



**In the matter of Phosphate Resources Limited  
[2003] ATP 03**

**Catchwords:**

*Rights issue following buyback – underwriting of rights issue – use of exemptions to confer control – shareholder approval for rights issue – transferring control without control premium – undertaking to Panel*

*Corporations Act 2001 (Cth), sections 606, 611 and 657C(3)*

**These are our reasons for declining to make a declaration of unacceptable circumstances in response to the application (Application) by Mr Gerry Pauley and Dr Gordon Elkington (Shareholders) in relation to a buy-back of 25% of the shares, and a proposed one-for-three rights issue, by Phosphate Resources Limited (PRL) (an unlisted public company). The Panel considered that undertakings offered in relation to obtaining shareholder approval for a rights issue, or underwriting by Asset Backed Holdings Limited (ABK), in the next 12 months sufficiently addressed its concerns in relation to the buy back and the proposed rights issue.**

1. The sitting Panel (the **Panel**) comprised Ms Marie McDonald (sitting President), Mr Chris Photakis (sitting Deputy President) and Mr Andrew Knox.
2. The Panel decided, under Regulation 20 of the ASIC Regulations, to conduct proceedings.

**Summary**

3. In June 2002, PRL approved a buy-back of 25% of the shares on issue at a price of \$4.00 per share (the **Buy-Back**). The Buy-Back offer closed on 31 July 2002 and the 25% of PRL's shares were cancelled on 7 August 2002. In December 2002, PRL proposed a one-for-three rights issue of ordinary shares at \$4.00 a share (the **Proposed Rights Issue**), partially underwritten by ABK.
4. As a result of the Buy-Back and the Proposed Rights Issue, assuming there was a complete shortfall in the Proposed Rights Issue, ABK's percentage holding could have risen from 19.9% to up to 39.6%.<sup>1</sup>
5. The Application submitted that the Buy-Back and the Proposed Rights Issue together were part of a planned artifice designed to give control of PRL to ABK without the payment of a control premium.
6. Following some extensive enquiries by the Panel, PRL informed the Panel that it would not proceed with the Proposed Rights Issue. PRL provided an undertaking to the Panel that, for the next 12 months it would not

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<sup>1</sup> As a result of the Buy-Back ABK's percentage holding rose from 19.9% to 26.7%. If there were a complete shortfall in the Proposed Rights Issue, ABK's percentage shareholding would have risen from 26.7% to 39.6%.

## Takeovers Panel

### Reasons for Decision - [Phosphate Resources Limited]

(a) proceed with a rights issue that could lead to ABK obtaining an increase in its shareholding above that which it would have been entitled to acquire under item 9 of section 611 (the 3% creep provision); or

(b) proceed with an underwriting of any rights issue by ABK,

without, in each case, shareholder approval by ordinary resolution ignoring any votes cast by ABK and its associates, and ABK's directors and their associates.

7. The Panel considered that the decision not to proceed with the Proposed Rights Issue together with PRL's undertaking would satisfy the Panel's concerns. Accordingly the Panel decided to decline the application for a declaration of unacceptable circumstances.

### Background

8. The following is a description of the facts underlying the Application, which has largely been taken from the Application.

9. PRL is an unlisted public company incorporated in Western Australia. It has approximately 240 shareholders. Commencing in August 2001, ABK acquired 19.9% of PRL, becoming its principal shareholder.

10. At the time of the application the directors of ABK included Michael Perrott, Peter Huston, David Argyle and Antony Rigoll. Mr Perrott, Mr Argyle and Mr Rigoll were also directors of PRL. Mr Perrot was appointed a director of PRL on 18 September 2002 and Mr Rigoll was appointed on 25 January 2002. Mr Argyle was the managing director of PRL from 1991-1994. He was appointed a director of ABK on 18 February 2002. Mr Huston was a legal adviser to PRL.

11. In June 2002 the Board of PRL held a general meeting to seek the support of shareholders for the buy-back of up to 25% of the shares on issue at a price of \$4.00 per share. The reasons for the Buy-Back were stated to be that shareholders had expressed an interest to PRL in selling their shares and PRL was expecting to receive a windfall payment of \$3.5 million.

