Takeovers Panel

Reasons for Decision
National Can Industries 01

In the matter of National Can Industries Limited 01
[2003] ATP 35

Catchwords:
Association - break fee – efficient market - substantial holder – related party – relevant interest – lock-up device – review of ASIC decision – undertaking to Panel – shareholder approval – scheme of arrangement

Corporations Act 2001 (Cth), chapter 2E, sections 12, 606, 608, 609, 671B
Takeovers Panel Guidance Note 7 – 'Lock-up Devices'

These are our reasons for concluding proceedings in relation to the affairs of National Can Industries Limited following acceptance by the Panel of undertakings by ESK Holdings Limited and National Can Industries Limited.

THE APPLICATION & PROCEEDING

1. These reasons relate to an application (the **Application**) to the Panel from Visy Industrial Packaging Holdings Pty Ltd (**VIPH**) on 19 September 2003 in relation to the affairs of National Can Industries Limited (**NCI**), a company listed on the stock market of Australian Stock Exchange Limited (**ASX**). The Panel concluded the proceeding (the **Proceeding**) arising from the Application following acceptance by the Panel of undertakings provided by NCI and ESK Holdings Pty Ltd (**ESK**).
2. VIPH is a substantial holder in NCI. It alleged that unacceptable circumstances arose from an implementation agreement under which ESK would acquire control of NCI through a scheme of arrangement. It also alleged a breach of the acquisition prohibition in section 606, and the substantial holding notice provisions in Chapter 6C, of the Corporations Act 2001 (Cth) (**Act**).
3. VIPH sought a declaration of unacceptable circumstances, orders to set aside the agreements and repayment of a break fee, revocation or variation of a modification provided by ASIC and disclosure of various associations and relevant interests in shares in NCI.
4. We decided not to revoke or vary the ASIC modification. We made no declaration of unacceptable circumstances or orders. We accepted undertakings provided by NCI and ESK in relation to the amount ESK would offer to acquire public shareholdings in NCI under the scheme of arrangement and that ESK would repay to NCI a break fee should a rival bid succeed. These undertakings are set out in Annexures A and B to these reasons (the **Undertakings**).

THE PANEL & PROCESS

5. The President of the Panel appointed Andrew Lumsden (sitting President), Anthony Burgess (sitting Deputy President) and Denis Byrne as the sitting Panel for the Proceeding.

6. We adopted the Panel's published procedural rules for the purposes of the Proceedings.

APPLICATION

Factual background – chronology of events leading up to the Application

7. The following is a description of the facts underlying the Application which has largely been taken from the Application and the submissions from the parties.

First Scheme

8. On 21 July 2003, NCI announced to ASX that (amongst other things):

   (a) NCI had signed an implementation agreement (**First Implementation Agreement**) with ESK pursuant to which ESK proposed to acquire all of the shares in NCI that were not owned by Tyrrell family members or companies controlled by Tyrrell family members (**Tyrrell Interests**), for a price of $1.40 cash per share (**First Proposal**);

   (b) it was proposed that the acquisition be implemented by way of a scheme of arrangement (**First Scheme**);

   (c) the independent directors of NCI believed that the transaction was in the best interests of NCI's minority shareholders and unanimously recommended that shareholders support the transaction;

   (d) NCI's independent directors would appoint an independent expert to provide an opinion on the proposed transaction – they appointed Grant Samuel & Associates Pty Limited (**Grant Samuel**);

   (e) NCI would reimburse a fixed amount of $1 million to ESK if the independent directors changed their recommendation or NCI is in breach of the First Implementation Agreement (**First Break Fee**); and

   (f) NCI had also agreed not to actively solicit an offer or proposal from any other person to acquire all or a substantial part of NCI's business, to acquire a substantial holding in NCI, or to acquire control of, or merge with, NCI (**First Lock Up**).

9. NCI's 21 July 2003 announcement noted the following about the offer price:

   '*The agreed price of $1.40 per share values NCI's ordinary equity at approximately $94 million and represents a premium of:*

   - *30% to the 12 month volume weighted average share price;*
   - *18% to the 6 month volume weighted average share price;*
   - *16% to the 3 month volume weighted average share price;*
   - *12% to the closing price on Friday 18 July 2003.*

The NCI share price has not traded in excess of the agreed price of $1.40 for over 3 years. In addition, only 15% of NCI's issued shares have been traded in the last 12 months.'

10. ESK is a company whose sole shareholder and sole director is Mr. Michael Tyrrell (**MT**), the current managing director of NCI and the son of NCI's founder, Mr. Harry Tyrrell.

11. During the discussions with MT which culminated in the First Proposal, the independent directors of NCI obtained a report from Deloitte Corporate Finance dated 4 March 2003 assessing the indicative fair equity value of NCI as being in the range of $1.28 to $1.54 per share. That report also addressed a number of related matters in relation to the proposed transaction such as taxation implications, financial capacity of the bidder, profile of the shareholders and relevant strategic considerations.

Substantial holder notices

12. On 2 November 2000, Tyrrell Investments Pty Ltd (**TI**) lodged a substantial holding notice with ASX (**November 2000 Notice**) disclosing relevant interests in shares in NCI of various Tyrrell Interests, including associations between the Tyrrell Interests, each of whom was stated to be entitled to 50.79% of the voting shares in NCI.

