

In the matter of Namakwa Diamond Company NL (No. 2)
[2001] ATP 9

Catchwords:

Takeover bid made two hours after initial listing of target – content of bidder’s statement – inadequate disclosure – content of chairman’s letter to shareholders in bidder’s statement – allegation of misleading and deceptive statements – offer premium – non-compliance with JORC Code – non-disclosure of assumptions underlying balance sheet – supplementary bidder’s statement

Corporations Law (Cth), sections 636(1), 710, 712 and 713

These are the reasons for our decision to make a declaration of unacceptable circumstances on the application by Namakwa Diamond Company NL under section 657C of the Corporations Law received on 30 March 2001 for interim orders and a declaration of unacceptable circumstances in relation to a takeover bid by Majestic Resources NL.

INTRODUCTION

1. The Panel in this matter is constituted by Nerolie Withnall (sitting President), Fiona Roche (sitting Deputy President) and Chris Photakis.
2. These are the reasons for our decision to make a declaration of unacceptable circumstances under section 657A of the Corporations Law (the *Law*) in relation to an application by Namakwa Diamond Company NL (*Namakwa*) dated 30 March 2001. The application was for interim orders and a declaration of unacceptable circumstances in relation to a takeover bid by Majestic Resources NL (*Majestic*) for Namakwa.¹ The decision to make a declaration was announced on 26 April 2001.

THE APPLICATION

3. The application related to the bidder’s statement lodged by Majestic on 15 March 2001. Under the terms of the takeover bid, Majestic offered two fully paid Majestic ordinary shares, plus one \$0.20 partly paid Majestic contributing share for every two Namakwa shares.
4. Namakwa was concerned that certain disclosures made by Majestic in the bidder’s statement were:
 - (a) in breach of the Law;

¹ Statutory references are to provisions of the Corporations Law, as in force at 9 March 2001. Findings of fact are based on submissions by the parties and ASX announcements.

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- (b) inadequate; and/or
 - (c) misleading and deceptive or likely to mislead or deceive Namakwa shareholders.
5. Namakwa sought a declaration of unacceptable circumstances and:
- (a) an interim order that Majestic be prevented from dispatching its bidder's statement to Namakwa shareholders; and
 - (b) final orders that Majestic lodge a new bidder's statement which:
 - (i) clarifies certain statements identified for the purposes of the application as being inadequate; and
 - (ii) corrects all of the deficiencies referred to in the application,such that it meets the requirements of the Law.
6. The disclosures made by Majestic in the bidder's statement referred to in Namakwa's application were as follows:
- (a) *Letter to shareholders* - the letter to shareholders on page 2 of the bidder's statement refers to the following benefits which Namakwa argued were misleading or inadequate:
 - (i) *Improved market profile* – Majestic suggests that the Majestic/Namakwa group has the potential to deliver more than 180,000 carats of annual production when all five (5) of the proposed production plants are in operation by the end of 2002;
 - (ii) *Mining Resources* – Majestic states that the Majestic/Namakwa group would have a “mineable resource” of over 100 million tonnes of diamondiferous gravels in two (2) strategic locations;
 - (iii) *Immediate management and operating benefits* – Majestic states that its exploration, construction and operational management structure in place in South Africa will deliver immediate benefits for the rapid development and operation of the Namakwa projects;
 - (iv) *Reduced Investment Risk* – Majestic states that the Majestic/Namakwa Group is likely to benefit from enhanced cash flows generated by the production of smaller diamonds from the Namakwa properties combined with the cash flow from the larger diamonds

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found on the Majestic properties. Majestic also notes that, in its first 3 months of operations, Majestic found a 123 and an 83 carat diamond - the two largest diamonds ever discovered by an Australian company;

- (v) *Accelerated development* – Majestic does not provide information as to how Majestic proposes to develop the relevant projects, the extent of accelerated development, nor a timetable of anticipated cash flow; and
 - (vi) *Established marketing network* – Majestic states that Namakwa shareholders will be able to benefit from immediate access to Majestic’s diamond marketing arrangements in Antwerp with Reliance bvba. Majestic does not, however, provide any further details in respect of the contractual arrangements with Reliance bvba, nor does it provide details of previous sales by Reliance bvba on behalf of Majestic. Similarly, no information in respect of Reliance bvba’s competitive advantage to market Namakwa’s diamonds is provided.
- (b) *Offer Premium* - Majestic has attributed a value of 35.3 cents to its shares for the purposes of comparing its offer with the Namakwa share price (representing the weighted average market price of a Majestic fully paid share over the five trading days preceding the date of the bidder’s statement). Majestic states that the value ascribed represents a premium of 41% over the issue price of Namakwa shares offered under the Namakwa prospectus dated 15 December 2000. Namakwa argued that, because of the price and volume surge in trading of Majestic shares around 8 March 2001, reference to the offer premium is misleading;
- (c) *Market interest and liquidity* – Namakwa argued that Majestic’s statement that there should be substantially greater market interest in Majestic and consequently greater liquidity in its shares following Majestic’s takeover of Namakwa than currently exists for either Majestic or Namakwa was without foundation, misleading and deceptive;
- (d) *Information about Majestic* – Majestic submitted that Majestic’s general level of disclosure about its key production and exploration assets was inadequate;
- (e) *Effect on Balance Sheet* – Namakwa submitted that the unaudited proforma consolidated balance sheet of Majestic and its