12. The Buy-Back was approved by approximately 74% of shareholders and PRL bought back 25% of the shares on issue. The Buy-Back offer closed on 31 July 2002 and the shares were cancelled on 7 August 2002.

13. The Buy-Back consideration totalled \$4.2 million and it was paid on the following dates:

- \$1,021,200 was paid in September 2002;
- \$2,150,000 was paid in October 2002;
- \$300,000 was paid in December 2002; and
- \$728,800 remained outstanding at the time of proceedings.

14. ABK did not sell into the Buy-Back. The Buy-Back resulted in ABK's percentage holding in PRL increasing from 19.9% to 26.7%.

## Takeovers Panel

### Reasons for Decision - [Phosphate Resources Limited]

15. In December 2002, PRL told shareholders that it needed to raise money in order to fund various projects including an accelerated mining program due to the Asia Pacific Space Centre Project and the proposed extension of the Christmas Island airport. PRL proposed a one-for-three issue of ordinary shares at \$4.00 a share, underwritten as to approximately 64% by ABK.
16. If fully subscribed the Proposed Rights Issue would have created almost exactly the same number of shares as were bought back and would have raised almost the same amount of money as was paid out by the Buy-Back.
17. If there had been a complete shortfall in the Proposed Rights Issue, ABK's percentage holding of PRL could have risen to 39.6%.
18. On 3 January 2003, ASIC issued an interim stop order in respect of the offer information statement for the Proposed Rights Issue (**Offer Information Statement**). ASIC had identified a number of concerns with the Offer Information Statement, including various disclosure issues. ASIC was of the preliminary view that the ABK underwriting agreement was a related party transaction and that shareholder approval would be required under Part 2E.1 of the Corporations Act (the **Act**).
19. At the time that the application was lodged, a petition was being circulated amongst PRL shareholders opposing the rights issue and calling for a general meeting to seek the removal of a number of the Board members. The requisitioned general meeting of PRL was due to be held on 1 March 2003.

#### **the Application**

20. The Shareholders submitted that, when considered in the light of the Buy-Back, the Proposed Rights Issue is likely to have the effect of transferring control of PRL to ABK without the payment of a takeover premium. The shareholders submitted that the circumstances would suggest that this was the intention.

#### *Interim orders sought*

21. The Shareholders sought interim orders under section 657E(1) of the Act that, pending the final determination by the Panel of these proceedings, PRL be restrained from issuing any shares to participants or the underwriters to the Proposed Rights Issue.

#### *Final orders sought*

22. The Shareholders also sought an order that ABK be prevented from underwriting the Proposed Rights Issue without the approval of PRL shareholders other than ABK.

#### **Submissions**

23. The Shareholders submitted that the proximity of the Buy-Back to the Proposed Rights Issue and the absence of cogent commercial reasons for the diametrically opposed corporate actions suggested that they were an artifice designed to give control of PRL to ABK without the payment of a control premium.
24. PRL submitted that the decisions to proceed with the Buy-Back and the Proposed Rights Issue were independent decisions that were legitimately made by PRL's Board

## Takeovers Panel

### Reasons for Decision - [Phosphate Resources Limited]

of directors. PRL noted that the composition of the Board had changed between the relevant times and that at the time of the Buy-Back there was no contemplation of the Proposed Rights Issue being undertaken. In particular, PRL noted that the decision to proceed with the Proposed Rights Issue was justified by an analysis conducted by the new chairman and director, Mr Perrot. This occurred in September 2002, after the cancellation of shares under the Buy-Back.

#### Discussion

#### Timing and jurisdiction

25. Under section 657C(3) of the Act, an application for a declaration of unacceptable circumstances can only be made within 2 months after the circumstances have occurred, or a longer period determined by the Panel. The Panel noted that the Buy-Back occurred more than 2 months before the application was made. However, the allegation was that the Buy-Back, the Proposed Rights Issue and the underwriting together gave rise to the unacceptable circumstances. The Proposed Rights Issue and the underwriting were still current at the time that the application was made. Therefore the Panel considered that it had jurisdiction to hear the application without the need to determine a longer period for the application to be made.

#### *Section 611*

26. The Panel notes generally that it would constitute unacceptable circumstances for a company to use the exemptions in section 611 of the Act to create an artifice designed to give one of its shareholders control.