13. On 22 July 2003, TI gave a notice to NCI and ASX (**July Notice**) that a change in the interests of TI and certain other persons in voting shares in NCI had occurred such that the voting power of TI and those other persons had increased from 49.97% to 50.91% and that TI had acquired shares, pursuant to certain share sale agreements, from other members of the Tyrrell family[1]. Those agreements were conditional on the approval of the First Scheme and had the effect of consolidating in TI the Tyrrell Interests in shares in NCI, other than those of MT.

14. On 22 September 2003, TI gave a further notice to NCI and ASX (**September Notice**) that a further change in the interests of TI and other persons in voting shares in NCI had occurred such that the voting power of TI and those persons had varied and further that TI had acquired shares, pursuant to certain share sale agreements, from other members of the Tyrrell family. Those agreements were conditional on the approval of the Second Scheme and had the effect of consolidating the Tyrrell Interests in shares in NCI in TI, other than those of MT (**Tyrrell Consolidation**).

15. The commencing percentage in the July Notice appears to differ from the ending percentage in the previous November 2000 Notice.

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[1] There had been no change in the number of shares on issue and only a vary small change in the number held by any of the Tyrrell Interests between the November 2000 Notice and the 2003 Notices.

Second Scheme

16. The directors obtained Grant Samuel's draft independent expert's report (**GS Report**) dated 26 August 2003 in which Grant Samuel valued NCI in the range of $1.62 - $1.95 per share. Further the report indicated that the offer price of $1.40 in the First Proposal was 14% below the bottom end of the valuation range and concluded that the First Proposal was not in the best interests of NCI non-associated shareholders.

17. As a consequence of a number of developments, including the GS Report, that the market price of NCI shares had substantially exceeded the offer price and recent significant changes in NCI's share register, the independent directors of NCI withdrew their recommendation for the First Proposal and on 18 September 2003, NCI announced to ASX that (amongst other things):

    (a) NCI had signed a revised implementation agreement (**Second Implementation Agreement**) with ESK pursuant to which ESK proposed to acquire all the shares in NCI that are not owned by the Tyrrell Interests, for a price of $1.55 cash per share (**Second Proposal**);

    (b) the Second Proposal replaced the First Proposal;

    (c) it was proposed that the acquisition be implemented by way of a scheme of arrangement (**Second Scheme**);

    (d) the independent directors of NCI believed that the transaction was in the best interests of NCI's minority shareholders and unanimously recommended that shareholders support the transaction, in the absence of a superior offer for all shares in NCI;

    (e) NCI's independent directors had decided that they could no longer continue to support the First Proposal as a consequence of a number of developments, including the receipt of the GS Report that indicated that the First Proposal was not in the best interests of NCI's minority shareholders;

    (f) NCI had paid to ESK the First Break Fee of $1 million (excluding GST);

    (g) NCI's independent directors had appointed Grant Samuel as an independent expert to provide an opinion on the Second Proposal;

    (h) NCI would reimburse up to $100,000 of actual costs incurred in connection with the Second Proposal from 18 September 2003, if the independent directors of NCI change their recommendation or NCI is in breach of the agreement and ESK terminates the agreement as a result (**Second Break Fee**); and

    (i) NCI had also agreed not to actively solicit an offer or proposal from any other person to acquire all or a substantial part of NCI's business, to acquire a substantial holding in NCI, or to acquire control of, or merge with, NCI (**Second Lock Up**).

ASIC Modification

18. On 21 July 2003 ASIC granted a modification (**ASIC Modification**) to vary subsection 609(7) of the Act to disregard the acquisition by TI of relevant interests in shares in NCI which arose from agreements for the Tyrrell Consolidation, conditional on approval of the scheme of arrangement proposed by ESK.

Declarations and orders sought in the Application

Application regarding ASIC Modification

19. VIPH applied to the Panel, pursuant to section 656A of the Act, for review of the decision of ASIC to grant the ASIC Modification. VIPH sought an order either:

    (a) that the decision to grant the ASIC Modification be set aside and substituting a decision not to grant the ASIC Modification for the decision under review; or

    (b) varying the decision to impose a condition in a form substantially similar to the conditions referred to in ASIC's policy on joint bids (IR01/295).

Application regarding unacceptable circumstances

20. VIPH applied to the Panel, pursuant to section 657C, for the Panel to make a declaration of unacceptable circumstances pursuant to section 657A

Interim orders sought

21. VIPH sought the following interim orders:

    (a) preventing NCI, ESK or MT from taking any step or doing any action in furtherance of the Second Scheme (including the distribution of information in relation to the Second Scheme to members of NCI) until the decision of the Panel in relation to the Application;

    (b) preventing ESK or MT from taking any step or doing any action that may result in either of them acquiring a relevant interest in any voting shares in NCI in respect of which they do not already hold a relevant interest until the decision of the Panel in relation to the Application; and

    (c) preventing ESK or MT from taking any step or doing any action that may result in either of them acquiring a relevant interest in voting shares in NCI of a different nature to that already held by them in respect of those voting shares in NCI until the decision of the Panel in relation to the Application.

