



**Australian Government**

**Takeovers Panel**

**Reasons for Decision  
Merlin Diamonds Limited  
[2016] ATP 18**

**Catchwords:**

*Association – association hurdle – common directors – convertible notes – options – substantial holder notices – family relationships – disclosure of association – extension of time for making application – declaration – orders – costs*

*Corporations Act 2001 (Cth), sections 9 ('relevant agreement'), 12, 16, 249D, 602(b) and (c), 606(1), 606(5), 609(5), items 7 and 9 of 611, 657C(3), 671B*

*ASIC Act 2001 (Cth), section 30, ASX Listing Rules 7.1, 7.1A and 10.11, Bankruptcy Act 1966 (Cth), section 116*

*Palmer Leisure Coolum Pty Ltd v Takeovers Panel [2015] FCA 1498, Tinkerbell Enterprises Pty Limited as Trustee for The Leanne Catelan Trust v Takeovers Panel [2012] FCA 1272, ASIC v Fortescue Metals Group Ltd [2011] FCAFC 19, ASIC v Yandal Gold Pty Ltd (1999) 32 ACSR 317, ACCC v CC (NSW) Pty Ltd [1999] FCA 954; (1999) 92 FCR 375, Adsteam Building Industries Pty Ltd & Anor v The Queensland Cement and Lime Co Ltd & Ors (1984) 14 ACLR 456*

*Guidance Note 4: Remedies General*

*Sovereign Gold Limited [2016] ATP 12, Ainsworth Game Technology Limited 01 & 02 [2016] ATP 9, The President's Club Limited 02 [2016] ATP 1, Avalon Minerals Limited [2013] ATP 11, World Oil Resources Limited [2013] ATP 1, Bentley Capital Limited 01R [2011] ATP 13, CMI Limited 01R [2011] ATP 5, CMI Limited [2011] ATP 4, Viento Group Limited [2011] ATP 1, Mount Gibson Iron Limited [2008] ATP 4, AMP Shopping Centre Trust 02 [2003] ATP 24, Winepros Limited [2002] ATP 18*

Interim order	IO undertaking	Conduct	Declaration	Final order	Undertaking
YES	NO	YES	YES	YES	NO

**INTRODUCTION**

1. The Panel, James Dickson (sitting President), Shirley In't Veld and Karen Phin, made a declaration of unacceptable circumstances in relation to the affairs of Merlin Diamonds Limited. The application concerned possible associations between directors and shareholders of Merlin in connection with the issue of convertible notes and options. The Panel considered Mordechai Gutnick is associated with Joseph Gutnick and Regals Fund LP, which resulted in contraventions of s606 and the substantial holder notice provisions. The Panel also considered the explanatory memorandum for a general meeting of Merlin shareholders held on 6 September 2016 to approve the issue of convertible notes and options was misleading. The Panel made a declaration of unacceptable circumstances and made orders including a restriction on one noteholder converting or exercising its notes and options in certain circumstances without item 7 of s611 shareholder approval, a voting restriction on Regals, disclosure and costs.

2. In these reasons, the following definitions apply.

**6 September Meeting**      the general meeting of shareholders of Merlin held on 6 September 2016

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<b>AHA</b>	Atlantic Holdings (Aust) Pty Ltd
<b>Chabad Properties</b>	Chabad Properties Pty Ltd as trustee of Machon Chaim College Fund
<b>GCG</b>	Great Central Gold Limited
<b>Green</b>	Emanuel Max Green and Sharon Green <The Green Super Fund A/C>
<b>Max Green</b>	Emanuel Max Green
<b>Mazil</b>	Mazil Pty Ltd as trustee of the Mazil Superannuation Fund
<b>Merlin</b>	Merlin Diamonds Limited
<b>Morzev</b>	Morzev Pty Ltd
<b>NRMZ</b>	NRMZ Pty Ltd as trustee of the NRMZ Family Trust
<b>Regals</b>	Regals Fund LP
<b>TMG</b>	Trinity Management Group Pty Ltd

3. Unless indicated otherwise, submissions described in these reasons as made by Merlin were also made on behalf of some or all of Mazil, GCG, AHA, Morzev, Mordechai Gutnick, Joseph Gutnick, NRMZ, Chabad Properties and Stera Gutnick.

## FACTS

4. Merlin Diamonds Limited is a listed diamond exploration and development company (ASX code: MED).
5. On 23 June 2016, Merlin entered into a secured note deed with Regals for the issue of 1,307,537 notes (the “**Regals Notes**”) and 87,169,569 options over Merlin shares. Regals is a Delaware limited partnership based in New York and is managed exclusively by David Slager. As at 23 June 2016, Regals had a relevant interest in 25,162,755 Merlin shares.
6. On 28 June 2016, Merlin entered into a secured note deed with Chabad Properties for the issue of 1,100,000 notes and 73,333,700 options over Merlin shares. The directors of Chabad Properties are Mordechai Gutnick and Stera Gutnick. Joseph Gutnick ceased to be a director on 7 July 2016. As at 28 June 2016, Joseph Gutnick, Stera Gutnick and Mordechai Gutnick each held one third of the shares in Chabad Properties.
7. On 30 June 2016, Merlin entered into a further secured note deed with Chabad Properties for the issue of 900,000 notes (together with the notes in paragraph 6, the “**Chabad Notes**”) and 60,000,300 options over Merlin shares.
8. On or around 4 July 2016, David Slager agreed by email to lend Mordechai Gutnick \$300,000 (USD) interest free to buy shares in Merlin.

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9. On or around 8 July 2016, Joseph Gutnick became bankrupt. On 7 July 2016, Joseph Gutnick resigned as a director of Merlin and Mordechai Gutnick was appointed as a director of Merlin on the same date.
10. On 12 July 2016, Merlin entered into a secured note deed with NRMZ for the issue of 392,054 notes (the “**NRMZ Notes**”) and 26,137,064 options over Merlin shares. Mordechai Gutnick is the sole shareholder and director of NRMZ.
11. The secured note deeds were in materially identical terms. The notes had a 3 year term, a face value of \$1.00 per note and a coupon rate of 10% per annum, payable monthly in arrears. Each subscriber was entitled to receive upon completion or anytime thereafter, to the extent Merlin was able to do so without being in breach of the Listing Rules or the *Corporations Act 2001* (Cth), convertible notes instead of non-convertible notes. The subscription amount, payable on completion, was the full face value of the notes. The face value of the convertible notes (plus any outstanding interest) was convertible into shares at the lower of \$0.015 per share or the 5 day VWAP on the trading day immediately preceding the date of the conversion notice.
12. The secured note deeds provided that, if shareholder approval was required for the issue of the notes or conversion of the notes, Merlin was required to procure that approval within 90 days of the issue of the notes. If approval was not obtained by such date, a coupon rate of 15% per annum applied and the noteholder had the right to redeem the notes at a penalty rate.
13. Merlin sought shareholder approval for the notes and options issued under the secured note deeds with Regals, NRMZ and Chabad Properties, as well as the issue of additional notes and options, at the 6 September Meeting, which was convened by a notice of meeting dated 2 August 2016. The record date for the meeting was initially stated to be 31 July 2016, but later changed to 2 September 2016. The four resolutions put to shareholders were:
  - (a) An issue of up to 1,307,537 convertible notes and 87,157,133 options to Regals in accordance with Listing Rule 7.1 and for all other purposes (“**Resolution 1**”)
  - (b) An issue of up to 392,054 convertible notes and 26,137,064 options to NRMZ in accordance with Listing Rules 7.1 and 10.11 and for all other purposes (“**Resolution 2**”)
  - (c) An issue of up to 2,000,000 convertible notes and 133,333,333 options<sup>1</sup> to Chabad Properties in accordance with Listing Rules 7.1 and 10.11 and for all other purposes (“**Resolution 3**”) and
  - (d) A placement of up to a further 2,000,000 convertible notes and 133,333,333 options in accordance with Listing Rule 7.1 and for all other purposes (“**Resolution 4**”).

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<sup>1</sup> The aggregate number of options issued to Chabad Properties under the secured note deeds for Chabad Properties was 133,334,000 options. Merlin’s Option register also records 133,334,000 options issued to Chabad Properties

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14. The explanatory memorandum for the 6 September Meeting indicated that if all the notes and options of Regals, NRMZ and Chabad Properties were converted and exercised (and no other shares were issued) they would hold 20.09%, 5.53% and 28.23% of Merlin shares, respectively.<sup>2</sup>
15. The explanatory memorandum for the 6 September Meeting stated, in relation to Resolution 1 regarding the Regals Notes, that the secured note deed with Regals “has a requirement that the conversion of the convertible notes cannot result in Regal holding more than 19.9% of the issued shares of the Company at the time of conversion, unless shareholder approval is obtained” (the “**19.9% Conversion Requirement**”). The preamble in relation to Resolutions 2, 3 and 4 stated that the notes and options to be issued under each of those resolutions “will have the same terms and conditions as those to be issued to Regal as set out in Resolution 1”. However the secured note deeds for the Regals Notes, NRMZ Notes and Chabad Notes did not include any express requirement to the effect of the 19.9% Conversion Requirement. Rather, if the notes became convertible, they conferred on Regals, NRMZ and Chabad Properties the ability to require the issue of shares over time (relying on the 3% creep exception in item 9 of s611<sup>3</sup>) giving them collectively more than 50% of Merlin shares (assuming no other shares were issued). The explanatory memorandum referred to Regals and Chabad Properties potentially holding over 20%, but did not attempt to reconcile those references with the 19.9% Conversion Requirement.
16. On 11 August 2016, NRMZ transferred the NRMZ Notes to Green.
17. On 29 August 2016, Merlin received a notice of requisition from S.H. Rayburn Nominees Pty Ltd to hold a shareholders meeting pursuant to s249D to replace the board (the “**s249D Requisition**”).
18. On 1 September 2016, Merlin issued 56,317,090 shares, including 50,000,000 shares issued to Regals on conversion of 750,000 convertible notes.<sup>4</sup>
19. Also on 1 September 2016, according to Merlin’s Note Register, the NRMZ Notes transferred to Green were converted into convertible notes.
20. On 2 September 2016, Merlin issued 38,236,933 shares, including 26,136,933 shares to Green on conversion of all of the NRMZ Notes.
21. At the 6 September Meeting, Resolutions 2, 3 and 4 passed and Resolution 1 failed.<sup>5</sup>
22. Green voted in favour of all the resolutions. Regals voted in favour of Resolutions 2, 3 and 4 but was excluded from voting on Resolution 1. Mazil, GCG, TMG and Morzev voted in favour of all the resolutions. AHA voted in favour of Resolutions 1 and 4 but was excluded from voting on Resolutions 2 and 3.

