agreement over its form.[15] For example, if~~ the wording does not clearly permit the target to respond to an alternative proposal or enquiry~~, the Panel is likely to treat the agreement in the same way as a no-talk agreement.~~ or

~~17. No-shop agreements are sometimes coupled with an obligation on the target (or shareholder) to disclose details of any competing proposal. This may increase the restrictive effect.~~

~~18. Potentially less restrictive variations[16] of no-shop agreements include:~~

~~(a) "Window-shop agreements". While the target cannot actively solicit offers, it can consider unsolicited offers, give the potential offeror information and accept the offer if necessary to avoid a breach of fiduciary duty~~

(b) ~~"Go-shop agreements". Allows the target (or shareholder) a set time in which it can 'shop' the market. It may include a break-fee during the go-shop period, which may increase once the go-shop period ends~~ it is coupled with a notification obligation to inform the original bidder of subsequent approaches that is too extensive (eg, requires all the details of the negotiations and does not have a fiduciary out).

~~(c) "Market-check agreements". Allows the target to announce that it will entertain third-party interest for a set period, after which it proposes to deal with the bidder.[17] They may be used in management buy-outs as a way of testing the fairness of the proposal by proving the market for other offers and~~

~~(d) "Matching right agreements". Allows the bidder to match the third-party deal found by the target.~~

No due diligence ~~agreements~~restriction

22. A no-due-diligence restriction prevents a target passing information to a potential competing bidder as part of due diligence without the

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~~[15] In ***Queensland Cotton Holdings Limited 02*** [2007] ATP 05, the board interpreted the agreement strictly and considered itself unable to respond to an inquiry that might have led to an alternative proposal. The Panel accepted undertakings the effect of which allowed the board to respond to a proper inquiry~~

~~[16] Such agreements may still give rise to unacceptable circumstances~~

~~[17] A fiduciary out should still allow alternative proposals~~

consent of the original bidder. Its anti-competitive effect is similar to a no-talk restriction.

23. ~~19. A no due diligence agreement is an agreement not to pass on information, similar to a no-talk agreement. It might also incorporate an obligation to provide details of any approaches regarding alternative proposals to the original bidder.~~ It might also incorporate a notification obligation, which may increase the anti-competitive effect.

24. ~~20.~~ Safeguards ~~and~~ (including 'fiduciary' outs) applicable to no-talk ~~agreements~~restrictions apply similarly to no due diligence ~~agreements and other similar agreements~~restrictions and like restrictions affecting dealings with potential rival bidders.

No-talk ~~agreements~~restriction

25. A no-talk restriction prevents a target negotiating with any potential competing bidder. It might be graduated from the least restrictive form (allowing negotiations if the approach was unsolicited) to the most restrictive form (no negotiations, even if the approach was unsolicited).

26. ~~21. No~~A no-talk ~~agreements are~~restriction is more anti-competitive than~~, for example,~~ a no-shop ~~agreements~~restriction. Therefore~~:~~ the safeguards need to be more stringent.

~~(a) the safeguards need to be more stringent. A fiduciary out is essential. The fiduciary out must be available to target directors in practice.[18]~~

~~(b) the benefits to target shareholders need to be greater or more certain. Target directors need to be convinced of the commercial and competitive benefits to their shareholders before agreeing to this form of agreement and~~

27. ~~(c)~~ In the absence of an effective 'fiduciary' out, a no-talk restriction is likely to give rise to unacceptable circumstances. Even with a fiduciary out, the period of restraint must be limited and reasonable~~.[19] Generally,~~.[20] However, generally a no-talk ~~obligation~~restriction subject to a 'fiduciary' out will have little practical effect ~~in the period~~ following announcement of the ~~relevant~~ bid, even if the restraint extends into that period.

~~[18] *Magna Pacific Holdings Limited 02* [2007] ATP 03; *Queensland Cotton Holdings Limited 02* [2007] ATP 05~~

~~[19] Usually ceasing once a public announcement of the relevant bid or proposal has been made Compare the restraint on disposing of shares in *PowerTel Limited 01* [2003] ATP 25.~~

[20] Compare the restraint on disposing of shares in ***PowerTel Limited 01*** [2003] ATP 25

28. A no-talk restriction (with a 'fiduciary' out) is less likely to give rise to unacceptable circumstances if the target has conducted an effective auction process before agreeing to it.

29. ~~22.~~ No-talk ~~agreements~~restrictions are sometimes coupled with ~~an~~a notification obligation ~~that the target (or shareholder) discloses details of any~~in respect of potential competing proposals. This may increase the ~~restrictive~~anti-competitive effect.

~~23. What is an acceptable no-talk agreement if the target has already conducted an effective auction process may not be acceptable if the target has not conducted an effective auction process before agreeing to the arrangement.~~

Asset lock-up

30. ~~24.~~ In the context of a control transaction, an asset lock-up agreement that involves an important asset of the target (usually the "crown jewel") can make the target less attractive as an acquisition candidate or investment for shareholders. Accordingly, it may be both anti-competitive and coercive. ~~If entered~~

31. This note applies to lockups in the context of an existing or anticipated bid. If the lock up was entered into after the target received notice of a bid or proposed bid, it may also constitute frustrating action.~~20~~21

32. ~~25.~~ In considering whether an asset lock up agreement gives rise to unacceptable circumstances, the Panel is guided by the following (among other things):

    (a) the commercial reason for it

    (b) the size or strategic value of the asset involved

    (c) whether the agreement was negotiated on an arms-length basis

    (d) the safeguards in place

    (e) whether the agreement is at a fair price. This includes whether any expert advice or sufficient evidence was obtained by the target on the appropriateness of any fixed price, or price formula, in the agreement ~~and~~

    (f) its effect on the amount of, or distribution of benefits to, shareholders in the target in connection with the takeover~~.~~ and

    (g) the timing of entry into the agreement and the length of the lock up.

