



**In the matter of Australian Leisure & Hospitality Group Limited
[2004] ATP 21**

Catchwords:

Defeating conditions – defence costs – independent expert report – supplementary target’s statement – valuation – Panel declining to commence proceedings

Corporations Act 2001 (Cth) section 638(1)

ASIC Practice Note 42: Independence of experts’ reports

Teh v Ramsay Centauri Pty Ltd [2002] NSWSC 456, 42 ACSR 354

These are the Panel’s reasons for declining to commence proceedings on Bruandwo Pty Limited’s application in relation to the affairs of Australian Leisure & Hospitality Group Limited. On 8 September 2004, the Panel issued a media release regarding its decision.

THE PROCEEDINGS

1. These reasons relate to an application dated 27 August 2004 from Bruandwo Pty Limited (**Bruandwo**) alleging unacceptable circumstances in relation to its off-market takeover bid for all the ordinary shares in Australian Leisure & Hospitality Group Limited (**ALH**).
2. The Panel decided not to conduct proceedings in relation to the application. This decision followed ALH’s agreement to issue a supplementary target’s statement containing further disclosure regarding:
 - (a) change of control clauses in ALH’s material agreements which might be relevant to one of the defeating conditions in Bruandwo’s bid; and
 - (b) the effect of ALH’s takeover defence costs on its expected dividend and earnings.

THE PANEL & PROCESS

3. The President of the Panel appointed Elizabeth Alexander (sitting President), Jennifer Seabrook (sitting Deputy President) and Ian Ramsay as the sitting Panel (the **Panel**) to consider the application.

APPLICATION

Background

4. Bruandwo alleged that unacceptable circumstances existed because of misleading or deceptive statements in, or material omissions from, ALH’s target’s statement. Specifically, Bruandwo alleged that the target’s statement was deficient in the following ways:

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- (a) it raised concerns regarding the process undertaken by KPMG Corporate Finance (Aust) Pty Limited (**KPMG**) in the preparation of its independent expert report, which was included in ALH's target's statement, as well as the content of that report;
 - (b) there was no information about the impact of ALH's takeover defence costs on the expected earnings and dividend for the 2004/2005 financial year;
 - (c) there was insufficient information regarding the ALH material agreements which could trigger the defeating condition set out in clause 8.8(a)(vii)(B) of Bruandwo's bidder's statement (the **Change of Control Waiver Condition**); and
 - (d) there was no information from the ALH board regarding its view of the likely post-bid ALH share price.
5. The Change of Control Waiver Condition requires that, before the end of the offer:
- ALH receives from each person who is entitled to exercise any right under any provision of any material agreement to which ALH or any subsidiary of ALH is a party, including any of the agreements referred to in Section 7.4 of the Bidder's Statement, that entitles the person to terminate or modify the agreement as a result of the acquisition of ALH Shares by Bruandwo, an irrevocable and unconditional waiver or release of that right in writing and provides Bruandwo with a copy of that written waiver or release.*
6. The Panel received preliminary submissions from ALH in response to the application urging the Panel to dismiss Bruandwo's application entirely and not to commence proceedings. It also received further correspondence from Bruandwo in support of its application.

DISCUSSION

Offer conditions

7. In its preliminary submissions to the Panel, ALH advised that there were no material agreements that could be the subject of the Change of Control Waiver Condition other than those agreements summarised in ALH's IPO prospectus dated 19 September 2003.
8. The Panel considered that this statement was significantly more informative than the statements made in Part D of ALH's target's statement that there were "many" material agreements to which the Change of Control Waiver Condition could apply. ALH submitted that the agreements summarised in its IPO prospectus were the "many" material agreements referred to in its target's statement. However, the Panel was concerned that the two statements gave different impressions about the identity and number of agreements to which the Change of Control Waiver Condition could apply.
9. Given the additional information provided in ALH's preliminary submissions, the Panel advised ALH that it would be appropriate for ALH to inform ALH shareholders about which of its material agreements were relevant to the Change of Control Waiver Condition. The Panel considered that this disclosure is important:

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- (a) to an ALH shareholder's decision whether or not to remain a shareholder if Bruandwo attains control of, but does not wholly own, ALH; and
 - (b) to allow shareholders to better assess the likelihood of whether the Change of Control Waiver Condition would be satisfied or waived by Bruandwo.
10. However, the Panel did not accept Bruandwo's argument that ALH should disclose this information in order to assist Bruandwo to decide whether or not to waive the Change of Control Waiver Condition.
 11. ALH agreed to provide the relevant information in its supplementary target's statement.

