



**In the matter of Wattyl Limited  
[2006] ATP 11**

**Catchwords:**

*additional disclosure; ACCC; assumptions; break fee; competition; content of target's statement; corrective disclosure;; defeating condition; effect of payment of special dividend; exclusivity agreement; investigating accountant's report; lock-up devices; negative assurance; no-shop; no-talk period of break fee; Pre-Bid Agreement; reconciliation of chairman's statement on ACCC opposition; revenue growth and margin forecasts; risk of non-satisfaction of ACCC condition during period of rival bid; selective payment of special dividend; supplementary target's statement; undertaking; proceedings concluded based on undertakings*

*Corporations Act 2001 (Cth): sections 638, 670A.*

*Guidance Note No. 7 on Lock-up devices*

*Wattyl Limited; AEP Financial Investments Pty Ltd; Allco Equity Partners Limited; Barloworld Limited; Taubmans; Bristol; White Knight*

**These are the Panel's reasons for declining the application by AEP Financial Investments Pty Ltd to make a declaration of unacceptable circumstances in relation to the affairs of Wattyl and final orders. The Panel decided not to make a declaration of unacceptable circumstances or final orders having received undertakings to amend the terms of a break fee agreement between Wattyl Limited and Barloworld and having required and approved additional and corrective disclosure by Wattyl to Wattyl shareholders by way of a supplementary target's statement.**

## **SUMMARY**

1. These reasons relate to an application (the **Application**) to the Panel from AEP Financial Investments Pty Ltd a wholly owned subsidiary of Allco Equity Partners Limited (**AEP**) on 1 March 2006 in relation to the affairs of Wattyl Limited (**Wattyl**). Wattyl was subject to a cash takeover bid by AEP (**AEP Offer**).
2. AEP alleged that:
  - (a) Wattyl had failed to provide Wattyl shareholders with enough information to enable them to assess the relative merits of the AEP Offer following Wattyl's announced intention to recommend a proposed rival takeover bid for Wattyl by Barloworld Limited (**Barloworld**), given concerns previously expressed by the Australian Competition and Consumer Commission (**ACCC**) and statements made by the chairman of Wattyl at the annual general meeting in October 2005;
  - (b) the Wattyl target's statement which responded to the AEP Offer (the **Wattyl Target's Statement**) failed to provide sufficient information in respect of certain assumptions relevant to a revenue forecast.
3. AEP had also alleged that unacceptable circumstances existed in respect of a special dividend that Wattyl had announced it would declare in certain circumstances and a pre-bid deed (the **Pre-Bid Deed**) that Wattyl and Barloworld had entered into which included break fee provisions and exclusivity provisions.
4. In summary, the Panel required Wattyl to disclose in a supplementary target's statement to the AEP Offer:

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- (a) a reconciliation of Wattyl's announced intention to recommend a proposed rival takeover bid for Wattyl by Barloworld, with a statement by the chairman made at Wattyl's Annual General Meeting in October 2005;
  - (b) the history of ACCC opposition to a merger between Wattyl and Taubmans;
  - (c) whether or not competition clearance for the proposed rival takeover bid for Wattyl by Barloworld was unlikely to be known within the time frame of the current AEP Offer; and
  - (d) further information about the special dividend.
5. Wattyl and Barloworld were also required to amend the Pre-Bid Deed.
  6. The Panel did not make a declaration of unacceptable circumstances or orders, having been offered undertakings which addressed its concerns and having approved the additional disclosure made by Wattyl.

## THE PROCEEDINGS

### The Panel & Process

7. The President of the Panel appointed Kathleen Farrell (sitting President), Meredith Hellicar and Alice McCleary (sitting Deputy President) as the sitting Panel (the **Panel**) for the proceedings (the **Proceedings**) arising from the Application.
8. The Panel adopted the Panel's published procedural rules for the purposes of the Proceedings.
9. The Panel consented to the parties being legally represented by their commercial lawyers in the Proceedings.

### Background

#### *Wattyl*

10. Wattyl is a paint and surface coatings company listed on Australian Stock Exchange Limited (**ASX**).

#### *AEP*

11. AEP is a wholly owned subsidiary of Allco Equity Partners Limited. Allco Equity Partners Limited is listed on the ASX, with a mandate to invest in private equity and public market opportunities.

#### *Barloworld Limited*

12. Barloworld is a South African company listed on the Johannesburg Stock Exchange which owns the Taubmans, Bristol and White Knight Paints brands in Australia. Barloworld is one of the two principal competitors of Wattyl in Australia.

#### *Competing takeover bids*

13. On 22 December 2005, AEP announced the AEP Offer. The AEP Offer was subject to a number of defeating conditions including:
  - (a) minimum acceptance of 50.1%;
  - (b) no material adverse change; and

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(c) availability of finance to AEP.

The price offered per share under the AEP Offer was \$3.25.