~~20~~21 See GN 12. See also ***Perilya Ltd 02*** [2009] ATP 1 at [22]-[33]

Lock-up devices with major shareholders

33. ~~26.~~ A bidder may seek to enter into a lock-up device with a major shareholder of the target in addition (or as an alternative) to the target itself. This note applies, with necessary adaptation, to such agreements. ~~21~~22

~~27. A lock-up device agreed with a major shareholder of a target as part of an arrangement for that shareholder to sell all or part of its holding to the bidder, by accepting the bid or otherwise, may be unacceptable because, for example:~~

~~(a) it may affect competition for control of the target[22] or~~

34. ~~(b) it may allow the bidder effectively to control the disposal of~~Primarily the Panel is interested in agreements that may undermine s606. The Panel will consider the anti-competitive effect[23] of any agreement that may relate to shares above the 20% threshold (in the shareholder's hands or when combined with shares already held by the bidder) otherwise than as contemplated in s611.~~23~~24

~~28. In general, coercion is not a factor in lock-up agreements with a major shareholder.~~

(a)

Disclosure

35. ~~29.~~ The existence and nature~~24~~25 of any lock-up device should normally be disclosed no later than when the relevant control proposal is announced, although it may be necessary to announce it earlier.~~25~~ under continuous disclosure provisions applicable to the bidder or target.[26]

~~21~~22 For example, the 1% cap will be calculated on the value of the shares held by the shareholder rather than the target's market capitalisation.

~~22 *Becker Group Ltd 01* [2007] ATP 13~~

[23] Coercion is not a factor in lock-up agreements with a major shareholder

~~23~~24 ***Alpha Healthcare Limited*** [2001] ATP 13 at [23]-[24]

~~24~~25 Include all the relevant terms, even if they are in separate documents: *Normandy Mining Limited (No. 3)* [2001] ATP 30 at [39]

~~25 Unless~~[26] For a listed disclosing entity, ASX Listing Rule 3.1 applies unless the exception in ASX Listing Rule 3.1A applies. ~~See also s675~~For other disclosing entities, see s675. An example is *AMP Shopping Centre Trust 01* [2003] ATP 21 (a decision on pre-emptive rights). On review, see *AMP Shopping Centre Trust 02* [2003] ATP 24

Remedies

36. ~~30.~~ The Panel has a wide power to make orders (including remedial orders) if a lock-up device gives rise to unacceptable circumstances, including cancelling agreements.~~26~~27 The Panel's orders (or undertakings~~27~~28) will be designed to remove any anti-competitive or coercive effect.

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Related material

GN 12 Frustrating actions

~~26~~27 In ***Ballarat Goldfields NL*** [2002] ATP 7 the Panel ordered that the shares which were to constitute the break fee not be issued and no other benefit be provided in substitution

~~27~~28 In ***Ausdoc Group Limited*** [2002] ATP 9 the Panel accepted undertakings from the fee-taker to waive its right to receive and not to accept the payment of a particular fee and from the fee-payer not to pay that fee.

Australian Government
Takeovers Panel

Guidance Note 12 – Frustrating actions

Introduction

1. This guidance note has been prepared to assist market participants understand the Panel's approach to actions that could frustrate a bid or potential bid. Usually such actions are taken by a target.

   Examples of frustrating action:

   1. Significant issuing or repurchasing shares, or issuing convertible securities or options[1]

   2. Acquiring or disposing of a major asset, including making a takeover bid

   3. Undertaking significant liabilities or changing the terms of its debt

   4. Declaring a special or abnormally large dividend

[1] A small number of convertible securities may be significant if this could, for example, prevent the tax benefits of 100% ownership. But compare ***Bigshop.com.au Ltd (No 2)*** [2001] ATP 24 at [45] which considered that a Panel might not regard a small issue of shares under an employee option plan to be unacceptable

5. Signif*icant change to company share plans.*

2. The ~~discussion is~~examples are illustrative only and nothing in the note binds the Panel in a particular case.

3. The policy basis for this note is that it is shareholders who should decide on actions that may:

   - interfere with the reasonable and equal opportunity of the shareholders to participate in a proposal or
   - inhibit the acquisition of control over their voting shares taking place in an efficient, competitive and informed market.

4. Some ASX Listing Rules require shareholder approval for transactions for similar policy reasons.[2]

Frustrating action

5. In this note the following definitions apply:

Term	Meaning
frustrating action	an action by a target, whether taken or proposed, by reason of which: • a bid may be withdrawn[3] or lapse • a potential bid is not proceeded with
potential bid	• a genuine potential bid communicated to target directors publicly or privately which is not yet a formal bid under Chapter 6.[4]

[2] See principally rules 7.1, 7.6 and 7.9, but also rules 10.1, 11.2 and 11.4.

[3] Section 652B (with ASIC approval; see RG 59) or s652C. References are to the ***Corporations Act 2001 (Cth)*** unless otherwise indicated

[4] Includes announcements to which s631 applies but not limited to these: ***MacarthurCook Ltd*** [2008] ATP 20

6. A bidder may make its bid (potential bid) subject to any conditions it chooses, with exceptions.[5] It must set out the conditions clearly. As this note extends to potential bids, it is incumbent on a potential bidder to make it clear to the target what conditions would apply if a bid were made.[6] This will help establish that it was a genuine potential bid and that the target was aware of the condition in issue.

7. An action that triggers a condition is a frustrating action, but whether the action gives rise to unacceptable circumstances will depend on its effect on shareholders and the market in light of ss602(a)[7] and (c)[8] and s657A. ~~For example, an action triggering a condition not commercially critical to the bid is unlikely to give rise to unacceptable circumstances.~~

   Example 1 An action triggering a condition not commercially critical to the bid is unlikely to give rise to unacceptable circumstances.

   2 An action that triggers a 'condition' in a potential bid may not give rise to unacceptable circumstances if the bidder indicated that it would proceed only if the bid was recommended and the directors have rejected the approach.