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<sup>2</sup> If only one of Regals, NRMZ or Chabad Properties converted/exercised all their notes and options (and no other shares were issued) the explanatory statement indicated that the holding of that party of Merlin shares could increase to as much as 31.89%, 10.38% or 37.14%, respectively

<sup>3</sup> Unless otherwise indicated, all statutory references are to the *Corporations Act 2001* (Cth), and all terms used in Chapter 6 or 6C have the meaning given in the relevant Chapter (as modified by ASIC)

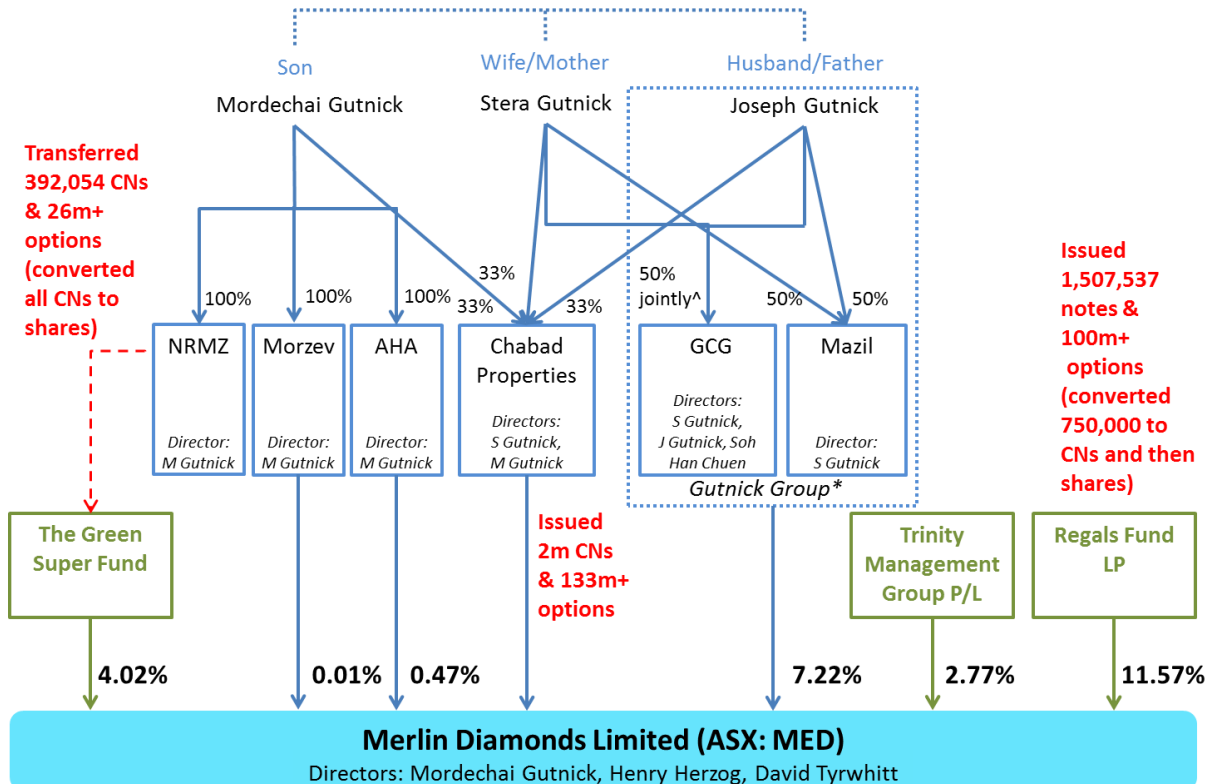
<sup>4</sup> Merlin submitted that it had capacity under Listing Rules 7.1 and 7.1A to convert the convertible notes into shares

<sup>5</sup> On 28 October 2016, Merlin lodged its Notice of Annual General Meeting, which included a resolution to approve the issue of 1,507,537 convertible notes and 100,502,969 options to Regals

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23. On 16 September 2016, the s249D Requisition was withdrawn.
24. On 28 October 2016, Merlin lodged its Notice of Annual General Meeting, which included a resolution to approve the issue of 1,507,537 convertible notes and 100,502,969 options to Regals. The explanatory memorandum disclosed that Merlin had issued 1,507,537 notes<sup>6</sup> to Regals and Regals had converted 750,000 notes into 50,000,000 shares under Merlin's 15% rule capacity.
25. Shareholdings in Merlin and various relationships between the parties are set out in the diagram below.



\* As described in the substantial holder notice dated 15 January 2015 [but excludes shares held by TMG]

^ 50% held by Soh Han Chuen

Shareholdings in Merlin are calculated as of 22 November 2016 (based on 649,680,949 total issued shares issued)

## APPLICATION

### Declaration sought

26. By application dated 31 October 2016, Thomas Reddcliffe (a shareholder in Merlin) sought a declaration of unacceptable circumstances. The applicant submitted (among other things) that:
  - (a) the issue of shares to Regals and others on 1 and 2 September 2016, to the extent those shares were voted, was to ensure that Resolutions 2 and 3 were passed

<sup>6</sup> Merlin entered into a second secured note deed dated 19 October 2016 with Regals for 195,236 notes and 13,015,798 options for a subscription amount of \$195,236. The Regals Notes plus the notes issued to Regals on 19 October 2016 is less than the total number of notes referred to in Notice of Annual General Meeting. Merlin's note register records 197,576 notes issued to Regals on 19 October 2016

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- (b) the voting by Mazil, GCG and TMG in favour of Resolutions 2 and 3 breached the related party provisions of the Act
  - (c) certain Merlin shareholders became associates or were acting in concert in relation to the affairs of Merlin
  - (d) the actions described above have resulted in those shareholders and their respective associates increasing their interests in Merlin in breach of s606 and
  - (e) the actions described above have enabled the noteholders to increase their voting power in Merlin by the use of the 3% creep exception without Merlin shareholders (i) having been given enough information to enable them to assess the merits of a proposal to acquire a substantial interest in Merlin and (ii) having a reasonable and equal opportunity to participate in any benefits accruing from such proposal, as required under s602(b)(iii) and (c), respectively.
27. The applicant submitted that the effect of the circumstances was that shareholders have not been given enough information to enable them to assess the merits of, or a reasonable and equal opportunity to participate in any benefits accruing through, the acquisition of a substantial interest in Merlin (s602(b) and (c)).

#### Interim orders sought

28. The applicant sought interim orders pending determination of his application including orders restraining the conversion and disposal of the notes and options approved at the 6 September Meeting, the disposal and voting of the shares issued by Merlin on 1 and 2 September 2016 and further issues of Merlin shares.
29. The Panel made interim orders on 7 November 2016 that certain persons named in the application not dispose of, transfer, charge or otherwise deal with their securities (which included their shares, notes and options) in Merlin (Annexure A). We specified that the restrictions would apply in the absence of Panel consent and indicated that we were open to considering varying the orders or replacing the orders with undertakings that reduce any adverse impact of the orders to a party while still preserving our ability to make appropriate final orders (in the event we made a declaration).
30. At the time we made a declaration but before making final orders, we varied the interim orders (Annexure B) to clarify that the expression “*or otherwise deal with*” included the conversion of any convertible securities into shares of Merlin or the exercise of any options into shares of Merlin. We made a further interim order preventing certain noteholders relying on rights to require redemption of their notes as a consequence of the application in this matter, the declaration of unacceptable circumstances, the interim orders or any final orders. We made this interim order following a submission from Merlin that the declaration could have serious financial effects for Merlin and its shareholders if then current noteholders sought early redemption of their notes. None of the affected noteholders objected to the making of the interim order.

### Final orders sought

31. The applicant sought final orders including orders requiring that the issues of shares on 1 and 2 September 2016 be ratified and the notes and options be re-approved by shareholders (in each case, excluding the vote of the allottees of shares on 1 and 2 September 2016, the alleged associates and each of their respective associates).

### DISCUSSION

32. We have considered all the submissions and rebuttals and other material, but address specifically only those things that we consider necessary to explain our reasoning.

### Association Test

33. Section 12 sets out the tests for association as applied to Chapter 6. There are two relevant tests here:

- (a) s12(2)(b) - which provides, in essence, that B is an associate of A if (and only if) B is a person with whom A has, or proposes to enter into, a relevant agreement for the purpose of controlling or influencing the composition of a company's board or conduct of its affairs and
- (b) s12(2)(c) - which provides, in essence, that B is an associate of A if (and only if) B is a person with whom A is acting or proposing to act in concert in relation to the company's affairs.

34. A relevant agreement is an agreement, arrangement or understanding:

- (a) whether formal or informal or partly formal and partly informal and
- (b) whether written or oral or partly written and partly oral and
- (c) whether or not having legal or equitable force and whether or not based on legal or equitable rights.<sup>7</sup>

35. As stated by the Panel in *CMI Limited 01R*,<sup>8</sup> the cases make it clear that there is significant overlap between the concepts of "acting in concert" and "relevant agreement" in s12.

36. An understanding means an understanding – "plainly a word of wide import"<sup>9</sup> – as to some common purpose or object in relation to the company in question.

37. In *Mount Gibson Iron Limited*<sup>10</sup>, the Panel said circumstances which are relevant to establishing an association include:

- (a) a shared goal or purpose

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<sup>7</sup> Section 9

<sup>8</sup> [2011] ATP 5 at [33]-[34]

<sup>9</sup> *Adsteam Building Industries Pty Ltd & Anor v The Queensland Cement and Lime Co Ltd & Ors* (1984) 14 ACLR 456 at 459

<sup>10</sup> [2008] ATP 4. These factors have been applied in several Panel decisions including *Ainsworth Game Technology Limited 01 & 02* [2016] ATP 9, *Viento Group Limited* [2011] ATP 1, *CMI Limited* [2011] ATP 4 and *World Oil Resources Limited* [2013] ATP 1

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- (b) prior collaborative conduct
- (c) structural links
- (d) common investments and dealings
- (e) common knowledge of relevant facts and
- (f) actions which are uncommercial.

#### Decision to conduct proceedings

38. We decided to conduct proceedings. In our view there was, in terms of the test set out in *Mount Gibson*, “a sufficient body of evidence of association and to convince the Panel as to that association, albeit with proper inferences being drawn.”<sup>11</sup>
39. We initially considered whether any transactions constituted, or gave rise to, a contravention of ss606 or 671B or were otherwise unacceptable as a result of associations among the directors of Merlin (being Mordechai Gutnick, Henry Herzog and David Tyrwhitt), Joseph Gutnick, Mazil, GCG, AHA, Regals and any companies controlled by them.
40. The information received in submissions and rebuttals on our brief provided no material to suggest any association involving Henry Herzog or David Tyrwhitt. In a supplementary brief, we asked for submissions in relation to other possible associations involving Stera Gutnick (Joseph Gutnick’s wife) and Green, which are discussed below.

#### Preliminary findings

41. Having considered the issues raised in the application and submissions and rebuttals, we made preliminary findings in relation to whether association had been established between Mordechai Gutnick, on the one hand, and each of Joseph Gutnick, Regals and Green, on the other hand. We invited comments on the preliminary findings.
42. Our conclusions below on association take account of comments made on the preliminary findings as well as the other material supplied to us.
43. We considered the cumulative effect of all the material and have drawn inferences that, in our view, are justified. In doing so we had in mind that we must be satisfied by logical and probative material and the potential seriousness of a finding of association.
44. Further, when making an assessment of all the material in this matter we have relied on our skills, knowledge and experience as practitioners (which has been made known to the parties) and as members of the sitting Panel.<sup>12</sup> We have

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<sup>11</sup> *Mount Gibson Iron Limited* [2008] ATP 4 at [15]

<sup>12</sup> See *Tinkerbelle Enterprises Pty Limited as Trustee for The Leanne Catelan Trust v Takeovers Panel* [2012] FCA 1272 at [114]



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procedural requirements to meet and statutory time constraints in which to make a decision.<sup>13</sup> In our view, we have met these.

#### **Mordechai Gutnick and Joseph Gutnick**

##### *Family relationship*

45. Joseph Gutnick and Stera Gutnick are husband and wife and Mordechai Gutnick is their son.
46. Merlin submitted that the fact that Mordechai Gutnick is related to Joseph Gutnick and Stera Gutnick does not make them associates within the meaning of s12 and denied any association between Mordechai Gutnick, on the one hand, and Joseph Gutnick and Stera Gutnick, on the other.
47. We agree that a familial relationship does not automatically make persons associates. However, such relationships may nevertheless be relevant in assessing whether the broader factual matrix establishes association<sup>14</sup> and we consider that they are relevant here.

##### *Common shareholdings and directorships*

48. Based on the information available from ASIC's register, two or more of Mordechai Gutnick, Joseph Gutnick and Stera Gutnick are, or were at some time, variously directors, shareholders or company secretary of 71 Australian registered companies including five listed companies (other than Merlin). Merlin provided information which showed that Mordechai Gutnick, Joseph Gutnick and Stera Gutnick were directors of a further 11 foreign companies, and in 5 of these companies more than one of them was a director.
49. Mordechai Gutnick replaced Joseph Gutnick on many boards on which Joseph Gutnick was a director on 7 July 2016 (shortly before the date of his bankruptcy). In over 50 of the Australian registered companies in which Joseph Gutnick was a director, Mordechai Gutnick was appointed director on or about 22 December 2015<sup>15</sup> or 7 July 2016.<sup>16</sup> Joseph Gutnick resigned from all of these boards on or about 7 July 2016.
50. Mordechai Gutnick has been a director and Chairman of Merlin since 7 July 2016. His appointment coincided with the resignation of Joseph Gutnick as Executive Chairman, Managing Director and Chief Executive Officer of Merlin.