Takeover defence costs

12. In its target's statement, ALH set out its forecast profit and loss for the 2004/2005 financial year. ALH stated in a footnote to its forecast that:

The forecasts do not include takeover defence costs on the basis that they are non-recurring and therefore not reflective of the underlying performance of ALH.
13. The Panel advised ALH that if there were circumstances under which the quantum of defence costs payable to ALH's advisers would have a material effect on ALH's earnings or dividend for the 2004/2005 financial year, ALH was required, under section 638(1) of the *Corporations Act 2001 (Cth)* (the **Act**), to disclose that possibility in its target's statement.
14. ALH agreed to include a statement in its supplementary target's statement regarding the effect that its defence costs may have on ALH's expected earnings and dividend.

Independent Expert Report

Leakage of report's valuation conclusions

15. In its application, Bruandwo alleged that the conclusion of KPMG's report as to the value of shares in ALH had been leaked, so that rumours about the valuation were circulating in the market on 4 August and articles referring to it appeared in the press on 6 and 11 August. KPMG's report dated 11 August 2004 and was not published until 12 August, when it was released with ALH's target's statement in response to queries from ASX regarding the press articles and speculation on the conclusions of KPMG's report. As a result of this speculation, ALH requested a trading halt on its shares on 11 August 2004, which was lifted upon release of the target's statement on 12 August 2004.
16. Bruandwo inferred from the alleged leak that KPMG had provided a draft of its report to ALH, and that ALH and KPMG were in discussion about the content of the report and that those discussions should have been outlined in KPMG's report or some other part of the target's statement. Bruandwo cited [42.24] of *ASIC Practice Note 42: Independence of expert's reports* in support of its argument, which says:

If the expert has discussed the appraisal method or the substance of the draft or final report ... with the client before signing it, he or she must negate any perception of bias. The expert should make notes during the discussions in order to do this. He or she should also disclose the nature and result of the discussions in the report so that readers can assess the report's independence for themselves. The expert should also keep all

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drafts of the report so that he or she can demonstrate changes made during its preparation and the reasons for them (to contradict any inference of bias).

17. In its preliminary submissions, ALH advised that on 1 August KPMG provided ALH a draft of its report for factual review, which valued ALH shares very close to the range mentioned in newspaper articles of 6 and 11 August (the draft included a valuation range of \$3.17 to \$3.41, but the articles said \$3.17 to \$3.42).
18. The range in KPMG's final published report was a little higher (\$3.19 to \$3.42) than that contained in the earlier draft. ALH advised that this was due to KPMG having taken account of the repayment of some bank debt by ALH, something about which ALH advised KPMG after the 1 August draft of the report had been provided.
19. When the draft report was provided on 1 August, ALH was due to post its target's statement on 11 August (although ASIC later granted ALH relief extending the date for dispatch of the target's statement to 16 August). ALH indicated that based on a posting date of 11 August, its printing deadline for having the final target's statement and KPMG report ready was 6 August. In this context, and having noted that KPMG had a few days longer than the statutory minimum period to prepare its report (as a result of a slight delay in the dispatch of Bruandwo's bidder's statement) the Panel did not consider it very unusual that a draft report with the valuation range was provided on 1 August.
20. KPMG stated in its report (at page 76), and ALH confirmed in its preliminary submissions, that:

During the course of this engagement, KPMG Corporate Finance provided draft copies of this report to ALH for comment as to factual accuracy, as opposed to opinions, which are the responsibility of KPMG Corporate Finance alone. Changes made to this report as a result of these reviews have not changed the opinions reached by KPMG Corporate Finance.

21. The Panel carefully reviewed Bruandwo's allegations regarding KPMG's independent expert report, as well as the details set out in ALH's preliminary submissions regarding the process undertaken in the preparation of KPMG's independent expert report. The Panel also had regard to ASIC Practice Note 42.
22. The Panel did not accept that the fact that KPMG provided ALH with a draft of the part of the report containing its conclusions on 1 August raised an inference that KPMG was not independent. The Panel did not consider that the process followed was inconsistent with ASIC Practice Note 42 or otherwise warranted further investigation by the Panel. The evidence provided indicated only the ordinary practice of an independent expert providing a client with a draft of the report before it is complete, for the purposes of checking the factual content, and an amendment being made to the report in response to a change in the factual situation.
23. The Panel considered that neither Bruandwo's application, nor the details provided in ALH's preliminary submissions indicated that the independence of KPMG had been diminished or compromised, and that no additional disclosure regarding the preparation of KPMG's report was required. The Panel did not consider it necessary to investigate the alleged leak of KPMG's valuation range, although it noted that clients in receipt of a draft report in such circumstances should ensure that the

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circulation of such sensitive information among its management team and advisers is restricted, so that the confidentiality of the information is not jeopardised.