Final orders sought

22. VIPH sought:

    (a) an order for full disclosure from all relevant persons of the nature of the association between the Tyrrell Interests or any of them in relation to NCI;

(b) an order for full disclosure from all relevant persons of any relevant interest of MT or ESK in voting shares in NCI;

(c) an order for full disclosure from all relevant persons of any relevant agreement through which MT or ESK would have a relevant interest in voting shares in NCI;

(d) an order for full disclosure from all relevant persons of any relevant agreement that contributed to the circumstances which necessitated the lodging of the TI Notice;

(e) an order for full disclosure from NCI of the first independent expert's opinion obtained in relation to the First Proposal (later identified as the GS Report);

(f) an order for full disclosure from MT and ESK of the financing arrangements in relation to the Second Scheme as referred to in the announcement by NCI to ASX on 18 September 2003;

(g) an order cancelling any agreement disclosed pursuant to the orders referred to in paragraphs (c) and (d) that was entered into in contravention of Chapter 6 of the Act or is otherwise unacceptable;

(h) an order cancelling the agreement to pay the First Break Fee and requiring that ESK repay the First Break Fee to NCI;

(i) an order cancelling the agreement to pay the Second Break Fee;

(j) an order cancelling the agreement to enter into the First Lock Up;

(k) an order cancelling the agreement to enter into the Second Lock Up;

(l) such other orders as the Panel considered necessary to ensure that the members of NCI are fully informed of all relevant information in relation to the Second Scheme and to restore all disadvantaged parties to the position they would have been in had the unacceptable circumstances not occurred; and

(m) an order under section 657D(2)(d) that any or all of MT, ESK and NCI bear the costs and expenses incurred by VIPH in relation to the Application, other than costs which relate to that part of the application that relates to the application for review of the decision to grant the ASIC Modification.

DISCUSSION

Break Fees

23. VIPH alleged that unacceptable circumstances arose as a result of NCI's agreement to pay ESK the First Break Fee in the event that any of the independent directors withdrew their support for the First Scheme, NCI's payment of the First Break Fee and NCI's agreement to pay the Second Break Fee.

Agreement to Pay First Break Fee

24. In the First Implementation Agreement of 21 July 2003 between NCI, ESK and MT, NCI agreed to reimburse an amount of $1 million, which was expressed to be a pre-estimate of the expenses which would be incurred by ESK in relation to the First Proposal, including:

    (a) reasonable professional costs of financial, public relations, legal and accounting advisers;

    (b) reasonable costs of management and directors' time;

    (c) reasonable travel and accommodation costs (including on due diligence); and

    (d) reasonable costs of financing ESK's bid.

25. NCI would become obliged to pay the First Break Fee if:

    (a) any independent director of NCI withdrew that director's recommendation of the First Proposal and the First Implementation Agreement was terminated as a result;

    (b) any independent director of NCI withdrew that director's recommendation of the First Proposal and the First Proposal was not approved by the scheme meeting; or

    (c) ESK terminated the First Implementation Agreement as a consequence of a material breach of that agreement by NCI.

26. The First Implementation Agreement expressly contemplated that the independent directors had the right to change or withdraw their recommendation of the First Proposal if the independent expert concluded that the scheme of arrangement was not in the best interests of public shareholders or a superior offer for all NCI shares was made and the independent directors (with the advice of senior counsel) decided their fiduciary duties required them to change their recommendation. Such a change of recommendation might nonetheless lead to payment of the First Break Fee if ESK terminated the First Implementation Agreement.

27. The First Implementation Agreement further provided that part or all of the First Break Fee need not be paid (and is to be repaid, if it has already been paid) if a Court or the Panel determines that the payment is unlawful, involves a breach of directors' duties or constitutes unacceptable circumstances.

28. NCI's independent directors negotiated the First Implementation Agreement with ESK with legal and financial advice. In particular, Deloitte Corporate Finance advised that an offer price within the range $1.28 to $1.54 would provide an outcome in the best interests of minority shareholders.

29. When negotiations commenced, it was on the basis that the First Break Fee would be $500,000. NCI's independent directors pressed ESK to increase its offer price from $1.37 to $1.40, and, when ESK agreed to do so, NCI's

independent directors agreed to increase the First Break Fee to $1 million as part of the negotiated arrangements leading to this increase.

Payment of the First Break Fee

30. As mentioned above, NCI paid the First Break Fee to ESK when the independent directors of NCI withdrew their recommendation of the First Scheme on receipt of the GS Report and ESK terminated the First Implementation Agreement. At the same time, they agreed to recommend the Second Scheme and to pay the Second Break Fee.

Submissions on the Break Fees

31. The Application contended that the payment of the First Break Fee:

    (a) tended to inhibit an efficient, competitive and informed market in shares in NCI;

    (b) denied shareholders equality of opportunity to participate in benefits accruing under ESK's proposal to acquire a substantial interest in NCI; and

    (c) was an inappropriate exercise of the directors' powers.

32. It is true that ESK, which was closely associated with a shareholder in NCI, received a benefit which would not be available to other shareholders. However, that is a normal effect of payment of a break fee, and the Panel's policy as set out in the Panel's Guidance Note on Lock-Up Devices (**GN7**)[2] is that such a benefit is reasonable, if it is under the 1% guideline and otherwise paid in appropriate circumstances.

33. Matters concerning directors' duties and related party transactions are not as such and without something to link them to Chapter 6 issues, within the Panel's functions. We discuss VIPH's reservations about the First Break Fee and Second Break Fee below, in connection with an assessment whether the payment of the First Break Fee detracted unacceptably from an efficient, competitive and informed market in shares in NCI.

34. Any break fee may inhibit an efficient market in shares in the relevant company, depending on its impact on declared and prospective bidders for the company. GN7 deals with when break fees are unacceptable because of their adverse effect on market efficiency. GN7 lists a number of factors which the Panel will take into account, but is explicit that other factors will be relevant on occasion.