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<sup>13</sup> In *Tinkerbell Enterprises Pty Limited as Trustee for The Leanne Catelan Trust v Takeovers Panel* [2012] FCA 1272, at [54] Collier J said: "That the Panel was created to deal with takeover disputes in a relatively informal and expeditious manner is clear from its enabling legislation..."

<sup>14</sup> See, for example, *Bentley Capital Limited 01R* [2011] ATP 13 at [45]-[56] and *Avalon Minerals Limited* [2013] ATP 11, [63]-[64]

<sup>15</sup> The day after the Victorian Supreme Court upheld a Singaporean arbitration ruling that required Joseph Gutnick and Legend to pay more than \$55 million to the Indian Farmers Fertiliser Co-Op

<sup>16</sup> The day before Joseph Gutnick declared himself bankrupt

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51. In addition to Merlin, Mordechai Gutnick has served as a director on the boards of several listed companies of which Joseph Gutnick was a director and/or executive officer.<sup>17</sup>
52. Joseph Gutnick is the Chairman of Legend International Holdings, Inc., a Delaware company (“**Legend**”) and had previously been its Chief Executive Officer. Legend’s common stock is quoted via the Over the Counter Bulletin Board in the United States. Legend acquired a controlling interest in Merlin in August 2009 and disposed of its shares in Merlin during 2013.<sup>18</sup> On 8 May 2016, Legend filed for Chapter 11 bankruptcy protection in the United States.<sup>19</sup> Mordechai Gutnick is joint Chief Executive Officer of Legend. He had also been a director of Legend from 24 November 2015 to 23 March 2016. As at 21 March 2014, Joseph and Stera Gutnick disclosed beneficial ownership in 17.10% of the issued and outstanding shares of Legend.<sup>20</sup>
53. Top End Minerals Limited is an ASX listed company (ASX code: TND). Its current directors are Peter Lee, David Tyrwhitt and Mordechai Gutnick. Mordechai Gutnick was appointed on 2 December 2015 and Joseph Gutnick resigned as a director on 7 July 2016. Joseph Gutnick was the Executive Chairman, Chief Executive Officer and Managing Director of Top End. As at 28 September 2016, Mazil held 37.23% of Top End’s issued capital.<sup>21</sup>
54. Quantum Resources Limited is an ASX listed company (ASX code: QUR). Joseph Gutnick was the Executive Chairman and Managing Director of Quantum until 28 April 2015. Mordechai Gutnick became a director of Quantum on 29 September 2014 and resigned as a director on 3 December 2015. He became Chairman upon Joseph Gutnick’s resignation. Peter Lee and David Tywhitt were also directors of the company prior to resigning around the time of Joseph Gutnick’s resignation.
55. The common shareholdings and directorships described above suggest a personal and professional relationship which is very close, even for father and son.

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<sup>17</sup> In addition to the examples at paragraphs 52-54, they have historical common involvement in other listed companies including Hawthorn Resources Limited (ASX code: HAW) in which Joseph Gutnick was Chairman, Managing Director and Chief Executive Officer until 22 November 2007 when the company announced a scheme of arrangement with another company and Mordechai Gutnick served as a director of the company from 9 May 2003 until 22 November 2007, the same day Joseph Gutnick resigned; Astro Resources NL (ASX code: ARO) in which Mordechai Gutnick was a director from 9 May 2003 to 29 November 2007 and Joseph Gutnick was Chairman and Managing Director from the company’s inception to 29 November 2007 and Regis Resources Limited (ASX code: RRL) in which Mordechai Gutnick was a director from 9 May 2003 to 18 August 2004 and Joseph Gutnick was Chairman, Managing Director and Chief Executive Officer from the company’s inception to 26 August 2004. Source: Morningstar

<sup>18</sup> Legend Form 10-K dated 26 March 2014, Item 1

<sup>19</sup> Legend Form 8-K dated 8 May 2016

<sup>20</sup> Legend Form 10-K dated 26 March 2014, Item 12. The shares of common stock beneficially owned by Joseph and Stera Gutnick include stock options and shares of common stock owned by a charitable organisation in which Joseph and Stera Gutnick disclaimed any beneficial interest.

<sup>21</sup> Top End’s 2016 Annual Report

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#### *Common dealings*

56. The close relationship between Mordechai Gutnick and his father is further supported by material provided to the Panel regarding their dealings in Merlin. Joseph and Mordechai Gutnick travelled together to New York to meet with David Slager in May or June 2016. Following Joseph Gutnick's resignation as director, Mordechai Gutnick kept his father up to date on developments in Merlin, including informing him of Regals' request for conversion of a portion of the Regals Notes, discussing with him the s249D Requisition and informing him of the later withdrawal of the s249D Requisition. Merlin also disclosed conversations among Peter Lee (Merlin's company secretary), Mordechai Gutnick and Joseph Gutnick, after despatch of the notice of meeting for the 6 September Meeting, regarding the votes being received by the shareholder registry. Joseph Gutnick remained employed as a consultant to Merlin and was consulted in respect of how much funds should be sought by way of additional convertible notes.

#### *Associated companies*

57. Mordechai Gutnick is the sole shareholder and sole director of AHA and Morzev which hold 3,076,923 and 76,923 shares in Merlin, respectively (or 0.47% and 0.01% of the current issued capital, respectively).<sup>22</sup> He is also the sole shareholder and sole director of, and controls, NRMZ.
58. Mazil is owned 50:50 by Joseph and Stera Gutnick. Stera Gutnick is the sole director of Mazil following Joseph Gutnick's resignation as director on 8 July 2016. Mazil is the trustee of the Mazil Superannuation Fund which is a regulated fund. It holds 32,307,692 Merlin shares or 4.97% of Merlin's current issued capital. Other than shares in Merlin and Top End Minerals Limited, Joseph Gutnick and Stera Gutnick submitted that Mazil holds no assets and has no day to day activities. They submitted that all decisions of Mazil are made by Joseph Gutnick and that the decision to vote the Merlin shares held by Mazil at the 6 September Meeting was made by Joseph Gutnick as a beneficiary of the Mazil Superannuation Fund. Merlin submitted that Joseph Gutnick's share in Mazil is vested in his trustees in bankruptcy but his interest as a beneficiary of the Mazil Superannuation Fund was unaffected by his bankruptcy.<sup>23</sup>
59. Mordechai Gutnick previously owned one share in Mazil which he transferred to Stera Gutnick on 11 August 2016. Merlin submitted that the transfer was made because Mordechai Gutnick had ceased to be a director of Mazil on 24 June 2014 and is not a beneficiary of the Mazil Superannuation Fund and therefore it served no purpose for him to hold any shares in Mazil.
60. GCG is a Marshall Islands company in which Joseph and Stera Gutnick are joint holders of 25,000 shares and Soh Han Chuen holds 25,000 shares. The current directors of GCG are Joseph Gutnick, Stera Gutnick and Soh Han Chuen. Mordechai Gutnick submitted that he has never had any involvement in the activities of GCG. GCG is a passive investment company which holds no assets

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<sup>22</sup> All percentages referencing the current issued capital of Merlin are based on 649,680,949 shares outstanding as disclosed in Merlin's Appendix 3B dated 22 November 2016

<sup>23</sup> Referring to s116(2)(d)(iii) of the *Bankruptcy Act 1966* (Cth)

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other than 14,615,385 shares in Merlin or 2.25% of Merlin's current issued capital. Joseph Gutnick and Stera Gutnick submitted that all decisions of GCG are made by Joseph Gutnick or, if material, in consultation between Joseph Gutnick and Soh Han Chuen and the decision to vote the Merlin shares held by GCG at the 6 September Meeting was made by Joseph Gutnick as a director of GCG.

61. Chabad Properties is the trustee of a charitable trust, the Machom Chaim College Fund. Joseph Gutnick, Stera Gutnick and Mordechai Gutnick each own one third of the shares in Chabad Properties. Stera Gutnick and Mordechai Gutnick are the current directors of the company. Mordechai Gutnick was appointed as a director on 22 December 2015 and Joseph Gutnick ceased to be a director on 7 July 2016. Chabad Properties owns the Chabad Notes which were changed to convertible notes on 29 September 2016. Joseph Gutnick and Stera Gutnick submitted that the decision for Chabad Properties to invest in notes was made by Mordechai Gutnick in consultation with Joseph Gutnick.
62. TMG is the trustee of the Merlin Diamonds Employee Share Trust under the Merlin Diamonds Employee Share Trust Deed. It is the registered holder of 18,000,000 Merlin shares. Merlin submitted that, prior to his bankruptcy, Joseph Gutnick had a right to direct the trustee to vote the Merlin shares represented by his Share Units (as defined in the Trust Deed) which meant that he had a relevant interest in the 18,000,000 underlying Merlin shares. In a notice of change of interests of substantial holder in Merlin dated 15 January 2015, Joseph Gutnick included the issue of these 18,000,000 shares in his total holding.
63. Merlin submitted<sup>24</sup> that, upon his bankruptcy, Joseph Gutnick's Share Units vested in his trustees in bankruptcy and therefore he no longer had a relevant interest in the underlying shares.<sup>25</sup> Notwithstanding this submission, Merlin subsequently submitted that Joseph Gutnick instructed Peter Lee to ask TMG to vote the 18,000,000 shares in favour of all resolutions at the 6 September Meeting, which it did.
64. Merlin submitted that Stera Gutnick had no communications with any of Merlin, Joseph Gutnick, Mordechai Gutnick, Mazil, GCG, NRMZ or Chabad Properties in relation to the conversion of the Regals Notes, voting at the 6 September Meeting and the s249D Requisition. We infer from this and the submissions above regarding who made voting decisions on behalf of Mazil, GCG, TMG and Chabad Properties that:
  - (a) Joseph Gutnick had full control over the decisions of Mazil and (in the absence of any suggestion of consultation with Soh Han Chuen) GCG
  - (b) Joseph Gutnick had practical control of the voting at the 6 September Meeting of Merlin of the shares held by TMG and
  - (c) Mordechai Gutnick and/or Joseph Gutnick made all decisions for Chabad Properties with respect to the Chabad Notes.

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<sup>24</sup> In a submission that appeared to be made also on behalf of Joseph Gutnick

<sup>25</sup> Merlin submitted that Joseph Gutnick's failure to update his substantial holder notice was an oversight. As at the date of these reasons, Joseph Gutnick has not updated his substantial holder notice

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#### Conclusion

65. We consider that the material before the Panel justifies a finding that Mordechai Gutnick and Joseph Gutnick continued to work together, following Joseph's resignation as a director, to achieve the recapitalisation of Merlin through the issue of notes and options. Among other things, that involved Joseph Gutnick making the decision to vote shares held by Mazil and GCG, and requesting the voting of shares held by TMG, in favour of the resolutions at the 6 September Meeting.<sup>26</sup>
66. We also infer, on the basis of the above, together with their family relationship, structural links and common dealings, that Mordechai Gutnick and Joseph Gutnick had an agreement, arrangement or understanding for the purpose of controlling or influencing the conduct of Merlin's affairs, including with respect to securing approval of the resolutions put to the 6 September Meeting. In addition, they acted in concert in relation to Merlin's affairs.
67. Merlin submitted that there was a commercial imperative for Joseph Gutnick to vote in favour of the resolutions at the 6 September Meeting. In relation to Resolutions 1, 2 and 3, the resolutions authorised the conversion of expensive secured debt into equity (notwithstanding the dilution caused by the issue of new shares) and avoided Merlin being subject to financial penalties under the terms of the secured note deeds (see paragraph 12). Resolution 4 authorised the obtaining of further convertible debt necessary for ongoing operations. Merlin submitted that the concurrence of views by shareholders does not mean that there is a relevant agreement.<sup>27</sup> That may be so, but here we have more than an alignment of commercial views, we have a father and son working closely together in relation to the affairs of Merlin.
68. Merlin submitted that there were obvious commercial reasons for Joseph Gutnick to support the resolutions absent an agreement, arrangement or understanding with his son, and the evidence did not even rise to "*conflicting inferences of equal degrees of probability*".<sup>28</sup> While Merlin submitted that certain inferences were not open to us, it did not expressly take issue with, or provide evidence to contradict, most of our specific proposed findings (as opposed to the inferences drawn from them, or conclusions based on them). In our view, based on the totality of the material before us, Mordechai and Joseph had an understanding for the common purpose of controlling or influencing the conduct of, or were acting in concert in respect of, Merlin's affairs and the alignment of commercial interests does not negate the basis for our finding of association.
69. Merlin also submitted that we excluded from our consideration submissions that Mordechai Gutnick and Joseph Gutnick had no conversations in relation to the conversion of the Regals Notes prior to Merlin receiving the notice of conversion

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<sup>26</sup> See paragraphs 22 and 63

<sup>27</sup> Quoting *Winepros Limited* [2002] ATP 18 at [33]

<sup>28</sup> Quoting *CMI Limited* [2011] ATP 4 at [42], in turn quoting from *ASIC v Fortescue Metals Group Ltd* [2011] FCAFC 19 at [78]: "... we had in mind that, while we must be satisfied by logical and probative material, the potential seriousness of a finding of association suggests that "the circumstances appearing from the evidence [must be established to] give rise to a reasonable and definite inference and not merely to conflicting inferences of equal degrees of probability."