14. On 28 December 2005, Wattyl released an announcement to ASX which stated that Barloworld had appointed an adviser to review the AEP Offer and advise it on a range of alternatives.
15. On 4 January 2006, in an announcement released to ASX Wattyl declared its intention to reject the AEP Offer on the basis that it materially undervalued Wattyl. Wattyl dispatched a letter to shareholders on terms similar to that announcement.
16. On 19 January 2006, Wattyl announced the appointment of an independent expert, Ernst & Young.
17. On 23 January 2006, Wattyl lodged the Wattyl Target's Statement with the Australian Securities and Investments Commission (ASIC) and sent it to AEP and ASX.
18. On 31 January 2006, Wattyl lodged with ASIC and sent to AEP and ASX its first supplementary target's statement which comprised the independent expert's report prepared by Ernst & Young.
19. On 13 February 2006, Barloworld announced its intention to make a cash takeover bid for Wattyl (**Barloworld Proposed Offer**). The Barloworld Proposed Offer was subject to a number of defeating conditions including:
  - (a) minimum 90% acceptance by Wattyl shareholders;
  - (b) all necessary regulatory approvals being obtained;
  - (c) no material adverse change in respect of Wattyl;
  - (d) Wattyl not paying dividends in excess of 100% of Wattyl's reported net profit after tax before significant items for any period after 30 June 2005.
20. On the same day, Wattyl lodged with ASIC and sent to AEP and ASX its second supplementary target's statement which annexed:
  - (a) an announcement by Wattyl released by Wattyl to ASX which included:
    - (i) a statement that the directors of Wattyl "*intend to unanimously recommend that Wattyl shareholders accept the Barloworld offer in respect of all of the Wattyl shares which they hold (in the absence of a superior proposal)*";
    - (ii) a statement that the directors of Wattyl had entered into the Pre-Bid Deed;
  - (b) the text of the announcement made by Barloworld on 13 February 2006.
21. On 27 February 2006, AEP further extended the offer period of the AEP Offer until 27 March 2006.

#### ACCC

22. On 12 March 1996, the ACCC announced that it had filed proceedings in the Federal Court seeking to restrain the completion of an agreement by Wattyl to acquire the

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architectural and decorative paint businesses of Taubmans, on the ground that it would be likely to substantially lessen competition<sup>1</sup>.

23. In 2005 Wattyl and Barloworld had discussions about combining their paint businesses, and Barloworld approached the ACCC for discussions concerning the possibility of Barloworld and Wattyl combining their paint businesses.
24. In September 2005, Wattyl and Barloworld discontinued negotiations pending clarification on proposed legislative changes to the trade practices legislation and to ensure management was focussed on its restructuring programme.
25. On 28 October 2005, at Wattyl's Annual General Meeting, a hypothetical question was put by a shareholder without notice as to whether it would be possible for Wattyl to now acquire the Taubmans business in the context of Wattyl's failure to obtain authorisation by the ACCC in 1996 to acquire the Taubmans paint business then owned by Courtalds (Australia) Pty Limited (and which, as a result of that failure, was acquired by Barloworld). Wattyl's Chairman stated, in response to that question:

*"Well, the ACCC hasn't changed [since the 1996 decision of the ACCC] and they work under the same legislation. And it's our view that given the very strong decision they gave there [in 1996], the opportunity or chance of turning that around right now would be very low. Having said that, as you know the Government has legislation before Parliament to change the power of the ACCC and have referral power to the Australian Competition Tribunal., And when that legislation is promulgated, I believe we might have an opportunity to look at that stage. But at this stage, we don't believe, (it's not something we haven't looked at) we don't believe we'd be successful in an application to them [the ACCC]."*

26. On 23 January 2006, Wattyl released a presentation to ASX which stated (among other matters) that *"in 2005 Wattyl and Barloworld pursued discussions"* and *"Barloworld has appointed ANZ Investment Bank to review the terms of the AEP proposal"*.
27. In the Wattyl Target's Statement of 23 January 2006, Wattyl cautioned Wattyl shareholders that:

*"Any combination of Wattyl and Barloworld's Australian paints and coatings business would be subject to obtaining regulatory approval by the ACCC or ACT. The outcome of any such approval process is uncertain and the Directors cannot give any assurance that approval would be obtained"*

The Wattyl Target's Statement also referred generally to the discussions Barloworld and Wattyl had had in 2005.

28. As mentioned above, Wattyl's second supplementary target's statement attached the announcement made by Barloworld on 13 February 2006 which stated (among other matters):

*"Barloworld has held preliminary discussions with the [ACCC]. The company understands that the ACCC will undertake market enquiries over the next number of weeks to address competition issues. Given the structural and other changes in the Australian coatings market*

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<sup>1</sup> See MR 025/96 of the ACCC.

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*over the last decade, Barloworld is confident of a successful conclusion to the transaction and looks forward to assisting the ACCC with its enquiries”*

29. The Barloworld Proposed Offer was subject to regulatory approval conditions which included ACCC or ACT clearance (the **Competition Condition**).
30. On 23 February, Wattyl sent to its shareholders a letter regarding the Barloworld Proposed Offer. It stated (among other matters) that the Barloworld Proposed Offer was subject to ACCC approval and that the ACCC had announced that it had commenced market enquiries, but that it is not clear when the ACCC will announce its decision on whether or not it will approve Barloworld's offer for Wattyl.
31. On 23 March 2006, the ACCC issued a Statement of Issues identifying its preliminary competition concerns in respect of the Barloworld Proposed Offer.