35. Any adverse effect of the payment of the First Break Fee on the efficiency of the market in shares in NCI is marginal. The fee was 1% of the value of the company, an amount specified in GN7 as immaterial to competition for control.

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[2] GN7 at para 7.14

36. We rejected a submission that the 1% benchmark was inapplicable in these circumstances because the ESK proposal related to a scheme of arrangement. The expense incurred by an acquirer under a members' scheme of arrangement may be as great as that incurred by a bidder under a Chapter 6 bid, and the cases for and against the scheme company meeting some of that expense are similar to the corresponding arguments in relation to a bid, except that the expense incurred directly by the scheme company is often higher.

37. We also rejected a submission that the 1% benchmark was inapplicable because the Tyrrell Interests already held over half of the shares in NCI. If both bids are full bids, a break fee has the same effect on the respective prices per share paid by the bidder who receives the fee and by a rival bidder who does not receive the fee, regardless of the number of shares each of them holds when the fee is paid or agreed to be paid.

38. The First Break Fee corresponded to amounts actually and not unreasonably paid as the costs of putting a corporate opportunity before shareholders. The fact that the Tyrrell Interests hold over 50% of the shares in NCI and favour the ESK proposal does not mean that the ESK proposal will succeed, but it makes it difficult for any rival proposal to succeed.

39. Although the effect of payment of the First Break Fee on market efficiency was marginal, we consider that the payment of the fee in these circumstances was unacceptable because it affected a proposed acquisition of a substantial interest and resulted from a decision of the Board of NCI which in our view was not appropriate in the circumstances of the ESK proposal. The agreement to pay the First Break Fee was unacceptable because:

    (a) ESK was a related party of the Tyrrell family, who have a controlling interest in NCI;

    (b) the initiative for the ESK proposal lay with ESK, not with NCI, and it does not appear that there was any urgency about the First Proposal from NCI's point of view;

    (c) the independent directors agreed to pay the First Break Fee before they had received the independent experts' report which would be provided to shareholders;

    (d) the payment of the First Break Fee tended to inhibit competition in the market for control of shares in NCI; and

    (e) the obligation to pay the fee was not triggered by rejection of the ESK proposal by shareholders, but by a decision of any one of the independent directors to withdraw their initial recommendation of the proposal. This trigger would tend to fetter the ability of the directors to carry out their duties.

40. In these circumstances, we consider that it was not necessary to agree to the fee to attract MT's attention to NCI, and away from other possible targets. While the Tyrrell Interests retained their controlling shareholding, it was unlikely that

MT would lose interest in NCI. Since MT could wait, but was unlikely to lose interest, he was likely to decide whether and when to bid for NCI on the basis of personal and family considerations, rather than being persuaded by the board and their agreement to pay the First Break Fee.

41. It seems to us that the independent directors could also afford to wait. Nothing about the financial or business position of NCI appears to require the bid to be made sooner, rather than later. In this situation, the independent directors did not need to rush into a decision and thus had time to obtain the independent experts' recommendation with respect to the valuation of the company.

42. In these circumstances, we do not entirely reject the notion that a fee should be payable if and when a proposal the directors have endorsed is rejected by shareholders. As GN7 puts it, such a fee may be an appropriate price to secure an opportunity broadly in the nature of an option.[3]

43. But the fee should not have been payable simply because the directors withdrew their recommendation, before putting the proposal to shareholders. That meant only that their recommendation had been premature. No recommendation should have been agreed to at a stage before the independent directors had received all the information they foresaw as being relevant to whether that recommendation should stand. The agreement itself reflects that the independent expert's report would be relevant to that decision. If the obligation to pay the fee were triggered, it would most likely be because there had been a defect in the process leading up to the recommendation, and it was most unlikely to be because a better bid had emerged. If ESK's attention had been likely to stray to other prospective targets, this may have been a risk that the directors were justified in incurring a fee to minimise. However, ESK was as much a captive bidder as NCI was a captive target.

44. In their submissions ESK and NCI highlighted the need to maintain the independence of the independent expert, Grant Samuel, indicating that it would have been inappropriate for Grant Samuel to report on the First Proposal and the terms of the First Implementation Agreement, prior to finalisation of the First Proposal. In our view it would have been normal and proper practice for the independent directors to have:

    (a) provided in the First Implementation Agreement that the First Break Fee would not be payable in the event of an adverse independent expert's report. This would have reduced the pressure on Grant Samuel and strengthened its position as an independent expert; or

    (b) waited until they had the first draft of the independent expert report on the valuation of the company without compromising the independence of Grant Samuel. The position of Grant Samuel in this case is different from that of the experts in *Phosphate Co-operative Co. of Australia Ltd v Shears &*

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[3] GN7 at para 7.21

Anor (No.3)[4] and *ANZ Nominees Pty Ltd v Wormald International Ltd*[5] where the experts were part of the "team" and had clearly rewritten parts of their report at the request of the company. It would also not appear to be contrary to ASIC's policy as explained in ASIC Practice Note 42 – Independence of experts' reports, although we acknowledge that care would need to be taken to ensure that this manner of proceeding did not prejudice the independence of the expert.

45. It makes no difference that the First Break Fee was only payable if ESK withdrew from the First Implementation Agreement when the independent directors changed their recommendation. If this term reflects the fact that public shareholders were likely to follow the independent directors' recommendation, that fact merely underscores the obligation of the independent directors to make no recommendation which could adversely affect the company or the public shareholders, until they had taken all measures reasonably necessary to test that recommendation.