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from Regals. Merlin submitted that this was “*fundamentally inconsistent*” with our conclusion that there was an agreement, arrangement or understanding between Mordechai Gutnick and Joseph Gutnick for the purpose of controlling or influencing the conduct of Merlin’s affairs, including with respect to securing approval of the resolutions put to the 6 September Meeting. We have carefully considered Merlin’s submissions, but do not believe they are necessarily inconsistent with our findings. In particular, given the unusually close relationship between Mordechai Gutnick and Joseph Gutnick, express conversations may not have been necessary for them to develop a common understanding as to how to proceed or to otherwise act in concert.

#### **Mordechai Gutnick and Regals**

##### *Structural links*

70. Mordechai and Regals are connected through Merlin and Legend.
71. As noted above, Mordechai Gutnick became a director and the Chairman of Merlin on 7 July 2016 following his father’s resignation.
72. Prior to the conversion of a portion of the Regals Notes, Regals was a substantial holder of Merlin with 25,162,755 shares which, immediately prior to the issue of shares on 1 September 2016, equalled 5.58% of Merlin.
73. Following the conversion of a portion of the Regals Notes, Regals had a relevant interest in 75,162,755 shares in Merlin (or 11.57% of the current issued capital).
74. Regals submitted that it had periodic discussions with the management of Merlin for investor relations purposes including updates regarding the business prospects and capital needs of Merlin.
75. Regals also holds shares of common stock in Legend which as at 21 March 2014 represented 25.98% of the issued and outstanding capital. As noted at paragraph 52, Mordechai Gutnick is joint Chief Executive Officer of Legend and has also been a director of Legend.
76. We consider that while these structural links fall well short of establishing an association between Mordechai Gutnick and Regals, they are consistent with our inferences discussed below.

##### *Collaborative conduct*

#### The loan from David Slager to Mordechai Gutnick

77. We asked Regals (and any of its directors, officers or advisers) whether it had any personal or professional connections, common investments, common directorships or relationships (past and present) with, among others, Mordechai and Joseph Gutnick. Regals submitted that it had none, other than its investment in Merlin and Legend.
78. Following being served by ASIC with a notice under section 30 of the ASIC Act, Mordechai Gutnick disclosed a loan agreement between Mordechai Gutnick and David Slager. In an exchange of emails on 4 July 2016, David Slager and Mordechai Gutnick agreed that: “*David Slager is lending Mordechai Gutnick \$300k usd interest free to buy shares in Merlin Diamonds . Mordechai Gutnick will pay David*

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*Slager back as the first use of the sale of those Merlin shares or from the first dividends or distributions from the company.”* In response to ASIC’s notice, Mordechai Gutnick stated that “[T]he loan funds of USD\$300,000 were used to purchase convertible notes in Merlin. No shares were, in fact, purchased and the convertible notes were subsequently on sold. The loan remains outstanding and is unsecured.” ASIC submitted that a payment of USD\$300,000 was transferred from David Slager to an account in the name of Mordechai Gutnick on 7 July 2016. On 12 July 2016, \$392,054.36 was deposited into an account in the name of NRMZ and the same amount was withdrawn from the account on the same day.

79. We consider that the loan provided by David Slager to Mordechai Gutnick evidences a level of understanding and cooperation between David Slager, on the one hand, and Mordechai Gutnick, on the other, in relation to the affairs of Merlin and a willingness on David Slager’s part to support the acquisition of Merlin shares by Mordechai.
80. While the terms of the loan appear to be uncommercial, we accept Merlin’s submission that Mordechai Gutnick and David Slager are both members of the orthodox Jewish community and in that community religious law forbids interest being charged on personal loans made between members of the community. We note, however, that the terms of the agreement did not appear to provide any benefit to David Slager.

#### Conversion of Regals Notes and issue and voting of shares

81. Regals submitted that in May or June 2016 Regals was visited by Joseph and Mordechai Gutnick to discuss the possibility of a capital raising. In the weeks following that meeting, Regals submitted that it negotiated and agreed the terms of the notes and options with Mordechai Gutnick.
82. Regals submitted that David Slager spoke with Mordechai Gutnick on several occasions in July and August 2016 regarding among other things the status of the capital raising process, the appetite of other investors, the desire of Regals to convert some of the Regals Notes into equity and mechanisms for exercising its voting rights. It submitted that all communications were handled over the phone and were not documented which was consistent with Regals’ normal business practice. It did, however, provide instructions to Merlin via email to convert a portion of the Regals Notes into shares. It also instructed Merlin to vote all of Regals’ shares in favour of all resolutions at the 6 September Meeting.
83. In relation to the conversion of some of the Regals Notes and the 6 September Meeting, Merlin submitted that material communications were between Mordechai Gutnick and David Slager. It submitted that those communications consisted of two telephone conversations, text messages in respect of those conversations and two “*facultative*” email chains between Peter Lee and Yuriy Musayev of Regals. Merlin submitted that during the first telephone conversation Mordechai Gutnick asked David Slager to support the resolutions being put to shareholders at the 6 September Meeting and, subsequently, Regals voted its existing 25,162,755 shares in favour of the resolutions. Merlin submitted that in the second telephone conversation on 31 August 2016, David Slager told Mordechai Gutnick that he

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wanted to convert Notes into shares for the purpose of further supporting the resolutions and this resulted in a further 50,000,000 shares being issued to Regals.

84. We asked Merlin, Mordechai Gutnick and Regals to provide further details regarding these two telephone calls. Merlin submitted that in the first call Mordechai Gutnick told David Slager of Merlin's need to recommence production at the Merlin mine by October, that further capital was required and that such capital could only be raised from new noteholders (i.e., the subject of Resolution 4). Merlin submitted that David Slager told Mordechai Gutnick that he supported the efforts to recapitalise the company and that he would be voting in favour. In relation to the second call, Merlin submitted that David Slager raised the possibility of converting notes into shares prior to the meeting and that if he could do so, he intended to convert some notes and vote those shares in support of the recapitalisation. Regals made a similar submission to Merlin.
85. In a text message from Mordechai Gutnick to David Slager on 28 August 2016, Mordechai Gutnick asked for Regals' vote on the resolutions at the 6 September Meeting stating that *"it's a necessity that we get your votes and the convertible note passes"*. In response, David Slager stated *"Sure. I'll push it along"* and following a telephone call between Mordechai Gutnick and David Slager, Regals voted its shares.
86. Merlin submitted that:
- (a) seeking of a proxy in support of resolutions does not give rise to a relevant agreement and to suggest otherwise would be contrary to ss16(1)(d) and 609(5) which effectively provide that a person may vote as a proxy on behalf of another person at a shareholders meeting without becoming an associate of the other or obtaining a relevant interest in the other's shares and therefore if one can hold and vote the proxy lawfully, then one can also seek and solicit it lawfully and
  - (b) Merlin submitted (leaving aside ss16(1)(d) and 609(5)) the mere soliciting of a proxy cannot by itself give rise to a relevant agreement. It submitted that this is because (i) a concurrence of views about the merits of a particular resolution is not sufficient to give rise to a relevant agreement<sup>29</sup> and (ii) at least one party must *"assume an obligation"* or give an *"assurance"* or *"undertaking"* that it will act in a certain way and a mere expectation that as a matter of fact a party will act in a certain way is not enough<sup>30</sup>.
87. ASIC submitted that, given that Regals was unable to vote on Resolution 1, it appeared the Notes for which Regals' vote was a *"necessity"*<sup>31</sup> related to Resolutions 2 and 3. Merlin submitted that the reference to *"necessity"* was *"obviously a reference to Resolution 4 only"* because it was the resolution primarily directed to recapitalisation. We accept that Resolution 2 was by then moot given

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<sup>29</sup> Referring to *Winepros Limited* [2002] ATP 18 at [33]. See also paragraph 67 above

<sup>30</sup> Referring to *ACCC v CC (NSW) Pty Ltd* [1999] FCA 954; (1999) 92 FCR 375 at [141]

<sup>31</sup> Referring to Mordechai's initial text message to David Slager on 28 August 2016 (see paragraph 85 above)



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that NRMZ's notes had already been transferred to Green. However we see no reason why the reference to "*necessity*" could not also have related to Resolution 3.

88. We infer that the communications between Mordechai Gutnick and David Slager went beyond soliciting a proxy or a concurrence of views about the merits of the resolutions or, as Merlin further submitted, "*seeking support*". We infer from the exchange of texts and emails discussed further below that:
- (a) the proposal to convert Regals Notes was instigated by Mordechai Gutnick at some time after the exchange noted at paragraph 85 and after Merlin had received the s249D Requisition on 29 August 2016<sup>32</sup> and
  - (b) Mordechai Gutnick and David Slager had an understanding that Mordechai would arrange for the new shares to be issued in time to be voted (which required prompt action given the record date of 2 September 2016) and that the new shares would be voted in favour of the resolutions.
89. In a text message from Mordechai Gutnick to David Slager on 30 August 2016, Mordechai Gutnick indicated that he needed to talk to David Slager "*ASAP*". Later that day, after missing a call from David Slager, Mordechai Gutnick texted "*Hi David are you available thanks*". Within a few minutes David Slager responded and provided Mordechai Gutnick with a telephone number on which to contact him.
90. On 31 August 2016 at 5.39am (Melbourne time), Mordechai Gutnick again contacted David Slager asking "*can you talk in 10 min*" and David Slager replied at 6.47am stating "*Hi Mordi. I'm out for dinner. Will call you in an hour or two*". David Slager resides in New York but was on vacation in London during this time. Approximately three hours later at 9.42am, Mordechai Gutnick texted David Slager saying "*Thanks again for your support*".
91. As noted above David Slager emailed Peter Lee, copying Mordechai Gutnick and blind copying Yuriy Musayev, instructing him to "*convert A\$ 750,000 worth of our convertible notes at A 1.5 cents per share into 50 million new shares in Merlin Diamonds*" and to "*vote all these shares in favour of all resolutions at Merlin meeting Sept 6*". This email would have been received in Melbourne at 9.38am on 31 August 2016.<sup>33</sup>
92. As discussed above, Merlin submitted that on 31 August 2016, David Slager told Mordechai Gutnick that he wanted to convert Notes into shares for the purpose of further supporting the resolutions. In a later submission, Merlin submitted that the discussion took place "*around 9.00 AM on 1 September 2016*". The reference to 1 September 2016 may be an error, which was meant to refer to 31 August 2016 (the date given in Merlin's earlier submission<sup>34</sup>). Even if not, our view is that Merlin's earlier submission should be preferred, given that:
- (a) Merlin submitted that in the conversation "*Mr Slager then asked about the possibility of converting notes into shares prior to the meeting. Mordechai Gutnick told Mr Slager, in words to the effect of, that he understood that the company had*