8. Section 657A(3) requires the Panel to take into account the actions of directors when considering the purposes in s602(c) in relation to the acquisition of a substantial interest. This includes actions that caused or contributed to the acquisition not proceeding. The provision was introduced in 1994:

   "The purpose of this provision is to ensure that the scope of unacceptable circumstances includes cases where the directors of a target company by their action, including such action which caused or contributed to the acquisition not proceeding, did not give shareholders of the company all reasonable and equal opportunities to participate in any benefits accruing to the company."[9]

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5 See Division 4 of Part 6.4. For example, a bid must not include a condition dependent on an event within the sole control of the bidder. A bidder could not rely on a condition that offended Part 6.4 to establish unacceptable circumstances

6 Includes any pre-conditions to the bid set out in a potential bid

7 Acquisition of control over voting shares takes place in an efficient, competitive and informed market

8 As far as practicable, holders of the relevant class of shares all have a reasonable and equal opportunity to participate in any benefits

9 Explanatory Memorandum to the ***Corporations Legislation Amendment Bill 1994,*** para [344]

Overlap with directors' duties

9. The Panel creates new rights and obligations.[10] It does not enforce directors' duties – that is for a court.

10. Undertaking a frustrating action may give rise to unacceptable circumstances regardless of whether it is consistent with, or a breach of, directors' duties. It is not to the point that there is no express requirement in the law for shareholder approval of frustrating action.

~~11. If a frustrating action may involve a breach of directors' duties, the Panel will consider whether it should conduct proceedings or the issues should be considered in a court. While the Panel may be the only forum generally available for the time being[11] it will need to consider whether it can provide an adequate remedy.~~

Unacceptable circumstances

11. ~~12.~~ In considering whether frustrating action gives rise to unacceptable circumstances, the Panel is guided by the following~~:~~.

~~(a) considerations~~***Considerations surrounding the bid***

(a) ~~§~~ how long the bid has been open and its likelihood of success (if a potential bid, of proceeding)~~[12]~~[11]

(b) ~~§~~ any clearly stated objectives of the bidder and whether the condition is commercially critical to the bid

(c) ~~§~~ whether it is 'unreasonable' for a bidder to rely on the condition before the Panel~~[13]~~[12]

Examples:

1. A condition that is overly restrictive or is invoked unreasonably~~[14]~~[13]

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[10] ***Precision Data Holdings Ltd v Will***s (1992) 173 CLR 167; ***AG (Cth) v Alinta Ltd*** [2008] HCA 2

~~[11] Under s659B, during a bid period only ASIC may initiate court proceedings in relation to the bid~~

~~[12]~~[11] That is, for a bid whether, having regard to the level and rate of acceptances, it is reasonable to conclude that target shareholders have rejected the bid. It may not be reasonable to conclude this if the bid is still conditional and the final bid close date is not known

~~[13]~~[12] The bidder is free to choose the bid conditions but the frustrating action may not give rise to unacceptable circumstances. One example may be where the condition is not commercially critical to the bid

2. A condition that requires the target's co-operation such as recommending the bid or allowing due diligence

3. A condition restricting target directors from seeking competing proposals where they have not entered a no-talk agreement

4. A condition that the target enters a material transaction that is outside its business plans

(d) § whether the bidder can waive the condition

(e) § the market price compared to the bid price

~~(b) considerations~~***Considerations surrounding the frustrating action***

(f) § whether there is a competing proposal already

(g) § whether the frustrating action was undertaken by the target in the ordinary course of its business. A bidder must accept that the target's normal business will continue~~15~~ normally[14]

(h) § whether there is a legal or commercial imperative for the frustrating action

Examples

1. Action to comply with a court order, legislative requirement or government directive regarding its licence

2. Action to avoid a materially adverse or to achieve a materially favourable financial consequence

3. A transaction announced before the bid

(i) § whether the frustrating action materially affects the financial or business position of the ~~company~~target[15]

(j) § the process the target undertook in considering whether to take the action~~.~~, for instance -

- the impact the acquisition may have on regulatory approval for the transaction (eg, ACCC approval)

- the "chilling effect" that the frustrating action has on any potential auction

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~~14~~13 ***Pinnacle VRB Ltd (No 8)*** [2001] ATP 17 at [49(e)]

~~15~~14 Relevant factors include the target's business plans and the size and nature of the transaction

15 It must be reasonable for the bidder to regard the impact as adverse

(k) how advanced the negotiations on the frustrating action were when the bid was made or communicated.

12. The following are some examples of actions that may give rise to unacceptable circumstances:

(a) issuing new shares (or convertible securities), or repurchasing shares, if significant in the context of the target's issued capital or the bid

(b) acquiring a major asset, including by making a takeover bid, or disposing of one

(c) undertaking significant liabilities or materially change the terms of its debt (where the takeover would not have given rise to these changes)

(d) declaring a special or abnormally large dividend

(e) significantly changing company share plans or

(f) entering into joint ventures.

Not unacceptable circumstances

13. If a frustrating action creates for shareholders ~~have~~ a choice between the proposals, the frustrating action will not generally give rise to unacceptable circumstances.

14. The Panel generally does not consider it an answer to unacceptable circumstances that, for example, a transaction may be lost because of the time involved in calling a general meeting. Relevant factors include the value of the transaction to the target and why it couldn't be conditional on shareholder approval. However, the Panel recognises that shareholders may be given a choice in different ways, as suits the particular transaction dynamics.

Examples:

1. Directors announcing that they will enter into an agreement after a specified, reasonable time,[16] unless control has by then passed to the bidder

2. Seeking prior shareholder approval or making the frustrating action conditional on shareholder approval[16][17]

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[16] Reasonable time may be affected by the length of the bid period or the status of any bid conditions

~~16~~[17] ***Pinnacle VRB Ltd (No 5)*** [2001] ATP 14 at [50]

3. Entering an agreement conditional on the bid failing or which contains a cooling-off clause which a new management might exercise

15. If a target offers to seek shareholder approval, time is needed to prepare adequate information for shareholders to decide between the competing proposals and to hold the meeting. The Panel will consider issues such as:

    (a) what is a reasonable time to prepare the notice of meeting

    (b) whether the bidder is willing to extend its bid to allow the holding of the meeting[18]

    (c) how long the target has been considering the proposed action

    (d) the benefits to target shareholders of the proposed action and

    (e) whether the bidder agrees not to rely on the defeating condition should the resolution fail. This may require the bidder to vary or waive the condition.

16. In general it will not give rise to unacceptable circumstances for a target:

    - not to facilitate a bid
    - to seek alternatives (without frustrating the bid)[19] or
    - to recommend rejection of a bid (if the directors consider this in the best interests of shareholders).[20]

Remedies

17. The Panel has wide powers to make orders,[~~17~~21] including to:

    (a) prevent an action or transaction from proceeding

    (b) require the target to seek shareholder approval of the action or transaction and

    (c) unwind an action or transaction.