24. In its deliberations, the Panel considered whether it would have been appropriate for KPMG to disclose in its report that the quantum of, and reason for, the change to the valuation range described in [18] above. After making some investigations as to what currently constitutes “market practice” in the preparation of independent expert reports, and having regard to the immaterial quantum of the change made and KPMG’s actual disclosures reproduced at [20] above, the Panel did not consider that further disclosure of the change and related circumstances was required in KPMG’s report.
25. However, the Panel noted that while such variations or amendments are not uncommon, market practice appeared to vary significantly in relation to the disclosure of these variations. In the Panel’s opinion, the market would benefit considerably from further guidance regarding the appropriate disclosures to be made in such circumstances.

Valuation issues

26. Bruandwo also raised issues in relation the KPMG valuation itself, relating to recent transactions and the choice of multiplier and its application to ALH’s earnings.
27. These issues have been canvassed extensively by the parties in public, via media releases and ASX announcements, between 12 and 27 August. The parties’ decision to canvass these issues publicly made the Panel’s decision not to commence proceedings in relation to those parts of Bruandwo’s application easier.
28. If such issues were raised in Panel proceedings, the Panel could only require both ALH’s view and Bruandwo’s to be put before shareholders (which is what has been done), unless it was persuaded that one or other view was untenable. Bruandwo’s submissions and the correspondence annexed to the application did not support an inference that either view is so devoid of merit that it could not properly have been put to shareholders.

Synergies

29. Bruandwo’s application also raised concerns regarding comments in KPMG’s report about the synergistic benefits which Bruandwo might derive from the acquisition of ALH. Bruandwo asserted that these synergistic benefits unique to Bruandwo ought not be taken into account in valuing ALH.
30. Bruandwo’s submission concerning synergy benefits was not persuasive. KPMG stated the following in its report (at page 5):

The potential value of these synergistic, strategic and special benefits specific to Bruandwo have [sic] not been factored into our valuation of an ALH share. Accordingly, the value of an ALH share to Bruandwo is likely to significantly exceed our assessed range.

31. Bruandwo compared this with the following passage in another report by KPMG on another company (provided as part of Bruandwo’s application):

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Special benefits that may be unique to [the bidder] have also not been quantified, as it is normal practice to exclude any special value to the bidder. Such benefits may, potentially, be significant.

32. The other KPMG report referred to in Bruandwo's application is correct in saying that it is normal to exclude from a valuation special value which may be unique to one buyer. The reason is that a valuation relates to the notional situation of a willing but not anxious buyer dealing with a willing but not anxious seller, each of them lacking "personal attributes, aspirations and interests, apart from their assumed willingness to deal and their familiarity with the subject matter and circumstances which might affect its value one way or the other".¹
33. It does not follow, however, that special value should not be mentioned in an independent expert report. It would be uncommercial and misleading for an adviser to shareholders deciding whether to sell at a particular price to overlook differences between the pure hypothetical situation to which a valuation refers and a given real situation, in which a buyer may be anxious or have a special need or opportunity in the light of which a seller can persuade the buyer to pay a higher price than valuation. The two KPMG reports quoted are, in fact, very similar in this regard. Each report gives a numerical valuation of the relevant shares on the usual basis of a willing but not anxious buyer and seller, and each report then points out the specific factors which, although not taken into account in the valuation, indicate that the shares in question are likely to be worth more to the relevant bidder than the valuation indicates, without quantifying the special value.
34. In considering the statements regarding synergistic benefits contained in KPMG's report, the Panel noted that the report contained significantly more detail in its discussion of this issue than, for example, its discussion of the prospect of ALH's share price falling post-bid (discussed in [36]-[38] below). The Panel did not consider that KPMG had given any undue or inappropriate prominence to the discussion of synergistic benefits in its report.
35. However, the Panel considers it an opportune moment to remind those preparing reports to shareholders of the potential for detailed discussion of one issue to appear to readers as though the expert is indicating that the issue should carry more weight than other issues, even if that was not the expert's intention.