#### *Special dividend*

32. In the Wattyl Target's Statement, Wattyl stated that if the AEP Offer closed unsuccessfully, Wattyl shareholders would receive a fully franked special dividend of 40 cents per Wattyl share (the **Special Dividend**).
33. Wattyl also disclosed in the Wattyl Target's Statement that, in respect of the Special Dividend, it had *“sought and obtained indicative support from its principal lender...for funding to return up to \$40 million of cash to Wattyl shareholders.”*
34. In its 13 February 2006 announcement, Wattyl stated:  
*“...the directors have determined that it is not appropriate to pay the 40 cent per share special dividend which Wattyl had previously stated it would pay in the event that the AEP offer is unsuccessful.”*
35. On 23 February 2006, in a letter to shareholders Wattyl stated:  
*“Barloworld's offer also includes a condition that Wattyl not pay dividends in excess of 100% of Wattyl's net profit after tax before significant items. In view of this and the improved value that Wattyl shareholders would receive from Barloworld's offer, your directors have determined that it is not appropriate to pay the 40 cent per share special dividend which we previously stated we would pay in the event that AEP's offer is unsuccessful, pending the outcome of the Barloworld offer.”*

#### *Pre-Bid Deed*

36. On 13 February 2006, Wattyl and Barloworld announced that they had entered into the Pre-Bid Deed.
37. Under the Pre-Bid Deed (among other matters):
  - (a) Wattyl agreed to pay Barloworld a break fee of \$3,200,000 if at any time before the end of the offer period under the Barloworld Proposed Offer:
    - (i) a competing transaction is announced or open for acceptance, the buyer under that transaction acquires a relevant interest in more than 50% of the fully paid ordinary shares in Wattyl or a substantial part of Wattyl's assets and, if that transaction is a takeover bid, that transaction becomes free from any defeating conditions; or
    - (ii) the Wattyl directors:

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- (A) fail to recommend the Barloworld Proposed Offer;
  - (B) revoke, withdraw or revise their previous recommendation of the Barloworld Proposed Offer; or
  - (C) recommend or promote a competing transaction or other transaction which would materially disadvantage the prospects of the success of the Barloworld Proposed Offer.
38. Payment of the break fee under the agreement was not to be enforced by Barloworld if a court, the Takeovers Panel, a regulatory authority or tribunal determined that payment of the break fee:
- “(i) is, was or would be unlawful;*
  - (ii) constitutes, or if performed would constitute, unacceptable circumstances...; or*
  - (iii) involves, involved or would involve a breach of the directors duties of any current or previous members of the Wattyl Board...”*
39. The Pre-Bid Deed prohibited Wattyl from making any application to a court, the Takeovers Panel, a regulatory authority or tribunal for a determination referred to above.
40. The Pre-Bid Deed also included a clause which was titled “No Shop”. It stated that:
- “(a) During the Exclusivity Period, Wattyl must not, and must ensure that its Representatives do not, except with the prior written consent of Barloworld, solicit, invite, encourage, directly or indirectly, any enquiries, discussions or proposals or initiate any enquiry from, negotiation or discussion with, or communicate by any means any intention or willingness to do any of these things to, any person (other than Barloworld or its Representatives) in relation to a Competing Transaction.*
  - (b) For the avoidance of doubt, [(a) above] will not prevent Wattyl from responding to a proposed Competing Transaction if the proposed Competing Transaction is a superior proposal to the Takeover Bid.”*
41. The “Exclusivity Period” was defined in the Pre-Bid Deed to mean the period ending on the later of three months after 13 February 2006 and the closing date of the Barloworld Proposed Offer.
42. The 13 February 2006 announcement, attached an appendix which summarised the break fee and exclusivity provisions of the Pre-Bid Deed.

### Application

43. AEP submitted in the Application that the competition for control of Wattyl between AEP and Barloworld and trading in Wattyl shares generally, was not taking place in an efficient, competitive and informed market given:
- (a) the lack of disclosure to Wattyl shareholders to enable them to properly assess the merits of the AEP Offer and the Barloworld Proposed Offer;
  - (b) the break fee and the exclusivity arrangements agreed between Wattyl and Barloworld; and
  - (c) the proposal to pay the Special Dividend only if the AEP Offer closed unsuccessfully.

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44. AEP sought a declaration under section 657A that each of the following constituted unacceptable circumstances:
- (a) the failure of Wattyl to give guidance in its second supplementary target's statement to enable Wattyl shareholders and their professional advisers to assess the likelihood of the ACCC not opposing the Barloworld Proposed Offer, particularly in light of:
    - (i) the statements made by Wattyl's Chairman at the Wattyl Annual General Meeting on 28 October 2005 that an acquisition by Wattyl of Barloworld's Taubmans business would have a very low probability of being approved; and
    - (ii) the statements in, and arrangements with Barloworld referred to in, its second supplementary target's statement, which imply that the directors of Wattyl had a high degree of confidence that the ACCC would approve the Barloworld Proposed Offer;
    - (iii) the failure of Wattyl to disclose in its second supplementary target's statement the risk of non-satisfaction of the Competition Condition, and the risk of delay in the determination of the satisfaction or non-satisfaction of the Competition Condition, and hence the risks to Wattyl shareholders of accepting the Barloworld Proposed Offer before the Competition Condition is satisfied or waived;
  - (b) Wattyl's entry into the Pre-Bid Deed;
  - (c) the failure of Wattyl in the Wattyl Target's Statement to disclose the basis of the directors' assumptions as to:
    - (i) forecast revenue in FY2006 and FY2007;
    - (ii) maintenance of market share and forecast growth in volume in FY2006 and FY2007; and
    - (iii) estimated price increases in FY2006 and FY2007,sufficient to enable Wattyl shareholders and their professional advisers to assess the validity of those assumptions or the likelihood of those assumptions being satisfied;
  - (d) the failure of the directors of Wattyl in the Wattyl Target's Statement to state unequivocally that they believed the above assumptions to be reasonable;
  - (e) the proposal by Wattyl to pay the Special Dividend only if the AEP Offer closed unsuccessfully; and
  - (f) the failure of the directors of Wattyl in the Wattyl Target's Statement to adequately disclose the source of, and effect on Wattyl and the Wattyl share price of the payment of, the proposed Special Dividend.
45. AEP sought final orders under section 657D that:
- (a) Wattyl prepare and issue a supplementary target's statement which set out:
    - (i) whether or not the directors of Wattyl have formed an opinion that the Competition Condition is likely to be satisfied;