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[18] Conversely it may point to unacceptable circumstances that the bidder is prepared to extend its bid yet the target is not prepared to seek shareholder approval

[19] This might even involve, for example, breaching a 'no talk' bid condition provided the directors did not agree to that condition

[20] The bid may nevertheless be subject to such conditions

[~~17~~21] Section 657D

18. The Panel may override directors' decisions even if they were made consistently with directors' duties.

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First Issue	16 June 2003
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Related material

GN 7 Lock-up devices

Australian Government
Takeovers Panel

Guidance Note 14 – Funding arrangements

Background

1. This guidance note has been prepared to assist market participants understand the Panel's approach to funding arrangements for the cash component of consideration under a takeover.
2. The ~~discussion is~~examples are illustrative only and nothing in the note binds the Panel in a particular case.
3. While focused on debt facilities, the principles in this note apply with the necessary adaptation to funding, in whole or in part, by raising equity.
4. Section 631(2)(b)[1] requires that a person not announce a bid if:

   "the person is reckless as to whether they will be able to perform their obligations relating to the takeover bid if a substantial proportion of the offers under the bid are accepted."
5. A bidder, therefore, must believe it will be able to implement its offer.[2] It must have (and maintain) a reasonable basis for that belief.

[1] Unless otherwise indicated, all references are to the ***Corporations Act 2001*** (Cth)

[2] See also ASIC RG 59.3. As to s631, see cases cited in ***Realestate.com.au.Ltd*** [2001] ATP 1 at [52] and [65]-[71], ***Brisbane Broncos Ltd (No 3)*** [2002] ATP 3. Other sections of the Corporations Act deal with funding as well: eg, s588G (Director's duty to prevent insolvent trading) and s588V (Holding company liability for subsidiary insolvent trading)

Funding

Source

6. A bidder may fund its bid from any source, internal or external.[3] It may have a combination of sources. It may also have alternative arrangements in place (eg, it has cash reserves but seeks debt funding). If ~~there are~~ alternatives are disclosed, each must be in place or provide a reasonable basis for the bidder to expect that it will be in place.

   Examples: cash reserves, liquidating assets, bank loan, accommodation from group member

7. A bidder may alter its funding arrangements after it bids. However, the altered funding will be assessed at the time of the alteration as to whether:

   (a) it is in place, or there is a reasonable basis for the bidder to expect that it will be in place and

   (b) it materially adversely affects target shareholders and the market for target (and bidder) shares.

Amount

8. In considering the amount of funding required, the Panel takes into account:

   (a) if the bid extends to securities issued during the offer period,[4] or unmarketable parcels in a proportional bid, [5] whether funding arrangements are sufficient to pay for them as well

   (b) whether the bidder has reasonable grounds not to expect acceptances in respect of particular securities

   Examples:

   1. The bidder or its subsidiary holds securities in the bid class

   2. A target shareholder has agreed not to accept the bid

   3. Convertible securities are materially out of the money

   (c) whether foreign currency funding has been hedged or is enough to ensure that there will be sufficient funds in Australian

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[3] Includes by loan or other accommodation from a member of the same corporate group . The ultimate source of funding and sufficient details must be disclosed: see ASIC Regulatory Guide 37 at [37.14] and [37.16]

[4] See s617(2)

[5] ***GoldLink IncomePlus Limited 0***3 [2008] ATP 21 at [18]

currency even if there is a material adverse exchange rate movement.[6]

9. Initial funding need not cover additional amounts that might be required if the bidder were to increase the offer price or offer to pay costs and expenses.[7] However, the bidder ought to have a reasonable basis to expect that funding of the increased amount will be in place before it announces the increase. The funding arrangements for the increase do not need to be the same as for the original bid.

Unacceptable circumstances

10. It may give rise to unacceptable circumstances if:

    (a) a bidder does not have funding in place, or a reasonable basis to expect that it will have funding in place, to pay for all acceptances when its bid becomes unconditional

    (b) funding arrangements fail (because of changes in circumstances or otherwise) and are not replaced promptly

    (c) funding arrangements become inadequate because of a change in the bid (eg, declaring the bid free from a condition or increasing the bid consideration)

    (d) the bid becomes unconditional when the funding arrangements are conditional and there is a real risk of the funding conditions not being fulfilled

    (e) the bidder proposes to pay accepting shareholders faster than originally proposed before funding arrangements are certain or

    (f) the bidder does not actually pay accepting shareholders. ~~In many bids, the~~The offer ~~allows~~might contain terms that allow the 'accepted shares' to be transferred before payment is made.~~8~~ (Compare an offer that might contain a term that the accepting shareholder retains an equitable interest in the shares until paid.[8]) If payment is not made, ~~accepting shareholders become~~

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[6] See ***Parker & Parsley Petroleum Australia Pty Ltd*** v ***Gantry Acquisition Corp*** (1994) 13 ACSR 689

[7] See ***AAPT Ltd v Cable and Wireless Optus Ltd*** (1999) 17 ACLC 974, at 1010 and ***Associated Dairies Ltd v Central Western Dairy Ltd*** (1993) 117 ALR 433, at 439. Cf ***Re Archaean Gold*** (1997) 15 ACLC ~~382,~~382 at 384

~~8 Compare ***George Hudson Holdings Limited*** v ***Rudder*** (1973) 128 CLR 387: the usual rule in transactions involving payment in return for a transfer of property is that the transfer of title to the property only occurs when payment is made, unless the contract provides otherwise~~

[8] See ***George Hudson Holdings Limited*** v ***Rudder*** (1973) 128 CLR 387: the usual rule in transactions involving payment in return for a transfer of property is that the transfer of title to the property only occurs when payment is made, unless the contract provides otherwise

~~unsecured creditors of the bidder, which~~this may give rise to a declaration of unacceptable circumstances and orders returning the shares to the acceptor.

What is a reasonable basis?

11. Whether the bidder has a reasonable basis to expect that it will have funding in place is assessed objectively and will depend on the circumstances of each case.