Future share price and alternative proposals

36. Bruandwo asserted that the ALH board's view about the price of ALH shares if Bruandwo's bid is unsuccessful was material information which should have been included in the target's statement, given the ALH board's recommended rejection of Bruandwo's offer and the trading price of ALH shares prior to the announcement of Bruandwo's bid.
37. KPMG's independent expert report includes statements (at page 6) regarding the prospects for the ALH share price in the event that Bruandwo's offer lapses. The Panel notes that Bruandwo has emphasised these statements in its own public releases following the dispatch of ALH's target's statement.

¹ *Teh v Ramsay Centauri Pty Ltd* [2002] NSWSC 456, 42 ACSR 354, at [14] to [17], per Barrett J.

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38. Given KPMG's stated view and the absence of any marked change in ALH's affairs since KPMG signed their report, the Panel did not think that it was necessary for ALH to make any prediction regarding the future market price of ALH shares in the event that Bruandwo's bid lapses and there is no counter-bid.
39. In its application, Bruandwo also argued that in the context where public statements were made on numerous occasions about alternative proposals, the ALH board had an obligation to provide information in the target's statement concerning whether it has or will seek alternative offers. In support of this argument Bruandwo referred to several statements attributed to ALH Chief Executive, Mr Geoff Rankin, in the press between 13 July and 13 August.
40. The comments attributed to Mr Rankin were substantially to the effect that ALH had not sought a rival bidder and knew of no firm proposal for a counter-bid, but would be receptive to a rival bid. ALH submitted that Mr Rankin's comments were largely in response to specific questions from the media. The Panel had no objections to Mr Rankin's comments, which appeared measured and reasonable, and did not consider that they gave rise to any additional disclosure obligation in the target's statement.

MEDIA CANVASSING AND POSSIBLE BREACH OF PANEL CONFIDENTIALITY

41. The Panel was concerned by a number of press articles published during the course of the Panel's consideration of Bruandwo's application. These articles contained the following details, which had only appeared in confidential communications between the parties and the Panel:
 - (a) specific matters raised in Bruandwo's application; and
 - (b) information regarding the Panel's areas of concern and its attitude towards the issues raised in Bruandwo's application.
42. The Panel considered it likely that these articles had been prepared with the aid of confidential information regarding the application before the Panel. The Panel received assurances from both parties that neither they, nor their advisers, were responsible for providing the information contained in these articles.
43. Notwithstanding the assurances received from the parties, the Panel considers the most likely explanation for the confidential material disclosed in the articles is that information was provided by either or both of Bruandwo and ALH (or their respective advisers) in contravention of the Panel's Procedural Rule 12.
44. The Panel considers leaks and media canvassing of this type to be highly objectionable. The Panel believes that its ability to resolve disputes as quickly and efficiently as possible will be adversely affected if parties seek to use publicity in any way and disapproves of any attempt by a party to use publicity to influence a decision of the Panel or detract from its authority. Further, the Panel considers that such conduct is in clear breach of the Panel's requirement that Panel proceedings (and in particular Panel correspondence) remain confidential and in breach of express undertakings given by the commercial solicitors on behalf of each party that they and their advisers would respect the Panel's rules in relation to confidentiality.

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DECISION

45. After considering Bruandwo's application and supporting correspondence, as well as ALH's preliminary submissions, the Panel wrote to the parties to advise them that the only issues raised in the application on which it may decide to conduct proceedings were the issues relating to the Change of Control Waiver Condition and the takeover defence costs. The Panel advised that its concerns in relation to these issues could be addressed by further disclosure in a supplementary target's statement. As indicated above, ALH agreed to prepare a supplementary target's statement providing further disclosure in relation to these issues.
46. The Panel reviewed the draft supplementary target's statement, and also gave Bruandwo an opportunity to make submissions regarding the draft supplementary target's statement, before it was lodged by ALH. The Panel considered that ALH's further disclosure in its supplementary target's statement addressed the only issues raised in Bruandwo's application on which it might have decided to conduct proceedings.
47. Accordingly, under Regulation 20 of the ASIC Regulations, the Panel decided not to conduct proceedings on the application.

Elizabeth Alexander AM

President of the Sitting Panel

Decision dated 8 September 2004

Reasons published 24 September 2004