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<sup>32</sup> See paragraph 17

<sup>33</sup> The email was dated Tuesday, 30 August 2016 at 7.38pm

<sup>34</sup> See paragraph 83

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*capacity to allow some conversion*", which suggests that the conversation occurred prior to the conversion on 31 August 2016 and

- (b) on 31 August 2016, after 9.43am (Melbourne time) David Slager asked Mordechai Gutnick to let him know "*when the conversion is confirmed*" (which appears to assume that conversion had by then been requested) and Yuriy Musayev, on behalf of Regals, emailed Peter Lee to discuss David Slager's instruction "*asap*" which would have been received in Melbourne at 12.09am on 1 September 2016.<sup>35</sup>

93. We infer that the conversation between Mordechai Gutnick and David Slager occurred at around 9am on 31 August 2016, which would be consistent with the timing and tenor of the text messages and the instructions from David Slager in relation to the conversion of notes being received at around 9.38am on 31 August 2016 (Melbourne time).
94. Merlin and Regals both submitted that David Slager proposed to Mordechai Gutnick converting a portion of the Regals Notes prior to the 6 September Meeting and that the conversion decision was made solely by David Slager. However, their submissions were expressed in terms that would not necessarily be inconsistent with the proposal to convert the notes having been instigated by Mordechai Gutnick rather than David Slager.
95. After the telephone call and instruction had been sent to Peter Lee, David Slager texts Mordechai Gutnick asking "*[d]oesn't my investment have to be confirmed by vote before the conversion can happen*" to which Mordechai Gutnick replies "*[n]o the company has capacity to convert the amount we are converting without shareholder approval*". It seems an odd question for David Slager to ask following his call with Mordechai Gutnick if, as Merlin submitted, on that call David Slager had asked about the possibility of converting notes before the 6 September Meeting and Mordechai Gutnick replied "*in words to the effect of, that he understood that the company had capacity to allow some conversion*".
96. In an email from Yuriy Musayev to Peter Lee on 1 September 2016 Yuriy expresses a similar reservation to that of David Slager when he states "*I don't even understand how we can do this now without approval*".
97. David Slager's text message and Yuriy Musayev's email highlight the curiosity that these notes would be converted into shares immediately prior to a meeting specifically called to approve the conversion of notes (including these notes) to convertible notes (notwithstanding Merlin's Listing Rule 7.1 capacity). In our view, this correspondence further supports the inference that the proposal to convert Regals Notes was instigated by Mordechai Gutnick.

#### *Actions which are uncommercial*

98. It appears to us that Regals entered into the secured note deeds following an arm's length negotiation with Merlin. Merlin, through Mordechai and Joseph Gutnick, marketed the notes to David Slager at a meeting in New York and following that meeting the terms of the notes were agreed. Regals submitted that the terms of the

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<sup>35</sup> The email was dated Wednesday, 31 August 2016 at 10.09am

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notes and options reflected concerns that it expressed to Merlin, namely, that *“Merlin had almost no spare capital, had already failed in prior efforts to operate its main asset and that the macro-economic environment for small mining company recapitalizations was very depressed”*.

99. Regals Notes were in the same form as secured note deeds entered into by Merlin with other investors in December 2015 except for changes to the number of options attaching to notes, the conversion price, the period by which shareholder approval was required and the interest payment date.
100. The terms of the secured note deeds entered by Regals are favourable to the noteholder in a number of respects including:
  - (a) the Notes are secured by a charge over the assets of Merlin
  - (b) the Notes have a term of 3 years
  - (c) the Notes accrue interest at 10% per annum
  - (d) if convertible, the Notes convert at a price per share of 1.5 cents per share or the 5 day VWAP up to the day prior to conversion, whichever is lower and
  - (e) if the Notes are not convertible within 90 days of issue, the noteholder is entitled to a higher interest rate and a right to accelerated redemption at a penalty redemption price.
101. Regals converted almost half of its Regals Notes into shares just over 2 months after they were issued. Regals submitted that it converted a portion of its Notes *“in order to have a greater voting power and influence over Merlin and help with the company’s recapitalization efforts in order to keep it afloat”*. We infer that Regals’ decision to convert the Regals Notes was inconsistent with its commercial interest given the favourable terms of the Regals Notes and that Regals subordinated its interest in connection with an understanding with Mordechai Gutnick regarding voting at the 6 September Meeting.
102. Merlin submitted that it can be inferred that Regals voted in favour of Resolutions 2 and 3 because it was in the interests of shareholders to vote in favour of the resolutions to avoid the financial penalties that would accrue to Merlin under the secured note deeds if the resolutions fail and to allow expensive secured debt to be converted into equity. This reason for voting in favour of the resolutions was not expressed by Regals. In our view, this does not adequately explain why Regals wished to convert its notes against its commercial interest, which supports our inference that there is an understanding between Mordechai Gutnick and Regals, or they are acting in concert, as to the affairs of Merlin.

#### *Conclusion*

103. In light of the above, including the fact and the circumstances surrounding the loan from David Slager to Mordechai Gutnick, the voting of Regals’ shares in favour of the Resolutions 2, 3 and 4, the subsequent conversion of some of the Regals Notes against its commercial interest and the voting of the new shares, we infer that Mordechai Gutnick and Regals had an understanding that Regals would convert some of the Regals Notes and Mordechai would arrange for the new shares to be issued in time to be voted and Regals would vote the new shares in favour of

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Resolutions 2, 3 and 4. Accordingly, in our view Mordechai Gutnick and Regals had an agreement, arrangement or understanding for the purpose of controlling or influencing the composition of Merlin's board or the conduct of Merlin's affairs and, in addition, they were acting in concert in relation to Merlin's affairs.

104. Regals denied that it had entered into any agreement with Mordechai Gutnick to the extent found by us but did not expressly address or take issue with our findings regarding the content or timing of communications between Mordechai Gutnick and David Slager (as opposed to the inferences drawn from those findings).

#### **Mordechai Gutnick and Green**

105. On 5 September 2006, Max Green lent Mordechai Gutnick the sum of \$275,000 payable without interest on demand ("**2006 Loan**") and secured by a cheque for the full amount (endorsed by Joseph and Stera Gutnick, each as surety and co-principal debtor).
106. Merlin submitted that during early to mid-2016 Max Green demanded repayment of the 2006 Loan. In full settlement of the 2006 Loan, Max Green and Mordechai Gutnick agreed by deed dated 11 August 2016 that Mordechai Gutnick would transfer 392,054 convertible notes and 26,136,933 options in Merlin to Max Green for a purchase price of \$500,000, with Max Green agreeing pay the balance of the purchase price on 1 April 2017, free of interest.
107. On 11 August 2016, NRMZ transferred the NRMZ Notes to Green pursuant to a convertible note transfer form.
108. On 1 September 2016, according to Merlin's Note Register, the NRMZ Notes transferred to Green were converted into convertible notes.
109. On 2 September 2016, Merlin issued 26,136,933 shares to Green on conversion of all of the NRMZ Notes. Green voted these shares in favour of the resolutions at the 6 September Meeting.
110. In May 2005, Max Green acquired a property in Western Australia on behalf of Chabad Properties. Merlin submitted that:
- At the time Mr Green and Mordechai Gutnick were both residents of Perth and were both members of the same Chabad congregation. Mr Green was well known in the Perth Chabad community as a person skilled in negotiating and purchasing properties on behalf of members of the community.*
111. In our view, there is insufficient material to support an inference that Green had reached any agreement, arrangement or understanding with Mordechai Gutnick regarding the conversion of the NRMZ Notes and voting of the shares.
112. Nevertheless, the fact that both the Regals Notes and the NRMZ Notes (held by Green) were converted into shares on or immediately before the record date for the 6 September Meeting provides some further support for the inference above at paragraph 103 that Mordechai Gutnick was seeking to arrange for the new shares to be issued in time to be voted.

**Conclusions in relation to association**

113. Considering the whole of the material, and drawing appropriate inferences, we infer that:
- (a) Mordechai Gutnick and Joseph Gutnick had an agreement, arrangement or understanding and, in addition, were acting in concert in relation to the affairs of Merlin, including with respect to securing approval of the resolutions put to the 6 September Meeting. This made them associates in relation to Merlin under s12(2)(b) and (c).
  - (b) Mordechai Gutnick and Regals had an agreement, arrangement or understanding and, in addition, were acting in concert in relation to the affairs of Merlin to procure that Regals would convert some of the Regals Notes and Mordechai would arrange for the new shares to be issued in time to be voted and Regals would vote the new shares in favour of Resolutions 2, 3 and 4. This made them associates in relation to Merlin under s12(2)(b) and (c).
114. We came to this view based on the overall weight of material.

**Conclusions in relation to contravention of s606**

115. Immediately prior to 1 September 2016 and the issue of 50,000,000 Merlin shares to Regals:
- (a) Regals had a relevant interest in approximately 5.58% of issued Merlin shares
  - (b) Joseph Gutnick had a relevant interest in approximately 14.39% of issued Merlin shares, as a result of his power to control the voting of Merlin shares held by Mazil, GCG and TMG and
  - (c) Mordechai Gutnick had a relevant interest in approximately 0.7% of issued Merlin shares, as a result of his power to control the voting of Merlin shares held by AHA and Morzev.
116. Immediately after the issue of the 50,000,000 Merlin shares to Regals, based on our findings in relation to association, Mordechai Gutnick had voting power in Merlin of approximately 28.22%.
117. Accordingly, we find that as a result of the acquisition of a relevant interest in 50,000,000 Merlin shares by Regals on 1 September 2016, the voting power of Mordechai Gutnick in Merlin increased from a starting point that is above 20% and below 90%. In our view, none of the exceptions in s611 applied and therefore, s606(1) was contravened.
118. Regals submitted that it did not know that Mordechai Gutnick had any relevant interest in Merlin shares held by Mazil, GCG or TMG. This neither contradicts our finding of an association between Mordechai Gutnick and Regals nor does it change our conclusion that s606(1) was contravened. It is not for us to decide whether it would support a defence to a prosecution under s606(5). Even if it would, that does not preclude us from making a declaration.<sup>36</sup>

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<sup>36</sup> See *The President's Club Limited 02* [2016] ATP 1 at [177]

**Conclusions in relation to contravention of s671B**

119. Based on our view in relation to association, we find that s671B was contravened as follows:
- (a) no substantial holder notice has been lodged disclosing Mordechai Gutnick's voting power in Merlin and association with Joseph Gutnick and Regals in relation to Merlin and
  - (b) the notice of change of interests of substantial holder lodged by Regals on 6 September 2016 is deficient because, among other things, it does not disclose Regals' association with Mordechai Gutnick.

**6 September Meeting**

*Disclosure regarding ability to creep*

120. We consider the explanatory memorandum for the 6 September Meeting was misleading. Shareholders were not informed that the holders of the notes and options would have the capacity to convert their convertible notes and exercise their options to increase their voting power in Merlin above 20% in reliance on the 3% creep exception.
121. As noted above at paragraph 15, the notes and options would have given Regals, NRMZ and Chabad Properties the ability to require the issue of shares over time (relying on the 3% creep exception) giving them collectively more than 50% of Merlin shares (assuming no other shares were issued). The explanatory memorandum for the 6 September Meeting did not draw shareholders attention to the very significant control implications of the notes and options. Rather, it wrongly indicated that the secured note deeds would be subject to the 19.9% Conversion Requirement. If that requirement had applied it may have prevented reliance on the 3% creep exception and prevented a holder of the notes and options from obtaining control by means of their conversion or exercise. We consider that Merlin shareholders were misled and given false comfort on material potential control implications of the notes and options.