#### *Procedure and submissions*

27. The Panel sought submissions with a view to understanding how and when the decision was made that the company would need the additional money and why the company did not realise that it would shortly be needing funds at the time it decided to proceed with the Buy-Back.
28. After the Panel issued its brief to the parties and before submissions were received, PRL proposed an undertaking to the Panel that it would:
- (a) not issue shares to ABK under the underwriting agreement unless the underwriting agreement was approved by the shareholders of PRL;
  - (b) lodge a supplementary Offer Information Statement that included an elaboration of the reasons for proceeding with the Buy-Back and the reasons for conducting the Proposed Rights Issue; and
  - (c) not issue any shares pursuant to the Proposed Rights Issue until 8 March 2003, which was after the date that the shareholder requisitioned general meeting was to be held.
29. The Panel considered that the submissions and evidence provided at that time were insufficient to rebut the inferences which the Shareholders had drawn and the Panel considered that there was a case for those inferences. The Panel noted that their concerns related to both the Proposed Rights Issue and the underwriting. Even if PRL did not proceed with the underwriting agreement, the combination of the Buy-

## Takeovers Panel

### Reasons for Decision - [Phosphate Resources Limited]

Back and the Proposed Rights Issue could lead to an increase in ABK's shareholding from 19.9% (before the Buy-Back) up to approximately 32.6%. The Panel had concerns as to why the board of PRL decided to proceed with the Buy-Back when shortly after the Buy-Back was completed the company sought to raise funds through the proposed rights issue.

30. Therefore the Panel decided to continue its investigations and it sought further evidence from the parties to gain a fuller understanding of the circumstances.
31. The Panel did not find any direct evidence that the Buy-Back and the Proposed Rights Issue were an artifice designed to give control of PRL to ABK. However, the evidence provided by the parties did not satisfactorily explain why PRL decided to complete the Buy-Back although it shortly afterwards decided that it would need additional money. The evidence tendered also did not properly explain why PRL was not, or should not reasonably have been, aware of the projects for which it said the funds from the Proposed Rights Issue would be needed, at the time it conducted the Buy-Back. The Panel might have conducted further investigations however the Panel accepted undertakings to resolve the matter as explained below.
32. On 28 January 2003, PRL informed the Panel that the Board had determined not to proceed with the Proposed Rights Issue and underwriting.
33. On 30 January 2003, PRL offered a revised undertaking to the Panel that, for the next 12 months, it would not:
  - (c) proceed with a rights issue that could lead to ABK obtaining an increase in its shareholding above that which it would have been entitled to acquire under item 9 of section 611 (the 3% creep provision); or
  - (d) proceed with an underwriting of any rights issue by ABK,without, in each case, shareholder approval by ordinary resolution ignoring any votes cast by ABK and its associates, and ABK's directors and their associates, and that PRL shareholders would be provided with adequate information which at least complies with item 7(b) of section 611 and relevant ASIC policy for the purposes of the shareholder meeting.
34. PRL informed the Panel that it would withdraw its Offer Information Statement dated 6 December 2002 regarding the Proposed Rights Issue. On 12 February 2003 PRL confirmed to ASIC that it had withdrawn its Offer Information Statement and that it consented to the issue of a final stop order by ASIC under s739(1) of the Act.
35. The Panel considered that the decision not to proceed with the Proposed Rights Issue together with the proposed undertaking made the Panel's concerns redundant. In particular, the Panel noted that PRL shareholders would have a veto over any increase on ABK's position which is not substantially equivalent in terms of control change to something that could occur under item 9 of section 611 of the Act (the 3% creep provision).

## **Takeovers Panel**

### **Reasons for Decision - [Phosphate Resources Limited]**

#### **Decision**

36. The Panel accepted PRL's undertakings and on the basis of those undertakings the Panel has decided to decline the application for a declaration of unacceptable circumstances in relation to the affairs of PRL.
37. The Panel advised the parties of its final decision in this matter on 31 January, once it had received the undertakings set out above from PRL.
38. The Panel made no order as to costs.
39. The Panel consented to the parties being represented by their commercial solicitors in the matter.

**Marie McDonald**

**Sitting President**

**Phosphate Resources Limited**

**3 April 2003**