46. VIPH alleged that the payment contravened Chapter 2E of the Act (related party transactions). The independent directors and ESK rejected this submission, on the basis that the terms were negotiated on an arm's length basis. We make no finding on this allegation, however it captures an important point. The directors quite properly obtained external advice and sought to negotiate an adequate price, but there was no market test of either the bid price or the First Break Fee: it was only possible to argue that they were arm's length amounts by reason of the process of negotiation which led up to them. Generally, in proposed privatisation transactions like the transaction we are considering here, we would expect the independent directors to make even greater efforts to ensure that the transaction occurs in an efficient and competitive market.

47. We do not suggest that there was any want of good faith on the part of the independent directors. We note the procedures followed and the advice obtained in negotiating the First Proposal and that they withdrew their recommendation of the First Proposal when Grant Samuel reported that it was not in the interests of public shareholders. Nonetheless, we considerthat the process committed NCI to paying ESK's expenses before it was appropriate, or indeed prudent, for it to do so.

48. In saying that this process was inappropriate, we acknowledge that neither GN7, nor any previous decision of the Panel, had specifically addressed the issue of the appropriateness of the process to be followed in such circumstances (in particular, bearing in mind the "going private" nature of the transaction and the matters that we have pointed to in [39]). However, despite this we consider that the NCI independent directors should have realised that it was

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[4] (1988) 6 ACLC 1046
[5] (1988) 13 ACLR 698

inappropriate in these circumstances for NCI to give both a recommendation by the NCI directors before they had received the views of the independent expert, and an agreement that NCI pay the First Break Fee in the absence of a competing proposal where the directors were possibly required by their duties to change that recommendation.

49. Although GN7 does not specifically address the facts of this case it is repeatedly expressed to be non-exhaustive. The two bases of GN 7 are that fees should not inhibit competition and that they should be objectively reasonable. In the circumstances, it was unsafe to assume that the terms under which the fee was to be paid were reasonable.

50. We dealt with these issues by obtaining undertakings from ESK:

    (a) to increase the consideration payable under the Second Scheme to give effect to the ESK proposal by 1.5 cents/share. This is the amount by which the payment of the First Break Fee depleted the assets of NCI on a per share basis. This undertaking ensures that shareholders are not adversely affected by the payment of the First Break Fee, if they approve the Second Scheme. In our experience, where a sale transaction is being considered, the proposed sellers (here, the shareholders in NCI) would prefer to receive an increased price for their assets (the shares in NCI) rather than to see an asset underlying the subject of the sale (NCI's cash resources) restored or enhanced. To proceed in the alternative way, by enhancing or restoring the underlying asset, means that any increased value will not be available to the sellers unless the sale does not proceed and, then only indirectly; and

    (b) to repay the First Break Fee if a rival bid is announced before the Second Scheme meeting and is eventually successful. This ensures that if a rival bid succeeds, NCI's assets will not have been depleted by the payment of the First Break Fee, overcoming any adverse effect of the fee on that rival bid. We consider that in this way, the effect of payment of the First Break Fee on the possibility (albeit remote) of a competing bid will be neutralised – a rival bidder knows that if it makes a counter-proposal, the assets of NCI will be replenished to the extent of the depletion effected by payment of the First Break Fee.

51. If shareholders do not approve the Second Scheme, ESK is not required to repay the First Break Fee. This outcome would be consistent with the policy set out in GN7 i.e. it is acceptable for a break fee to become payable if and when a proposal endorsed by the board is rejected by shareholders. In such a case, the fee is in effect the price paid to secure the opportunity for shareholders to consider the proposal and it becomes payable only as a result of their decision to reject the proposal.

52. It is not for us to enforce Chapter 2E of the Act. Related party considerations are only relevant in our proceedings, so far as they indicate that a price or transaction may be different from what would have been agreed at arm's

length. We made no finding that the independent directors were influenced by related party considerations.

53. The mischief of the First Break Fee which is relevant to our proceedings is its effect on the existence of an efficient, competitive and informed market in shares in NCI. That effect is at the margin, since it is only 1% of the value of NCI. Nonetheless, it gives ESK a 1% advantage over any rival bidder. Because of the nature of the process which led to the agreement to pay the fee, we think it appropriate that while the company is "in play", the fee should give ESK no advantage over any possible rival bidder. Once ESK's bid is over, whether it succeeds or fails, the fee will no longer impact on the competitive market for shares in NCI, and whether ESK retains it should depend on the general law.

54. Given the related party aspect of the fee and of the process followed by the directors, it is appropriate for this outcome to be decided by the shareholders, not the board.

55. We considered whether the payment of the First Break Fee should be the subject of separate shareholder ratification, and the fee should be repaid if ratification was withheld and the Second Scheme was not approved. Had it been above the 1% materiality threshold in GN7 or had it in any other way been excessive or materially affected the market in shares in NCI, the fee should clearly have been repaid, unless it was separately ratified by shareholders. As the First Break Fee is under that threshold, it is appropriate for the fee to be treated like the other expenses of the transaction as requiring no separate approval, but to depend on the outcome of the scheme meeting.

56. We also accepted an undertaking from ESK that it would not accept payment from NCI of the Second Break Fee and an undertaking from NCI that it would not pay all or any part of the Second Break Fee. To pay a second fee because the first was paid prematurely only underlines the fact that the directors should not have agreed to pay the First Break Fee until they knew at least as much as they did when they agreed to pay the Second Break Fee. The duplication reinforces our finding as to the deficiencies of the process.