12. If funding arrangements have not been formally documented[9] or remain subject to conditions precedent to drawdown,[10] the bidder may still have a reasonable basis if there is a sufficiently detailed binding commitment in place when it announces its bid[11] or the bidder's statement is given to ASIC. However, documentation[12] should be completed and signed before offers are sent to target shareholders, and security documents should be finalised and executed before the bid becomes unconditional.

13. If external debt funding is subject to approval by the lender's credit committee, the bidder may still have a reasonable basis if the bidder is of substantial worth relative to the funding requirement, reasonably believes it has access to other sources of funds and has been informed that credit committee approval is likely.

14. If funding is by or through the bidder's corporate group, it should be binding[13] and fully documented before the bidder's statement is given to ASIC. The parent of the group should agree to procure compliance by group members with the arrangements. The existence of outside interests between the lender and bidder may require arms-length negotiations, which is a factor the Panel would take into account when considering whether to regard the funding as provided by an 'external lender'.

15. If funding is by using cash reserves, the reserves should not be subject to security interests, rights of set off or other arrangements (such as being required for other group operations) that may materially affect

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[9] In ***Goodman Fielder*** [2003] ATP 1 the Panel granted withdrawal rights until the funding was settled and signed. In ***Pinnacle VRB Ltd (No 6)*** [2001] ATP 11 and ***Consolidated Minerals Ltd 03*** [2007] ATP 25 at [44] the Panel looked at the funding of the bidder by its funder (on review: ***Consolidated Minerals Ltd 03R*** [2007] ATP 28 at [32]-[34])

[10] See for example ***ACI Ltd*** v ***Rossington Holdings Ltd*** (1992) 106 ALR 221 and ***Goodman Fielder*** [2003] ATP 1

[11] See ***Indophil Resources NL*** [2008] ATP 18 at [17]

[12] Executed loan or other financing documents, although a facility or commitment letter or term sheet may be acceptable if it is binding and sets out all material terms and conditions

[13] If the group lender's ability to fund the bid depends, in turn, on an external facility, the internal facility should have an appropriate condition precedent to drawdown

the bidder's ability to use them. If they are, the bidder should have standby funding available or other sources of cash.

16. If funding is by drawing down pre-existing facilities, the bidder should ensure that the funds are available and not required for other group operations. Otherwise, the bidder should have standby funding available or other sources of cash.

17. If the bidder (or a group company) is realising non-liquid assets[14] to fund the bid, the assets must be realisable on a timely basis for a sufficient amount. If they may not be, the bidder should have standby funding available or other sources of cash.

18. The degree of certainty about the availability of the funds may increase during a bid as the likelihood of bid conditions being fulfilled or waived increases.[15] A bid should not be declared, or allowed to become, unconditional until:

    (a) binding funding arrangements are documented in final form and

    (b) commercially significant conditions precedent to drawdown have been fulfilled or there is no material risk that they won't be.

19. A bidder would be unlikely to have a reasonable basis for external funding that is subject to:

    (a) documentation without a binding commitment (see paragraph 12)

    (b) internal approval by the lender if the requirements of paragraph 13[16] are not met

    (c) unusual repayment or expiry provisions that may result in the funding not being available to pay for acceptances[17] or

    (d) conditions precedent to drawdown, unless it is likely that the conditions will be satisfied or waived when the bid becomes unconditional.[18]

20. A bidder would be unlikely to have a reasonable basis for funding:

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[14] In ***Taipan Resources NL (No 10)*** [2001] ATP 5 and ***Taipan Resources NL (No 11)*** [2001] ATP 16 the relevant asset was a portfolio of listed shares. However, the major part of the portfolio was a single parcel of more than 10% in another company – in the circumstances this was a non-liquid asset

[15] In ***Indophil Resouces NL*** [2008] ATP 18 the Panel declined to commence proceedings on an announcement. See also ***Magna Pacific (Holdings) 02*** [2007] ATP 3

[16] ***Taipan Resources NL (No 10)*** [2001] ATP 5

[17] ***ICAL Ltd*** v ***County Natwest Securities Australia Limited*** (1988) 6 ACLC 467

[18] For example, funding that is subject to a bid's minimum acceptance condition. Before waiving the minimum acceptance condition, the bidder needs to take reasonable steps to ensure that the funding will be available or alternative funding is available

(a) that is informal or unenforceable or on a "best endeavours" basis[19] or

(b) if the lender has insufficient funds to pay for acceptances.

Disclosure

21. Timely disclosure of funding arrangements, and updated disclosure as needed, is an important aspect of an efficient, competitive and informed market,[20] and ensures that holders of shares are given enough information to enable them to assess the merits of the proposal.[21] Disclosure is specifically required in a bidder's statement.[22]

22. A bidder should consider making disclosure in relation to:

(a) establishing that its funder has the necessary financial resources.[23] If the funder is an Australian bank, this may require only that it is identified. For other financial institutions, there may need to be limited disclosure (eg, its latest audited net assets and a description of its prudential regulation). For other funders, more disclosure may be needed (eg, full accounts, or in most cases an accountant's certificate as to its ability to meet the obligation with disclosure of the content of the accountant's certificate or enough of it to allow shareholders to be satisfied of the sufficiency of the arrangements)[24]

(b) if the funder is a group member, the terms of the intra-group arrangements

(c) the amount available for drawdown, or under alternative or stand-by funding, or available by way of any other sources of cash or non-cash assets relied on (and arrangements for realization of non-cash assets)

(d) the basis for any expectation that there will not be acceptances for particular securities

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19 ***Taipan Resources NL (No 10)*** [2001] ATP 5

20 Section 602(a). See also ***MYOB Ltd*** [2008] ATP 27 at [11]

21 Section 602(c)

22 Section 636(1)(f) requires disclosure in relation to cash consideration under a bid. See also ASIC RG 37

23 ***Tower Software Engineering Pty Ltd 01*** [2006] ATP 20

24 ***GoldLink IncomePlus Limited 0***3 [2008] ATP 21. Compare ***Golden West Resources Ltd 01*** [2007] ATP 31 at [18]-[19] where the Panel did not require information about sub-underwriters to be disclosed when the underwriting of the bid was by an ASX-regulated broker. See also fn 3

(e) material conditions precedent to drawdown, and any basis on which the bidder believes it will be able to satisfy the conditions

(f) the status of conditions precedent to drawdown if the bid is declared or allowed to become unconditional. If there are remaining conditions, the basis on which the bidder believes it will be able to satisfy them and

(g) material changes to funding terms or to circumstances which affect the availability or sufficiency of the arrangements.