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controlled entities as at 31 December 2000 adjusted for certain events was misleading or deficient in a number of respects.

INTERIM ORDER

7. We decided not to make an interim order restraining Majestic from dispatching its bidder's statement to Namakwa shareholders. We did not consider that the balance of convenience favoured granting the interim order in this case. The application by Namakwa did not, in our view, disclose sufficiently clear and serious inadequacies in Majestic's disclosure. We were therefore satisfied that remedial orders would be an adequate remedy if Namakwa's allegations were substantiated.

SUBSTANTIVE ISSUES

Production Claims

8. The statements in the chairman's letter about proposed production plants and output are forward-looking statements which go beyond anything for which Majestic or Namakwa has disclosed a reasonable basis.

9. The passage in the Chairman's letter runs:

'Improved market profile - the Majestic/Namakwa Group has the potential to become one of the world's largest publicly-listed alluvial diamond producer[s], with more than 180,000 carats of annual production when all five of the proposed production plants are in operation by the end of 2002.'

10. Majestic does not explain in the bidder's statement or in previous market disclosures which five plants it has in mind or how it proposes to produce 180,000 carats per annum. In its submissions in response to the Panel's brief, Majestic advises that the five proposed plants are:

Riet River	commissioned in November 2000
Pniel Estate	commissioned in April 2001
Orange River	construction was to start in May 2001. It will not now begin before the end of June
Vaal River	Majestic proposes to start construction in December 2001
Namakwa	target's prospect – Majestic proposes to start construction in April 2002

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11. The bidder's statement states that:

'Majestic has secured and is evaluating further properties at Riet River [this is additional to the existing mine], Orange River [this is the mine about to be built], Bloemoff/Christiana [this is the Vaal River prospect] and Namaqualand [this is a separate prospect to Namakwa's]' (page 18),

and that Majestic intends to:

'finance Namakwa's projects to mining status', subject to a review to determine 'which, if any, require further development and refinement' (page 26).
12. Majestic's Quarterly report for the quarter to 31 December 2000 was released on 31 January 2001. It indicates that exploration was then at an advanced stage on the Orange River property, but had barely commenced at Bloemoff/Christiana and Namaqualand. The most recent release indicates that early drilling has been conducted at Orange River and was satisfactory.
13. It was reasonable to include Orange River as a proposed mine, but both Vaal River and Namakwa are as yet unexplored. Majestic bases its plans on old prospecting, neighbouring tenements and information published by Namakwa itself about its prospect. There is little firm information on the Vaal River prospect.
14. Most of Majestic's proposed production (120,000 out of 180,000 carats) would come from a mine on Namakwa's prospect. Namakwa, however, proposes to spend \$3.7 million over 18 months proving up this prospect before committing to mine it, and the geologist's report in its prospectus concludes at para 3.7 that:
 - (a) there is adequate evidence of gravel deposits, but limited evidence of the distribution of economic quantities of diamonds in the gravels;
 - (b) the available data 'justify comprehensive exploration';
 - (c) 'it is realistic to expect that the exploration results will justify the project proceeding to a full mining feasibility study'; and
 - (d) 'It is not possible at this stage to surmise about the size of a future operation'.
15. This falls a long way short of predicting that a mine can be developed in less than 2 years, to produce 120,000 carats per annum.
16. We requested Majestic to disclose which plants it proposes to construct, their respective intended outputs and the timetables and risk factors for

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each of them. In particular, Majestic should explain that the timetables for the proposed plants at Vaal River and Namakwa and their outputs are dependent on exploration which is far from complete. We required Majestic to provide this additional information in a supplementary bidder's statement.

Reserves and Resources

17. The statements in the chairman's letter concerning reserves are also forward-looking statements which go beyond anything for which Majestic or Namakwa has disclosed a reasonable basis. The reserves and inferred resources mentioned in the two companies' publications to date are about half of the 100 million tons which Majestic has claimed exist within the Majestic and Namakwa tenements.
18. The total of the well-explored reserves is much less than this. In previous ASX releases, Riet River is given as 8.3 million tons, Pniel Estate as 3 - 5 million tons and Orange River as up to 20 million tons. There are no firm figures for Vaal River. The independent geologist's report accompanying the Namakwa prospectus says only that the resource is at least 5-10 million tons, although there are indications that it could be 20 million tons or even more.