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- (ii) the factors known to the directors of Watty Limited which, in their assessment, would be relevant to a consideration by the ACCC of whether or not to oppose the Barloworld Proposed Offer;
- (iii) the precise bases on which the directors of Watty Limited formed the view, expressed by Watty Limited's Chairman at Watty Limited's Annual General Meeting on 28 October 2005, that an acquisition by Watty Limited of Barloworld's Taubmans business would not be approved by the ACCC;
- (iv) if the Watty Limited Directors have formed an opinion that the Competition Condition is likely to be satisfied, the precise circumstances which have changed since 28 October 2005, as a result of which the directors of Watty Limited are now of the opinion that an acquisition by Barloworld of Watty Limited is unlikely to be opposed by the ACCC;
- (v) if the directors of Watty Limited have not formed an opinion that the Competition Condition is likely to be satisfied:
  - (A) the precise circumstances which have changed since 28 October 2005, as a result of which the directors of Watty Limited now have no opinion as to whether the Competition Condition will be satisfied;
  - (B) the precise basis on which the directors of Watty Limited have formed the view that they will unanimously recommend that Watty Limited shareholders should accept the Barloworld Proposed Offer notwithstanding that the directors of Watty Limited now have no opinion as to whether the Competition Condition will be satisfied;
  - (C) the precise basis on which the directors of Watty Limited have agreed that Watty Limited will pay the break fee of \$3,200,000 to Barloworld if the Competition Condition is not satisfied and, as a consequence, while the Barloworld Proposed Offer remains open for acceptance:
    - (a) another bidder acquires more than 50% of Watty Limited Shares and the bid is unconditional; or
    - (b) the Watty Limited Directors change their recommendation in relation to the Barloworld bid;
  - (D) the precise basis on which the directors of Watty Limited have formed the view that it is no longer appropriate to pay the proposed Special Dividend;
  - (E) the precise basis of the directors of Watty Limited statement in Watty Limited's announcement of 13 February 2006 that the Barloworld bid "will provide" improved value to Watty Limited shareholders;
- (b) in conjunction with any statement of the directors' of Watty Limited intended recommendation that shareholders accept the Barloworld Proposed Offer, a clear and full statement of the risk of non-satisfaction of the Competition Condition, and the risk of delay in the determination of the satisfaction or non-satisfaction of the Competition Condition, and hence the risks to Watty Limited shareholders of following the directors' of Watty Limited recommendation to accept the Barloworld Proposed Offer;



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- (c) the precise basis of certain assumptions as to the future financial performance of WattyL sufficient to enable WattyL shareholders to assess the validity of these assumptions and the likelihood of these assumptions actually occurring;
- (d) an unequivocal statement by the directors of WattyL that they believe that the basis supporting their assumptions as to the future financial performance of WattyL, and therefore the assumptions themselves, are reasonable;
- (e) whether or not the proposal to pay the Special Dividend will revive if the Barloworld Proposed Offer lapses and the AEP Offer remains open for acceptance;
- (f) in relation to the Special Dividend:
  - (i) the precise elements of WattyL's "internal restructuring";
  - (ii) how that "internal restructuring" will of itself create sufficient retained earnings to pay the Special Dividend;
  - (iii) the fact that WattyL will not have sufficient available cash to pay the Special Dividend, and must borrow the cash to pay it;
  - (iv) the effect on WattyL of assuming additional borrowings on WattyL's risk profile;
  - (v) the fact that the Special Dividend will have the direct result of removing from the share price of WattyL an amount broadly comparable to the amount of the dividend; and
  - (vi) why it is in the best interests of WattyL shareholders to pay the Special Dividend only if the AEP Offer fails;
- (g) the break fee and exclusivity provisions of the Pre-Bid Deed be either:
  - (i) cancelled in their entirety; or
  - (ii) cancelled if the Competition Condition is not satisfied or waived within a reasonable time; and
- (h) WattyL withdraw its proposal to pay the Special Dividend.

## DISCUSSION

### Disclosure deficiencies

#### *ACCC - inconsistency of statements by WattyL*

46. AEP submitted that WattyL shareholders were misled as to the risks surrounding the likelihood of Barloworld obtaining ACCC approval and the potential timeframes involved for satisfying the Competition Condition because:
- (a) WattyL shareholders had been provided with inconsistent messages from the directors of WattyL regarding the likelihood of the Competition Condition being satisfied given that (among other matters) the:
    - (i) statement the chairman made at WattyL's Annual General Meeting in October 2005 (which was to the effect that the likelihood of ACCC

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approval of a combination of the Wattyl and Barloworld businesses was very low);

- (ii) the Wattyl directors' publicly stated intention to recommend the Barloworld Proposed Offer;
- (iii) the directors of Wattyl had annexed to Wattyl's second supplementary target's statement the Barloworld announcement which stated that:

*"Barloworld has held preliminary discussions with the [ACCC]. The company understands that the ACCC will undertake market enquiries over the next number of weeks to address competition issues. Given the structural and other changes in the Australian coatings market over the last decade, Barloworld is confident of a successful conclusion to the transaction and looks forward to assisting the ACCC with its enquiries";*

- (b) Wattyl directors had failed to adequately explain the basis for the Wattyl directors' recommendation of the Barloworld Proposed Offer; and
- (c) Wattyl shareholders had not been given enough information to assess the likelihood or otherwise of the Competition Condition being satisfied.