23. The terms of the funding arrangement (interest rate, repayment, covenants, security) may not need to be disclosed unless the bid is likely to result in a continuing minority shareholding in the target and:

(a) the bidder intends to rely on the target for help with the funding arrangement (eg, provision of security) or

(b) the target will require on-going funding which may be affected by the bidder's funding.

24. If the bid consideration comprises foreign currency, additional disclosure regarding any exchange rate risks and their management may also be needed.[25]

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[25] In ***Rinker Group Ltd*** [2006] ATP 35 the Panel likened foreign currency to a scrip offer in which the value of the shares offered as consideration may vary during the offer but the number does not vary: see para [25]

Australian Government
Takeovers Panel

Guidance Note 17 – Rights issues

Background

1. This guidance note has been prepared to assist market participants understand the Panel's approach to rights issues which have, or are likely to have, an effect on control or the acquisition of a substantial interest in the company.[1]
2. The ~~discussion is~~examples are illustrative only and nothing in the note binds the Panel in a particular case.

[1] This note applies also to Managed Investment Schemes

Exception for rights issues

3. Section 611[2] provides exceptions to the prohibition on persons acquiring control of a company in s606. The two relevant exceptions are item 10 and a similar exception in item 13 (see Appendix A).

4. The Panel does not seek to narrow the exceptions. Many rights issues[3] will not affect control. Moreover, the fact that control is affected by a rights issue does not of itself give rise to unacceptable circumstances, bearing in mind:

   (a) the legislation recognises an exception from s606 for rights issues

   (b) shareholders invest in the knowledge they may be diluted if they do not participate in capital raisings and

   (c) companies are entitled to manage their capital as they see fit.

5. However, if there is a potential for a rights issue to affect control, the directors should carefully consider all reasonably available options to mitigate that effect. The Panel considers, among other things, whether the control effect exceeds what is reasonably necessary for the fundraising purpose.[4]

Unacceptable circumstances

6. In considering whether a rights issue gives rise to unacceptable circumstances, the Panel ~~is guided by~~looks at the effect of the rights issue against the principles in s602. In doing so, it considers the following factors:

   (a) the company's situation

   - what methods of raising funds are available to the company
   - whether the company has explored other capital-raising alternatives
   - the financial situation and solvency of the company, including the reasons for raising the funds. ~~If the company has no compelling need for funds, or gets no readily discernible benefit, the rights issue is more likely to give rise~~

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[2] References are to the ***Corporations Act 2001*** (Cth) unless otherwise indicated

[3] An issue by the company of new shares offered to shareholders in proportion to their existing holdings, which may be renounceable (ie tradeable) or non-renounceable, and may be underwritten (ie to take up any shares not taken up by shareholders) or non-underwritten~~.~~

[4] ***Bisalloy Steel Group Limited*** [2008] ATP 29 at [21]; ***Dromana Estate Limited 01R*** [2006] ATP 8 at [43]

~~to unacceptable circumstances~~How much the company needs funds may influence what is reasonable for it to accept as a potential control effect

- market factors leading up to the rights issue and those reasonably likely to occur during the rights issue. Market factors have a significant bearing on the structure of a rights issue (below)
- whether the company received, and followed, advice from financial advisers

(b) the structure of the rights issue[5]

- size, price, discount to market, timing, underwriting and renounceability[4]
- whether the rights issue is underwritten by professional underwriters or sub-underwriters or a related party or major shareholder
- whether there is a dispersion strategy[6]

(c) the effect of the rights issue

- any effect on control~~,~~ or the acquisition of a substantial interest ~~or s602 effect.~~
- the purposes of Chapter 6 as set out in s602
- the steps the board has taken to minimise ~~the~~ potential control effects
- disclosure of ~~the~~ potential control effects
- the response, or likely response, of the shareholders (and particularly any substantial shareholders) to the rights issue.

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[5] ***InvestorInfo Ltd*** [2004] ATP 6 at [38] lists factors relevant to assessing whether a rights issue is genuinely accessible to shareholders

~~[4] *InvestorInfo Ltd* [2004] ATP 6 at [38] lists factors relevant to assessing whether a rights issue is genuinely accessible to shareholders~~

[6] ***Multiplex Prime Property Fund 03*** [2009] ATP 22. On review, [2009] ATP 23, the review Panel declined to conduct proceedings

Some factors

Need for funds

7. When considering the company's need for funds, the Panel will look at the company's financial situation, the amount sought to be raised and the suitability of raising capital by the rights issue. The Panel is likely to accept the directors' decision on these issues if the decision appears to be reasonable and supported by rational reasons unless the applicant can point to something that suggests deeper inquiry may be warranted.[7]

8. However, need for funds is not a safe harbour. Notwithstanding a company's need for funds, the Panel may still declare the circumstances unacceptable.

Structure overall

9. ~~8.~~ Structural matters (such as price, number of shares offered, renounceability, underwriting) cannot be considered in isolation from each other and the market conditions at the time of the rights issue. The Panel will look at the structure of the rights issue as a whole, and the market, in deciding whether the rights issue gives rise to unacceptable circumstances. In practice, if the rights issue is underwritten, the underwriter will usually influence the structure (and may in some cases decide on it).[8]

Pricing

10. ~~9. Directors need to consider, as an aspect of pricing a rights issue, the need to minimise any unnecessary potential effects on control.~~ Price influences the decision of shareholders whether to take up the rights offer. ~~Their decision is affected also by other factors, such as the size of the rights issue compared to the company's existing share capital, whether or not the rights issue is renounceable and the effect on the prospects of the company if the rights issue is fully taken up~~[9] The more shareholders take up their rights, the less potential there is for a control effect.