57. We are concerned to ensure that the payment of break fees, such as the First Break Fee, does not adversely affect the efficiency of the Australian market in shares in companies to which Chapter 6 applies generally, not just NCI. That market would be adversely affected by a perception that break fees could be paid in inappropriate circumstances and not be required to be re-paid, provided the fee was paid before there was any intervention. Fees paid in privatisation transactions, while not objectionable *per se*, are of particular concern in this regard.

58. We wish to emphasise that the Panel felt free to find the agreement to pay the fee unacceptable because of the circumstances in which it was entered into irrespective of immateriality of the amount. The Undertakings have overcome the adverse effects of the payment of the First Break Fee on competition and efficiency in the market for shares in NCI and generally. In our view, that is as

far as a Takeovers Panel should take this particular matter. If the board's decision to agree to the First Break Fee, or to pay the fee, is open to challenge in the Courts, the interaction between this decision and section 659C of the Act will not prevent an action being brought to recover back the amount of the fee.

Disclosure of substantial holdings/associations

59. In its Application, VIPH alleged breach of section 606 of the Act (the 20% threshold) resulting from dealings between the Tyrrell Interests and breaches of the substantial holder notice provisions of the Act due to a discrepancy in the disclosure of voting power in NCI disclosed in the substantial holding notices, lodged on behalf of TI. VIPH further alleged that the relationship and dealings between the Tyrrell Interests suggest an association amounting to unacceptable circumstances.

60. VIPH made several assertions concerning these provisions. In each case, the assertion depended on inferences to be drawn from the public announcements and public material, particularly contained in substantial holding notices lodged by TI and statements of the directors' relevant interests in Annual reports of NCI. Those documents did not present a consistent picture of the relevant interests and/or voting power of MT or his mother and sister.

61. The unsatisfactory nature of the public documents led VIPH to make several submissions which amounted to an assertion that either the July Notice and the September Notice were incorrect bearing in mind the November 2000 Notice or if the November 2000 Notice was incorrect, that there had been a contravention of section 606.

62. On these related issues, we would like to make some preliminary points:

    (a) Although we recognise that compliance with section 671B and the prescribed forms can often be difficult and may sometimes seem to be a somewhat artificial exercise, care should be taken at all times to ensure that substantial holding notices not only comply with the provisions of Chapter 6C of the Act but also with the spirit and purpose of these provisions. Chapter 6C relates to the purpose of the legislation set out in paragraph 602 (b), particularly enabling the shareholders and directors of the target company to know the identity of the controllers of significant parcels of shares in a company and, by reason of the timing provisions and triggers of giving notices, to afford a reasonable time to consider any proposal. The notices are also essential for the existence of an informed market.

    (b) In considering whether or not a person is a substantial holder and what information should be disclosed in a notice under section 671B of the Act, regard needs to be taken of the provisions relating to relevant interests, association and voting power contained respectively in sections 608 and 609, 12 and 610 of the Act. These provisions, as Marks J said almost 20 years ago are concerned with the identification of real aggregations and

combinations of persons with control over shares.[6] In making this assessment parties should take care neither to fantasize nor to ignore necessary inferences from the facts.

(c) As a general proposition, it should not be possible for allegations such as those made by VIPH to be made - the relevant substantial holding notices should sufficiently display the reality of the existence of relevant interests, associations and voting power, and the reason for their existence, so that the effect of any new transaction, proposed transaction or change in relevant facts can be determined by the market generally.

63. In this case, the November 2000 Notice provided a shaky foundation on which to construct future disclosure. This allowed VIPH to invite us to draw inferences adverse to MT and the other Tyrrell Interests in terms both of disclosure under Chapter 6C and of compliance with section 606. The November 2000 Notice was an unusual document. It appeared to be given on behalf of members of the Tyrrell family and their relevant corporate structures. It identified all those persons as having voting power in respect of all the shares identified, apparently on the basis that they were all associates of the holders of those shares. However, in particularising that association, the November 2000 Notice referred to statutory provisions that had been repealed some eight months before it was given and which did not make sense in terms of the statutory provisions at the time of the giving of the notice. The persons referred to were both natural persons and bodies corporate. Even if the statutory reference in the notice which purports to explain the basis of association between the Tyrrell interests is read as being to the legislation in force before the amendments of March 2000, the disclosure suggested that the natural persons were related bodies corporate of each other and other bodies corporate. As a matter of statutory construction and legal analysis, that would not be possible. Whatever the deficiencies of the November 2000 notice, however, it could not be maintained that after its publication the market was not aware that at all relevant times the Tyrrell family spoke for approximately 51% of NCI.

64. The July Notice and the September Notice were also quite curious. For instance, although identifying the November 2000 Notice as the previous notice given by the substantial holders, the level of voting power identified in them as being last the subject of disclosure differed from that disclosed in the November 2000 Notice. In addition, the authors of the July Notice and the September Notices appear, without referring to the admittedly Delphic disclosure in the November 2000 Notice, to proceed on an entirely different basis as regards the nature of the interests of members of the Tyrrell family in relation to the shareholdings in NCI of TI and Tyrrell Nominees Pty Ltd (**Nominees**). It appears that the drafters of these notices were influenced by issues arising from

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[6] *Elders IXL Limited v NCSC (No 4)* (1986) 10 ACLR 719 at 730

the proposed privatisation transaction which do not appear to have been relevant to the issues generally before us.