47. The Panel considered that Wattyl shareholders would be able to make their own determination as to risk or uncertainty in respect of the Barloworld Proposed Offer if they were adequately informed. Accordingly the Panel decided that the primary disclosure issues in relation to the Competition Condition were:

- (a) disclosure of the history of ACCC issues known to the directors of Wattyl; and
- (b) the fact that the outcome of the Competition Condition may not be known during the currency of the AEP Offer.

48. The Panel therefore required Wattyl to disclose in a supplementary target's statement to the AEP Offer:

- (a) the statement that the chairman made at Wattyl's Annual General Meeting in October 2005 (which was to the effect that the likelihood of ACCC approval of a combination of the Wattyl and Taubmans businesses was very low (Taubmans by 2005 having been acquired by Barloworld));
- (b) the history of ACCC opposition to a merger between Wattyl and Taubmans, and that since the ACCC's opposition to a merger in 1996 Barloworld had made further acquisitions of competitive businesses in the Australian market such that Wattyl shareholders would be aware that the satisfaction of the Competition Condition was not a foregone conclusion; and
- (c) the risk that the outcome of the Competition Condition was unlikely to be known within the time frame of the current AEP Offer.

49. The Panel considered that Wattyl directors need not address the reasons for their intention to recommend the Barloworld Proposed Offer until Wattyl responded to Barloworld's bidder's statement. In this regard, the Panel acknowledged Wattyl's submissions that it would include in its target's statement in response to the Barloworld bidder's statement (among other matters) the Wattyl directors' reasons for recommending acceptance of the Barloworld Proposed Offer.

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#### *The risks surrounding ACCC approval*

50. The Panel did not find that Wattyl was required to make any disclosure beyond that necessary to explain to shareholders the history of ACCC involvement so as to make clear to shareholders that the risk of Barloworld not gaining ACCC approval was a material issue for Wattyl shareholders to consider in deciding whether to sell Wattyl shares on market (having regard to current and historical trading prices), accept the AEP Offer or wait for the Barloworld Offer to be made. The Panel considered that unless something else became public, other comments on the prospects of Barloworld obtaining ACCC approval need not be made by Wattyl until Wattyl responded to Barloworld's bidder's statement.
51. The Panel agreed with Wattyl's submissions that Wattyl was not obliged to engage in speculation regarding the views of the ACCC<sup>2</sup>. However, the Panel considered that Wattyl:
  - (a) could nonetheless have its own reasoned view; and
  - (b) should disclose advice received from the ACCC regarding the Barloworld Proposed Offer. The failure to disclose information of this kind could constitute unacceptable circumstances.

#### *The directors' opinion*

52. AEP submitted that:
  - (a) it was highly unlikely that the Wattyl Directors had not formed any opinion as to the likelihood of the Competition Condition being satisfied and that therefore the Wattyl directors should state their opinion;
  - (b) Wattyl should disclose the factors relevant to an ACCC assessment of the Barloworld Proposed Offer; and
  - (c) Wattyl should explain why it had changed its view held as at 28 October 2005.
53. The Panel did not consider that Wattyl or its directors could reasonably be required to forecast how the ACCC (or any appeal or subsequent proceedings) would be decided.

#### *Special Dividend*

54. AEP submitted that it was not entirely clear whether or not the proposal to pay the Special Dividend would revive if both the AEP Offer and the Barloworld Proposed Offer closed unsuccessfully.
55. The Panel found that the disclosure by Wattyl in respect of the Special Dividend was not sufficient and the Wattyl shareholders would be confused by Wattyl's disclosure to date.

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<sup>2</sup> Wattyl submitted that the ACCC had cautioned companies against making predictions of the ACCC's view. This finding is also consistent with the previous Panel decision in *S.A. Liquor Distributors Ltd* [2002] ATP 22 although the Panel noted that decision was concerned with disclosure in a bidder's statement and the target and bidder did not have the same history with the ACCC as is the case with Wattyl and Barloworld.

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56. In particular, the Panel considered that Wattyl needed to clarify, in a supplementary target's statement:
- (a) Wattyl's intention with respect to reintroducing the Special Dividend; and
  - (b) the timing of any reintroduction.
57. Wattyl had provided to the Panel in a letter dated 8 March 2006 the following summary in respect of the status of the Special Dividend:
- "1. ...no special dividend has been declared or paid and, at the current time there is no proposal to pay the special dividend. As set out in Wattyl's letter to shareholders, Barloworld's offer includes a condition that Wattyl not pay dividends in excess of 100% of Wattyl's NPAT. Wattyl does not currently propose to take any action which is likely to trigger this condition. Accordingly, whilst the Barloworld offer is pending or on foot, there is no proposal to pay the special dividend.*
- 2. ...the Wattyl directors may reintroduce the special dividend...*
- 3. If all offers for Wattyl close unsuccessfully, Wattyl proposes to pay the special dividend."*
58. The Panel considered that Wattyl's disclosure of the above would assist the Wattyl shareholders to understand Wattyl's intentions regarding the Special Dividend. Wattyl undertook to provide these disclosures in a supplementary target statement and did on 28 March 2006.