*Voting exclusions and voting on the resolutions*

122. At the 6 September Meeting, Resolutions 1 and 4 were subject to voting exclusion statements to the effect that Merlin would disregard any votes cast by any person who may participate in the issue, any person who may obtain a benefit and any associate of that person. Regals' votes were excluded on Resolution 1. No votes were excluded on Resolution 4.
123. Resolutions 2 and 3 were subject to voting exclusion statements to the effect that Merlin would disregard any votes cast by any person who is to receive the securities and any associate of that person. The votes of two shareholders were excluded from these resolutions – AHA holding 3,076,923 shares and Harapid Pty Ltd holding 450,000 shares.
124. Merlin submitted that, in respect of Resolutions 2 and 3, Mordechai Gutnick determined not to vote any shares in Merlin held by any company which he or his wife controlled, whether or not such company was an associate of NRMZ or

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Chabad Properties, as applicable. Mordechai Gutnick's wife is the sole shareholder and sole director of Harapid Pty Ltd and accordingly, was excluded from voting.

125. Merlin submitted that the Merlin shares held by Morzev were voted in error contrary to Mordechai Gutnick's stated intent.
126. Regals, Mazil, GCG and TMG each voted in favour of all the Resolutions. Neither Resolution 2 nor 3 would have passed if:
  - (a) the 50,000,000 Merlin shares issued to Regals and all the Merlin shares held by Mazil, GCG and Morzev had not been voted in favour<sup>37</sup> or
  - (b) all the Merlin shares held by Regals had not been voted in favour<sup>38</sup> or
  - (c) all the Merlin shares held by Mazil, GCG, Morzev and TMG had not been voted in favour.<sup>39</sup>
127. Merlin submitted, and we agree, that Resolution 2 was made redundant upon the transfer of the NRMZ Notes to Green prior to the meeting.
128. It is not a matter for us to determine whether, in these circumstances, the requirements of the Listing Rules have been satisfied. We consider that, in the light of our findings on association, the control implications of the notes and options and the disclosure defects noted above, for Resolution 3 to have been passed only because of votes cast by, or as a result of the decision or request of, any of Regals, Mordechai Gutnick or Joseph Gutnick gives rise to unacceptable circumstances.

#### Extending time for application

129. Section 657C(3) provides that a Panel application can only be made within two months after the circumstances have occurred, or a longer period determined by the Panel. We invited submissions on whether the application was made out of time and, if so, whether we should grant an extension of time under s657C(3)(b) on 7 November 2016 and again, after making preliminary findings, on 23 November 2016.
130. ASIC submitted that it was unlikely that the applicant would have been aware of an association involving Regals until 7 September 2016 when Regals lodged a notice of change of interests disclosing the issue of 50,000,000 Merlin shares upon conversion of notes. In these circumstances, ASIC submitted that unacceptable circumstances should not go without a remedy merely because they were substantially unknown or unproven for more than two months. ASIC also submitted that the application made credible allegations of clear and serious unacceptable circumstances and the effect of the circumstances is ongoing.

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<sup>37</sup> In relation to Resolution 3, votes cast for would have been 136,057,301 or 44.05% of total votes, assuming open proxies were cast in favour

<sup>38</sup> In relation to Resolution 3, votes cast for would have been 157,894,546 or 47.74% of total votes, assuming open proxies were cast in favour

<sup>39</sup> In relation to Resolution 3, votes cast for would have been 168,057,301 or 49.30% of total votes, assuming open proxies were cast in favour

## Takeovers Panel

### Reasons – Merlin Diamonds Limited [2016] ATP 18

131. We recognise that the discretion to extend time should not be lightly exercised. However, we think there is a clear basis for extending time in this matter given:

- (a) the application made credible allegations of clear and serious unacceptable circumstances with ongoing effects and
- (b) essential matters supporting the application remained hidden during the 2 month period preceding the application<sup>40</sup> and in some cases until after the application had been made.<sup>41</sup>

132. Having weighed the relevant factors including the public interest,<sup>42</sup> we extend the time under s657C(3)(b) for the making of the application to the date it was made.

## DECISION

### Declaration

133. It appears to us that the circumstances are unacceptable:

- (a) having regard to the effect that we are satisfied they have had, are having, will have or are likely to have on:
  - (i) the control, or potential control, of Merlin or
  - (ii) the acquisition, or proposed acquisition, by a person of a substantial interest in Merlin
- (b) in the alternative, having regard to the purposes of Chapter 6 set out in s602 and
- (c) in the further alternative, because they constituted, constitute, will constitute or are likely to constitute a contravention of a provision of Chapter 6 or of Chapter 6C of the Act.

134. Accordingly, we made the declaration set out in Annexure C and consider that it is not against the public interest to do so. We had regard to the matters in s657A(3).

135. Merlin submitted that we should not make a declaration of unacceptable circumstances since, by the time we were minded to do so, the total combined holdings of Mazil, GCG, TMG, AHA, Morzev and Regals had been diluted below 20% as a result of further share issues (including the conversion of convertible notes issued following the passage of Resolution 4). In our view, the subsequent dilution of Mordechai Gutnick's voting power does not provide a sufficient reason for us to decline to make a declaration.

136. We consider that:

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<sup>40</sup> For example, some of the circumstances the application relates to would not have been apparent to the Applicant until 7 September 2016 when Regals lodged a substantial holder notice disclosing a change of interests on 1 September 2016 due to the conversion of notes

<sup>41</sup> For example, the loan agreement between David Slager and Mordechai Gutnick described at paragraph 78, the communications between David Slager and Mordechai Gutnick regarding the conversion of notes and issue and voting of shares described at paragraphs 89 - 91 and the instruction given by Joseph Gutnick to Merlin's company secretary regarding the voting of shares held by TMG described at paragraph 63

<sup>42</sup> See *The President's Club Limited 02* [2016] ATP 1 at [106]-[160] and *Palmer Leisure Coolum Pty Ltd v Takeovers Panel* [2015] FCA 1498



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### Reasons – Merlin Diamonds Limited [2016] ATP 18

- (a) the acquisition of control over voting shares in Merlin has not taken place in an efficient, competitive and informed market
- (b) the holders of shares in Merlin do not know the identity of persons who have acquired a substantial interest in Merlin and
- (c) the holders of shares in Merlin have not been given enough information to enable them to assess the merits of a proposal which would result in persons acquiring a substantial interest in Merlin.

#### Orders

137. Following the declaration, we made the final orders set out in Annexure D. Under s657D the Panel is empowered to make 'any order'<sup>43</sup> if 4 requirements are satisfied:
- (a) it has made a declaration under s657A. This was done on 29 November 2016.
  - (b) it must not make an order if it is satisfied that the order would unfairly prejudice any person. For the reasons below, we are satisfied that our orders do not unfairly prejudice any person.
  - (c) it gives each person to whom the proposed order would be directed, each of the parties and ASIC an opportunity to make submissions. This was done on 1 December 2016.
  - (d) it considers the orders appropriate to achieve the outcomes in one or more of the paragraphs in s657D(2), which relevantly include protecting the rights and interests of persons affected by the unacceptable circumstances, or any other rights or interests of those persons. We are satisfied that the rights or interests of Merlin shareholders have been, are being or are likely to be affected by the circumstances identified in the declaration. For the reasons below, we consider that our orders are appropriate to protect those rights or interests.
138. We have carefully considered all of the extensive submissions we received on possible orders. Our reasons below primarily address the orders we have ultimately decided to make, rather than the many alternatives we considered but rejected.
139. We consider that the interests of Merlin shareholders have been (or are being or are likely to be) affected by the unacceptable circumstances in the following ways:
- (a) The terms of the Convertible Notes were such that they could have resulted in NRMZ or Chabad Properties or transferees using the 3% creep exception to acquire effective control of Merlin over time on terms affording no control premium to (and potentially a significant value transfer *away* from) other shareholders. The 19.9% Conversion Requirement might have provided some protection to Merlin shareholders, had it existed. Merlin's misleading disclosure on this exacerbated the adverse effects of the Convertible Notes' terms on other Merlin shareholders and denied them the opportunity to reject those terms or insist on appropriate protection of their interests.

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<sup>43</sup> Including a remedial order but not including an order directing a person to comply with a requirement of Chapters 6, 6A, 6B or 6C

## Takeovers Panel

### Reasons – Merlin Diamonds Limited [2016] ATP 18

- (b) Mordechai Gutnick's association with Regals and Joseph Gutnick led not only to contraventions of s671B and s606, but also to shares being issued and voted, in conjunction with other shares in which Mordechai Gutnick had voting power, to approve resolutions suffering from the disclosure defects and adverse control implications described in paragraph (a).

140. To protect the interests of Merlin shareholders in respect of the effects outlined in paragraph 139, we have decided to make the following orders.

#### *Order 1*

141. This order restricts Chabad Properties and its associates converting or exercising any notes or options if that would result in any person's voting power in Merlin increasing above 19.9% unless it is previously approved by a resolution satisfying item 7 of s611. This effectively gives Merlin shareholders the protection they could reasonably have assumed applied, with respect to the Chabad Notes, on the basis of the disclosure in the explanatory statement.
142. ASIC submitted that the disclosure in the explanatory statement created the impression that it was referencing the threshold in s606 and therefore the likely impression created by the disclosure was that the notes would not be converted if it would result in an increase in voting power of the holder or any other person. We agree and accordingly this order is drafted to prevent conversion or exercise resulting in any person's voting power in Merlin exceeding the specified threshold.<sup>44</sup>
143. Chabad Properties submitted that this order was punitive and unfairly prejudicial because it punishes Chabad Properties for an omission made by Merlin. We consider that any prejudice to Chabad Properties is not unfair given the knowledge and involvement of Mordechai Gutnick,<sup>45</sup> a director and shareholder of Chabad Properties, with respect to the unacceptable circumstances.<sup>46</sup>

#### *Order 2*

144. This order restricts Regals and its associates from voting the number of Merlin shares issued to it as a result of the unacceptable circumstances.
145. ASIC submitted that the most appropriate order, given that the issue contravened s606, was to divest the shares. The applicant also supported a divestment order. Regals and Merlin submitted such an order would be unfairly prejudicial to Regals as its contravention was "*innocent and inadvertent*".
146. We are not satisfied the material before us justifies an inference that Regals knew of the association giving Mordechai Gutnick voting power in the shares in which Joseph Gutnick had a relevant interest. If Regals lacked that knowledge, an order divesting its shares may be unfair. The material given to us indicates that it was Mordechai Gutnick, rather than Regals, who instigated the conversion of notes and

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<sup>44</sup> Given the explanatory statement expressly refers to 19.9% that figure is used rather than (as in s606) 20%

<sup>45</sup> Who, with another, signed both of the deeds for the Chabad Notes on behalf of Chabad Properties

<sup>46</sup> See: *ASIC v Yandal Gold Pty Ltd* (1999) 32 ACSR 317 at [140]-[153]; *AMP Shopping Centre Trust 02* [2003] ATP 24 at [54]-[59]

## Takeovers Panel

### Reasons – Merlin Diamonds Limited [2016] ATP 18

issue of shares leading to the effects outlined in paragraph 139(b), but Regals alone would suffer the prejudice flowing from divestment.

147. Merlin submitted that, if orders are to be made, then Regals should be given the choice of:
- (a) orders cancelling and reversing the conversion of the convertible notes and the issue of the 50 million shares or
  - (b) orders or undertakings requiring Regals not to vote or dispose of the 50 million shares *“for a period of time equivalent to the time that it would have taken it to lawfully acquire those shares in accordance with the 3% creep exception”*.
148. Regals submitted that it should be permitted to elect the order described in paragraph 147(a). We consider such an order could be unfairly prejudicial to other Merlin shareholders given it would allow Regals to convert the notes at some later date when the resulting issue of shares might well be far more dilutive.<sup>47</sup> Regals also submitted that the voting freeze order described in paragraph 147(b) should only apply to a smaller number of shares for a period of 6 months.<sup>48</sup>
149. Taking account of the unusual circumstances noted in paragraph 146, we consider that the voting freeze is a sufficient and proportionate order to protect the interests of Merlin shareholders. Given our finding that the shares were issued to be voted at the 6 September Meeting, we consider it appropriate that this order restrict voting of the number of shares issued (ie the 50 million shares). Having regard to the time it would take to acquire the excess voting power over 20% at the time of the contravention under the 3% creep exception and balancing the seriousness of the contravention of s606 with the subsequent dilution as a result of further share issues,<sup>49</sup> we think a 12 month period is appropriate to protect the interests of Merlin shareholders.
150. We are satisfied that any prejudice to Regals as a result of this order is not unfair. We note Regals’ submission that it did not know of Mordechai Gutnick association with Joseph Gutnick. However, we consider that the circumstances of Mordechai Gutnick instigating the conversion of notes and issue of shares in order for those shares to be voted in favour of resolutions at the 6 September Meeting were sufficient to put Regals on inquiry and support our view that the limited prejudice this order may cause Regals is not unfair. We also note that Regals’ submissions appear to suggest it regards voting restrictions as less likely to be prejudicial than divestment.