JORC Code

19. The JORC Code is an industry code, issued by the Joint Ore Reserves Committee of The Australasian Institute of Mining and Metallurgy, the Australian Institute of Geoscientists and the Minerals Council of Australia, and is binding on members of those bodies. The Code has also been incorporated into the Listing Rules of the Australian Stock Exchange and the New Zealand Stock Exchange, and is widely used by mining companies, even outside Australia.
20. The JORC Code attempts to improve and standardise disclosures about mineral resources and ore reserves. Prior to the adoption of the JORC Code, disclosures regarding mineral reserves and ore reserves were often woefully inadequate or misleading. The terms recommended by the JORC Code for the description of mineral resources and ore reserves have become standard usage in publications by listed companies, and material departures from them risk being misleading.
21. In its bidder's statement Majestic uses the term "mineable resources" to describe the diamond bearing gravels that it proposes to mine. The JORC Code does not have a category called a 'mineable resource'. It requires minerals to be described as 'resources' (with various qualifications) where the reference is to the amount and description of minerals (without reference to whether they can be economically mined)

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and as 'reserves' (again with various qualifications) where the reference is to what can be practically and economically mined.

22. Majestic advised the Panel that it has chosen to use an expression which does not comply with the JORC Code, because it has difficulty complying with the Code.
23. Mr Manfred Marx, a director of Majestic, states in a statement to support Majestic's response to the brief that:

'Majestic has purposely not used the JORC classification of resources and reserves because they share the view expressed by the JORC Code that low grade secondary or alluvial diamond sources are "variable and complex".'
24. The use of the expression "mineable resource" allows Majestic to state that a resource of a certain size is rated highly and has a good chance of being mined. Such a resource usually contains ore of different grades and kinds, in different locations, some of them economic to mine, others not. Majestic's own reports state that some gravels, although diamond-bearing, are too poor, too deeply buried or too small to be worth mining. The JORC Code category of a reserve focuses on how much of a resource can be practically and economically mined. The use of the concept of a "mineable resource" is potentially misleading as it dodges precisely this issue. The JORC Code requires greater precision, not less, because of the 'variable and complex' nature of secondary diamond resources.
25. We did not accept the company's explanation for the use in its ASX announcements and the bidder's statement of the expression "mineable resources" in disregard of the requirements and categories of the JORC Code.
26. We considered that the reserves and resources should be restated by Majestic in terms which comply with the JORC Code, including classifying them into resources and reserves and stating the nature of each geological environment, together with its form, age and size. We requested Majestic to provide this information in a supplementary bidder's statement.

Offer Premium

27. We considered that Majestic's claimed premium of its offer over the issue price of Namakwa shares was misleading. The premium was based on Majestic share prices over a period of 5 days before the issue of the bidder's statement. Those prices were unrepresentative, because they were higher than the prices during most of the three months before the bid was announced. The highest and lowest figures provided by Majestic were not adequate to illustrate the market in Majestic shares over that period. We therefore considered that Majestic should provide

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price and volume charts for trading in Majestic shares over the three months before the bid was announced in a supplementary bidder's statement.

Pro Forma Balance Sheet

28. The assumptions underlying the proforma balance sheet included in Majestic's bidder's statement balance sheet were not disclosed and we considered that that it was misleading without them. To remedy this we required that the following additional information should be provided in a supplementary bidder's statement:
- (a) the balance sheet should be clearly labelled as an unaudited balance sheet;
 - (b) all assumptions and notes on which it relies should be set out;
 - (c) in particular, the notes should list the post-balance date events listed in Majestic's half-yearly accounts as at 31 December 2000 and state which of them have been taken into account;
 - (d) it should be stated that Majestic will not have unrestricted access to cash held by Namakwa, unless it obtains 100% control of Namakwa; and
 - (e) the half-yearly accounts themselves should also be incorporated by reference and a copy offered to any offeree who required one.

Forecasts

29. We did not require Majestic to provide financial forecasts. However, as Majestic has chosen to refer to its projected production, we required it to provide to shareholders any financial information available to directors about that projected production, with detailed reference to specifically relevant risks, or a full explanation why it is not doing so, clarifying whether it has reasonable grounds for the projections. We requested this information to be provided in a supplementary bidder's statement.

Other issues raised by Namakwa

30. In relation to the other matters raised by Namakwa in its application, we were satisfied that the disclosure of Majestic was not misleading or inadequate. We also considered that these were largely matters of opinion or judgement, on which it would be appropriate for Namakwa to comment in its target's statement.