#### Forecasts

59. AEP submitted that the Wattyl Target's Statement failed to disclose the basis of the Wattyl directors' assumptions that:
- (a) Wattyl will generate revenue of \$431.9 million in FY2006 (an increase of 2.5% from FY2005) and that Wattyl's revenue will grow by a further 4.9% in FY2007 to \$453.0 million;
  - (b) Wattyl will maintain its market share in the Australian and New Zealand paints and coatings industry and will achieve sales volume of 63.7 million litres in FY2006 and 65.5 million litres in FY2007, with forecast growth in volume of (0.3)% for FY2006 and 2.9% for FY2007;
  - (c) Wattyl will achieve price increases of 2.8% for FY2006 and 2.0% for FY2007, such that Wattyl shareholders and their professional advisers are unable to assess the validity of those assumptions or the likelihood of those assumptions being satisfied.
60. AEP also submitted that:
- (a) there were no reasons, verifiable or otherwise given anywhere in Wattyl's Target's Statement to support the assumptions to the forecasts set out above in paragraph 59;
  - (b) the disclaimers given by the Wattyl directors in respect of the forecasts were excessive such that Wattyl shareholders had no basis to rely on the assumptions to the forecasts,
- and that these matters also negated the assertion of reasonableness provided by the Wattyl directors in section 5.3.1 of the Wattyl Target's Statement.

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61. The Panel did not find that Wattyl was required to make additional disclosure. The Panel noted the explanations that Wattyl provided in the forecasts, the review undertaken by PriceWaterhouseCoopers<sup>3</sup>, and the customary nature of the negative assurance PriceWaterhouseCoopers had given as to methodology and assumptions used in the forecasts.
62. AEP has also submitted that the way in which Ernst & Young had used the director's forecasts in its expert's report was inappropriate. The Panel did not find that this was the case.

### The break fee and exclusivity arrangements

#### *The break fee*

63. AEP submitted that:
  - (a) the break fee in clause 5 the Pre-Bid Deed (as described in paragraph 37 above) was anti-competitive and would have a coercive effect on the Wattyl shareholders;
  - (b) the Wattyl directors should disclose the precise basis on which the Wattyl directors had agreed to pay the break fee under the Pre-Bid Deed, because failure to do so would result in the market for control of Wattyl shares not being efficient, competitive and informed.
64. AEP also submitted that it was premature for the directors of Wattyl to enter into the Pre-Bid Deed prior to the decision of ACCC on the Barloworld Proposed Offer being known.
65. AEP submitted that the Pre-Bid Deed was anti-competitive because the break fee equated to more than Wattyl's projected adjusted profits after tax in the 2006 financial year and potential financial buyers of Wattyl would be discouraged by the payment of the break fee to Barloworld a competitor of Wattyl in the circumstances set out in the Pre-Bid Deed.
66. AEP also submitted that the Pre-Bid Deed was anti-competitive because the break fee would last for as long as Barloworld chose to keep its bid open. On the basis that Barloworld had not yet lodged its bidder's statement and its offer could remain open for up to 12 months following the making of the Barloworld offer, AEP submitted that the break fee and the exclusivity agreement could last for up to fourteen months. AEP submitted that this period was unacceptably long when compared to the Panel's guidance in paragraphs 7.30 and 7.46 of the Panel's Guidance Note 7 on Lock-up Devices.
67. The Panel's Guidance Note No. 7 on Lock-up devices considers that a break fee should not exceed 1% of the equity value of the target. The break fee agreed to in the Pre-Bid Deed did not exceed this guideline. Although it was significant in terms of

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<sup>3</sup> PricewaterhouseCoopers had prepared an investigating accountant's report (which was contained in the Wattyl Target's Statement) which stated that PricewaterhouseCoopers had made a review of the prospective financial information for financial years ending 2006 and 2007 relating to Wattyl and set out in the Wattyl Target's Statement as well as the preparation of the forecasts and the assumptions which underpinned those forecast financials.

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the 2006 adjusted, after tax profit, the Panel did not find that the quantum of the break fee was excessive. The Panel therefore then considered the structure and effect of clause 5 of the Pre-Bid Deed in the context of the AEP Offer and the Barloworld Proposed Offer.

68. Following consideration of the parties' submissions, further correspondence between the parties and the Panel and the Panel's policy, the Panel found that the break fee provision in clause 5 of the Pre-Bid Deed was unacceptable given the length of time it would operate over and lack of a carve out in respect of the situation where the Competition Condition was unable to be satisfied.
69. The Panel's policy on break fees at paragraph 7.27 of Guidance Note No. 7 on Lock-up devices is that:

*"If a step which is beyond the control of target directors but which critically affects the ability of those target directors to enter into a proposal is outstanding, those directors should consider whether it is appropriate to delay entry into the break fee arrangement until that step has been taken or consider making the payment of the break fee contingent upon completion of that step."*
70. The Panel considered that the principle set out in paragraph 7.27 of the Lock-Up Devices Guidance Note applied to the directors of Wattyl in the context of the Competition Condition and the known background to any Barloworld acquisition and their entry into the Pre-Bid Deed. The Panel considered that in this context the directors of Wattyl needed to consider and address the effect of the Pre-Bid Deed if the Competition Condition was not determined within a reasonable period of time, which in these circumstances was very likely.
71. The Pre-Bid Deed did not address the Competition Condition in the context of the:
  - (a) history of ACCC opposition to a merger between Wattyl and Taubmans; and
  - (b) risk that the outcome of the Competition Condition is unlikely to be known for potentially a long period of time.
72. The Panel acknowledged that entry into or the operation of the Pre-Bid Deed could not realistically be suspended until the Competition Condition was satisfied or waived. That said, the Panel considered the circumstance could be addressed by an appropriate carve out, which the Panel considered was required.
73. The Panel found that clause 5 of the Pre-Bid Deed should be amended such that the break fee would not be payable if:
  - (a) the Competition Condition had not been satisfied by 13 August 2006 (six months from the date of the announcement of Barloworld's intention to bid); or
  - (b) the approval needed to satisfy the Competition Condition had been refused and that decision had been accepted by Barloworld prior to 13 August 2006,and the triggers for payment (as described in paragraph 37 above) were not otherwise triggered.
74. The Panel made no finding regarding whether or not the entry into the Pre-Bid Deed by the Wattyl directors would have contravened any laws relating to directors duties.