65. In light of the unsatisfactory state of the evidence, we requested and received a helpful witness statement from MT which explained the existing and proposed arrangements concerning the ownership and control of the holdings in NCI of the Tyrrell Interests.

66. MT's statement enabled us to form the view that:

    (a) Notwithstanding its peculiarities, the November 2000 Notice had correctly identified TI, Nominees, Harry Tyrrell and MT as associates in relation to NCI. Although its description of the basis of that association was cryptic, we inferred that the basis of the association between Harry Tyrrell and MT was like that of members of a "family" of companies - a loose arrangement which would constitute acting in concert in relation to the affairs of NCI.

    (b) In proceeding on a different basis, the July Notice and September Notice did not assist in informing the market, particularly as they did not identify a change, if any, in associations and voting power as having occurred since the November 2000 Notice.

    (c) The market and the board of NCI had, notwithstanding the differing disclosures that had been made, at all relevant times consistently taken the view that the Tyrrell Interests should be regarded as a block and that, at least, MT, Harry Tyrrell, TI and Nominees were part of the block.

67. On 8 October 2003, we informed the parties of our views on the associations, relevant interests and voting power of MT. As a result of that, TI prepared and, on 15 October 2003 gave to NCI and ASX, revised forms of the July Notice and the September Notice (**October Notices**). That having been done, it seemed to us to that the relevant information had been provided to the market. Further, there was no evidence produced of significant transactions or decisions having been made on the basis of any other view of the matter and this appeared to rectify any unacceptability that might have otherwise existed and not to justify further intervention by us. We note, however, that had significant decisions or transactions been made or entered into on the basis of incorrect information in the substantial holding notices, intervention by the Panel may have been justified, notwithstanding the correction of that information, to rectify the unacceptability arising in connection with those decisions or transactions.

68. The effect of our approach to the substantial holding notices issues is that almost all of the issues relating to section 606 raised by VIPH ceased to be relevant. However, in relation to section 606, the October Notices revealed that the association between the Tyrrell Interests was manifested in the agreements attached to the notices that had been entered into the purposes of giving effect to the Tyrrell Consolidation. In a sense, we considered this to be the **current** manifestation of the association that had existed since at least November 2000. As the agreements attached to the October Notices had been entered into on the

basis of the ASIC Modification and as no share transactions had been completed on basis of them, we consider that the Tyrrell Consolidation did not contravene section 606. We note that, as a matter of logic, it must have been the case that agreement was reached between the parties to those agreements prior to the making of an application to ASIC for the grant of the ASIC Modification. However, this agreement must have been subject to a condition that ASIC modification be granted, and, to the extent that acquisition of a relevant interest was involved, it would be exempted by either or both of section 609(7)(a) (ii) and the decision of Tadgell J in *Precision Data Holdings v Titan Hills*.[7]

69. As in a number of recent matters before the Panel[8], there was an attempt to limit disclosure in the July Notice and September Notice. We encourage all people who believe that they may be substantial holders in Australian listed companies and trusts to obtain competent and detailed legal advice as to their position and the consequent disclosure obligations. We urge those advising on substantial holding notices to ensure that disclosures in those notices are both accurate and meaningful and that they fully and properly explain the basis on which the relevant interests in securities and associations giving rise to the relevant voting powers are considered to exist. Those matters should not just be described generically by reference to the provisions of the Act or in vague terms. If there is any uncertainty as to the requirements of the provisions of the Act on substantial holding notices, the persons giving them should adopt greater rather than lesser levels of disclosure. The Panel regards full compliance with substantial holders' obligations (both as to content and timeliness) to be fundamental to the maintenance of an efficient, competitive and informed market in securities of listed entities.

ASIC Modification

70. The Application sought an order that ASIC's decision on 21 July 2003 to grant the ASIC Modification be set aside or be varied to impose a condition similar to the conditions referred to in ASIC's policy on joint bids. The ASIC Modification varied subsection 609(7) of the Act to disregard the acquisition of relevant interests in shares in NCI which arose from agreements for the Tyrrell Consolidation, conditional on approval of the scheme of arrangement proposed by ESK.

71. We note that, on one view, TI (which was the acquirer whose proposed acquisitions were exempted by the ASIC Modification) did not require the ASIC Modification in order to enter the relevant agreements with members of the Tyrrell family in order to effect the Tyrrell Consolidation without contravening section 606. As acquirer, TI already had a relevant interest in more than 49% of the NCI shares and the shares the subject of the agreements would not increase

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[7] (1990) 2 ACSR 707 at 727

[8] eg Austar United Communications Ltd [2003] ATP 16 and Grand Hotel Group (Media Release TP 03/98)

TI's voting power by more than 1%. It was accordingly quite conceivable that the exception in section 611 item 9 (the 3% creep provision) may have applied to the acquisition of relevant interests in NCI shares by TI.

72. However, as ESK and MT explained to us, the effect of Corporations Regulation 1.0.18, which applies the definition of "affairs of a body corporate" in section 53 to the definition of an associate in sections 12(2)(b) and (c), may be to confer on the vendor of shares voting power in all shares in the same body corporate in which the purchaser may have a relevant interest.[9] As this does not appear to have been an intended consequence of recent drafting changes to these provisions, and because of the manifest practical difficulties that it would raise, it was appropriate for ASIC to grant the ASIC Modification to exempt from section 606 a proposed acquisition by TI which did not raise control issues as a practical matter.