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DECISION

31. We decided to conduct proceedings in relation to the application under Regulation 20 of the Australian Securities and Investments Commission Regulations.
32. We were satisfied that, taking into account Majestic's reliance on sections 712 and 713, the bidder's statement did not provide all of the information which offerees would reasonably require to assess the merits of Majestic's bid, in the respects set out in these reasons above. Accordingly, on 26 April, we made a declaration of unacceptable circumstances under section 657A in relation to the bid.
33. A copy of the declaration is at Annexure A to these reasons.
34. We considered whether it would be sufficient for Namakwa to deal with these issues in its target's statement. However, we concluded that this would not provide sufficient clarification, as they were matters of fact, on which specific clarifications were needed and most of the relevant facts were best known to Majestic.
35. We requested Majestic to provide an undertaking to the Panel to prepare a supplementary bidder's statement dealing with the issues referred to in these reasons and to provide a copy to the Panel for examination by 2 May 2001, with a view to providing it to Namakwa and posting it to offerees by 4 May 2001.²
36. On 4 May, we examined the draft supplementary bidder's statement provided to us by Majestic and provided a number of comments to Majestic, including that:
 - (a) the statement should explain that it corrects statements in the Chairman's letter and original bidder's statement, at the direction of the Panel, to correct or supplement deficiencies in the originals;
 - (b) the pro forma balance sheet should:
 - (i) include a column for Majestic as a standalone entity;
 - (ii) include numbered footnotes on all post-balance day events and assumptions (for both Majestic and Namakwa) and their effect should be quantified;

² The supplementary bidder's statement was subsequently dispatched to shareholders by Majestic on 7 May 2001.

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- (iii) include a reference number to the relevant footnote in each line item affected by a post balance date event or assumption;
 - (iv) set out the number of Majestic shares to be issued and the values assumed for those shares and for Namakwa shares, under each merged entity column; and
 - (v) be prefaced with a statement that it should be read in conjunction with the notes;
- (c) the statement that Majestic can only access cash in Namakwa if it obtains 100% acceptances or shareholder approval should be under a separate heading and the amount of cash Majestic had at 31 March should then be set out;
- (d) the statement should set out the net asset backing of a Majestic share in the following three scenarios:
- (i) Majestic pre bid;
 - (ii) Majestic owning 51% of Namakwa; and
 - (iii) Majestic owning 100% of Namakwa;
- (e) references to "economic diamondiferous gravels in the measured and indicated categories" should be replaced with expressions referring to probable and proven reserves, as appropriate; and
- (f) Majestic should check a number of dates referred to in the statement to confirm their accuracy.
37. To allow Namakwa time to respond to the supplementary bidder's statement in a supplementary target's statement and to allow offerees sufficient time to consider that document, we requested Majestic to extend its bid until at least 28 May 2001. We also requested Majestic to offer all shareholders who had accepted Majestic's bid prior to dispatch of the supplementary bidder's statement an opportunity to withdraw. Majestic subsequently extended its bid until 28 May 2001 and offered accepting shareholders an opportunity to withdraw as requested by the Panel.
38. We decided not to make any orders for costs. We granted all parties leave to be represented by their solicitors.

Nerolie Withnall

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President of the Sitting Panel

Decision dated 27 April 2001

Reasons published 15 May 2001

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Annexure A

CORPORATIONS AND SECURITIES PANEL

CORPORATIONS LAW – SECTION 657A

DECLARATION

Whereas

- (a) Majestic Resources NL (*Majestic*) has made offers to acquire all of the ordinary shares in Namakwa Diamond Company NL (*Namakwa* and the *Bid*) and issued a bidder's statement (the *Bidder's Statement*) in relation to the Bid;
- (b) The Bidder's Statement includes or is accompanied by a letter by the Chairman of Majestic which makes claims about the production capacity of the merged entity comprising Majestic and Namakwa, which are not substantiated;
- (c) The Bidder's Statement and statements previously issued by Majestic under the Listing Rules of Australian Stock Exchange Limited describe mineral resources in terms at variance with the requirements of the Australian Code for Reporting of Mineral Resources and Ore Reserves of the Joint Ore Resources Committee;
- (d) The Bidder's Statement includes a pro forma balance sheet for the merged entity, material assumptions underlying which are not set out in the Bidder's Statement or otherwise disclosed;
- (e) The Bidder's Statement claims that the Bid offers a premium over the issue price of shares in Namakwa, based on market prices for shares in Majestic which are not representative of the market for shares in Majestic in the recent past,

The Panel declares that unacceptable circumstances exist in relation to the affairs of Namakwa.

26 April 2001

Nerolie Withnall
President