#### Order 3

151. This order requires that each noteholder must not rely on any right it may have to require redemption of its notes as a consequence of the Panel application, the

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<sup>47</sup> We consider the Regals Notes to be unusually favourable to Regals in that, among other things, they allow conversion of the face value (plus any outstanding interest) into shares at the lower of \$0.015 per share or the 5 day VWAP. See paragraph 100.

<sup>48</sup> Regals submitted that the freeze should only apply to the excess of the relevant combined holdings over 20% as at the date of the orders, which would then be covered by the 3% creep exception in 6 months.

<sup>49</sup> See *Sovereign Gold Limited* [2016] ATP 12 at [159]

## Takeovers Panel

### Reasons – Merlin Diamonds Limited [2016] ATP 18

declaration and any orders made. We consider this order necessary to protect the interests of Merlin shareholders, who may otherwise be adversely affected by redemptions based on the Panel application, which was itself made necessary by the unacceptable circumstances identified in the declaration. We do not accept the submission from Merlin that we do not have the power to make this order in relation to noteholders other than Chabad Properties and Regals.<sup>50</sup>

#### *Orders 4 and 5*

152. These orders require Merlin to make an ASX announcement in a form approved by the Panel describing the circumstances and effect of the associations found by the Panel and the impact of the Panel's orders. We also considered ordering disclosure of information in the form of a substantial holder notice. Merlin submitted that such an order would be contrary to s657D(2) and would involve the exercise of judicial power.
153. We do not agree with Merlin's submissions. However we consider that, in the unusual circumstances of this matter, the market will be better informed by the disclosures required by order 4.

#### **Costs**

154. ASIC sought an order for costs. Parties are entitled to make, and resist, an application without exposure to a costs order, provided they present a case of reasonable merit in a businesslike way.<sup>51</sup> ASIC acknowledged this but submitted, nevertheless that a cost order should be made in this matter given, among other things:
- (a) Merlin, Mordechai Gutnick and Joseph Gutnick submitted that *"it is simply absurd to submit that Joseph Gutnick retains any relevant interest in [Merlin shares held by TMG] after his bankruptcy in July 2016"* without disclosing (as was later admitted) that Joseph Gutnick had instructed Merlin's company secretary to request that the shares be voted in favour of all resolutions at the 6 September Meeting, which it did.
  - (b) Regals and Mordechai Gutnick provided incomplete responses to certain questions and some information was only made known to the Panel as a result of ASIC's use of its compulsory information gathering powers.

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<sup>50</sup> Each noteholder was given an opportunity to make submissions in relation to this order. We did not receive any submissions opposing this order from noteholders other than those made by Merlin. Both Chabad Properties and Regals offered undertakings to the same effect as the orders. However we consider it preferable that the order extend to them also.

<sup>51</sup> Guidance Note 4 *Remedies General* at [28(c)]-[28(d)]

**Takeovers Panel**

**Reasons - Merlin Diamonds Limited  
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155. Having regard to the above and their conduct of the proceedings, we are satisfied that it is appropriate to require Merlin, Mordechai Gutnick and Regals to bear the costs of ASIC and the applicant.

**James Dickson**

**President of the sitting Panel**

**Decision dated 29 November 2016 (Declaration) and 13 December 2016 (Orders)**

**Reasons published 23 December 2016**

## Takeovers Panel

Reasons – Merlin Diamonds Limited  
[2016] ATP 18

### Advisers

Party	Advisers
Merlin (and see paragraph 3 of the reasons)	NA
Thomas Reddicliffe	NA
Regals	NA



**Australian Government**

**Takeovers Panel**

**Annexure A**

**CORPORATIONS ACT  
SECTION 657E  
INTERIM ORDERS**

**MERLIN DIAMONDS LIMITED**

Mr Thomas Henry Reddicliffe made an application to the Panel dated 31 October 2016 in relation to the affairs of Merlin Diamonds Limited (“**Merlin**”).

**The Panel orders:**

1. Without the consent of the Panel, each of the persons named in the schedule, and each of their respective associates, must not dispose of, transfer, charge or otherwise deal with any securities of Merlin in which they have a relevant interest.
2. These interim orders have effect until the earliest of:
  - (i) further order of the Panel
  - (ii) the determination of the proceedings and
  - (iii) 2 months from the date of these interim orders.

**Schedule**

Regals Fund LP, a Delaware limited partnership

Mazil Pty Ltd ACN 166 570 270

Great Central Gold Limited

Trinity Management Group Pty Ltd ACN 089 073 361

Atlantic Holdings (Aust) Pty Ltd ACN 165 242 759

NRMZ Pty Ltd ACN 604 624 580

Chabad Properties Pty Ltd ACN 107 936 229

Mordechai Gutnick, director of Merlin

Joseph Gutnick, former director of Merlin

**Bruce Dyer**

**Counsel**

**with authority of James Dickson**

**President of the sitting Panel**

**Dated 7 November 2016**



**Australian Government**

**Takeovers Panel**

**Annexure B**

**CORPORATIONS ACT**

**SECTION 657E**

**VARIATION OF INTERIM ORDERS**

**MERLIN DIAMONDS LIMITED**

The interim orders made on 7 November 2016 are varied by adding the following after Interim Order 1:

- “2. Each Noteholder must not rely on any right it may have to require redemption of any and all Notes held by it (including under clauses 9(h) and 10.1 of the Secured Noted Deed) as a consequence of the application to the Panel in this matter, the declaration of unacceptable circumstances, these interim orders or any final orders.

3. In these orders the following terms have the corresponding meaning:

deal with	includes the conversion of any convertible securities into shares of Merlin or the exercise of any options into shares of Merlin
Noteholder	Chabad Properties Pty Ltd Dovid L Szmerling and Nechama R Shmerling L1 Capital Global Opportunities Master Fund Martin Suman <Suman Family A/C> Neil Richard Kaner Regals Fund LP Scintilla Capital Pty Ltd Scintilla Strategic Investments Pty Ltd Slade Technologies Pty Ltd <Embrey Family Superfund>
Notes	notes issued under a Secured Note Deed
Secured Note Deed	(i) in the case of Chabad Properties Pty Ltd, the Secured Note Deeds between Merlin and Chabad Properties Pty Ltd dated 28 June 2016 and 30 June 2016, respectively (ii) in the case of Regals Fund LP, the Secured Note Deeds between Merlin and Regals Fund LP dated 23 June 2016 and 19 October 2016, respectively (iii) in the case of each other Noteholder, a Secured Note Deed between Merlin and the Noteholder entered



into on or after 6 September 2016”

so that the interim orders as varied read:

**CORPORATIONS ACT  
SECTION 657E  
INTERIM ORDERS**

**MERLIN DIAMONDS LIMITED**

Mr Thomas Henry Reddicliffe made an application to the Panel dated 31 October 2016 in relation to the affairs of Merlin Diamonds Limited (“**Merlin**”).

**The Panel orders:**

1. Without the consent of the Panel, each of the persons named in the schedule, and each of their respective associates, must not dispose of, transfer, charge or otherwise deal with any securities of Merlin in which they have a relevant interest.
2. Each Noteholder must not rely on any right it may have to require redemption of any and all Notes held by it (including under clauses 9(h) and 10.1 of the Secured Note Deed) as a consequence of the application to the Panel in this matter, the declaration of unacceptable circumstances, these interim orders or any final orders.
3. In these orders the following terms have the corresponding meaning:

deal with	includes the conversion of any convertible securities into shares of Merlin or the exercise of any options into shares of Merlin
Noteholder	Chabad Properties Pty Ltd Dovid L Szmerling and Nechama R Shmerling L1 Capital Global Opportunities Master Fund Martin Suman <Suman Family A/C> Neil Richard Kaner Regals Fund LP Scintilla Capital Pty Ltd Scintilla Strategic Investments Pty Ltd Slade Technologies Pty Ltd <Embrey Family Superfund>
Notes	notes issued under a Secured Note Deed
Secured Note Deed	(i) in the case of Chabad Properties Pty Ltd, the Secured Note Deeds between Merlin and Chabad Properties Pty Ltd dated 28 June 2016 and 30 June 2016, respectively  (ii) in the case of Regals Fund LP, the Secured Note Deeds between Merlin and Regals Fund LP dated

23 June 2016 and 19 October 2016, respectively

(iii) in the case of each other Noteholder, a Secured Note Deed between Merlin and the Noteholder entered into on or after 6 September 2016

4. These interim orders have effect until the earliest of:

- (i) further order of the Panel
- (ii) the determination of the proceedings and
- (iii) 2 months from the date of these interim orders.

**Schedule**

Regals Fund LP, a Delaware limited partnership

Mazil Pty Ltd ACN 166 570 270

Great Central Gold Limited

Trinity Management Group Pty Ltd ACN 089 073 361

Atlantic Holdings (Aust) Pty Ltd ACN 165 242 759

NRMZ Pty Ltd ACN 604 624 580

Chabad Properties Pty Ltd ACN 107 936 229

Mordechai Gutnick, director of Merlin

Joseph Gutnick, former director of Merlin

**Allan Bulman**

**Director**

**with authority of James Dickson**

**President of the sitting Panel**

**Dated 29 November 2016**



**Australian Government**

**Takeovers Panel**

**Annexure C**

**CORPORATIONS ACT**

**SECTION 657A**

**DECLARATION OF UNACCEPTABLE CIRCUMSTANCES**

**MERLIN DIAMONDS LIMITED**

**CIRCUMSTANCES**

1. On 23 June 2016, Merlin Diamonds Limited (**Merlin**) entered into a secured note deed with Regals Fund LP (**Regals**) for the issue of 1,307,537 notes and 87,169,569 options over Merlin shares. Regals is managed exclusively by Mr David Slager. As at 23 June 2016, Regals had a relevant interest in 25,162,755 Merlin shares.
2. On 28 June 2016, Merlin entered into a secured note deed with Chabad Properties Pty Ltd as trustee of the Machon Chaim College Fund (**Chabad Properties**) for the issue of 1,100,000 notes and 73,333,700 options over Merlin shares. The directors of Chabad Properties are Mr Mordechai Gutnick and Ms Stera Gutnick. Joseph Gutnick ceased to be a director on 7 July 2016. As at 28 June 2016, Mr Joseph Gutnick, Ms Stera Gutnick and Mr Mordechai Gutnick each held one third of the shares in Chabad Properties.
3. On 30 June 2016, Merlin entered into a further secured note deed with Chabad Properties for the issue of 900,000 notes and 60,000,300 options over Merlin shares.
4. On or around 4 July 2016, Mr Slager agreed by email to lend Mr Mordechai Gutnick \$300,000 (USD) interest free to buy shares in Merlin.
5. On or around 8 July 2016, Mr Joseph Gutnick became bankrupt. On 7 July 2016, Mr Joseph Gutnick resigned as a director of Merlin and Mr Mordechai Gutnick was appointed as a director of Merlin on the same date.
6. On 12 July 2016, Merlin entered into a secured note deed with NRMZ Pty Ltd as trustee of the NRMZ family trust (**NRMZ**) for the issue of 392,054 notes and 26,137,064 options over Merlin shares. Mr Mordechai Gutnick is the sole shareholder and director of NRMZ.
7. On 2 August 2016, Merlin issued a notice of meeting for a general meeting to be held on 6 September 2016 (**6 September general meeting**) which included the following resolutions:
  - (a) To approve Merlin *“in accordance with ASX Listing Rule 7.1 and for all other purposes, issuing 1,307,537 convertible notes at a price of \$1 per convertible note and 87,157,133 options”* to Regals. Regals was excluded from voting on this resolution.
  - (b) To approve Merlin *“in accordance with ASX Listing Rules 7.1 and 10.11 and for all other purposes, issuing 392,054 convertible notes at a price of \$1 per convertible note and 26,137,064 options”* to NRMZ.