73. It was also appropriate for ASIC to grant the ASIC Modification on the basis that it did because the conditions of the proposed agreements (that it was subject to the approval of the scheme of arrangement proposed by ESK) meant that the only circumstance in which these agreements could lead to any transfer of rights in the subject of shares would be circumstances in which the prohibition in section 606 could not apply. This is because, at that stage, NCI would have less than 50 members. It is, in our view, appropriate for ASIC to grant modifications to allow arrangements to be entered into in anticipation of other transactions where those other transactions will mean that Chapter 6 will have no relevance to the agreements in the circumstances which they can be performed.

74. We consider that the ASIC Modification was soundly based in policy.

75. The effect of the ASIC Modification, however, was to make the Tyrrell Consolidation effectively conditional on the approval by NCI shareholders of the First Scheme and the Second Scheme (as appropriate). As mentioned above, the ASIC Modification made exemptions to allow the Tyrrell Consolidation conditional on the outcome of the vote on the scheme of arrangement. Where otherwise prohibited transactions are permitted subject to shareholder consent, whether as a result of ASIC relief or otherwise, we consider that it is essential that shareholders receive complete disclosure about the exempt transactions to ensure that shareholders are fully aware of the consequences of their vote.

76. In the case of a scheme of arrangement, this disclosure will typically be in the explanatory statement in relation to the scheme issued by the relevant company (here, NCI) under section 412 of the Act. That document is lodged with and reviewed by ASIC and is then the subject of further scrutiny by the Court. We were concerned not to trespass on areas of responsibility of ASIC and the Court. Accordingly, the Panel indicated to the parties that it considered that the terms of the Tyrrell Consolidation should be the subject of disclosure to the scheme

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[9] especially by reason of paragraphs 53(e) and (f)

meeting, commensurate with the requirements of section 611 (acquisitions approved by shareholders).

77. NCI assured us that appropriate disclosure would be made of those matters in the explanatory statement and that the terms of the Tyrrell Consolidation would be reviewed and commented upon by Grant Samuel, the independent expert. ASIC assured us that it would conduct its review of the documents bearing in mind our observations. On the basis of these assurances, the Panel considered that no unacceptable circumstances had arisen or were threatened which necessitated its intervention.

Miscellaneous Issues

Funding

78. VIPH submitted that the circumstances indicated that there is an arrangement between ESK and a financier to provide funds for subscription which will then be lent back to fund the scheme and that this should be disclosed to shareholders.

79. We decided that there was no indication that ESK had not properly arranged funding, or that the basis on which it has funded the bid requires to be notified to the market before the explanatory statement is released. It is clear that details of the funding have not yet been disclosed, but nothing indicates that the funding is precarious. If anything, the fact that security arrangements are already being made suggests the opposite.

80. The First Proposal involved a requirement for a vote of NCI shareholders to approve NCI providing financial assistance to ESK for the acquisition of shares in NCI. This was not mentioned in the announcement of the First Proposal, although it is a material aspect of that proposal and ought to have been drawn to shareholders attention.

DECISION

Undertakings and conclusion of Proceeding

81. In light of:

    (a) the provision of the Undertakings with respect to the First and Second Break Fees to the Panel by ESK and NCI;

    (b) the release of the October Notices by TI;

    (c) assurances by NCI that appropriate disclosure would be made in the Explanatory Statement with respect to the Tyrrell Consolidation,

    we concluded the Proceeding on the basis that it appeared to us that no declaration of unacceptable circumstances was appropriate and no order was required.

Legal representation and costs

82. We consented to the parties being legally represented by their commercial lawyers in the Proceedings.

83. We received an application for an order under section 657D(2)(d) that any or all of MT, ESK and NCI bear the costs and expenses incurred by VIPH in relation to the Application, other than costs which relate to that part of the Application that relates to the application for review of the decision to grant the ASIC Modification.

84. As we made no declaration of unacceptable circumstances we would be unable to order that any person pay costs and so did not consider this issue.

Andrew Lumsden
President of the Sitting Panel
Decision dated 17 October 2003
Reasons published 21 November 2003

Annexure A – Undertakings provided by NCI during the Proceeding

Undertaking

By: National Can Industries Limited (NCI)

To: The Takeovers Panel (Panel)

Date: 15 October 2003

Subject to ESK undertaking not to require or receive payment of all or any part of the Second Break Fee in accordance with its contractual entitlements, NCI undertakes to the Takeovers Panel not to pay all or any part of the Second Break Fee to ESK.

Annexure B – Undertaking provided by NCI during the Proceeding

Undertaking

By: ESK Holdings Pty Limited

To: The Takeovers Panel (Panel)

Date: 16 October 2003

Pursuant to subsection 201A(1) of the *Australian Securities and Investments Commission Act* 2001 (Cth), ESK undertakes to the Takeovers Panel that it will:

(a) increase the consideration offered under the Second Proposal by 1.5 cents per NCI share so that the total offer price is $1.565 per NCI share;

(b) in the event that, before the date on which the Second Proposal is considered by shareholders, another person announces a higher bid for NCI (a higher bid being one with a cash value in excess of $1.565 per NCI share) which subsequently leads to a change in control of NCI, repay the first Break Fee in full to NCI after the bidder acquires beneficial ownership of more than 50% of NCI shares; and

(c) not enforce its right to receive payment of the Second Break Fee and will not accept payment from NCI of the Second Break Fee.