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[7] In Rey Resources Ltd [2009] ATP 14, the Panel accepted that there was a need for funds based on the documents submitted by the company. The underwriter undertook to disperse shortfall shares to a number of sub-underwriters

[8] An example of alternatives being explored, and the interaction of underwriters with the company is structuring the rights issue is DataDot Technology Ltd [2009] ATP 13

[9] Their decision is affected also by other factors, such as the size of the rights issue compared to the company's existing share capital, whether or not the rights issue is renounceable and the effect on the prospects of the company if the rights issue is fully taken up

11. ~~10.~~ The question of pricing is more easily considered in relation to liquid, listed securities because there is a market price against which to compare the issue price for the rights. Unlisted securities, illiquid listed securities or listed securities with a volatile market price may not have a readily accessible price comparison.

12. ~~11.~~ A small discount to market (or a premium to market) provides less incentive for shareholders to take up the rights offer. It also undermines the ~~usefulness~~effectiveness of renounceability~~. This increases~~, in mitigating the likelihood of control becoming concentrated with an underwriter or other participating major shareholder.

13. ~~12.~~ A large discount to market is likely to be attractive to shareholders and encourage them to take up the rights offer (to gain the benefit of the discount). This reduces the shortfall and thus the likelihood of control becoming concentrated with an underwriter or other participating major shareholder. On the other hand, ~~it~~a large discount may have an adverse effect on shareholders who elect not to participate by transferring value to new shares and diluting the shareholders more than would otherwise be the case. This may be particularly so in a large issue.

Size

14. ~~13.~~ A large rights issue may have a potential control effect, even if priced at a large discount, because shareholders may not have the capacity to pay for all the shares. A company undertaking a large rights issue may need to more clearly demonstrate its need for those funds.~~5~~10

Renounceability

15. ~~14.~~ In a renounceable~~6~~11 rights issue, a large discount is likely to facilitate an active market for the rights. This allows shareholders an opportunity to recoup some of the value transfer by selling their rights.~~7~~12 The buyer is likely to take up the rights offer. ~~Because there~~There is no exception from s606 for buyers who exercise rights~~, this is likely to reduce the control effect of the issue.~~ .

~~5~~10 The company may also require shareholder approval, for example under the Listing Rules

~~6~~11 Renounceable rights can be transferred to a third party; non-renounceable rights cannot. Listing and quotation will establish a price and on-market trading of rights can occur, but listing and quotation is not essential to renounceability

~~7~~12 Helps meet the reasonable and equal opportunity principle in s602(c). See also ***Emperor Mines Ltd 01R*** [2004] ATP 27 at [26]

16. ~~15.~~ A non-renounceable rights issue may result in greater flow-through to an underwriter or sub-underwriter, so increasing the potential control effect. The effect is exacerbated if the rights issue is underwritten or sub-underwritten by a related party.

17. ~~16.~~ However, renounceability is not a safe harbour.

18. Non-renounceability may not be a significant factor in deciding unacceptable circumstances if ~~a market for rights is unlikely (eg, the company is not listed or the stock is illiquid) or it is unreasonably costly to make the rights issue renounceable. Note that the same factors which make renounceability less attractive also increase the risk of the rights issue having a control effect.~~:

    (a) a market for rights is unlikely (eg, the company is not listed or the stock is illiquid)

    (b) it is unreasonably costly to make the rights issue renounceable or

    (c) the market circumstances are such that underwriters for the issue are not available for a renounceable issue (eg, because of the longer term of the underwriting).

Underwriting

~~17. Underwriters and sub-underwriters[8] may be financial institutions, stock-brokers, major shareholders of the company or other related or unrelated parties.~~

19. ~~18.~~ An underwriter (or sub-underwriter) may acquire control of a company relying on:

- the second limb of the exception in item 10 of s611 or
- if a ~~prospectus~~disclosure document has been lodged in relation to the rights issue, the exception in item 13 of s611.

20. ~~19.~~ Underwriters (sub-underwriters)[13] may be professional,[~~9~~14] a related party, an unrelated party or a major shareholder. A professional underwriter generally seeks to earn an underwriting fee rather than hold shares, so is unlikely to have any interest in obtaining control of

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~~[8] The underwriter guarantees the funds to be raised by contracting, subject to conditions, to subscribe for shares not taken up by shareholders. A sub-underwriter takes some of that risk by contracting to take some (or all) of the shares the underwriter might have taken~~

[13] The underwriter guarantees the funds to be raised by contracting, subject to conditions, to subscribe for shares not taken up by shareholders. A sub-underwriter takes some of that risk by contracting to take some (or all) of the shares the underwriter might have taken

[~~9~~14] That is, a person who underwrites in the normal course of their business such as a financial institution or stock-broker

the company, although it may not be able to readily on-sell shares subscribed for under the underwriting agreement.

21. ~~20.~~ For many companies, a related party or major shareholder is the only realistic source of underwriting (sub-underwriting).~~10~~15 Underwriting (sub-underwriting) by a related party or major shareholder does not, of itself, give rise to unacceptable circumstances. However, greater care is needed to mitigate the potential control effects if a related party or major shareholder underwrites (sub-underwrites). The failure of directors to properly canvass professional underwriters or seek out alternatives to a related party or major shareholder underwriter (sub-underwriter) may increase the likelihood of unacceptable circumstances.

Safeguards

22. ~~21.~~ To mitigate potential control effects of a rights issue, a company might consider the following:

(a) A dispersion strategy for dealing with the shortfall rather than it flowing through to the underwriter (sub-underwriter)~~11~~16

Examples:

1. A shortfall facility for shareholders or others to nominate to take extra shares~~12~~17

2. A back-end book-build of shortfall shares~~13~~18

(b) Using several non-associated~~, professional~~ sub-underwriters

(c) Informed approval by non-associated shareholders of the rights issue and underwriting (sub-underwriting) by related parties.