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#### *“No shop” provision*

75. AEP submitted that the exclusivity provisions in clause 8 of the Pre-Bid Deed (as described in paragraph 40 above):
- (a) did not contain a fiduciary carve out as required by the Panel’s Guidance Note No. 7 on Lock-up devices; and
  - (b) the provisions operated for too long a period (i.e. they were to last for as long as Barloworld decided to keep its bid open) contrary to the Panel’s Guidance Note No. 7 on Lock-up devices.
76. AEP submitted that the exclusivity provisions in clause 8 of the Pre-Bid Deed were effectively “no shop” and “no talk” provisions.
77. The Panel’s Guidance Note No. 7 on Lock-up devices describes a no talk agreement as *“an arrangement entered into between a bidder, or potential bidder, and the target by which a target agrees not to negotiate with any bidder or potential bidder, even if that bidder’s approach to the target is unsolicited.”*<sup>4</sup>
78. The Panel’s Guidance Note No. 7 on Lock-up devices identifies that no talk agreements are more anti-competitive than no shop agreements. Accordingly, the Panel’s Guidance Note No. 7 on Lock-up devices states that:
- (a) *“target directors need to be convinced of the proper commercial and competitive benefits to their shareholders before agreeing to this form of agreement”*<sup>5</sup>;
  - (b) *“the period of restraint must be limited and reasonable: in order not to be unacceptable, a no-talk obligation should usually cease once a public announcement of the relevant bid or proposal has been made”*<sup>6</sup>;
  - (c) it is *“essential that a no-talk agreement contain an appropriate ‘fiduciary exception’, allowing directors to respond positively to any better proposal if they form the view that to do so would be in the best interests of target shareholders”*<sup>7</sup>.
79. On the other hand, the Panel’s Guidance Note No. 7 on Lock-up devices describes a no-shop agreement as *“an arrangement entered into between a bidder, or potential bidder, and the target by which a target agrees not to solicit a takeover bid or other control transaction from a third party, usually during some defined period of exclusivity”*<sup>8</sup>.
80. The Panel does not generally require that a no-shop agreement be constrained by a fiduciary exception. The period of restraint must be limited and reasonable and may extend into the bid period where this is justifiable having regard to the advantages that the agreement offers to target shareholders.
81. The Panel found that the exclusivity provision in clause 8 was very close to one that would be unacceptable. The Panel considered it would have been unacceptable if it extended to a prohibition on WattyL talking to other bidders or prospective bidders (i.e. it was a “no talk” provision). However, each of the parties to the Pre-Bid Deed

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<sup>4</sup> See paragraph 7.28.

<sup>5</sup> See paragraph 7.30.

<sup>6</sup> See paragraph 7.30.

<sup>7</sup> See paragraph 7.31.

<sup>8</sup> See paragraph 7.34.

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had assured the Panel that the provision was not a "no talk" provision and would not be applied as one. The Panel therefore did not consider this circumstance to be an unacceptable circumstance, although if, in practice, the parties acted as if the provision was a "no talk" provision, that could be grounds for the Panel to reconsider the clause on a new application.

#### *The assistance provision*

82. AEP also sought, in its submissions, an additional order that clause 3 of the Pre-Bid Deed be cancelled.
83. Clause 3 of the Pre-Bid Deed dealt with Watty providing assistance and information to Barloworld during the period of the Barloworld Proposed Offer. It required Watty, among other things, to "consult and discuss with Barloworld all material facts, events or circumstances affecting or likely to affect Watty or its businesses". There were exceptions in clause 3, including an exception for commercially sensitive information. AEP submitted that even with these exceptions the information which Watty would be required to provide to Barloworld under clause 3 would give Barloworld a competitive advantage over Watty should Barloworld's bid not succeed. That would discourage alternative bidders and also have a coercive effect in that, since Watty may be weakened as a competitor of Barloworld, Watty shareholders may be forced to accept the Barloworld bid on the basis that Watty may be rendered unattractive to any bidder other than Barloworld.
84. The Panel did not find clause 3 created unacceptable circumstances. It considered that the information provided under the clause, given the exceptions, would not provide Barloworld with an unreasonable advantage or the ability to frustrate or deter a rival bidder.

#### **Special Dividend**

85. AEP sought that Watty withdraw its proposal to pay the Special Dividend. As discussed above, at the time of the Application Watty had done this.
86. AEP submitted that Watty held the Special Dividend out as a form of "reward" to Watty shareholders for rejecting the AEP Offer and that this constituted unacceptable circumstances.
87. The Panel considered that the Special Dividend, if consistent with the Watty directors' duties in managing a solvent enterprise, would not constitute frustrating action or unacceptable circumstances in regard to the AEP Offer. The Panel considered that the Watty directors were entitled to put forward alternative scenarios to Watty shareholders where there was one or more competing control proposals set before the Watty shareholders. Watty described the Special Dividend as one way of maintaining price tension in relation to the AEP Offer, and as such was in the interests of Watty shareholders.
88. However, the Panel considered that such a capital transaction could be coercive on shareholders. The Panel considered that shareholders who may have preferred not to have accepted either the AEP Offer or the Barloworld Proposed Offer might feel coerced into accepting one of them if they considered that the capital transaction proposed by the Watty directors made Watty a less attractive investment than the



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consideration offered under either of offers, when Wattyl may have been more attractive without the capital transaction.