- (c) To approve Merlin *“in accordance with ASX Listing Rules 7.1 and 10.11 and for all other purposes, issuing 2,000,000 convertible notes at a price of \$1 per convertible note and 133,333,333 options”* to Chabad Properties.
  - (d) To approve Merlin *“in accordance with ASX Listing Rule 7.1 and for all other purposes”* placing a further 2,000,000 convertible notes at a price of \$1 per convertible note and 133,333,333 options.
8. The explanatory memorandum for the 6 September general meeting disclosed in relation to the resolutions for the issue of convertible notes and options to Regals, NRMZ and Chabad Properties that the secured note deeds have *“a requirement that the conversion of the convertible notes cannot result in [the noteholder] holding more than 19.9% of the issued shares of the Company at the time of conversion, unless shareholder approval is obtained”*. There was no such requirement in the secured note deeds.
  9. On or about 28 August 2016, Mr Mordechai Gutnick asked Mr Slager to vote Regals’ shares in favour of the resolutions to be put to the 6 September general meeting that Regals could vote on, and sent a text message to him stating *“it’s a necessity that we get your votes and the convertible note passes without a problem”*. Regals voted in favour of the resolutions (that Regals could vote on) on or about 30 August 2016.
  10. On or about 29 August 2016, Merlin received a requisition under s249D<sup>1</sup> seeking to remove and replace each of the directors of Merlin.
  11. On 31 August 2016, Mr Mordechai Gutnick initiated by text message a telephone conversation with Mr Slager, during which Mr Slager told Mr Mordechai Gutnick that he wanted to convert notes into shares for the purpose of further supporting the resolutions. On 1 September 2016, 750,000 convertible notes held by Regals were converted into 50,000,000 Merlin shares.
  12. Regals subsequently voted its additional 50,000,000 Merlin shares in favour of the resolutions to be put to the 6 September general meeting that Regals could vote on.
  13. The Panel considers that Mr Mordechai Gutnick and Regals have an agreement, arrangement or understanding in relation to the affairs of Merlin and are associated under s12(2)(b). In addition, Mr Mordechai Gutnick and Regals are acting in concert in relation to Merlin’s affairs and are associated under s12(2)(c).
  14. The Panel considers that Mr Mordechai Gutnick and Mr Joseph Gutnick have an agreement, arrangement or understanding in relation to the affairs of Merlin and are associated under s12(2)(b). In addition, Mr Mordechai Gutnick and Mr Joseph Gutnick are acting in concert in relation to Merlin’s affairs and are associated under s12(2)(c).
  15. Immediately prior to 31 August 2016 and the issue of 50,000,000 Merlin shares to Regals:
    - (a) Regals had a relevant interest in approximately 5.58% of issued Merlin shares.
    - (b) Mr Joseph Gutnick had a relevant interest in approximately 14.39% of issued Merlin shares, as a result of his power to control the voting of Merlin shares held by Great Central Gold Limited (**GCG**), Mazil Pty Ltd (**Mazil**) and Trinity Management Group Pty Ltd (**TMG**).

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<sup>1</sup> References are to the *Corporations Act 2001* (Cth)

- (c) Mr Mordechai Gutnick had a relevant interest in approximately 0.7% of issued Merlin shares, as a result of his power to control the voting of Merlin shares held by Atlantic Holdings (Aust) Pty Ltd and Morzev Pty Ltd (**Morzev**).

- 16. Immediately after the issue of the 50,000,000 Merlin shares to Regals, Mr Mordechai Gutnick had voting power in Merlin of approximately 28.22%.

#### **Contravention of s606**

- 17. As a result of the acquisition of a relevant interest in 50,000,000 Merlin shares by Regals on 1 September 2016, the voting power of Mr Mordechai Gutnick in Merlin increased above 20%. None of the exceptions in s611 applied and accordingly s606 was contravened.

#### **Contraventions of s671B**

- 18. In contravention of s671B:
  - (a) No substantial holder notice has been lodged disclosing Mr Mordechai Gutnick's voting power in Merlin and association with Mr Joseph Gutnick and Regals in relation to Merlin.
  - (b) The notice of change of interests of substantial holder lodged by Regals on 6 September 2016 is deficient because, among other things, it does not disclose Regals' association with Mr Mordechai Gutnick.

#### **6 September general meeting**

- 19. The Panel considers that the explanatory memorandum for the 6 September general meeting was misleading as Merlin shareholders were not informed that the holders of the notes and options the subject of the resolutions would have the capacity to convert their convertible notes and exercise their options to increase their voting power in Merlin above 20% in reliance on item 9 of s611.
- 20. Mr Joseph Gutnick has 50% voting power in Mazil and a 50% interest (held jointly with Ms Stera Gutnick) in GCG. At the 6 September general meeting Mazil and GCG voted in favour of issuing convertible notes and options to Chabad Properties and NRMZ. The decision to vote the Merlin shares held by each of Mazil and GCG was made by Mr Joseph Gutnick.
- 21. TMG is the trustee of the Merlin Diamonds Employee Share Trust under the Merlin Diamonds Employee Share Trust Deed. It is the registered holder of 18,000,000 Merlin shares. Mr Joseph Gutnick instructed Merlin's company secretary to ask TMG to vote the 18,000,000 shares in favour of all resolutions at the 6 September general meeting, which it did.
- 22. Mr Mordechai Gutnick is the sole shareholder and sole director of Morzev which holds 76,923 shares in Merlin. Morzev voted in favour of all the resolutions at the 6 September general meeting.
- 23. At the 6 September general meeting, the resolution to issue convertible notes and options to Regals was defeated. The resolutions to issue convertible notes and

options to Chabad Properties and NRMZ were passed.<sup>2</sup> Those resolutions would not have passed if:

- (a) the 50,000,000 Merlin shares issued to Regals and all the Merlin shares held by Mazil, GCG and Morzev had not been voted in favour<sup>3</sup> or
- (b) all the Merlin shares held by Regals had not been voted in favour<sup>4</sup> or
- (c) all the Merlin shares held by Mazil, GCG, Morzev and TMG had not been voted in favour.<sup>5</sup>

## **EFFECT**

24. It appears to the Panel that:

- (a) the acquisition of control over voting shares in Merlin has not taken place in an efficient, competitive and informed market
- (b) the holders of shares in Merlin do not know the identity of persons who have acquired a substantial interest in Merlin and
- (c) the holders of shares in Merlin have not been given enough information to enable them to assess the merits of a proposal which would result in persons acquiring a substantial interest in Merlin.

## **CONCLUSION**

25. It appears to the Panel that the circumstances are unacceptable circumstances:

- (a) having regard to the effect that the Panel is satisfied they have had, are having, will have or are likely to have on:
  - (i) the control, or potential control, of Merlin or
  - (ii) the acquisition, or proposed acquisition, by a person of a substantial interest in Merlin
- (b) in the alternative, having regard to the purposes of Chapter 6 set out in section 602
- (c) in the further alternative, because they constituted, constitute, will constitute or are likely to constitute a contravention of a provision of Chapter 6 or of Chapter 6C of the Act.

26. The Panel considers that it is not against the public interest to make a declaration of unacceptable circumstances. It has had regard to the matters in section 657A(3).

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<sup>2</sup> The resolution approving the issue of convertible notes and options to NRMZ became redundant because prior to the meeting NRMZ transferred the relevant underlying notes and the notes were converted into Merlin shares

<sup>3</sup> In relation to the resolution approving the issue of convertible notes and options to Chabad Properties, votes cast for would have been 44.05% of total votes, assuming open proxies were cast in favour

<sup>4</sup> In relation to the resolution approving the issue of convertible notes and options to Chabad Properties, votes cast for would have been 47.74% of total votes, assuming open proxies were cast in favour

<sup>5</sup> In relation to the resolution approving the issue of convertible notes and options to Chabad Properties, votes cast for would have been 49.30% of total votes, assuming open proxies were cast in favour

## **DECLARATION**

The Panel declares that the circumstances constitute unacceptable circumstances in relation to the affairs of Merlin.

**Bruce Dyer**  
**Counsel**  
**with authority of James Dickson**  
**President of the sitting Panel**  
**Dated 29 November 2016**



**Australian Government**

**Takeovers Panel**

**Annexure D**

**CORPORATIONS ACT  
SECTION 657D  
ORDERS**

**MERLIN DIAMONDS LIMITED**

The Panel made a declaration of unacceptable circumstances on 29 November 2016.

**THE PANEL ORDERS**

1. Chabad Properties and its associates must not convert any Chabad Notes into shares in Merlin or exercise any Chabad Options if the conversion or exercise would result in any person's voting power in Merlin increasing to, or from, a point above 19.9% unless it is previously approved by a resolution satisfying item 7 of s611.<sup>1</sup>
2. For twelve months from the date of this order, Regals and its associates must not exercise, or allow the exercise of, and Merlin must disregard, voting rights attached to:
  - (a) if Regals and its associates have a relevant interest in more than 50,000,000 shares in Merlin – 50,000,000 of those shares or
  - (b) if Regals and its associates have a relevant interest in 50,000,000 or less shares in Merlin – all of those shares.
3. Each Noteholder must not rely on any right it may have to require redemption of any and all Notes held by it (including under clauses 9(h) and 10.1 of the Chabad Deeds or any similar clause in a Secured Note Deed) as a consequence of the application to the Panel in this matter, the declaration of unacceptable circumstances, the interim orders or these final orders.
4. As soon as practicable, and in any event within two business days after the date of these orders, Merlin must provide a draft ASX announcement to the Panel, ASIC and the other parties in the matter that:
  - (a) describes the circumstances around and the existence and nature of Mr Mordechai Gutnick's association with each of Regals and Mr Joseph Gutnick as found by the Panel
  - (b) describes the effect of those associations on the voting power of Mr Mordechai Gutnick as of 1 September 2016, including the contraventions of ss606 and 671B as found by the Panel and
  - (c) the effect of the Panel's final orders.

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<sup>1</sup> All statutory references are to the *Corporations Act 2001* (Cth) and all terms used in Chapter 6 or 6C have the meaning given in the relevant Chapter (as modified by ASIC)



5. Merlin must provide to the ASX for release the announcement referred to in order 4, in a form approved by the Panel, forthwith after approval.
6. Within 15 business days of the date of these orders, Merlin, Mr Mordechai Gutnick and Regals must pay in aggregate to:
  - (a) ASIC, \$13,995.55 and
  - (b) the applicant, Thomas Reddicliffe, \$2,350.00,

in each case representing the costs actually, necessarily, properly and reasonably incurred in the course of the proceedings. Liability for these costs is joint and several.

7. In these orders the following terms apply:

<b>Chabad Deeds</b>	the secured note deeds between Merlin and Chabad Properties dated 28 June 2016 and 30 June 2016, respectively
<b>Chabad Notes</b>	notes issued under the Chabad Deeds
<b>Chabad Options</b>	options issued under the Chabad Deeds
<b>Chabad Properties</b>	Chabad Properties Pty Ltd as trustee of the Machon Chaim College Fund
<b>Merlin</b>	Merlin Diamonds Limited
<b>Noteholders</b>	Regals, Chabad Properties and any person who holds Notes under a Secured Note Deed at the date of these orders
<b>Notes</b>	the Chabad Notes and any other notes issued under a Secured Note Deed
<b>Regals</b>	Regals Fund LP
<b>Secured Note Deed</b>	any deed entered into by Merlin on or after 23 June 2016 providing for the issue of notes or options in similar terms to the Chabad Deeds

**Bruce Dyer**  
**Counsel**  
**with authority of James Dickson**  
**President of the sitting Panel**  
**Dated 13 December 2016**