23. ~~22.~~ Features which may help a dispersion strategy ~~to~~ mitigate potential control effects include:

(a) an underwriter (sub-underwriter) receiving entitlements under the dispersion facility after all other requests have been satisfied

(b) sufficient time and disclosure being offered to shareholders and other investors to assess the rights or shares being offered and

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~~10~~15 ***Emperor Mines Ltd 01R*** [2004] ATP 27 at [28]-[30]

~~11~~16 For example, ***Data & Commerce Ltd*** [2004] ATP 7

~~12~~17 A facility for shareholders to subscribe for shares not taken up under the rights issue. If the rights issue is underwritten, participation is usually in advance of determining the shortfall available to the underwriter

~~13~~18 An offer of shares not taken up under the rights issue to investors - typically institutions - for whom bids are sought, and allotments and issue price determined based on those bids

(c) external investors being able to take up shares offered under the dispersion strategy.~~14~~19

24. ~~23.~~ The item 10 or item 13 exceptions may not protect an acquisition under a dispersion strategy, whether by existing shareholders or other persons, if the acquisition is not by a person in the capacity of underwriter or sub-underwriter (ie, one who facilitates a capital raising by contracting to subscribe for the shortfall before the offer is made).

Disclosure

25. ~~24.~~ Disclosure is of increased importance when shareholders are considering the desirability of making a further investment in the company, the control implications of the rights issue and whether to take steps to protect against the dilution of their existing holding.~~15~~20

26. ~~25.~~ Rights issue disclosure may be made in different forms under Part 6D.2:

(a) a full prospectus (with or without a profile statement) under ss709(1) and (2)

(b) a "transaction specific" prospectus under s713

(c) an Offer Information Statement under s709(4) or

(d) a "cleansing notice" under s708AA.

27. ~~26.~~ Exceptionally, a rights issue may be made without disclosure under Part 6D.2 if it meets the requirements of s708 (a small scale offering, an offering to professional investors, etc).

28. ~~27.~~ The Panel would expect more disclosure in relation to a rights issue that has more potential control effects (eg, increase in a person's voting power from 10% to 40%, compared to increase in a person's voting power from 51% to 55%).

29. ~~28.~~ In considering whether unacceptable circumstances exist, the Panel takes into account:

(a) the legislative intention for the disclosure required and the type of document used and

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~~14~~19 In ***Dromana Estate Ltd 01 and 01R*** [2006] ATP 4 and [2006] ATP 8 the Panel addressed discretion in respect of, and a cap on, shortfall allocations. It considered that discretion to refuse to accept applications under the shortfall facility was not appropriate, and a cap imposed on individual shareholders under the shortfall facility, which replaced the discretion, was likely to interfere inappropriately with the acquisition of control of shares in Dromana in an efficient competitive and informed market. See also ***Lachlan Farming Ltd*** [2004] ATP 31 at [46]

~~15~~20 Apart from, where relevant, an understanding of the issuer's business, financial performance, plans and prospects

(b) the adequacy of disclosure in respect of potential control effects.

30. ~~29.~~ Shareholders will be better able to make an informed decision on participation in a rights issue and its potential control effects if the following is disclosed:

(a) the possible control scenarios (to the extent they can be)

(b) the identities of those who may end up owning any shortfall

(c) the reasons behind the choice and roles of any supporting shareholders, underwriters and sub-underwriters

(d) the future shareholding pattern of the issuer

(e) the intentions for the company of persons who may obtain control (to the extent it can be ascertained by the company)~~16~~[21] and

(f) the potential effects on control which its proposed dispersion strategy (if any) might cause.

31. ~~30.~~ Such information would be expected to be found in a full prospectus or cleansing notice because of the requirements in the Act. The Panel thinks it is likely that such information would be required in a transaction specific prospectus. Because an Offer Information Statement is used for small capital raisings, there may be limited control implications. But that may not be so for a company with low capitalisation, and therefore the circumstances may suggest that such information should be disclosed.~~17~~[22]

32. ~~31.~~ The Panel is not the primary regulator of the disclosure content of rights issues and does not provide detailed guidance on what constitutes complete disclosure.

Managed investment schemes

33. ~~32.~~ A managed investment scheme must set out in its constitution "adequate provision for the consideration that is to be paid to acquire an interest in the scheme".~~18~~[23] This restricts the discretion of the responsible entity to set an issue price at the time of an issue of interests, but has been modified by ASIC Class Order CO 05/26.

~~16~~[21] This information should be available in relation to underwriters and sub-underwriters but not necessarily major shareholders whose voting power may increase simply by taking up their entitlement in a non-underwritten offer while other shareholders do not

~~17~~[22] ***Anaconda Nickel Limited 02-05*** [2003] ATP 04 at [69]-[70]

~~18~~[23] section 601GA(1)

Applications

34. ~~33.~~ An applicant is likely to have less access to relevant information than the directors of the company. The Panel will take this into account when assessing whether or not to conduct proceedings.

35. ~~34.~~ Nevertheless, an application needs to demonstrate (by evidence and reasoning) a basis for the Panel's intervention, identifying the effect complained of. The application must be made in a timely manner to minimise potential harm and disruption to the company and shareholders.

Remedies

36. ~~35.~~ The Panel has wide powers to make orders,[~~19~~24] including to:

(a) prevent the rights issue proceeding

(b) reopen the rights issue

(c) require further disclosure

(d) divest shares acquired under the rights issue

(e) freeze voting power of shares acquired under the rights issue

(f) require shareholder approval of the rights issue or

(g) require different underwriting or sub-underwriting arrangements.

37. ~~36.~~ The question of motive or intention to bring about the unacceptable circumstances is a factor in deciding whether the Panel's preferred orders would unfairly prejudice any person.

Publication History

First Issue	10 January 2006
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[~~19~~24] Section 657D

Appendix: Items 10 and 13 of section 611

Item 10

An acquisition that results from an issue of securities that satisfies all of the following conditions:

(a) a company offers to issue securities in a particular class;

(b) offers are made to every person who holds securities in that class to issue them with the percentage of the securities to be issued that is the same as the percentage of the securities in that class that they hold before the issue;

(c) all of those persons have a reasonable opportunity to accept the offers made to them;

(d) agreements to issue are not entered into until a specified time for acceptances of offers has closed;

(e) the terms of all the offers are the same.

This extends to an acquisition by a person as underwriter to the issue or sub-underwriter.

Item 13

An acquisition that results from an issue under a disclosure document of securities in the company in which the acquisition is made if:

(a) *the issue is to a person as underwriter to the issue or sub-underwriter; and*

(b) the disclosure document disclosed the effect that the acquisition would have on the person's voting power in the company.