89. In view of the withdrawal of the Special Dividend, the Panel did not consider it was necessary to decide whether or not payment of the Special Dividend itself would give rise to unacceptable circumstances. That said, the Panel considered that Wattyl should give consideration to making any reintroduction of a proposed special dividend to be paid in the event of both takeover bids failing subject to Wattyl shareholder approval.

#### Delay

90. AEP submitted that the course of conduct adopted by Wattyl had the effect of delaying consideration by Wattyl shareholders of the merits of the AEP Offer in an efficient, competitive and informed market. The Panel did not consider that that delay, if any, and any conduct of Wattyl in producing any delay, had raised concerns for the Panel.
91. The Panel noted AEP's concern that the timeframe for Barloworld's bidder's statement for the Barloworld Proposed Offer had not yet been disclosed. However, the Panel considered that the timetable for Barloworld making its offer was subject to the constraints of section 631 and, the time specified in section 631 not having elapsed yet, was not an issue for the Panel at this stage.

## DECISION

#### Decision

92. The Panel was minded to make a declaration under section 657A that the following circumstances in relation to the affairs of Wattyl constituted unacceptable circumstances:
- (a) the Wattyl directors' published intention (in an ASX announcement annexed to its second supplementary target's statement to the AEP Offer) to recommend acceptance of the Barloworld Proposed Offer, without adequately dealing with:
    - (i) the statement by the chairman of Wattyl to the Annual General Meeting in October 2005 following the merger discussions with Barloworld in September 2005;
    - (ii) the history of ACCC opposition to a merger between Wattyl and Taubmans and that since then Barloworld had made further acquisitions of competitive businesses in the Australian market; and
    - (iii) the fact that the Barloworld Proposed Offer was subject to the Competition Condition, but the satisfaction or triggering of the Competition Condition was unlikely to be known within the time frame of the AEP Offer;
  - (b) the level of disclosure concerning the status of Wattyl's proposed Special Dividend; and
  - (c) in respect of the break fee provision in clause 5 of the Pre-Bid Deed, the length of time it would operate, and lack of a carve out if the Competition Condition was unable to be satisfied.

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93. The Panel advised Wattyl and Barloworld that it was prepared to consider undertakings from Wattyl (and in respect of the Pre-Bid Deed, Barloworld), to its satisfaction, that may indicate that declining to make a declaration would not be against the public interest.
94. Following the receipt of further submissions from the parties:
- (a) Wattyl and Barloworld undertook to the Panel to give effect to the changes to the break fee clause in the Pre-Bid Deed requested by the Panel;
  - (b) Wattyl prepared, lodged with ASIC, sent to ASX, AEP and Wattyl shareholders its third supplementary target's statement which addressed the Panel's concerns with Wattyl's disclosure as identified in these reasons, to the Panel's satisfaction;
  - (c) Wattyl and Barloworld drafted, agreed and submitted to the Panel a deed of amendment in order to effect the changes to the break fee clause in the Pre-Bid Deed required by the Panel.
95. Given:
- (a) receipt by the Panel of undertakings from both Barloworld and Wattyl to amend the Pre-Bid Deed as requested by the Panel;
  - (b) the lodgement, release and despatch of Wattyl's third supplementary target's statement as approved by the Panel; and
  - (c) approval by the Panel of the deed of amendment between Wattyl and Barloworld which was to effect the changes to the break fee clause in the Pre-Bid Deed required by the Panel,

the Panel considered that, in accordance with section 657A, it was not against the public interest to decline to make a declaration of unacceptable circumstances.

### Matters that occurred before Wattyl despatched its corrective disclosure

#### *Close of the AEP Offer*

96. The Panel also noted that, after it had approved Wattyl's third supplementary target's statement but before Wattyl had in fact printed and despatched, there had been speculation in the media that AEP had indicated that it had decided not to extend the AEP Offer after the date it was at that time due to close (i.e. Monday 3 April 2006).
97. The Panel therefore asked AEP on Thursday 30 March 2006 whether the speculation was correct and, if so, asked the parties to provide it with submissions as to whether or not there was any merit in requiring Wattyl's third supplementary target's statement to be printed and dispatched to Wattyl shareholders.
98. AEP responded later that day, stating (among other matters) that:
- "With one exception the articles...merely speculate that AEP will not extend its offer, with no indication from AEP as to its actual position..."*
- and that
- "...The decision will be made on Monday..."*

## **Takeovers Panel**

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99. In addition, AEP suggested that Watty wait until 3 April 2006 to see whether the AEP Offer would be extended before posting.
100. Watty printed and posted its third supplementary target's statement to Watty shareholders on 31 March 2006. AEP did not extend the AEP Offer.

### **Orders**

101. As the Panel did not make a declaration of unacceptable circumstances, the Panel made no orders for costs or otherwise.

**Kathleen Farrell**

**President of the Sitting Panel**

**Decision dated 28 March 2006**

**Reasons published 29 May 2006**